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SMALL STATES AND ECONOMIC RESILIENCE: LESSONS FOR LARGER DEVELOPING COUNTRIES

Lino Briguglio¹

Abstract. Given the high degree of vulnerability to external shocks, which characterise the economies of small states, it could have been expected that these states, more than any other group of countries, were to be highly adversely affected by the current turmoil. In reality, many small states have not been heavily impacted in their financial sector, the main reason being that these states tend not to be highly exposed to the main factors that led to the financial crises including excessive reliance on wholesale financing and collateralised debt obligations. However, many small states have been affected by the spill-over effects of the crises, which led to the global recession, and are experiencing, amongst other things, reductions in remittances (a major source of foreign exchange inflows in many small states), drops in income from tourism activity and other exports and a slowdown in construction activity linked to the tourist sector. However, it is likely that many small states will take appropriate action to mitigate the effects of such shocks. In a study by Briguglio et al (2009), it was found that many small states have developed a high degree of economic resilience, resulting from good economic governance, leading them to register relatively high GDP per capita, even though they are very exposed to external shocks. The paper will investigate whether there are lessons which larger developing states can learn from this reality.

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1. INTRODUCTION

Given the high degree of vulnerability to external shocks which characterise small states, it could have been expected that these states, more than any other country grouping, were to be highly adversely affected by the 2008-2009 financial turmoil.

In reality, however most small states were not heavily impacted in the financial sector, the main reason being that these states tend not to be highly exposed to the main factors that led to the crises, including excessive reliance on wholesale financing and collateralised debt obligations. However, many small states have been affected by the spillover effects of the crises, which led to the global recession, and are experiencing, amongst other things, reductions in tourist inflows, remittances and construction linked to the tourist sector. Again here, the impact on many small economies is not likely to be as large as is the case in many larger economies. In a study by Briguglio et al (2009), it was found that many small states have developed a high degree of economic resilience, resulting from good economic governance, leading them to register relatively high GDP per capita, even though they are highly exposed to external shocks. The paper will investigate whether there are lessons that larger developing states can learn from this reality.

The paper is organised as follows. Section 2, which follows this introduction, deals with the conceptual framework relating to economic vulnerability and resilience. Section 3 explains how economic resilience can be measured through an index, and how this index can be used to classify countries in terms of the vulnerability/resilience nexus. Section 4 then discusses the main difference between the eight best-performing small states and the eight worst-performing large states in terms of economic resilience, and, on the basis of this discussion, attempts to draw some lessons for large states. Section 5 concludes the paper by some policy recommendations.

1. Vulnerability and Resilience: Conceptual Framework

Many small states² manage to generate a relatively high GDP per capita when compared to other developing countries³ in spite of their high exposure to exogenous economic shocks. This would seem to suggest that there are factors which may offset the disadvantages associated with economic vulnerability. This phenomenon was termed by Briguglio (2003) the “Singapore Paradox”, referring to the reality that although Singapore is highly exposed to exogenous shocks, this small island state has managed to register high rates of economic growth and to attain high GDP per capita. This reality can be explained in terms of the ability of Singapore to build its resilience in the face of external shocks.

1.1 Economic Vulnerability

Economic vulnerability is well-documented in the literature from the conceptual and empirical viewpoints (see for example Briguglio, 1995; Briguglio and Galea, 2003; and Atkins et al., 2000, Farrugia, 2004). Most studies on economic vulnerability provide empirical evidence that small states, particularly island ones, tend to be characterised by

² In this study, the terms “state” and “country” are used synonymously and interchangeably, however the term “state” mostly refers to small states and the term “country” mostly refers to large ones. The size of countries is measured in terms of population. In this paper a small state is defined as one with a population of about 1.5 million or less, a definition similar to those adopted by the World Bank and the Commonwealth Secretariat.

³ This finding is reported in many studies. See for example Briguglio (1995).

high degrees of economic openness and export concentration. These lead to exposure to exogenous shocks, which could constitute a disadvantage to economic development by magnifying the element of risk in growth processes (Cordina, 2004).

