Economic Vulnerability and Resilience: Lessons from Eastern Caribbean Small Island Developing States

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Abstract

This thesis addresses the surprising economic resilience of Dominica, a small island developing state, in the wake of the global economic downturn of 2008. The relatively stronger economic resilience of Dominica is analyzed through a vulnerability and resilience analytical framework. The analysis reveals that the variance of Dominica could be explained by resilience-building policies implemented there but not in its similar neighbors St. Lucia and St. Vincent and the Grenadines, namely macroeconomic stabilizing policies and a more moderate reliance on tourism revenues. The thesis suggests that differentiated policy responses are needed in the case of small island developing states, which have unique economic vulnerabilities and development needs.

Table of Contents

Abstract	i
Table of Contents	ii
List of Tables and Figures	iii
Introduction	1
Chapter 1: The Problems with Smallness 1.1 Small Island Developing States Literature and Debate 1.2 Concepts of Vulnerability and Resilience	7
 1.3 The Erosion of Trade Preference in the Eastern Caribbean as a Natural Experir the Vulnerability and Resilience Hypothesis 1.4 The Gap Between Theory and Empirics 1. 5 Contribution to Small Island Developing States Literature 	nent for 15 17 18
Chapter 2: Methodology and Theoretical Framework	20
Chapter 3: Empirical Analysis 3.1 Background: The Eastern Caribbean Banana Industry, Before and After 3.2 Resilience in the Eastern Caribbean 1.3 Post-crisis Outcomes 1.4 Resilience-building Policies as an Explanatory Variable 1.5 Limitations	25 25 27 32 35 36
Chapter 4: Policy Implications	
Conclusion	40
Reference List	42

List of Tables and Figures

Table 1: Resilience and Vulnerability Typology	13
Table 2: Selected Characteristics of Windward Islands	15
Figure 1: Banana production and exports	26
Figure 2: International tourism receipts	34

Introduction

Scholars have long debated the merits of state size in facilitating development. Theoretically, there are a number of reasons to believe that smaller states do suffer for their smallness. In the classical economic understanding of international trade, small states are defined as "price takers," suggesting structural economic differences between large and small states that shape their development path (Briguglio 1995; Croes 2006). A small state is constrained by limited natural resources, capital and labor, all of which may affect the ability of the state to compete internationally (Armstrong and Read 2003). With an inability to exploit economies of scale at home, small states are compelled to engage in trade to fulfill domestic demand (Baldacchino 1993; Bishop 2010). Such states tend toward a narrow range of production and exports in economies dominated by a few activities that become highly exposed to exogenous shocks, such as export price fluctuations or earnings instability (Armstrong and Read 2003). An additional small state characteristic may be public sector largesse; the ratio of population size to government activities tends to be wider in small states, owing to the necessity of economies of scale in the production of public goods (Alesina, Spolaore, and Wacziarg 2005).

In addition to facing all of the aforementioned maladies of small states, small island states are believed to suffer added difficulties in the international economy due to high transportation costs, time delays and high costs in accessing external goods (Pelling and Uitto 2001). Islands share risk of exogenous shocks in the form of environmental hazards – including natural disasters, e.g. hurricanes, floods, etc., and climate change consequences, such as sea-level rise (Guillaumont 2010; Pelling and Uitto 2001; Turvey 2007). So potentially damaging are these factors that international organizations have focused increasing attention on understanding and

recognizing the disadvantages experienced by small islands (UNCTAD 1983, 2004). Reflecting the challenges perceived to be faced by these nations, the UN Conference on Environment and Development formally recognized small island developing states (SIDS) as a distinct group of developing countries in June 1992 and launched special initiatives to address their concerns (Briguglio et al. 2009).

Despite academic and international concern about the vulnerabilities islands face particularly related to exogenous shocks, there is no program for specialized treatment for SIDS within the WTO framework, except in the case of SIDS that are also designated as least developed countries (LDCs). This rejection of preferential treatment for SIDS was nowhere more apparent than during the prolonged "banana wars" negotiations that ultimately lead to the erosion of trade preferences between the EU and African, Caribbean and Pacific (ACP) countries, through which European nations protected smallholder banana producers in several Caribbean islands from potentially devastating competitors from Latin America. Among these Caribbean ACP nations, the tiny islands of St. Lucia, St. Vincent and the Grenadines (SVG) and Dominica, with economies heavily concentrated on banana production and exportation, were predicted to suffer damaging economic and social consequences if forced to compete with the cheaper, monoculture banana plantations in Central and South America.

Part of this conflict between the multilateral trading system, which extols the positive effects of trade liberalization for all countries regardless of development stage or size, and development programs, which recognize size and islandness as constraints to development, has to do with the ambiguous empirical evidence that connects small size and islandness to growth. Several studies suggest that neither characteristic need preclude economic growth; in fact, because small developing states are more likely to be open, they are more likely to experience

economic growth from trade – ultimately offsetting any losses from the volatility accompanying openness (Armstrong et al. 1998; Easterly and Kraay 2000; Srinivasan 1986). Small states that focus on services versus agriculture are associated with strong growth performance; the success of small islands specializing in services such as tourism and offshore finances suggests islandness has little to do with growth, despite *a priori* reasoning suggesting its importance (Armstrong and Read 2003). Indeed, the Caribbean islands themselves, despite self-professed vulnerability, enjoy higher GDP per capita and growth rates than their Latin American counterparts. Such findings imply "that the lessons of growth experience from all countries seem to be applicable to small states" (Easterly and Kraay 2000, 15-16). Indeed, a great number of economically successful small island states would seem to imply that smallness is not a "necessarily and sufficient condition" for slow economic growth – and small may, in fact, be beautiful (Srinivasan 1986, 207).

The collapse of the banana trade in the Eastern Caribbean provides an interesting way to examine these competing claims. Under the trade preferences granted by European nations to Eastern Caribbean states through the Lome Agreements, these islands experienced strong growth thanks to one economic activity – banana production. The erosion of these preferences following unfavorable WTO rulings, opening up the Eastern Caribbean islands to international competition, was considered a death sentence for the banana industry there, and disastrous for the economic and social fabric of the countries. However, despite the collapse of the banana trade following preference erosion, the performance of one banana-producing state, Dominica, appears to be surprisingly rosy, particularly in light of the 2008 global economic downturn. The question of how Dominica managed to overcome the inherent disadvantages of smallness and islandness and experience improving economic and social performance in the wake of an

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exogenous shock, while its neighbors SVG and St. Lucia did not, is the focus of this paper.

Briguglio's suggestion that small states grow "not because they are small, but in spite of this fact" (1998) provides one way to examine this puzzle. Briguglio, backed by decades of research on small island states, hypothesize that small islands may be more vulnerable than other states to exogenous shocks, but they may also have achieved greater resiliency to those shocks through resilience-building policies (Briguglio 2004). Islands that are better at achieving resiliency do not experience the problems of growth volatility as intensely; on the other hand, islands that are less resilient may experience such instability that it impedes social development and ultimately future growth (Briguglio et al. 2009). Small islands that are successful in building resilience, according to Briguglio, are better able to weather the booms and busts associated with greater openness, ultimately leading to greater growth and development (2004).

