



# SMALL STATES: MEETING CHALLENGES IN THE GLOBAL ECONOMY

Report of the Commonwealth Secretariat/  
World Bank Joint Task Force on Small States

April 2000

# DEVELOPMENT COMMITTEE

JOINT MINISTERIAL COMMITTEE  
OF THE  
BOARDS OF GOVERNORS OF THE BANK AND THE FUND  
ON THE  
TRANSFER OF REAL RESOURCES TO DEVELOPING COUNTRIES

Excerpt from the Final Communiqué of the 61<sup>st</sup> meeting of the Development Committee held in Washington, D.C., on April 17, 2000:

**Report of the Commonwealth Secretariat/World Bank Joint Task Force on Small States:** Ministers welcomed the report to the Development Committee and its analysis of the special characteristics of small states that make them particularly vulnerable, while noting that a number of larger states shared some or all of the same characteristics. They noted the report's conclusions that tackling small states' development challenges will take a combination of correct domestic policy action, continued external assistance, and where achievable, improvements in the external environment. They also noted the report's recommendation that the circumstances of small states should be taken into account in the policies and programs of the multilateral trade, finance and development organizations. The Committee supported World Bank and IMF proposals for their future work programs on the issues of small states, as set out in the report, and agreed that these steps could make a valuable contribution in helping small states face their development challenges.

# Small States: Meeting Challenges in the Global Economy

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The report also benefited from extensive consultations with governments of small states, as well as the written submissions received from many of them.

## **SMALL STATES: MEETING CHALLENGES IN THE GLOBAL ECONOMY**

### **Executive Summary**

1. The report of the joint Commonwealth Secretariat/World Bank Task Force sets out a contextual framework in which to consider development problems peculiar to small states. Each small state is unique, and needs to address its development prospects in the context of its own cultural, historical, and social realities. There are also differences between regions. But most small states share a number of common characteristics. Assistance to small states can be made more effective with a better understanding of these characteristics and the development problems they pose. The report presents a range of common relevant policy actions for small states and the international community. The report also collects together more specific work programs (“frameworks”) on small states issues prepared and submitted to the Task Force by a number of multilateral institutions, including the World Bank and Commonwealth Secretariat.
2. Among the world’s sovereign developing states with populations of less than 1.5 million people, 41 are members of the World Bank, more than 30 are eligible for Bank Group borrowing, and 29 are members of the Commonwealth. The incomes and stages of development of these states vary widely, from very poor African countries such as Guinea-Bissau (with per capita GNP of \$160) to wealthy countries such as Brunei, Cyprus, Malta, and Qatar (with per capita GNP of more than \$9,000). While there is no special significance in the 1.5 million population threshold, it provides a useful starting point. But no single definition is adequate, and the Task Force does not recommend the creation of a special category of small states. Countries should be regarded as lying along a size continuum, with a number of larger states sharing some or all of the same characteristics.

#### **Work and consultations of the Task Force**

The Task Force’s Interim Report was circulated in October 1999. It noted further work to be carried out before production of a final report. The Interim Report was discussed and welcomed in November 1999 by the Commonwealth Ministerial Group on Small States and Commonwealth Heads of Government. The Interim Report was also circulated widely for comment, to small states and development institutions and published electronically.

In continuing consultations, the Task Force received many comments from multilateral organizations as well as from small states, including a substantial written submission from the CARICOM Secretariat. The Task Force has drawn on these contributions as it completed its work. In particular, the last stage of the Task Force’s work was guided by the discussions at a major global conference arranged by the World Bank and the Commonwealth Secretariat in London on 17–18 February 2000. That conference focussed on the four areas for further work identified in the Interim Report: tackling volatility, vulnerability and natural disasters; strengthening capacity; issues of transition to the changing global trade regime; and new opportunities and challenges from globalization. The final report of the Task Force draws extensively on the discussions and conclusions at that conference.

### **What makes small states different? Their special development challenges**

3. The report concludes that developing small states do share a number of characteristics that pose special development challenges. They are especially vulnerable to external events, including natural disasters, that cause high volatility in national incomes; many of them are currently facing an uncertain and difficult economic transition to a changing world trade regime; and they suffer from limited capacity in the public and private sectors. More specifically, the following characteristics define the special development challenges and vulnerabilities that many small states face.
  - ***Remoteness and isolation.*** Of the developing small states, three out of four are islands and in some cases widely dispersed multi-island states, others are landlocked, and some of them located far from major markets. For many small states, like those in the Pacific, high transport costs make it harder for them to turn to world markets to compensate for the drawbacks of the small size of their domestic markets. And small domestic markets combine with large distances from other markets to reduce competition and its spur to efficiency and innovation.
  - ***Openness.*** A high degree of openness to the rest of the world brings benefits. But it also means that small economies are heavily exposed to events in global markets, and developments in the global trade regime, over which they have little if any influence. They also tend to rely more heavily on taxing imports as a source of revenue, leading to difficulties as tariffs are reduced.
  - ***Susceptibility to natural disasters and environmental change.*** Most small states are in regions susceptible to natural disasters such as hurricanes, cyclones, drought and volcanic eruptions, which typically affect the entire population and economy. Some are threatened by global environmental developments. Since most of such adverse events affect the entire population, risk pooling at the national level is not feasible.
  - ***Limited diversification.*** Because of their small domestic markets, many small states are necessarily relatively undiversified in their production and exports. Where one dominant activity has declined, it has tended to be replaced with another. This adds to vulnerability to changes in the external environment.
  - ***Poverty.*** There is some evidence that poverty levels tend to be higher, and income distribution more uneven, in smaller than in larger states. Where this is so, income volatility can create additional hardship as the poor are less able to weather negative shocks to their incomes.
  - ***Limited capacity.*** While weaknesses in both public and private sector capacity are a key problem for most developing countries, smallness of size adds a further dimension to the challenge. This is further compounded in states, like the Pacific islands, where the internal distances are large and the population is scattered. In the public sector small states face diseconomies of small size in providing public services and in carrying out the business of government, and tend to have relatively larger public sectors than other developing countries. As they face the challenges and opportunities of globalization small states are also finding they do not have sufficient institutional capacity to participate fully in international finance and trade negotiations—the outcomes of which can profoundly affect their economies. In the private sector, as already noted, lack of diversification and domestic competition can hold back successful development.

4. Many of these factors combine to make small states' economies especially vulnerable, and in particular they affect:
  - ***Income volatility.*** Overall, the range of per capita incomes and rates of growth are not significantly different in small and large developing countries. However, the residents of small states experience higher volatility in their incomes—the standard deviation of annual real per capita growth in small states is about 25 percent higher than in large states. This reflects several of the factors listed above—their high levels of exports and imports and low diversification in production and trade which leaves them exposed to fluctuations in world markets, and their susceptibility to natural disasters.
  - ***Access to external capital.*** Access to global capital markets is important for small states, and is one way to compensate for adverse shocks and income volatility. But the evidence is that private markets tend to see small states as more risky than larger states, so that spreads are higher and market access more difficult.

**The way ahead: challenges and opportunities for small states; policies and external assistance to address them**

5. The Task Force has concluded that addressing these challenges successfully will take a combination of the following: correct domestic policy action; in some cases new approaches to regional co-operation; continued external support and assistance from multilateral and bilateral development institutions; and improvements, where achievable, in the external environment. In particular, the Task Force has studied in detail four areas of special relevance to successful development in small states: how best to tackle volatility, vulnerability and natural disasters; issues of transition to the changing global trade regime; strengthening capacity; and key challenges and new opportunities arising from globalization. In these areas the report identifies an ongoing work program of actions, analysis, and new initiatives for the states themselves and for the international community. All these conclusions are consistent with views expressed during the extensive consultations carried out by the Task Force, and in particular with the conclusions reached at the global conference held in London in February 2000.

*Tackling volatility, vulnerability and natural disasters*

6. The Task Force has identified the following actions to help small states deal with problems of income volatility and natural disasters.
  - The work carried out by the Commonwealth and other organizations in analyzing the vulnerability of small states and deriving vulnerability indices for developing countries demonstrates that most small states are considerably more vulnerable than larger developing countries. This vulnerability should be taken into account in programs of assistance provided by the multilateral development, finance and trade institutions.
  - The vulnerability and special characteristics of small states, and weak capacity in the private sector, contribute to perceived riskiness and difficulty in attracting private investment flows. A relatively high level of official assistance is therefore appropriate for small states where they have policies in place for such assistance to be effective, as is the continued application of flexible graduation procedures at the multilateral institutions.
  - The strong risks and consequences of natural disasters in many small states require new approaches by the states themselves and the international community. Donor support for disaster mitigation, for example in infrastructure, can have a high pay-off. The work by the World Bank on new approaches to disaster mitigation and insurance in the Caribbean is very relevant, as is the Bank's intention to co-operate with states in the region to develop and support regional risk-pooling arrangements, to complement improved disaster mitigation and prevention measures (for example, in the context of the ProVention Consortium) which can greatly reduce the costs of disasters when they occur. Similar approaches, that build on this experience, should be extended to other areas.
  - Many small states remain dependent on commodity production, and it would therefore be useful if the International Task Force on commodity price risk management could pay attention to issues and commodities of relevance to small states in its future work. Many small states are exposed to different risks, however—for example, fluctuations in volumes and tourism earnings and different land tenure systems—and these will need a combination of different approaches.
  - Many small states have vulnerable physical environments as well as vulnerable economies. As development takes place it will be crucial to ensure that it is sustainable, by protecting the environment at the same time. Mistakes have been made in this area, for example in insensitive tourism development and over-exploitation of non-renewable resources. This environmental vulnerability is compounded by the likely impact of climate change for some small states, particularly those in the Pacific. It will be important for donors and international agencies, including the World Bank, to continue to support small states in this regard, both with advice and finance.

*Issues of transition to the changing global trade regime*

7. Small states must adapt, indeed transform, their economies to secure the benefits of globalization and the increasingly open global trading environment—trade policy for small states, as for other developing countries, needs to be seen as part of sound overall economic development strategy. Clear signals about the direction of trade and regulatory policies and the length of transition periods will be needed to guide the process and to attract new investment. Action wherever possible to reduce or remove barriers to small states exports will also be helpful.
- The work of the Task Force has shown that many small states will face special difficulties in making this transition and will need time to adjust to changes in the external trade regime, and sequence changes in their economies. The particular vulnerabilities of many small states should be recognized as justifying special consideration to deal with the issues that are crucial to transformation of their economies, including length of transition periods, as the global process of trade liberalization, and removal of special protective regimes, continues. It would be useful to review the current process of WTO accession as it affects small states to see if the problems and costs these countries face in the process can be reduced.
  - Another issue related to WTO participation is the lack of adequate resources to participate fully in international trade negotiations. The Commonwealth, through its permanent trade advisers in Geneva and Fiji, already provides assistance of this type to its member countries. It will continue to do so and has expressed a willingness to take a lead in expanding such facilities. The EU is financing an ACP countries' bureau in Geneva to facilitate relations and negotiations with WTO and UNCTAD. Additional support would be welcome, as is the recent creation of an "Advisory Centre on WTO Law". The WTO should examine other ways to help, for example by allowing groups of small states to be represented collectively at discussions where they wish to do so.
  - Trade liberalization can have major fiscal consequences for small states. The IMF should continue to take a pragmatic approach to the advice it gives to small states that risk losing a major source of fiscal revenue as tariffs fall, recognizing that for some open, small economies low, flat-rate tariffs may be a component of an efficient tax system. However, as small states move to more service-based economies, they will need to adopt broader-based consumption taxes. They will also need technical assistance from the IMF and others in tax administration.

### *Strengthening capacity*

8. Small states and those providing support for them need to continue to address problems of limited capacity, both in the private and public sectors. Specific issues to pursue in this context include the following.
  - There is a continuing task of accumulation of knowledge about policies and approaches that work and do not work for small states, and sharing this knowledge and experience among states both within and across regions.
  - An important approach in tackling limited capacity in small states is to develop regional approaches wherever feasible. The multilateral institutions and other donors should reinforce existing programs by enhancing their lending and non-lending services to encourage and support such co-operation, particularly by assisting regional organizations dealing predominantly with small states.
  - To help develop private sector capacity, both regional and country approaches are needed, including providing information to facilitate business decision making, training, and encouraging formation of networks and associations of entrepreneurs. Another aspect of limited capacity where the multilateral institutions can also help is dealing with utilities' regulation and competition policy; issues of considerable importance with the prevalence of monopoly or oligopoly suppliers in small states.
  - Activities and requirements of a multiplicity of donors place heavy and unnecessary burdens on limited administrative capacity in many small states. This was well illustrated by a recent study by the World Bank Operations Evaluation Department. This problem needs to be addressed by a new approach building on principles of partnership and country leadership that underlie the Comprehensive Development Framework approach. Donors and international agencies should join together country by country, in country-led partnerships to align their objectives, rationalize their support and simplify and harmonize their procedures to reduce these burdens. Helping build country capacity and forging of closer working relationships with regional organizations would help in this regard.
  - Building institutional capacity needs to be undertaken in close consultation with recipient agencies and tailored carefully to their particular needs. Experience in the Pacific suggests the need for a long-term commitment by donors to strengthen generally weak institutional and human resource capacity. Further, the design of capacity building activities needs to be flexible and responsive to a country's needs and political realities

### *New opportunities and challenges from globalization*

9. Some small states will need external support and advice as they seek to reposition their economies. They need enabling environments and the right kind of public policy support—for example in training and education, and creating regulatory frameworks—to encourage new activities, many of which will be in the service sectors. In this context actions in two specific areas will be important for many small states.
  - One new area in the service sector where some small states have been successful is in the provision of onshore and offshore financial services. Such financial services have come to be of substantial importance to their economies. For a variety of reasons offshore financial centers have come to be a matter of concern to the international community. There is a clear need for improvements in financial operating practices

and regulatory standards, and also a need to take action to prevent financial and tax crime and to address concerns about harmful aspects of tax competition. Improvements in these areas can benefit small states as well as reduce risks to the international banking and financial system. Many small states are already cooperating in international efforts to combat money-laundering. Assistance by multilateral institutions and others in strengthening financial sector regulation and supervision will be important. Because of their potential international impact offshore centers are currently the subject of scrutiny by the OECD's Forum on Harmful Tax Competition and the Financial Stability Forum (FSF). This is causing concern for a number of small states because of lack of representation in the OECD and FSF and lack of adequate consultation on the matters being addressed. At the London conference in February 2000, the OECD indicated its willingness to engage constructively with small states on tax competition issues and to respond to their call for a multilateral discussion. It is important for all these issues to be considered in international fora where small states themselves have a voice so that their interests can be taken into account.

- Finally, work on the opportunities that information technology and electronic commerce can bring to small isolated states suggests that these technologies can be a major source of help in their development. But success requires the correct public sector infrastructure, crucially a regulatory framework that will deliver high quality/low cost telecommunications services. It is important to note that this provides a challenge in which many small states will need external support from the multilateral development banks and others.

### **Specific actions by multilateral institutions**

10. The more specific World Bank and Commonwealth Secretariat frameworks set out in Part II of the report focus on knowledge accumulation and dissemination, institutional capacity building, including support for regional approaches, risk management, and the management of transition.
11. The World Bank framework centers around helping small states develop and implement effective strategies to reduce poverty by applying the general principles of country ownership, participation, partnership and a holistic approach to diagnosis and policy development to their special characteristics. While the work programs for small states are prepared in the context of individual country diagnosis and country assistance strategies, the special problems of vulnerability and transition underscore the need to link lending and non-lending services to encourage institutional and policy reform. More specifically, the Bank's framework includes:
  - continuing a flexible approach to graduation policy, including from IDA, that takes into account the special circumstances of small states, ensuring that none is graduated prematurely;
  - reducing transactions costs for small states by actively promoting better donor coordination, and by exploring for small states the full flexibility in the use of its new lending instruments, such as adaptable program loans (APLs) and learning and innovation loans (LILs);
  - supporting private sector development as small states seek to transform their economies in the process of transition and to meet the challenges of globalization, especially in terms of education and training, creating improved regulatory frameworks, and

infrastructure development – and in the policies and investments needed to exploit the opportunities that information technology and electronic commerce can bring;

- supporting regional initiatives as an important way for small states to overcome diseconomies of scale in the public and private sectors;
- helping to lower the costs of natural disasters, including the provision of loans for disaster-proof infrastructure and exploring new approaches to Bank support for risk pooling and disaster insurance; and
- in partnership with small states, continuing attention to cross-cutting issues and to accumulating and sharing of relevant knowledge generated within the Bank and outside—using mechanisms such a Bank-wide thematic group, development of a World Bank small states web site, and arranging regular meetings where representatives of small states can share experiences and discuss new developments. These actions will be coordinated with existing capacities, such as SIDS/Net, a UNDP-based network, dedicated to small island developing states.

12. The Commonwealth framework commits to maintain and, where possible, expand overall levels of support for small states development, in terms of both advocacy and provision of technical assistance. In particular, it targets advice on vulnerability and risk management, trade negotiations, capacity building for regional organizations involving small states, focusing on its preparedness to:

- sharpen its advocacy role and to pursue commitments from the UN system and others to include vulnerability as an additional criterion in determining their treatment of small states on issues such as graduation, aid flows, development strategies and investment;
- assist in the development of national and regional capital markets, stock exchanges and commodity risk mechanisms;
- take a lead in the strengthening of facilities in Geneva to assist small states in their dealings with WTO, and provide support for these countries in their relations with the EU under the successor agreement to the Lomé IV Convention;
- provide support for capacity building in regional organizations dealing predominantly with small states;
- take a lead in broadening the Trade and Investment Access Facility to provide policy advice and technical assistance and promote trade-related investment in small states in order to allow them to exploit the opportunities afforded by globalization;
- explore ways of further expanding the Commonwealth Private Investment Initiative to provide venture capital-type funds and mobilize financial flows to small states; and
- seek agreement on a mechanism to track implementation of commitments and proposals by partner organizations, regarding their treatment of small states.

13. Partner organizations are also developing their responses toward small states. Part II of the report includes frameworks submitted to the task force by the following organizations: IMF, WTO, EU, UN, UNDP, UNCTAD, and major regional development banks. Indications of action by them include:

- Eligibility for access to resources under the IMF's concessional facility closely follows IDA eligibility; the IMF will also continue to give countries facing balance of payments difficulties access to the Fund's financial facilities and loans; and a wide range of technical assistance will continue to be provided. The IMF has been consulting with UNDP and other donors on the establishment of a regional technical assistance center in the Caribbean, similar to the one already in place in the South Pacific.
- The EU is: financing an ACP office in Geneva to assist member countries in their dealings with WTO; will take into account the dimensions of vulnerability when determining its programs toward small states; has developed a Disaster Prevention, Mitigation and Preparedness Programme to assist countries vulnerable to natural disasters; is supporting transition of the most banana-dependent economies by improving competitiveness of the banana sector, by creating new activities to replace traditional banana production, by financing new infrastructure and by retraining labor; and is creating a new Investment Facility for the support of private sector development in ACP countries.

## **Conclusion**

14. Small states share a number of special development challenges in the global economy. The Task Force report, as summarized above, lists ways in which these challenges can be met. In some cases relevant actions are already under way. In others the report identifies useful initiatives that should be pursued. And in others the Task Force has been able to do little more than set out issues that should be addressed. The Task Force commends this as an agenda for the future. Tackling it successfully will take a combined effort by small states themselves and by the international community.

## Introduction

1. The Commonwealth and the World Bank have long been interested in the development of small states. The Commonwealth Secretariat has carried out pioneering work and advocacy on understanding the economic, environmental, political and social characteristics that distinguish small states (Commonwealth Secretariat 1985, 1997). And for many years the World Bank and the International Development Association (IDA) have recognized the particular problems of small island countries, through the granting of special access to IDA resources.
2. At the request of Commonwealth Heads of Government, a Ministerial Mission on Small States met with the president of the World Bank in July 1998, and following that meeting the Bank and the Commonwealth Secretariat established a Joint Task Force on Small States. The purpose of the Task Force was to assess the case for special treatment advanced by the Commonwealth small states at the Edinburgh Heads of Government Meeting and enable the Bank to examine its instruments for assisting these countries, considering alternatives and adaptations to address their unique problems, including their vulnerability to marginalization, natural disasters, and external economic shocks. In addition, the Task Force was to address the transitional problems associated with the changes in international trade rules that followed the implementation of Uruguay Round agreements by the World Trade Organization (WTO), and the arrangements for a successor agreement to the European Union's Lomé IV Convention. The Task Force has also sought to address other major issues of special interest and concern to small states within a rapidly globalizing economy.
3. The Task Force met for the first time in October 1998.<sup>1</sup> At that time, it invited experts on small states and senior officials from international organizations that serve small states to form an Advisory Board. In addition, the Task Force commissioned a series of papers to support its efforts, and the papers were discussed at a high-level conference in St. Lucia in February 1999. That conference involved representatives from twenty-five small states, academia, the private sector, and bilateral, regional, and multilateral development and finance organizations. Following the conference, there was a period of consultations with the Advisory Board, partner organizations and small states themselves. A preliminary draft was presented to the EU, WTO, UNCTAD, and South Pacific trade ministers during the summer, and a revised report was circulated in August 1999. Following discussions at the Commonwealth Finance Ministers' meeting on September 23 and a further round of consultations with small states and their representatives in September and October 1999, the Task Force issued its Interim Report in October 1999.
4. The Interim Report set out a contextual framework for considering an agenda for the international community and small states themselves as they face up to challenges in the

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<sup>1</sup> Lists of the members of the Task Force, of the Advisory Board, and a chronology of the meetings and consultations are set out in Annex 1.

global economy. It also noted further work to be carried out before production of a final report. The Interim Report was discussed in November 1999 by the Commonwealth Ministerial Group on Small States which welcomed it and expressed “broad support for the recommendations of the report.” Commonwealth Heads of Government, in their Communiqué of November 15, 1999, gave the Interim Report a similar welcome. They recommended submission of a final report to the spring 2000 Development Committee meeting. The Interim Report was circulated widely to small states and development institutions and published electronically.

5. The Task Force has continued to take all available opportunities to consult on its Interim Report, including at an IMF-CDB high-level seminar in Barbados in February 2000. Comments were received from multilateral organizations as well as from small states, including a substantial written submission from the CARICOM Secretariat. The Task Force has drawn on these contributions as it completed its work. In particular, the last stage of the Task Force’s work has been guided by the discussions at a major global conference which the Commonwealth Secretariat and the World Bank arranged in London on 17-18 February 2000, involving senior ministerial and other representatives from 35 developing small states, 45 governments, and representatives of 25 multilateral, bilateral and regional institutions, and which was chaired by Prime Minister Owen Arthur of Barbados. This conference focussed on the four areas for further work identified in the Interim Report: tackling volatility, vulnerability and natural disasters; strengthening capacity; issues of transition to the developing global trade regime; and new opportunities and challenges from globalization. Paragraphs 46–105 below draw extensively on the work presented to that conference, and the subsequent discussions and emerging areas of consensus.
6. This Report is addressed both to small states themselves, and to the international development community. It seeks to set out a unified framework and a continuing agenda for action and analysis by the states themselves, and by the international and other organizations that provide external support and influence their development. Part II collects together more specific work programs (“frameworks”) on small states issues prepared and submitted to the Task Force by a number of multilateral institutions, including the World Bank and Commonwealth Secretariat. Part III presents comments about the work and conclusions of the Task Force delivered to the spring 2000 meeting of the Development Committee.

## What Makes Small States Different?

### Defining a small economy

7. There is no single definition of a small country because size is a relative concept. For instance, Simon Kuznets in “Economic Growth of Small Nations”<sup>2</sup> used an upper limit of 10 million people—by this measure, 134 economies are “small” today. Other indicators such as territory size or GDP are sometimes used. But population is highly correlated with territory size as well as with GDP; therefore, use of population as an indicator of size helps highlight small states’ limited resources.<sup>3</sup>
8. By the same token, there is no special significance in the selection of a particular population threshold to define small states. Indeed, the Commonwealth, in its work on small states, uses a threshold of 1.5 million people,<sup>4</sup> but it also includes larger member countries (Jamaica, Lesotho, Namibia and Papua New Guinea) because they share many of the same characteristics of smallness. For the work of the Task Force, the same threshold was chosen as a convenient yardstick for classifying all small states, and only sovereign states were considered. But we also concluded that no definition, whether it be population, geographical size or GDP, is likely to be fully satisfactory. In practice there is a continuum, with states larger than whatever threshold is chosen sharing some or all of the characteristics of smaller countries. This report and its conclusions should therefore be taken as applying, at least in some degree, to all such countries and territories.
9. Using the standard of a population below 1.5 million people, 45 developing countries<sup>5</sup> are small (see Table 1), accounting for nearly one third of the total number of developing countries. They are home to 20 million people, less than 0.4 percent of the total population of developing countries. They range in size from “micro-states” like Cook Islands, Nauru, Niue, Palau, St. Kitts and Nevis, and Tuvalu (with fewer than 50,000 people each) to Botswana, Gabon, The Gambia, Guinea-Bissau, Mauritius, and Trinidad and Tobago (with more than 1 million people each). The per capita GNP in these countries also ranges widely, from less than \$400 in several African countries (Comoros, The Gambia, Guinea-Bissau, and Sao Tome and Principe) to just \$700-1,300 in such countries as Cape Verde, Guyana, Kiribati, Maldives, Solomon Islands, and Tuvalu; to more than \$9,000 (The Bahamas, Brunei, Cyprus, Malta, and Qatar). There are small states in every geographic region, but most countries fall into three main groups: twelve

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<sup>2</sup> “Economic Growth of Small Nations” in E.A.G. Robinson, ed. 1960. *Economic Consequences of the Size of Nations*.

<sup>3</sup> Richard L. Bernal, 1998, “The Integration of Small Economies in the Free Trade Area of the Americas”, CSIS Policy Papers on the Americas, Volume IX.

<sup>4</sup> This definition of size was agreed by the Commonwealth Advisory Group in producing its report, *A Future for Small States: Overcoming Vulnerability*, Commonwealth Advisory Group, 1997.

<sup>5</sup> The coverage here is of all countries eligible for official aid, including one transition economy (Estonia) and developing countries, as listed in the *List of Aid Recipients Used for 1997 and 1998 Flows* issued by the OECD Development Assistance Committee. Further references to “small states” in this report are to this group of countries.

**Table 1. Population and GNP per capita of small states in 1998 \*\***

Country	Population (thousands)	Population Rank (1=smallest)	GNP per capita (US\$)
<b>Africa Region</b>			
Botswana	1,562	45	3,070
Cape Verde	416	27	1,200
Comoros	531	30	370
Djibouti	636	32	c/
Equatorial Guinea	431	29	1,110
Gabon	1,180	41	4,170
Gambia, The	1,216	42	340
Guinea-Bissau	1,161	40	160
Mauritius	1,160	39	3,730
São Tomé and Príncipe	142	16	270
Seychelles	79	10	6,420
Swaziland	989	38	1,400
<b>East Asia and Pacific Region</b>			
Brunei	315	24	a/
Cook Islands	20	5	..
Fiji	790	36	2,210
Kiribati	86	11	1,170
Marshall Islands	62	7	1,540
Micronesia, Fed. Sts.	113	14	1,800
Nauru	11	3	b/
Niue	2	1	..
Palau	19	4	b/
Samoa	169	18	1,070
Solomon Islands	416	28	760
Tonga	99	13	1,750
Tuvalu	11	2	1,150
Vanuatu	183	19	1,260
<b>Latin America and the Caribbean Region</b>			
Antigua and Barbuda	67	8	8,450
Bahamas, The	294	23	a/
Barbados	266	22	b/
Belize	239	20	2,660
Dominica	73	9	3,150
Grenada	96	12	3,250
Guyana	849	37	780
St. Kitts and Nevis	41	6	6,190
St. Lucia	152	17	3,660
St. Vincent and the Grenadines	113	15	2,560
Suriname	412	26	1,660
Trinidad and Tobago	1,285	43	4,520
<b>Other Regions</b>			
Bahrain	643	31	7,640
Bhutan	759	35	470
Cyprus	753	34	11,920
Estonia	1,450	44	3,360
Maldives	263	21	1,130
Malta	377	25	10,100
Qatar	742	33	a/

\*\* Countries listed are limited to those with a population of less than 1.5 million. In addition, Jamaica

Lesotho, Namibia, and Papua New Guinea are included among the Commonwealth small states.

Source: World Bank database. Classification according to 1998 GNP per capita, calculated using

the *World Bank Atlas* method:

a/ High income economy (per capita GNP \$9,631 or more)

b/ Upper middle income economy (per capita GNP \$3,031-\$9,630)

c/ Lower middle income economy (per capita GNP \$761-\$3,030)

d/ Low income economy (per capita GNP \$760 or less)

states are in the Caribbean region, fourteen in East Asia and Pacific, and twelve in Africa. Of the remaining seven countries, two are in South Asia, two in the Middle East, and three in Europe.

### **Economic implications of small size and emerging challenges**

10. The following characteristics have important implications for development and are shared by many small states:

- *Remoteness and insularity.* Of the 45 small states, 34 are islands, a number of which are located far from major markets—as in the case of the Pacific islands and Mauritius. Some are widely dispersed multi-island micro-states.
- *Susceptibility to natural disasters.* Most small states are in regions frequently affected by adverse climatic and other natural events which, typically, affect the entire population and economy. They may also be susceptible to severe environmental and ecological threats.
- *Limited institutional capacity.* Sovereignty necessitates certain fixed costs of providing public services, including policy formulation, regulatory activities, education and social services, justice, security, and foreign affairs. Indivisibilities in the provision of these public goods mean that small states face higher costs per person unless ways can be found to pool such costs, for example on a regional basis.
- *Limited diversification.* Because of their narrow resource base and small domestic markets, many small states are necessarily relatively undiversified in their production and exports. So capacity in the private sector is also limited, posing difficulties when faced with a need to respond to changing external circumstances.
- *Openness.* Small economies tend to rely heavily on external trade and foreign investment to overcome their inherent scale and resource limitations. While this can prove beneficial in exposing them to outside competition and ideas, it leaves them vulnerable to external economic and environmental shocks, especially where the domestic economy is undiversified.
- *Access to external capital.* Access to global capital markets is important for small states, and is one way to compensate for adverse shocks and income volatility. But the evidence is that private markets tend to see small states as more risky than larger states, so that spreads are higher and market access more difficult.
- *Poverty.* There is some evidence that poverty levels are higher, and income distribution more uneven, in smaller than in larger states.

11. In outlining these common characteristics, it is also important to recognize a great diversity among the small states themselves. For instance, the stage of development, constraints and opportunities facing a remote micro-state such as Kiribati (see Box 1) vary significantly from, for example, a larger and wealthier state in the Caribbean or a landlocked African small state. Thus, policy options and approaches will need to be tailored to regional and country circumstances.

12. A limited capacity to exploit economies of scale or to diversify production in small domestic markets does not necessarily imply lower per capita income or slower economic growth. If small states have a richer per capita endowment of natural resources or human

resources than large states, this will tend to offset size disadvantages—as in oil-abundant small states or those that are well-situated climatically for tourism. Small states do tend to have higher education attainment and better health indicators than larger developing countries, reflecting sound domestic policies in these areas in many small states. Historically, they have also benefited from relatively high inflows of official development assistance. This has contributed to the advancement of small states and helps explain their development record but, along with indivisibilities in the provision of public services, has resulted in relatively large proportion of their economic activities being in the public sector. Most important, smaller economies tend to rely heavily on external trade in goods and services and openness to foreign investment to overcome their inherent scale limitations, and this openness is itself a strength. On balance, there is no statistically significant difference in per capita incomes and in economic growth rates between large and small states, indicating that other factors have offset the inherent disadvantages of small states' remoteness, small domestic markets, and public sector dominance of their economies.

### *Remoteness and isolation*

13. The remoteness and isolation of many small states, particularly in Africa and in the Pacific, has significant economic and administrative implications. Isolation means that these countries are far from the major centers of trade and commerce. It becomes more difficult to compensate for the drawbacks of limited size and small domestic markets by turning to world markets. Transportation costs tend to be high, resulting from the distance of these countries from principal export markets and their main suppliers of inputs. Further, in small states made up of dispersed island groups such as in the Pacific, the development of even a small domestic market is constrained by distances between settlements and infrequent internal transport services.
14. Small economies also pay higher transportation costs because of the relatively small volume of cargo, small cargo units, and the need for bulk breaking, particularly if freight carriers and airlines attempt to exploit monopoly positions. High international transport costs serve to increase the cost of exports, thereby reducing their competitiveness and reducing export returns. Similarly the costs of imports are increased, resulting in consumer welfare losses. Using the ratio of insurance and freight debits to merchandise imports as an indicator of transport costs,<sup>6</sup> demonstrates that small, especially island, states are heavily represented amongst countries facing the highest costs. For example, the percentage values of this ratio are, for: Kiribati 26; Comoros 24; São Tomé 23; Tonga 22; Vanuatu 20; Gabon 20; The Gambia 20; Solomon Islands 20; Equatorial Guinea 19; Trinidad & Tobago 18; and Seychelles 18 (others with high ratios were large, land-locked African countries)<sup>7</sup>. These figures are significantly higher than the median value of 14 percent for all developing countries.

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<sup>6</sup> The ratio to imports, rather than exports, is used since goods exports are a fraction of merchandise imports for many small states. As a result, to use exports in such cases would seriously bias upward the transport cost ratio for those countries.

<sup>7</sup> Atkins, J P, Mazzi, S, A & Easter C D, *Commonwealth Vulnerability Index for Developing Countries*, Economic Paper, No. 40, Commonwealth Secretariat, London, 2000.

### **Box 1. The challenges facing Pacific island states – the case of Kiribati**

Kiribati has a population similar in size to that of Andorra, but spread over an area roughly equal to that of Europe. Most of its area is ocean: its land mass amounts to 810 square km, compared to an Exclusive Economic Zone of 3.55 million square km. The vast geographic spread of the 33 islands reaches 4,000 km from east to west and roughly 2,000 km from north to south. Transport within Kiribati is extremely limited and is primarily by boat. The nearest large markets are 4,000 km away, in Honolulu and Brisbane. There are only six flights a week in and out of the country, all by small plane. Hence distance from and access to markets not just externally but internally presents challenges of a magnitude faced by few other countries.

The resource base is very narrow. The arid climate and poor soil offer little potential for agricultural development. Ocean resources are the mainstay of the economy—about 80% of households make a living or survive through fishing. The public sector dominates all spheres of economic activity. Fishing licensing fees are the major source of foreign exchange and government revenue while import duties and remittances from I-Kiribati employed in foreign shipping fleets provide significant additional government revenue and foreign exchange, respectively.

The population of 88,500 is concentrated in the Gilbert Islands Group, which includes Tarawa, the capital. One-third of the population live in the urban center on South Tarawa, where density reaches 1,610 persons per square km while the Phoenix Group is virtually uninhabited. If present trends continue, population will double within 20 years; such an outcome will present even greater challenges to efforts to overcome environmental and health problems, particularly in Tarawa where sanitation and water problems are already pressing. The demographic profile of Kiribati is skewed to the young which is placing significant strain on the Government to provide basic health and education services.

Kiribati's numerous, small and low-lying islands heighten its environmental vulnerability, especially to sea-level rises; some islets and bird sanctuaries have already disappeared.