Such vulnerability stems from a number of inherent and permanent economic features, including (i) a high degree of economic openness, which renders the economy particularly susceptible to economic conditions in the rest of the world; (ii) dependence on a narrow range of exports, giving rise to risks associated with lack of diversification; and (iii) dependence on strategic imports, in particular energy and industrial supplies, exacerbated by limited import substitution possibilities.

Small size leads to additional constraints, such as a limited ability to reap the benefits of economies of scale, relatively high infrastructural, administrative and other overhead costs due to the indivisibility⁴ problem, and the prevalence of natural monopolies and oligopolistic structures, which lead to high costs to consumers. Small size also creates problems associated with public administration mostly due to the fact that many government functions tend to be very expensive per capita when the population is small, again due to the indivisibility problem.

1.2 The Meaning of Economic Resilience

Briguglio et al (2009) define economic resilience as the policy-induced ability of an economy to recover from or adjust to adverse exogenous shocks and to benefit from positive shocks.⁵ The term is used in two senses by Briguglio et al (2009), respectively relating to the ability to (i) recover quickly from a shock; and (ii) withstand the effect of a shock.

Ability of an economy to recover from the effects of adverse shocks. This is associated with the flexibility of an economy, enabling it to bounce back after being adversely affected by a shock. This ability will be severely limited if, for example, there is a chronic tendency for large fiscal deficits. On the other hand, this ability will be enhanced when the economy possesses discretionary policy tools which it can utilize to counteract the effects of negative shocks, such as a strong fiscal position, which would entail that policymakers can utilise discretionary expenditure or tax cuts to contrast the effects of negative shocks. This type of resilience is therefore associated with “shock-counteraction”.

Ability to withstand shocks. This relates to the ability to absorb shocks, so that the end effect of a shock is neutralised or rendered negligible. This type of resilience occurs when the economy has in place mechanisms to reduce the effects of shocks, which can be referred to as “shock-absorption”. For example, the existence of a flexible, multi-skilled labour force could act as an instrument of shock absorption, as negative external demand shocks affecting a particular sector of economic activity can be relatively easily met by shifting resources to another sector enjoying stronger demand.

The issue of resilience building is important for small states in view of the fact that such states tend to be inherently economically vulnerable, as already explained. In an analysis of the economic performance of small states, it is important to distinguish between

⁴ The reason for this is that overhead expenses cannot normally be downscaled in proportion to the number of users.

⁵ Most dictionaries define resilience in terms of the ability to recover quickly from the effect of an adverse incident. This definition originates from the Latin *resilire* ‘to leap back’.

vulnerability considerations and resilience factors. For example, some studies argue that small economic size presents an economic advantage on the basis of simple correlations between small size and indicators of economic performance, such as GDP growth and GDP per capita. However a proper analysis of the relationship between size of countries and economic performance should factor in control variables, such as good economic governance. This paper is built on the premise that the relatively good performance of small states is certainly not due to small size, but is attributed to nurtured economic resilience. In other words, such performance by small states is not because, but in spite of, their small size.⁶

Consideration of economic resilience building is also important because it conveys the message that small vulnerable states should not be complacent in the face of their economic vulnerability, but could and should adopt policy measures to enable them to improve their ability to cope with or bounce back from external shocks.

1.3 The Singapore Paradox

Briguglio (2003; 2004) explains the “Singapore Paradox” in terms of the juxtaposition of economic vulnerability and economic resilience and proposes a methodological approach in this regard. In this approach, economic vulnerability is ascribed to inherent conditions affecting a country’s exposure to exogenous shocks, while economic resilience is associated with actions undertaken by policy-makers and private economic agents which enable a country to withstand or recover from the negative effects of shocks.

On the basis of this approach, Briguglio (2004) identifies four possible scenarios into which countries may be placed according to their vulnerability and resilience characteristics. These scenarios are termed as “best case”, “worst case”, “self made”, and “prodigal son”.

