Special and Differential Treatment for Small and Vulnerable Countries Based on the Situational Approach

By Werner Corrales-Leal, International Centre for Trade and Sustainable Development
Felipe Baritto, Universidad Metropolitana, Caracas, Venezuela
Sarah A. Mohan, International Centre for Trade and Sustainable Development
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Acknowledgments

The authors would like to thank Ambassador Trevor Clarke and Ms Brigitte Cuendet for their comments, inputs, and cooperation. Secondly, thanks to the SECO and to the UN International Strategy for Disaster Reduction (ISDR) for their cooperation with ICTSD on this project. Thanks also to Deborah Vorhies for her continuing support in the development of this program.

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ICTSD welcomes feedback and comments on this document. These can be forwarded to Werner Corrales-Leal, wcorrales@ictsd.ch


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<tr>
<td>ASCM</td>
<td>Agreement on Subsidies and Countervailing Measures</td>
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<td>CBA</td>
<td>Characteristic Based Approach</td>
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<td>CI</td>
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<td>COM-1</td>
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<td>CTD</td>
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<td>CL</td>
<td>Complementarity and Linkage</td>
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<td>DA</td>
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<td>DRM</td>
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<td>DSU</td>
<td>Dispute Settlement Understanding</td>
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<td>EAP</td>
<td>Exceedance Annual Probability</td>
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<td>ENH</td>
<td>Exposure to Natural Hazards</td>
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<td>TSDS</td>
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<td>United Nations Conference on Trade and Development</td>
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<td>UNDP</td>
<td>United Nations Development Program</td>
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<tr>
<td>UN-ISDR</td>
<td>United Nations International Strategy for Disaster Reduction</td>
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<td>WTO</td>
<td>World Trade Organization</td>
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FOREWORD

Beyond the general constraints on trade and competitiveness affecting nearly all developing countries, a special class of concerns applies more specifically to the so-called Small and Vulnerable Economies (SVEs). Small economies usually depend more on international trade than other countries and are more exposed to risks resulting from trade-related external shocks. In addition, many of them have encountered disasters related to natural hazards with increasing frequency and impact.

In fact, in the case of small countries, the impacts of these events may be of significant magnitude relative to the size of their economies. The large-scale discontinuities that such events may cause can lead to instantaneous losses of competitiveness that may prove difficult for the affected country to recover from. To ensure that their long-term development paths are sustainable, small and vulnerable countries must implement both appropriate competitiveness policies aimed at medium- and long-term goals, and policy systems able to manage the risks presented by natural hazards and other "external shocks".

The special circumstances of SVEs, in particular their needs for special support, were recognized in paragraph 35 of the Doha Declaration, in which specific considerations on Special and Differential Treatment (S&DT) were made in favour of these countries.

However, if Special and Differential Treatment is to be effective in meeting the challenges of competitiveness and vulnerability of the SVEs, they must have the opportunity to put appropriate policies in place. This involves discussing whether the revision of S&DT mandated in Doha—expressed both in paragraphs 35 and 44 of the Ministerial Declaration—should be limited to extending the time periods for compliance and giving effective support for institutional adaptation. Another consideration is to adopt a different vision, involving sufficient flexibilities and the use of resources for development support that the countries may need to implement active supply-side policies.

This paper condenses the results of the exercises undertaken between 2004 and 2006 by ICTSD on small and vulnerable economies, as part of its project on a Situational Approach to S&DT (SA). From the outset, the project sought to identify circumstances in relevant areas of trade and development policies, one of which is obviously competitiveness and vulnerability of SVEs, rather than to attach S&DT provisions to country categories. The SA sets out to achieve two goals. The first is guaranteeing access by all developing countries and LDCs to a set of basic S&DT benefits: their respective S&DT acquis and the improvements to it that result from the Doha-mandated review. The second is to create additional S&DT benefits based on specific development situations.

The situations studied on economic vulnerability, remoteness and size of the economy do not imply that countries belonging to the SIDS or landlocked groups should necessarily be treated differently - in terms of flexibilities to implement competitiveness policies - from other developing countries that face severe constraints on their competitiveness. Rather, a developing country that simultaneously meets two or more of the three traits mentioned - smallness, vulnerability or remoteness - would receive treatment designed to help it overcome the specific negative effects associated with those constraints, additional to and different from S&DT to address the problems of competitiveness involved in other development situations, which are also briefly presented in this paper.

Ricardo Meléndez-Ortiz
Chief Executive, ICTSD
EXECUTIVE SUMMARY

The unique challenges of small countries have been for many years the subject of international consideration in several fora. In the United Nations, for example, a grouping of countries calling themselves the Small Island Developing States (SIDS) have for decades been advancing their interests in international negotiations. The successful representation of their characteristics in international political and environmental fora was one of the reasons a group of former British colonies approached the Commonwealth Secretariat in 1997 and asked them to examine the economic and trade-related problems of small economies. The resulting paper, which was published in 2000, examines the problems of Commonwealth countries with populations smaller than 1.5 million, and concludes that they have particular economic development challenges that could be addressed by special trade rules. A group of WTO Members, fuelled by this finding and their belief that they faced different conditions that demanded different trade rules, thus pushed for a recognition of their interests at the Second Ministerial Conference of the WTO in Geneva in 1998, action at the Seattle Ministerial Conference, and finally at the Doha Ministerial Conference in 2001 the paragraph 35 mandate was agreed to.

The Doha text, however, does not specify which countries would be the beneficiaries of this special treatment. In fact, it goes so far as to say explicitly that the outcome of the negotiations was not to be the creation of a sub-category of WTO Members. This reflected the concerns of the majority of developing countries that further differentiation amongst the membership of the organisation would be contrary to their interests. In the five years of negotiations that have ensued since the adoption of this mandate, these concerns have resurfaced as many times as the proponents of special treatment for Small and Vulnerable Economies (SVEs) have explored ways of identifying targeted rules that deliver the needed flexibilities.

More than three years after the negotiations had been initiated, a proposal from the proponents of the SVE programme (PSVEs) gained relatively wide support from the WTO Membership. According to the approach, any WTO Member whose share of world merchandise, agriculture and NAMA trade was below a specified threshold would be allowed to access a special set of rules that would involve, amongst other elements, lower tariff reduction commitments and greater ability to use other flexibilities from the rules. While this so-called “characteristic-based approach” had been in discussion amongst the SVE proponents for over two years, it represents one of the first times that the WTO Membership has supported triggering Special and Differential Treatment (S&DT) through the satisfaction of a statistical requirement, rather than targeting S&DT at the traditional categories of developed, developing or least-Developed Country (LDC) Member.

