

COMPETITIVENESS STRATEGIES FOR SMALL STATES

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LAYOUT OF THIS PRESENTATION

- ▶ **Section 1** of this presentation gives some information about Malta
- ▶ **Section 2** introduces the issue of competitiveness in small states
- ▶ **Section 3** argues that competitiveness is of major concern for small states, given that they are highly dependent on international trade
- ▶ **Section 4** presents some brief case studies on experiences of small states.
- ▶ **Section 5** deals with the social aspects of competitiveness
- ▶ **Section 6** outlines the major elements of a competitiveness strategy for small states.

Some Facts about the Malta

Malta is one of the ten states that joined the European Union in May 2004. This was a momentous event for Malta, not least from an economic perspective.

The Maltese economy comprises merely 0.04% of the economy of the EU. It has one of the lowest rates of unemployment in the Union. Its per capita income level is about 80% of the EU average, and is therefore one of the highest among the new member states. It depends highly on exports and imports (about 50% of total final sales).

2. THE ISSUE OF COMPETITIVENESS

During the past two decades or so, competitiveness received considerable attention in academic and policy circles reflecting in part the insufficiencies of short-term oriented demand management approaches in macroeconomics and the consequent need for a better study of supply-side dynamics.

The literature on competitiveness has grown considerably and Governments of developed as well as of developing countries have placed competitiveness at the centre of their development agenda.

The EU Lisbon Agenda in the early 2000 stated the EU wants to be "the most competitive and dynamic knowledge-driven economy by 2010", which was not met, but it is still a major EU objective. The US, Japan, China, India, Mexico, and other countries are equally passionate about the need to compete in the global stage.

This paper is based on the notion that competitiveness has a significant role to play in the development of small states, particularly in the current wave of globalisation. In a globalised free trade context, competitiveness is the means for firms as well as for countries to survive and thrive. This is because the alternative to competitiveness, namely protection from competition, has time and again proved to be futile, as it results in inefficiencies and poor returns. It is only through enhanced competitiveness that living standards can be maintained and upgraded over time.

3. COMPETITIVENESS AS A MAJOR ISSUE FOR small states

Competitiveness is a special issue for small states because of their inherent very **high dependence on international trade (exports and imports)**. Their small domestic markets necessitates that a large share of output of goods and services be sold in the export markets. Their limited availability of natural resources, necessitates that a relatively high proportion of the country's expenditure is serviced by imports.

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Competitiveness is Essential for Small States

The promotion of competitiveness is therefore crucial for small states.

This is the main message that is being conveyed by this presentation.

Characteristics of small states

Small states are characterised by a number of special features, which include the following:

- ▶ High dependence on economic conditions in the rest of the world.
- ▶ Inability to influence international prices.
- ▶ Limited ability to exploit economies of scale.
- ▶ Limitations on domestic competition.
- ▶ Limitations on diversification possibilities.
- ▶ Insularity.
- ▶ Problems of public administration.

These factors **exposes small states to external shocks**

Is Smallness an Advantage?

Some small states have done remarkably well, prompting some analysts to argue that smallness may actually be an advantage, but a deeper analysis would indicate that the economic success of some small states resulted in spite of and not because of their size.

► In particular, economic smallness increases the proneness to external shocks over which a country has no control rendering it economically **vulnerable**.

The Globalisation Process

The characteristics of small states just outlined render the growth patterns of small economies strongly influenced by developments in the international economy, and in recent years this has been exacerbated by the globalisation process.

This process has led not only to improvements in technology and in the means of communication, but also to deliberate economic policies aimed to achieve higher rates of growth. An approach commonly adopted is the liberalisation of markets.

Opportunities and Costs of Globalisation

It is however also recognised that these **opportunities come at a cost**, associated mostly with greater risk and uncertainty in economic performance, as international economic developments over the past five years have shown.

Integrated markets for goods and for capital transmit developments from larger economies to the rest of the world, as was the case in recent US economic activity when its deceleration affected the global economy leading for the first time in recent history to a synchronised deceleration in all of the major economies in the world.

Limited Options for Small States

These considerations leave no option for small states but to continuously strive to improve their competitiveness if they are to succeed in swimming, rather than sinking, in the face of international competition, given the disadvantages associated with small size and insularity.

Exports, imports and investment flows are all affected by competitiveness.

Strategic Options

A number of strategic options are available to small states in this regard.

Protectionism. One route could be to shelter the economy from the shocks of international markets and pursue an inward-looking growth policy. Numerous experiences of protectionist policies have shown that this course of action only serves to promote inefficiencies that would defeat the original purposes for which it was instituted.

Demand side policies. An alternative route would be to pursue growth led by fiscal policy, through an expansion in expenditure or a reduction in taxes. A disadvantage associated with this option is that government expenditure is likely to stimulate aggregate demand without necessarily expanding the economy's supply capabilities, leading to inflationary pressures and/or an increase in imports. It also creates gives rise to unhealthy public finances.

Such policies could be appropriate if the economy were in a situation of severely depressed demand relative to its supply capabilities.

Not Good Options

It is therefore argued that protectionist and exclusively demand-side policies are not appropriate for the promotion of economic development of small states.

Best Option: Competitiveness

The only viable option for small states to promote economic development is to perform successfully in the international market-place. This, in turn, requires a concentrated focus on maintaining and improving the country's competitiveness.

This is by no means an easy task. It is a challenge that involves making choices, some of which might be difficult to absorb in the short run. Yet, it is the economic imperative on which the economy's future success and livelihood depends.

5. CASE STUDIES OF COMPETITIVENESS OF small states

The issue of competitiveness in small states has been extensively treated in Briguglio and Cordina (2004) *Competitiveness Strategies for Small States*, which carried a number of case-studies on this issue. Some salient aspects of competitiveness in small states are reviewed in this section.