The “best-case” category applies to countries that are not inherently vulnerable and which at the same time adopt resilience-building policies.

The “worst-case” category refers to countries that compound the adverse effects of inherently high vulnerability by adopting policies that run counter to economic resilience.

Countries classified as “self-made” are those with a high degree of inherent economic vulnerability, but which are economically resilient through the adoption of appropriate policies that enable them to cope with or withstand the effects of their inherent vulnerability.

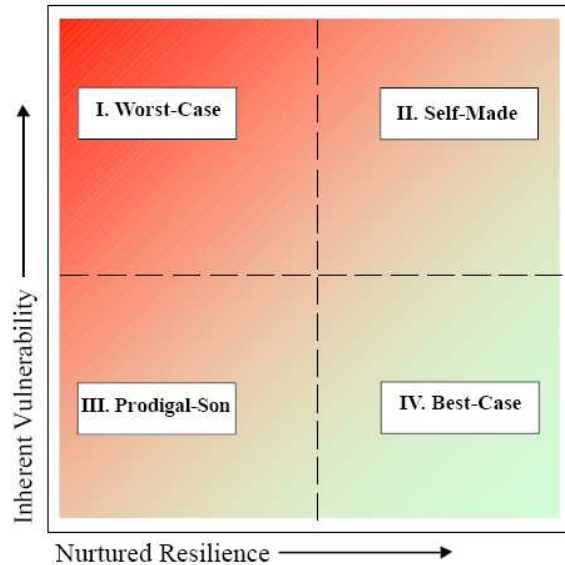
Countries falling within the “prodigal-son” category are those with a relatively low degree of inherent economic vulnerability but whose policies are deleterious to economic resilience, thereby exposing them to the adverse effects of shocks.⁷

These four scenarios are depicted in Figure 1, where the axes measure inherent economic vulnerability and nurtured resilience, respectively.

⁶ By way of example, the fact that Manuel de los Santos - a one-legged golfer - is having major success in international golf tournaments, should not lead one to argue that it is an advantage to have one leg.

⁷ The analogy with the prodigal son is that these countries, though “born in a good family”, squander their riches.

Figure 1
The Four Scenarios



1.4 Benefits of the approach

This method of defining vulnerability in terms of inherent features and resilience in terms of policy-induced changes has a number of advantages.

Firstly, the vulnerability index would refer to permanent (or quasi-permanent) features over which a country can practically exercise no control and therefore cannot be attributed to inadequate policies. In other words, countries scoring highly on the index cannot be accused of inflicting vulnerability on themselves through misguided policy approaches.

Secondly, the resilience index would refer to what a country can do to mitigate or exacerbate its inherent vulnerability. Scores on this index would therefore reflect the appropriateness of policy measures.

Thirdly, the combination of the two indices would indicate the overall risk of being harmed by external shocks due to inherent vulnerability features counterbalanced to different extents by policy measures.

Given that vulnerability refers to inherent characteristics which render countries prone to exogenous shocks, vulnerability scores for a particular country should not differ much over time, and therefore it is not expected that a country moves vertically along the quadrants of Figure 1. But horizontal movement is possible for those countries that adopt measures which build resilience and vice versa. It would thus be possible for countries to switch between the worst-case and the self-made scenarios, or the prodigal-son and the best-case scenarios, through changes in their economic policies.

By distinguishing between inherent economic vulnerability and nurtured economic resilience, it is possible to create a methodological framework for assessing the risk of being affected by external shocks, as shown in Figure 2.