The fundamental purpose of the “characteristic-based approach” is very similar to that of the Situational Approach to S&DT in which the ICTSD has been working since year 2004. The main rationale in the two approaches is responding to special development needs that certain developing countries or LDCs may have as part of the circumstances they experience.

In the first quarter of 2004 the ICTSD had started exploring the Situational Approach within its project designated ”Special and Differential Treatment: Policy Research and Consultations for the WTO Negotiations”, as a contribution to breaking the stalemate of the negotiations on S&DT that were taking place in the Committee on Trade and Development. From its outset the initiative entailed identifying circumstances in relevant areas of development instead of attaching S&DT provisions to country categories, and was supported by extensive consultations with developing and developed countries’ delegates. The main outcome of the Project, the proposal of a “Situational Approach to S&DT”, implies a comprehensive agreement on special and differential treatment.

This paper addresses the issues of S&DT for small and vulnerable countries from the perspective of the Situational Approach. Chapter 1 briefly discusses the framework in which the ICTSD studies on
competitiveness and vulnerability were conducted, introducing the fundamentals of the Situational Approach and the Trade-supported Strategies for Sustainable Development. Chapter 2 summarizes the process of negotiations that have taken place on S&DT for small and vulnerable countries according to the Doha mandate, highlighting the “Characteristics Approach” that the proponents devised in the negotiations and its similarities with the Situational Approach. Finally, Chapter 3 presents the most important findings and conclusions of the studies conducted by ICTSD on the vulnerability of small economies, as well as on competitiveness situations which affect many developing countries, including the SVEs. It includes a discussion on the extent to which the SVEs conform a group of countries that have relevant common features in terms of development and trade, as well as ideas on how to best define the lists of countries that should have access to additional benefits in the Situations-based S&DT, and the kinds of such additional benefits. Finally, this chapter also presents recommendations for further research that should be undertaken on the issues of vulnerability, competitiveness and trade-supported strategies for sustainable development.

A Situational Approach to make S&DT an instrument for development in the multilateral trade system

The Situational Approach aims to shore up developing countries, by means of S&DT, to implement trade-supported strategies for development in the economic, social and environmental dimensions, involving competitiveness policies and measures to address their vulnerability problems, amongst other. Clearly not all problems of development can be solved by competitiveness policies, which are mainly economic in nature, but these policies may be instrumental - if so designed - in promoting sustainable development in its three spheres. In order to play this role in developing countries, various fundamental sets of economic, social and environmental goals must be addressed by national competitiveness policies, which in turn should be supported by national competitiveness policies, which in turn should be supported by S&DT flexibilities.

The first and the second sets of goals are economic in essence. The first consists of securing conditions for achieving effective market access and fair treatment for the country’s exports, for which market-access S&DT may be useful. This set of goals is very important, but not the only one and certainly not the most important from the long-term perspective of development in economic, social and environmental terms. The second set is to help the country derive sustained economic growth from international competition, while at the same time achieving a capacity to internally amplify the effects of that growth in terms of productivity increases, more and better jobs and income improvements for ever-greater proportions of the population, which implies combining a strategy for technological learning and innovation; and a strategy for creating inter-sectoral complementarities and linkages. Supply-side policies involved may have to be supported by S&DT flexibilities in rules.

Equity goals of a competitiveness policy can also be supported by means of S&DT. The connections between equity goals and economic policies are very important for the sustainability of development in the majority of developing countries, where social exclusion and polarization are partially rooted in the inability of the “modern economy” to provide jobs and sources of income for a substantial part of the population. S&DT flexibilities may enable implementing policies that contribute towards equity goals, through the effects on employment and income that may result of combining the strategies for innovation and linkages already mentioned, and through the effects of a strategy for human capital and social capital formation.

Positive environmental impacts may indirectly derive from the economic effects of a competitiveness policy. However, fostering direct environmental benefits in developing countries is necessary, and may be made feasible if S&DT flexibilities are granted to implement certain supply-side policies. Amongst the objectives of these policies we can mention the reversal of current trends towards increased developing countries’ specialization in exports of goods; the improvement of energy efficiency and the
gradual shift towards sustainable energy sources; the strengthening of their competitive advantages based on a sustainable use of their bio-diversity bases; and addressing compliance with environmental standards to secure access for their exports to many markets.

The occurrence of external shocks and disasters, which increasingly affect developing countries, warrants a final consideration on the sustainability of their long-term development paths. To ensure that the long-term path is sustainable, it is not only necessary to implement the appropriate trade-supported strategies aiming at medium and long-standing sustainable development goals; there is also a need for policy management that is aware of the risks of disasters involving natural phenomena and of those relating to other "external shocks". Therefore, the Situations-based S&DT should help developing countries to overcome the constraints that result from their vulnerability to the two kinds of events mentioned. In particular, the situations experienced by small and vulnerable developing economies may not be resolved without far-reaching action of two types, which the Situations-based S&DT should help to undertake. Firstly, own action through policies to develop production and competitiveness, such as those mentioned when referring to the trade-supported strategies for sustainable development. Secondly, international cooperation going beyond immediate aid after disasters and taking a form that is not a burden on those economies.

Access of small and vulnerable countries to S&DT benefits in the Situational Approach

Regarding access to S&DT benefits by developing countries and LDCs, the Situational Approach is conceived on two main bases. Its implementation involves adjusting the structure of the S&DT system, for which two components are proposed.

S&DT Benefits In The Situational Approach: Bases For Accessing The Benefits, And Components Of The Implementation

The Bases: Generalised access to S&DT

The first basis is that all developing countries and LDCs should have access to a set of basic S&DT benefits, which would include all the S&DT provisions they currently benefit from, based on the two pre-existing country categories, and to the improvements resulting from the revision of the respective acquis that they would negotiate under the Doha Mandate. Adopting the first basis of the Situational Approach implies ruling out any further differentiation amongst developing countries as a precondition for improving S&DT.

The second basis is that additional S&DT benefits should be created in order to contribute to solving specific Development Situations. All LDCs would be granted these additional benefits, and all developing countries would have access to them in the measure in which they effectively experience such situations.

The components in the implementation

The first component of the proposal consists of a general set of principles, rules and measures that would constitute the structure of the S&DT system (i.e. would support a system based on both basic and additional S&DT benefits); and would facilitate negotiating the improvement of the respective acquis of developing countries and LDCs in agreement with the Doha Mandate.