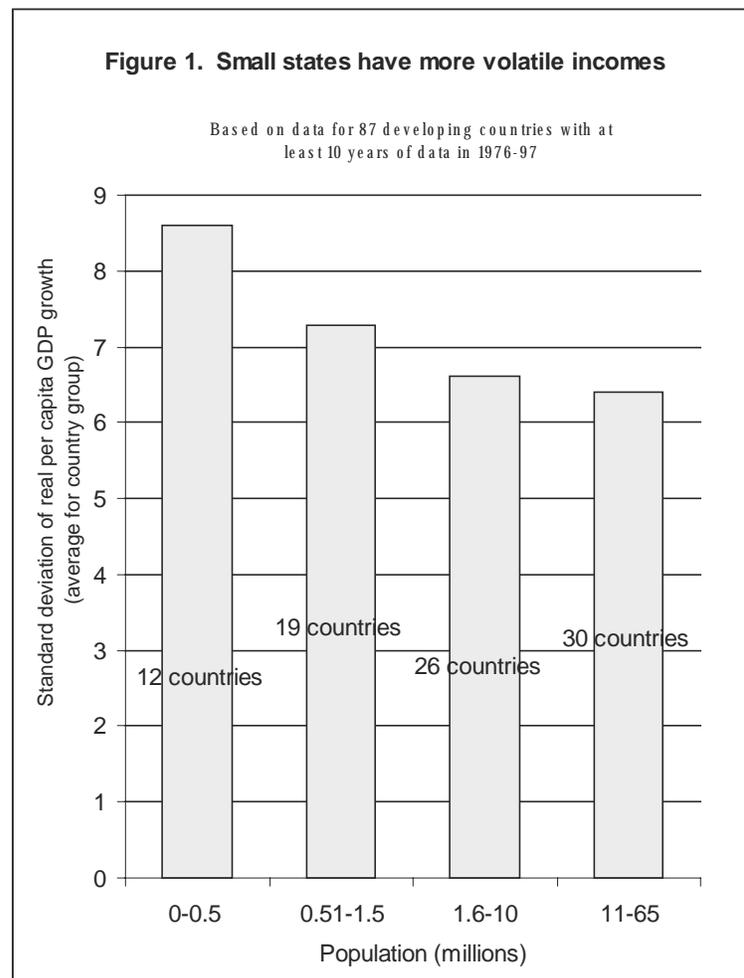
In addition to these constraints, Kiribati's potential to benefit from globalization is hampered by its limited institutional and human capacity. The society has strong traditional practices and values based on family relationships, the sharing of resources and a co-operative approach to economic activity. The private sector is very small and fragmented; the privatization program has not progressed very far, in part because of fears that the private sector cannot fill the gaps. These factors present challenges to the Government in determining the most appropriate pace and sequencing of policy changes in areas such as privatization, downsizing and improving the performance of the public sector, tax and duty reforms (which would initially have negative revenue consequences), and the installation of modern technologies. And while embracing the global trading regime will deliver certain benefits, commodity exports will continue to be hampered by Kiribati's remote location and irregular supply routes.

15. Limited domestic market size combined with large distances from overseas markets often results in a lack of competition; in some instances the size of the market can only support a single producer. As a result, the economies of small states do not benefit from the effects of competition on improving efficiency, lowering costs, and spurring innovation.
16. One positive aspect of remoteness is that some isolated small states have entitlements to vast areas of the ocean, through the designation of Exclusive Economic Zones. For example, the Exclusive Economic Zone of Kiribati is approximately the same size as the entire Caribbean Sea. However, successful and sustainable exploitation of such resources

requires large investment as well as monitoring and policing of their use by national and foreign agents.

*Income volatility*

17. The residents of small states experience higher volatility in their incomes than people living in large states; the standard deviation of annual real per capita growth is about 25 percent higher (Figure 1). This year-to-year volatility stems from three causes: (i) the economies are more open to fluctuations in world market prices because in small states a much larger share of domestic economic activity is accounted for by exports and imports than in larger economies; (ii) small states by their nature have relatively undiversified production and exports ; and (iii) many of the small states are particularly prone to natural disasters, which because of small size affect the whole community. The importance of these factors varies widely among small states. For most of the poorer small states, small size is associated with relatively high specialization in production and trade. Some states—for instance, Cyprus and Malta—are both very open to trade and have relatively more diversified economies.



## Openness

18. While most small states produce a relatively narrow range of goods and services, they consume a wide range of them and, as a result, they have high trade to GDP ratios (Table 2). The high degree of openness brings real benefits that accrue from trade—consumers in small states are able to obtain a greater variety of goods at lower costs than if their choices were confined to domestically produced goods while producers in small states can sell on the world market—provided they have effective market access—earning more than if they were confined to meeting limited domestic demand. Participation in the world market also helps to channel new ideas and information about opportunities to firms and consumers in small states.

**Table 2. Small economies are highly open to trade**

Region	Number of countries with data	Average share of GDP (percent)		
		Exports	Imports	Exports+Imports
Africa	12	49	67	116
Caribbean & Latin America	11	55	65	120
Pacific	6	38	74	112
<i>Memo:</i>				
<i>All low income countries</i>		19	19	38
<i>All middle income countries</i>		22	24	45

Source: World Bank database. Based on data for exports of goods and services for latest available year in 1992-98.

19. Openness to trade also means that small countries have a larger stake in a stable, rule-based, world trade environment than their small share of world trade would indicate. The terms of trade of small countries—the price of their exports (which tend to be concentrated in a relatively narrow range of goods and services) relative to the price of their imports (which tend to cover a broad range of goods and services)—are not significantly more volatile than those of other developing countries. But because such a large proportion of domestic economic activity is accounted for by exports and imports, even minor disruptions in world markets—such as fluctuating demand and prices for exports, whether of commodities or services like tourism—can have a large impact on their economies. Because of their high openness to trade, small states tend to be more dependent than large states on taxes on imports for their fiscal revenue.<sup>8</sup> The high volume of external trade provides a convenient, broad tax base from which taxes can be collected at a relatively low administrative cost. Reduction of average import tariffs as part of overall external trade liberalization therefore can lead to a fall in tax revenues that is not always easy to offset in the short term by raising other taxes, creating potential problems of rising debt.

<sup>8</sup> Some open small states derive as much as 60 percent of their tax revenues from taxes on external trade, compared to an average of 21 percent for large developing countries.

### *Limited diversification*<sup>9</sup>

20. As already noted, a major reason why small size may be disadvantageous is that it constrains the opportunities for diversification, and promoting efficiency through domestic competition.
21. The Pacific countries provide a stark example of commodity export concentration (Table 3). Similar situations prevail in small states in other regions. In Lesotho, over 80 per cent of total merchandise exports came from garments in 1997. Reflecting a different dimension of concentration, re-exports to neighboring countries accounted for 85 per cent of The Gambia's total exports in 1996/97. Tourism is a major export for the Caribbean and the Indian Ocean (Table 4). Total earnings from tourism and bananas in Dominica changed little over the period 1991-1996. However, at the start of that period, bananas contributed more than 56 per cent of these earnings, whereas tourism provided almost 70 percent in 1996. In the same year, tourism contributed over 82 per cent of Grenada's export earnings. For the Maldives, the growth of merchandise exports has plummeted from over 40 per cent in 1994 to less than 6 per cent in 1996. Reduced fish exports was a major factor in this decline, but tourism continued to expand. To a large extent, export concentration remains high in these regions—albeit with movement toward specialization in different sectors.

**Table 3. Concentration of export commodities and services in the Pacific**  
(as a percentage of exports of goods and services, 1997)

		First commodity or service	Second commodity or service
Fiji		26.3 (tourism)	11.9 (sugar)
Kiribati	<i>a/</i>	34.5 (copra)	18.2 (tourism)
Marshall Islands		38.0 (chilled fish)	7.3 (tourism)
Micronesia, FS	<i>b/</i>	40.1 (fish)	9.8 (tourism)
Papua New Guinea	<i>a/</i>	28.3 (gold)	18.7 (crude oil)
Samoa		50.6 (tourism)	4.1 (copra)
Solomon Islands		33.9 (logs)	8.3 (palm oil)
Tonga		28.4 (tourism)	11.9 (squash)
Vanuatu		41.6 (tourism)	14.4 (copra)

*a/* 1998 data. *b/* 1996 data.

Source: *World Bank database*.

22. Tourism development can capitalize on the considerable and unique natural endowment of many small states and their coastal areas, especially those that are well-situated climatically or have high potential for ecotourism. Tourism expansion has particular consequences for small states, however. In all regions, it is generally associated with rapid import growth. For many countries, this involves non-indigenous food imports (meat, milk and dairy products feature strongly in the Caribbean) or inputs to construction of tourism-related facilities—especially for countries such as the Maldives. Linkages to the

<sup>9</sup> Where not otherwise specified, the data presented in this sub-section are sourced from Commonwealth Secretariat, *Small States: Economic Review & Basic Statistics*, Fourth Volume, December 1998.

rest of the domestic economy are often limited as many types of tourism facilities are in effect enclave developments. And the environmental impact can be large, may limit the scope for expanding tourism, and needs careful handling if tourism development is to be sustainable. So while tourism development can contribute and has contributed to development in many small states, it should not be regarded as a panacea.

**Table 4. Concentration of export commodities and services in the Caribbean**  
(as a percentage of exports of goods and services, 1997)

	First commodity or service	Second commodity or service
Antigua & Barbuda <sup>a/</sup>	61.0 (tourism)	4.6 (re-export of petroleum)
Barbados <sup>a/</sup>	54.9 (tourism)	2.8 (sugar)
Belize	27.8 (tourism)	14.2 (sugar)
Guyana	17.9 (sugar)	11.3 (rice)
St. Kitts	50.7 (tourism)	12.1 (sugar)
St. Lucia <sup>a/</sup>	75.6 (tourism)	8.6 (bananas)
St. Vincent <sup>a/</sup>	43.7 (tourism)	10.5 (bananas)

<sup>a/</sup> 1996 data.

Source: *World Bank database*.

23. Overall, there appears to have been little significant diversification in recent years in the majority of small states. In some countries, income from the production and export of primary commodities has been replaced by that from service sector activities—notably tourism, and in some cases financial services. In other small states, which have remained concentrated on primary commodities, GDP growth has often been poor or stagnated as a result of weak or volatile world market prices. But generally where one dominant activity has declined it has tended, as would be expected, to be replaced by another dominant activity, rather than leading to a more diversified economy.

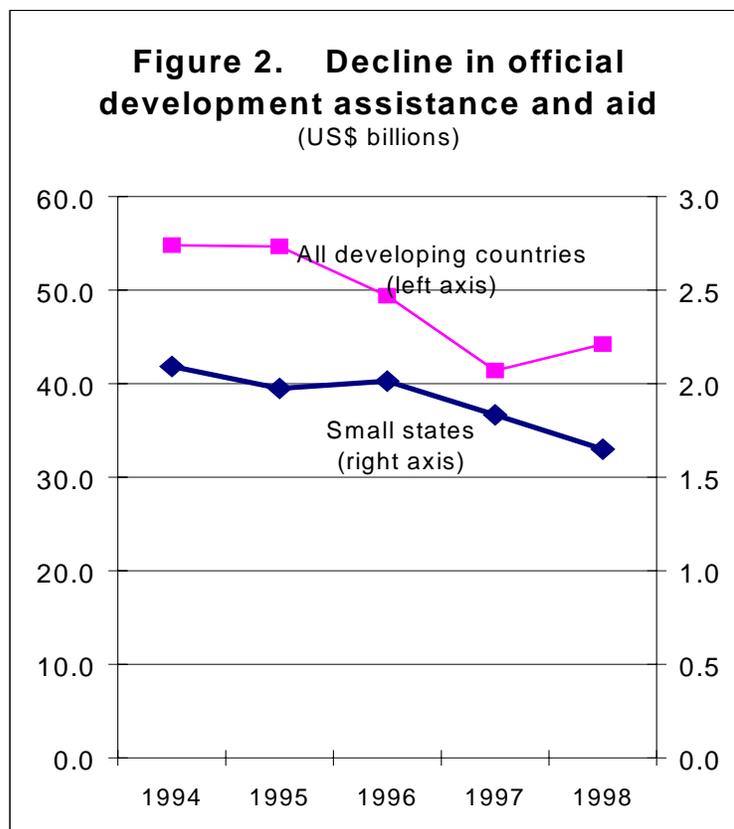
#### *Susceptibility to natural disasters and environmental change*

24. Most small states are situated in regions which are highly susceptible to natural disasters—cyclones, floods, hurricanes, tsunamis, drought, desertification, volcanic activity, etc. Their incidence regularly results in severe economic disruption through infrastructure damage and production and export losses. Because of the catastrophic nature of many of these disruptions, considerable income and development opportunities are regularly forgone. Notably, the entire physical environment, population and economy are affected and, often, so are those of neighboring countries. In extreme cases, such as volcanic eruptions, a nation's very existence may be threatened. The United Nations Disaster Relief Organization has estimated that the impact on the 25 most disaster-prone countries (including 13 small island states) has entailed costs between 28 percent and 1,200 percent of their annual GDP. For instance, in 1989 a series of cyclones in Vanuatu resulted in damage and economic losses amounting to twice the country's national income. Small states can also suffer from other kinds of disaster: for example, like larger developing countries, some have a high incidence of HIV/AIDS which can have a disproportionate impact in small communities with already limited capacity.

25. Global developments pose major environmental challenges for small states, made more serious by the fragility of some ecosystems, especially the coral reefs surrounding many of the island states. Global climatic change has increased the incidence and severity of natural disasters and it has been suggested that, as a consequence of global warming, sea-level may rise by one meter over the coming 100 years. This could result in significant losses in land area for some low-lying countries; in Kiribati, the Maldives, the Marshall Islands, and Tuvalu, entire atolls and islands might face extinction. On average, the effects of sea-level rise are estimated to be disproportionately more severe for small states than for larger countries.

*Access to external capital*

26. Openness to capital flows is important for small states. Like other developing countries, they stand to benefit from foreign direct investment flows. And those with access to world capital markets can in principle turn to them to smooth out consumption over time to compensate for adverse shocks to domestic production—though this cannot and should not be used to compensate for a permanent loss of national income. Many small states, however, depend heavily on official development assistance and official aid to help finance their development expenditures and have only limited access to commercial borrowing, particularly those that suffer from the repeated incidence of natural disasters or that for other reasons may be perceived as high risk.
27. For this reason they have been particularly hard-hit by declining trends in aid. The flow of official development assistance and official aid to small states has fallen in recent years—from \$2 billion annually in the mid-1990s to \$1.8 billion in 1997 and further to \$1.6 billion in 1998 (Figure 2). Small states thus experienced a decline in assistance of 24 percent between 1994 and 1998, which is even more pronounced than the decline that affected all developing countries (19 percent during the same period). Similarly, in the last two years for which data are available (1997 and 1998) many small states received a lower level of aid per capita than in the early 1990s, with the decline most marked in small African countries (see Table 5).



28. Turning to private financial flows, many small states are limited in their access to commercial borrowing. A number already have high levels of indebtedness, practically precluding commercial borrowing.<sup>10</sup> Even those countries which have relatively low levels of external debt, however, can find it difficult to borrow. Evidence suggests that information costs and country risk issues, sometimes reflected in financial and capital market regulation in capital exporting countries, often result in small states' facing higher spreads for their borrowing, if they are able to borrow at all. Gathering information about the capacity to repay a loan has significant fixed costs. While there are no major differences in the cost of monitoring the capacity to repay of small and large states, there are large differences in the absolute size of the underlying financial transaction, making lending to small states less attractive. The higher cost of enforcing contracts, reflecting differences in legal, administrative and justice systems, is a further factor leading to higher spreads. Moreover private markets and credit rating agencies also take account of the greater vulnerability and volatility of small states' incomes, as discussed above. For all these reasons, many small states' integration with the international financial and capital markets is more costly and narrow than is desirable.

<sup>10</sup> Annex 3 shows indicators of external indebtedness.

**Table 5. Inflows of assistance and foreign direct investment to small states**

Country	Aid per capita, annual average, US\$		FDI per capita, annual average, US\$	
	1991-92	1997-98	1991-92	1997-98
<b>Africa</b>				
Botswana	92	74	-4	63
Cape Verde	319	293	0	33
Comoros	125	60	2	4
Djibouti	203	132	2	9
Equatorial Guinea	170	58	65	52
Gabon	106	36	34	-65
Gambia, The	108	32	8	10
Guinea-Bissau	109	96	0	1
Mauritius	53	35	15	29
Sao Tome and Principe	449	220	0	0
Seychelles	297	243	204	646
Swaziland	66	29	103	80
<b>East Asia and Pacific</b>				
Brunei	17	1	..	..
Fiji	71	51	72	58
Kiribati	311	194	6	5
Marshall Islands	80	930	..	..
Micronesia, Fed. Sts.	71	784	..	..
Palau	..	3,467	..	..
Samoa	327	189	25	21
Solomon Islands	118	103	43	55
Tonga	223	270	5	25
Tuvalu	..	..	..	..
Vanuatu	302	187	166	158
<b>Latin America and the Caribbean</b>				
Antigua and Barbuda	93	106	578	285
Bahamas, The	8	44	-2	764
Barbados	5	38	40	55
Belize	115	62	76	79
Dominica	199	228	250	281
Grenada	149	78	203	224
Guyana	136	212	90	109
St. Kitts and Nevis	175	168	407	600
St. Lucia	180	105	362	302
St. Vincent and the Grenadines	130	118	129	363
Suriname	153	164	-44	-52
Trinidad and Tobago	2	18	141	675
<b>Other Regions</b>				
Bahrain	106	99	..	..
Bhutan	93	81	0	0
Cyprus	48	49	135	68
Estonia	39	53	53	292
Maldives	155	98	32	37
Malta	36	59	162	646
Qatar	3	1	..	..
<b>Median for small states</b>	109	98	37	53
<i>Memo: Median for all</i>				
<i>low income countries</i>	42	31	1	3
<i>lower middle income ctries</i>	44	31	4	33
<i>upper middle income ctries</i>	13	12	14	68

Source: World Bank database.

"Aid" is Official Development Assistance and Official Aid (DAC definition).

29. Foreign direct investment brings not only capital but is often critical in linking the more isolated small states to developments abroad. Foreign firms can be an important source of know-how for improving private sector capacity overall and of information on new technologies and market opportunities. As the data in Table 5 show, some small states received substantial inflows of FDI in the late 1990s. Total flows of FDI to small states averaged about \$2.1 billion annually in 1996-98<sup>11</sup>, some 15 percent above the official development assistance and aid flows, but with a very different distribution among the regions and countries. Nearly 80 percent of the FDI received by small states went to just seven countries (Bahamas, Botswana, Estonia, Equatorial Guinea, Guyana, Malta, and Trinidad and Tobago). As with commercial borrowing and other financial flows, an analysis of FDI flows in the last two decades shows that small states are at a disadvantage in attracting FDI relative to other developing countries. Even when they have good policies and other characteristics (such as good human resource development indicators), small states are rated to be significantly more—28 percent more—risky.<sup>12</sup> To some extent, this may reflect greater underlying riskiness of their economies. It may also reflect the weaker incentives that risk rating agencies and investors have to do their homework and learn about opportunities in small states. International development institutions should use every opportunity to help ensure that existing market information is made available to potential investors to reduce the perceived risks. It has been estimated that, on average, the relatively high flows of aid to small states are appropriate to offset additional perceived risks to private direct investors.<sup>13</sup>

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<sup>11</sup> Based on available data for 30 countries.

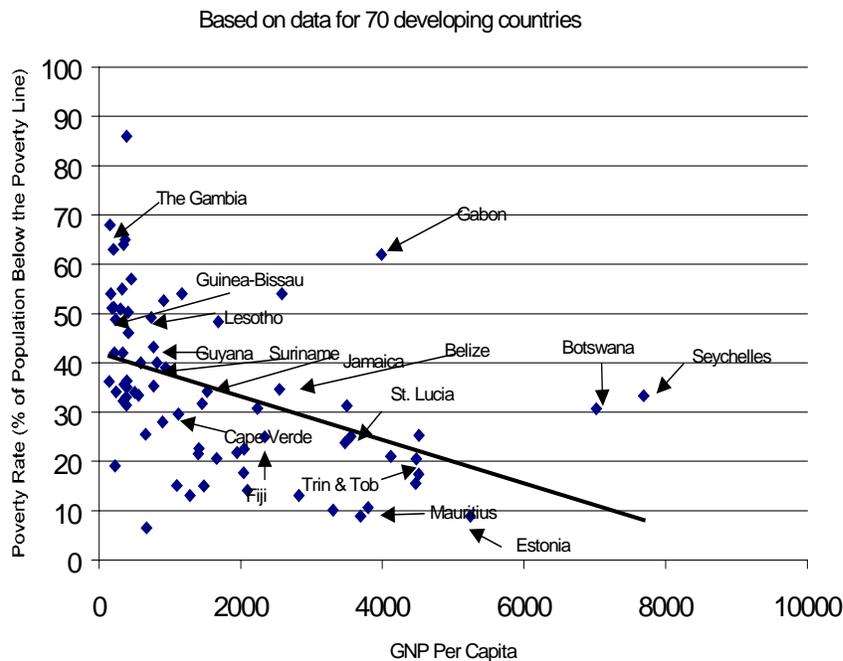
<sup>12</sup> Paul Collier and David Dollar, *Aid, Risk, and the Special Concerns of Small States*, February 1999.

<sup>13</sup> *Ibid.*

Poverty

30. Though a number of the small states have achieved high average per capita incomes relative to other developing countries, poverty remains a serious challenge. Most of the small states (with the notable exception of the low-income countries in Africa and the Pacific) have better education and health indicators than larger developing countries.<sup>14</sup> Figure 3 shows available data on the percentage of households living in poverty in seventy developing countries. These data indicate that, as expected, poverty prevalence declines with per capita income (the trendline shown in the figure). Although only a few small states have reliable information on poverty and equality, for a number of those for which data are available poverty rates are higher than those expected in countries with the same per capita income. While the sample size for small states is small, and the data on poverty rates are not strictly comparable because of methodological differences, the fact that a number of small states have higher poverty than their per capita income indicates corresponds with anecdotal evidence that, for example, the multi-island nature of some states is in many cases associated with a particularly uneven distribution of income, with the bulk of economic activity concentrated in the capital while more remote regions are much poorer. Clearly, where there is a high prevalence of poverty because of an uneven distribution of income, income volatility creates additional hardship and may tend to reduce equality over time as the poor are less able to weather negative shocks to their incomes.

Figure 3. High poverty rates prevail in some small states



<sup>14</sup> Annex 3 shows recent basic and social indicators.

### *Limited institutional capacity*

31. Sovereignty implies the provision of a range of public goods and services. These include the central functions of government, regulatory activities, tax administration, provision of education, health and social services, a judicial system, foreign relations, and security. To the extent that there are indivisibilities in the provision of such public services, the fixed costs must be spread among the population. While regional co-operation has helped in some cases, a state's small size implies higher unit costs. In the private sector, firms from small countries tend to be small both by global standards and by comparison with firms in large developing countries; size often makes a difference in a firm's ability to survive and compete in the global marketplace.

- *Public sector capacity*

32. The limited institutional capacity of the public sector tends to be stretched in all small states, but particularly so in those countries that have high internal transport costs. Provision of basic services—education, health, social welfare—is highly fragmented, increasing unit costs, decreasing efficiency, and making access difficult, especially in the poorer countries of Africa or widely dispersed islands in the Pacific. Similarly, physical infrastructures relating to these services can be expensive; typically most of the inputs must be imported and transported over great distances. Government services and extension, and the legal and financial systems cannot be practically replicated in many separate locations, resulting in greater cost of access to them by citizens not located in the main centers.

33. To take one public service as an illustration, in education, small schools and training facilities often imply generalist rather than specialist teaching staff, and small class sizes lead to mixed age groups. Often, it is simply not economically feasible to provide secondary, tertiary and specialist training, and resort is made to education abroad. While this has potential advantages, a significant proportion of trained personnel become part of a “brain drain”, choosing not to return to their home countries, preferring the higher remuneration, living standards and opportunities that they can enjoy elsewhere. Distance learning, such as the Commonwealth of Learning helps to provide, can enable students to qualify at home, increasing the likelihood that necessary skills will remain in country. But the provision of the necessary support, human and technical, can be beyond the means of the poorer and more dispersed states who, accordingly, will require supplementary resources and assistance.

34. Small country size also means that, in order to try and confine the size of the public sector within reasonable limits, Ministerial portfolios must be multifaceted, involving a range of sectors and issues and placing heavier burdens on administrators and personnel. When one individual performs a number of different functions, there are benefits of information-integration but also a significant institutional capacity loss when the services of that individual are no longer available. The median wage bill of the public sector as a proportion of GDP in small states (31 percent) is significantly higher than in large developing countries (21 per cent).<sup>15</sup> This high share of the public sector reduces the

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<sup>15</sup> Comparable data were available for 10 small states and 37 large countries, in 1995.

efficiency with which small states resources are used and diminishes the productivity of investments.

35. The administrative characteristics of many small states can be summarized as follows<sup>16</sup>

- Small staffing for multiple portfolios—leading to overextended personnel, small spare/reserve capacity, few specialists attracted or retained, limited promotion and mobility;
- Limited financial resources—resulting in inadequate compensation levels, inappropriate and infrequent training, high turnover rate;
- Lack of training—leading to shortage of management skills, low problem solving capacity, low levels of innovation and entrepreneurship, low adaptability to changing conditions, timid decision making, excessive routine dependence;
- Poor working environments and lack of alternative opportunities outside the public sector—creating low morale and motivation, low job satisfaction, low productivity, high levels of fear and frustration, absenteeism, systemic uncertainty

36. In a global context, insufficient institutional capacity in the public sector (and often the high financial costs involved) means that many small states are unable to participate fully in international financial and trade negotiations, the outcomes of which can profoundly affect their economies. Indeed, some small states do not have a presence in Brussels or Geneva to represent their interests on ACP/EU issues relating to the successor agreement to the Lomé IV Convention and in the WTO. Nor are these countries able to hire experts and trade negotiation lawyers to advance their cause. In bilateral negotiations of this nature on trade and finance, the uneven balance of power significantly influences the outcomes. This is starkly illustrated by the case of Vanuatu, the first Least Developed Country (LDC) to apply for accession to the WTO, which after five years of negotiations costing nearly \$400,000 is considering the withdrawal of its application on the basis of what it considers to be unreasonable demands from powerful WTO members for concessions. Finally, for the development institutions and donors, smallness leads to high transactions costs for what are inevitably small projects. This can result in a reluctance to provide financing which, coupled with the lack of capacity for project formulation within the country, closes off potential development opportunities.

- *Private sector capacity*

37. Most firms in small states are small, largely because small domestic markets and poor endowments of physical resources limit entrepreneurial opportunities. Small firms are at a disadvantage because they cannot realize economies of scale (which are important in some sectors), are not attractive business partners (often because they are less well known and hence are perceived as unreliable), and cannot spend significant funds on marketing, market intelligence, and research and development. Competitive advantage is more likely to occur when the domestic economy is large enough to support clusters of firms in any given sector, with horizontal and vertical relationships. Such opportunities—and the realization of economies of scope, whereby a large firm or cluster of firms use existing resources, skills and technologies to generate new products—are less available in small

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<sup>16</sup> Khan, J. *Public Administration in the Caribbean*, Typescript, 1991.

and isolated economies.<sup>17</sup> Small size and isolation also limit development of new knowledge and technology oriented to the domestic market. Moreover, small firms in small states are often nevertheless monopolies or oligopolies in terms of the local market, without the advantages of the spur of local competition. Regulating local monopolies is often too great a challenge for a thinly-spread administration. Moreover, the task can be made more difficult in some very small states when the regulator and the regulated are from the same family or childhood friends;<sup>18</sup> or where the local monopoly is owned by a large and powerful overseas investor.

38. For physical goods, the need to focus on production for exports in distant and changing markets can make for particularly difficult, often risky, product-selection decisions which must take into account possibilities for economical aggregation of cargo and sharing of marketing costs. Small domestic markets and the difficulties in establishing export competitiveness are exacerbated by education and training limitations, poor market institutions and infrastructures, as well as small and sometimes inadequate local financial institutions and regulations.
39. A weak private sector also tends to limit the absorptive capacity of small states, both in terms of aid and investment (foreign and domestic). This is because participants in the sector lack the necessary skills in generating innovative project ideas and proposals, and in demonstrating their investment worthiness with respect to returns. An weak private sector may also lack the capacity to adjust to lower tariff protection and greater competition without transitional assistance.

### **A measure of vulnerability**

40. The above factors—remoteness and isolation, volatile economic growth, investor perceptions, high poverty and limited institutional capacity—suggest intuitively that small states would be more vulnerable than their larger developing country counterparts. Vulnerability means exposure to exogenous shocks over which the affected country has little or no control, and relatively low resilience to withstand and recover from these shocks. Hence, it is useful to consider the combined effect of these different sources of vulnerability on particular countries, allowing for their resilience. A number of alternative indices have been developed by the Commonwealth Secretariat<sup>19</sup>, the Caribbean Development Bank (CDB)<sup>20</sup>, the Committee on Development Policy (CDP) of the UN ECOSOC<sup>21</sup>. and, earlier, by Briguglio.<sup>22</sup> While the results differ in detail and coverage from the Commonwealth index, these other indices give broadly similar results.

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<sup>17</sup> Richard L. Bernal, 1998, *The Integration of Small Economies in the Free Trade Area of the Americas*, CSIS Policy Papers on the Americas, Volume IX.

<sup>18</sup> Richard L. Bernal, 1999, oral comments to the Task Force.

<sup>19</sup> See Atkins, J P, Mazzi, S and Easter, C D (2000), *A Commonwealth Vulnerability Index for Developing Countries: The Position of Small States*, Economic Paper No. 40, Commonwealth Secretariat, London. This index was developed based on three years of intensive research carried out with the mandate and encouragement of Commonwealth finance ministers, endorsed by heads of government.

<sup>20</sup> Described in Crowards, T (2000), *An Index of Economic Vulnerability for Developing Countries*, Draft, Caribbean Development Bank, Barbados.

<sup>21</sup> See Guillaumont, P, (1999), *On the Economic Vulnerability of Low Income Countries*, mimeo, CERDI-CNRS, Université d'Auvergne, France. Although the intended purpose of this index is to discriminate between Least Developed and other developing countries.

41. The Commonwealth vulnerability index ranks developing countries according to measurable components of exposure and resilience to external shocks. The analysis confirms that small states are considerably more vulnerable than other developing countries. Construction of the index is based on the observation that income growth volatility is the most apparent manifestation of vulnerability,<sup>23</sup> and starts by identifying sources of this volatility. The three most significant determinants of income volatility identified by the Commonwealth Secretariat are:
- The lack of diversification (as measured by the United Nations Conference on Trade and Development's diversification index).
  - The extent of export dependence (as indicated by the share of exports in GDP).
  - The impact of natural disasters (as represented by the portion of the population affected, reflecting the cumulative frequency and impact of these events over the past 27 years).<sup>24</sup>
42. These underlying sources of volatility are then combined to form a composite index of the impact of vulnerability on developing countries. The resulting index is then weighted by average GDP as a proxy for resilience, the second component of the Commonwealth vulnerability index.<sup>25</sup>
43. The ranking of countries is based on a sample of 111 developing countries (34 small and 77 large) for which relevant data were available. According to the impact component of the index small states are systematically more vulnerable than large countries, regardless of income. When impact is combined with resilience to form the Commonwealth vulnerability index, some country rankings improve dramatically, reflecting an intuitive notion that such states should be able to manage their vulnerability by using their own resources. But as shown in the quartile analysis of Table 6, small states still account for most vulnerable developing countries:
- Of the 28 most vulnerable countries, 26 are small states (18 islands)
  - Of the 28 countries with higher medium vulnerability, 6 are small states (6 islands)
  - Of the 27 countries with lower medium vulnerability, only 2 are small<sup>26</sup>
  - Of the 28 countries with low vulnerability, all are large
44. An important aspect in interpreting the results of the Commonwealth's vulnerability index is that it measures the total effect of the elements included. The results should not be interpreted to imply that trade openness is detrimental to small states. But they do suggest that when openness is associated with an undiversified economy, the high incidence of

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<sup>22</sup> Briguglio, L (1995), *Small Island Developing States and their Economic Vulnerabilities*, World Development, 23(9)

<sup>23</sup> There was no significant difference between small and large countries in terms of per capita GDP or GDP growth rates.

<sup>24</sup> About 30 variables—representing the economic, environmental, and spatial dimensions of the characteristics of developing countries—were tested in an econometric modeling exercise to identify a small number of highly significant indicators influencing vulnerability.

<sup>25</sup> Government reserves and domestic savings, net of debt servicing requirements, could have been used, subject to data availability. However, GDP was selected because of the large income costs associated with the most severe external shocks - natural disasters.

<sup>26</sup> The two small countries were Cyprus, which has an advanced, diversified economy, and Trinidad and Tobago, which is also reasonably diversified, including benefiting from oil export revenues.

natural disasters and relatively low incomes, these factors combine to make small states vulnerable. Looking at components of the index another way, a high degree of diversification can be interpreted as a measure of resilience in that it creates a lower level of vulnerability. When coupled with high trade openness, this can give greater scope for responding to new trade opportunities and exploiting economic dynamism. Further, it should be noted that the index makes no attempt to explain total income growth volatility. Other factors, both internal and within the control of government, can have an influence.

45. Another dimension of vulnerability relates to threats to the environment and damage to fragile ecosystems. The Commonwealth report (Atkins, et al, 2000), describes some preliminary work on a composite environmental index. The components of this simple index included: deforestation; population pressure; water scarcity; marine inundation; threats to biodiversity; and the incidence of natural disasters. Data constraints limited the sample to 106 countries. The results suggested that, with the single exception of Bangladesh, the ten most vulnerable countries were small states. However, the index does not discriminate as clearly between large and small states as does the Commonwealth (economic) vulnerability index. This might be expected, since threats to ecological systems are not necessarily related to size. The South Pacific Applied Geoscience Commission (SOPAC) has also completed preliminary work on developing an environmental/ecological index. This index has more comprehensive coverage through its 47 component indicators. While it may be inappropriate to use it to rank countries because of wide differences in ecosystems, it could be useful in the development of vulnerability profiles for individual countries.

**Table 6. Country groups according to the Commonwealth vulnerability index**

<i>High Vulnerability</i>	<i>Higher Medium Vulnerability</i>	<i>Lower Medium Vulnerability</i>	<i>Low Vulnerability</i>
Antigua & Barbuda	Angola	Bolivia	Algeria
Bahamas	Bahrain	Cameroon	Argentina
Belize	Barbados	Congo, Dem. Rep.	Bangladesh
Bhutan	Benin	Costa Rica	Brazil
Cape Verde	Botswana	Côte d'Ivoire	Chile
Comoros	Burkina Faso	Cyprus	China
Djibouti	Burundi	Dominican Rep.	Colombia
Dominica	Central Afr. Rep.	Ecuador	Egypt
Equatorial Guinea	Chad	El Salvador	Guatemala
Fiji	Congo	Ethiopia	India
The Gambia	Gabon	Ghana	Indonesia
Grenada	Haiti	Guinea	Iran
Guyana	Honduras	Jordan	Libya
Kiribati	Jamaica	Kenya	Malaysia
Lesotho	Malawi	Madagascar	Mexico
Maldives	Mali	Nepal	Morocco
Mauritania	Malta	Oman	Myanmar
Samoa	Mauritius	Panama	Nigeria
São Tomé & Princ.	Mozambique	Paraguay	Pakistan
Seychelles	Namibia	Senegal	Peru
Solomon Islands	Nicaragua	Sri Lanka	Philippines
St. Kitts & Nevis	Niger	Sudan	Singapore
St. Lucia	Papua New Guinea	Trinidad & Tobago	South Africa
St. Vincent & the Gren.	Rwanda	Tunisia	Syria
Suriname	Sierra Leone	Uganda	Thailand
Swaziland	Tanzania	Yemen	Turkey
Tonga	Togo	Zimbabwe	Uruguay
Vanuatu	Zambia		Venezuela

*Note:* Small states are shaded. Within groups, countries are listed in alphabetical order, not by their index ranking.