Figure 2
Risks associated with being affected by External Shocks

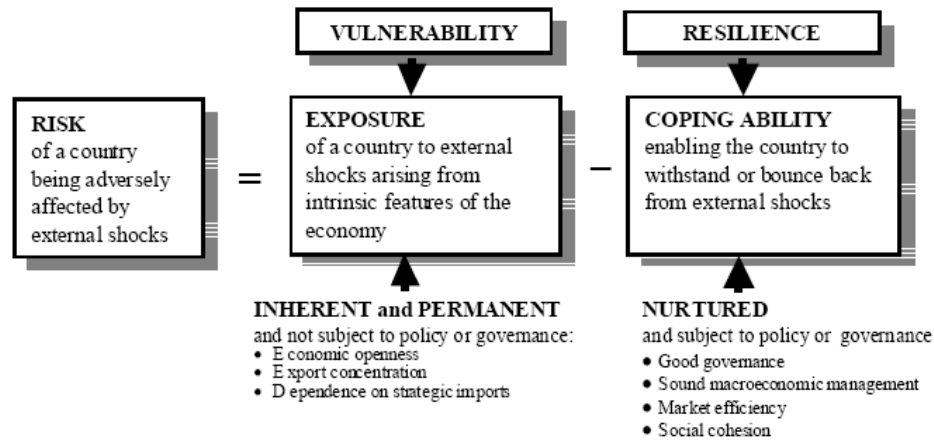


Figure 2 shows that risk has two elements, the first is associated with the inherent conditions of the country that is exposed to external shocks and the second associated with conditions developed to absorb, cope with or bounce back from adverse shocks. The risk of being adversely affected by external shocks is therefore the combination of the two elements. The negative sign in front of the resilience element indicates that the risk is reduced as resilience builds up.

2. Measuring Economic Resilience⁸

2.1 Components of the Resilience Index

In order to measure economic resilience Briguglio et al (2009) proposed an index intended to capture the effect of shock absorption or shock counteraction policies across countries. The authors hypothesised that the variables that capture these effects are the following:

- macroeconomic stability;
- microeconomic market efficiency;
- good governance; and
- social development.

2.2 Macroeconomic Stability

Macroeconomic stability relates to the interaction between an economy's aggregate demand and aggregate supply. If aggregate expenditure in an economy moves in equilibrium with aggregate supply, the economy would be characterised by internal balance, as manifested in a sustainable fiscal position, low price inflation and an unemployment rate close to the natural rate, as well as by external balance, as reflected in the international current account position or by the level of external debt.

⁸ The Resilience Index and the sources of the data. are available at: <http://www.informaworld.com/smpp/content~db=all~content=a914797666>.

These can be all considered to be variables which are highly influenced by economic policy and which could act as good indicators of an economy's resilience in facing adverse shocks.

The macroeconomic stability component of the resilience index proposed in this study consists of three variables, namely (i) the fiscal deficit to GDP ratio; (ii) the sum of the unemployment and inflation rates; and (iii) the external debt to GDP ratio. The variables are available for a reasonably wide set of countries spread over a spectrum of stages of development, size and geographical characteristics.

Fiscal deficit. The government budget position is suitable for inclusion in the resilience index because it is the result of fiscal policy, which is one of the main tools available to government, and relates to resilience of a shock-counteracting nature. This is because a healthy fiscal position would allow adjustments to taxation and expenditure policies in the face of adverse shocks. The fiscal deficit, standardised as a ratio to GDP, is thus included in the resilience index proposed in this chapter.

Inflation and unemployment. Price inflation and unemployment are also considered to be suitable indicators of resilience and at the same time they potentially provide additional information to that contained in the fiscal deficit variable. This is because price inflation and unemployment are strongly influenced by other types of economic policy, including monetary and supply-side policies. They are associated with resilience because if an economy already has high levels of unemployment and inflation, it is likely that adverse shocks would impose significant costs on it. If on the other hand, the economy has low levels of inflation and unemployment, then it can withstand adverse shocks to these variables without excessive welfare costs. In this sense, therefore, unemployment and inflation are associated with resilience of a shock-absorbing nature. The sum of these two variables, also known as the Economic Discomfort Index (or Economic Misery Index), is thus included in the resilience index proposed here.