The second component consists of the additional S&DT benefits that would be created according to the second basis, i.e. responding to development needs specific to certain Development Situations.
According to the above explained bases, small and vulnerable countries may have access to the additional benefits of various situations, some of them focused on competitiveness constraints, which they may share with many other developing countries, and some others focused on vulnerability problems, in which the SVEs are unique. An interesting finding of the studies conducted is that a large proportion of small and vulnerable countries, i.e. small countries that are highly vulnerable (SVE situation) and circumstances of smallness and remoteness (SRE situation) are also included in the lists of Competitiveness Situations COM-1, referred to economic problems frequently faced by weak economies in the process of joining the international economy, and COM-3, referred to economies that have tried to change their export specializations into manufactures but feature important deficiencies in internal linkages and technological capabilities. This means that small and vulnerable countries should have access not only to the respective additional benefits of the SVE and SRE situations, but also to those associated to the two mentioned competitiveness situations.

The initial negotiations on SVEs

The Doha Declaration gave the General Council responsibility for the carrying out of the SVE mandate. After several consultations, WTO Members agreed to a framework to carry out negotiations in March 2002. The framework, based on revisions to a draft tabled by the proponents of the SVE work programme (the PSVEs), calls for the Committee on Trade and Development to be responsible for the SVE work programme, to regularly report to the General Council on progress, and to hold dedicated sessions of the Committee on Trade and Development (CTD-DS) on the mandate under the Chairmanship of the Chair of the CTD. The framework also calls for the Secretariat to undertake studies on impact of WTO rules on Small Economies; on the constraints faced by Small Economies; and on the effects of Trade Liberalization on Small Economies.

The PSVEs have also made submissions, and engaged in talks, in the negotiating groups on Non-Agricultural Market Access (NAMA), agriculture, services, rules (on fisheries and on subsidies and countervailing measures), trade facilitation and the working party on domestic regulation. While they have been very active in the NAMA negotiating group, there has been relatively less progress on their proposals in the other negotiating groups. In the NAMA and agriculture groups they have called for SVEs to be exempted from the obligation to reduce tariffs according to the formula being negotiated for other WTO Members. Instead, they have called for smaller cuts to their tariffs. In the other negotiating areas, and for special products in the agriculture negotiations, they have asked for special flexibilities to the rules to accommodate their particular situation.

Successive documents on the relationships between smallness and vulnerability or the need for S&DT were tabled by the PSVEs and individual countries, between April 2002 and November 2004, facing the permanent opposition of the US and Chile, the frequent antagonism of several Latin-American countries and other large developing countries, and the occasional -although strong- disagreement of Canada, New Zealand and Japan. The most emphasized and repeated arguments of the opponents related to what they defined as proposals that lead to creating new categories of developing countries in the WTO, which contradicts the Doha mandate on SVEs.

In the initial documents, the PSVEs mentioned a list of features characterizing and adversely affecting small economies’ trade and development status. At the same time, the PSVEs suggested that they have very limited trade policy-making capacity which adversely impacts on their ability to promote and defend their interests at the WTO, and advanced concrete proposals for S&DT in specific WTO Agreements, along with explanations of why they are necessary to address the needs of SVEs. The needs and characteristics of landlocked countries were also introduced and discussed by the end of 2003, and concrete proposals aimed at addressing their concerns were introduced in May 2004.
A review of the literature on small economies was presented by the WTO Secretariat at an informal meeting of the CTD-DS, and two additional reports were presented by the Secretariat attempting to provide more analytical depth on the relationship between smallness and key economic indicators, and to compile some provisions that could be of interest to or impact small economies.

In the eighth session of the CTD-DS, on 3 November 2004, the PSVEs said they were happy with the mention given to the SVE mandate in the WTO General Council decision on 1 August 2004 (the July Package, WT/L/579). In reaction to earlier questions about the need for special rules for SVEs, which was linked to the issue of whether SVEs were “unique”, the PSVEs noted that it was a combination of the disadvantages and the inability to deal with them that made small economies worthy of special consideration. Reportedly, at this time the PSVEs began to consider the use of a "characteristic-specific" approach to link the needs of small economies with special rules at the WTO. Although they hoped this would enable them to surmount the ban on the creation of a sub-category, there was little clarity at this time on how such an approach would be operationalised.

Turning points in the negotiations, the “Characteristics” and the “Two-tracks” approaches of SVEs

A major turning point in the negotiations came on 25 January 2005, when the CTD-DS Chair tabled a new approach to the negotiations in an informal meeting of the group. The Chair’s approach essentially reframed the process to be used by the group to address the paragraph 35 mandate. The Chair proposed a new three-step process, namely (1) consideration of the use of characteristics to identify what can be accepted as small, vulnerable economies; (2) the consideration of the trade-related problems that could reasonably be attributed to those characteristics; and (3) framing responses to those trade-related problems that these countries could use.

By making explicit mention of the importance of identifying the "characteristics" of SVEs, the PSVEs thus intended to try to address the concerns raised in previous sessions by developed countries such as the US, Canada and EU regarding how the new rules would be applied only to SVEs. By defining the characteristics and problems of SVEs, and linking them to solutions, they hoped it would strengthen the perceived link between the new rules and the concrete needs of SVEs that arose owing to their particular "situation" or "characteristics", and also possibly give a concrete tool for triggering eligibility for the new rules. Still, in so doing, they elicited a backlash from large developing countries, who questioned the uniqueness of the SVE’s situation as a result of fears that such a definition of uniqueness, triggered through characteristics, would exclude their relatively large economies from S&DT that had hitherto been shared amongst all developing countries.

However, Members agreed to move forward by taking up steps one and two simultaneously, and then move on to the framing of systemic responses. On the heels of the mention of the SVE mandate in the July Package, the new three-step process injected new energy into the negotiations and launched a new, more intensive phase of the talks.

In another major turning point in the negotiations, on 29 July the PSVEs issued a press release saying that they would be pursuing a two-track approach to the negotiations according to which they would be making proposals on how to address their particular problems directly in the relevant WTO negotiating group, while the CTD-DS would monitor the progress of these proposals. Noting once again that “no one characteristic and problem by itself” was unique to SVEs, the proposal nonetheless emphasises “the cumulative effect” of these characteristics and problems on SVEs and reaffirms the “characteristic based approach” as the three-step way to fulfil the paragraph 35 mandate.