Inspired by Briguglio's work on vulnerability and resilience, this paper addresses the variance of Dominica by using a vulnerability and resilience framework to examine postpreference erosion policies in the Eastern Caribbean islands of St. Lucia, SVG and Dominica. To explore these issues, this paper draws upon a wealth of secondary evidence discussing small island state theory, vulnerability, trade preference erosion and in particular, preference erosion affecting banana-producing Eastern Caribbean states. Primary documents on social development, poverty and growth in the region are utilized, including World Bank reports and statistics, IMF reports and UN indicators on human development and poverty.

Using a most-similar case study design, this paper argues that the variation noted in the economic and social performance among St. Lucia, SVG and Dominica during the recent economic crisis can be explained as an effect of the pro-resiliency policies implemented by Dominica, but not in SVG and St. Lucia. If development success in islands is attributed to

resilience-building policies as Briguglio et al. argue, then we would expect Dominica to have implemented resilience-building policies since trade preference erosion. The analysis reveals that Dominica does appear to have implemented macroeconomic reforms, including the introduction of a VAT, debt restructuring and decreased spending, that enabled it to bounce back more quickly from the exogenous shock of the crisis. Limited dependence on tourism also sheltered the country from the worst of the downturn.

Dominica's success in boosting its resiliency suggests that it is the policies islands pursue that ultimately shape their outcomes. This implies that it is critical for both the international community and domestic policymakers to recognize not only the inherent vulnerabilities of the islands, but also the importance of creating mechanisms for improved resilience. This paper argues that the concept of vulnerability can be an additional variable to explain how islands do face certain unique challenges – which some islands are better able to surmount than others. The use of a more nuanced classification system for SIDS is suggested as a way to enable policymakers to differentiate policy solutions that address the critical need for such states to build resilience in the face of vulnerability, particularly that which is related to trade preference erosion.

Chapter 1 of this thesis traces the debate on smallness and islandness as inhibitors to growth and development. Chapter 2 sets up the methodology and theoretical framework used to answer the critical question: How did the small island state of Dominica manage to overcome the inherent disadvantages of smallness and islandness and experience improving economic and social performance in the midst of the global economic crisis? Chapter 3 reveals that while islandness and smallness have created challenges to stable growth and development in the Eastern Caribbean, Dominica has managed its vulnerabilities more successfully than others

through prudent resilience-building policies. In Chapter 4, policy implications are suggested that reflect the uniqueness of small island developing states. The final section concludes.

Chapter 1: The Problems with Smallness

When it comes to growth and development, does the size of a state matter? There are a number of compelling theoretical reasons to believe that it does. Small state literature identifies multiple constraints that oblige such states to suffer for their smallness; islands, as both small and remote, face significant challenges. Generally, the disadvantages of smallness or islandness are identified as (a) small domestic market size; (b) limited resources, including natural resources, labor and capital; (c) lack of diversification; (d) exposure to exogenous economic shocks, namely price volatility; (e) exposure to exogenous environmental shocks, e.g. hurricanes, floods, and the like; and (f) insularity/remoteness. This chapter examines the concepts of smallness and islandness and associated disadvantages as identified in the literature. These disadvantages can be seen as components of vulnerability and resilience, concepts used to hypothesize why some island states perform better than others (Briguglio et al. 2009). The case of three Eastern Caribbean island states – St. Lucia, SVG and Dominica – provides a starting place to examine the issues of smallness, islandness, vulnerability and resilience, and how they affect the growth and development of islands.

The first section of this chapter explores the disadvantages of smallness and islandness as identified in the literature. Section 2 describes the concepts of vulnerability and resilience to explain how some small island states perform better than others, even when confronted with economic shocks. In Section 3, the natural experiment provided by the cases of St. Lucia, SVG and Dominica is described. Section 4 examines the gap between small island theory and

empirical work. The final section discusses how the present case study contributes to the literature.

1.1 Small Island Developing States Literature and Debate

While smallness is the subject of much research, there is little consensus as to how to define smallness or measure it (Armstrong and Read 2003). Depending on the academic discipline, a state may be defined as small based on its economic size, terms of trade or land area. Many studies use population as an easily available indicator that serves as a proxy for two economic variables: the size of the domestic market and local labor force (Armstrong and Read 2003); however, the threshold of smallness often varies from less than 1 million to 10 to 15 million (Easterly and Kraay 2000).

Despite this conceptual ambiguity, small states have long been a concern among international organizations seeking to address their development issues. More recently, discussion has focused on small island states, considered to face additional constraints due to remoteness and insularity. Since the development of the Barbados Programme of Action in 1994, the UN has identified priority areas of action to address the special challenges in planning and development faced by SIDS (Briguglio et al. 2009). Like the LDCs category (which also includes many SIDS), the SIDS category reflects the idea that some countries may need special attention to solve problems that are not being addressed by other agencies or donors (Srinivasan 1986).

The UN's Department of Economic and Social Affairs defines the 51 members of its SIDS category as "low-lying and island nations that share similar physical and structural challenges to their development" (SIDS Members 2009). Those characteristics include remoteness, small land area, small population (less than 1.5 million), narrow resource base, fragile ecosystems, high

vulnerability to natural disasters, and heavy dependence on trade (SIDS Members 2009). Academic literature has focused on similar challenges, broadly grouped into the following economic and environmental dimensions:

- a. Small domestic market size. A relatively low population means that domestic demand is below the minimum efficient scale of production (Armstrong and Read 2003).
 Furthermore, this inability to capture the benefits of economies of scale implies that typical import substitution possibilities are limited. Small islands have small domestic markets and may rely heavily on imports to meet their needs (Briguglio et al. 2009, 4). The need for a relatively large amount of foreign exchange required to pay for these imports leads to a higher dependence on exports (Briguglio et al. 2009, 5)
- b. Limited natural, human and capital resources. With smaller land area, SIDS often suffer from poor or narrow natural resource endowment, further increasing their dependence on imports (Briguglio et al. 2009, 5). A smaller labor pool implies that states are unable to compete with other states that have large endowments of low-skilled labor (Armstrong and Read 2003). The spread of specialization among the labor force is narrow, leaving the potential for unpredictable shortages of specific skills and difficulty in adjusting to shortfalls or surpluses in labor market segments (Baldacchino 1993). A shortage of capital forces small states to look abroad to fulfill their demand, making them highly dependent on external capital (Croes 2004).
- **c.** Lack of diversification. Small size may also limit the ability of a state to diversify its exports. The issue of "having too many eggs in one basket" exacerbates the problem of dependency on international trade (Briguglio et al. 2009, 5). Attempts to diversify at low cost are problematic, given the diseconomies of scale linked to smallness and the higher

per unit costs associated with production, infrastructure construction and training manpower (Briguglio et al. 2009, 5). States that adopt protectionist policies to counter the difficulties in diversification have a higher risk of encouraging growth in inefficient or uncompetitive sectors, spelling problems for future liberalization (Guillaumont 2010).

- d. Exposure to exogenous economic shocks. Because of their dependence on trade, small islands are more exposed to trade-related shocks, including slumps in demand, instability in world commodity prices, and international fluctuations of interest rates (Guillaumont 2010). The large changes in the terms of trade may trigger economy-wide effects (Santos-Paulino 2010).
- e. Exposure to exogenous environmental shocks. Small islands appear to be disproportionately vulnerable to natural disasters. About half of the countries that suffered the greatest number of natural disasters in the 1970s and 1980s were islands (Pelling and Uitto 2001). While disaster may also strike large nations, in a small island state, the effects of a disaster are expected to be greater the damage per unit of area and costs per capita are higher due to their small size. Increasingly, global warming and sea rise are also among small islands' environmental concerns, due to the potential for relatively large land loss, especially among low-lying islands (Briguglio et al. 2009, 11).
- f. Insularity and remoteness. While islands are by definition insular and isolated by their islandness, they may not necessarily be remote. Remoteness from other trading partners implies higher costs per unit for transport, uncertainty of supply and inability to respond efficiently to unexpected changes in demand (Pelling and Uitto 2001). However, some scholars contend that advances in communication and technology render these concerns moot (Read 2004).