External debt. The adequacy of external policy may be gauged through the inclusion of the external debt to GDP ratio. This is considered to be a good measure of resilience, because a country with a high level of external debt may find it more difficult to mobilize resources in order to offset the effects of external shocks. Thus, this variable would indicate resilience of a shock-counteracting nature.⁹

2.3 Market Efficiency

Briguglio et al (2009) argue that the science of economics views markets and their efficient operation through the price mechanism as the best way to allocate resources in the economy. If markets adjust rapidly to achieve equilibrium, following an external shock, the risk of being negatively affected by such a shock will be lower than if market disequilibria tend to persist. Indeed, if with very slow or non-existent market adjustment, resources will not be efficiently allocated in the economy, resulting in welfare costs, manifested, for instance, in unemployed resources and waste or shortages in the goods

⁹ It is however recognised that certain countries may have external debt not because of a weak policy framework but due to a highly-developed international financial activity. This is a weakness in the use of this indicator. However the inclusion of other variables related to market efficiency and governance would to an extent "correct" this weakness, since these variables either exacerbate the effect of external debt in the presence of a weak policy framework or counteract it otherwise.

markets. These considerations have important implications for resilience of the shock absorbing type.

There are not many available indicators of market efficiency which span a sufficiently wide range of countries as required for the purpose of this study. Following a search for suitable indicators, it was decided to use a component of the *Economic Freedom of the World Index* (Gwartney and Lawson, 2005), entitled “regulation of credit, labour and business” which is aimed at measuring the extent to which markets operate freely, competitively and efficiently across countries. It is designed to identify the effect of regulatory restraints and bureaucratic procedures on competition and the operation of markets.

In the financial market this index assesses the extent to which (a) the banking industry is dominated by private firms; (b) foreign banks are permitted to compete in the market; (c) credit is supplied to the private sector; and (d) controls on interest rates interfere with the market in credit. All these relate to the degree of interference by government in the financial market, which could preclude the economy from reacting flexibly to shocks.

Similar considerations apply in the case of the labour market. Here interference relates to unduly high unemployment benefits (which could undermine the incentive to accept employment), dismissal regulations, minimum wage impositions, centralised wage setting, extensions of union contracts to non-participating parties and conscription. All these are viewed as possibly precluding work effort, thereby limiting the ability of a country to recover from adverse shocks. A country would have a higher market efficiency score if it allows market forces to determine wages and establish conditions of dismissal, avoid excessive unemployment, and refrain from the use of conscription.

Bureaucratic control of business activities is also thought to inhibit market efficiency. This sub-component is designed to identify the extent to which bureaucratic procedures limit competition and the operation of markets. When such activities retard entry into business and increase the cost of production, when prices are not market-determined and when governments use their power to extract financial payments and reward some businesses at the expense of others, private sector involvement is discouraged, thereby inhibiting the freely-operating markets to absorb shocks.

2.4 Good Governance

Briguglio et al (2009) argue that good governance is essential for an economic system to function properly and hence to be resilient. Governance relates to issues such as rule of law and property rights. Without mechanisms of this kind in place, it would be relatively easy for adverse shocks to result in economic and social chaos and unrest. Hence the effects of vulnerability would be exacerbated. On the other hand, good governance can strengthen an economy’s resilience.

The *Economic Freedom of the World Index* has a component which focuses on legal structure and security of property rights.¹⁰ This is considered to be useful in the context of

¹⁰ An alternative governance index is presented by the World Bank (Kaufmann et al., 2006). A Pearson correlation test of the World Bank governance indicators and the Economic Freedom of the World’s “legal structure and security of property rights” component yielded a value of 0.92. Thus, both indices are likely to be measuring a similar phenomenon. In fact when the Kaufmann Index was used in the compilation of the resilience index the ranking of countries only changed marginally.

the present exercise in deriving an index of good governance. The component covers five sub-components, namely (a) judicial independence; (b) impartiality of courts; (c) the protection of intellectual property rights; (d) military interference in the rule of law; and (e) political system and the integrity of the legal system.