## The Way Ahead: Challenges, Opportunities, Policies and External Assistance

46. The characteristics that make small states different thus give clear indications of the challenges they face in improving their development prospects. Reducing income volatility and mitigating the risks they face are important to increasing the well-being of their populations, especially the poor. Reducing perceived risk to private investors is a further challenge. In some cases poverty is higher than expected given average incomes, and tackling it should be a priority. Equally important will be efforts to strengthen institutions and build capacity in the public and private sectors.
47. At the same time, many of the small states are at a crossroads. The post-colonial model—based on trade preferences, official aid, and relationships with former powers—is fading, and a new model is being born. Terms of trade of some countries may suffer as export prices decline when preferred access is eroded while aid flows may continue to decline. To adjust to these changes, resources will have to move away from protected activities to other sectors of the economy—some of which do not even yet exist—and conditions will need to be created to attract private foreign savings. Beyond that, small states, like other countries, have to face all the other opportunities and challenges that come from economic globalization.
48. As they face these challenges, good domestic policies will be more than ever essential—essential but of course not in themselves sufficient—to successful development. As with all other countries, policies that bring macroeconomic stability need to be supplemented by good and appropriate structural and social policies, that provide the basis for growth, successful transformation of their economies, and reducing poverty. Arguably such policies are even more important in small states than in larger ones, first because in countries that are vulnerable to external shocks it is even more important to avoid internally generated instability; and second because in small states policy mistakes, for example in using non-renewable resources, or in environmental protection, can have longer lasting and more pervasive effects than they would in larger states. In effect, one aspect of vulnerability is susceptibility to domestic policy mistakes.
49. The remainder of this part of our report shows how in four crucial policy areas small states can tackle the challenges they face with a combination of appropriate policies and external support and assistance. We also highlight challenges to the international community in securing improvements, where achievable, in the external environment. The final section draws together some conclusions about the role of external assistance. And in each section we identify, on the basis of further work carried out since preparation of the Interim Report, further consultations, and discussion at the London conference in February 2000, a more specific list of action points for the future. Taken together, these constitute an ongoing work program of actions, analysis, and proposed new initiatives for small states themselves and for the international community.

## **Tackling volatility, vulnerability and natural disasters**

50. In the absence of access to borrowing or insurance to smooth the effects of income volatility on consumption and investment, the people of small states have been forced to increase their reliance on alternative mechanisms. These alternative 'insurance technologies' have ranged from: using high tariffs and other incentives, intended to encourage greater diversity in the production structure; to the cultivation of crops that are more resistant to natural disasters, such as drought, or recover relatively quicker from hurricane and cyclone damage; to the migration of some household members, so as to diversify income risk by adding remittances to locally originated incomes.
51. While these arrangements may have helped reduce income volatility, they can also have a high efficiency cost. For instance, smoothing consumption and investment by way of smoothing income (through diversification in production) is costly and often not feasible. Diversification in production occurs as a consequence of development. It follows the accumulation of capital, and the improvement in knowledge of technologies and markets. When diversification of production is forced through economic planning, and occurs as a result of the use of tariffs, or other mechanisms that create a wedge between international and domestic relative prices, it implies an efficiency loss, which is likely to be higher the smaller the size of the economy. Moreover, if the main source of income fluctuations is supply shocks, such as those caused by natural disasters, then diversification of agriculture and industry may not result in smoothing income fluctuations.
52. In finalizing its report, the Task Force has focused its attention on three of the mechanisms that can serve to reduce vulnerability or lessen its impact on the quality of life of residents of small states. They included forms of risk management, involving disaster mitigation, disaster insurance and commodity risk management.

### *Disaster mitigation*

53. Disaster mitigation measures, such as appropriate zoning and hazard mapping, establishment and enforcement of building codes, and disaster information mechanisms should be promoted. These measures can reduce loss of life, infrastructure damage, and the cost of ex-post insurance. Assisting regional co-operation and co-ordination of disaster mitigation strategies is important. The multilateral development and finance institutions can help in this through: the provision of technical assistance and financial resources; promoting the exchange of information on successful practice; and assisting regional co-operation and coordination of disaster mitigation strategies. Donor finance for mitigation measures, for example in infrastructure, in small states subject to repeated natural disasters can have a very high pay-off.
54. The work by the World Bank on new approaches to disaster mitigation and insurance in the Caribbean represents important progress. The program supports comprehensive disaster management. First, it deals with key policies and will improve the regulatory framework for disaster mitigation, help develop incentives to involve private insurance in sharing disaster risk, and develop and enforce better building codes and land-use planning. Second, the program has a capacity-building component, to strengthen the performance of the national emergency management agencies. Third, there is support for community involvement by organizing, training and equipping community disaster committees in

disaster preparedness and mitigation. Finally, the program includes investments in protection of key infrastructure and facilities. These and other initiatives are being reinforced by the recently-launched ProVention Consortium which will bring together the main agencies active in disaster mitigation and management so as to promote safety by raising the awareness of disaster-related risks among governments and communities so they can devise effective preventive measures; support public policies that reduce the risk of natural and technological disasters in developing countries ; and develop governments' ability to anticipate, and respond effectively, to disasters when they strike through the use of early warning systems and civil defense.<sup>27</sup>

### *Catastrophe insurance*

55. After risks have been reduced to the maximum extent possible through physical mitigation measures, natural disaster insurance can provide some relief in the event of a catastrophe. Since natural disasters are by nature low-probability events, the pricing of insurance for such risks tends to involve 'over-pricing' in order to compensate insurance suppliers for the uncertainty inherent in the occurrence of such events and for the risk of insolvency if the probability is incorrectly estimated. Natural disasters (such as hurricanes) are peculiar in that the probability of a household being affected by a hurricane is not independent of the probability of others in the area being equally affected. As a result, natural disaster insurance for small states, unlike other types of insurance such as life cover, requires finding ways for the more optimal spreading of such risks, including through local/regional market mechanisms and integration into international markets that are better able to absorb the large economic/financial risks.<sup>28</sup> Promotion of development of such insurance necessitates improved financial and insurance sector regulations.
56. In designing insurance schemes, it must be made clear which risks are covered and which are not.<sup>29</sup> Efforts should be made to make insurance accessible to the low-income sector, including crop insurance for small farmers. In addition, insurance should extend to protecting critical public sector assets. In all this, the importance of finding better ways for small states to develop fluid and efficient markets (in both the real and financial sectors) needs to be emphasized. These, and well-implemented policies to gain access to respective international markets, would help reduce the vulnerability of small states.

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<sup>27</sup> The World Bank's partners in the consortium include the Pan-American Health Organization, the UN Development Program (UNDP), the International Federation of the Red Cross and Red Crescent Societies, the Office for the Coordination of Humanitarian Affairs of the UN, the World Meteorological Organization, the UN Environment Program, the World Conservation Union (IUCN), the Inter-American, Asian, and African Development Banks, the US Federal Emergency Management Agency (FEMA), the Organization of American States, the Land Planning Agency and the Ministry of Construction of Japan, the International Institute for Applied Systems Analysis, the governments of Norway, Saint Lucia, Mexico, and Turkey, the Wharton School of the University of Pennsylvania, Virginia Polytechnic Institute and State University (Virginia Tech), the Federal Institute of Technology, and others. For more information on disaster management, see [www.worldbank.org/dmf](http://www.worldbank.org/dmf) and [www.worldbank.org/provention](http://www.worldbank.org/provention).

<sup>28</sup> Philippe Auffret and Jacqueline Mora-Baez, World Bank, *Absence of Optimal Risk Sharing: Large Costs for Developing Economies, Huge Costs for Caribbean Countries and Small State*, Draft, December 1999.

<sup>29</sup> Some small states may be exposed to uninsured risks from shipment of hazardous wastes (such as nuclear wastes) through nearby waters.

57. The World Bank intends to co-operate with states in the Caribbean region to develop and support risk-pooling arrangements, designed to assist in providing better, more reliable, and lower-cost catastrophic risk insurance.<sup>30</sup> It would be useful for the Bank also to build on the same approaches in other regions—particularly those prone to natural disasters, such as the Pacific. In addition, further work is needed to explore the practicability of new instruments and underwriting that would help ensure adequate financing for post-disaster rehabilitation and reconstruction and improve incentives for the private sector to enter the natural disaster insurance market at premiums that would be attractive to small states.

#### *Commodity risk management*

58. Risks to export earnings are important to small states because of their reliance on trade. Some small states remain dependent on commodity production, and using hedging instruments in the international financial markets could help to offset temporary price fluctuations. While these market mechanisms exist, they are often not used because of their high cost, lack of information, and lack of training in their use. Moreover, some government interventions can reduce the incentive of private sector agents to pay for the cost of hedging. The population of small states can benefit from government efforts to spread information about the use of hedging instruments, relevant training in their use, and development of a sound legal and regulatory framework.

59. To explore possibilities for sustainable and effective ways to assist developing countries to better manage their vulnerability to risks associated with commodity price fluctuations is the objective of the International Task Force (ITF) on Commodity Risk Management in Developing Countries.<sup>31</sup> Its work is still at an exploratory stage; pilot testing should begin in 2000 and will include some small states and pay attention to issues and commodities of relevance to these countries. It is important to recognize, however, that many small states are exposed to different risks—for example, fluctuations in volumes and tourism earnings—and that these will need a combination of different approaches in order to reduce income as well as price volatility. One possible approach could be the introduction of relevant crop insurance schemes.

#### *Other causes of vulnerability and action to reduce it*

60. Many small states have vulnerable physical environments as well as vulnerable economies. As development takes place it will be crucial to ensure that it is sustainable, by protecting the environment at the same time. Many mistakes have already been made in this area, for example in insensitive tourism development and over-exploitation of non-renewable resources. International agencies, including the World Bank, are willing to support small states in this regard, both with advice and finance. Work also needs to continue on environmental indices presently being developed. These could be useful in measuring and monitoring resource depletion and environmental degradation, with a view to identifying problems early and introducing preventative measures. Small states can

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<sup>30</sup> John Pollner, World Bank, *The Management of Catastrophic Risks Using Pooled Insurance Structures and Alternative Financing and Risk Transfer Mechanisms*, discussion draft, February 2000.

<sup>31</sup> This Task Force was convened by the World Bank in 1998 and includes participation from all stakeholders in international commodity markets. See <http://www.worldbank.org/commrisk>.

also be affected disproportionately by health catastrophes. Just as in many large states, AIDS is not only a public health problem, but is becoming a major development crisis in small states—in Africa, the Caribbean, and other regions—necessitating urgent efforts to contain the spread of the epidemic.

61. Diversification of activities and assets is another important means of reducing vulnerability to risk. As noted elsewhere in the report, such diversification may be difficult for small states but it should not be ruled out altogether as an option. While the multilateral development, finance and trade organizations offer support and technical assistance for commodity, industry and service sector diversification, it is vital that governments, through policies and programs, create an enabling environment for resource mobilization (in terms of physical and financial assets and human resources) and to attract domestic and foreign investment.
62. As noted, small states have more volatile income growth than other states, yet their size limits their capacity to develop insurance at the national level. Small states should aim to strengthen their integration with the world market by developing domestic regulation to reduce the cost of information gathering by lenders and of performance monitoring by international investors or lenders. In addition, in designing social security systems tailored to their realities, increasing integration among the systems of countries within a region would help protect against fluctuations in current income. Further, asset management considerations suggest that investing part of the backing funds abroad entails lower risks to the funds than investing all of them at home. Practical assistance could facilitate the integration of small states with global capital markets, to reduce the costs of diversifying risk. Effective participation in financial markets abroad, however, requires specialized skills and institutions that may be expensive to develop for some of the poorer small states.
63. Finally, the Task Force notes that the work of the Commonwealth, described above, in analyzing the vulnerability of small states<sup>32</sup> provides a useful basis for some forms of action that can help offset the vulnerability of small states.<sup>33</sup> In demonstrating that many small states are more vulnerable than their larger developing country counterparts, the analysis provides a basis for taking this vulnerability and potential volatility into account in programs of assistance provided by the multilateral development, finance and trade institutions. Similar work being carried elsewhere is also relevant, for example by UN ECOSOC's Committee on Development Policy (CDP)—which, however, aims to identify Least Developed Country status, rather than focusing on the specific problems of small states. Nevertheless, the analyses of small states vulnerability can and should be used by international organizations, including the CDP, to inform decisions, including decisions concerning graduation.

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<sup>32</sup> Commonwealth Advisory Group (1997), *A Future for Small States: Overcoming Vulnerability*, Commonwealth Secretariat, London.

<sup>33</sup> Atkins, *et al* (2000), *op. cit.*

## **Box 2. Key actions to tackle volatility, vulnerability and natural disasters**

- The work carried out by the Commonwealth and other organizations in analyzing the vulnerability of small states and deriving vulnerability indices for developing countries demonstrates that most small states are more vulnerable than larger developing countries. This vulnerability should be taken into account in programs of assistance provided by the multilateral development, finance and trade institutions.
- The vulnerability and special characteristics of small states, and weak capacity in the private sector, contribute to perceived riskiness and difficulty in attracting private investment flows. A relatively high level of continuing official assistance is therefore appropriate for small states, as is the continued application of flexible graduation procedures at the multilateral institutions.
- The strong risks and consequences of natural disasters in many small states require new approaches by the states themselves and the international community. Donor support for disaster mitigation, for example in infrastructure, can have a high pay-off. The work by the World Bank on new approaches to disaster mitigation and insurance in the Caribbean is very relevant, as is the Bank's intention to co-operate with states in the region to develop and support regional risk-pooling arrangements, to complement improved disaster mitigation and prevention measures (for example, in the context of the ProVention Consortium) which can greatly reduce the costs of disasters when they occur. Similar approaches, that build on this experience, may be relevant in other areas.
- Many small states remain dependent on commodity production, and it would therefore be useful if the International Task Force on commodity price risk management could pay attention to issues and commodities of relevance to small states in its future work. Many small states are exposed to different risks, however—for example, fluctuations in volumes and tourism earnings and different land tenure systems—and these will need a combination of different approaches.
- Many small states have vulnerable physical environments as well as vulnerable economies. As development takes place it will be crucial to ensure that it is sustainable, by protecting the environment at the same time. Mistakes have been made in this area, for example in insensitive tourism development and over-exploitation of non-renewable resources. This environmental vulnerability is compounded by the likely impact of climate change for some small states, particularly those in the Pacific. It will be important for donors and international agencies, including the World Bank, to continue to support small states in this regard, both with advice and finance.

## Issues of transition to the changing global trade regime

### *Erosion of trade preferences*

64. Recent years have seen the progressive liberalization of world trade as a consequence of unilateral liberalization by countries; proliferation of regional trade arrangements; and agreements reached under the auspices of the WTO. As a result the trade preferences once afforded to small states have been eroded. Indeed, following the agreement on post-Lomé arrangements recently concluded between the European Union (EU) and the 71 African, Caribbean, and Pacific (ACP) countries, the latter will have to gradually give up the principle of non-reciprocal trade preferences. In addition, small non-LDC states will face increased competition from non-ACP LDCs as these countries will enjoy duty free access to EU markets on “essentially all products” as a result of a unilateral EU commitment to be implemented over the 2000-2005 period.
65. The European Union has entered into many new trade agreements, and the Maastricht Treaty has set the new framework for development cooperation, linking it (if only implicitly) to the EU’s external policy. The Lomé IV Convention, which epitomized a unique relation between the EU and a substantial group of its development partners, lapsed at the end of February this year. While a number of the trade preferences of the Lomé Convention will be rolled over for a limited period (until end of 2007), there is little doubt that this unique EU-ACP relationship will undergo adjustment with the elaboration of alternate trade arrangements (after 2007) that are both compatible with WTO rules and take account of the capacity of small states to adapt their economies in response to liberalization. Similarly, while small states were treated at par with LDCs in many of the Convention provisions, this special treatment of small states has been called into question with the new provisions on access to additional funding in the event of shortfalls in export earnings (see Box 3). Fundamental to this shift in policy has been a change in trade patterns, with an increase in the importance of trade in manufactures and services (mostly with non-ACP countries) and a decrease in the importance of importing raw materials and exporting manufactured products (mostly from and to ACP countries). The development of the single European market with trade policy decisions made at the Union level is a further factor affecting many small states.

### **Box 3. Status of small states in EU-ACP relations**

The provisions of the Lomé IV Convention between the European Union and 71 African, Caribbean, and Pacific (ACP) countries and the post-Lomé ACP-EU Partnership Agreement give special treatment to small states, often equivalent to that offered to LDCs.

First, recognizing the dependency on commodities of many ACP countries, the Lomé Convention provided compensation for shortfalls in commodity export earnings through its Stabex and Sysmin mechanisms, with LDCs, landlocked and island states eligible on conditions that were less restrictive than for other ACP countries. Under Lomé IV, small economies in the Caribbean have been among the substantial beneficiaries of the Stabex facility. These resources have helped countries to diversify and have promoted sectoral competitiveness.

Second, small economies also benefited from the various commodity protocols (banana, sugar, rum, beef, and veal), although many of these have been dismantled as a result of the recent negotiations on post Lomé arrangements.

In addition to these provisions, small vulnerable states receive higher financial aid per capita from the European Development Fund than other developing countries.

#### **Changes to Lomé under the new “Partnership Agreement”**

In addition to the effects of adapting Lomé commodity protocols to WTO rules, small states can be affected by the new framework of additional macroeconomic support established under the Partnership Agreement to replace the Stabex and Sysmin schemes so as to mitigate the adverse effects of instability in export earnings, particularly from the mining and agriculture sectors. In this new setting some small states may, however, find themselves ineligible for these additional resources, because the qualifying threshold has been set high; a lower threshold applies to LDCs. The new arrangements also provide support for market-based insurance schemes to address export earnings fluctuations.

There is a further distinction between LDCs and small states in the proposed new trading arrangements to replace Lomé preferences in line with the WTO rules. By 2005, LDCs will benefit from duty-free access to EU markets for “essentially all goods”—a preference that will not be extended to small states in general.

66. In just one example, the new trading environment has produced changes in the regulation of the market for bananas because the old regulation was considered incompatible with WTO rules. Though changing the regulation of the market for bananas will yield considerable benefits for European consumers, the short-term cost of the loss of banana preferences is high for a number of small states in the Caribbean, some with relatively undiversified economies (Table 7). The dispute over bananas has had wider implications. In its judgement on the EU banana regime, the WTO Dispute Settlement Panel brought into question the coverage of the waiver of the Lomé Convention from international trade rules implemented by the WTO.

**Table 7. Potential costs of the loss of banana preferences in selected small states**

<i>Country</i>	<i>Thousands of 1995 ECU</i>	<i>Thousands of 1995 U.S. dollars</i>	<i>Percentage of merchandise exports</i>	<i>Percentage of GDP</i>
Belize	3,084	4,034	2.45	0.69
Dominica	2,495	3,264	7.08	1.47
Grenada	342	447	1.73	0.16
St. Lucia	7,612	9,957	8.69	1.82
St. Vincent and the Grenadines	3,575	4,676	7.55	1.78
Suriname	2,099	2,746	0.66	0.53

*Source:* Based on Stevens, McQueen, and Kennan 1999, Table 2.

67. The creation of the WTO will also erode Lomé preferences by promoting further trade liberalization of the products of particular interest under the convention—clothing and temperate agricultural output. Although EU trade policy has been eroding preferences for ACP countries for several years, the trend is likely to accelerate markedly over the next 10 years, under the combined effect of the new trading arrangements that will come into effect between the EU and ACP countries and further multilateral liberalization. In particular, the phasing out, by 2004, of the Multifibre Arrangement (MFA) will remove an incentive to invest in ACP clothing exports capacity (as well as a key competitive advantage for such exports). Liberalization of temperate agricultural output risks eroding the advantages enjoyed by some ACP countries in global markets for sugar and beef.
68. Both time and resources will be needed to change the structure of small states economies in response to this new trading environment. And in most cases successful adjustment will require both policy change and external support: many small states are highly dependent on aid inflows which may continue to decline in real terms. Nevertheless, successful adjustment in time will enhance welfare, as measured by attainment of long-term development goals, poverty reduction, and an increase in the standard of living for the majority of their populations.

#### *Domestic policies and economic management*

69. There are a number of issues that small states will need to address in order to adapt, indeed transform, their economies in response to the changed trading environment and thus ensure sustained economic development. In this as in other endeavors sound domestic economic policies—macroeconomic, structural and social policies—will be key. They include not only policy reforms to increase private sector investment and employment but also complementary public policy action and investment. Growth based on attracting private investment, both national and foreign, requires public policies and investment to provide better infrastructure, education, and institutions. A stable macroeconomy, low average tariffs and tariff dispersion, well-established property rights, effective governance and the rule of law, high investment in education and health care, are also essential. It will be also be important to address the structural problems specific to small states, such as income volatility, difficulties in attracting the attention of investors and weak domestic capacity, both in the public sector and in commercial activities. And complementary action will be needed to create safety nets to ease the hardships some will face in the process of adaptation and to avoid an increase in poverty.

70. To facilitate transition and attract private investment, a number of specific domestic policy areas merit attention:

- First, as small states adjust to the changing external environment, they must send clear signals on the direction of their own trade policies and regulation. The costs of transitional changes are closely related to the time needed to adapt to new market conditions (the longer the time, the greater the total cost that needs to be borne by the economy) and to the flexibility that economies have in reallocating resources. Transition takes time; but governments need to give a clear message that changes will occur and will not be postponed indefinitely. When there is uncertainty about whether new market conditions are permanent, investments in an economy are often postponed—and earning and employment opportunities are lost.
- Second, a drop in import tariff revenues, which may result from tariff reduction as part of import liberalization, can pose a problem for small states where prudent fiscal policies are more than ever essential to ensure the macroeconomic stability that is needed for investment and growth: tax reform and its implementation will require time and resources, especially in those small states where capacity is weak. A range of options are available to raise tax revenue through other means than import tariffs.<sup>34</sup> Some small states (including Barbados, Estonia, Fiji, Gabon, Malta, Mauritius, and Samoa) have successfully implemented a value added tax (VAT), for example. The VAT has many advantages for economies undergoing structural transformation, especially a shift toward greater reliance on services, but it does require good administrative capacity. Other ways to proceed in the smallest economies could be to implement a retail sales tax or a low flat-rate tax on imports, the latter supplemented by taxes (such as excises) targeted at domestically produced goods and services such as tourism.
- Third, flexibility in domestic factor markets should be encouraged to facilitate transformation of the productive structure of small economies. Distorted factor markets can impede long-term, growth-seeking investment; for instance where land markets are locked in a social-legal regime that favors subsistence rather than transfer, security, collateral, investment, and growth. Labor markets can be distorted by the wages and performance expectations prevalent in a dominant public sector. Labor market flexibility can be enhanced by re-training programs and by reducing obstacles to dismissal of workers by firms so as to increase labor demand in the medium and long-term and foster faster employment growth. Similarly, small states stand to gain from putting in place regulatory environments—including a transparent and predictable tax regime, effective financial sector regulation and supervision—that invite new investment as well as inflows of foreign capital in general.
- Fourth, in some states the unfinished structural reform agenda is still large and should be tackled as a priority. Small states—like many large states—have a mixed policy record.<sup>35</sup> After independence some small states nationalized banks, public utilities, and vast parts of agriculture and manufacturing. Governments often interfered in the allocation of economic resources, imposed ineffective and counterproductive price regulations, and severely restricted foreign investment. Such policies discouraged investment in physical

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<sup>34</sup> Liam Ebrill, Janet Stotsky, and Reint Gropp, *Revenue Implications of Trade Liberalization*, Occasional Paper 190, IMF, 1990.

<sup>35</sup> Indeed, during the 1990s, there was no statistically significant difference in the quality of macroeconomic and structural policies in small states and other developing countries (Collier and Dollar, February 1999).

capital, encouraged the emigration of skilled workers, and ultimately caused economic stagnation or contraction. By contrast, small states that avoided or moved away from nationalization and heavy state intervention fared far better (Box 4).

71. Part of the problem in designing transition policies is that it is unknown which activities will succeed—for example, when adjusting the central role of agriculture in countries where agricultural export preferences have been eroded. Here, two lessons of experience are relevant. First, the costs of mistakes—poor governance and inappropriate policies—in a small state are disproportionate, given the difficulty in recovering from the consequences of inappropriate policies and practices sustained over a long period. Second, governments in many small states realize that despite genuine efforts towards diversification, they have a poor track record in “picking winners”—what to produce, how to organize production, how to market, how to diversify.
72. Rather than trying to predict winners, small states should therefore focus on improving infrastructure and public services, on cutting red tape and bureaucracy affecting enterprises, on improving the information available to investors and entrepreneurs, on facilitating business linkages on a regional basis, and on lowering the costs of reallocating resources—especially labor—across activities. This process involves new investments in human resource development, in physical capital, and in retraining workers with the necessary skills. Many types of training and public infrastructure are relevant across a range of manufacturing and service sectors. For instance, a strong information and communications capability at reasonable cost to businesses will help improve the competitiveness of perishable produce as well as of financial services. More efficient, information-technology based, port operations will help exporters in all sectors—as well as domestic consumers of imported goods. Such capability is required for a resilient, export-oriented economy. Information and communications capabilities are expensive both in terms of money and people, but costs are going down in areas such as software and more simplified hardware. Small states have a strong interest in ensuring that their institutions are abreast of these developments and acquire as soon as possible the capability to take advantage of them. These issues are discussed further below in sections dealing with private sector capacity building and positioning small states better to benefit from the opportunities of globalization.

#### **Box 4. Small island states adjusting to changing external conditions: Cyprus and Mauritius**

Cyprus (in the eastern Mediterranean) and Mauritius (in the Indian Ocean) have small territories and populations. Cyprus has a surface of 9,300 square kilometers and is home to 753,000 people while Mauritius has 2,000 square kilometers and 1.2 million people. Despite their small sizes and limited natural resources, Cyprus and Mauritius have achieved remarkable economic growth and excellent social indicators. These outcomes were achieved by ensuring macroeconomic stability, being oriented to exports and open to foreign investment, exploiting international market niches, and providing social services to the entire population—especially the poor.

##### ***The success stories***

The numbers tell the story. Over the past 25 years real annual GDP growth in both countries has averaged 6 percent, resulting in a 1999 per capita income of \$13,000 in Cyprus and \$3,800 in Mauritius. Social indicators have also improved remarkably. Unemployment is about 4 percent in Cyprus and 6 percent in Mauritius. Absolute poverty is almost nonexistent in Cyprus and has fallen to less than 5 percent in Mauritius. And life expectancy has increased to 78 years in Cyprus and 71 years in Mauritius.

In addition, both economies have increased the share of non-primary exports in total exports. The share of non-primary exports—primarily financial services, transportation, and tourism—from Cyprus skyrocketed from 13 percent in 1965 to 96 percent in 1996. In Mauritius non-primary exports—primarily textiles—jumped from 14 percent in 1975 to 76 percent in 1997. Another indicator of the transition to service-based economies is both islands' development of tourism, with 1997 tourist arrivals for Cyprus exceeding 2 million and for Mauritius reaching 500,000.

##### ***How did they do it?***

Both countries lack natural resources, cannot exploit economies of scale, face high transportation costs for imports and exports (especially Mauritius), experience natural disasters (earthquakes in Cyprus and cyclones in Mauritius), and depend on international trade. So how did they manage to do so well? By adopting prudent fiscal and monetary policies and flexible exchange rate policies, aggressively pursuing foreign direct investment (Mauritius), participating in the EU Sugar Protocol (Mauritius), exploiting textile preferences for EU and U.S. markets, emphasizing education (Cyprus), building physical infrastructure, promoting the rule of law and inspiring confidence in the judiciary, fostering democratic institutions, promoting public-private partnerships, and encouraging entrepreneurship.

##### ***The new challenges***

Both countries now face difficult challenges: Cyprus is preparing for future membership in the EU while Mauritius' international competitiveness is at risk (reflecting its success and the resulting higher wages and the emergence of new, cheaper competitors). In Mauritius these challenges are complicated by the possible erosion of certain trade preferences, saturation in tourism areas and ecological constraints to tourism expansion, and costly welfare systems.

But these challenges can be overcome. Education reform—with a stronger emphasis on science and technology—can raise skills. Policies can be further reformed to reduce distortions. Welfare programs can be adjusted. And efforts to attract the next generation of foreign direct investment can increase technological sophistication.

*Source:* Matsis 1999; Treebhoohun 1999.

### *External support and global economic environment*

73. While domestic policy choices in these areas by the affected countries will be critical to the success of transition, international development, trade and finance institutions must recognize also that external financial and policy support is needed if small states are to succeed in bringing about transition without excessive social costs that would set back their development. There are five types of external support that would be particularly helpful. First, agreement on transition periods of sufficient length; second, the provision of financial assistance in the process; third, action wherever possible to reduce or remove barriers to small states' exports, including agricultural exports<sup>36</sup>; fourth, recognition of the difficulties small states face because of their vulnerability and limited public and private sector capacity; and fifth, active support for their participation in the WTO and international trade discussions.
74. Where will external financial support be most effective? Changes in global trade have made unprofitable some sectors that once accounted for a large portion of some small states' economies; reallocating resources to new sectors will take both time and new investments in physical and human capital. Improving small states' human capital is the most important vehicle for a rapid transition and more equal income distribution. A better-educated, healthier workforce is likely to be more entrepreneurial in raising its incomes and welfare, efficiently using the resources at its disposal. This should be complemented by efforts to build a knowledge base for productive activity and economic development. So support for human capital development is certainly one way to assist. Another will be support to mitigate the adverse social impact of transition. There will be others, linked to specific country circumstances—support must be sensitive to country needs and constraints. But in general, for aid to be effective during the transition, it must be channeled to modernizing the economy rather than to delaying adjustment. This would send signals to the private sector as to the direction of economic policy and accelerate economic restructuring, rather than hold it back.
75. Turning to participation in the WTO, the experience of Vanuatu illustrates well the case for lowering the small states' cost of accession to and use of international trade conventions (Box 5). It is hard to believe that the process and costs of accession to the WTO for small states could not be streamlined and accelerated. Small states would find it easier to become WTO members if they were given financial and technical assistance in the process of accession, and if membership costs were lower. In the Interim Report of the Task Force, it was proposed that the costs of WTO membership—the lower end of which was based on a threshold of 0.03 percent of world trade of the membership—could be reduced for small states given that these states account for just 0.25 percent of world trade and that the per capita contribution required of them far exceeded that of some larger members. Efforts in the WTO on this have already borne success; for the budget year 2000, that threshold has been reduced to 0.015 per cent. Nevertheless, small states need additional support in participating in trade negotiations, and accessing the WTO Dispute Settlement Mechanism, where the recent creation of an Advisory Center on WTO law is welcome. It would also help small states use their limited capacity better if they were

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<sup>36</sup> The critical importance of access to markets is highlighted in World Bank (SecM2000-97), *Trade Policy for Development and Poverty Reduction*, Draft, March 2000.

permitted to be represented collectively—for example by regional grouping—where they wish to be so.

#### **Box 5. Costs of accession to the WTO—the experience of Vanuatu**

Vanuatu has been trying to accede to the WTO for five years. So far, it has spent nearly \$400,000—about \$2 per capita—on its effort. It has reached the point where it has completed almost all protocol negotiations as well as negotiations with all its major trading partners (the European Union, Australia, Canada, and New Zealand). The only outstanding problems are in the bilateral negotiations with the US, a country with which Vanuatu has very limited trade.

Vanuatu (population of 182,000 and GNP per capita of \$1,270) has no income tax, so the government relies on import duties for revenue; a VAT has recently been introduced. Vanuatu has agreed to limit its tariff to an average of 45% and has also agreed to liberalize imports of services and information technology. But this has not been sufficient to conclude negotiations with the US. The main outstanding issues are a further reduction of tariffs as well as opening of the telecommunications sector where France Telecom has a monopoly till 2012. Vanuatu believes, however, that agreement to open up its telecommunications sector would lower the incentives for France Telecom to invest in necessary service improvements. Telecommunications infrastructure is vital for this remote country that is highly dependent on services and tourism.

Based on Dr. Roman Grynberg, *The Pacific Island States and the WTO: Towards a Post-Seattle Agenda for the Small Vulnerable States*, February 2000.

76. Finally, there is the question of special treatment in the WTO. At the February conference in London it was recognized that a blanket approach, as given to LDCs in Special and Differential Treatment, would not be suitable for small states given their varying stages of development. Nevertheless, the special characteristics and vulnerability of many small states should be recognized as justifying special consideration by the international system to deal with those issues that are crucial to the transformation of their economies, such as length of transition periods.<sup>37</sup> In particular, it would seem practical that specific characteristics of certain small states—such as low institutional capacity and vulnerability—should be among the criteria used to determine any specific treatment. It is clear that many small states will need help to ensure that emerging global trade rules and procedures fully reflect their special circumstances and advance, rather than hinder, their development prospects. For example, monitoring of compliance with the new rules applicable to small states should not disproportionately burden their limited capacity and resources. It is also clear that without help, the small states cannot begin to match the negotiating power of larger WTO members.

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<sup>37</sup>This argument was included in the WTO Ministerial declaration of 1998 – WT/MIN(98)/DEC/1 –which noted that ministers were “deeply concerned over the marginalization of LDCs and certain small economies and recognised the urgent need to address this issue”.

### **Box 6. Key actions to facilitate transition**

- Small states must adapt, indeed transform, their economies to secure the benefits of globalization and the increasingly open global trading environment—trade policy for small states, as for other developing countries, needs to be seen as part of sound overall economic development strategy. Clear signals about the direction of trade and regulatory policies and the length of transition periods will be needed to guide the process and to attract new investment.
- The work of the task force has shown that many small states will face special difficulties in making this transition and will need time to adjust to changes in the external trade regime, and sequence changes in their economies. The particular vulnerabilities of those small states that are not LDCs should be recognized as justifying special consideration to deal with the issues that are crucial to transformation of their economies, including length of transition periods, as the global process of trade liberalization, and removal of special protective regimes, continues. It would be useful to review the current process of WTO accession as it affects small states to see if the problems and costs these countries face in the process can be reduced.
- Another issue related to WTO participation is the lack of adequate resources to participate fully in international trade negotiations. The Commonwealth, through its permanent trade advisers in Geneva and Fiji, already provides assistance of this type to its member countries. It will continue to do so and has expressed a willingness to take a lead in expanding such facilities. The EU is financing an ACP countries' bureau in Geneva to facilitate relations and negotiations with WTO and UNCTAD. Additional support from the World Bank and others would be welcome, as is the recent creation of an "Advisory Centre on WTO Law". The WTO should examine other ways to help, for example by allowing groups of small states to be represented collectively at discussions where they wish to do so.
- Trade liberalization can have major fiscal consequences for small states. The IMF should continue to take a pragmatic approach to the advice it gives to small states that risk losing a major source of fiscal revenue as tariffs fall, recognizing that for some open, small economies low, flat-rate tariffs may be a component of an efficient tax system. However, as small states move to more service based economies, they will need to adopt broader-based consumption taxes. They will also need technical assistance from the IMF and others in tax administration.