Despite the wealth of theoretical reasoning on the negative effects of smallness and islandness, their relationship with growth is spurious. Using a sample of 157 countries – including 33 small states with less than 1 million people – Easterly and Kraay find that small states have higher than average income and productivity than larger states and share similar growth rates, even after controlling for a range of factors including continental location, oil and OECD status (2000). Per capita GDP growth rates are more volatile in smaller states because of greater exposure to terms of trade changes; still, these disadvantages of volatility are outweighed by the benefits of trade openness (Easterly and Kraay 2000). An IMF study on the effects of multilateralism also predicted the net benefits to outweigh losses due to the loss of trade protection in all but two countries - Dominica and St. Lucia (Mlachila, Cashin, and Haines 2010). The great number of economically successful small island states would seem to imply that smallness "is neither a necessarily nor sufficient condition for poor development performance" (Srinivasan 1986). Small states specializing in tourism and offshore financial services have performed particularly well; specializing in services as opposed to agriculture or manufacturing has become "an important vehicle to overcome size constraints" (Croes 2004). Tourism has been used as a growth strategy to achieve greater economic and development outcomes in several small islands, including those in the Eastern Caribbean, albeit with some questions about the sustainability of this strategy (Croes 2004).

Some scholars suggest that smallness, rather than being detrimental to growth, may be advantageous. Small states tend to have more heterogeneous, socially cohesive populations that allow for greater stability and adaptation to change (Armstrong and Read 2003; Kuznets 1960). If social fragmentation is considered to be an inhibitor to growth, than smallness and islandness, and the associated relatively higher social cohesion, are factors that work in these states' favor

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(Guillaumont 2010).

These divergent conclusions on smallness and islandness, despite *a priori* reasoning that these variables should affect growth and development, suggest that another variable might be at play. The concept of vulnerability has been used recently in literature to reconcile this conflict between a state's economic and environmental exposure and its growth and development. The next section explores this concept and its relation to small island states.

1.2 Concepts of Vulnerability and Resilience

Economic vulnerability refers to a country's risk of hampered development as a result of natural or external shocks (Guillamont 2010). This vulnerability arises from several factors considered "inherent and permanent" in a state, including:

- 1. Relatively high degree of economic openness
- 2. Dependence on a narrow range of exports
- 3. Dependence on strategic imports, with limited opportunities for import substitution
- 4. Insularity, peripherality and remoteness, and associated high transport costs and marginalization (Briguglio 2004, 4)

These factors are highly associated with small states, particularly SIDS. Small size requires islands to seek trade with greater necessity than their larger counterparts, and they are less able to take steps to mitigate their vulnerability, because small factor endowment may inhibit diversification and economies of scale (Briguglio et al. 2009). As a concept, vulnerability – and economic vulnerability in particular – is handy because it captures more adequately the reality of island developing countries and their unique institutional and structural handicaps (Briguglio et al. 2009). Using the concept of vulnerability, Briguglio suggests that states can exhibit a high level of vulnerability, regardless of their level of development (2004). The crux of the argument

is that GDP per capita is not in and of itself an accurate indicator of the level of development in SIDS; vulnerability, alternatively, captures the potential weaknesses and fragility of SIDS. States that are more vulnerable will experience greater export instability, terms of trade instability, shifts in investment, real exchange rate fluctuations, public finance effects – all of which may ultimately have a negative effect on the long-term average rate of growth (Guillaumont 2010). Economic vulnerability can have spillover effects on poverty reduction, due to the impact on growth or direct effects on the poor (Guillaumont 2010).

Dovetailing the concept of vulnerability is resilience. Briguglio et al. define resilience as the ability to recover from or adjust to change (2009). Resilience refers to the ability of an economically vulnerable country to cope with change. The concept of resilience helps to explain the "Singapore Paradox" – that is, why some small states do better than others, in spite of their economic vulnerability (Briguglio and Galea 2003). Resilience, unlike vulnerability, can be nurtured and developed by policy. Countries can adopt policies that mitigate – or exacerbate – their inherent vulnerabilities, thus affecting their resilience (Briguglio et al. 2009).

Briguglio (2004) utilizes a two-by-two typology to describe the interplay between vulnerability, resilience and

policies (Table 1). The matrix describes how states may be defined as vulnerable because of inherent features they cannot control – but states do have control over

Table 1: Resilience and Vulnerability Typology					
	Countries that adopt policies to withstand vulnerability	Countries that adopt policies that exacerbate vulnerability			
Inherently vulnerable countries	The "self made" scenario	Worst case scenario			
Inherently resilient countries	Best case scenario	The "prodigal son" scenario			

Source: (Briguglio 2004)

what actions they take in the face of such vulnerability. Encouraging resilience-building policies,

then, is something both countries and the international community can do to support the development of vulnerable states (Briguglio et al. 2009).

Concerns about vulnerability and development are reflected at the international policy level. Several indices attempt to operationalize vulnerability as a tool to allow policymakers to better understand the problems of developing countries in terms of the "structural constraints and root causes that perpetuate underdevelopment" (Guillaumont 2007). The Economic Vulnerability Index (EVI), used by the United Nations Committee for Development Policy since the 1990s to identify least developed countries (LDCs), evaluates vulnerability via seven indicators:

- 1. population
- 2. remoteness
- 3. export concentration
- 4. share of agriculture as part of GDP
- 5. homelessness owing to natural disasters
- 6. instability of agricultural production
- 7. instability of goods and services exports (Turvey 2007)

As a criterion for development, vulnerability provides for a broader assessment of the situation of developing countries. Vulnerability also addresses the variance observed in small island states by suggesting that small islands can be vulnerable but manifest relatively higher GDP per capita – specifically through the application of resilience-building policies. However, few studies have systematically examined the interplay of vulnerability, resilience-building policies and development, and whether some policies might do more to build resilience than others. The case of three Eastern Caribbean states, to which this paper now turns, provides fertile ground upon which to test this hypothesis.

1.3 The Erosion of Trade Preference in the Eastern Caribbean as a Natural

Experiment for the Vulnerability and Resilience Hypothesis

The Eastern Caribbean nations of St. Lucia, SVG and Dominica face all of the handicaps of smallness and islandness

identified by both scholars and the international community. The landmass of all three islands combined is smaller than Luxembourg (Land area (sq. km) 2010). St. Lucia boasts the largest

	St. Lucia	St. Vincent and the Grenadines	Dominica
Population in 2010	174,000	109,000	68,000
Size (sq. km.) in 2010	610	390	750
Hydrological and Meteorological ¹ Disasters (1980-2009)	11	8	8

Table 2: Selected Characteristics of Windward Islands

Source: (Environmental indicators: Natural disasters, Hydrological Disasters 2010; Environmental indicators: Natural disasters, Meteorological Disasters 2010; Land area (sq. km) 2010; Population total 2010)

population with less than 180,000 people (Population total 2010). In the last two decades, the islands have regularly faced exogenous economic and environmental shocks (Table 2).