At a session of the CTD-DS held in February 2006, the PSVEs noted they were happy about the mentions of the situation facing SVEs in the December 2005 Hong Kong Ministerial Declaration. Given that
the deadlines for NAMA, agriculture and services negotiations were closely approaching in April and July, they stressed that the proponents of the small economies work programme would focus on promoting their concerns in the relevant committees. At the April 2006 session the PSVEs tabled a new proposal which compiled the relevant sections of the PSVE proposals made to other negotiating groups. However, at the meeting some delegations, including Brazil and China, suggested that it was not clear in all the relevant negotiations on SVEs which WTO Members would qualify for the rules being sought for SVEs. Overall, they insisted that to preserve the rules-based nature of the WTO, and to avoid creating a new category, they opposed limiting eligibility to a list of countries.

Commonalities and differences: The empirical evidence in favour of the SVEs claims

Although in recent years the arguments of the PSVEs have evolved from the linear relationship originally exposed between smallness, on the one hand and competitiveness or volatility problems, on the other, to a more comprehensive explanation on the combined and cumulative influence of several characteristics, robust proofs of the existence of these links have been missing so far, particularly proofs of the non-existence of equivalent links between characteristics of the rest of the developing countries and competitiveness problems that they - as the SVEs- face. Almost all arguments and evidence on these kinds of links found in the literature are based on analysis of the variables taken one-by-one, and not considering whole sets of characteristics or variables determining the problems of competitiveness, trade marginalization, etc. Both the arguments in favour and those against SVEs allegations are usually supported in this manner.

The studies conducted by ICTSD in its project on the Situational Approach to S&DT included assessing the above mentioned relationships. Three fundamental conclusions may be derived of these studies, including the results of multiple statistical tests of hypotheses.3

The first conclusion is that using a rational combination of indicators (various and not just one determinant) leads to a robust statistical confirmation of the existence of a particular disadvantaged situation of the SVEs. The counterpart of this conclusion is that analyzing variables in an isolated way does not allow properly assessing the issues of smallness, vulnerability and remoteness in the context of trade and development.

The second conclusion, derived from the first, has very practical consequences: the definition of the lists of countries in the situations of smallness and vulnerability must be based on combining thresholds on various characteristics and problems, and not on only one or a few characteristics.

Finally, the third conclusion refers to the fact that development situations involve relative disadvantages of countries in the particular situation vis a vis the rest of the countries. The thresholds must not be arbitrarily defined but take in account the relative position of the country under analysis in the whole WTO membership according to the variables considered.

Regarding characteristics strongly related to competitiveness, no significant differences have been found between SIDS and landlocked countries, on the one hand, and the rest of developing economies on the other. The problems of trade and competitiveness in which no differences are perceived are, amongst others, insufficient value added or insufficient processing of exports, insufficient links between export activities and the rest of the economy, volatility in the price of exports, advantages or disadvantages for attracting foreign investment, or difficulties in overcoming problems relating to international technical and health standards.

However, the studies have concluded that small countries have scale restrictions that can aggravate the constraints that other developing countries experience in trying to diversify or to integrate into their own economies the processing of their commodities. Also because of their high level of
dependency, their fiscal earnings depend to a great extent on import tariff revenues, which make them more vulnerable to reductions in those tariff levels. Compared to other developing countries, small countries tend to have more limited institutional capacity to formulate and implement trade or productive development, diversification and competitiveness policies, to face an international trade dispute, or put into effect comprehensive disaster risk management plans. If, in addition, they suffer from external shocks or frequent disasters, they face even more severe constraints to preserve any improvements in competitiveness that they may have achieved and to recover from any damage suffered during these events. The same can be said for countries whose per unit transportation costs are in fact much higher than those of the rest of the world and that in addition have economic scales that prevent them from making themselves the investments - in logistics and infrastructure - they would need to overcome their disadvantages. Worse yet is the situation in countries that simultaneously meet the three conditions - smallness, vulnerability and remoteness.

These are the real reasons that differentiate the situations of SVEs from those circumstances of limited competitiveness that most developing countries experience. It is on these traits that the policies that could be useful and the considerations of S&DT that both situations would deserve should be based.

Eligibility of small countries to additional S&DT benefits based on situations: the specific SVE and SRE situations, and other competitiveness situations

Based on the above made considerations the Situational Approach (SA) proposal defines two Situations involving S&DT for small countries: the SRE situation and the SVE situation. A list of developing countries and LDCs characterised as SVEs in one of the simulations, serves to illustrate the outcome of a particular combination of these features. This list results from a simulation that limited the market share to 0.12 percent of the world exports and the population to 10 million inhabitants, while considering various vulnerability criteria including natural risk indicators, GDP volatility and exposure to price shocks.

Situation SVE: List of LDCs and Developing Countries with Global Market Share under 0.12 percent and Population under 10 million inhabitants

Albania; Antigua & Barbuda; Armenia; Barbados; Benin; Bolivia; Botswana; Burundi; Central African Rep; Chad; Costa Rica; Djibouti; Dominica; Dominican Republic; El Salvador; Fiji; Gabon; Gambia; Grenada; Guinea-Bissau; Guyana; Haiti; Honduras; Jamaica; Jordan; Kyrgyzstan; Macau; Macedonia; Maldives; Mauritania; Mauritius; Moldova; Mongolia; Nicaragua; Panama; Papua-New Guinea; Paraguay; Rwanda; Sierra Leone; St Kitts & Nevis; St Lucia; St Vincent & the Grenadines; Solomon Islands; Suriname; Swaziland; Togo; Tonga; and Trinidad & Tobago.