## Strengthening capacity

77. Paragraphs 31 to 39 above describe the main features and causes of limited institutional capacity in small states, both in the public and private sectors. Many of the weaknesses are an almost inevitable consequence of the very small absolute sizes of government or domestic markets. A further factor that representatives from small states see both as a weakness and potential strength is, in many cases, the existence abroad of a substantial expatriate community—often individuals with high levels of skills, which could be utilized were they to return home, but who, while abroad, provide valuable links with the global economy. All these weaknesses are particularly critical at a time when small states face new challenges in transforming their economies to benefit from globalization. Analysis and discussions held by the Task Force, and experiences of small states themselves, suggest a number of ways to strengthen capacity. They are likely to require a combination of domestic policy action and outside support. The following paragraphs identify approaches that can work, and some key policy issues that need further attention.
78. One general point emphasized by small states themselves is that building capacity and stronger institutions will require sustained political commitment. This is most obviously the case in building regional institutions, as discussed below, which almost inevitably involves some loss of national sovereignty. But it is also true in other areas. In addition small states rightly emphasize the importance of a background of good and transparent governance to sustained capacity building.
79. As to external support, in addition to the various specific actions discussed below—not least in improved donor co-ordination—there are two further forms of help that outside agencies are well placed to provide. The first is by maintaining links with and pools of outside expertise, both from advanced and other developing countries, to help with specific issues as they come up. The second is by helping maintain and disseminate a pool of knowledge about approaches that work and those that do not, so that small states can learn from each other's experience. Relevant and welcome here is the proposal by the World Bank to develop such a pool of knowledge on a website and to arrange regular meetings where representatives from small states across regions can meet, discuss issues, and compare experiences. The Commonwealth Secretariat has also recently finalized the development of a dedicated small states website. Its purpose is as a medium for outreach, information exchange, advocacy on issues of concern to small states, and delivery of Secretariat programs.
80. While there are capacity weaknesses in both the private and public sectors, the Task Force has focussed mainly on action that the public sector can take, both to improve efficiency and effectiveness in providing public services, and to provide an environment that encourages stronger private sector development. There are clearly ways that national financial institutions, donors and international institutions such as the IFC can come together to provide direct support for private investments, particularly where high perceived risks are discouraging external private investors, and where involvement by such agencies is catalytic, giving external private investors the confidence to invest also. In the public sector, many small states already receive a high level of assistance—both financial and advisory—to strengthen capacity. This is clearly appropriate and should

continue, with emphasis on infrastructure, improved efficiency, and development of human capital. Much can be done in many small states to improve the quality of governance at the national and local levels (Box 7). High priority should be accorded to education and training. Distance education is especially promising in bringing complex services to remote small states and to isolated regions.

### **Box 7. Good governance requirements in small states**

The domestic institutional environment in many small states can benefit from effective and supportive working relationships between the development partners (public and private sectors, domestic and foreign producers, civil society). Good governance requires a large number of functioning institutions. Some requirements are basic, such as security of property rights, rule of law, a reliable, functioning and accessible justice system, a relative freedom from crime and high levels of personal security, a non-corrupt and professional bureaucracy operating strictly on a rules basis, and smooth, non-disruptive changes in administrations. Equally key fundamental are sound management of public resources and the development and maintenance of a good economic and regulatory environment conducive to efficient private sector activities.

Others are not so basic, but are nevertheless of significant importance. They include: a solicitous bureaucracy, strong civil society participation in public affairs, willingness of the population to engage in community development activities, and functioning local government systems with strong community participation. These good governance requirements need to be emphasized for three reasons. First, given the higher levels of personal relationships (and hence the likelihood of less formality) which tend to obtain in small states, civil rights may be more fragile, particularly where the country has experienced significant levels of outward migration over time, especially of professional and skilled people. Second, there may not be very strong traditions of openness, participation and accountability in some small, post-colonial societies but there may be quite strong pressures on the political leadership to behave in ways which contribute to uncertainty and thus reduce confidence (and with it, investment). Third, taking stock of the institution-building and institution-maintenance tasks is a necessary first step in taking actions to improve governance.

The costs of poor governance in a small society is very large, given the extreme difficulty in recovering from the consequences of inappropriate policies and practices sustained over a long period. A national consensus on the importance of governance is needed in many small states, as is an appreciation for the ease with which the system can go off-track as a result of both domestic and external shocks.

Source: *Caribbean Community's Comments on Selected Issues*, February 2000.

81. Other public actions that help develop the private sector include:

- broadening the tax base, eliminating customs surcharges that have an anti-export bias, and simplifying the tax structure and strengthening its administration;
- providing a clear transparent and effective regulatory framework for business, particularly – given the prevalence of monopoly and oligopoly situations in small states – in the area of competition policy;
- providing, either directly or through appropriate policies of privatization and regulation, the high quality low cost infrastructure that business needs. Given the potential future role

of information based business, this will be particularly important in the area of telecommunications;

- simplifying all government regulations so as not to tax private sector capacity by red tape and unnecessary regulations;
- providing information to facilitate business decision making; and developing the human resource base to underpin employment growth in the private sector; and
- encouraging formation of networks and associations of entrepreneurs within countries and regions—such as business councils, and use of relevant international resources (for example, the Commonwealth Business Council), strengthening of regional chambers of commerce, product standardization and the sponsorship of missions for trade and investment promotion are also likely to strengthen the private sector.

82. An important approach that can help in building capacity in all these areas is co-operation between states on a regional or sub-regional basis. This involves some pooling of sovereignty. But regional or other international agreements can lower the costs of providing public goods and services. Such agreements are already widely used in the areas of security (defense treaties), education (University of the South Pacific, University of the West Indies), and central banking (Eastern Caribbean Central Bank). The Task Force has devoted some effort to exploring the potential for intensifying such co-operation, and discussing the issue with representatives of small states, and regional institutions. There is strong support for developing regional approaches further, not only in the Caribbean, where distances are relatively small, but also in the Pacific Region, where many believe that modern communications can be used to facilitate further co-operation. Areas where there appears to be potential for stronger co-operation include: regulatory regimes, for example for telecommunications (see Box 8), but also for the financial sector; legal and judicial systems; education and health facilities; sharing of investment codes; environmental regulations; and social security, tax and customs rules. Creation of regional single markets is one of the ways small states can encourage the formation of stronger local businesses. Joint representation in international bodies is another area where co-operation could provide stronger capacity at lower cost.

83. As noted above, such co-operation will take sustained political commitment. It also implies strengthening further existing regional and sub regional bodies such as CARICOM and the Pacific Forum. Multilateral institutions, including the World Bank, and other donors should intensify their efforts to encourage and support regional approaches of this kind between small states and the regional organizations that underpin them, with financial and technical support.

### **Box 8. The OECS and regional telecommunications reform**

Five member countries of the Organization of East Caribbean States (St Lucia, Dominica, Grenada, St Vincent and the Grenadines, and St. Kitts and Nevis) have embarked upon a unique experiment in telecommunications liberalization. The reform, away from private monopoly provision and vital to the economic future of the islands, received financing from IBRD (\$3.6 million) and IDA (\$2.4 million). It has two interesting features. First, the islands hope that a large part of the functions of a telecommunications regulator will be carried out at the regional rather than the national level. Second, the reform effort has recently been dramatically enhanced by a legal ruling that monopoly telecommunications provision is unconstitutional.

#### **The need for telecommunications reform in the OECS**

The OECS countries have been undergoing significant economic change. Declining European markets due to the renegotiation of the Lomé agreements and weak local markets are hurting traditional agricultural production. Bananas, which account for a large part of OECS countries' exports—over 50 percent of St Lucia's visible exports in 1997—face the most serious threat. At the same time, and in response, the region is keen to diversify away from a heavy reliance on farming and tourism. One important element of this diversification will exploit growing opportunities in traded information services industries; this is expected to create 1,500 new jobs in the OECS by 2002.

For information services to flourish, however, an efficient telecommunications sector is vital. The monopoly service provider common to all of the OECS countries has failed to provide this—for example a 10-minute call between St. Lucia and St. Vincent cost as much as \$40 two years ago. Not only is service expensive and costs are unbalanced, but there is also limited availability of new and value added services (for example, there is no packet switched service for business).

Since the project was approved two years ago, the reforms are already showing results, as the current monopoly service provider started to rapidly reduce prices of international calls.

#### **The regional telecommunications authority**

The OECS countries have embarked upon a radical program of liberalization in the sector, to be backed by new regulations and a regional regulatory body, the Eastern Caribbean Telecommunications Authority (ECTA). Although sovereign power over licensing and regulation will be retained by the member countries, ECTA will provide technical expertise, advice and support for the creation of coordination national regulations at the country level. It will promote harmonized, transparent and objective regulation of telecommunications in the region, hand-in-hand with new telecommunications bills in each country that will establish a National Telecommunications Commission as the regulatory mechanism for that country. ECTA's primary role will be to ensure that the telecommunications sectors of the contracting states have fair competition, consumer protection and investor confidence. In addition, ECTA will manage the 'radio frequency real estate' of the member states.

84. There is one further area where those providing support for small states can assist greatly in strengthening their capacity. As was well illustrated by the recent report of the World Bank's Operations Evaluation Department,<sup>38</sup> the activities and requirements of multiple donors place a disproportionate burden on already hard pressed administrative capacity in small developing states, with donors seeking to impose their own, often overlapping, priorities and administrative requirements. This is an issue that can and must be tackled. The conclusion of the Task Force is that it needs to be addressed country by country, and using the principles of partnership and country leadership that underlie the Comprehensive Development Framework approach. Countries themselves will need to lead the effort—but it will also require donors to join together, align their objectives with each other and those of the country, rationalize their interventions so all important areas are supported, and simplify and align their procedures to reduce the administrative burden on the recipients. To help the process countries may need extra support in developing their capacity to manage these donor relationships—but this should provide a good pay-off in reduced donor demands. Regional organizations also have a useful role to play in this regard.

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<sup>38</sup> World Bank, Operations Evaluation Department, *The Drive to Partnership: Aid Coordination and the World Bank*, November 1999.

### **Box 9. Key actions for building capacity**

Small states and those providing support for them need to continue to address their problems of limited capacity, both in the private and public sectors. Specific issues to pursue in this context include the following:

- There is a continuing task of accumulation of knowledge about policies and approaches that work and do not work for small states, and sharing this knowledge and experience among states both within and across regions. Relevant actions to help in this respect include the establishment by the Commonwealth Secretariat of a dedicated small states web site; and the proposal that the World Bank help accumulate and share such knowledge, generated within the Bank and outside—using mechanisms such as the creation of a Bank-wide small states thematic group, developing a World Bank small states web site, and arranging regular meetings where representatives of small states can share experiences and discuss new developments. These actions should be coordinated with existing capacities, such as SIDS/Net, a UNDP-based network, dedicated to small island developing states.
- An important approach in tackling limited capacity in small states is to develop regional approaches wherever feasible. The multilateral institutions and other donors should reinforce existing programs by enhancing their lending and non-lending services to encourage and support such co-operation, particularly by assisting regional organizations dealing predominantly with small states.
- To help develop private sector capacity, both regional and country approaches are needed, including providing information to facilitate business decision making, training, and encouraging formation of networks and associations of entrepreneurs. Another aspect of limited capacity where the multilateral institutions can also help is dealing with utilities' regulation and competition policy; issues of considerable importance with the prevalence of monopoly or oligopoly suppliers in small states.
- Activities and requirements of a multiplicity of donors place heavy and unnecessary burdens on limited administrative capacity in many small states. This was well illustrated by a recent study by the World Bank Operations Evaluation Department. This problem needs to be addressed by a new approach building on principles of partnership and country leadership that underlie the Comprehensive Development Framework approach. Donors and international agencies should join together country by country, in country-led partnerships to align their objectives, rationalize their support and simplify and harmonize their procedures to reduce these burdens. Helping build country capacity and forging of closer working relationships with regional organizations would help in this regard.
- Building institutional capacity needs to be undertaken in close consultation with recipient agencies and tailored carefully to their particular needs. Experience in the Pacific suggests the need for a long-term commitment by donors to strengthen generally weak institutional and human resource capacity. Further, the design of capacity building activities needs to be flexible and responsive to a country's needs and political realities.

## **New opportunities and challenges from globalization**

85. Earlier sections of this report have dealt with vulnerability, the transitional needs in moving to a more liberalized trading environment, and capacity building, but small states face more general difficulties and opportunities in adapting to globalization. Globalization is a multi-dimensional process that is transforming in a profound way all aspects of national and global activities and interactions. Inherent in the process is the decline or demise of some industries and products and the simultaneous generation of opportunities for the creation of other goods and services. The process is driven by continuing innovation and technological change and is associated with the elimination or reduction of national barriers to the global movement of goods, services, capital, technology and certain kinds of labor. The emerging global market is characterized by intense competition and the need for flexibility in economies and responsiveness by economic agents within them.
86. Globalization is not a new phenomenon but rather the process has accelerated in recent years, calling for more rapid reaction from small states, many of which have limited resources and capacity to respond. Hence, globalization brings opportunities as well as challenges for small states. The latter, particularly as related to the globalization of trade, pose special difficulties for these countries. However, the prospects for small states to benefit from globalization exist in both trade and other areas of endeavor as information and communications technology shrink distances and help overcome the disadvantages of remoteness and isolation.
87. In order to take advantage of such opportunities, small states will need to undertake what some have described as a strategic global repositioning of their economies. As in the case of responding to changes in the international trade regime, they need to create enabling environments and provide the right kind of public policy support – for example, in training and education and new or modified regulatory frameworks – to encourage new activities, many of which will be in the service sectors. Some small states will need external support and advice as they seek to achieve this repositioning. Of course, globalization affects different countries in different ways and a mix of unique responses will be needed to meet the individual circumstances of countries and regions.
88. In its further work since the Interim Report, the Task Force has focused in particular on emerging issues that bear on the provision of international financial services, and on the new opportunities provided by information technology and electronic commerce. Both areas were the subject of extensive discussion at the London conference in February 2000.

### *International financial services*

89. A number of small developing countries have already become successful in the provision of both onshore and offshore financial services. For a variety of reasons the provision of offshore financial services is also a matter of concern to the international community. One is the need to combat money laundering, an areas where the small states concerned have been cooperating in global efforts. Recently international concerns have turned to the subjects of harmful forms of tax competition, and possible implications of offshore centers for global financial stability. These two topics are currently the subject of scrutiny, respectively, by the OECD's Forum on Harmful Tax Competition and the Financial Stability Forum.
90. This is causing concern for a number of small states because of a lack of adequate consultation on the matters being addressed. At the London conference in February 2000, the OECD indicated its willingness to engage constructively with small states on tax competition issues and to respond to their call for a multilateral discussion. This represents a positive development on both sides. Financial services are of substantial importance to the economies of small states, and small states therefore have a strong interest in fostering the predictability and stability of the operations of financial institutions based in their territory. At the same time, these countries need to improve financial operating practices and regulatory standards in order to safeguard the international banking and financial system. There is also a global interest in action to combat financial and tax crime, and to address harmful forms of tax competition. It is important for all these issues to be considered in international fora where small states themselves have a voice, so that their interests can be taken into account. It would therefore be appropriate for multilateral institutions to study these issues and look for solutions that pay proper regard to the interests of small states as well as the need to foster stability in the global financial system and to counter international financial and tax crime.

### *Information technology and electronic commerce*

91. Work on the opportunities that information technology and electronic commerce can bring to small isolated states suggests that these technologies can provide a major impetus to their development, especially for those countries with a well-educated and computer-literate workforce. Using the technology of efficiency—information technology and e-commerce—in a globalized, technology-based trading system means that competitors can now become collaborators, suppliers and customers, irrespective of size.<sup>39</sup>
92. These technologies also offer unprecedented opportunities for small states to reform and re-engineer government services, become part of global supply and demand chains, create new businesses and generally increase welfare. Success will depend upon planning and generating the preparedness to adapt and become responsive to change.

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<sup>39</sup> Schware, R & Kimberley, P, *Exploiting Information Technologies for Electronic Commerce and Better Public Sector Management*, paper presented at the Global Conference on the Development Agenda for Small States, London, 17-18 February 2000.

93. Success also requires the correct public sector infrastructure, crucially a regulatory framework that will deliver high-quality/low-cost telecommunications services. The level of investment for telecommunications can remain disproportionately high for small states as compared with larger countries, although in this area too technology and global competition are dramatically reducing costs. This is especially relevant in some areas—for example, the Caribbean and Pacific—where some existing, long-term monopoly supply agreements militate against the attainment of potential international competitiveness by small states seeking to diversify into new, high-technology- and communication-dependent service industries. It is important to note that, in facing this challenge, many small states will require external support from the multilateral development banks and others. Box 8 illustrates the kind of regional approach, with support from international institutions, that can work in this area.
94. Small states will also need support from international organizations on the issues of appropriate regulation on the taxation of e-commerce and control of criminal use of the technology.

*Public and private sector policies for exploiting new opportunities*

95. These two areas—financial services and use of information technology and e-commerce—represent two examples of the kind of new opportunities open to small states in the new global economy. There will be others. Earlier sections of this report, on the transition to a new global trading environment and building capacity, set out the kind of domestic policies and external support that will best position small states to take advantage of these opportunities. Sound economic policies will be key, as will regional co-operation—including not only improved economic management and reform but also complementary public policies and investments to provide infrastructure, education, appropriate regulation, and all the other underpinning of a successful market economy.
96. Actions on the above policy fronts and the ability to discern changes, to adopt and adapt to new technology, and to reorganize rapidly will determine the capacity of the productive sector in small states to respond to the new opportunities. Firms, governments, and individuals must get accustomed to a lack of permanence.
97. The fortunes of production of goods and services in small states may increasingly depend on their firms' ability to seek out and form strategic corporate alliances. Companies have to be flexible, responsive, competitive, innovative, efficient, and customer-focused. The fragmentation of transnational production processes into separate stages being undertaken in different countries and strategic corporate alliances has made it possible for networks of small firms to overcome the limitations of size and compete effectively against large corporations. In this context, and provided that the right kind of enabling policies and supporting infrastructures are in place, strategies for small firms to ensure their survival and profitability in the global economy include:
- specializing in a single aspect of production or distribution;
  - capitalizing on specific market niches where economies of scale are not a determinant of competitiveness;
  - flexible service industry specialization;

- concentrating on the economies of speed, which are now more important than the economies of scale—and which can be exploited thanks to new low-costs communications technologies; and
  - strategic corporate alliances which have made it possible for networks of small firms to overcome the limitations of size.
98. Increasingly, the world economy will be dominated by knowledge-based industries, especially services, making the quality of human capital a critical factor. The productivity of labor (workers and managers) will have to be upgraded, and this means improvement in the quantity and quality of education. Because of past emigration, a significant part of the human capital of small states resides outside of their borders. Policies to encourage repatriation of skilled nationals can have a high pay-off, as this is the quickest way to improve the quality of the workforce. Making the workforce more knowledgeable and productive involves better education both within the individual enterprise and in the society as a whole. Firms need to put more emphasis on vocational training and on-the-job education. New technologies can help—for example, multimedia training enables workers to learn faster and in more detail, particularly those workers who are functionally illiterate.
99. Firms in small developing countries cannot generally afford the costs of research and development but can realize opportunities in the global marketplace by the transfer and adaptation of knowledge, and by greater use of indigenous research capacities combined with networking with relevant institutions abroad. The capacity for absorption of knowledge and new technology requires the development of an appropriate national educational institutional infrastructure. Education should thus remain a priority of governments in small states. In the more developed small states—such as in the Caribbean, there should be an emphasis on increasing the scientific and technological component of education and the devotion of more resources to secondary and university level training. Much of the university-level education will have to be undertaken overseas—although the substantial cost involved, particularly for study at institutions in developed countries, is an impediment to the efforts of small states to expand institutional capacity and research. On the other hand, many of the small states in the Pacific and Africa still need to first grapple with the challenges of simply delivering effective and universal basic and secondary education. While some needs can be met by overseas training sponsored by donors, for the most part these small states need to embark on a long-term effort to overcome problems of delivering culturally appropriate education in a cost-effective manner in order to build up education standards more generally.
100. As discussed above, a strong information and communications capability will help improve the competitiveness in new areas of business, including financial services. Acquisition of these capabilities has been expensive both in terms of money and people, but costs are going down, and regional approaches can help. It will be important for small states to have institutions that are abreast of these developments and able to take advantage of them quickly. In some small states, the revolution in information technologies and in communications has already encouraged an expansion of tourism and of other service sectors (into areas such as communications, information technology-based activities and financial services). In the medium-term, these are areas of business most likely to offer significant new opportunities for small states.

101. As stressed throughout this report, it will be important also that the international development, finance and trade organizations and donors offer their support when small states implement the public policies and investments needed to facilitate such developments.

### **Box 10. Key actions to respond to globalization opportunities**

Some small states will need external support and advice as they seek to reposition their economies. They need enabling environments and the right kind of public policy support—for example in training and education, and creating regulatory frameworks—to encourage new activities, many of which will be in the service sectors. In this context actions in two specific areas will be important for many small states.

- One new area in the service sector where some small states have been successful is in the provision of onshore and offshore financial services. These activities are, however, currently the subject of scrutiny by the OECD's Forum on Harmful Tax Competition and the Financial Stability Forum (FSF). This is causing concern for a number of small states because of lack of representation in the OECD and FSF and lack of adequate consultation on the matters being addressed. At the London conference in February 2000, the OECD indicated its willingness to engage constructively with small states on tax competition issues and to respond to their call for a multilateral discussion. It is important to recognize the substantial importance of financial services to the economies of many small states. But this must be weighed alongside the clear need for improvements in financial operating practices and regulatory standards, in order to safeguard the international banking and financial system, and the need to take action to prevent financial and tax crime and to address concerns about harmful aspects of tax competition. It is important for all these issues to be considered in international fora where small states themselves have a voice so that their interests can be taken into account. It would therefore be appropriate for multilateral institutions, including the IMF, to study these issues and look for solutions that pay proper regard to the interests of small states.
- Finally, work on the opportunities that information technology and electronic commerce can bring to small isolated states suggests that these technologies can be a major source of help in their development. But success requires the correct public sector infrastructure, crucially a regulatory framework that will deliver high quality/low cost telecommunications services. It is important to note that this provides a challenge in which many small states will need external support from the multilateral development banks and others.

## External assistance

102. As noted above (paragraphs 26 to 29), small states have benefited from relatively high levels of external assistance. Donors can help small states tackle their special vulnerability, offset income volatility and mitigate risks through economic and sector work, effective knowledge management, and—more important—through support to current initiatives addressing these issues such as disaster mitigation and insurance programs. Small states also warrant special consideration in aid allocation decisions because of their relatively high levels of poverty, because they need more help than large states to attract foreign direct investment, and because their institutional capacity is limited in relation to the development challenges they face, in particular, for many, a need to transform their economies to respond to changes in their trading environment. These characteristics peculiar to small states should continue to be reflected in decisions on aid eligibility and graduation of small states. A relatively high level of aid is appropriate and donors and the international financial institutions should continue to allocate larger aid amounts, in per capita terms, to small states than to other developing countries.

103. Earlier sections of this report have dealt with a range of conclusions about how donors and other external agencies can best help small states in their development. This section pulls together a few key messages for donors and international agencies. Because aid flows can be a large part of public sector resources in small states, the economic performance of small states is highly “vulnerable” to poor donor policies. As elsewhere in the world there is no doubt that the effectiveness of aid to small states—on poverty, and on facilitating the economic transformation and lowering its costs—could be improved (see Box 11). In particular:

- Aid should be targeted to modernize the economy; aid allocations should reflect the quality of the recipient country’s overall policies and entire public spending program rather than on flows to individual projects. By taking explicit account of the fungibility of aid, this approach would maximize the effectiveness of aid in small states, as elsewhere.
- Donors should adapt their instruments to suit small states’ institutional capacity and scale. Aid is often fragmented, allocated in the same format, regardless of a country’s institutions. As a result, lending and other development operations and their monitoring by separate donor agencies often place unrealistic demands on the institutional capacity of small states, resulting in delays in program implementation, disbursements and difficulties in ensuring a positive development impact.
- In particular donors should make a major effort to co-ordinate their activities in small states, in a country-led framework. Multiple donors with overlapping or conflicting priorities and administrative requirements place an unnecessary burden on the limited administrative capacity of small states.
- More generally, donors should avoid burdening the implementation capacity in small states. One approach is to support private executing agencies as a means of improving project implementation.<sup>40</sup>

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<sup>40</sup> In recent years this approach has been used successfully by some African states, including small states (The Gambia and Guinea-Bissau), for implementing World Bank projects in infrastructure and the social sectors.

104. A final issue for donors is the high transactions cost associated with external assistance flows to small states. As noted above, the small states account for nearly one-third of the World Bank's (IDA and IBRD) borrowers, but are home to less than 0.4 percent of the total population of developing countries and receive less than 1 percent of the World Bank's financial commitments. Programs supporting objectives that require cross-country support, such as the regional approaches that are so important for small states will also involve high transaction costs and long institution-building periods. To some degree, this is inevitable and reflects also the weak institutional capacity of the recipient countries. But it may be possible to find approaches that reduce donor costs, for example through more effective aid coordination (to avoid duplication of efforts and to limit demands on the recipients' capacity) and through other innovative approaches such as programmatic lending.

### **Box 11. Aid effectiveness**

Aid makes a big difference in developing countries with sound economic management. But where economic management is weaker, the impact of aid is much smaller (World Bank, 1998). In well-managed economies, aid boosts growth, reduces poverty, and improves social indicators. Aid can help countries improve their economic policies, but successful reform requires a strong commitment from recipient countries—a concept referred to as reform ownership. Where such broad political support for reform has been absent, aid has typically been unable to bring about sustained change. Community ownership and involvement is also essential for the success of social and investment projects.

Effective aid could be a particularly important issue for small states. Even with good policies, small countries are perceived as highly risky by private investors—more risky than large developing countries. Here aid can help. The combination of good policies and significant financial aid decreases the perceived riskiness of countries (as measured by private risk ratings) and leads to larger private capital flows. That is, aid “crowds in” private investment in a good policy environment. The crowding-in effect has two aspects. On the one hand, the presence of aid increases investor confidence that good policies will be maintained. On the other hand, aid helps governments finance investments that are complementary to private investment: roads, schools, and the general infrastructure of development.

*Source:* Collier and Dollar, 1999.

## **A continuing work program**

105. The analysis and discussion in this section, and in particular the specific action points set out in Boxes 2, 6, 9, and 10 constitute a continuing work program for small states themselves and for the international community. Further details are spelled out, institution by institution, in Part II of this report, which compiles the action plans (“frameworks”) submitted to the Task Force by the key multilateral institutions. As multilateral institutions and donors co-operate in helping take this work program forward they will need to continue to be guided by the views and experiences of small states themselves, as the Task Force has been in the preparation of its report. The World Bank and the Commonwealth Secretariat intend to monitor progress, working in partnership with each other, with small states, and with other multilateral institutions and donors. The completion of the Task Force’s work should not be seen as the end of a process, but as a stepping stone to a new partnership between small states and the international institutions, and continued attention to small states issues by the international development community.

## **Part II: Responses of International Institutions**

Development, trade, and finance institutions are responding to the challenges faced by small states. They can serve small states by providing financial resources and technical assistance in support of strong domestic policies.

The Commonwealth Secretariat and World Bank frameworks towards small states, described in this section, focus on institutional capacity building, risk diversification, and transition. The development frameworks towards small states from the European Union, the World Trade Organization, the International Monetary Fund, the United Nations, UNDP, UNCTAD, the African Development Bank, the Asian Development Bank, and the Inter-American Development Bank are also appended.

## The World Bank Framework

1. *Poverty reduction is the World Bank's overarching objective.* The Bank helps countries in their efforts to reduce poverty by providing support in addressing developmental constraints and building national capacity. The Bank's strategies are tailored to the conditions of borrowers and emphasize the principles underlying the Comprehensive Development Framework—country ownership, participation by civil society and national and international development partners, and a holistic and long-term approach to both the diagnosis of poverty conditions and the assessment of policy and institutional constraints to improving poverty outcomes. The importance of small-state issues—such as volatile incomes, low capacity to pool risks at the national level, low institutional capacity, and the challenges of transition—is increasingly taken into account in country-specific work programs. Linking lending and non-lending services to encourage policy and institutional reforms is key, as is making use of a wide range of lending instruments, of knowledge available from other development experiences, and careful monitoring of results. Finally, in small states which are both IDA and PRGF-eligible, the Bank is working in partnership with the IMF to help these countries prepare Poverty Reduction Strategy Papers, as the common basis for Bank and Fund programs, including, for those countries which are severely indebted, debt relief under the HIPC initiative.
2. *A partnerships approach to development.* The Bank is working with other development partners to harmonize approaches toward small states and increase impact of interventions. This implies increasingly taking into account comparative advantage to increase selectivity of interventions, to share responsibilities across sectors and agencies within countries, and to coordinate and harmonize operational processes and requirements, so that, for instance, the Bank can:
  - operate within an agreed country assistance strategy, possibly led by another development partner (as has been piloted in the South Asia region in recent years); and
  - present for Board approval loan operations supported by documentation prepared by other development agencies (as in the case of the Panama Roads Rehabilitation Project where the Inter-American Development Bank prepared the appraisal report).

## The World Bank's assistance strategy for the Pacific islands

The Bank's work in the Pacific supports the nine member governments' respective development strategies and is based on a recognition of both the vulnerabilities they share with other small states and the unique set of circumstances that sets the region apart. Some of these unique circumstances include:

- *Size and remoteness.* In terms of land size and population Pacific Island States are among the smallest in the world. Most of the approximately 2,700 islands that make up the region are remote from major economic centers with a total land area of only 88,800 square kilometers.
- *Dispersion and isolation within and between countries.* Significant distances between island states and within states lead to isolation and inadequate service provision in many islands. Travel and communication between countries can be difficult and costs of communication are often high.
- *Strong, vibrant cultural traditions and organizations.* Unlike the Caribbean and Indian ocean countries to which they are sometimes compared, indigenous cultures and traditions have remained strong in the Pacific Islands and continue to play a large role in political, economic and cultural life.

The Bank's draft Pacific Regional Strategy identifies how the Bank, in partnership with member countries and other development partners, can assist in addressing the particular mix of challenges that shape development prospects in the region. The Strategy highlights a World Bank role in three key areas:

- *Helping take the small states agenda forward in the Pacific region.* The Bank will continue to provide advice and analysis of regional trends and options through the biennial Regional Economic Reports, the ongoing work of the small states network and regionally focussed sector work. This will include work on catastrophe insurance, commodity risk management, adaptation to climate change, trade regimes post-Lome, globalization, management of ocean resources and the growth of towns.

*A targeted and innovative lending program.* The Bank will maintain a focused lending program in key areas including health, education, transport infrastructure and private sector development. In line with the thin institutional capacity in the region and the often high transaction costs involved for small states, the lending program will move away from project based financing to the development of program lending and sector wide approaches developed in partnership with other development partners.

*A responsive program of country-based economic and sector work.* The Bank will maintain its capacity to respond flexibly to individual member country requests for short term analytical work and technical assistance.

The Bank's Strategy has been circulated widely for comment and will be finalized by mid 2000.

The Bank's decision to relocate the PNG and Pacific Islands Country management Unit to Sydney will be an important step in improving the Bank's understanding of and responsiveness to the specific needs of its small Pacific members. The decision to relocate the CMU is both part of broader process of decentralization within the Bank's East Asia and Pacific department and a tangible expression of the commitment of the Bank to its Pacific members.

### The World Bank's framework at work: the Caribbean

The **Caribbean** Country Management Unit serves 15 countries, the vast majority of them "small." Interaction between this unit and the Task Force has already strengthened partnerships and stimulated new initiatives—such as support for disaster mitigation, economic analysis of catastrophe insurance, a sharper focus on aid coordination, and assessment of institutional capacity. Activities that are responsive to the characteristics of small states include

- flexible support for **disaster mitigation**, including availability of contingent loans (see paragraph 7 below).
- analysis of the **insurance market for natural disasters**, its low penetration in Caribbean states, and whether it is possible to diversify the risks of natural disasters through international capital markets. This work has benefited from discussions in the context of the Task Force; it will continue so as to provide a basis for Bank lending in support of reforms in the financial and insurance sectors. The objective is better, lower-cost protection for businesses and households, as well as for key public agencies, from disaster risks. Future Bank lending could support (i) strengthening the local insurance industry, its links with international reinsurance, and the supervisory/regulatory capacity to assure long term solvency in light of the risk exposures of assets in the region; (ii) design and testing of a catastrophe insurance/reinsurance sub-regional pool to transfer the 'catastrophe' portion of risk premiums and associated coverages, using international reinsurance support plus other long term risk financing mechanisms (including insurance therein of critical government assets and infrastructure); and (iii) setting up and enforcing upgraded building codes.
- an **institutional review** of Eastern Caribbean States to identify areas where it is politically and technically feasible to develop cross-country agreements that reduce the unit costs of public services; technical assistance to the OECS Secretariat for the same purpose.
- work on the OECS **telecommunications sector** to introduce pro-competition reforms and increase the supply of informatics-related skills in the client countries. Bank financing and advice associated with this project have already had a major impact, both in prices of service and in sub-regional cooperation: in anticipation of liberalization, the current monopoly reduced international call rates by 27-50% in October 1999; a common regulatory system for Dominica, Grenada, St Kitts-Nevis, St Lucia and St Vincent was designed; and negotiations are currently on-going between the OECS and the monopoly, C&W.

3. *Emphasis on programs as well as on projects.* In small states as elsewhere, and in line with the CDF approach, the Bank will increasingly be seeking to deliver assistance to countries where it can be used most effectively for higher impact, through designing lending and non-lending services based on the quality of public sector budget programs and sector budgets rather than as isolated interventions. For instance, a flexible, multi-year, budget-support operation is being considered for Cape Verde and could be replicated in other small countries with strong performance on macro and structural policies, good project portfolio management ratings, a credible public expenditure program, and sufficiently strong institutional capacity (especially in procurement and financial management) to manage such an operation without close Bank supervision.
4. *Graduation policy.* Decisions on eligibility for borrowing from IBRD and IDA are based on per capita income, social indicators, and creditworthiness, and economic performance. Both IDA and IBRD graduation programs are flexible and decisions are reversible. For

example, flexibility allows the avoidance of automatic graduation in cases when a country reaches the per capita income IBRD threshold but has no access to international capital markets. It also allows the Bank to accommodate situations when a country becomes non-creditworthy as a result of a shock such as a natural disaster or adverse external events. The IDA12 agreement (which covers a three-year period ending on June 30, 2002) includes a specific exception to the per capita income criterion for small island economies, continuing a practice that has been in effect since 1985. The exception extends IDA eligibility to a number of small island countries that have per capita incomes in excess of the operational cut-off<sup>41</sup> and lack creditworthiness for IBRD. The analysis and conclusions of the Task Force strengthen the case for a continuation of this IDA exception. It is expected that the exceptional vulnerability of small island economies to external economic shocks and disruptive natural disasters would be considered during discussions of IDA13 (which would cover the three-year period ending on June 30, 2005) and would continue to be taken into account by the IDA Deputies in establishing eligibility for IDA.