The economic profiles of each country since the 1970s are also similar. Their colonial ties to Britain, coupled with trade preferences granted by first the UK and then the European Community, encouraged the proliferation of banana production from 1970s-1990s. The countries heavily relied upon the preferences granted to them by their former colonial sovereigns; without that protection, the bananas produced on smallholder farms in rugged territory would never be able to compete with the large, monoculture banana plantations in other Latin American countries. Upon erosion of the trade preference arrangement after a prolonged WTO dispute with the US and Latin American producers, banana production in the Eastern Caribbean collapsed.

¹ Meteorological disasters are defined as events caused by short-lived/small to meso-scale atmospheric processes (lasting minutes to days), e.g. tropical storms and extra-tropical cyclones. Hydrological disasters are defined as events caused by deviations in the normal water cycle and/or overflow of bodies of water caused by wind set-up, e.g. floods (Environmental indicators: Natural disasters, Hydrological Disasters 2010; Environmental indicators: Natural disasters 2010)

The effect of this erosion on these banana-producing states was predicted to be severe. Indeed, while the IMF noted that erosion of trade preferences in general is beneficial to all developing countries, it would very likely negatively affect the Windward Islands, including SVG, St Lucia and Dominica (Mlachila, Cashin, and Haines 2010).

Given their similar economic structures, dependency on export markets, susceptibility to preference erosion, risk of natural disasters, and demographic profiles, these three states provide a way of assessing whether concepts of vulnerability and resilience shed light on how small island states respond to exogenous shocks. Briguglio (2004) suggests that the reason some islands do better than others is because some islands implement better resilience-building policies. The deviation of Dominica as a better performing country, as seen in its rebound from the 2008 crisis, provides a way to test this hypothesis and address the previous discussed primary question of how Dominica managed to experience better economic and social outcomes versus its neighbors. Using Briguglio et al.'s conception of resilience, we would expect this positive performance to be a result of resilience-building policies that Dominica successfully implemented, while St. Lucia and SVG did not.

According to Briguglio et al., we expect to find these elements of resilience in the following policy areas: macroeconomic stability, microeconomic market efficiency, good governance, and social development (2006). By using a most-similar case study design (Gerring 2008), one can examine how and whether the variable of interest – resilience policies – as implemented in Dominica contributed to its social and economic development. The absence of such policy intervention in St. Lucia and SVG allow these countries to act as a "control group" in the analysis. St. Lucia, SVG and Dominica should all experience the detrimental effects of an exogenous shock as predicted by small island state theory; however, the intervention of

resilience-strengthening policies in Dominica could account for its observed greater adaptability.

1.4 The Gap Between Theory and Empirics

As described earlier in this chapter, the literature on small island states is somewhat contradictory. While small islands' unique characteristics are perceived to significantly constrain their ability to grow and develop, empirical studies suggest that neither size nor islandness is significant in determining a state's growth. This discrepancy paves the way for an alternative proposition on vulnerability: that the variance among SIDS' economic performance can be explained through their use of resilience-building policies.

Following Briguglio's hypothesis, the variance of Dominica as compared to two very similar neighbors is likely due to Dominica's ability to become a "self-made" resilient state, according to the vulnerability/resiliency typology (2004). While Dominica, SVG and St. Lucia are inherently vulnerable states, Dominica appears to have achieved greater resiliency through its adoption of policies that counteract vulnerability.

The analysis of Dominica and its two Caribbean neighbors addresses the gap between small island state theory and empirics by testing an alternative proposition: that resilience makes a difference. This thesis suggests that Dominica was more successful at introducing policies that mitigated its inherent vulnerabilities. It should be noted that this analysis does not disprove orthodox small island state theory that discusses the inherent challenges faced by such nations. However, by confirming the role of resilience-building policies in reducing inherent vulnerabilities, this paper suggests that vulnerability is also a key explanatory variable in island state performance, and that resilience-building policies may explain the variance in the development of SIDS – thus addressing a gap in small island state literature.

1. 5 Contribution to Small Island Developing States Literature

While smallness and islandness are much discussed in the literature, the implications of these structural characteristics are often examined only in terms of economic growth. While these studies may indeed be accurate in assessing growth itself, they fail to capture other – and perhaps more important – dimensions of development. Sen offers an alternative to this fixation on growth through the concepts of entitlements and capabilities that call attention to "what people can or cannot do, e.g. whether they can live long, escape avoidable morbidity, be well nourished, be able to read and write and communicate, take part in literary and scientific pursuits, and so forth" (Sen 1983). Literature that empirically explores small states in terms of these dimensions is surprisingly scant.

Incorporating the concepts of vulnerability and resiliency into SIDS research help to address this deficiency by fostering understanding of how small islands respond comprehensively to economic, environmental and social challenges (UNDP report 2002). Briguglio et al.'s conceptualization of economic resilience reflects this multi-dimensional approach: resilience is not just a factor of economic growth, but rather includes economic, institutional and social components (2009).

While issues of vulnerability have received sizable scholarly attention and recognition from international organizations as a development concern, there is a lack of a robust empirical understanding of economic vulnerability and its effects on SIDS (Read 2004). Issues of economic resiliency are similarly in need of additional empirical work. Although researchers have proposed an economic resilience index to compliment the economic vulnerability index already in use by the UN, the resilience index has yet to be adopted. Reasons for the paucity of empirical work may be due to the lack of reliable data from many small island states on non-

economic indicators, making quantitative studies on all but economic growth difficult to perform. Exploiting the "natural experiment" found in the Eastern Caribbean allows for a closer examination of issues of economic vulnerability and resilience in a systematic way, paving the way for future empirical research and understanding on these topics.

Chapter 2: Methodology and Theoretical Framework

As discussed in Chapter 1, part of the deficiency in small state literature is the reliance on economic growth to measure the effects of smallness, at the expense of other dimensions of development such as those noted by Sen (1983). However, the paucity of small state literature addressing development from additional dimensions likely arises from the lack of comprehensive and reliable data. Many small islands, including those in the Caribbean, lack capacity to gather reliable social data at regular intervals, although regional and international efforts hope to change this (Briguglio and Galea 2003; United Nations Development Assistance Framework 2011). At the present, however, a quantitative assessment of a large number of SIDS on poverty, education, health, or other indicators over a long time period would be difficult, if not impossible.

Given these data constraints, a case study design that focuses on a small number of SIDS over a limited time horizon is a useful tool to lend insight on the effects of size and islandness. As previously discussed, the natural experiment presented through the variance among three Eastern Caribbean states provides a way to examine additional explanatory variables and their impact on outcomes including, but not limited, to growth. It should be noted that this paper does not aim to disprove small island state theory, but rather its purpose is to add to the understanding of causal factors that affect growth and development among SIDS. This paper seeks to understand why three similar small Caribbean island states have experienced varying economic and social performance during the global economic downturn. In order to come up with an explanation for the variance observed, Dominica will be compared with St. Lucia and SVG using a most-similar case design, in which the cases selected are similar in all aspects except the dependent variable, resilience (Gerring 2008).