However, the ICTSD studies found that the majority of developing countries in situation SVE are also present in the lists of three competitiveness situations characterised as "Severe supply-side constraints found in low-income countries", "Diversifying exports and strengthening technological capabilities in mineral-dependent economies", and "Deepening shallow productive-sector development in manufacture" (designated as COM-1 through COM-3 in the ICTSD studies). Thirty seven developing countries in the SVE list would benefit from at least one of the situations COM-1, COM-2 or COM-3 and twenty-three would benefit from at least two.
Due to the fact that countries in situations SVE and SRE share many supply-side constraints related to competitiveness with those in competitiveness situations COM-1 through COM-3, some of the policy actions and instruments identified in the Situational Approach studies are also shared. However, international technical assistance and international development assistance are relatively more important in SVE and SRE. The expected development of Aid for Trade programmes in WTO would provide additional resources for both purposes.
1. THE SITUATIONAL APPROACH TO S&DT, AND COMPETITIVENESS AND VULNERABILITY ISSUES: A FRAMEWORK

Competitiveness and vulnerability are closely intertwined in developing countries, and particularly in the case of small economies. Competitiveness expresses itself in the form of firms participating in competition with other firms. Nevertheless, competitiveness policies in developing countries must address processes that take place at the micro, meso and macro levels because such policies must serve the purpose of a positive integration of these countries into the global economy, contributing to the economic, social and environmental goals of sustainable development of societies as a whole, and not just resulting in trade growth or economic achievements of particular firms. Regarding vulnerability, developing economies are increasingly subject to risks of external shocks and disasters that may lead to instantaneous losses of competitiveness gains, which may be very difficult for small countries to recover from.

Policies to address competitiveness and vulnerability problems of small economies may thus involve implementing active policies in combination with trade liberalization, demanding trade-related policy measures that may require special and differential treatment responses in trade rules.

This Chapter in the paper briefly introduces the Situational Approach to S&DT as well as concepts on competitiveness and trade-supported strategies for sustainable development from which small and vulnerable countries could positively benefit. The ideas presented here are summarized versions of concepts that are discussed in detail in other papers produced by the ICTSD project “Special and Differential Treatment: Policy Research and Consultations for the WTO Negotiations”. Considerations made in this part of the paper serve as a background for characterizing the Development Situations discussed in Chapter 3.

1.1 A Summary of Concepts in the Situational Approach to S&DT

Responding to three relevant questions is an easy way of summarizing the objectives and the logic of the Situational Approach: what would be the main objectives of the SA in the S&DT negotiations in WTO?; how would a Development Situation be characterized in the context of S&DT?; and do Situations imply policy prescriptions?

Maximizing development benefits from S&DT: the main objectives of the SA in the negotiations in WTO

The motivations and fundamentals of the Marrakech Agreement establish that, although the function of WTO is related to trade liberalization, trade relations are conceived as instruments for sustainable development. Framed in this structure of thought, the SA aims at two goals related to: i) maximizing - by means of S&DT - the development benefits that developing countries and LDCs should get from trade liberalization; and ii) facilitating the current Doha-mandated negotiations on the subject.

Maximizing development benefits for all developing countries implies that liberalization must be used as an instrument to optimize development, and not that trade must be maximized while trying to keep below certain limits the negative impacts that short term liberalization might eventually have on the development goals of countries involved.

So far, the SA proposal covers development situations in three areas: Agriculture and Rural Development; Competitiveness; and Vulnerability of Small Economies.

The more operational objective of facilitating the negotiations would consist of helping to build a development framework for the Doha-mandated review and specific improvements in S&DT provisions. The framework would be based on a group of general principles and general rules whose application would ensure that the revised S&DT system would serve the development objectives of developing countries’ integration while preserving the values of the rules-based multilateral trade system.
The bases and the components of the proposal of a Situational Approach to S&DT

The proposal of a Situational Approach to S&DT is founded on two main bases, and has two components.

The first basis is that all developing countries and LDCs should have access to a set of basic S&DT benefits, which would include all the S&DT provisions they currently benefit from, based on the two pre-existing categories, and to the improvements resulting from the revision of the respective acquis that they would negotiate under the Doha Mandate, i.e. making S&DT more effective and operational. Adopting this first basis implies ruling out any further differentiation amongst developing countries as a precondition for improving S&DT.

The second basis is that additional S&DT benefits should be created in order to contribute to solving specific Development Situations; all developing countries would have access to these additional benefits in the measure in which they effectively live such situations.

The first component of the SA proposal is a general set of principles, rules and measures that would constitute the structure of the S&DT system, i.e. would support a system based on both basic and additional S&DT benefits; and would facilitate negotiating the improvement of the respective acquis of developing countries and LDCs in agreement with the Doha Mandate.

The second component consists of the additional S&DT benefits that would be created according to the second basis, i.e. responding to development needs specific to certain Development Situations.

Characterizing development situations

A Development Situation would be characterized by three elements, as outlined in Box 1.1. The first two elements (A and B) would describe circumstances involving development needs (development constraints or development policy objectives) of the country concerned; and the third (C) would portray the set of policy instruments (a policy tool box) from which one or more instruments could be used for addressing the former.

Box 1.1 Elements for Characterizing Development Situations in the Context of the Situational Approach to S&DT

| The first two elements: the circumstances and the policy objectives |
| The first element (A) should describe the economic and trade circumstances in which the needs (problems or constraints) are present; and the second element (B) should express the particular trade and development policy objectives established in response to the problems and constraints previously mentioned. |
| Describing the context (A) may or may not require the use of quantitative indicators. However, when applicable, there is a need to agree on a set of indicators and thresholds that can serve as benchmarks for defining when a Development Situation would deserve the additional flexibilities (S&DT provisions) involved. |
| WTO Members would eventually agree that a particular situation or set of situations deserve certain additional benefits provided that the chosen indicators fall within pre-established limits for a region, a group of sectors or the whole economy. Therefore, if a Developing Country Member’s indicators fall within these limits, the member will have automatic access to the additional benefits of S&DT provisions associated. |
However, a situation is not intended to prescribe the use of any particular policy mechanism or combination of instruments, but does identify a collection of these instruments that countries may or may not want to use in addressing the constraints or policy objectives.

1.2 Goals and Strategies of Competitiveness Policies from a Developing Country Perspective of Sustainable Development

Clearly not all problems of development can be solved by competitiveness policies, which are mainly economic in nature, but these policies may be instrumental - if so designed - in promoting sustainable development in its three spheres. Conversely, if they are directed exclusively towards maximizing trade or trade-led GDP growth, they might well end up obstructing the diversification and knowledge intensification of the economy at large, deterring relevant improvements in productivity and, most importantly, hindering the possibilities of achieving legitimate social and environmental objectives.

The most relevant strategies in achieving the economic goals of competitiveness policies

Two fundamental sets of economic goals should be addressed by national competitiveness policies of developing countries. The first consists of fair competition in international markets, i.e. securing conditions for achieving effective market access and fair trade for the country's exports. The second is to help the country derive sustained economic growth from that competition, while at the same time achieving a capacity to internally amplify the effects of that growth in terms of productivity increases, more and better jobs and income improvements for ever-greater proportions of the population.