#### *A work program for small states*

5. Within this overall framework, the Bank intends to continue and strengthen the attention it gives to small states issues in the future.
6. *Reducing transactions costs for small states and donor coordination.* Activities and requirements of multiple donors place a heavy and unnecessary burden on limited administrative capacity in many small states. Tackling this will require a major effort by donors, cooperating in a genuine partnership, country by country, to try to rationalize their support and simplify their procedures to reduce the burden. The Bank will actively promote such cooperation in all small states where it operates.
7. The recently introduced adaptable program loans (APL) and learning and innovation (LIL) loans give the Bank more flexibility in serving small states. Both types of loans considerably ease demands on local capacity and simplify the design of loan operations, reducing implementation problems. Learning can occur over time, by accumulating experience with a certain project design in one country, or ‘horizontally’ by using the same project model to address a problem in several countries. For instance, in December 1998, the Board approved a ‘horizontal APL’ to support a disaster mitigation operation for Eastern Caribbean States affected by hurricane George. The project includes infrastructure improvements, strengthening regulation and enforcement, and establishing a contingent loan that can provide funds in the event of a catastrophe to countries that have adopted appropriate mitigation measures. The design of the project was adapted to the institutional capacity and country needs. The program is being phased to allow countries that have already developed rehabilitation and institutional strengthening program components (Phase 1) to conclude loan agreements immediately (Phase 2), while allowing the remaining countries to “sign up” as soon as their programs are ready. All countries still require long-term support to further improve their preparedness to mitigate risks and respond quickly to future disasters. The APL anticipates subsequent phases —flexibly timed in a “seamless” fashion as each country becomes ready—to provide continued

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<sup>41</sup> The operational cut-off for IDA eligibility is currently per capita GNP in 1998 of \$895 using the World Bank Atlas methodology. Information on IDA eligibility and resource allocation is at <http://www.worldbank.org/ida/>.

support for institutional and infrastructure development (Phase 3). Finally, the operation makes financial resources readily available for emergency reconstruction to restore, inter alia, critical public services (Emergency Contingency Phase). Experience with APLs in the Pacific has been limited to an Infrastructure Asset Management Project in Samoa. Lessons from the Samoa experience will be valuable in looking further at the use of APLs in the Pacific region. Another example of a promising approach is the Learning and Innovation Loan (LIL) for the St. Lucia Poverty Reduction Fund. It is designed as a standard “off-the-shelf” regional project. If this project works well in St. Lucia, the Bank will be able to replicate it readily in other small countries of the Eastern Caribbean. Bank regions will continue to look for other ways to simplify their operations in small states and reduce costs.

8. *Supporting private sector development, as many small states seek to transform their economies to meet the challenges of globalization.* One aspect of this support will be continued special efforts by the IFC, including the Caribbean Project Development Facility; the African Project Development Facility; and the South Pacific Project Development Facility. These aim to help domestic entrepreneurs to develop projects that could be attractive to foreign investors. Support from bilateral donors for these activities has been important as well. But perhaps even more important in future will be support from the Bank to the public sector in this area. Small states need enabling environments and the right kind of public policy support—for example in training and education, and creating regulatory frameworks—to encourage new activities, many of which will be in the service sectors. The Bank will, for example, provide support for policies that promote competition and properly regulate utilities and other industries. These issues are of considerable importance with the prevalence of monopoly or oligopoly suppliers in so many small states. Constrained capacities, limited administrative capabilities and the focus on private sector development also highlight the need for effective coordination within the World Bank Group: IBRD/IDA, IFC and MIGA. Tight cooperation and coordination will enhance efficiency (a key factor in a small state) and will ensure that private sector activities directly support broader development objectives.
9. *Supporting regional initiatives.* One approach that can work in tackling limited public sector capacity in small states is to seek to develop regional approaches to public sector functions wherever feasible. The Bank will support regional initiatives which aim to share infrastructure, public goods and services (so as to lower per capita costs to the residents of small states) and provide help to strengthen regional bodies that can advance these objectives. Action on a regional basis is possible to improve the quality and reduce prices of telecommunications, as Bank support for the OECS telecommunications project demonstrates (see Box 8). The Caribbean Country Management Unit is undertaking an institutional review of Eastern Caribbean states to identify areas where it is politically and technically feasible to design and implement cost-saving cross-country agreements. Moreover, an Institutional Development Fund grant is supporting the OECS Secretariat and providing assistance to the OECS countries to strengthen their sub-regional ties. Capacity building is a high priority in the Africa region where small states have full access to the services provided by the Partnership for Capacity Building in Africa (PACT). Regional and sub-regional action has been a feature of the approach taken to overcoming development constraints in the Pacific for some time; an impressive range of regional arrangements and organizations have evolved. The Bank will continue to work with members and those organizations to identify further opportunities where shared regional

action is sensible. This will include through the Bank's biennial Pacific Regional Economic Report and regionally focussed economic and sector analysis.

10. *Assistance in exploiting the opportunities that information technology and electronic commerce can bring to small isolated states.* Work sponsored by the Task Force suggests that these technologies can be a major source of help in the development of small states' economies. But success requires the correct public sector infrastructure, crucially a regulatory framework that will encourage high quality/low cost telecommunications services, and the competition that will deliver that. The Bank plans to provide further support in this area to small states in all regions. For example, a recently approved education and training project in Cape Verde will facilitate distance learning at the primary level for teacher upgrading and pedagogical outreach. With technical assistance from Brazil, this operation will reduce the problems of Cape Verde's highly dispersed teaching force.
11. *Lowering the costs of natural disasters, and improving risk management.* Every year natural disasters exact a large toll. Their adverse effects can be eased through ex-ante mitigation measures, and ex-post prevention insurance. In December 1998 the World Bank approved a loan for infrastructure investments and regulatory improvements in the Eastern Caribbean, with the goal of reducing the impact of tropical storms. The loan package also includes a contingency facility—providing automatic access to funds in the event of a catastrophe—for countries that have adopted mitigation measures. The Bank has started work on the feasibility of catastrophe insurance. Such insurance is conceivable in a highly integrated global financial market, possibly through the use of credit-based and capital market instruments that may be attractive to investors with highly diversified portfolios. These activities are complemented by GEF to help mitigate the effects of climate change (global warming, sea level rise). The Bank is also a founder and a major participant in the ProVention Consortium, a global partnership aiming at reducing disaster risk in developing countries and making disaster prevention and mitigation an integral part of development efforts. Also, the work of an International Task Force on Commodity Risk Management in Developing Countries, though still at a very early and exploratory stage, may identify ways through which small states could better manage the impact of price volatility on their small farmers. The Bank is also active in assisting in the restructuring of pension systems and improving management of pension system financial reserves.
12. *Protecting the physical environment.* Many small states have vulnerable physical environments as well as vulnerable economies. As development takes place it will be crucial to ensure that it is sustainable, by protecting the environment at the same time. Many mistakes have already been made in this area, for example in insensitive tourism development and over-exploitation of non-renewable resources. The Bank will step up its support for small states in this regard, both with advice and finance. Coastal zone management operations are planned in several West African small states such as The Gambia and Guinea-Bissau. A focus of the forthcoming Pacific Regional Economic Report will be on identifying and discussing adaptation strategies available to Pacific countries as they respond to climate change. The report will also focus on how Pacific countries manage their ocean resources and the continuing growth of towns in the region.

13. *Knowledge management.* There is a continuing task of accumulation of knowledge about policies and approaches that work and do not work for small states, and sharing this knowledge and experience among states both within and across regions. The Bank intends to help in accumulating and sharing such knowledge (see par. 14-14). A good example of this is the West African Enterprise Network (WAEN), a group of dynamic, second-generation businessmen and women in West Africa. WAEN is supported by the World Bank, the European Union and several bilateral donors; its logistical support is facilitated by a two-person unit in OECD in Paris. It has built a membership of over 350 entrepreneurs in 13 West African countries and has concluded several transnational and national ventures. It is now recognized as a credible partner by African governments, regional institutions and donors, as well as by offshore investor groups in North America, Europe, and Asia.

*Enhanced attention to cross-cutting issues*

14. While the bulk of this agenda will be for the Bank regional departments to carry through, in partnership with the countries themselves, there is also a need for a continuing capacity in the Bank to handle issues concerning small states that cut across regions. Some of these issues will be carried forward in parts of the Bank with responsibility for global policy topics. Effort will be made to ensure that the experiences, developments, and challenges facing small states are appropriately reflected in Bank publications, and that the Bank's policy work takes account of the special characteristics of small states. For example, the units dealing with trade policy or environmental issues will incorporate the specific items of concern to small states in their overall activities.
15. In addition, the Bank will continue to learn about and help monitor small states issues, in partnership and cooperation with representatives of small states. Sharing of analyses and experiences with different approaches relevant to small states will be taken up by a planned Bank-wide thematic group. Also, the Bank will develop a small states web site where small states can share experiences and access information, and arrange an annual small states forum at the time of the Bank/Fund Annual Meetings, where new ideas can be discussed and experiences shared. This forum will also provide a structured opportunity for small states' representatives to take stock of their and their partners' progress in implementing the agenda set out in the Task Force report.

## The Commonwealth Secretariat Framework

1. With 32 small states within its 54-country membership, the Commonwealth has a long-held interest and programme of action in support of small developing countries. In recent years, the Commonwealth Secretariat has maintained a strong focus on these countries, with some 60 per cent of total programme expenditure under the Commonwealth Fund for Technical Co-operation disbursed through projects which benefited small states. This level of support was sustained despite falling levels of funding for the organisation's work.
2. The Secretariat has provided advocacy, policy advice and technical assistance. In particular, pioneering work has been carried out on the vulnerability of small states - the most recent being reported in, *A Future for Small States; Overcoming Vulnerability*. It has also developed a Commonwealth Vulnerability Index for developing countries, showing that small states are more vulnerable than their larger counterparts, and produces a unique, annual report, *Small States Economic Review and Basic Statistics*, drawing from the Commonwealth database and the organisation's work on small states' issues.
3. In response to the Task Force report, the Commonwealth Secretariat is committed to maintaining and where possible expanding present, overall levels of support for small states development, in terms of both its advocacy and provision of technical assistance. In so doing, a sharper focus will direct efforts towards the following areas:
4. *Tackling Volatility, Vulnerability and Natural Disasters*. As in its other areas of assistance to small states, the Secretariat will sharpen its advocacy role on vulnerability. Attention will be placed on obtaining commitments from the UN system and the IFIs to define predictable guidelines and criteria for the graduation of countries from least developed (LDC) status. While the World Bank already follows a flexible approach to graduation, some countries (and small states, in particular) feel that there remains considerable uncertainty, which may affect development strategies and foreign investment. On the other hand, there appear to be strong grounds for some small states, presently excluded from access to IBRD funds, to regain their eligibility to borrow from that source. In both cases, justification might be drawn, in part, from consideration of an additional criterion for eligibility, namely, vulnerability. In this regard, use can be made of the Commonwealth vulnerability index.
5. Services will be provided to assist in the establishment of national and regional capital markets, stock exchanges and commodity risk management mechanisms. The latter focus follows from the Secretariat's participation in the World Bank's International Task Force on Commodity Risk Management and will contribute to the programme of action to implement the recommendations of that group. This is likely to include designation of an international intermediary, identification and training of national entities, development of transmission mechanisms to ensure that benefits from price risk management flow through to small-scale producers, and facilitating the development of commodity price risk insurance markets, involving international development agencies and the private sector. The Secretariat has already provided assistance of this nature in supporting the establishment of local stock exchanges in developing Commonwealth member countries. It is especially appropriate that a number of small states are among those included in the proposed pilot testing of the commodity risk management programme.

6. On the environment, assistance is available for the development of regional programmes for water resource management (in association with partner organisations), and to develop or strengthen programmes on the management of Exclusive Economic Zones (EEZs), coastal zones, fisheries and other environmental resources.
7. *Transition to the Changing Global Trade Regime.* The Secretariat is ready to take the lead in strengthening the existing Commonwealth facility in Geneva, which presently provides support to small member countries in their relations with WTO on notifications, negotiations and use of the Dispute Settlement Mechanism. It is intended that the facility be expanded so as to provide advisory services on new issues in WTO, back-stopping small states during the forthcoming new Round of Multilateral Trade Negotiations. This will best be achieved through a multilateral initiative, perhaps involving the Secretariat, the World Bank, WTO UNCTAD and other partner organisations or donors, with whom discussions can be held in order to carry this forward.
8. The Secretariat will continue to provide support to small states as they negotiate trade agreements and other relations with the EU under the recently agreed successor to the Lomé IV Convention. This will be in close collaboration with member governments, the ACP Secretariat and the administrators of the EU's assistance facilities.
9. *Strengthening Capacity.* The Commonwealth Secretariat will strengthen its support to regional organisations dealing predominantly with small states - e.g. the Secretariats of the Caribbean Community (CARICOM), the Indian Ocean Commission (IOC) and the South Pacific Forum (SPF). This is already in train, in terms of assistance in preparations for the next WTO Ministerial Meeting. It will be extended to other areas of Secretariat competence, where the regional organisations have a particular focus. For example, in the areas of government, finance and regulation, this might include matters relating to governance, anti-money laundering measures, investment codes, common taxation regimes, arrangements relating to international financial centres, customs rules and labour mobility.
10. The Commonwealth Secretariat is co-operating with the World Bank and others in the implementation of the Comprehensive Development Framework (CDF). At present, all pilot projects are to take place in large developing countries. Given the problems faced by small states in aid absorption and the institutional constraints in these countries vis-à-vis traditionally inflexible modes of aid delivery, it seems especially appropriate that some small states should be included in the CDF pilot.
11. *New Opportunities and Challenges from Globalisation.* The Commonwealth Trade and Investment Access Facility (TIAF) was set up by Heads of Government at their 1997 meeting in Edinburgh in order to assist developing member countries, particularly small states and least developed ones, to adjust to, and take advantage of, the opportunities presented by globalisation and the rapidly increasing flows of world trade and investment.
12. Under the Facility, projects are funded which provide either: (i) policy advice and technical assistance to help countries identify and manage the potential economic and social impacts of trade and investment liberalisation, including restructuring strategies, and the identification of new sources of revenue, and new market opportunities; (ii) technical assistance and training in helping to put in place legal and regulatory frameworks to promote trade and investment flows; or (iii) assistance to countries to

increase their capacity to participate in WTO negotiations and to meet requirements or standards of WTO agreements and other international trade and investment agreements.

13. It is intended that TIAF be broadened to accommodate an enlarged, specific focus on small states. Attention will be directed toward providing policy advice, technical assistance and promoting trade-related investment, as outlined above, as well as facilitating the development of small and medium-sized enterprises. For this purpose, the funding base of TIAF needs to be expanded to include other donor countries, and its operations extended for a further three years. The Secretariat is ready to take a lead in expanding the TIAF.
14. Through the Commonwealth Private Investment Initiative (CPII), initiated in partnership with the Commonwealth Development Corporation (CDC), the Secretariat has already played a lead role in the launch of four venture capital-type funds - in particular, for small states in the Caribbean (the Tiona Fund) and the Pacific (the Kula Fund). The Commonwealth will explore ways to further expand these private capital flows and to develop new instruments to mobilise such financial flows to the benefit of small countries. The Secretariat also stands ready to provide assistance in support of work on disaster preparedness and mitigation. In particular, help can be provided in designing national and regional building codes, which are acceptable to insurers, as a means of opening the way for greater private sector participation in disaster insurance.
15. Finally, following endorsement by Commonwealth Heads of Government, the Secretariat will seek agreement on a mechanism to track the implementation of commitments made by all Task Force partners. Such a mechanism will be designed to review the progress of programmes, in close consultation with the partner organisations involved in their delivery. The aim is to ensure that benefits are indeed accruing to small states.

## **The European Framework**

1. The European Union is very committed to the debate on Small States and in the international dialogue established on the Vulnerability Factor. In this context the European Community and its Member States are involved in the on-going activities connected with the Barbados Programme of Action for the Small Island Developing States (SIDS) and the work carried out by the UN and some of its specialized agencies in helping SIDS to better adapt to the challenge of their sustainable development. During 1999 the European Commission produced the Report "The EU's co-operation with SIDS in the Framework of the Barbados Program of Action" and financed studies of UNEP, Universities, NGOs and some Regional Organizations in topics affecting the vulnerabilities of small states. These studies are showing that the Community Aid is contributing both to the Small States' trade concerns and the financing of programs and projects in the fourteen priority areas of intervention established by the Barbados Program of Action for the Sustainable Development of the Small Island Developing States: climate change and sea-level rise, natural and environmental disasters, management of wastes, coastal and marine resources, freshwater resources, land resources, energy resources, tourism resources, biodiversity resources, national institutions and administrative capacity, regional institutions and technical cooperation, transport and communications, science and technology, and human resource development.
2. The European Union has a comprehensive development policy that for historical reasons differentiates between the actions in favor of the ACP (Africa, Caribbean and Pacific) countries covered by the Lomé Partnership Convention; the Overseas British, French, Dutch, and Danish Territories; and the rest of Developing Countries in Asia, Latin America and the Mediterranean. In all cases the assistance to each individual country is flexible and adapted to the specific country circumstances and vulnerabilities. The EU can contribute its experience from the Lomé Convention in providing differential treatment to certain groups of countries including small island states and small landlocked states. Differentiated treatment includes aid allocation and preferential trade arrangements, e.g., quota systems for specific commodities. For most Small Developing States EU's Aid inflow is well above that of the developing countries average.
3. The European Union grants market access to products originating from developing countries including special treatment for ACP (under the Lomé Convention) and for other developing countries (under the Generalized System of Preferences Scheme (GSP). The EU's present Trade regime with developing countries will change in the future in order to better adapt to the World Trade Organization rules. Vulnerable Islands and Landlocked States will continue to benefit from maximum level of tariff preferences and trade promotion support.
4. The ACP-EU Partnership Agreement recognizes the specific difficulties confronted by island developing states and (during the negotiations for a Post-Lomé Agreement) the EU and the ACP group reaffirmed their attachment to maintaining special treatment for LDCs and to duly take into account the vulnerabilities of Small, Landlocked and Island ACP countries when discussing the role and importance of trade and services development as a means of enhancing developing countries competitiveness in the global economy.

5. Taking into consideration that small Caribbean banana-dependent countries are under threat (following the WTO's ruling against the EU banana regime) the EU is supporting the transition of the most banana-dependent economies to meet the challenge of globalization by improving competitiveness of the banana sector, by creating new activities to diversify from the traditional banana production, by financing new infrastructure and by retraining much of the labor force.
6. The EU is financing the establishment of the ACP office in Geneva to secure a more effective involvement of these small and disadvantaged economies in the WTO machinery and negotiations at the multilateral level.
7. The EU is paying considerable attention to foster the harmonious and gradual integration of the developing countries into a globalized and liberalized world economy. In this line EU support is provided for addressing supply and demand constraints, macroeconomic stability and structural adjustment at national and regional level and regional integration issues, especially important for small economies.
8. The European Union is the single major provider of grant aid to assist developing countries. In organizing financial and technical co-operation, the EU is ready to take into account the different needs of developing countries and regions in order to tailor the assistance to the specific circumstances of vulnerable, landlocked and Island ACP countries. In the joint effort to support the small states in implementing sound macroeconomic reforms and in establishing the grant resources available to them, the EU is ready to ensure flexibility and tailor assistance to evolving or changing country circumstances and needs. One of the results of the application of this principle is that the aid granted per capita to small states economies through National and Regional Indicative Programmes financed by the European Development Fund is higher than that provided to bigger economies.
9. The EU agrees that regional co-operation is important for small states in many areas through which economies of scale can be attained. The European Commission therefore supports specific requests from the different regions in the Caribbean, Indian Ocean and Pacific in order to enhance regional co-operation in areas like capacity building at the regional level, information gathering and dissemination, capacity building, training, environment, transport, research, technology, tourism, promotion of intra-regional trade, etc. This regional action will be reinforced in line with the Regional Economic Partnership Agreements (REPAs) foreseen for the future ACP-EU relations in order to arrive to a kind of relation WTO compatible.
10. Recognizing that instability of export earnings, particularly in the agricultural and mining sectors may adversely affect the development of the ACP States, the 2000 new ACP-EU Partnership Agreement establishes a system of additional grant support within the European Development Fund financial envelope for support to long term development. This support substitutes the traditional STABEX and SYSMIN previously operated to compensate the instability of export earnings in agriculture and mining sectors. Both systems foresee a more favorable treatment for LDC, landlocked and Island ACP states.
11. In the specific area of the management of environment and natural resources covered by the Barbados Programme of Action for Small Island Developing States, the EU financially supported the preparation of three separate reports within the framework of the United

Nations Environment Programme Global Environment Outlook for the Caribbean, Indian Ocean and Pacific Region. These reports have been prepared by regional organizations in the three regions and have been officially launched during the 22nd Special Session of the UN General Assembly for the review and appraisal of the implementation of the Barbados Programme of Action for the Sustainable Development of Small Island Developing States held in New York in September 1999. The reports describe environmental trends, policy responses and emerging issues for the small states and provide basis for national governments action.

12. In the specific area of natural disaster prevention, the European Community Humanitarian Office (ECHO) has created a Disaster Prevention, Mitigation and Preparedness Program for Caribbean states vulnerable to natural catastrophes. Taking a diagnostic approach to identifying hazards and assessing the vulnerability of the people, and the existing capacity to respond to disasters. Risk maps are being drawn up and proactive strategies developed to reduce the impact of future hurricanes, volcanoes, earthquakes and floods. In the Indian Ocean support to regional meteorological co-operation is on-going. In the Pacific Region support for a cyclone warning system has been decided.
13. Recognizing the importance which both the EU and the ACP Countries attach to the private sector as a primer mover of economic development, the New 2000 Partnership ACP-EU Agreement creates a new investment facility for the support of private and business sector development in the ACPs. The Facility will be managed by the European Investment Bank (EIB) as a revolving fund, enabling net income earned by the Facility to be reinvested in the ACPs. The Facility will be able to offer a range of financial instruments including equity, quasi-equity instruments and risk sharing or subordinated loans. In general the Facility will be invested on market related terms, taking into account the risk element in a particular transaction. For small states the risks covered in these operations, could, subject to a more detailed study, be broadened out from purely commercial risks to include some of the weather and environmental risks to which these countries are vulnerable. Moreover, in appropriate cases, the new EU-ACP Partnership Agreement allows more concessional terms to be made available. It is envisaged that a significant proportion of the Facility resources will be made available through financial intermediaries in the ACP concerned, but, for small island states, there will be an increasing emphasis on regional financial institutions where these exist and effectively serve the interests of the countries concerned.

## The World Trade Organization Framework

### *Small Economies in the WTO - The Geneva Ministerial Declaration and its Follow-Up*

1. The Geneva Ministerial Declaration of 1998 states that Ministers "remain deeply concerned over the marginalization of least-developed countries and certain small economies, and recognize the urgent need to address this issue which had been compounded by the chronic foreign debt problem facing many of them."<sup>42</sup>
2. The issue of small economies was first raised in the WTO by Bolivia in a discussion in March 1997, prior to the High-Level Meeting on Least-Developed Countries' Trade Development. Bolivia, while appreciating the efforts made by international organizations in cooperating to better integrate LDCs into world trade, suggested that the results of the Meeting should be applied to other countries with small economies, including land-locked economies.<sup>43</sup>
3. Mauritius took up the issue in the Intersessional Committee of the WTO General Council, as part of the preparatory process for the Seattle Ministerial Meeting. It was then raised in the Committee on Trade and Development in November 1998, with the circulation of a paper jointly sponsored by Barbados, Jamaica, Mauritius, Sri Lanka and Trinidad and Tobago.<sup>44</sup> Bolivia, Cuba, Dominica, Dominican Republic, El Salvador, Guatemala, Haiti, Lesotho, Malta, Nepal, Nicaragua and Sri Lanka associated themselves with the ideas expressed. Barbados, Fiji, Guatemala, Lesotho and Mauritius also circulated papers describing their experiences as small economies.
4. The joint paper referred to the vulnerability of small economies, the inadequacy of per capita income as a measure of the level of development, and the proposition that a vulnerability index should be used to assess the developmental levels of small economies. Small economies were seen as vulnerable because of (i) natural features such as their demographic structure, the availability of economically exploitable land, their vulnerability to natural disasters and their geographical location; (ii) considerations such as their small internal market, problems of realizing economies of scale because of the small size of the economies and small size of firms, difficulties in ensuring effective and developed infrastructure and efficient provision of government services, heavy reliance on a few commodities and a few overseas markets and consequent instability of export earnings, high transport costs stemming from cartel-like activities of carriers and small volume of goods transported, and consequent constraints in pursuing economic diversification programmes; and (iii) other elements such as high dependence on trade taxes for revenue, limited domestic savings capacity and difficulties in attracting FDI, a high share of public sector expenditure in GDP, high per capita costs in establishing basic infrastructure and a shortage of "critical mass" in the economy.
5. In terms of specific trade-related proposals, the paper suggested that preferential trade agreements had partly compensated for the lack of comparative advantage of small economies, and that it would therefore be difficult to contemplate the easy integration of small economies into the Multilateral Trading System if preferences were removed abruptly. The authors also pointed to a link between the existence of trade preferences

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<sup>42</sup> WT/MIN(98)/DEC/1, paragraph 6

<sup>43</sup> WT/COMTD/M/14

<sup>44</sup> WT/COMTD/W/50

and the attraction of FDI into small economies, a need to improve telecommunications links with small economies to enable them to take advantage of the electronics revolution in communications, and the high cost for small economies of the WTO Dispute Settlement procedures.

6. In discussions in the Committee on Trade and Development, although some initially expressed concerns about the overlap between "small economies" and least-developed countries (LDCs), there was increasing support for the small economies' paper. The importance of structural features of small economies such as size, trade concentration and consequent vulnerability to external shocks, and the crucial importance of market access, were emphasised. Some support was expressed for the use of a vulnerability criterion in applying "special and differential" treatment to small economies, in addition to LDCs, and a proposal was made that the concept of "small economies" be further refined to determine its fit with the WTO rules-based system. Some industrialized Members also supported the arguments presented by the small economies in seeking ways to overcome marginalization, particularly through increased and more focused technical assistance to enable them to participate in the multilateral system, and the importance of preferences.

### *Definitional Issues*

7. Developing countries in WTO are a self-defined group, without particular reference to any policy question. Special characteristics, interests and concerns of various groups of countries, other than "developing countries" or "least-developed countries" are, however, identified in some of the WTO Agreements; for example, net-food-importing developing countries and developing countries affected by the growth of illicit narcotic crops in the Agreement on Agriculture, developing countries whose per capita GNP is below US\$1,000 in the Agreement on Subsidies and Countervailing Measures, and small textile and clothing suppliers and cotton and wool producing or exporting countries in the Agreement on Textiles and Clothing,.
8. The only clearly identified group of developing countries accepted as such by WTO Members as a whole is the least-developed countries (LDCs) as defined according to the criteria used by the United Nations. Twenty-nine of the 48 LDCs are currently WTO Members. The fit between LDCs and the "small state" grouping defined by the World Bank and Commonwealth is highly imperfect; only 4 of the 29 LDCs that are WTO Members are "small states" while nine of the WTO Members that have raised the issue of "small economies" in the WTO setting are not identified as "small states" according to the World Bank/Commonwealth criteria (Bolivia, Cuba, Dominican Republic, El Salvador, Guatemala, Haiti, Jamaica, Nicaragua and Sri Lanka).
9. In addition, it must be said that there is still a certain doubt among WTO Members, both developed and some of the larger developing countries, concerning the need for special consideration for small developing economies, and it is felt that the case has not been fully established. This is one reason why a number of developing countries have called for a work programme on the subject before the Fourth WTO Ministerial Meeting (see below, Section IV).
10. One method of identifying a group of "small, vulnerable" developing economies among the WTO membership might be to relate them to their scale of payments of contributions

to the WTO budget, which is based on the share of Members in world trade.<sup>45</sup> In the 1999 WTO budget, 50 Members were liable to pay the minimum subscription of 0.03 per cent of world trade. Forty-nine of these Members were classed as least-developed countries, "small states" as defined by the Commonwealth/World Bank, and/or Highly Indebted Poor Countries in the IMF/World Bank terminology. Extending the contribution level to 0.05 per cent would add seven more "small states": and to 0.1 per cent, an additional three.

### *Steps Proposed And Taken In Favour Of Small Economies*

11. In their statement to the Committee on Trade and Development in July 1999, the representatives of the World Bank and Commonwealth Secretariat proposed four steps that might be taken by WTO Members in respect of small, vulnerable states. These were:
  - to recognize that small vulnerable states face difficult challenges in making the necessary adjustments to multilateral trade liberalization and achieving a sustainable threshold of development sufficient to free them from dependence on aid and trade preferences;
  - to streamline and accelerate procedures for accession to the WTO;
  - to establish arrangements that will ease the legal costs of using the Dispute Settlement Mechanism for small states; and
  - to lower the subscription fees of small states to the WTO.<sup>46</sup>

#### *(i) Challenges to developing countries, including small states*

12. The challenges that developing country Members face in adapting to conditions of multilateral trade liberalization can be addressed in the WTO Agreements through their provisions for special and differential treatment (S&D). These fall into five main groups: provisions aimed at increasing trade opportunities, provisions that require WTO Members to safeguard the interests of developing country Members, flexibility of commitments, transitional time periods, and provisions for technical assistance.<sup>47</sup>
13. Among the first group are measures falling under the "Enabling Clause" (preferences under the GSP, regional agreements among developing countries, and special preferences for least-developed countries) or under waivers (e.g. for Lomé IV, preferential arrangements for the Caribbean by the United States and Canada, or a recently agreed waiver permitting more advanced developing countries to extend duty-free preferences on a non-reciprocal basis to LDCs<sup>48</sup>). The second group includes provisions for taking account of special interests of developing countries in Agreements such as the TBT, Anti-Dumping, Subsidies and Safeguards Agreements. The third group allows for lower levels of WTO commitments by developing countries than by others (e.g. in tariff bindings or agricultural export subsidies). The fourth relates to greater flexibility in time periods for implementation of WTO Agreements by developing countries. And the fifth provides the overall framework for technical assistance by the WTO and its Members to developing

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<sup>45</sup> This issue is discussed in Commonwealth Secretariat/World Bank (1998) "The Trade Policy Implications for Small Vulnerable States of the Global Trade Régime Shift".

<sup>46</sup> Statement by Sir Humphrey Maud to the Committee on Trade and Development, 7 July 1999.

<sup>47</sup> See High Level Symposium on Trade and Development, March 1999, Background Paper by the WTO Secretariat.

<sup>48</sup> WT/L/304, 17 June 1999

countries for capacity-building. Specific S&D provisions for least-developed countries are contained in the Enabling Clause of GATT 1994, provisions relating to non-reciprocity in trade negotiations in GATT 1994 and GATS, in Article 24 of the Understanding on Dispute Settlement, and in the Agreements on Agriculture, Subsidies, TRIPS, TRIMs and SPS. Generally, S&D is judged to be applicable according to the level of development or specific problems of the Member; however, there are specific cases identified in certain Agreements, as noted in the joint paper referred to above.

14. The scope and application of "special and differential" treatment and of other developmental considerations has for long been under discussion, but without any particularly definite outcome, in the Committee on Trade and Development and in the WTO General Council pre-Seattle discussion.

(ii) *Accession*

15. The length and complexity of accession procedures has long been recognized by WTO Members. An initial response to this challenge has been the identification of practical ways and means capable of facilitating accession processes, particularly through special technical assistance efforts by the WTO Secretariat and the active movement of Chairpersons of particular Accession Working Parties, notably those relating to "small economy" island states. The 1997 High-Level Meeting on Least-Developed Countries recommended the WTO to further develop its efforts to assist least-developed countries in the process of accession to the WTO.
16. The issue was taken up by the former Director-General in a statement to the WTO General Council on 15 June 1999, made on the basis of his consultations with all Chairpersons of Accession Working Parties. In his statement, the Director-General, emphasised *inter alia* the roles of Members in the smooth functioning of the accession process, of Chairpersons of working parties in smoothing the concluding stages of negotiations, the need for terms and conditions of accession to uphold the integrity of the WTO system, and the urgent need of all acceding governments for focused technical assistance.<sup>49</sup>
17. Attempts were also made to bring this issue into discussion in the Seattle Ministerial Conference (see *Proposals To The Seattle Ministerial Conference*, below).

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<sup>49</sup> WT/GC/W/212, 17 June 1999

(iii) *Dispute settlement*

18. Although the Dispute Settlement system is recognized to be valuable, effective, and central to the legal rules established in the WTO, many concerns have been expressed about the costs of the system for developing countries. An initiative has been taken by a number of WTO Members to establish an "Advisory Centre on WTO Law", independent of the WTO Secretariat, whose task would be to complement the training and technical assistance already provided by the WTO Secretariat (which is required to be impartial) and provide legal advice to developing countries and economies in transition. Users of the Centre will be charged fees in accordance with their membership status in the Centre and their ability to pay. Least-developed countries, and founding members of the Centre, would pay no subscription and receive free advice in consultations up to a certain number of hours per year; for least-developed countries (but not for other developing countries, including small economies that are not LDCs), the fees for assistance during legal proceedings would also be heavily discounted (10 per cent of normal rates).
19. The Centre was successfully launched in Seattle, at the time of the WTO Ministerial Conference, and is expected to be fully active by 2001, subject to ratification by national Parliaments..

(iv) *Minimum contribution*

20. The issue of the minimum contribution to the WTO has been actively pursued by LDCs and other small economies in the Committee on Budget, Finance and Administration and the Committee on Trade and Development. These efforts have borne success; for the budget year 2000, the minimum contribution has been reduced to 0.015% of world trade in goods and services of the members. Most of the 47 WTO Members touched by this change are least-developed countries. However, 13 Members classed as "small states" by the Commonwealth and World Bank benefit.

***Proposals To The Seattle Ministerial Conference***

21. Two sets of proposals were made to the third WTO Ministerial Conference in Seattle on the issue of marginalization of small economies. The first, by Barbados, Dominica, Fiji, Grenada, Jamaica, Lesotho, Mauritius, Papua New Guinea, Solomon Islands, Saint Lucia and Trinidad and Tobago<sup>50</sup>, recalled the specific factors making small economies vulnerable and leading to comparatively higher costs of production and distribution on the world market for small economies and the vital role played by preferences under the GSP and under CBI, CARIBCAN, and the Lomé Convention. It proposed that the WTO Secretariat should prepare a consolidated list of products of export interest to small economies and that all developed markets should extend duty free access to products of export to small economies. The proposal also suggested that regional trade agreements should be encouraged as part of the process towards successful integration of small economies into the world market.
22. In relation to the Agreement on Agriculture, the proposal suggested that, because of the particular vulnerability of small economies to price and supply fluctuations, higher fixed costs of production and marketing, and susceptibility to natural disasters, future rules

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<sup>50</sup> WT/GC/W/361, 12 October 1999

should provide for measures at international level to assist small economies whenever they are adversely affected on account of any natural disaster, and to diversify into products which have greater potential for higher value-added. In addition, WTO Members should take steps for the rapid implementation of the Decision on Net-Food-Importing Countries and: give priority consideration to future agricultural trade liberalization to market access for small economies' products; to the provision of technical and financial assistance by major agricultural exporters and development institutions to improve agricultural productivity; and to make concessional facilities available when food prices exceed a particular ceiling or when domestic food production drops below a certain level.