The selection of three Caribbean states also aids in overcoming the lack of reliable, comparable data over a long time period. As discussed in the previous chapter, these Caribbean states share a similar colonial heritage, and similar economic, geographic and demographic profiles prior to the erosion of trade preferences, which occurred at the same time in all three states. These similarities make it possible to isolate the variable of interest, resilience-building policies. The collapse of the banana industry engendered economic and social policies addressing the effects of this shock. Herein lies the natural experiment, as the countries did not pursue the same policies post-trade preference erosion. We can assume that the outcomes observed in the three countries can be attributed to changes that occurred post-trade preference erosion. We can also consider the Caribbean islands as representative of typical islands in the larger universe of SIDS. Like the majority of SIDS, Dominica, SVG and St. Lucia are middleincome developing countries with narrow economic bases, vulnerability to disasters, and high risk of exposure to exogenous shocks (Mlachila, Cashin, and Haines 2010).

This paper employs a qualitative and quantitative approach to examine development differences in the countries since trade preference erosion. While data collection on development issues have not been collected annually, each country has completed at least one country poverty assessments in the last decade with support from the Caribbean Development Bank using the same methodology and framework, including statistical analyses, participatory surveys and an institutional assessment. In addition, international organizations have conducted extensive analyses at the regional level through the Organization of Eastern Caribbean States (OECS) framework. These reports, among other documents and statistics culled from the IMF, World Bank, UNDP and secondary literature, shed light on development trends in each country and relevant policy changes.

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Before continuing with the analytical framework, important assumptions should be noted. First, this paper assumes that smallness and islandness matter in a state's development. While this assumption is challenged by some scholars (e.g. Easterly and Kraay 2000), a vast number of scholars and the international community recognize that SIDS face specific development challenges and needs. Briguglio et al. conceptualize these challenges as economic vulnerability arising from inherent structural characteristics and suggest that variance in development is a function of these inherent characteristics and policies that mitigate them (2006, 2009). The second assumption, then, is that some policies work better than others in vulnerable states, and policies that work well in larger states may not work well in small, vulnerable ones. While the idea that differentiated development solutions work better than a "one size fits all" development approach is nothing new, the idea that some policies may be more effective in a specific category of countries (within which there is much variation) rests on the assumption that small island states are structurally different enough to merit a special development approach but structurally similar enough that such approaches might be useable across the larger category. While this assumption makes intuitive sense, much more empirical research is needed to understand the phenomenon of resilience and whether development policies that foster resilience in SIDS carry distinct features.

This focus of this paper is on explaining the deviation observed in Dominica on the dependent variable, resilience, through a comparison with SVG and St. Lucia. According to Briguglio's typology of states, we would expect a state with inherent vulnerabilities, but also the ability to bounce back from shocks, to have resilience-building policies characteristics of other "self-made states" (2004). Briguglio et al. propose that economic resilience can be measured through the following dimensions:

- Good governance. The ability of an economic system to function properly relies on good governance. The rule of law, property rights, judicial independence and corruption are aspects of good governance and are mechanisms that serve as a buffer between economic and social chaos in the event of a shock (Briguglio et al. 2009, 9). In this thesis, World Bank indicators on governance are utilized to assess this dimension.
- 2. Macroeconomic stability. A state's fiscal position, price inflation and unemployment rate, and level of external debt are indicators of macroeconomic stability that are also highly influenced by economic policy (Briguglio et al. 2009, 7). A healthy fiscal position and level of external debt enables a country to better mobilize resources in order to withstand the effects of external shocks (Briguglio et al. 2006, 10). Similarly, balanced levels of inflation and unemployment mean that a state can weather an adverse shock without "excessive welfare costs" (Briguglio et al. 2006, 10). In addition to World Bank data on unemployment, inflation, fiscal deficit and external debt, this paper relies on analyses from the IMF and Caribbean Development Bank Country Poverty Assessments to explore this dimension.
- 3. Microeconomic stability. The ability of markets to allocate resources in the economy efficiently and rapidly to adjust to shocks is another indicator of strong resilience; on the other hand, market disequilibria that prevent these adjustments tend to create additional welfare costs. The size of government and the freedom to trade internationally are both policy-influenced indicators that suggest the ability of markets to allocate resources efficiency (Briguglio et al. 2006, 12). While Briguglio et al. suggest using the Economic Freedom of the World Index to examine these indicators, this particular index does not include the countries at hand; data from the Heritage Foundation is used instead.

4. Social development. A state's levels of human and social capital affect its ability to create collaborative responses in the face of adverse shocks (Briguglio et al. 2006, 14). The UN's Human Development Index captures some of these dimensions. The Caribbean Development Bank's Country Poverty Assessments also provide detailed data on other social indicators.

These four dimensions provide a useful framework to analyze policies that after the collapse of the banana industry could have made Dominica more resilient to exogenous shocks such as the 2008 global crisis. The next chapter uses empirical data from the three countries to test the resilience-building policy hypothesis.

Chapter 3: Empirical Analysis

To facilitate understanding of the policy context in the Eastern Caribbean prior to the global economic downturn, it is useful to examine the history of the Caribbean-EU banana trade and the events that created the need for urgent policy responses. The first section of this chapter charts the fall of the banana industry and the changing trading relationship between the Caribbean and the EU. The second section discusses the resilience of St. Lucia, SVG and Dominica prior to the global economic downturn in 2008. In the third section, the effects of the crisis in the three countries are explored. The fourth section analyzes the deviance in outcomes in terms of resilience-building policies according to Briguglio et al.'s framework (2006). In the final section, potential limitations are discussed.

3.1 Background: The Eastern Caribbean Banana Industry, Before and After

Throughout the 1970s and 1980s, the economies of St. Lucia, SVG and Dominica were dominated by one product: bananas. Buoyed by preferential licensing and market access granted by the UK and other European nations to their former ACP colonies, bananas in the late 1980s contributed to: 69 percent of export revenue in Dominica, 32 percent of GDP and 50 percent of employment; in St. Lucia, 37 percent of export revenue, 37 percent of GDP and 46 percent of employment; and in SVG, 42 percent of export revenue, 25 percent of GDP and 54 percent of employment (Nurse, Sandiford, and Stiftung 1995). Like in other small island states, relative abundance of a resource led to a narrow concentration in not only one sector, but one agricultural product.

This narrowness of exports emerged partly because of the development context in the Eastern Caribbean, which differed than that of its Latin American counterparts. While "dollar zone" bananas – produced less expensively in Latin American countries – evolved largely according to market forces, the banana industry in the Caribbean developed with the help of





protective regimes and government interventions (Anderson, Taylor, and Josling 2003). Thus, when a single European market emerged in 1992 and threatened ACP countries' access to preferential markets, the Caribbean lobbied hard for the continuation of preferred access to European markets; without the preferential treatment, their higher-cost bananas would not be competitive against an influx of cheap Latin American bananas. The creation of a New Banana Regime in 1993 replaced the old banana volume quotas, which limited the bananas that Latin American countries could export into Europe, with new tariff quotas that allowed countries to export bananas beyond their quota but only with higher tariff rates (Fridell 2011). This "managed" market allowed for the Caribbean countries to maintain their market position in Europe, despite a more expensive product (Sutton 1997, 11).

