

ORGANIZATION OF EASTERN CARIBBEAN STATES

TRADE POLICY BRIEF

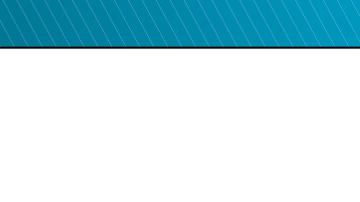
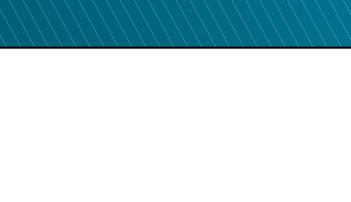
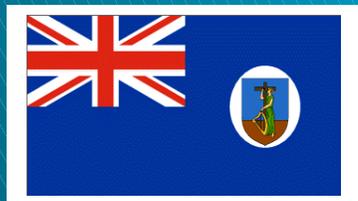
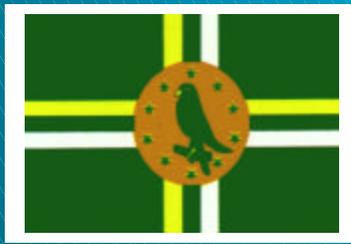
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Small Economies: **A Conceptual Note**

1. Introduction

The WTO General Council, on 1 March 2002, agreed on a framework and procedures for a work programme on small economies; see 'Framework and Procedures' (WT/L/447). This follows action requested in the Fourth WTO Ministerial Declaration – Doha, Qatar, November, 2001 - (Paragraph 35) on small economies. As per the Declaration the following is stated in respect of small economies:

“we agree to a work programme, under the auspices of the General Council, to examine issues relating to the trade of small economies. The objective of this work is to frame responses to the trade-related issues identified for the fuller integration of small, vulnerable economies into the multilateral trading system, and not to create a sub-category of WTO Members. The General Council shall review the work programme and make recommendations for action to the Fifth Session of the Ministerial Conference”.

Following the agreement by Ministers at the Doha Ministerial to establish a work programme “to frame responses to the trade-related issues identified for the fuller integration of small, vulnerable economies into the multilateral trading system”, the General Council agreed that:

1. The question of small economies would be a standing agenda item of the General Council;
2. The [Committee on Trade and Development \(CTD\)](#) will hold dedicated sessions on this question and report to the General Council; and,
3. In the light of the outcome of this work, relevant subsidiary bodies will be asked by the General Council to frame responses on the trade-related issues identified in the CTD.

As per the Doha Declaration, then, the General Council is mandated to examine problems/challenges in small economies' participation in world trade and to make recommendations to the next Ministerial Conference as to what trade-related measures could improve the integration of small economies to this end.

2. What is a Small Economy?

By small economies reference is made primarily to (economic) size which some studies have suggested include: total GNP, total population and total arable land. Earlier work at the Commonwealth Secretariat has shown that a composite index of all three indicators (unweighted) ranks countries in terms of size in much the same way as their ranking according to population alone.¹ Hence, population can justifiably be used as a proxy for economic size and ease of data availability provides further justification.

Small economies are a diverse group comprising land-locked countries, those with access to the sea and also island states. This diversity has traditionally raised some interesting questions in respect of terminology. Consider that even within the small economy group there is immense diversity not just in geographic construct but also population, economic predisposition, etc. Consider the case of what are commonly referred to as small island developing states (SIDS); they are not a homogenous group. Often, SIDS are thought of as very small states especially in terms of population, but the fact is the island of Hispaniola's (Dominican Republic and Haiti) total population is 15m million. With respect to other factor endowments there are also significant differences, consider The Islands of the Bahamas in comparison to the OECS islands for example. Given the inherent heterogeneity of the small economies grouping of countries and differences within sub-sets of that grouping, 'definition' has always been difficult. The fact is, an important concern with any threshold is the problem of exclusion at the margins - the 'tyranny of round numbers'.

The heterogenous nature of small economies is brought into even sharper focus when we consider that even in terms of per capita GNP and growth in per capita GDP some have appeared amongst the most successful developing countries while others amongst the least successful. However, common to the group, at large, is that they are more homogeneous in terms of the *volatility* of per capita GDP growth over time, having a propensity to experience a greater degree of volatility than do large states.

3. Characteristics of Small Economies

It has been difficult, then, to agree on a common definition in respect of the term and concept of 'small economy'. However, there is agreement that small economies are characterized by certain *structural* (e.g. population, land area and GDP) and *policy related* (e.g. high degree of openness - having some of the highest trade to GDP ratios, often exceeding 100 percent, lack of export diversification and dependence on trade taxes) indicators that differentiate them from other larger developing countries. Small size is a constraint on growth

¹ see: 'Classification of Economies by Size', Chapter 2 in B. Jalan (ed.), *Problems and Policies in Small Economies*, London: Croom Helm, 1982.

and trade/integration given various sub-optimalities and certain manifest characteristics, *inter alia*:

1. Small domestic markets (small population base) that make it difficult to attract foreign investment and insufficient scale economies (small and sometimes fragmented markets leading to market structures characterized by substantial imperfections e.g. one or two firms effectively dominating the small domestic market);
2. Insignificant share of trade in the multilateral trading system;
3. Limited resource base (leading to high level of reliance on imports and exports), including labor;
4. Limited availability of economically exploitable land;
5. In some cases physical isolation/remoteness from main markets;
6. Narrow output and export structures;
7. Lack of a critical mass makes it difficult to apply new technologies;
8. Limited scope for diversification of economic activity, resulting in vulnerability to changes in the external environment;
9. Acute supply-side constraints;
10. Limited capacity in both the public and private sectors;
11. Limited access to external capital markets, which is of importance to countries since private markets tend to view small states as being more risky than larger states;
12. High levels of poverty and underdevelopment;
13. Structural openness to trade (extreme/acute vulnerability to external shocks);
14. Export concentration in a few commodities/services and dependence on one or two export markets; and,
15. Vulnerability - economic, political and environmental².

Many of these above characteristics appear in a seminal report of the Commonwealth Secretariat and the World Bank that jointly studied the problems

² For example, low lying and coastal parts of small islands are threatened by global phenomena such as rising sea levels and more severe cyclones (and hurricanes) as predicted effects of climate change. Such environmental hazards can devastate whole sectors or islands.

of small states³. In addition, these characteristics were the subject of a number of international conferences, the UN Conference on Sustainable Development of Small Island Developing States (Barbados, 1994) being the culmination of this process. This Conference adopted the Barbados Programme of Action (BPA)⁴ that proposes actions to be taken at the national, regional and international level in order to strengthen the sustainable development of SIDS. This notwithstanding, many of the priority areas identified in Barbados are partially implemented and on others no action has been taken. The special and differential needs of SIDS are not recognised in the WTO and many small states have either been graduated, or face graduation from, international financial institutions, resulting in diminished access to concessional development finance.

Whilst the characteristics and ramifications of small size, as reviewed above, constitutes an acute constraint on growth and trade/integration what this list really speaks to are 'vulnerabilities'.⁵ In effect, many of the above characteristics whilst not necessarily unique to small economies are, in effect, magnified as a result of extreme 'smallness'. In many ways these 'small economies' are 'small vulnerable states' (SVS). 'Small' and 'vulnerable' – terms that both define and describe a situation where domestic markets offer no/limited economies of scale or the combined challenge and comfort of a cluster of peer enterprises, and the higher risk of economic instability and physical disruption of services that comes with 'economic exposure; remoteness and insularity; and proneness to natural disasters'⁶.

4. Concluding Remarks

Vulnerability is widely acknowledged to be associated with 'significant' *exposure to external economic forces and environmental hazards*. For small states, then, there are two principle categories of vulnerability - economic and environmental. In the Commonwealth Secretariat's 1997 report, *A Future for*

³ A three-year process of research and consultation, culminating in the publication of *Small States: Meeting Challenges in the Global Economy - Report of the Commonwealth Secretariat/World Bank Joint Task Force on Small States*, Commonwealth Secretariat, 2000.

⁴ The Barbados programme is viewed as the blueprint for sustainable development in SIDS. Actions are defined in over a dozen agreed priority areas such as climate change, natural and environmental disasters, waste management, coastal and marine resources, tourism, biodiversity, institutions and administrative capacity, regional cooperation, transport, and human resources. This comprehensive Programme of Action as per the UN global conference in Barbados has precipitated a process where since then, the UN General Assembly confirmed the need for international support to help SIDS, Commonwealth Heads of Government approved a series of recommendations to enhance the development of SIDS, and the World Bank joined a task force with the Commonwealth Secretariat to address the concerns of small states.

⁵ Vulnerability is the 'acute' propensity for attributes of a country to be undermined and placed under threat by exogenous factors.

⁶ *A Commonwealth Vulnerability Index for Developing Countries*, Economic Paper No 40, Commonwealth Secretariat, 2000.

Small States: Overcoming Vulnerability, the contention is that 'vulnerability is the consequence of two sets of factors: (1) the incidence and intensity of risk and threat and (2) the ability to withstand risks and threats (*resistance*) and to "bounce back" from their consequences (*resilience*)'. The Report argues such threats emanate from three main sources: economic exposure; remoteness and insularity; and proneness to natural disasters.

The vulnerability of certain developing countries, specifically small states, then, dampens their long-run growth path such that they have a lower long-run trend rate of growth than larger states. Coupled with greater volatility (as previously mentioned the interplay of factors such as smallness, geographical dispersion, vulnerability to natural disasters and a highly limited internal market, to name a few) around this dampening effect there are significant negative ramifications for such states' fuller integration into the multilateral trading system. In point of fact, the vulnerabilities of small states are multi-dimensional and inter-related but are connected especially to and are compounded by acute exposure to external economic forces and environmental hazards. It is this appreciation, as regards the additional constraints faced by and peculiar characteristics associated with small economies, that needs to be forthcoming in special and differential treatment afforded to countries like those of the Caribbean in the multilateral trading system.

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