2.5 Social Development

According to Briguglio et al (2009) social development is another essential component of economic resilience. This factor indicates the extent to which relations within a society are properly developed, enabling an effective functioning of the economic apparatus without the hindrance of civil unrest. Social development can also indicate the extent to which effective social dialogue takes place in an economy, which would in turn enable collaborative approaches towards the undertaking of corrective measures in the face of adverse shocks.

Social development in a country can be measured in a number of ways. Variables relating to income, such as its dispersion and the proportion of the population living in poverty, the long-term unemployment rate—indicating the proportion of the population with low skills and inadequate employment prospects—and the proportion of the population with low levels of education, could be useful indicators. Still another possible approach would be to measure the number and extent of instances of industrial or civil unrest. These approaches are interesting but rather narrow in scope and very difficult to measure across countries.

The social development component of the resilience index consists of the education and health indicators utilised to construct the UNDP Human Development Index. Educational advancement, measured by the adult literacy rate and school enrolment ratios, is considered to be a good indicator of social development. In addition, an improved standard of education could be indicative of an improved ability to cohere in the face of external shocks—a condition conducive to economic resilience. Life expectancy at birth is considered to be suitable for measuring the health aspects in society. This in turn is likely to be related to medical facilities, housing and degree of proneness to accident or risk of injury. Again, advancement in health standards is considered to be conducive to economic resilience.

2.6 The Resilience Index across countries

The results of averaging the four components of the Economic Resilience Index show that many of the small states including Singapore, Barbados, Malta and Cyprus, Hong Kong, Slovenia and Estonia register relatively high resilience scores. Unfortunately data for small island developing states that register low resilience scores was available for two countries only, namely Jamaica and Papua New Guinea.

2.7 Juxtaposing vulnerability and resilience

Going back to the scenarios proposed in Figure 1, it is possible to place the countries included in the index in the four quadrants shown therein, using the resilience index proposed in this chapter and the vulnerability index presented by Briguglio and Galea (2003).

The overall tendencies that were derived from juxtaposing economic vulnerability and resilience, can be summarised as follows:

- countries which fall in the “best-case” quadrant are mostly the large “developed countries”;
- countries which fall in the “self-made” quadrant include a number of small states with a high vulnerability score;
- countries which fall in the “prodigal-son” quadrant include mostly large third world countries; and
- countries which fall in the “worst-case” quadrant include a few vulnerable small countries with weak economic performance.

2.8 GDP per capita, resilience and vulnerability

It would be interesting to investigate the extent to which GDP per capita of the different countries is explained by vulnerability and resilience.

Using the ordinary least squares (OLS) method of regression, GDP per capita was regressed on the vulnerability index (as proposed in Briguglio and Galea, 2003) and on the resilience index produced in this study.

The results are the following:

$$G = 0.14 + 0.95R - 0.14V$$

<i>t statistics</i>	(3.5)	(17.2)	(-2.4)
$R^2 = 0.78$	Number of observations = 86		

In Table 2, G represents GDP per capita; R represents the Resilience Index; and V represents the Vulnerability Index. All variables have been standardised as explained above, so that their values range between 0 and 1.

This result confirms the hypothesis in Briguglio (2004) that the performance of countries depends on their inherent vulnerability and their nurtured resilience. It also confirms that the resilience index is highly correlated with GDP per capita, with countries having the highest GDP per capita, being, as expected, those with the highest resilience scores. This is not an extraordinary finding, because it validates a very plausible assumption. However the results of the regression exercise have some interesting implications. In particular, the results show that the economic well-being of nations is more dependent on man-made policies than on inherent vulnerabilities.

3. Some Lessons for Large Developing Countries

The results of the resilience index just described lead to the conclusion that many large developing countries can improve their policy milieu to enable them to better withstand economic shocks. Many large countries are large enough to have a sizeable domestic market and a relatively diversified economy – a reality that is not the result of policy choice but occurs because of the large size of the economy. This characteristic, to an extent, shelters large countries from external shocks, although no economy is totally

isolated from external economic influences, as even large economies like that of the Philippines have a foreign sector and engage in international trade.