Ensuring social effectiveness: strategies and lines of action

Competitiveness policies must be socially effective, i.e., they must effectively contribute to the enhancement of opportunities and freedoms, including the generation of sustained and relevant real income increases for the majority of the population. Obviously a competitiveness policy package cannot on its own secure the full attainment of these objectives, but it may positively contribute towards them through the effects of combining the strategies already mentioned (i.e. technological learning and innovation; and complementarities and linkages) and the Strategy for Human Capital and Social Capital formation.

In relation to human capital, the obvious actions consist of education in the formal system and training within the production sectors; in the social capital areas the actions consist of inducing positive impacts in the urban informal sectors and the rural low-productivity sectors by promoting synergies between them and the economy-wide reforms. The connections between economic
policies and social goals are very important for the sustainability of development in many developing countries, where social exclusion and political polarization are rooted in the inability of the "modern economy" to provide jobs and sources of income for a substantial part of the population. The "social effectiveness" of a competitiveness policy must pass this test.

Mainstreaming an environmental sustainability strategy in competitiveness policy

There are positive environmental impacts which may indirectly derive from the attainment of specific goals of a competitiveness policy in the economic dimension. However, mainstreaming direct environmental considerations in competitiveness policies is a need for developing countries, based on three considerations. In the first place, complying with environmental standards is increasingly important to secure access for exports from developing countries to many markets. Secondly, trends shown by the majority of developing countries' trade, based on an increase in exports of commodities supported in natural resources, lead to increased rates of exhaustion of their natural capital. Additionally, there is also a trend to increase exports based on potentially degrading processes, which entails both a deterioration of their own environment and possible market-access limitations. Finally, bio-diversity, if properly managed with a sustainable perspective, may become a concrete and very important competitive advantage for many developing countries.

In consequence, mainstreaming an Environmental Sustainability Strategy in competitiveness policies would be a necessity for developing countries, and policy instruments should be available to them in order to make its implementation feasible.

Inequality and poverty effects of the combined application of trade liberalization and the trade-supported strategies for sustainable development

Not all the instruments that a society can use to achieve its aims of equality and eradicating poverty are to be found in the fields of competitiveness and trade, nor are they the most important. But the strategies discussed here, managed together under appropriate guidelines, can help to control some of the adverse trends referred to.

These are not only the strategies relating to human capital and social capital, but all trade-supported strategies for sustainable development (TSDS) as summarized in Box 1.2 below. The Box shows the most important contributions that the TSDS can make to improving income distribution and alleviating poverty, and include ideas on macroeconomic policies since the latter have a very great influence on these two expressions of inequality.

Summarizing: synergies and intertwined effects of the trade-supported strategies

By combining trade liberalization and measures from the four Trade-supported Strategies for Sustainable Development, policies of developing countries may expect to attain economic, social and environmental benefits from their integration into global trade, as economic, social and environmental processes involved in integration of a country in the global economy are intertwined.
Box 1.2 Illustrations Of The Guidelines That Competitiveness Policies Should Follow To Maximize Their Contributions To Equitable Income Distribution And Poverty Reduction.

Guidelines relating to human capital and relational social capital strategies

In addition to prioritizing public spending that maximizes access to education and health (see macroeconomic guidelines below), the following two cross-cutting guidelines can be applied to sectoral policies in general:

- foster chains of cooperation between micro-businesses and other forms of cooperation that connect the informal sectors and the main body of the "modern" economy; and
- use performance requirements, whether or not based on incentives, designed to increase firms’ participation in initiatives for training the labour force.

Guidelines on policies relating to development of production sectors

Regarding policies relating to production, measures such as the following deserve to be highlighted:

- promoting internal complementarities and linkages, and fostering chains of SME suppliers;
- providing access to credit for SMEs, micro-enterprises and entrepreneurs in the informal economy.

General macroeconomic guidelines

Macroeconomic policy must be based on general principles relating to equilibrium and liberalization, but they must be applied after being adapted to the local institutions and conditions. In addition, this macroeconomic framework must take account of guidelines such as the following:

- give priority to public spending aimed at overcoming poverty, giving special priority to improving access to education and health; and the formation of human capital in general; and eliminate regional and ethnic bias in public spending.
- minimize the volatility of growth using appropriate mechanisms in the international exchange and finance fields, and stabilization funds where there is high exposure to shocks. Where adjustment programmes are essential in response to the impact of shocks, implement the necessary countervailing measures to limit the regressive effect of such adjustments.

Source: Adapted from Corrales (2007a).
The matrix in Table 1.1 above illustrates how the effects of the policy actions in the four Trade-supported Strategies for Sustainable Development may take place. From the viewpoint of sustainable development goals the table shows how many policy measures belonging to the four basic strategies converge on single goals in the economic, social and environmental spheres.

For instance, the measures under the learning and innovation strategy can reinforce environmental sustainability goals, while the measures under the environmental sustainability strategy can help to improve productivity or equality. Another example of this is the goal of increasing the effects of employment and knowledge spill overs, to which all the policy measures illustrated, belonging to all the strategies, contribute.

To round off all these arguments, the integration of a developing country into the global economy through trade can bear fruit in the various spheres of sustainable development, provided that trade liberalization is combined synergistically with development strategies such as those introduced above.

<table>
<thead>
<tr>
<th>POLICY ACTIONS IN THE TRADE-SUPPORTED STRATEGIES</th>
<th>SUSTAINABLE DEVELOPMENT GOALS</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>ECONOMIC SPHERE</td>
</tr>
<tr>
<td>Learning and Innovation</td>
<td></td>
</tr>
<tr>
<td>Promote production and exports of higher knowledge content goods &amp; services (LI-1)</td>
<td>x</td>
</tr>
<tr>
<td>Support R&amp;D and innovation for product differentiation and process efficiency (LI-2)</td>
<td>x</td>
</tr>
<tr>
<td>Increase compliance with technical, environmental and health standards in processes and products (LI-3)</td>
<td>x</td>
</tr>
<tr>
<td>Environmental Sustainability</td>
<td></td>
</tr>
<tr>
<td>Support local capabilities in environmental goods, services and technologies (ES-1)</td>
<td>x</td>
</tr>
<tr>
<td>Foster sustainable use of biodiversity-based advantages in trade (ES-2)</td>
<td>x</td>
</tr>
<tr>
<td>Interiorize externalities and incorporate best environmental practice in production (ES-3)</td>
<td>x</td>
</tr>
<tr>
<td>Complementarities and Linkages</td>
<td></td>
</tr>
<tr>
<td>Promote competition; promote transparency in public policies (CL-3)</td>
<td>x</td>
</tr>
<tr>
<td>Enhance &amp; use + externalities in the territory (e.g. through infrastructure &amp; clustering) (CL-2)</td>
<td>x</td>
</tr>
<tr>
<td>Promote and support downstream processing and upstream chains of SME suppliers (CL-1)</td>
<td>x</td>
</tr>
<tr>
<td>Trade policy to improve net labour content in trade balance (e.g. through tariff modulation) (CL-4)</td>
<td>x</td>
</tr>
<tr>
<td>Human &amp; Social Capital</td>
<td></td>
</tr>
<tr>
<td>Human capital formation at all levels within formal education system &amp; productive sector (SH-1)</td>
<td>x</td>
</tr>
<tr>
<td>Cooperation networks to increase scale and connect informal sector units to formal economy (SH-2)</td>
<td>x</td>
</tr>
</tbody>
</table>