23. In relation to the Agreement on Textiles and Clothing, the small economies proposal sought the provision of concessional loans by the World Bank and other financial institutions for upgrading, rationalizing or rehabilitation of their production units, and the provision of technical assistance for the adaptation of production to changing trends in designs and fashions and for marketing.
24. A particular emphasis was placed in the proposal on the high share of tariff revenues in the budgets of small economies and the harmful results of tariff reduction on Governmental budget balance. It was seen as "imperative" that small economies should be granted necessary flexibility to reduce tariff levels, in keeping with what they considered necessary for their balanced development and sustained growth, the competitiveness of their products, and sustaining their developmental momentum. The proposal sought also to embody in the rules a principle that small economies not be required to make further commitments to reduce tariffs and to bind reduced rates beyond what they consider consistent with their trade, development and financial needs; and that the level of tariff reductions should, *inter alia*, be based on individual assessment of their effective capacity to apply trade remedies such as anti-dumping and safeguard measures.
25. The document also contained requests for greater flexibility to be applied to small economies in the WTO rules on subsidies and a higher *de minimis* level in relation to the application of countervailing duties and safeguard measures. In relation to services, the proposal emphasised the importance of Article IV of GATS, relating to increasing participation of developing countries, and sought priority in new negotiations for the removal of barriers in sectors of export interest to developing countries; extension by developed markets of incentives to improve the access of small economies to technology, distribution channels and information networks, particularly through electronic commerce, and concrete capacity-building measures to assist their services sectors.
26. A second, highly focused submission to Seattle by Jamaica and Mauritius<sup>51</sup> proposed six principal areas where trade rules should be adapted in favour of small developing economies: transitional trade preferences; longer transitional periods for trade liberalization in small economies; concrete measures to address food security in small economies that are also net food-importers; assistance with modernization of sectors, such as textiles and clothing, on which countries may be heavily reliant for employment, income and foreign exchange earnings; more flexible arrangements for the establishment of regional trade agreements; and higher subsidy thresholds for the application of countervailing measures. The paper also proposed that the Committee on Trade and Development should elaborate a Work Programme to address the constraints faced by

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<sup>51</sup> WT/GC/W/373, 15 October 1999

small economies and make recommendations to the General Council for adoption before the Fourth Ministerial Conference.

27. The text that was carried forward to Seattle stated in the preambular section that "We give particular emphasis to the need to ensure that developing countries, *and particularly the least-developed and vulnerable small economies*, secure a share in the growth of international trade commensurate with the needs of their economic development", that "we take note of the problems and concerns facing economies in transition and the vulnerable situation of certain small economies and instruct that these be given due priority in the WTO work programme", and that "we...direct that all possible efforts be made to accelerate the process of accession, and in particular for least-developed and small economies". Other references to "small" or "vulnerable" economies occur in the sections on textiles, implementation of the Agriculture Agreement, reinforcement of technical assistance efforts, developmental objectives of proposed trade negotiations, assistance for participation in negotiations, small *island* developing states (in the proposals for negotiations on agriculture), and finally in a proposal for a work programme in the Committee on Trade and Development, as requested in the proposals submitted, "to identify concrete measures for the fuller integration of small economies into the multilateral trading system, and to make recommendations for action to the General Council before the end of the year 2000".
28. With the failure of Seattle to agree, all proposals are currently on hold. WTO Committees and Councils, including the Committee on Trade and Development, are currently considering their work programmes for the year. Conditions for technical assistance for least-developed and small economies have not improved as hoped. Work must begin in 2000 on the "Built-in Agenda" of negotiations on agriculture, services and aspects of TRIPs; however, it is yet too soon to say under what conditions and parameters these will begin, and in the absence of agreement on a round of negotiations it is not clear what time-frame may be set for their completion. Again, in the absence of agreement in Seattle on extensions, time periods have now expired for the application of certain WTO Agreements (notably, TRIMs and Customs Valuation) by developing countries, except those that have requested extension of the period for examination of their TRIMs, and the only security against the calling of such measures into dispute is the good will expressed in the General Council Chairman's statement on 17 December 1999.<sup>52</sup>

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<sup>52</sup> At the meeting of the General Council held on 17 December 1999, the Chairman made the following statement: "As I have proposed, this meeting of the General Council will be adjourned and resumed as early as possible next year to take up item 3 of the Agenda. It is my understanding that the question raised by a number of delegations concerning the provisions which lapse and deadlines which expire on 31 December of this year will be part of the consultations to be continued. The General Council will therefore revert to these matters when it resumes early next year.

It is understood that all Members will exercise restraint on the matters under consultation so as not to prejudice further fruitful discussion and decisions on these matters, or the position of other Members.

Members have made it clear that informal consultations are necessary on a wide variety of issues, including the issue of deadlines. Many Members urged understanding by all Members in those consultations, and they urged due restraint on the part of Members. This approach would be without prejudice to the position on rights and obligations of Members."

## **The International Monetary Fund Framework**

1. The Fund provides support to member countries through policy advice, technical assistance and financial assistance. Advice and assistance are tailored to each country's specific circumstances and needs, including special factors related to size.
2. *Surveillance.* A main channel for the Fund's policy advice is its surveillance over all members' economies, including those of small states. For slightly more than half of its small member states, the Fund maintains a close dialogue through annual consultations. Other small member states, including most of those in the Asia and Pacific region, are on a 24-month cycle (18-month in one case). For these countries, the Fund nevertheless maintains continuity in its surveillance activities through, inter alia, interim staff visits. Countries that are on a longer cycle can request to return to the annual cycle, or to have a staff visit, or the staff can recommend this to the authorities if economic developments suggest it would be useful. Small states have also availed themselves of staff monitored programs with the Fund, another channel by which the Fund maintains a close policy dialogue with member countries. During the period January 1995 – February 2000, six of the small member states had such a program, which can play an important role as a catalyst for aid and private capital inflows.
3. These various forms of bilateral discussions are supplemented by discussions with the regional authorities of those small member states which participate in a monetary union (namely, Eastern Caribbean Currency Union, West African Economic and Monetary Union, and Central African Economic and Monetary Community).
4. One of the changes in the global economy faced by all developing countries, large and small, is the decline in global aid flows. Many donors are also increasingly concentrating their scarce aid resources in countries that adopt sound policies. In these circumstances, it is doubly important that recipient countries adopt appropriate economic policies that serve their own needs. The economic policy advice provided by the Fund to small states plays a major role in helping these countries adopt policies that will attract foreign assistance. As the Fund continues to increase its emphasis on regional aspects of surveillance, it will be in a better position to offer small states policy advice that focuses on their transition to the new global economy.
5. In order to assist members to adjust to the changing global environment and improve the functioning of the international monetary system, the Fund, together with other institutions, is promoting greater transparency in both economic policy and in economic and financial data. Transparency is particularly important for small states: while in its absence, investors may find it cost effective to research and penetrate large markets, they are less likely to make the same effort for small opaque markets. Transparency and prudent macroeconomic management help reduce the overreactions and unnecessary shocks to which small states are particularly vulnerable. The Fund can bring its international experience to bear in providing small countries with advice that will help them to make adjustments before they are forced to do so by the markets. The Fund also promotes the orderly liberalisation of current and capital transactions, of which small states are potentially some of the greatest beneficiaries.

6. *Financial assistance.* Like all member countries, small states which face balance of payments difficulties are eligible for all of the Fund's financial facilities and loans (see the Box below on the various IMF loan facilities). Over the past twenty years, small states have in fact used a wide range of Fund assistance (see the Table below). For all Fund lending, the size of the loan is based on the country's economic size as measured by its quota in the Fund. All programs take into account country-specific circumstances, including size of the economy. An important principle in Fund lending is uniformity of treatment across all members. Two types of financial assistance that may be particularly helpful to small states that are vulnerable to natural disasters or have higher degree of export concentration, are emergency assistance for natural disasters and the Compensatory Financing Facility which, inter alia, provides financial assistance to countries that have balance of payments problems because of a shortfall in their export receipts. Small states that have low per capita income are eligible for the Fund's concessional loan facility, the Poverty Reduction and Growth Facility (PRGF). Eligibility for the use of PRGF resources has tended to follow closely the World Bank's decisions on IDA eligibility. Of the 19 small states eligible for PRGF (or its predecessor, ESAF) financing, eight have used these concessional resources to date (some more than once); two are currently in an PRGF arrangement with the Fund.
7. *Technical assistance.* The Fund provides a wide array of technical assistance (TA) to member countries through its Fiscal Affairs, Monetary and Exchange Affairs, Statistics, and Legal departments, and its IMF Institute offers training courses and seminars to member government officials both in Washington and outside. The area departments, as well as the Research and the Policy Development and Review departments, also provide technical assistance on occasion. It should be noted that in the early 1990s procedures were put into place to ensure that the sudden increase in TA provision to the transition economies would not crowd out other regions and countries, and these remain in effect.
8. Small states have made extensive use of the Fund's TA services, including through regional entities such as the Eastern Caribbean Central Bank. The provision of technical assistance to the small states of the South Pacific (by the Fund and UNDP) has benefited from the establishment of a regional centre in Fiji in 1993 (PFTAC), whose activities are co-ordinated by the Fund and now financially supported by the AsDB, Australia and New Zealand. More recently, the Fund has been consulting with the governments of the region, UNDP and other interested regional and donor agencies regarding a similar initiative for the Caribbean. The IMF will also be organizing high-level policy seminars and a program of applied research into common structural problems in the Caribbean (e.g., the phase-out of Lomé preferences for banana exports).

## **Summary of IMF lending facilities and access policies**

The IMF offers financial assistance to members to help them correct balance of payments problems and to cushion the impact of reform. The IMF's financing is provided through both its general resources and its concessional financing facility, which is administered separately. The extension of IMF credit is subject to Executive Board approval and, in most cases, to the member's commitment to take steps to address the causes of its payments imbalance.

### *Stand-By Arrangements and Extended Arrangements*

The typical stand-by arrangement (SBA) is designed to provide medium-term financial assistance to help countries deal with balance of payments deficits of a temporary or cyclical nature. Under an SBA, a country in consultation with the IMF staff designs and implements a program (which usually lasts for 12-18 months but can be up to three years) that includes macroeconomic policy changes to resolve its external payments problems. To receive financing, the member must comply with this program, including meeting the performance criteria that mark its successful implementation. These criteria, which allow both the member and the IMF to assess progress and may signal the need for further corrective policies, generally cover ceilings on government budget deficits, domestic credit, and external debt, as well as targets for international reserves. Access is normally subject to an annual limit of 100 percent of quota and a cumulative limit of 300 percent of quota. The repayment period is 3¼–5 years.

The IMF provides financial support to its members for longer periods under the Extended Fund Facility. Extended arrangements, which normally run for three years but can be extended for a fourth, are designed to correct external imbalances that stem largely from structural problems and take longer to correct. Access is normally subject to an annual limit of 100 percent of quota and a cumulative limit of 300 percent of quota. The repayment period is 4½ to 10 years.

### *Compensatory Financing Facility*

The purpose of the Compensatory Financing Facility (CFF)—formerly part of the Compensatory and Contingency Financing Facility (CCFF)—is to ensure timely financial assistance to members that are experiencing balance of payments difficulties resulting from a temporary decline in export earnings or rise in cereal import costs, attributable to factors largely beyond their control. If the member has balance of payments difficulties beyond the effects of the shortfall/excess, the member is expected to cooperate with the Fund in an effort to address its balance of payments difficulties. Under the export element, compensation can be given also for a shortfall in receipts from services (excluding investment income), if reliable statistics are available.

Access limits under the CFF for export shortfalls and cereal import excesses are separate from those under the credit tranches and the EFF and are determined by a member's balance of payments position, past cooperation with the Fund to resolve its balance of payments difficulties, and willingness to adopt adjustment policies. Depending on these considerations, access limits can range from 10 percent to 55 percent of quota. The repayment period is 3¼-5 years.

#### *Emergency Assistance Related to Natural Disasters*

The IMF can also provide emergency financial assistance to a member facing balance of payments difficulties caused by a natural disaster and has provided such assistance on a number of occasions. The assistance is available through outright purchases, provided that the member is co-operating with the IMF to find a solution to its payments problems. Access is usually limited to 25 percent of quota but in some cases has been as high as 50 percent of quota. The repayment period is 3¼—5 years.

#### *Poverty Reduction and Growth Facility*

Resources under the Poverty Reduction and Growth Facility (PRGF) are made available to low income countries in the form of highly concessional loans to support medium-term macroeconomic and structural adjustment programs. Such programs are explicitly oriented toward a lasting improvement in the external payments position, stronger economic growth, and a reduction in poverty. The PRGF is the successor to the Enhanced Structural Adjustment Facility (ESAF), the primary differences being the addition of poverty reduction as a goal of the PRGF and the requirement that PRGF-supported programs be derived from country-led, participatory poverty reduction strategies. It is intended that PRGF arrangements should play a catalytic role in mobilizing and co-ordinating resource flows from other multilateral and bilateral sources of finance. Eligibility for PRGF arrangements has been based principally on per capita income and eligibility under the International Development Association (IDA), the concessional lending organization of the World Bank.

PRGF arrangements cover a period of three years. The interest charged on PRGF loans is 0.5 percent. Access under PRGF arrangements is determined according to members' balance of payments needs, the strength of their adjustment programs, their outstanding use of IMF credit, and their record of such use in the past. The maximum access under a three-year arrangement is 140 percent of the member's quota, or, under exceptional circumstances, up to 185 percent of quota. The repayment period is 5½–10 years.

**IMF lending to small states, June 1979—February 2000**

Country	Loan	(in millions of SDRs)		Amount Approved 2/	Amount Drawn
		Approval Date	Expiration Date 1/		
Barbados	SBA	10/1/82	5/31/84	31.9	31.9
	CCFF	10/6/82		12.6	12.6
	SBA	2/7/92	5/31/93	23.9	14.7
	CCFF	2/12/92		22.2	22.2
Belize	CCFF	Jun-93		3.6	3.6
	SBA	12/3/84	6/1/86	7.1	7.1
Cape Verde	SBA	2/20/98	4/19/99	2.5	0.0
Comoros	SAF	6/1/91	6/1/94	3.2	2.3
Cyprus	SBA	7/16/80	7/15/81	8.5	8.5
Djibouti	SBA	4/15/96	3/31/99	8.3	8.3
	PRGF	10/18/99	10/17/02	19.1	2.7
Dominica	EA	12/27/79		1.0	1.0
	CCFF	12/27/79		1.0	1.0
	EFF	2/6/81	2/5/84	8.6	8.6
	CCFF	2/11/81		2.0	2.0
	SBA	7/18/84	7/17/85	1.4	1.0
	SAF	Nov-86	Nov-89	2.8	2.8
Equatorial Guinea	SBA	7/1/80	6/30/81	5.5	5.5
	CCFF	7/3/80		6.4	6.4
	CCFF	4/13/81		4.7	4.7
	SBA	6/28/85	6/27/86	9.2	5.4
	SAF	Dec-88	Dec-91	12.9	9.2
	ESAF	2/3/93	2/2/96	12.9	4.6
Fiji	CCFF	2/8/82		13.5	13.5
	CCFF	1/30/85		4.8	4.8
Gabon	EFF	6/27/80	12/31/82	34.0	0.0
	SBA	12/22/86	12/31/88	98.7	73.1
	SBA	9/15/89	3/14/91	43.0	10.5
	SBA	9/30/91	3/29/93	28.0	4.0
	SBA	3/30/94	3/29/95	38.6	38.6
	CCFF	4/5/94		21.5	21.5
	EFF	11/8/95	3/7/99	110.3	110.3
Gambia	SBA	11/2/79	11/1/80	1.6	1.6
	CCFF	6/8/81		9.0	9.0
	SBA	2/22/82	2/21/83	16.9	16.9
	SBA	4/23/84	4/22/85	12.8	2.6
	SBA	9/17/86	10/16/87	5.1	5.1
	CCFF	9/25/86		4.7	4.7

**IMF Lending to Small States June 1979—February 2000 (cont.)**

Country	Loan	(in millions of SDRs)		Amount Approved 2/	Amount Drawn
		Approval Date	Expiration Date 1/		
	SAF	12/1/86	12/1/89	10.9	8.6
	ESAF	11/23/88	11/5/91	20.5	20.5
	PRGF	6/29/98	6/28/01	20.6	6.9
Grenada	SBA	11/6/79	12/31/80	0.7	0.7
	CCFF	4/1/81		2.1	2.1
	SBA	5/11/81	5/10/82	3.4	2.9
	EFF	8/24/83	1/24/84	13.5	1.1
Guinea-Bissau	SAF	Oct-87	Oct-90	5.3	3.8
	ESAF	1/18/95	7/24/98	10.5	10.5
Guyana	SBA	8/15/78	6/24/79	6.3	6.3
	EFF	6/25/79	6/24/80	62.8	10.0
	CCFF	1/17/80		6.3	6.3
	EFF	7/25/80	7/21/82	150.0	51.7
	CCFF	11/10/82		5.9	5.9
	SBA	7/13/90	12/31/91	49.5	49.5
	ESAF	7/13/90	12/20/93	81.5	81.5
	ESAF	7/20/94	4/17/98	53.8	53.8
	PRGF	7/15/98	7/14/01	53.8	17.9
Mauritius	SBA	10/31/79	9/4/80	73.0	40.0
	SBA	9/5/80	9/4/81	35.0	35.0
	CCFF	4/15/81		40.5	40.5
	SBA	12/21/81	12/20/82	30.0	30.0
	SBA	5/18/83	8/17/84	49.5	49.5
	SBA	3/1/85	8/31/86	49.0	49.0
	CCFF	3/6/85		7.5	7.5
St. Kitts-Nevis	EA	Dec-98		1.6	1.6
St. Lucia	EA	Nov-80		1.8	1.8
	CCFF	4/1/81		2.7	2.7
St. Vincent and the Grenadines	EA	Nov-80		0.4	0.4
	CCFF	3/25/81		1.3	1.3
Samoa	SBA	8/17/79	8/16/80	0.8	0.0
	SBA	6/27/83	6/6/84	3.4	3.4
	CCFF	6/27/83		1.2	1.2
	SBA	7/9/84	7/8/85	3.4	3.4
	CCFF	4/1/91		2.0	2.0
	EA	4/1/91		0.8	0.8
Sao Tome and Principe	SAF	June-89	June-92	2.8	0.8
Solomon Islands	SBA	5/29/81	5/28/82	1.6	0.8
	CCFF	10/28/82		1.6	1.6
	SBA	6/22/83	6/21/84	2.4	1.0

**IMF Lending to Small States June 1979—February 2000 (cont.)**

Country	Loan	(in millions of SDRs)		Amount Approved 2/	Amount Drawn
		Approval Date	Expiration Date 1/		
	EA	Sep-86		1.3	1.3
Swaziland	BSFF	Jan-83		0.9	0.9
	CCFF	6/27/83		9.0	9.0
Trinidad & Tobago	CCFF	11/23/88		85.1	85.1
	SBA	1/13/89	2/28/90	99.0	99.0
	SBA	4/20/90	3/31/91	85.0	85.0

Source: International Monetary Fund, Treasurer's Department.

**Notes:**

BSFF: Buffer Stock Financing Facility

CCFF: Compensatory and Contingency Financing Facility

EA: Emergency Assistance

EFF: Extended Fund Facility

ESAF: Enhanced Structural Adjustment Facility

PRGF: Poverty Reduction and Growth Facility

SAF: Structural Adjustment Facility

SBA: Stand-By Arrangement

1/ In some cases there was an extension of the original expiration date.

2/ Including subsequent augmentations

## The UNCTAD Framework

1. Most small developing States face a risk of increased economic marginalization in the context of trade liberalization and globalization. This risk closely relates to the difficulties that small developing States face in competitive terms, either in existing activities, or vis-à-vis new trading opportunities. For activities pertaining to sectors of goods or services that involve global markets, increasing or only maintaining international competitiveness is generally difficult for small economies because of the intrinsic disadvantages they incur, in particular, the implications of smallness and remoteness (e.g., the lack of skilled human resources and economies of scale; high transport costs). For primary commodities (e.g., bananas) that have been exported by small States under specially favourable terms of preferential market access, preferences are or will be eroded in the new multilateral trade system. Manufacturing activities, in which some small States have specialized with success (e.g., textile products) are also faced with intensifying competition although trading opportunities have expanded. Only in international services (with tourism as the dominant service sector) do many small States maintain a competitive advantage, even though competition has dramatically increased among suppliers.
2. For many small States in general, and small island developing States in particular, economic vulnerability is becoming a more and more complex reality. Globalization forces, beside bringing new trading opportunities, translate into competitive challenges, some of which can be analysed as external shocks that may entail a risk of marginalization from the global economy. Remedies to alleviate the vulnerability of small States to external shocks necessarily involve development policies to reduce competitive disadvantages and facilitate evolutions in the economic structures, toward less severe external dependence and improved economic specialization.

### *Twenty-five years of UNCTAD action in favour of Small Island Developing States*

3. UNCTAD, under two distinct mandates, deals with the 31 *Small Island Developing States* (SIDS)<sup>53</sup> and five *Least Developed* small continental States. Thus, although the notion of *Small States* is not officially dealt with as a distinct category by the United Nations, most of the small States covered by the Task Force fall under special mandates of UNCTAD, and receive considerable attention accordingly.
4. Between 1974 and 1994, UNCTAD was the focal point, in the UN system, for analyzing and monitoring the problems of island developing countries. Since 1994, UNCTAD has had a successor mandate to support the implementation of the Programme of Action for the Sustainable Development of Small Island Developing States, which resulted from the Global Conference on the Sustainable Development of Small Island Developing States (Barbados, April-May 1994). UNCTAD, in its mandated support to this implementation, pursues the following goals to spare SIDS further marginalization from the global economy:

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<sup>53</sup> Antigua and Barbuda, Bahamas, Bahrain, Barbados, Cape Verde, Comoros, Cyprus, Dominica, Fiji, Grenada, Jamaica, Kiribati, Maldives, Malta, Mauritius, Micronesia, Marshall Islands, Nauru, Palau, Papua New Guinea, Samoa, Sao Tomé and Príncipe, Seychelles, Solomon Islands, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Tonga, Tuvalu, Trinidad and Tobago, Vanuatu.

- (a) assisting SIDS in their efforts to circumvent their intrinsic competitive handicaps, which are fundamental causes of the lack of diversification and inadequate specialization of many SIDS economies;
- (b) enhancing the capacity of SIDS to take advantage of new trading opportunities in the context of trade liberalization and globalization, in particular, vis-à-vis relevant niche markets and in the area of international services;
- (c) facilitating recognition, by the international community, of the economic vulnerability of many SIDS to a variety of external shocks, with a view to encouraging the provision of special concessions to SIDS (especially those that are not among the Least Developed Countries) in terms of access to foreign markets and external finance, in order to help these countries to overcome their competitive disadvantages.

***UNCTAD's technical co-operation with small states***

5. UNCTAD's ongoing assistance to SIDS is also relevant to continental small States, in particular, to the five among them that are *Least Developed Countries* (Djibouti, Equatorial Guinea, Gambia, Guinea-Bissau, Lesotho). Direct assistance is provided to individual Least Developed small States in their preparation of Round Table meetings under the Integrated Framework resulting from the 1997 High-Level Meeting on Integrated Initiatives for Least Developed Countries Trade Development. Assistance is also provided to small States in the preparation of project submissions to donors, and in the subsequent implementation of such projects (e.g., Forum Secretariat, Seychelles, St. Lucia). Technical cooperation, in this context, mainly involves subjects relating to trade and investment policies, trade efficiency, and sectoral action relevant to international trade in services.
6. Relevant subjects currently dealt with by UNCTAD, and in which cooperation could be envisaged and organized with the Commonwealth Secretariat, the World Bank, and other international organizations, comprise the following:
  - (i) advisory services to individual countries in their negotiations with WTO on accession, use of the dispute settlement mechanism, trade agreements, new issues and upcoming negotiations;
  - (ii) policy advice, technical assistance and training for institutional strengthening in relation to trade and investment;
  - (iii) analysis of the implications of trade liberalization and globalization, and identification of new trading opportunities for small States;
  - (iv) sensitization to, and advice and training in commodity trading risk management;
  - (v) financial innovations (mobilization of private capital and development of new instruments for mobilizing investment finance);
  - (vi) country-specific vulnerability studies in support of the work of the Committee for Development Policy (CDP) relating to the question of graduation from, or inclusion in the list of Least Developed Countries (see below);

- (vii) research, analysis and support to the development of economic sectors of special interest to small States: tourism, air transport, health services, environmental services, offshore financial services, music industry;
  - (viii) assessment of trade efficiency and competitiveness (e.g., St. Lucia, Vanuatu);
  - (ix) assistance in trade facilitation: modernization of customs (many small States have UNCTAD's Automated System for Customs Data/ASYCUDA), maritime transport, trade information (Global Trade Point Network);
  - (x) investment policy review (e.g., Mauritius);
  - (xi) innovation and technology reviews (e.g., Jamaica);
  - (xii) support to debt management (several small States are among recipient countries).
7. Current examples of small States in which UNCTAD carries out technical cooperation are Djibouti, the Gambia, St. Lucia, Seychelles, and Vanuatu.

***Measuring the economic vulnerability of small States: UNCTAD's role in the work of the United Nations in favour of the Least Developed Countries***

8. The Committee for Development Policy (CDP), in its April 1999 session, recommended the substitution of a composite *Economic Vulnerability Index (EVI)* for the old, composite *Economic Diversification Index (EDI)* among the criteria for determining the list of Least Developed Countries (LDCs). The new *EVI*, with five components (two of which being the instability of agricultural production and the instability of exports of goods and services), is calculated by the United Nations Secretariat (DESA) on the basis of CDP's recommendations.
9. At the same time, CDP called for country-specific "*vulnerability profiles*" of countries near the borderline of graduation from, or inclusion into the list of LDCs, in order to appreciate the relevant characteristics of the countries. Such profiles are specially desirable for the LDCs that are small island developing States and near the borderline of graduation (Vanuatu, Maldives, Samoa, Cape Verde). With the additional information expected from the country-specific profiles, CDP aims at better understanding the complex vulnerability situation of the relevant countries, and making well-founded recommendations regarding their graduation or non-graduation.
10. UNCTAD, which has been associated with the work of CDP on LDC criteria for many years, is carrying out a series of country-specific studies to establish the desired "*vulnerability profiles*". The methodology used to that end is based on the following elements:
- (a) External shocks: natural shocks, economic shocks of non-natural origin, instability in the socio-economic performance
  - (b) Exposure to external shocks: degree of external dependence (openness), degree of economic concentration, changes in economic specialization
  - (c) Intrinsic handicaps explaining vulnerability to external shocks: issues of smallness ("islandness"), and remoteness.

**Relevant events**

14. Issues regarding small States are likely to receive particular attention, in accordance with UNCTAD's mandates on the Least Developed Countries and on Small Island Developing States, during the following two major events: the Tenth Session of the United Nations Conference on Trade and Development (UNCTAD X: Bangkok, February 2000); and the Third United Nations Conference on the Least Developed Countries (Brussels, April 2001).

## **The United Nations Framework**

### *Least developed countries*

1. At the end of the 1960s, it was felt that special supplementary measures were called for to assist countries whose low level of development limited their ability to benefit from international measures adopted in favour of all developing countries. The United Nations grouping of "least developed countries" (LDCs) was established to identify such countries. It has operational significance in that, in addition to the United Nations and its specialized agencies, the World Trade Organization (and previously GATT) (see page 68, para 8) and some bilateral donors use it as a criterion to differentiate among countries in terms of development assistance and trade access.
2. Since 1971, the General Assembly has requested the former Committee for Development Planning (now called the Committee for Development Policy (CDP)) to make recommendations regarding the countries that should be designated LDCs. CDP established a statistical methodology for doing so; this methodology has been refined over the years as more and better data have become available. The present list of LDCs was determined on the basis of GDP per capita, an Augmented Physical Quality of Life index (APQLI) and an Economic Diversification index (EDI). CDP's recommendations are referred to the UN Economic and Social Council which in turn makes a recommendation to the General Assembly. The General Assembly is responsible for the final determination of the list of LDCs. The list is reviewed every three years (the next review is scheduled for 2000), using the most recent data on countries' developmental situations.
3. The current list of LDCs comprises 48 countries. Fourteen of the Commonwealth/World Bank list of 42 small developing countries are LDCs and are therefore eligible for the favourable treatment accorded to LDCs by the international community. These 14 are all the small states on the list that are indicated as having a 1998 per capita income of \$1,500 or less. One small state, Botswana, was graduated from LDC status in 1994 in the light of its developmental progress. Another, Vanuatu, was recommended for graduation in 1997 but this recommendation has not been endorsed by the Economic and Social Council or the General Assembly; a further three small states (Cape Verde, Maldives and Samoa) were identified in 1997 as prospects for graduation in 2000, subject to further consideration at that time.
4. In considering these last four cases, the CDP has been called upon to give greater attention to the "vulnerability" of the countries concerned. Some aspects of economic vulnerability are already captured in the EDI, but CDP recognized that this dimension should be in its criteria for determining a country's inclusion in or graduation from the LDC list. However, CDP concluded that existing vulnerability indices were not suitable for its purpose of LDC identification for reasons of both methodology and data deficiencies.
5. In order to take into account those aspects of vulnerability that affect LDC determination, CDP has formulated an Economic Vulnerability index (EVI) which is intended to capture a country's vulnerability to weather-related and external shocks in a composite index that reflects the size and the extent of exposure to these shocks. The instability of agricultural production and the instability of exports of goods and services were selected as the best universally available measures of the size of these respective shocks. The former captures

the economic impact of climatic and other natural events, while the latter represents external shocks resulting from changes in international prices and demand. The extent of exposure to shocks is represented by the share of manufacturing and modern services in total GDP, export concentration and population size.

6. CDP recognized that the EVI would give only a partial and approximate measure of vulnerability and that other elements should be considered on a country-by-country basis. In order to take these other elements into account in determining the list of LDCs, particularly in considering countries close to the statistical cut-off points, CDP has called for country "vulnerability profiles" to be prepared by UNCTAD (see pages 83 – 84, paras. 9 – 10). These profiles will provide information about country-specific aspects of vulnerability that are not captured by the universally-applied indicators. This combination of qualitative and quantitative information will ensure that vulnerability is taken fully into account in determining a country's LDC status in the 2000 review.

### ***Small Island Developing States (SIDS)***

7. The United Nations Conference on the Sustainable Development of Small Island Developing States (SIDS), held in Barbados in May 1994, adopted the Barbados Programme of Action designed to address the special problems of SIDS and to promote these countries' sustainable development. A special session of the United Nations General Assembly was held on 27-28 September 1999 to undertake a comprehensive assessment and appraisal of the implementation of the Barbados Programme of Action. The special session called for concerted efforts to support the effective implementation of the Barbados Programme of Action, focusing on regional and national strategies and programmes that are country-driven and taking into account the areas identified for priority action, namely, climate change and sea-level rise, natural disasters, fresh water resources, coastal and marine resources, energy and tourism. Since the lack of adequate resources was identified as one of the constraints to the full implementation of the Barbados Programme of Action, the special session reiterated the need for more effective utilization of existing resources and for the mobilization of new and additional resources to support the implementation of the SIDS Programme of Action. Globalization and the critical question of donor coordination were also given considerable attention during the special session.

## **The United Nations Development Programme (UNDP) Framework**

### *Assistance to SIDS*

8. In consonance with its assigned responsibilities for capacity-building in the Barbados Programme of Action, UNDP assistance to the SIDS has included the elaboration of a Small Island Developing States Technical Assistance Programme (SIDSTAP), an assessment of unmet technical cooperation needs and priorities in the SIDS regions, the completion of a Directory of SIDS experts and institutions to facilitate the implementation of the Barbados Programme of Action and training at the ILO Turin Training Centre for SIDS regional training institutions. UNDP support was also instrumental in the launching of a Small Island Developing States Information Network (SIDSNET) to enable SIDS to access and make their information available on the internet and to facilitate exchanges of information between SIDS in areas of sustainable development, focusing initially on three Chapters of the Barbados Programme of Action, namely, coastal and marine resources, energy and sustainable tourism.
9. In the Caribbean SIDS, in addition to the formulation of a compendium of project profiles, UNDP has provided support through its Capacity 21 Fund for the formulation and implementation of national strategies for sustainable development and has provided assistance to strengthen capacities for sustainable development in Barbados, British Virgin Islands, Dominica, Grenada, Jamaica and St. Lucia. In the context of forging partnerships, training of Caribbean officials in environmental technology and management, urban management, telecommunications and building services, information technology management and civil aviation management was provided through a joint initiative between UNDP and the Government of Singapore. Other assistance in the Caribbean SIDS, including activities funded from the Global Environment Facility (GEF), have focused specifically on environmental management, formulation of national biodiversity strategies and action plans, watershed management, forestry development, capacity-building for climate change and sea-level rise, renewable energy development and disaster management.
10. In the Pacific Island countries, assistance provided by UNDP has focused on support for the improved development and management of forest resources, offshore fisheries development, water supply and sanitation, conservation and sustainable use of coral reefs, tourism development planning, disaster preparedness and management, strengthening of national capacity for sustainable development, renewable energy village power systems, as well as national biodiversity strategies and action plans in Fiji, Kiribati, Marshall Islands, Papua New Guinea and Samoa.
11. In collaboration with the African Development Bank, UNDP organized a Ministerial Meeting of Small Island Developing States in the Indian Ocean, Mediterranean Sea and Atlantic Ocean (IMA) which adopted the Mahe Declaration and Programme of Action as a regional strategy for the implementation of the Barbados Programme of Action. The Programmes of assistance supported by UNDP in the IMA include the formulation of national sustainable development plans in Cape Verde and Sao Tome and Principe, reforestation in Mauritius, environmental protection programme in Comoros and National Biodiversity Action Plans in Cape Verde, Madagascar, Mauritius and Seychelles.

12. In consonance with the General Assembly's call for the mobilization of resources to enhance the effective implementation of the Barbados Programme of Action, UNDP and the United Nations Department of Economic and Social Affairs organized a meeting of Prospective Donors and representatives of Small Island Developing States in New York in February 1999. The meeting facilitated consultations on specific project proposals submitted by SIDS and renewed the spirit of partnership between donors and SIDS for the implementation of the Barbados Programme of Action.
  
13. In support of the efforts of SIDS to diversify their production base, enhance their international competitiveness and facilitate their integration into the global economy, UNDP is currently formulating a flagship project focusing on strengthening national capacity in selected SIDS to support the accelerated growth of small and medium size enterprises. With regard to UN system coordination, consultations undertaken with SIDS governments, within the framework of the Resident Coordinator system and the United Nations Development Assistance Framework (UNDAF), ensure that UN system development cooperation is fully integrated into national strategies for sustainable development.