While this preferential treatment managed to survive criticism from the U.S. and Latin American countries in the GATT, the creation of the WTO produced a more binding framework for regulating trade disputes. In 1994, the US and several banana-producing Latin American countries requested a dispute settlement panel, claiming that the EU policy violated WTO rules because it allowed for preferential access for some banana imports, but not others (Alter and Meunier 2006). The WTO repeatedly ruled that the EU's banana regulations were

in violation of free trade agreements (Raynolds 2003). Not until 2001 was an agreement reached in which the EU would implement a new regime by 2006 based on a tariff-only system (Alter and Meunier 2006). The Economic Partnership Agreement between the EU and Caribbean states in 2007 ended the preferential, non-reciprocal trade access for Caribbean goods in the EU, opening the Caribbean economies to even greater foreign competition (Clegg 2008). This effectively annulled the special treatment the islands received from their former colonizers, leaving them to the whims of the multilateral trading system.

As expected, Caribbean banana exports declined precipitously. In SVG, banana exports dropped to 17,514 tons in 2007, down from 79,863 tons in 1992. The number of active farmers declined from 7,855 to 1,151, a drop of 85 percent (Fridell 2011). Across the three states, banana production and exports fell sharply during the WTO dispute settlement process, and continue to decline today (Figure 2).

These changes forced St. Lucia, SVG and Dominica to create policy options to offset losses in banana exports and foreign exchange, address adverse social impacts such as unemployment and poverty, and forge new pathways for economic growth. National policy decisions were also complemented by development aid from the EU, IMF and World Bank, among other entities.

These development decisions affected the ability of the islands to recover following the 2008 economic downturn. As the next section illustrates, different policies in different countries engendered different resilience responses.

3.2 Resilience in the Eastern Caribbean

According to Briguglio et al., economic resilience – the ability to bounce back from exogenous shock – may be measured through four dimensions: good governance, social development, macroeconomic stability and microeconomic stability (2009). In order to gauge the expected reaction to the exogenous shock of the crisis, this section examines each

dimension using 2007 indicators where possible.

Good governance. St. Lucia, SVG and Dominica are characterized as open democracies with political stability and high election participation, and they rank highly on multiple governance indicators. The public sectors, while large relative to their small size, are characterized by "well established organizational structures and institutional rules and regulations, respect for the rule of law, and a high degree of judicial independence" (Regional Partnership Strategy 2010). The three countries outrank their regional and income group peers on the 2007 World Governance Indicators, which measure voice and accountability, political stability, government effectiveness, regularity quality, rule of law and corruption; St. Lucia performs slightly better than the other islands (World Governance Indicators 2007). Still, all three countries would seem to have relatively strong and similar institutional resilience to exogenous shock, with St. Lucia ostensibly slightly stronger.

Social development. St. Lucia, Dominica and SVG benefit from a relatively high level of human development. On the 2007 Human Development Index, St. Lucia ranks 69th, Dominica 73rd and SVG 91st out of 182 countries (Regional Partnership Strategy 2010). While all three states are designated as upper middle-income countries, their poverty remains relatively high, ranging from to 28 percent in St. Lucia in 2008 to 38 percent in SVG in 2008 (Regional Partnership Strategy 2010). Lack of data makes it difficult to assess trends on the gap between rich and poor in these countries. However, the intensity of poverty appears to have diminished over the past decade, as noted in the significant reduction of indigence in St. Lucia and Dominica (Country Poverty Assessment - Dominica 2010; St. Lucia Country Poverty Assessment 2006). In Dominica, poverty among individuals dropped from 39 percent in 2003 to 26 percent in 2009 (Country Poverty Assessment - Dominica 2010). Overall, poverty in the Eastern Caribbean region appears to be "predominantly income- and employment- based, as opposed to rooted in lack of access to broad social services," a

testament to a history of investment in social and human capital (Organization of Eastern Caribbean States 2005).

From a comparative perspective, the three countries tend to outperform their counterparts in the region – and small island states overall. For example, they record higher average years of schooling versus the Caribbean region as a whole (UNDP Human Development Indicators 2012). Primary schooling is universal and secondary school enrollment is high, and with high gender parity. Life expectancy similarly outpaces that of the region and is comparable to OECD countries (Regional Partnership Strategy 2010). However, participatory surveys suggest that many individuals are struggling to make ends meet, particularly the rural poor who were hit hard by the loss of trade preferences (Country Poverty Assessment - Dominica 2010; OECS Human Development Report 2002 2002; St. Lucia Country Poverty Assessment 2006).

Based solely on the Human Development Index, the three countries display relatively high levels of human development. However, this positive ranking would appear to mask high unemployment rates, particularly among the young. Many individuals leave the countries to find better opportunities elsewhere. In SVG, more than one quarter of the labor force emigrated to OECD countries between 1970 and 2000 (St. Vincent and the Grenadines 2009). While remittances provide households with needed extra income, the countries' dependence on remittances creates yet another mechanism for an exogenous shock to bring adverse economic and social effects.

Overall, the similar levels of human development suggest that the three countries may be relatively more resilient than other states. However, high unemployment and poverty suggests that they may also share important fragilities that could be adversely affected via an economic shock.

Microeconomic stability. All three islands are characterized as "moderately free"

according to the Index of Economic Freedom in 2009, the first year they were included in the survey that measures rule of law, regulatory efficiency, limited government and open markets. St. Lucia led the group as the 39th freest economy in the world, while SVG and Dominica followed at 60nd and 70th, respectively (Miller and Holmes 2009). While this data post-dates the crisis, it appears that there have not been dramatic microeconomic policy changes since 2008, suggesting the rankings would have been more or less similar in 2007.

In this dimension of resilience, St. Lucia's open economy would be expected to make the quickest adjustment following an exogenous shock, although the difference between the states may be minimal.

Macroeconomic stability. In recent years, Dominica has diverged from SVG and St. Lucia in trends of fiscal position and external debt. While all three countries post high levels of external debt – in fact, the Eastern Caribbean is one of the most indebted regions in the world – Dominica will likely meet its debt reduction target of 60 percent of GDP by 2015, five years ahead of its goal (Regional Partnership Strategy 2010). That said, Dominica still has the highest debt-to-GDP ratio at 86.9 percent of GDP; SVG follows with 67.5 percent of GDP and St. Lucia at 66.2 percent of GDP. However, Dominica has posted a multi-year trend of reducing its debt-to-GDP ratio from a high of 128 percent in 2003, while SVG and St. Lucia's debt ratio is increasing (Regional Partnership Strategy 2010).

Inflation has also been variable in the region in recent years, with higher inflation and increases in consumer prices in SVG versus St. Lucia and Dominica (Regional Partnership Strategy 2010, Figure 4). Inflation accelerated in 2007 to more the double its 20-year historical average of 2-3 percent, although notably, this trend reversed in the latter half of 2008 (Regional Partnership Strategy 2010, 7). On the whole, however, inflation has been lower among these states than in the Caribbean region.

Public expenditures have increased in the past decade as governments have used

spending to stimulate growth following the collapse of the banana sector. Governments expanded primary fiscal deficits which was accompanied by borrowing from commercial markets in 2002-2006 (Regional Partnership Strategy 2010). Fiscally, Dominica was the only country to post a surplus in fiscal year 07/08 (2.2 percent of GDP), and only a modest deficit (0.8 percent of GDP) in 08/09 (Regional Partnership Strategy 2010). Overall, current account deficits in the Eastern Caribbean have been variable, increasing from 16.4 percent to 33.9 percent of GDP during 2004-2008 before dropping to 24.4 percent in 2009. The variance in public expenditures may be related to increases in the trade deficit due to higher imports following natural disaster reconstruction, increased consumer demand, and increased imports of investment goods (mostly for tourism) (Regional Partnership Strategy 2010).