Failures

- ▶ Market distortions and macroeconomic instability in Fiji and Jamaica (Jayarman, Reddy, Wint)
- ▶ Too much dependence on trade preferences in Belize (Gomez)
- ▶ Excessive government expenditure in Malta (Briguglio and Cordina)
- ▶ Poor Governance in Fiji and Jamaica (Reddy, Wint)
- ▶ Unbalanced development in Trinidad –Natural Resources Endowments (Pantin)
- ▶ Dominica – neglecting the social aspect of competitiveness (Letang)
- ▶ Small states as LDCs (Marong, Moletsane and Masia)

Successes

- ▶ Far sighted fiscal and monetary policies: Singapore as a success story (Bhaskaran)
- ▶ The Institutional set-up for competitiveness in Mauritius, Malta, Cyprus and Bahrain (Treebhoohun, Brigugli, Mavris, Suliman)
- ▶ Benefits of regional integration: Malta, Cyprus, Slovenia and (Briguglio, Mavris, Kovacic)
- ▶ Successful transformation: Slovenia (Kovacic)
- ▶ Promoting productivity: Barbados (Downes)

6. A PROPOSED COMPETITIVENESS STRATEGY FOR small states

Competitiveness is a multi-faceted phenomenon, which spans economic, social, political and international dimensions and involving all the players in the economy.

Competitiveness cannot in the long run be sustained unless all the dimensions contributing to it are properly addressed.

Conflicting Priorities

It is however often the case that these dimensions result in **conflicting priorities**, especially in the short run where, for example, the attainment of social objectives may conflict with economic efficiency considerations.

The achievement of competitiveness across all these dimensions in a sustainable manner will depend upon ten golden rules that could result in win-win situations for all economic players in the longer term.

Ten Golden Rules

These golden rules, inspired by the World Competitiveness Yearbook methodology published by the Instituted of Management Development in Geneva (IMD, 2001), are:

1. A stable and resilient macroeconomic structure.
2. An adequate and predictable legislative environment.
3. Adequate infrastructural services.
4. Investment in human capital through education.

Ten Golden Rules (Cont)

5. Innovation, research and development.
6. Quality, speed, efficiency and transparency in public administration.
7. Balancing wage levels, productivity and taxation.
8. Preserving the social fabric and maintaining social cohesion.
9. Exploiting Market Opportunities.
10. Fostering investment attractiveness.

► The golden rules for competitiveness thus cover virtually all aspects of economic policy and require inputs from all social partners.

► They also highlight the fact that economic objectives should not be blindly pursued while incurring excessive social costs, as these are ultimately very detrimental to competitiveness as to fostering ownership of the social partners with regard to government reform policies.

5. THE SOCIAL ASPECTS OF COMPETITIVENESS

The Social Aspect of Competitiveness

Briguglio et al (2005) argue that social cohesion is important in its own right, but it is also indispensable for a country to sustain its competitiveness and its international image as a suitable and stable place where to invest and conduct business.

The welfare system plays an essential role in competitiveness by ensuring basic rights and benefits to workers, assisting more vulnerable segments of society and combating poverty. They also argue that the success of a competitiveness strategy depends on the extent to which it finds support from all the social partners, including employee unions.

This aspect of competitiveness is amply treated by Letang (2004). She argues that although competitiveness is an economic imperative for Dominica, calling for sound macroeconomic policies, due regard should be assigned by the government and the IMF to the social aspects of economic development. She explains how the IMF stabilisation programme in Dominica may have had negative social side effects, and that the government, in consultation with the IMF, should have ensured that all the stakeholders were parties to these consultations and their recommendations given a credible hearing.

Win-Win Situations

In spite of the complexity and far-reaching domain of these rules, they highlight the importance of two objectives that carry the promise of a win-win outcome with regard to economic, social and environmental concerns.

- ▶ One is the need to achieve efficiency in the allocation of resources.
- ▶ The other is the need to promote economic activity based on knowledge and innovation.

Difficult Task for small states

The constraints arising from small size and insularity, outlined above in this presentation, render the tasks of small island jurisdictions somewhat difficult, mainly due to:

- ▶ the problem of expenditure indivisibilities (leading to high per capita costs of government and other overhead costs),
- ▶ limited ability to reap economies of scale, and relatively high transport costs.

But Indispensable

However, the ten golden rules which are laid out in this section however still apply, and apply **a fortiori** , given that small states tend to depend heavily on exports and imports, due to the very small size of the market and lack of natural resources.

7. CONCLUSION

This paper argues that competitiveness is a prerequisite for the **improvement of living standards** of the people of small states, more so than is the case of larger territories, given the high degree of dependence of small states on international trade.

Competitiveness calls for Change

Competitiveness is not something static. It calls for change, especially that related to loss of jobs and creation of new ones, as low productivity jobs get replaced by higher-productivity ones, possibly in new areas of business. This continuous change calls for continuous learning, upgrading of skills and innovation. Such a process is of course incompatible with complacency.

Flexibility is a Must

An important point that emerged from this paper is that in small states resources are limited and therefore the attraction of new productive business will find it difficult to access idle resources, but will instead induce labour mobility and change.

Such transformation requires **flexibility** in the attitudes of the social partners, including employee unions, and an efficient public administration, committed to uphold competitiveness.

The Government has a Role to Play

Competitiveness is to a large extent **an enterprise issue**, and it is the individual company at the micro level that needs to be competitive, in order to enhance national competitiveness.

► However the public sector has a major role to play, not least of which by taking a lead in place competitiveness on top of the policy agenda, and taking the lead in removing business bottlenecks when these occur.

THE END

Thank you for your attention