## **The African Development Bank Framework**

1. The Country Strategy Paper (CSP) normally prepared every three years for each AfDB Group regional member country and updated yearly, represents the framework of assistance by the Bank Group for promoting poverty reduction and sustainable economic growth in its regional member countries, small and large. The document is prepared using participatory approach to ensure ownership of development strategy by member countries and the participation of the various stakeholders in strategic development decision and debate. The allocation of AfDB Group resources in support of member countries development agenda is based on country performance, which is assessed annually.
2. For the African island countries, the Mahe declaration and program of action, which emanated from the African Island Countries Ministerial Meeting held in Seychelles in July 1998, represent a major step by the AfDB Group to articulate a special initiative for sustainable development of, and poverty reduction in, these countries given their special vulnerability as small island states. The Mahe Program of action for the African Small Islands Developing Countries is being operationalised within the context of the country strategy paper for each country. The Mahe program of action puts a great deal of emphasis on regional co-operation among the small islands countries and the need for their effective integration into the African continental and global economy.
3. In furtherance of its regional integration promotion mandate, the AfDB Group is in the process of putting in place a regional integration policy to facilitate economic co-operation and regional integration including the financing of multinational projects and programs.

## **The Asian Development Bank Framework**

1. The charter of the ADB (Bank) calls for the Bank to give special attention to the needs of smaller or less developed countries. “Small states” members of the Bank include eleven of the twelve Pacific Developing Member Countries (PDMCs)<sup>54</sup>, which are soon to be joined by East Timor, as well as Bhutan and the Maldives.
2. Small states are entitled to assistance from the Bank prepared in accordance with the Bank’s annual cycle of country programming and cycle of project preparation. The Bank engages in a wide range of social and economic development activities aimed at improving the welfare of the people of the region. Its over-arching strategic objective is to reduce poverty. In all its work, the Bank seeks to encourage the private sector, strengthen public sector management capacity, develop human resources, and help manage natural resources sustainably.
3. To promote investment of public and private capital for development purposes, the Bank makes loans and equity investments. It offers a range of lending modalities. Most Bank loans are to the public sector and are for specific projects, but the Bank also makes loans to the private sector for specific projects and to governments for program purposes. The Bank also provides technical assistance for the preparation and execution of development projects and programs, and for advisory purposes. It pays special attention to the needs of smaller or less-developed countries, and gives priority to projects and programs that contribute to the harmonious economic growth of the region as well as a whole and that promote regional cooperation.
4. Bank policies and procedure are continuously being updated in an effort to better serve member countries. Relevant current reviews include the drafting of new policies with respect to the operations of Resident Missions, Performance-Based lending, and the preparation of a new regional strategy for the PDMCs.

### ***Resident missions***

5. The Bank is reviewing the need for a stronger presence in developing member countries, increasing the number, strength, and responsibilities of Resident Missions. This is likely to lead to a greater Bank presence in borrowing-member countries consistent with what is practical.

### ***Performance-based lending***

6. The Bank is reviewing means to adopting a performance-based allocation of ADF resources. Although performance-based lending has been endorsed in principle the means to adopting this approach has not yet been approved.
7. A factor that has a bearing on a country’s need for development assistance is population size. At one level this is straightforward: the larger the population, the higher the total allocation. However, small countries merit special attention. The underlying rationale is

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<sup>54</sup> The PDMCs are: Cook Islands, Fiji, Kiribati, Marshall Islands, Federated States of Micronesia, Nauru, PNG, Samoa, Solomon Island, Tonga, Tuvalu, Vanuatu.

that many of them, especially the PDMCs, suffer from structural vulnerability to shocks. The sources of vulnerability include high exposure to external economic forces, remoteness, and proneness to natural disasters.<sup>55</sup> Here, the smaller the population, the larger the allocation on a per capita basis. This is in consonance with the Bank's Charter mandate. There is also the consideration that for very small countries, an allocation below a certain amount ceases to be operationally meaningful i.e. projects/programs must be of some minimum size to have a development impact.

8. Second, country size matters. The formula should ensure that the larger the population, the larger the allocation on an absolute basis and the smaller the allocation on a per capita basis. However, large allocations to big countries may crowd-out small countries. In the Bank's context, three DMCs account for 82 percent of the total population with ADF access. Hence, there is a need to moderate the effect of population in the allocation formula. The formula must build in what is referred to as the small country bias.
9. Third, the formula must respond to needs. The poorer the country, the larger the resources that ought to be made available, other factors being the same. This calls for an inverse relationship between allocation and per capita GNP (GNPC). Excluding the PDMCs that have relatively high per capita incomes, there is a wide range of per capita incomes among ADF recipient countries. Per capita GNPC levels range from \$210 (Nepal) to \$ 1180 (Maldives).<sup>56</sup> Hence, overemphasis on per capita GNPC can distort the allocation of resources among ADF recipients. While the formula must indeed retain the poor country bias, it needs to be carefully calibrated.
10. A project or program has to have a certain minimum size to have any development impact. Application of the allocation formula to the PDMCs along with the other larger DMCs can result in allocations to the PDMCs as a group and individually that are too small to be operationally meaningful. It is, therefore, proposed that PDMCs be treated as a distinct category. A specific amount, could be set apart for this category, and the formula, or a variant thereof, applied to obtain relative shares of countries. Further, efforts will be made to adapt and/or develop indicators of structural vulnerability as determinants of allocation for small countries.

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<sup>55</sup> Of relevance in this regard is ongoing work by the World Bank and the Commonwealth Secretariat on developing measures of structural vulnerability of the type faced by small states.

<sup>56</sup> ADB's policy on ADF eligibility takes into account not only per capita GNP but also debt repayment capacity in determining which countries should have access to ADF resources. The DMCs that currently are ADF-eligible and have ADF access are identified in R204-98. A Graduation Policy for the Bank's DMCs, 4 November.

### ***Regional Strategy for the PDMCs***

11. The Bank plays a lead role in providing advice and assistance to many of the small states that are its members. For instance, in the 1990s the Bank has played an important role in economic and public sector reform in the PDMCs.
12. The Bank is currently updating its regional strategy for the Pacific<sup>57</sup>. An Initiating Paper for the new strategy has been prepared and this is now subject to internal discussion.
13. The paper proposes that across all Pacific DMCs, the cornerstone of the strategy will continue to be support for economic reform in the areas of economic policy, public sector management, and governance. In this regard and given the large need for capacity building, the technical assistance function will continue to have greater importance than resource transfer in the Bank's assistance mix.
14. In line with the Bank's adoption of poverty alleviation as its overarching objective, a larger proportion of Bank resources and assistance is proposed to be shifted to the Melanesian countries (Papua, New Guinea, Solomon Islands, Vanuatu) and East Timor where both poverty and population in the Pacific are concentrated. The thrust of poverty alleviation assistance will be on expanding access in rural areas (and by women and children) to basic health and education, including non-formal education. This assistance could also include support for transport infrastructure (to improve access to disadvantaged regions) and for capacity building of local governments. Bank assistance will also seek to reduce high population growth rates in these countries.
15. In the small, isolated, and vulnerable atoll economies (Republic of Marshall Islands, Nauru, Tuvalu, Kiribati), a special concern is the sustainable financing of essential services. Accordingly, the Bank will seek to establish and expand trust funds, in collaboration with other donors, to finance recurrent expenditures. Given the limited scope for growth in these economies, as appropriate, the Bank will explore opportunities for marine resource development, niche-market tourism support, and skills development for labor export.
16. In the other countries (Fiji, Samoa, Federated States of Micronesia, Tonga, Cook Islands) with relatively good growth prospects, a broader natural resource base, and generally skilled human resources, the Bank will focus on private sector development and physical infrastructure to promote economic growth (including support for tourism-related infrastructure).

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<sup>57</sup> Pacific Studies Series. Strategy for the Pacific. Policies and Programs for Sustainable Growth. ADB March 1996.

## **The Inter-American Development Bank Framework**

1. On the basis of the 1.5 million-population criterion for determining small states, which the World Bank-Commonwealth Secretariat Task Force has adopted, the IDB members that qualify as small states are The Bahamas, Barbados, Belize, Guyana, Suriname and Trinidad and Tobago. This is a diverse group of small states, with per capita income varying from US\$748 to US\$11,092 in 1996. The Task Force Interim Report notes that use of the 1.5 million population threshold is a “convenient yardstick” and that a number of larger countries (e.g., Jamaica) share many of the same characteristics of smallness. For this reason, and given the realities of IDB membership, the Bank would wish to approach the issue of small state definition with flexibility.
2. The IDB has historically been sensitive to the issue of size in dealing with its borrowing members. This sensitivity is manifested in a classification system whereby small states are grouped as ‘C’ or ‘D’ countries and accorded treatment that recognizes their peculiar circumstances. In addition to per capita income, the IDB classification employs criteria that take account of, among other things, the dimension of size in determining economic status. These include (i) potential for development (e.g., size, resource endowment), (ii) degree of vulnerability (e.g., due to openness and trade concentration), and (iii) dependence on external savings.
3. In recent years, however, an increasing reliance on the per capita income criterion in determining access to concessional resources has eroded the historic framework for applying special treatment to small states. In addition, the practice of focussing on the development status of a country in determining lending and technical cooperation activities has recently given way to an emphasis on the nature of the operation to be financed, with particular attention being paid to priority areas identified in the lending guidelines of the Eighth Replenishment, i.e., (i) poverty reduction and social equity, (ii) modernization and integration, and (iii) the environment.
4. The issue of graduation is of considerable relevance to the small states of the Caribbean Region where a case can be made for using vulnerability criteria in determining access to concessional resources. The IDB has never entertained the notion of graduation from access to its ordinary capital resources but some Caribbean states have been graduated from the declining availability of concessional resources. It should also be observed that some non-member Caribbean countries of the OECS (essentially the IDA-eligible countries) enjoy access to FSO and non-reimbursable TC (grant funds) of the Bank through its on-lending arrangements with the CDB.
5. Notwithstanding the modifications to the framework outlined above, the IDB is responding to the special challenges facing small states in a number of ways. Firstly, the IDB has supported regional integration, which contributes to overcoming the limitations of small size. Secondly, the IDB is supporting the dialogue about strategies and approaches to promote development in the Caribbean Region. Thirdly, the IDB is supporting disaster mitigation efforts, which is recognized as an important area of vulnerability for small states, especially in the wake of several severe hurricane and other natural disasters in the region in recent years. Fourthly, the IDB maintains strong programs of assistance to its small member states on an individual basis.

### ***Regional Integration Support***

6. It is well recognized that regional integration and cooperation among small states can act as an important vehicle for overcoming vulnerability, weak institutional capacity, high infrastructural costs and limited access to external capital. Unique among multilateral development institutions, the IDB has a specific mandate to support regional integration, and has throughout its 40 years of existence financed a large number of integration projects among its member states, including the small Caribbean states.
7. IDB support for regional integration in the Caribbean can be divided into three categories: support for the strengthening of economic integration, support for enhancing the negotiating capacity of Caribbean countries in meeting their regional and global obligations, direct assistance to support functional cooperation among small states in areas such as education, health and the justice sector.

### ***Strengthening of economic integration***

8. The Bank is supporting work toward the establishment of a single market economy within the Caribbean Community (CARICOM) as well as efforts to improve and modernize the common market instruments (particularly the functioning of the common external tariff and rules of origin system). In addition, particular attention has been paid to the development of harmonization and mobility in Caribbean capital markets. In this regard, the Bank is supporting the harmonization of capital markets and Caribbean stock exchanges and capital market development in the Eastern Caribbean. A project for the upgrading and harmonization of investment legislation and business establishment procedures throughout the Caribbean Community is also under consideration.

### ***Support for negotiating capacity***

9. It is recognized that, given their high degree of openness, the small countries of the Caribbean have a high stake in on-going international negotiations which condition the changing international trade and economic environment faced by these countries. The sub-region therefore has a vital need for assistance in pooling its limited resources and expertise in order to achieve adequate negotiating capacity and participate effectively in these discussions. In this connection, the IDB is supporting the operations of the Caribbean Regional Negotiating Machinery, which has been set up to help Caribbean countries participate effectively in international trade negotiations such as the FTAA, LOME and the WTO. A project funding regional activities to facilitate the implementation of WTO commitments by Caribbean countries is in the final stages of preparation.
10. As a member of the IDB-OAS-ECLAC Tripartite Committee, the Bank has actively supported the participation of its member countries in the Free Trade Area of the Americas (FTAA), among other things, providing financial and technical assistance to the FTAA Working Groups in the pre-negotiation phase (1995-1998). One example of such support is that given to the Smaller Economies Working Group in the preparation of discussion papers and background documents. Within the tripartite framework, the Bank has also supported the FTAA Administrative Secretariat and several of the FTAA Negotiating and Consultative Groups in the current negotiation phase, including the

Consultative Group on Smaller Economies, whose mandate includes monitoring and commenting on issues of concern to smaller economies in the negotiations.

### ***Support of functional cooperation***

11. The Bank provides assistance on a regional basis in a diverse range of activities which include (i) the expansion and re-equipping of the University of the West Indies, (ii) the work of the West Indian Commission leading to the preparation of its report entitled, Time for Action in 1992, (iii) training in a variety of areas including labor relations, (iv) environmental conservation and protection, (v) the development of policy and project frameworks for the administration of justice and the prevention of domestic violence, and (vi) the establishment of a regional credentialing system for the hospitality and tourism industry.

### ***Development Dialogue Support***

12. The IDB supports the ongoing dialogue about appropriate approaches and development strategies for its small member countries. In this regard, the IDB is an active participant in the CGCED and is taking the lead in preparing a paper on capacity building issues, with a focus on the justice system, for the 2000 CGCED. The IDB is also supporting the search for strategies to enable the small countries of the Caribbean to make an effective transition in the context of globalization. In particular, the IDB is considering proposals for the formation of an IDB-CDB Task Force charged with assessing and supporting the process of transition for Caribbean countries in the face of globalization challenges.

### ***Disaster Mitigation Support***

13. The Interim Report has identified vulnerability to natural disasters as a major Achilles' heel of small states and this issue has been a prominent concern in recent years as a result of major disasters in the Caribbean. The IDB itself has responded to this challenge by strengthening its attention to disaster mitigation efforts. This issue will be the focus of much attention at the next Annual General Meeting of the Bank which in March 2000, where Caribbean and Central American countries will have an opportunity to voice their concerns and contribute to a search for more effective preparedness and mitigation of the effects of natural disasters.

### ***Country Assistance***

14. The IDB maintains strong programs of assistance to its small member countries, making available the full array of its expertise and resources which are tailored to their particular needs. Its assistance is built on the foundation of a country strategy dialogue aimed at determining the appropriate development approaches and program designs. Its lending programs focus upon social, economic and environmental infrastructure (e.g., education, health, transport, water and sanitation) which is critical to the development of these countries. The loan programs are supported by technical cooperation programs, including grant assistance provided through the Multilateral Investment Fund, which is a special vehicle established to support private sector activity. Technical cooperation and assistance of this kind is particularly important in small states where it helps to address the problem of limited institutional and absorptive capacity.

**PART III. COMMENTS MADE ON THE WORK AND CONCLUSIONS OF THE TASK  
FORCE AT THE APRIL 2000 MEETING OF THE DEVELOPMENT COMMITTEE<sup>58</sup>**

From the summary statement by H.E. Tarrin Nimmanahaeminda  
Chairman of the Development Committee  
and Minister of Finance, Thailand

The report was welcomed. Most ministers agreed small states did have special characteristics, but also agreed with the report that a new country category should not be created. Many ministers urged the Bank and others to follow up on the report's recommendations with firm actions, with some concern that such steps not harm the interests of other countries. Technical assistance and capacity building were considered particularly important forms of Bank support. Small states were encouraged to open up to international trade, in their own interest, but the need for more time to adjust was noted by several ministers. Support was expressed for "novel regional integration modalities" to mitigate difficulties caused by globalization.

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<sup>58</sup> Joint Ministerial Committee of the Boards of Governors of the Bank and the Fund on the Transfer of Real Resources to Developing Countries, meeting in Washington, D.C., on April 17, 2000. List of members and their constituencies is set out starting on page 109 below.

His Excellency Hamad Al-Sayari, Governor, Saudi Arabian Monetary Agency, Saudi Arabia

It is timely and appropriate that the agenda for this meeting of the Development Committee focuses on trade as an engine of growth and poverty reduction, and on the Heavily Indebted Poor Countries and small states, which are most vulnerable to external shocks and epidemics.

N'Golo Coulibaly, Minister of Economy and Finance, Côte d'Ivoire

We welcome the Joint World Bank/Commonwealth Initiative on Small States. We congratulate the Joint Task Force for having produced an excellent report analyzing the specific problems facing small states in their efforts to meet the new challenges of globalization. This document also provides an ideal vehicle for describing the activities of small states and the assistance of the international community. We also appreciate the fact that the Task Force held many consultations with the small states themselves in the course of drawing up this report.

The recommendations of the Task Force are relevant and could form the nucleus of the policies to be adopted to help bring these states out of their isolation, either through regional integration policies or new approaches in cooperation with bilateral and multilateral development institutions. We support the recommendations to mitigate the destabilizing impact on revenue and the vulnerability of these countries to natural disasters. In addition, we give our support to the proposals to ensure a calm transition to a new world trading system, and to strengthen human and institutional capacity.

Nitin Desai, Under-Secretary-General, Department of Economics and Social Affairs, United Nations

The United Nations has always recognized – and endeavoured to respond to – the diverse nature and needs of Member States. We therefore support the proposition, expressed in the Report of the Joint Task Force on Small States, that in-depth analysis of the structural and conjunctural features of small states should be continued with a view to identifying their particular problems and formulating effective solutions. These should include examining the adequacy of different types of international assistance.

For its part, the United Nations Committee for Development Policy - an independent international expert body - has recognized that economic vulnerability should be taken into account in its review of the countries to be classified as Least Developed. In the General Assembly, it has been agreed that the needs of selected groups of countries, including both the Least Developed Countries and Small Island Developing States, should be given special attention in the high-level event on financing for development.

## Nicolas Eyzaguirre, Minister of Finance, Chile

Although we do not consider adequate the enactment of a new and special category of countries only on the basis of their size, it is necessary to analyze them within the context of their particular characteristics. The global economy may impose heavy adjustment costs on some small states and compel them to assume higher risks. Their economic exposure, remoteness and insulation, their proneness to natural disasters, inadequate institutional capacity and lack of export diversification leave small states unprotected in face of external shocks. However, although globalization may entail a higher degree of volatility, it is important to remember the countless opportunities it creates for raising average national income.

The Commonwealth has long recognized ways, in numerous instances, to incorporate exposure in the design of development strategies for small states. The World Bank has pledged to further help small states that have difficulty mastering the complexities of market access and external imbalances. The joint Commonwealth Secretariat/World Bank Task Force advances a suitable contextual framework to deal with threats from external shocks.

The framework also provides for the use of quantifiable indicators—like the Commonwealth's composite index of vulnerability—to measure progress toward assistance goals. Although the index encapsulates the key causes of vulnerability, the Bank cannot apply it in isolation to determine whether a small state is eligible for differential treatment. In our opinion, assistance should be judged on a much larger perspective than that merely provided by an index in isolation.

The Bank's Country Assistance Strategies (CAS) made in full consultation with the small states should be the vehicle to address their particular features. It should establish the main determinants of their vulnerabilities and propose remedies tailored to each individual country. This instrument should establish clear policies, expected results and outcome benchmarks. It should also include strategic areas selected for Bank-supported investment. Technical assistance—by far the most powerful device for the Bank to assist small states—should be given high priority. In this vein, we encourage the use of market-based instruments, such as derivatives, and the creation of stabilization funds to smooth-out volatility in commodity prices and income.

Concomitant to the discussion on trade and poverty reduction at the Development Committee, we are raising the issue that trade liberalization is central for poverty reduction. Liberalization will not necessarily reduce volatility and, in some instances, it may actually increase it. But not accepting it may lead to further stagnation and poverty. On the other hand, taking it up will provide the mechanisms and resources for reducing the impact of volatility. Small states should have an open attitude towards eliminating agricultural subsidies and reducing tariffs and non-tariff barriers to international trade in goods and services. In this context, we would like the CAS to include a much closer partnership with the World Trade Organization to help integrate small states into a rules-based trading system, and to develop their institutional capacity to participate in trade negotiations.

It should also be considered that the ecosystems of small island states are fragile. We believe that there is a place for the International Task Force on Commodity Risk Management

working on the insurance market to cover natural disasters and fluctuation in the prices of commodities and volumes traded. Recent experience at the Bank shows that adaptable program loans and learning and innovation loans are flexible enough to accommodate support to mitigate the effects of natural disasters.

Laurent Fabius, Minister of the Economy, Finance and Industry, France

Development is an on-going process, we have nothing to gain by creating artificial separations. In this regard, France does not share the analysis, which would group countries according the theoretical categories--for example "small states".

Jorge Giordani, Minister of Planning and Development, Bolivarian Republic of Venezuela

We are grateful to management for commissioning this carefully balanced report. We are convinced not only that the cooperative relationship which already exists between the World Bank and other organizations should be encouraged and deepened in the immediate future, but also that such cooperation should be broadened to include additional multilateral organizations. At a time when financial restrictions are severe and widespread, renewed emphasis on inclusive and concerted institutional action is clearly both justifiable and appropriate.

We endorse the general recommendation that a special category of small states should not be created. Nevertheless, the report is of particular interest to the members of this constituency, primarily because many of the countries it discusses are our immediate neighbors and share similar problems. Unfortunately, the intensity and consistency of our relations has generally not reflected our geographical proximity. Often, past history and bilateral trade agreements these countries have negotiated with their former colonial powers during their recent decolonization process have posed an obstacle to our relations with them. We are convinced that the strengthening of novel, albeit still emerging, modalities for regional integration will – by expanding trade and interregional cooperation – mitigate some of the difficulties associated with the globalization process, and compensate in no small measure for the specific problems – and in some cases relative problems such as geographical distance from their primary markets – facing these countries.

Eveline Herfkens, Minister for Development Cooperation, The Netherlands

The added value of the report of the Task Force on Small States is the identification of shared problems of small states and their possible solutions. The main problem is the economic vulnerability of small states. New and existing initiatives to limit this vulnerability deserve our full attention.

Nevertheless, a standard solution does not do justice to the individual problems and uniqueness of small states nor does it recognise that the problems faced by 'small' states are also relevant - sometimes even more so - to other countries. Therefore we prefer the current

tailor made approach which applies to all borrowing members to the creation of a separate country category for small states.

We furthermore note with some regret that according to the report of the Task Force the small states in my constituency are either slightly too rich or slightly too populous to be counted as small, and therefore deserving of special attention. It raises the question of how criteria for small states were arrived at.

**Victor Khristenko, Deputy Chairman of the Government, Russian Federation**

In the era of globalization, development problems peculiar to small states deserve special attention. In our view, analysis and conclusions of the report are quite important and helpful. We support the combination of relevant actions set out in this document for both small states themselves and the international community. We are pleased to note that the recommendations of the report are consistent with the views expressed by the representatives of small states from all regions in the course of an extensive consultation process.

It should be recognized that many small states are extremely vulnerable due to the unfavorable combination of such factors as a small domestic market, relatively undiversified production and exports, a high dependence on distant foreign markets, susceptibility to natural disasters and environmental change, weaknesses in both public and private sector capacity, relatively higher poverty level and more uneven income distribution.

These issues should be carefully taken into account in determining special treatment of small states in the areas of trade liberalization, control of international financial flows and regulation of related financial services, development assistance and aid eligibility. At the same time, favorable treatment of small states must not be in conflict with the interests of larger developing and transitional countries. For instance, the provision of financial services by some small states is an area where the correct balance of interests needs to be found so that the prevention of international financial and tax crime is insured.

The World Bank as a major partner of small states has a very important role to play in helping them meet challenges of globalization. On the one hand, most of the small developing countries are World Bank members and borrowers. On the other hand, the Bank has a number of comparative advantages of great value to small states. In view of this, we would like to encourage the World Bank's pursuit of small states agenda, including the promotion of better donor coordination, support for regional initiatives in the public and private sectors, lending for disaster-proof and disaster mitigation projects, and the buildup and dissemination of knowledge of special interest for small states.

**Senator The Hon. Rod Kemp, Assistant Treasurer, Australia**

As the representative of seven small Pacific island states, with populations ranging from 20,000 to 400,000, I strongly endorse the joint World Bank/Commonwealth Secretariat taskforce report on the challenges facing small states.

The adoption and implementation of sound domestic economic and social policies lie at the heart of the development of small states. Nevertheless, as the report states, most small states face problems that are inherent in their small size and make them particularly vulnerable. Small size, limited domestic markets and narrow resource bases require an extraordinarily high dependence on trade – the small states covered in the report have an average trade to GDP ratio well over 100 per cent – and limited scope for diversification. As a result, they are highly exposed to changes in their export markets and in their terms of trade, while financial markets view them as riskier than larger states for investment. These problems are compounded by remoteness and insularity (a particularly acute problem for the Pacific Island economies), which bring high transport and other costs, and limited institutional capacity in both the public and private sectors. The small size also constrains their capacity to respond to natural disasters, to which many of them are more than usually prone, while some small island states stand to suffer disproportionately from environmental and climate change shocks.

Enhanced trade liberalisation will, when accompanied with appropriate domestic policies, benefit both small and large states. The report does highlight, though, the particular difficulties small states face in adjusting to changes in the global trading regime. These range from difficulties in finding alternative revenue sources through to a lack of capacity to effectively utilise dispute resolution processes.

It is, therefore, entirely appropriate that the special circumstances of small states be taken into account in the policies and programs of the multilateral trade, finance and development organisations. For the Bank, this should entail a continuation of a flexible approach to the graduation of small states from concessional financing. I also support the report's recommendation that the Bank undertake a substantive forward work program focussed on particular impediments to the development of small states.

The Bank does have a special and valuable contribution to make in the development of small states. This is illustrated well in its strategy for the Pacific. Given the roles being played by bilateral donors and other multilateral organisations, the Bank is not, nor will it seek to become, the major player in the region. But the Bank can engage governments on broader structural and sectoral reform dialogue which other donors are either unwilling or unable to undertake. This reform dialogue is likely to be most effective when supported by strategic lending operations and non-lending services. Further, in its engagement with the countries in the Pacific, the Bank can bring to bear its experience and knowledge of small states development from other parts of the world, particularly the Caribbean and Africa. I am therefore very supportive of the Bank's evolving strategy in the Pacific and see it as critical for the development of the small states in the region. In this context, I also welcome the decentralisation of the Pacific country management unit to Sydney which should significantly improve its effectiveness.

**Mr. Jin Liqun, Vice Minister of Finance, People's Republic of China**

Due to the geographic locations and historical reasons, many small states face peculiar difficulties in their economic development. More often, the international community has not paid adequate attention to their legitimate interests and reasonable requirements in the process

of globalization. In this regard, we call for more official aid to those small states to help accelerate their development drive and improve their links to international markets. In assisting them, the international community should promote a better coordination among donors in order to minimize the extra cost and burden the small states are forced to bear in meeting different requirements and procedures from different donors.

We welcome the joint study of the World Bank/Commonwealth Secretariat Task Force on the challenges facing small states in the global economy, and we support the application of flexible IDA graduation policy on small states. It is very encouraging to see that the Bank has recommended to adopt the different development policies in the context of each country's different reality. Such a flexible and realistic approach will surely make the development assistance more pragmatic and effective.

**Pedro Malan, Minister of Finance, Brazil**

Small States are particularly vulnerable and deserve special attention by the international community. We support the recommendations contained in the Report "Small States: Meeting Challenges in the Global Economy" and urge the Bank to mainstream those findings in activities related to those countries, including in sector, thematic and policy work.

**The Honorable Kelebone Albert Maope, Deputy Prime Minister and Minister of Finance, Lesotho**

We welcome the Joint Commonwealth Secretariat/World Bank report on this subject. It succinctly provides a candid analysis of the problems faced by small states, giving full consideration to the specific characteristics of each. This group of countries shares a number of common characteristics: they are prone to natural disasters; a great number of them are remote and isolated from major markets and are, therefore, less diversified; they have limited capacities, high incidence of poverty and limited access to international financial markets, among other things. Therefore, the recommendations of the International Task Force for addressing these difficulties are apt. The vulnerability of these states to external shocks should be taken fully into consideration in the design of multilateral and bilateral assistance. Given the lack of interest by foreign investors in these states, more reliance on concessional assistance seems inevitable. It is also important that the International Task Force on Commodity Price Risk Management gives special attention to the specific needs of these countries.

Donors, particularly multinationals, should also provide assistance that enables them to safeguard against environmental vulnerability, a phenomenon most of them often experience. The international community also has to help by removing all trade barriers that confront the exports of these countries into their markets, preferably through extensive special preferential treatment, and compensatory financing, particularly during the transitional period until they become fully integrated in the global trade regime. This should also be complimented by adequate technical assistance, particularly from the WTO, UNCTAD, EU, and the Bretton Woods institutions to develop their negotiating capacities. Financial services, both on-shore and off-shore, is an area where several small states have a comparative advantage and where external assistance is of crucial importance.

An important aspect of the proposed framework of assisting these countries is the clear delineation of the division of labor among the different development partners. While this is well spelled out in the last section of the report, we hope that the respective states will be the ones in the driver's seat when it comes to the coordination of donors' assistance.

Finally, putting the Task Force's agenda in action would entail the concerted efforts of all if the objective of integrating these states into the global economy is to be attained.

The Honourable Paul Martin, Minister of Finance, Canada

We would like to highlight the special challenges facing the world's smallest developing states. Adjustment to the evolving global trading system for the small states, many of which are in the Caribbean, is proving very difficult. These countries face enormous capacity-building challenges and without support they risk being left behind in the increasingly global economy. Their scarce resource endowments, including limited human capital and stretched institutional capacity, underlie the challenges these countries face in trying to restructure their economies and diversify their production and export structures to benefit from the global trading system. We also need to appreciate the special difficulties they face as they seek to make the transition from a concessions-based to a rules-based global trading regime.

In this regard, I would like to quote the striking and eloquent words of the Governor from Barbados, Prime Minister Owen Arthur:

*It is however important that the two crucial, qualitative aspects of the process of Caribbean reconstruction be constantly held up so that both the urgency and the scale of what now has to be undertaken in the next decade can be fully appreciated.*

*The first is to properly appreciate the time dimension of the adjustment. The advanced, industrialised countries have over the course of the past fifty years, through an effort spread across 8 rounds of multilateral trade negotiations gradually but efficiently and effectively made the adjustments to their fiscal systems and their real economy to prepare themselves to participate fully in the present phase of globalisation which is driven in such large measures by the liberalisation of trade, financial and technological flows globally....These economies face today's intensely competitive international environment having benefited from a gradual and carefully managed phased process of liberalisation extending over half a century....*

*The Caribbean will be expected to successfully carry out over a period of ten years a process of liberalisation which has taken the advanced economies over fifty years to master. It will be expected to do so with a relatively weaker resource endowment, faced with fewer options, and hence confronting the spectre of doing severe damage to its fiscal system, its real economy and indigenous business by compressing necessary change into too short a period of time....*

*The second qualitative aspect of the economic challenge which faces the region is the sheer magnitude and scope of what has now to be undertaken in a very short*

*period with very limited resources to correct longstanding social and economic deficiencies to accommodate the competitive pressures arising from globalisation.*

The multilateral trading environment has been with the industrialized states for some time. Developed nations have indeed had the luxury of time to both build the system from the ground up, on our terms, and to facilitate adjustment in our economies. It is both unrealistic and short-sighted to assume that the small states can adjust to this new reality overnight.

In small states, the transition to an open, competitive trading regime will require the development of a level of production flexibility, innovation and marketing capacity that will be new for many of them, and this is likely to prove to be an enormously challenging process. The adjustment is likely to take some time, and will require strong domestic political commitment and domestic effort in addition to significant external support from both multilateral and bilateral partners.

I would like to take this opportunity to thank both the Bank and the Commonwealth Secretariat for their efforts over the last 18 months in producing the special study that focused on the challenges and vulnerabilities of small states. This is an important report. The drafting process was enormously instructive and informative. We not only deepened our understanding of the small states, but also learned more about how institutions and developed countries behave towards them. It is now time to move forward with an appropriate work program to further development and poverty reduction efforts in the small states.

We are grateful to the Commonwealth Secretariat and World Bank Task Force for their role in catalyzing a very valuable policy discussion among the small states. Indeed, this has set a process in motion that will better equip small states for their external discussions and negotiations as well as offered a valuable opportunity to strengthen the inter-regional network and dialogue. It has resulted in a heightened recognition within small states of the critical importance of implementing the right mix of policies and of staying the course through adverse circumstances, and of the pressing need for own-account action and self-reliance.

Most importantly, however, this process has incorporated a range of international institutions and external actors. We now look to the Bank and other international institutions to systematically review and amend where necessary their own approaches to the small states and to ensure that all general policy work addresses as appropriate the special circumstance of the small states, both at the analytical and policy prescription stages.

It is my hope that the work of the Task Force marks the launch of a strong and sustained multilateral effort to recognize, understand and respond to the circumstances and challenges facing the small states. It is critical that the momentum built so far is maintained and compels us all to act on the recommendations of the report.

It is also appropriate that I use this opportunity to recognize and express my appreciation for the contributions of Prime Minister Arthur and President Wolfensohn to the small states process. In particular, Prime Minister Arthur led the Commonwealth delegation that met with President Wolfensohn to establish the Task Force; he has nurtured the process through two international conferences and several working drafts; and has shown great leadership across the Caribbean, our constituency more broadly defined and within small states worldwide.

**Fathallah Oualalou, Minister of Economy and Finance, Morocco**

Although small States do not comprise a homogeneous category, and although the size of a country's population definitely does not predetermine its economic situation, most of these countries display certain vulnerabilities which should be taken into account.

The least developed small States are single-commodity exporters or their economies are not very diversified, and their institutional and human resource capacities are limited.

Accordingly, it behooves the international community to devote particular attention to these countries and to countries facing similar constraints by supporting their integration at the regional and international levels and promoting capacity building.

The international community as a whole must confront these challenges in a spirit of solidarity not purely as a matter of necessity, but as a moral obligation, for if it does not do so, many countries risk sliding into marginality and poverty.

**His Excellency Abdulla Hassan Saif, Minister of Finance and National Economy,  
Bahrain**

On a more specific area that needs more attention by the international community is the special case of the small states that is on our agenda for today. Experience has shown that although small states have common problems with many other developing countries, they do have peculiar features that intensify their vulnerability and require particular attention by donors and international institutions. This is clearly shown in the analysis submitted to us and we commend the work of the Commonwealth Secretariat/World Bank Task Force for bringing this issue to the fore. We note that the small states are heterogeneous in several respects, including their resources and capacity to cope, but we also note that thirty of them are borrowing countries.

We endorse the Task Force's conclusion that addressing the special challenges facing the small states requires a combination of actions involving domestic policy action and some new approaches by bilateral donors and international institutions. There is a large number of specific measures covered in the report of the Task Force and they should be considered in tackling the issues faced by individual small states.