Source: "Developing-Country Policy Issues in Reconciling Trade Liberalization and Sustainable Development Goals" (Corrales, 2007a).
1.3 Risk Management, Vulnerability and Resilience to External Shocks and Disasters: A Major Challenge to Developing Countries' Competitiveness

National economies in the process of deep integration into the world perform as open systems, subject to risks of shocks which may not depend fundamentally on the development policies that they apply at national level. These shocks may originate in financial and price shocks and also in disasters involving natural hazards. In certain cases, the large-scale discontinuities that these events may cause can lead to huge instantaneous losses of competitiveness gains, which may be very difficult for the affected country to recover from, particularly if this country’s economy is small. In fact, unless risks of these events are properly managed by developing countries in all areas of development, a large proportion of the efforts made in implementing trade-supported strategies for sustainable development, or other development strategies, may be spoiled.

In other words, to ensure that the long-term path is sustainable, it is not only necessary to implement the appropriate competitiveness policies aiming at medium and long term goals; there is also a need for policy management that is aware of the risks of disasters involving natural phenomena and of those relating to other "external shocks".

Risk management more directly related with competitiveness policies and the trade-supported strategies that we have briefly introduced (i.e. technological learning and innovation; creation of complementarities and linkages; human capital and social capital formation; and environmental sustainability) must be focused on two kinds of measures. The first is minimizing risks by means of ex-ante measures, i.e. by controlling exposure and introducing prevention practices. The second is strengthening institutional and economic capabilities to recover; i.e. enhancing resilience.

However, since the economic resilience of an economy to disastrous events may be expressed in terms of the ratio of the damage caused by their typical disasters to their Gross Domestic Saving, this draws attention to the close relationship that there can be between a country’s resilience and its net export earnings. Indeed, for any economy, but in particular for small economies subject to frequent disasters, there is a strong feedback between disasters and international competitiveness. In small economies not only is competitiveness adversely affected by external shocks and disasters, but a high level of competitiveness could improve the capability to recover from disastrous events.

Trade-supported strategies, competitiveness and vulnerability to economic shocks

In terms of structural solutions, the contribution that trade-supported strategies can offer for (trade-related) price shock risks is to diversify production and exports, and to upgrade technology.

Regarding financial shocks, trade-supported strategies would be related to the conditions under which the agreements on investment and the chapters on investment in the free-trade agreements are negotiated. Not only would the conditions of financial and exchange policy have to adopt precautionary rules (e.g. the Basel rules), but the rules on foreign investment treatment would also have to pay attention to the conditions relating to the recognition of various types of investment “covered investment”. These rules would have to include safeguard clauses that could be activated as required when there were serious indications of risk.

Disasters related to natural hazards: policy measures to reduce vulnerability and increase resilience in small economies

Regarding disasters involving natural phenomena, there is clear evidence that developing countries are suffering them more frequently. In the case of small countries, these disasters may have a significant magnitude in relation to the size of the economies, making them increasingly vulnerable. Aside from their exposure to disasters, small developing economies often
experience severe economic and social restrictions regarding their integration into the world economy. Added to the circumstances of the disasters, especially the effects of recession associated with disaster events, these economies can fall into vicious circles of stagnation and poverty, characterized by serious limitations for implementing improvements in competitiveness, and be unable to recover.

Actually, the resilience of small developing countries may be choked off to the extent that they become unable to recover without major external intervention, not only in terms of humanitarian aid after the disaster, but also mainly for reconstruction and prevention, and for the generation of greater resilience of their own.

Indeed, the situations experienced by small and vulnerable developing economies may not be resolved without far-reaching action of two types. Firstly, own action through policies to develop production and competitiveness, such as those we mentioned when referring to the trade-supported strategies. Secondly, international cooperation going beyond immediate aid after disasters and taking a form that is not a burden on those economies.

It is not merely that these countries require international aid for immediate humanitarian assistance when the events occur, or reconstruction loans. In small economies subject to frequent disasters it may be necessary for international cooperation to take numerous measures and in some cases major ones, for various purposes. Those purposes include rapid recovery from losses in international competitiveness; reconstruction of infrastructure in such a way as to prevent similar losses from future events; and especially mainstreaming risk management in all public and private activities involving strategic planning of development, regional planning and planning of future investment in general.

Only if international cooperation takes such steps can it help these small countries to improve their own capability to recover without compromising the investment they need for their future development.

1.4 A Framework for Applying the Situational Approach to S&DT Negotiations related to Competitiveness and Vulnerability Issues of Developing Countries

In practical terms, the application of the Situational Approach to S&DT to the fields of competitiveness and vulnerability implies creating suitable mechanisms in those fields for maximizing access for all developing countries to the basic benefits of S&DT and to such additional benefits as correspond to the specific development situations experienced by the countries.

Although the Doha-mandated revision on S&DT is in principle the task of the Committee on Trade and Development (CTD), in the committee the negotiations really take place on the most systemic issues of S&DT and all those that can affect developing countries’ competitiveness policies and the vulnerability of the small economies, not directly related to the agricultural sector or non-agricultural tariffs.

The mandates under which the Situational Approach must produce its recommendations on vulnerability and competitiveness-related situations

The official mandates under which the negotiations on S&DT are taking place that affect both competitiveness and the vulnerability of small economies are basically paragraph 44 of the Ministerial Declaration and the “July (August 2004) Framework”, and paragraphs 35 to 39 as well as annex F of the Hong Kong Ministerial Declaration.