Despite high human development indicators and a GDP per capita classified as "upper middle income" by the World Bank, unemployment remains relatively high and persistent in the three islands, particularly among youth, despite gains in recent years. Unemployment stood at 13.9 percent in Dominica in 2008, down from 25 percent in 2003 (Country Poverty Assessment – Dominica 2010). In St. Lucia it was 16.8 percent in 2008, while 21 percent in SVG were estimated to be unemployed in 2007/2008 (Regional Partnership Strategy 2010). Anecdotal evidence suggests that there are growing numbers of "jobless" youth, or young people that are neither working or in school. This is particularly troubling as this heightens their risk of becoming involved in crime (Regional Partnership Strategy 2010).

This macroeconomic snapshot suggests that during the time prior to the crisis, problems of large external debt loads, fiscal imbalances and unemployment were weaknesses in the islands' ability to bounce back from exogenous shock. A high amount of debt and public spending suggests that when states are hit with an exogenous shock, their ability to mitigate the impacts of that shock through counter-cyclical fiscal policy are limited (Regional Partnership Strategy 2010). Without sufficient fiscal maneuvering space, the role government

can take to limit adverse effects of poverty and unemployment is constrained. In this respect, Dominica's ability to reduce its debt-to-GDP ratio could be considered a factor of resilience. The next section examines the islands' response to the global economic crisis.

1.3 Post-crisis Outcomes

The Eastern Caribbean region was substantially affected by the global economic downturn in 2008. In 2009, output declined in all OECS states except Dominica, and debt ratios worsened (Regional Partnership Strategy 2010). SVG and St. Lucia's debt level has increased since the crisis, owing to contractions in output and the widening of the primary deficit. Growth slippage in both countries reflects crisis-related decreases in two main sources of growth – tourism and FDI-related construction – and lack of diversification has exacerbated the impacts that uncertainty in advanced countries levied on the islands (St. Vincent and the Grenadines 2011).

While the lack of reliable data make it difficult to assess the impact of the crisis on poverty and unemployment, it is likely that as in other Caribbean countries, the Eastern Caribbean islands are experiencing increased poverty despite being classified as upper middle income countries, a result of increasing food and fuel costs, decreased remittances and increased unemployment (Regional Partnership Strategy 2010).

In St. Lucia and SVG, the crisis and associated downward pressure on the tourism sector fueled the contraction in GDP. Declines in FDI, remittances, construction and agriculture, notably a decrease in banana production, also contributed to slower growth. In SVG, real GDP growth contracted by 0.6 percent in 2008, followed by 2.3 percent and 1.8 percent contractions in 2009 and 2010, respectively, due to the effects of the crisis and a subsequent drought and hurricane (St. Vincent and the Grenadines 2011). In St. Lucia, economic activity contracted 5.2 percent in 2009, owing to the decline in demand for tourism, its primary export activity, and tourism-related construction (St. Lucia: Staff Report 2010).

Effects on SVG and St. Lucia deficits were similarly significant. In St. Lucia, the overall deficit quadrupled from 1.8 to 7.8 percent of GDP, while the primary balance deficit expanded to \$111 million EC compared to a \$40 million surplus in 2008 (Regional Partnership Strategy 2010). Reversing a trend toward debt reduction, the public debt-to-GDP ratio grew to 75 percent of GDP compared to 66 percent in 2008 (St. Lucia: Staff Report 2010). Continuing a decades-long trend, total public debt in SVG increased in the wake of the crisis, reaching 66.8 percent of GDP in 2010 – compared with 43.3 percent of GDP in 1996 and 55.7 percent in 2007 (St. Vincent and the Grenadines 2011).

In SVG and St. Lucia, the banana industry continues to deteriorate as a result of trade preference erosion. EU support for diversification and the transition from banana agriculture has been dispersed in amounts smaller than anticipated (St. Vincent and the Grenadines 2011). Two main sources of growth – tourism and FDI-related construction – were significantly exacerbated by the continued slowdown in advanced countries.

Unlike its counterparts, Dominica recorded growth during and after the crisis, along with debt reduction. The economy grew 1.8 percent in 2008, following 3.2 percent growth in GDP in 2007. In 2009 it was the only OECS country to experience growth, due to increases in the construction sector and a rebound in agriculture as the banana industry recovered from Hurricane Dean in 2007. However, like in SVG and St. Lucia, tourism revenues also shrank, a reduction worth 3.6 percent of GDP (Regional Partnership Strategy 2010).

All three countries requested loans from the IMF's Exogenous Shock Funds to offset declines in revenues and mitigate the impact of the shock on the most vulnerable. Funds ranged from St. Lucia's \$10.65 million disbursement in 2009 to Dominica's \$5.1 million disbursement in 2010 (St. Lucia: Request 2009). Despite St. Lucia's high-performing economy prior to the crisis, the IMF noted that the state's extreme reliance on tourism for tax revenue, foreign exchange reserves and employment meant that "damage to the economy

Figure 2: International tourism receipts



from the crisis has been widespread" (St. Lucia: Request 2009). In the process of transition from an agriculture-based to a service-based economy, the country has become reliant on tourism for three-fourths of export earnings, while visitor spending provides one-third of GDP (St. Lucia: Request 2009) (Figure 1). Development of the tourism sector is almost entirely dependent on FDI. Public debt increased from 66 to 75 percent between 2008 and 2009 (St. Lucia: Staff Report 2010).

Both the World Bank and IMF have noted Dominica's apparent resilience to more severe effects following to the economic slowdown. The IMF notes that the "crisis had a relatively mild impact on Dominica" (Dominica: Request for Disbursement 2009). This contrasts the crisis' "severe impacts" on the rest of the members of the Eastern Caribbean Currency Union (Dominica: 2010 Article IV Consultation 2010). In the two years following the downturn, Dominica's government maintained capital spending at high levels moderated the impact of the crisis (Dominica: 2010 Article IV Consultation 2010). The government's response included repairing critical infrastructure with the help of donors and providing assistance to those who lost earnings due to the crisis (Dominica: Request for Disbursement 2009).

In summary, it would appear that Dominica exhibited relatively greater resilience to

the exogenous shock of the global financial crisis, as evidenced by its continued growth rates and ability to maintain capital spending and social nets while reducing debt. Unlike its counterparts, Dominica absorbed the shock better and bounced back quicker – characteristics of economic resilience.

1.4 Resilience-building Policies as an Explanatory Variable

Dominica, St. Lucia and SVG share many characteristics: historical backgrounds, vulnerabilities and resiliencies in 2007. However, Dominica diverges from St. Lucia and SVG in its pursuit of a strong fiscal position and debt reduction. These fiscal policies seem to have created a shock-absorbing buffer that the other countries could not count on, thus increasing their debt load and further constraining their ability to implement counter-cyclical policy measures.

Dominica's fiscal adjustment measures included introducing a VAT, lowering spending and restructuring its debt in 2004-2005 – measures which have allowed the public debt-to-GDP ratio to fall quickly and sharply from 128 percent in 2003 to 84.5 percent in 2009 (Regional Partnership Strategy 2010). While SVG took advantage of a debt write-off from Italy in 2007 equivalent to 10 percent of GDP, it is notable that public debt in both SVG and St. Lucia appear to be on upward trajectories, while Dominica is scheduled to meet the goal of debt reduction to 60 percent debt-to-GDP by 2015, five years ahead of schedule. These policies created the fiscal space for the government to respond to the downturn with a moderate stimulus package (Organization of Eastern Caribbean States 2005). Rising debt, on the other hand, increases the vulnerability of the economies to external shocks via exchange rate fluctuations, as even domestic debt is pegged to foreign currencies.