To assess the major differences between large developing countries and small states in terms of economic resilience, the eight best-performing small states will be compared with the eight worst-performing large countries. Large countries are defined as those with a population exceeding 70 million and small states as those with a population of 1.5 million or less. The resilience index constructed by Briguglio et al (2006) will be used to gauge this difference between the two groups of countries. The scores for the 8 large countries and the 8 small states are shown in Figures 4 and 5.

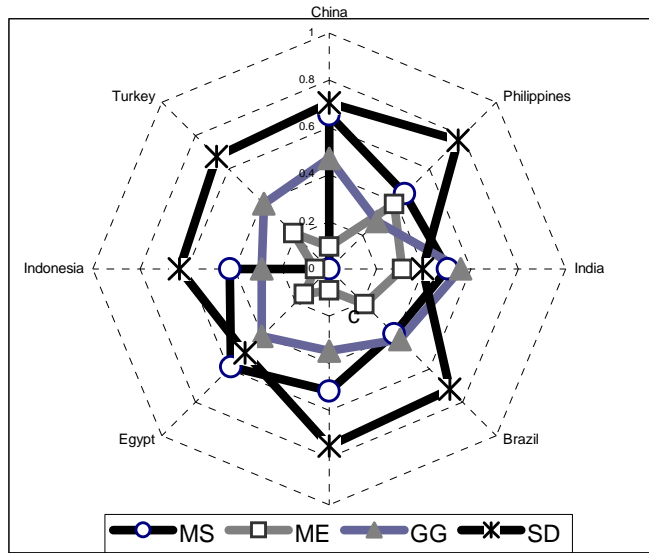
An indication of the economic performance of these two groups of countries can be derived also from GDP per capita scores and their human development index (HDI) scores. According to the *Human Development Report* (2008) the average GDP per capita (in terms of PPP for 2006) of the small states was \$24,000 with an average HDI of 0.889, whereas the average GDP per capita of the large countries was \$6300 with an HDI of 0.721. These averages conceal a wide range of values, but in general the small states considered in this study performed better in terms of their GDP per capita and their HDI, pointing to a higher state of development.

Figure 4 shows the 6 large countries in terms of the four components of the resilience index, namely Macroeconomic Stability (MS), Market Efficiency (ME), Good Governance (GG) and Social Development (SD). It can be seen that in general, large countries have done relatively well in terms of social development, and with the exception of Turkey, in macroeconomic stability. This conclusion applies to the Philippines as well.¹¹

It can be seen also that most of the large countries performed badly in terms of market efficiency and political governance.

¹¹ It should be noted that the Resilience Index computed by Briguglio et al (2009) covers 86 countries only, as data was missing for many large countries, particularly less developed ones. It is therefore possible that there were other large countries that performed worse, in terms of economic resilience, than the eight large countries considered in this paper.

Figure 4
Resilience Scores for the Eight Large Countries



On the other hand, the best-performing small states, with the exception of Cyprus, did well in all four components of the index, although the best results were obtained with regard to good governance and social development, as shown in Figure 5.