**Mt. Ousmane Seck, Vice-President (Operations), Islamic Development Bank**

The IsDB welcomes the Report of the Commonwealth Secretariat / World Bank Joint Task Force on Small States. In our view, findings and recommendations of the Report are going to benefit particularly four of the IsDB member countries, namely Comoros, Djibouti, Maldives, and Suriname. The IsDB has already recognized the special needs of Small States among its member countries and provided financial assistance on highly concessional terms. Accordingly, of the total financing extended to the said member countries amounting to US\$

87.4 million till April 1999, around 60 per cent was either loan carrying a nominal administrative fee or outright grants.

In term of further steps in this area, the IsDB is of the view that because of smallness of the states, action plan for them could be made as comprehensive as possible. The areas of assistance could be selected from sectors such as health services, education, sanitation, water supply, and nutrition. Here, the direct improvement in the living standard of the people could be used as one of the measurements for the success of the operations of a multilateral development institution.

In addition, for developing the operational plan for any small state, intensive study and first hand inquiry of the pressing problems facing the majority of the population would be highly useful. The inquiry should include as broad development participants as possible from government, non-government organizations, and others. Regular evaluation of the impact of the projects on the level of development in the small states would also be required.

Finally, in the small states, the private sectors usually are also small; some of them can even be considered as micro-enterprises. In most cases, small private sectors cannot even have an access to existing financial sectors. Thus, the MDBs could further extend their role in this area through the facility of micro financing. At the same time, they could possibly also pave the way, through partnership with the related authorities for the creation of business friendly environment in these states. The IsDB has designed a scheme for micro financing which will start this year. A special unit has been created to define the operational policy in this regard and help on identifying sectors, areas, and prospects of using the net-work of selected NGOs.

The RT HON Clare Short MP, Secretary of the State for International Development  
and The RT HON Gordon Brown MP, Chancellor of the Exchequer, United Kingdom

We welcome the Report of the Task Force on Small States as a pragmatic outcome of a unique and extensive consultation process. The report sets out the range of special challenges facing small states which will need to be addressed by the states themselves, multilateral and bilateral donors. We encourage the multilateral donors to focus their assistance to small states in the areas identified in the report. We agree with the Task Force that the creation of a special category of small states is not required.

We urge stronger co-ordination between donors working in small states, to help streamline programmes and procedures, thereby reducing the transaction costs of donor processes and the pressure placed on administrations of small states. We agree with the emphasis the report places on strengthening the capacity of small states. This is especially important in enhancing their participation in trade negotiations as mentioned above. In the Caribbean, for example, the UK Government is providing technical assistance to the Caribbean's Regional Negotiating Machinery, which represents the small states of the region at international trade negotiations.

Yashwant Sinha, Finance Minister, India

I must congratulate the joint Task Force of the World Bank and the Commonwealth Secretariat for having studied the particular problems of small states. There are a number of important issues that face them, or which in their context assume much greater significance. These basically relate to the impact that natural disasters have on their economies and on their people. The world community would do well to work with these states to strengthen their preventive capacities and to help them in post-disaster situations.

Most of the small states have undiversified economy with a very narrow range of goods, products and services in their export basket. Legally it would not be possible to extend them Special and Differential treatment under WTO. We have been urging the developed countries to allow duty-free non-risk access to products of developing countries, particularly of the LDCs. A list of such products should be identified which could include products from small states as well.

We would also urge that the next round of IDA replenishments should take into account the special needs of these small states, including those, which are not LDCs. Of course it is our hope and conviction that the donors will see that IDA is sufficiently replenished to meeting the rising demand of LDCs.

H.E. Dr. Bambang Sudibyo, Minister of Finance, Indonesia

This report represents the resolve of small states, through their affiliation with the World Bank and Commonwealth Secretariat, to put forward their special development problems on the international development agenda. It should not stop there but we should move forward with a firm commitment to explore and implement policies and strategies that effectively address these problems. In partnership with regional development banks, the Bank's presence would considerably heighten the policy credibility of small states and help reduce risks perceived by capital markets and foreign investors vis-à-vis small states. In our view, the Bank's could play a critical role in carrying this agenda forward.

An action plan to implement the proposed framework should be laid out as part of our continuing agenda. Part of the agenda is to address the issue of 'smallness' an inherent economic characteristic of small states, and to assess how far domestic policies and external support can effectively overcome the problems of diseconomies of scale and competitiveness. We believe these issues would remain principal constraints to small states' development as they face the challenges of globalization.

Anne Kristin Sydnes, Minister of International Development, Norway

The problems faced by small states can differ in nature from those faced by other developing countries, and donors and creditors should help these countries to participate on equal terms with other developing countries in the global community. This underlines the need for a flexible approach by the World Bank in order to meet the special needs of each and every borrowing country.

The work of the World Bank to help small states should build on the efforts and experience of the UN with Small Island Development States and Landlocked Countries. Any further efforts in this field need to be closely coordinated with the UN and the WTO, and with the Regional development banks.

The availability of modern technology has large potential impact on the economic development of small states. The World Bank should encourage efforts to adapt information technology in small states.

**Heidemarie Wieczorek-Zeul, Federal Minister for Economic  
Co-operation and Development, Germany**

Small states, as highlighted in the Task Force's Report, do face special problems, mainly due to the limited size of their economies, their low capacity to diversify risk at the national level, their physical location and, in the case of Small Island Developing States (SIDS), their susceptibility to natural disaster. Many problems reflect global processes and increased interactions between states and regions at several levels, such as the change of the global climate and the changing structure of global trade regimes.

The design of global structures for the benefit of worldwide development has special relevance for many small states. Germany supports all endeavours that lead to better consideration of the special interests and needs of developing countries in the WTO. We are committed to continuing our support to the Global Environment Facility as well as to the implementation of the Rio Conventions.

We endorse the Task Force's call for enhanced regional integration and collaboration as well as capacity building to support the small states' development and transition strategies in order to enable them to profit from globalisation. Furthermore, efforts should be increased to improve donor co-ordination and enhance the effectiveness and efficiency of support efforts by the Bretton Woods Institutions, the Regional Banks, the United Nations and the EC.

## Members of the Development Committee

April 2000

Tarrin Nimmanahaeminda, Chairman

James D. Wolfensohn, President, World Bank

Stanley Fischer, Acting Managing Director, International Monetary Fund

Alexander Shakow, Executive Secretary

Members	Constituency
Ibrahim Al-Assaf Minister of Finance and National Economy Saudi Arabia	Saudi Arabia
Giuliano Amato Minister of the Treasury Italy	Albania, Greece, Italy, Malta, Portugal
Peter Costello Treasurer of the Commonwealth of Australia	Australia, Cambodia, Kiribati, Republic of Korea, Marshall Islands, Federated States of Micronesia, Mongolia, New Zealand, Papua New Guinea, Republic of Palau, Samoa, Solomon Islands, Vanuatu
Pascal Couchepin Federal Councillor and Minister of Economic Affairs Switzerland	Azerbaijan, Kyrgyz Republic, Poland, Switzerland, Tajikistan, Turkmenistan, Uzbekistan
Seydou Elimane Diarra Minister of State in charge of Planning, Development and Government Coordination Côte d'Ivoire	Benin, Burkina Faso, Cameroon, Cape Verde, Central African Republic, Chad, Comoros, Côte d'Ivoire, Democratic Republic of Congo, Djibouti, Equatorial Guinea, Gabon, Guinea, Guinea-Bissau, Madagascar, Mali, Mauritania, Mauritius, Niger, Republic of Congo, Rwanda, São Tomé and Príncipe, Senegal, Somalia (informally), Togo
Nicolás Eyzaguirre Minister of Finance Chile	Argentina, Bolivia, Chile, Paraguay, Peru, Uruguay
Laurent Fabius Minister of Economy, Finance and Industry France	France
Jorge Giordani Minister of Planning and Development Venezuela	Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Spain, Venezuela
Victor B. Khristenko First Deputy Chairman of the Government of the Russian Federation	Russian Federation
Pedro Sampaio Malan Minister of Finance Brazil	Brazil, Colombia, Dominican Republic, Ecuador, Haiti, Panama, Philippines, Suriname, Trinidad and Tobago

<b>Members</b>	<b>Constituency</b>
Kelebone Albert Maope Deputy Prime Minister and Minister of Finance and Planning Lesotho	Angola, Botswana, Burundi, Eritrea, Ethiopia, The Gambia, Kenya, Lesotho, Liberia, Malawi, Mozambique, Namibia, Nigeria, Seychelles, Sierra Leone, South Africa, Sudan, Swaziland, Tanzania, Uganda, Zambia, Zimbabwe
Paul Martin Minister of Finance Canada	Antigua and Barbuda, The Bahamas, Barbados, Belize, Canada, Dominica, Grenada, Guyana, Ireland, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines
Kiichi Miyazawa Minister of Finance Japan	Japan
Fathallah Oualalou Minister of Economy And Finance Morocco	Islamic State of Afghanistan (informally), Algeria, Ghana, Islamic Republic of Iran, Iraq, Morocco, Pakistan, Tunisia
Didier Reynders Minister of Finance Belgium	Austria, Belarus, Belgium, Czech Republic, Hungary, Kazakhstan, Luxembourg, Slovak Republic, Slovenia, Turkey
Abdulla Hassan Saif Minister of Finance and National Economy Bahrain	Bahrain, Arab Republic of Egypt, Jordan, Kuwait, Lebanon, Libya, Maldives, Oman, Qatar, Syrian Arab Republic, United Arab Emirates, Republic of Yemen
Clare Short Secretary of State for International Development United Kingdom	United Kingdom
Yashwant Sinha Minister of Finance India	Bangladesh, Bhutan, India, Sri Lanka
Lawrence Summers Secretary of the Treasury United States	United States
Anne Kristin Sydnés Minister of International Development and Human Rights Norway	Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway, Sweden
Tarrin Nimmanahaeminda Minister of Finance Thailand	Brunei Darussalam, Fiji, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, Nepal, Singapore, Thailand, Tonga, Vietnam
Heidmarie Wieczorek-Zeul Federal Minister for Economic Cooperation and Development Germany	Germany
XIANG Huaicheng Minister of Finance P.R. of China	China
Gerrit Zalm Minister of Finance Netherlands	Armenia, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Georgia, Israel, former Yugoslav Republic of Macedonia, Moldova, Netherlands, Romania, Ukraine

Commonwealth Secretariat/World Bank Joint Task Force on Small States  
Membership, Advisory Board and Chronology of Meetings and Consultations

Membership of the Task Force

**Commonwealth Secretariat**

Dame Veronica Sutherland, DBE, CMG, Deputy Secretary-General, Economic and Social Affairs<sup>59</sup> (Co-chair)

Mr. Rumman Faruqi, Director, Economic Affairs Division

Dr. Chris Easter, Deputy Director, Economic Affairs Division

Dr. Jackson Karunasekera, Chief Programme Officer, Economic Affairs Division

Ms. Judith Pestaina, Special Adviser, Political Affairs Division

**World Bank**

Mr. Masood Ahmed,<sup>60</sup> Vice President, Poverty Reduction and Economic Management (Co-chair)

Ms. Joanne Salop, Vice President, Operations Policy and Strategy Group

Mr. Mahmood Ayub, Director, West Africa Department

Ms. Orsalia Kalantzopoulos, Director, Caribbean Department

Mr. Klaus Rohland, Director, Pacific Islands Department

Mr. Michael Sarris, Director, Africa and Indian Ocean Department

**Secretariat:** Mr. David Peretz (Executive Secretary), Ms. Olga Jonas (Principal Economist, Assistant Executive Secretary), Mr. Laurence Dunn, Mr. Constantine Symeonides-Tsatsos, Mr. Edgardo Favaro. Technical support was provided by Ms. Linda Chu and Mr. Wungram Shishak.

Membership of the Advisory Board

Dr. Dwight Venner, Governor, Eastern Caribbean Central Bank

Mr. Timothy Thahane, Deputy Governor, Reserve Bank of South Africa

Prof. Francisco Granell, Chief Adviser, Directorate-General for Development, European Commission, EU

Mr. Peter Tulloch, Representative of the Director-General, World Trade Organization

H.E. Mr. Ronald Sanders, CMG, High Commissioner of Antigua & Barbuda, UK

Mr. David Edwards, Assistant Chief Economist, Economics and Development Resource Center, Asian Development Bank

H.E. Mr. Alieu Ngum, Ambassador of the Gambia to Saudi Arabia

H.E. Mr. D Baichoo, Ambassador of Mauritius to the WTO

H.E. Mr. Neroni Slade, Ambassador of Samoa to the UN

Mr. Frits van Beek, Representative of the Managing Director, IMF

Mrs. Glenys Kinnock, Member of European Parliament

Professor Andreas Antoniou, Professor of Economics, Cyprus

Messrs. John Toye/Pierre Encontre, Representative of the Secretary-General, UNCTAD

Mr. Edwin Carrington, Secretary-General, Caribbean Community Secretariat (CARICOM)

Mr. Noel Levi, Secretary-General, South Pacific Forum Secretariat

Mr. Mohamed Caabi Elyachroutu, Secretary-General, Indian Ocean Commission

<sup>59</sup> The Hon. Sir Humphrey Maud, KCMG, was Co-chair of the Task Force from September 1998 to November 1999.

<sup>60</sup> Mr. Shahid Javed Burki was Co-chair of the Task Force from September 1998 to August 1999.

## Meetings and Consultations of the Task Force

29-30 September 1998 – Task Force presentation to the Meeting of the Commonwealth Finance Ministers.

8 October 1998 – First meeting of the Task Force, on terms of reference and modus operandi. Washington DC.

7-8 December 1998 – Second meeting of the Task Force and its Advisory Board to discuss the coverage of technical papers to be prepared and commissioned. London.

9-10 December 1998 – Visit of the Task Force to the WTO and UNCTAD for preliminary discussions.

12 February 1999 – Technical briefing by the Task Force of the World Bank Executive Directors.

17-19 February 1999 – International Conference on Small States and second meeting of the Commonwealth Secretariat/World Bank Joint Task Force on Small States to discuss technical papers in support of the work of the Task Force and follow-up. St. Lucia. (Program is appended). Third meeting of the Task Force.

26-28 February 1999 - International Conference on Small States, covering discussion of the Commonwealth's Vulnerability Index for developing countries. Wilton Park, UK.

1-3 March 1999 – Meeting of the Working Group of the UN Committee on Development Policy, covering discussion of the Commonwealth's Vulnerability Index for developing countries and alternative measures. London.

26 March 1999 – Meetings with ACP Ambassadors and experts in the European Commission to discuss the work of the Task Force and the Commonwealth's Vulnerability Index for developing countries. Brussels.

12-13 April 1999 – Fourth meeting of the Task Force, to discuss a first draft of its report. Washington DC.

1 June 1999 – Attendance by the Commonwealth Secretariat co-chair of the Task Force at the Meeting of South Pacific Forum Trade Ministers to outline the work of the Task Force and components of an initial draft report. Suva, Fiji.

1-2 July – Briefing of the Pacific Forum Finance and Economic Ministers on the activities of the Task Force by the World Bank's East Asia and Pacific Region's Director for Strategy, Mr. Schweitzer.

6-8 July 1999 – Task Force mission to the European agencies to make presentations to the WTO Committee on Trade and Development, Geneva-based Ambassadors, UNCTAD, the European Commission and Brussels-based ACP/EU Ambassadors. Objectives were to obtain feedback on a July draft report of the Task Force and to obtain inputs to the final section of the report from partner organizations. Brussels and Geneva.

9 July 1999 – Fifth meeting of the Task Force and third meeting with its Advisory Board, to report back on the Brussels/Geneva mission and discuss the July draft report of the Task Force. London.

12 July 1999 – Meeting of the Commonwealth Consultative Groups on Small States (London-based High Commission Representatives from the 54 Commonwealth member countries) to report back on the Brussels/Geneva mission and present the July draft report of the Task Force. London.

23-26 August 1999 – Consultations with small states of Caribbean Community on the draft Report. Discussions with Belize, Dominica, Guyana, St. Kitts and Nevis, St. Vincent and the Grenadines, Trinidad and Tobago, and the regional organizations, Caribbean Development Bank, Eastern Caribbean Central Bank and the OECS Secretariat.

1-2 September 1999 – Meeting with Ministers of Finance of three West African small states to discuss the August draft report of the Task Force. Praia, Cape Verde.

11 September 1999 – Meeting between the Commonwealth Secretariat co-chair of the Task Force and Prime Minister Owen Arthur on Caribbean comments on the August draft report of the Task Force. Barbados.

16 September 1999 – Meeting of the Commonwealth Consultative Groups on Small States to discuss the August draft report of the Task Force. London.

26 September 1999 – Meeting of the Task Force and representatives of small states to discuss main issues of concern relating to the August draft report of the Task Force, receive suggestions for change and consider the way forward to finalize the document. Bank/Fund Annual Meetings, Washington DC.

27 September 1999 – Meeting of the Task Force and representatives of Pacific small states to discuss main issues of regional concern relating to the August draft report of the Task Force and receive suggestions for change in order to accommodate regional aspects. Bank/Fund Annual Meetings, Washington DC.

29 September 1999 – Meeting of the Task Force and representatives of Caribbean small states to discuss main issues of regional concern relating to the August draft report of the Task Force and receive suggestions for change in order to accommodate regional aspects. Bank/Fund Annual Meetings, Washington DC.

29 September 1999 – Meeting of the Task Force and representatives of African and Indian Ocean small states to discuss main issues of regional concern relating to the August draft report of the Task Force and receive suggestions for change in order to accommodate regional aspects. Bank/Fund Annual Meetings, Washington DC.

11 November 1999 – Meeting of the Commonwealth Ministerial Group on Small States discussed the Interim Report of the Task Force and provided guidance for its completion. Durban, South Africa.

14 November 1999 – Commonwealth Heads of Government Meeting welcomed the Interim Report of the Task Force as a landmark document that confirmed vulnerabilities of small states. They called on the Task Force to complete its report in time for the meeting of the Development Committee in April 2000 after fullest consultations with governments and multilateral agencies. Durban.

8-9 February 2000 – IMF/CDB high-level seminar on globalization provided an opportunity for the Task Force to discuss the main findings of its report in this context, especially policies to cope with adjustments it entails. Barbados.

17-18 February 2000 – Global Conference on the Development Agenda for Small States, London (see program below).

25 February 2000 – Circulation of Provisional version of the final report to Members of the Advisory Board.

29 February-2 March 2000 – UN ECOSOC, Committee for Development Policy, Expert Group Meeting on Economic Vulnerability, considered vulnerability indicators in order to design an index to determine Least Developed Countries. In this context it reviewed the work of other agencies including the Commonwealth Vulnerability Index. Paris.

21 March 2000 – Discussion of the Final Report and of the Draft Executive Summary by the World Bank Executive Directors.

5 April 2000 – Discussion of the work of the task force and the Executive Summary at an informal meeting of the IMF Board.

Program of the Small States Conference, St. Lucia, February 17–19, 1999

**Opening Presentation:** *Diplomacy and Politics of Small States*, Mr. Alan K. Henrikson, The Fletcher School of Law and Diplomacy, Tufts University

**Opening Remarks**

The Right Honorable Kenny D. Anthony, Prime Minister, St. Lucia  
Mr. Shahid Javed Burki - LAC Vice-President, World Bank  
Sir Humphrey Maud, Deputy Secretary General for Economic and Social Affairs,  
Commonwealth Secretariat

*Aid Effectiveness*

Chairs:

The Honorable Kinikinilau Tutoatasi Fakafanua, Minister of Finance , Tonga  
Mr. Guillermo Perry, Chief Economist for Latin America and the Caribbean, World Bank

Presenter: Mr. David Dollar, Research Manager, Development Research Group, World Bank

Discussant: Mr. Francisco Granell, Special Advisor to the Director General DGVIII, European Union

*Economics for Small States and Vulnerability Index*

Chairs:

Mr. Claudio Loser, Director, Western Hemisphere Department, IMF  
Mr. Rumman Faruqi, Director, Economic Affairs Division, Commonwealth Secretariat

Presenters: Mr. William Easterly, Lead Economist, Development Research Group, World Bank

Mr. Christopher Easter, Deputy Director, The Commonwealth Secretariat

Discussants: Mr. David Edwards, Assistant Chief Economist, Asian Development Bank  
Mr. Stephen Free, Director, Commonwealth Caribbean Program, Canadian International Development Program

*Knowledge Management, Capacity Building*

Chairs:

The Honorable James Alex Michel, Vice President of Seychelles.  
Mr. Cesar Gaviria, Secretary General, Organization of American States

Presenters:

Mr. Philip Karp, Division Manager, Economic Development Institute, World Bank  
Mr. Carl Dahlman, Program Manager, Economic Development Institute , World Bank

Discussants:

Sir Alistair McIntyre, former Chancellor of the University of the West Indies  
The Hon. Dwight Venner, Governor, Eastern Caribbean Central Bank

*Country Studies*

Chairs:

The Honorable. Purryag Rajkeswur, Deputy Prime Minister, Ministry of Foreign Affairs and International Trade, Mauritius

Mr. Gordon Shroff, Director, Development Corporation Division, Ministry of Foreign Affairs, Development Division, New Zealand

**Cyprus:** *Lessons from the Experience of Cyprus - A Small Island Economy*

Presenter: Mr. Symeon Matsis, Permanent Secretary, Ministry of Agriculture, Natural Resources and the Environment, Cyprus

**Mauritius:** *Is Small a Handicap? The Mauritian Experience*

Presenter: Mr. Nikhil Treebhohun, Director, Export Processing Zones Development Authority, Mauritius

**Eastern Caribbean Central Bank:** *The Experience of Sub-regional Institutions*

Presenter: The Hon. Dwight Venner, Governor, ECCB

*World Bank's Policy on Small States*

Chair

The Rt. Honorable Owen S. Arthur, Prime Minister of Barbados

Presenter: Ms. Joanne Salop, Director, Operations Policy and Strategy, World Bank

*International Trade Challenges for Small States*

Chair:

The Rt. Honorable D. Kenny Anthony, Prime Minister and Minister of Finance, St Lucia

Presenters:

Mr. John Toye, Director, Globalization and Development Strategies Division, UNCTAD

Mr. Roman Grynberg and Mr. Christopher Stevens, Commonwealth Secretariat

Discussants:

H.E. Hassan Abouyoub, Ambassador at large, Morocco

H.E. Dr. Richard Bernal, Ambassador of Jamaica to the United States

Mr. Constantine Michalopoulos, Special Economic Advisor, World Trade Organization

*Insurance and Disaster Management*

Chairs:

The Honorable Casimir Oye-Mba, Secretary of State, Minister of Planning, Programming of the Development of the Territory, Gabon

Mr. Francisco Granell, Special Advisor to the Director General DGVIII, European Union

Presenter: Mr. John Daniel Pollner, World Bank

Discussants:

Mr. Neil Doherty, Wharton School, University of Pennsylvania

Mr. Ian McLean, Greig Benfield Reinsurance

Mr. Rodney Lester, World Bank

Mr. David Deane, Barbados Insurance Co.

*Private Sector Round Table:*

Mr. Frank Vukmanic, Division Chief, Inter-American Development Bank

Mr. Danny M. Leipziger, Director, Finance, Private Sector, and Infrastructure for Latin America and the Caribbean, World Bank

Discussants:

Ms. Pauline Bernard, St. Lucia Representative Services, Ltd.

Mr. Cornell Charles, JQ Charles

Mr. Peter Divoux, Minvielle and Chastanet

Mr. Lyle Chase, Chase, Skeete and Boland

Mr. Michael Millette, Goldman Sachs

Program of the Global Conference on the Development Agenda for Small States,  
London, February 17–18, 2000

**Chairman: The Rt. Hon. Owen Arthur, Prime Minister of Barbados**

**Thursday, 17 February 2000**

Opening Remarks

Dame Veronica Sutherland, Deputy Secretary-General (ECOSOC)

Masood Ahmed, Vice President, World Bank

The Rt. Hon. Owen Arthur, Prime Minister of Barbados and

Chairman, Commonwealth Ministerial Mission on Small States

**Agenda Item 1: Reducing Vulnerability Chair: The Rt. Hon. Owen Arthur**

Presentations:

Dr. Chris Easter, Commonwealth Secretariat: *The Impact of Vulnerability on Small States*

Ms. Nawal Kamel, World Bank: *Commodity Risk Management in Developing Countries: A Proposed Market-Based Approach and its Relevance for Small States*

Mr. John Pollner, World Bank: *The Management of Catastrophic Risks Using Pooled Insurance Structures and Alternative Financing and Risk Transfer Mechanisms*

Plenary Discussion of ***Reducing Vulnerability***

**Agenda Item 2: Capacity Building - Delivering Effective Development Assistance at Lower Transaction Costs  
Chair: Masood Ahmed**

Presentations:

Mr. Dwight Venner, Governor of the Eastern Caribbean Central Bank: *From Aid Co-ordination to Development Management in the Eastern Caribbean*

Ms. Wendy Jarvie, Manager, Corporate Evaluation and Methods, Operations Evaluation Department, World Bank: *Lessons from the Review of Aid Co-ordination*

Plenary Discussion of ***Delivering Effective Development Assistance***

**Agenda Item 3: Capacity Building - Sharing Capacity: Regional Co-operation/ Integration Experience  
Chair: Dame Veronica Sutherland**

Presentations:

Mr. Byron Blake, Assistant Secretary-General, CARICOM: *The Case of the Caribbean Community*

H.E. Mr Noel Levi, Secretary-General, South Pacific Forum Secretariat: *The Pacific Experience with Regional Co-operation and Integration*

Plenary Discussion of ***Sharing Capacity***

## **Regional Break-Out Sessions**

### ***Africa Region: African Perspectives***

Chairman: Mr. Godfrey Gaoseb, Executive Director, World Bank

Rapporteur: H.E. Mr. D Baichoo, Permanent Representative of Mauritius to the UN

### ***Caribbean Region: Key Issues***

Chairman: Sir Neville Nichols, President, Caribbean Development Bank

Rapporteur : Mr. Byron Blake, Assistant Secretary-General, CARICOM

### ***Pacific Region: Regional Co-operation and Capacity Building***

Chairman: H.E. Mr. Noel Levi, Secretary-General, South Pacific Forum

Rapporteur: H.E. Mr. Neroni Slade, Permanent Representative of Samoa to the UN

## **Plenary Session : Reports from Regional Break-out Groups**

**Chair: Dame Veronica Sutherland**

**Friday, 18 February 2000**

### **Agenda Item 4: Transition to the New Trade Regime**

**Chair: Sir Shridath Ramphal**

#### Presentations:

Dr. Roman Grynberg, South Pacific Forum: *The Pacific Islands and the WTO: Towards a Post-Seattle Agenda for the Small Vulnerable States*

Mr. Sam Laird, Senior Counsellor, Development Division, WTO:

Mr. Liam Ebrill, Assistant Director, Tax Policy Division, Fiscal Affairs Department, IMF:  
*The Revenue Implications of Trade Liberalisation - Issues Facing Small Economies*

Plenary Discussion of *Transition to the New Trade Regime*

### **Agenda Item 5: Globalisation and Small States**

**Chair: HRH Prince Ulukalala Ata, Prime Minister of Tonga**

#### Presentations:

Sir Alister MacIntyre, Chief Technical Adviser, Caribbean Negotiating Machinery: *Issues in Globalisation*

Mr. Paul Kimberley, Consultant, World Bank: *Exploiting Information Technologies for Electronic Commerce and Better Public Sector Management*

Plenary Discussion of *Globalisation and Small States*

## Thematic Break-out Sessions

- ♦ *Tackling Volatility, Vulnerability and Natural Disasters*  
**Chair:** The Hon. Rajkeswur Purryag, Deputy Prime Minister and Minister of Foreign Affairs and International Trade, Mauritius  
**Lead Presentation:** Dr. Russell Howarth, Programme Manager, SOPAC:  
*Environmental Vulnerability*  
**Rapporteur:** Mr. Jeremy Collymore, Regional Co-ordinator, Caribbean Disaster Emergency Response Agency
  
- ♦ *Strengthening Capacity*  
**Chair:** H.E. Mr. Bertrand Rassool, High Commissioner of Seychelles to the United Kingdom  
**Presenter:** Margaret Callan, Director, Policy and Management Reform Section, South Pacific Branch, Aus AID: *A Donor's Perspective*  
**Rapporteur:** Mr. Neville Beharie, Inter-American Development Bank
  
- ♦ *Transition to the Evolving Global Trade Regime*  
**Chair::** The Hon. George Odum, Minister of Foreign Affairs and International Trade, St. Lucia  
**Rapporteur:** Dr. Arnold McIntyre, Economic Adviser, Grenada
  
- *New Opportunities and Challenges from Globalisation*  
**Chair:** Sir Shridath Ramphal, Chief Negotiator, Caribbean Regional Negotiating Machinery  
**Presentation:** Mr. Anthony Hughes, Solomon Islands  
**Rapporteur:** The Hon Clement J Rohee, Minister of Foreign Affairs, Guyana

**Concluding Session      Chair: The Rt. Hon. Owen Arthur**

Reports from four thematic break-out sessions

*Chairman's Conclusions* The Rt. Hon. Owen Arthur

## Small states and their memberships in key international organizations

<i>Country</i>	<i>Asia, Caribbean, and Pacific</i>	<i>Commonwealth</i>	<i>World Bank</i>	<i>World Trade Organization</i>
Antigua and Barbuda	×	×	× <sup>a/</sup>	×
Bahamas	×	×	× <sup>a/</sup>	
Bahrain			× <sup>a/</sup>	×
Barbados	×	×	×	×
Belize	×	×	×	×
Bhutan			×	○
Botswana	×	×	×	×
Brunei		×	× <sup>a/</sup>	×
Cape Verde	×		×	○
Comoros	×		×	
Cook Islands		× <sup>b/</sup>		
Cyprus		×	×	×
Djibouti	×		×	×
Dominica	×	×	×	×
Equatorial Guinea	×		×	
Estonia			×	×
Fiji	×	×	×	×
Gabon	×		×	×
Gambia, The	×	×	×	×
Grenada	×	×	×	×
Guinea-Bissau	×		×	×
Guyana	×	×	×	×
Kiribati	×	×	×	
Maldives		×	×	×
Malta		×	× <sup>a/</sup>	×
Marshall Islands			×	
Mauritius	×	×	×	×
Micronesia, Federated States			×	
Nauru		×		
Niue		× <sup>b/</sup>		
Palau			×	
Qatar			× <sup>a/</sup>	×
Samoa		×	×	○
São Tomé and Príncipe	×		×	
Seychelles	×	×	× <sup>a/</sup>	○
Solomon Islands	×	×	×	×
St. Kitts and Nevis	×	×	×	×
St. Lucia	×	×	×	×
St. Vincent and the Grenadines	×	×	×	×
Suriname	×		×	×
Swaziland	×	×	×	×
Tonga	×	×	×	○
Trinidad and Tobago	×	×	×	×
Tuvalu	×	×		
Vanuatu	×	×	×	○

× = Full membership; ×<sup>a/</sup> = Member of IBRD only, not member of IDA. ○ = Observer status.

×<sup>b/</sup> = Member in association with New Zealand.

Source: World Bank data; Commonwealth Advisory Group 1997.

**Annex 3**  
**Selected Economic and Social Indicators**

Region/Country	Surface Sq km	PPP Adj GNP Per Capita current US\$	External debt		Safe Water % population with access	Life Expectancy years	Illiteracy Rate %	Female Illiteracy Rate %	Adolescent Fertility Rate births per 1000 women 1998	Secondary School Enrollment % of relevant age group 1993-1998	Infant Mortality per 100,000 live births 1993-1998
			as % of GNP	conces- sional as % of total							
		1998	1998	1998	1993-98	1998	1993-98	1993-98			
<b>Africa</b>											
Botswana	581,730	5,796	12	54	70	46	24	22	76	65	62
Cape Verde	4,030	3,192	50	79	..	68	27	35	91	55	55
Comoros	2,230	1,400	103	88	48	60	42	48	101	21	63
Djibouti	23,200	..	0	91	..	50	..	..	29	14	106
Equatorial Guinea	28,050	..	76	47	95	50	19	29	173	..	106
Gabon	267,670	5,615	91	21	67	53	..	..	164	56	86
Gambia, The	11,300	1,428	117	91	76	53	65	73	170	25	76
Guinea-Bissau	36,120	573	504	72	53	44	63	83	187	..	128
Mauritius	2,040	8,236	60	14	..	71	16	20	38	65	19
Sao Tome & Principe	960	1,289	684	93	..	64	..	..	152	..	49
Seychelles	450	10,185	36	38	97	72	..	..	52	..	15
Swaziland	17,360	4,195	19	57	43	56	22	23	113	54	69
<b>East Asia &amp; Pacific</b>											
Fiji	18,270	4,094	13	13	100	73	8	10	43	..	19
Kiribati	730	3,880	..	..	100	61	..	..	62	..	58
Micronesia, Fed. Sts.	700	..	..	..	100	67	..	..	40	..	28
Samoa	2,840	3,854	102	83	68	69	..	..	21	62	25
Palau	500	..	..	..	100	..	..	..	..	..	25
Solomon Islands	28,900	1,904	52	64	..	71	..	..	92	17	22
Tonga	750	4,187	37	85	100	71	..	..	20	..	21
Vanuatu	12,190	2,892	28	85	87	65	..	..	49	..	36
<b>Latin America &amp; Caribbean</b>											
Antigua and Barbuda	440	8,890	..	..	95	75	..	..	62	..	17
Bahamas, The	13,880	13,990	..	..	97	74	5	4	60	87	17
Barbados	430	..	0	12	100	76	..	..	48	..	14
Belize	22,960	4,367	52	32	73	75	..	..	97	49	28
Dominica	750	4,777	47	76	..	76	..	..	46	..	15
Grenada	340	5,557	56	39	85	72	..	..	95	..	14
Guyana	214,970	3,139	249	58	..	64	2	2	58	74	57
Jamaica	10,990	3,344	63	27	70	75	14	10	100	..	21
St. Kitts and Nevis	360	9,790	43	76	100	70	..	..	91	..	21
St. Lucia	620	4,897	32	47	100	72	..	..	94	..	17
St. Vincent and the Gr	390	4,484	139	20	..	73	..	..	57	..	22
Suriname	163,270	..	..	..	72	70	..	..	22	45	28
Trinidad and Tobago	5,130	7,208	36	1	82	73	2	3	42	74	16
<b>Other regions</b>											
Bahrain	690	11,556	..	..	100	73	14	19	23	94	9
Bhutan	47,000	1,438	32	100	64	61	..	..	73	6	61
Estonia	45	7,563	15	4	..	70	..	..	36	104	9
Maldives	300	3,436	58	80	89	67	4	4	47	69	31
Malta	320	22,901	..	..	100	77	9	8	9	84	6
Qatar	11,000	..	..	..	100	74	20	18	48	80	18
<b>Small states average</b>		5,456	30	33	84	67	21	24	73	57	38
<b>All countries</b>											
<i>Low income</i>		2,170	40	34	..	63	32	42	85	58	69
<i>Lower middle income</i>		4,700	49	16	..	68	14	18	49	68	38
<i>Upper middle income</i>		8,020	39	3	79	70	11	13	59	62	27

Source: World Bank database.



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<sup>61</sup> This bibliography draws extensively on the "Selected Bibliography on Small States' Issues," compiled for the Joint Task Force Report by the CARICOM Secretariat in October 1999.

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