Dominica also deviates from its counterparts in its economic makeup. It is less dependent on tourism that SVG and St. Lucia, partly because it is a less traditional tourist destination, marketed as a rugged eco-tourism destination versus the white sandy beach

destination that characterizes St. Lucia and SVG. The sector has grown slowly, and Dominica has worked to diversify its economy through nonbanana agriculture, soaps and oils. The banana sector, like in St. Lucia and SVG, has almost entirely converted to niche exports of Fair Trade and organic bananas, allowing limited numbers of banana producers to continue in agriculture, albeit with some difficulties owing to the stringent certification standards (Fridell 2011). Unlike in St. Lucia and SVG, however, Dominica's GDP growth in the midst of the crisis was partially attributed to a rebounding banana industry following a 2007 natural disaster that decimated production – however, exports were still lower than from 2006 levels. Meanwhile, in St. Lucia and SVG, production declined during the crisis, perhaps part of the ongoing trend in declining numbers of farmers and output. While the causes of these fluctuations in production may be difficult to trace back to policies, the ability of Dominican banana production to rebound so soon after the 2007 disaster could be perceived as another testament to the country's resiliency, and the government's ability to navigate external shocks more effectively.

This analysis suggests that, as Briguglio (2004) predicts, differences regarding resiliency may be attributed to resilience-building policies. In the case of these three island states, the ability of Dominica to feel fewer effects from the global downturn and bounce back more quickly may be attributed to Dominica's policy decisions in the past decade to improve its fiscal position and lower its debt. These policy decisions seemed to give the government more maneuvering ability to weather the storms of exogenous shocks through counter-cyclical policies and attention to the social welfare net. Thus, policy interventions could explain the variance among similar small island states, despite the *a priori* reasoning that SIDS are more vulnerable to adverse effects of exogenous shocks.

1.5 Limitations

While this analysis describes one example of resilience-building policies influencing

the outcome of an economic shock, it should be noted that, while the country comparison helps control for some variables, it is still difficult to purport with certainty that the fiscal policies of Dominica gave it an advantage. While the three states face on average a high rate of natural disasters, their occurrence does not always affect all islands at the same time, and it is possible that interplay of other factors such as disasters could have an impact on their ability to grow resilience.

Furthermore, the high dependence of the other economies on tourism relative to Dominica could be due to consumer tastes rather than any particular policy success or failure on the part of the islands. Indeed, tourism allowed SVG and St. Lucia to grow at a faster rate than Dominica in the 2000s, even as their GDP contracted at a faster rate during the crisis. This suggests there may be tradeoffs between economic growth and resilience. Dominica is also projected to have slower growth post-crisis than SVG and St. Lucia, and all of the Eastern Caribbean is predicted to have a slower overall recovery than its Latin American counterparts (Regional Partnership Strategy 2010). Indeed, while Dominica bucked the trend and posted moderate growth and stability throughout the crisis, it cannot be considered the "Singapore" of the Caribbean. Rather, its case provides limited evidence that a history of smart fiscal policies can made a difference in a country's ability to recover from exogenous shock.

Chapter 4: Policy Implications

The case of St. Lucia, SVG and Dominica demonstrate a "development paradox" – that is, most of the countries have relatively high levels of GDP per capita, stability, and human development, but yet poverty and unemployment remain persistently high (Assessment of Development Results 2009). Briguglio (1995) suggests that the exposure to adverse shocks, or economic vulnerability, explains this paradox and is particularly associated with small island states. The analysis of the three islands' responses to the global economic downturn suggests that indeed, small states may suffer disproportionately for their vulnerabilities when faced with an exogenous shock, particularly because of their embeddedness in sectors that are sensitive to business cycle changes in advanced countries.

However, the ability of Dominica to avoid a severe contraction in GDP and continue to reduce its debt-to-GDP ratio, while implementing a stimulus package, suggests that small states can enact policies to mitigate the impacts of exogenous shocks. While much more empirical work is needed to extend the policies used in Dominica in the last decade to all small states, what is apparent is that resilience-building policies do make an impact on outcomes following shocks. This finding has critical importance for international organizations and central governments themselves. As opposed to Easterly and Kraay's finding that small states need no differentiated development advice (2000), the experience of Dominica suggests that policies aimed at improving a state's ability to respond to exogenous shock are appropriate and effective measures. As such, addressing vulnerabilities and strengthening resilience should be key elements of development aid in not only these three islands, but also SIDS in general.

These findings also suggest that small island developing states are in need of a more

nuanced classification that depicts their particular context. While the ACP agreements recognized the vulnerabilities of small island former colonies, no similar differentiated treatment has emerged in the wake of trade preference erosion. The UN has a special SIDS classification, but this recognition has not developed into substantial special treatment per se and is stymied by a lack of clear and bright definition of a small island developing state. The WTO Doha rounds ruled out the creation of a new sub-category of member states apparently because of this definitional issue (UNCTAD 2004).

A narrower classification would help in allowing international organizations to direct development assistance more adequately and help assuage some of the persistent development issues in the Eastern Caribbean SIDS – namely, high unemployment and poverty. The use of Briguglio's economic vulnerability index (1995), and the further development of a economic resilience index, could aid in the creation of a more adequate classification for SIDS and contribute toward a better understanding of the developmental realities of these states.

Conclusion

This thesis analyzed the unexpected resilience displayed by Dominica in the wake of the global economic downturn compared to two very similar small island states, St. Lucia and SVG. While small island states are expected to be highly vulnerable to adverse shocks, the surprising performance of Dominica – the only state to increase output during the crisis – suggests that other factors associated with smallness and islandness may affect the severity of an exogenous shock on such states. Dominica could be considered a "self-made" state according to Briguglio's typology (2004): despite the detrimental effects of trade preference erosion, it appears that Dominica has emerged in the intervening years as the most resilient state among the three. While still experiencing inherent vulnerabilities, Dominica seems to have developed the ability to bounce back from shocks.

Utilizing the framework for vulnerability and resilience developed by Briguglio et al. (2009), the resilience of Dominica was traced to economic policies put into place years before the crisis that were aimed at stabilizing the economy through debt restructuring, introduction of a VAT and prudent spending. These measures have allowed Dominica to rapidly reduce its debt burden, freeing up more fiscal maneuvering space to respond to exogenous shocks. Indeed, the state's ability to reduce its debt-to-GDP ratio while continuing a high level of capital spending during the crisis suggests its ability to implement counter-cyclical fiscal policies and prevent hardships among the poor and vulnerable.

The importance of resilience-building fiscal policies lends empirical weight to Briguglio et al.'s work on resilience. Dominica, St. Lucia and SVG are a "development paradox," countries that exhibit high human capital yet have persistently high poverty and unemployment (Assessment of Development Results 2009). In the case of small island states,

such outcomes may have to do with booms and busts associated with smallness and islandness, and such growth volatility creates negative social outcomes. While more empirical studies are needed to confirm the association between resilience-building policies and performance in an exogenous shock, the case of Dominica suggests that states can indeed buffer their exposure to adverse events. This suggests that international organizations need a narrower SIDS classification would aid international organizations in directing development assistance more adequately and help assuage some persistent development issues through specialized treatment for small island states.

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