Figure 5
Resilience Scores for the Eight Best-Performing Small States

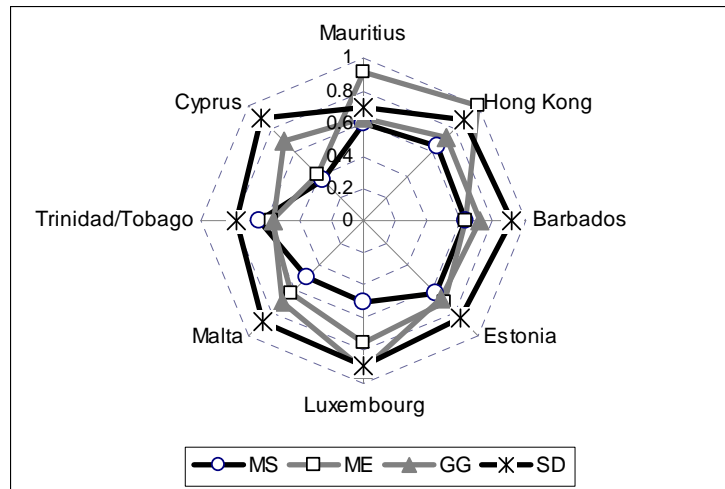
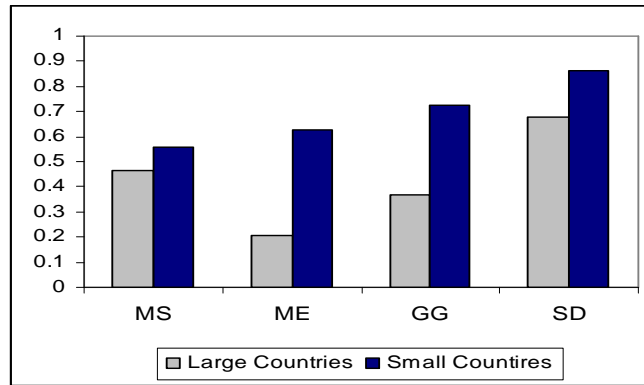


Figure 6 summarises the scores for the large and small countries. It can be seen that the major differences between the two groups of countries occur in market efficiency and in political governance, as was observed with regard to Figures 4 and 5.

Figure 6
Average Resilience Scores for Small and Large Countries



It appears therefore that most countries, including the large developing states, are adopting improved macroeconomic and social policies. But in terms of market efficiency large developing states tend to perform badly. This is also true with regard to political governance.¹²

The main conclusion that can be derived from the foregoing discussion is that because many small states have adopted sound policies to build up their economic resilience, they have managed to step up their development endeavors, even though they are highly exposed to external shocks. The most important contributing factors in this regard would seem to be good political governance and market efficiency.

It follows that a major lesson that could be drawn by large developing countries in this regard is that it is important for them to emulate the successful small states, which, though very much open to forces outside their control, have made an effort to mitigate this disadvantage by adopting appropriate economic policies. As already argued, the major policy deficit, as far as large developing countries are concerned, would seem to relate to market efficiency and good governance.

3.1 Why compare large countries with small states?

An interesting question in connection with this study relates to the reason as to why it is useful to compare large developing countries with small states and not with large developed countries. The main reason is that many large developed countries are endowed in terms of natural resources and this may have helped them achieve their status as developed countries. In addition, many large developed countries are former colonizing powers, including Western European countries, and it has been argued that these may have enriched themselves by exploiting the third world. Small states on the other hand,

¹² It should be pointed out here that there were many developing states, with a population of between 1.5 million and 50 million, performed worse than the 8 very large countries. In fact the Philippines was ranked as 57th among 86 countries.

especially the most successful ones, are generally poorly endowed with natural resources and what they have achieved is mostly policy induced. In addition, these states were part of the third world until they gained independence, and their success therefore cannot be attributed to natural wealth or to the exploitation of other states.

4. Conclusion

The policy mix associated with resilience building, as outlined in this study, is aimed at improving economic management, so as to allow the country affected by an external economic shock, room for manoeuvre and flexibility for quick response.

It is important to note that the relative good performance that a number of small states may be enjoying, relative to larger developing economies, does not negate their economic vulnerability. They will remain very open to external shocks. However, the resilience elements that these economies have developed over the years, including their predictable governance structure and their market efficiency can assist them to better weather difficult times.

This study has argued that although large developing countries are not, in general, as economically vulnerable as small states, they could end up being more effected by external shocks due to “policy failure” with regard to their relative inability to withstand such shocks.

Thus a major lesson that can be derived by large developing countries is that it is important for them to emulate the successful small states, which, though very much open to forces outside their control, have made the best to mitigate this disadvantage by adopting appropriate policies in this regard. The major policy deficit, as far as large developing countries are concerned, would seem to relate to market efficiency and good governance.

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