The negotiations relating to small vulnerable economies also have specific mandates in paragraph 35 of the Doha Declaration, paragraph 1 of the July Framework; paragraphs 21 and 41 and paragraph 8 of Annex C to the Hong Kong Declaration.
Table 1.2 shows a simplified view of the location of the negotiations by negotiating body, organizing them by the three dimensions through which they are related to development policies and trade rules (i.e. market access and fair trade for developing country exports; policy spaces; and resources for development support).

### Table 1.2 Bodies Where Negotiations On S&DT Take Place (Organized By The Three Dimensions In Which Trade Rules And Development Strategies Interact)

<table>
<thead>
<tr>
<th>S&amp;DT Negotiation</th>
<th>MARKET ACCESS &amp; FAIR TRADE FOR D.C. EXPORTS</th>
<th>SPACES FOR DEVELOPMENT POLICIES (POLICY SPACES)</th>
<th>RESOURCES FOR DEVELOPMENT SUPPORT</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Tariffs Rules</td>
<td>Border measures</td>
<td>Behind the border measures</td>
</tr>
<tr>
<td>S&amp;DT in Market Access other than agricultural</td>
<td>NAMA</td>
<td>NAMA</td>
<td>NAMA</td>
</tr>
<tr>
<td>S&amp;DT for supply-side competitiveness policies</td>
<td>CTD-SS</td>
<td>CTD-SS</td>
<td>CTD-SS</td>
</tr>
<tr>
<td>S&amp;DT related to small countries’ vulnerability</td>
<td>NAMA</td>
<td>NAMA</td>
<td>NAMA</td>
</tr>
</tbody>
</table>

Source: An approach to Special and Differential Treatment based on “Development Situations” (Policy paper; ICTSD 2007).

The general principles and rules in the first component of the SA proposal

The first component of the proposed SA contains a set of principles and general rules, on the one hand, and the Common Benefits of S&DT to which all the developing countries would have access, on the other.

Six general principles would constitute the fundamentals of a Situations-based S&DT system, which in addition would reaffirm the character of S&DT as a tool for development and not only as an instrument to facilitate the developing countries and LDC’s adjustment to the international trade commitments.

Together with the principles, the general rules, after been agreed by the member countries, could constitute a framework for the review of all S&DT as mandated in Doha, where the assessment of the proposals presented by developing countries and LDCs would be accomplished. In practical terms the general rules should be limited in number, in order to facilitate the negotiations, and should be applicable to all the WTO agreements.
Box 1.3 Ideas on the General Principles and General Rules of the Situational Approach

**General Principles**

**P1**: The fundamental purpose of the Special and Differential Treatment (S&DT) is to help developing countries and LDCs to make their integration to such system an effective instrument for their sustainable development, and therefore they will address the mentioned capacities and development needs. The compliance with disciplines and trade rules to be requested from developing countries and LDCs in their integration to the multilateral trading system, shall take into account the development needs that they experiment and shall be commensurate with their economic and institutional capacities;

**P2**: The positive contribution that trade liberalization might have to the sustainable development of developing countries and LDCs is recognized, particularly when it is combined with other development strategies, such as technology development and innovation; human capital accumulation; development of productive chains; and environmental sustainability. Based on this, S&DT shall contribute to enable developing countries and LDCs to implement the policies that would render the combinations of those strategies feasible, in order to address the economic, social or environmental needs they face;

**P3**: S&DT involves collective commitments from all WTO members and specific obligations from the developed country members, all with mandatory character in accordance with the stipulations of the multilateral trading system agreements;

**P4**: Framed in the considerations made above, two sets of S&DT provisions will constitute *Basic Benefits*, the first of which will be accessible to all developing countries, including LDCs, and the second to be accessible to LDCs. A third set of S&DT provisions will constitute *Additional Benefits* that will respond to specific situations, and will be accessible to the countries that are experiencing those situations;

**P5**: Given that Additional Benefits of S&DT would constitute extraordinary supports associated with the existence of specific development needs, and that some of them would involve flexibilities that could have negative spillovers on other member countries, those Additional Benefits should terminate once the problems or specific needs are overcome. This implies that there is a need to monitor progress on problem solving, attained by countries that have received additional benefits; and

**P6**: LDCs will advantage from all S&DT provisions, whether they are Common Benefits or Additional Benefits.

**General Rules**

In order to guarantee that the S&DT provisions become effective and enforceable, and to facilitate the implementation of the Situational Approach to S&DT, the General Rules would implement the Principles in the direction of:

**R1**: To assure that the benefits of S&DT referred to Market Access are not impaired, nullified or circumvented by means of the interpretation of the S&DT or the application of other trade rules by the importing countries (e.g. to assure that the imposition of sanitary or phitosanitary standards upon imports originating from LDCs has an appropriate counterpart in technical assistance to the exporters; or to prevent the arbitrary interpretation and application of the *De Minimis* norms in relation to antidumping, safeguards and textiles amongst others.).
Box 1.3 continued

**R2**: Contribute to making effective S&DT provisions in the various agreements referred to flexibilities in rules (provide effective policy spaces), to allow the implementation of supply-side policies oriented to various legitimate development purposes, such as regional integration schemes; diversification of production; innovation and technology development; environmental sustainability; social and human capital development; rural development and food security. (e.g. ensuring that the procedures to access provisions are not made too cumbersome);

**R3**: To guarantee that agreements to be eventually reached in the revision of the respective *acquis*, which might imply making certain technical assistance provisions obligatory, are enforceable; that the mentioned assistance responds to the necessities of the beneficiary countries and to the fundamental purpose of the S&DT; and that the cost of the assistance to be taken by the beneficiary countries is commensurate to their respective financial capacities (which could require that the respective rules define modalities and benchmarks for the obligations on technical assistance); and

**R4**: To establish a transparent procedure for the approval of the Situations on which the additional benefits of S&DT would be based, and to monitor the progress achieved by the beneficiary countries.

The legal architecture in which the second component (additional S&DT benefits) would be framed

The logic of the legal framework for Additional Benefits of S&DT according to the proposals of the Situational Approach is that there should be an Initial List to bring into force what has been agreed, which the countries concerned should refine and negotiate. The specific framework proposal for the additional benefits is summarized in Box 1.4.

Box 1.4 Ideas On a Process To Frame The Additional S&DT Benefits In The WTO Architecture

**Recognition (approval) of a Development Situation and the associated eligibility criteria**

The CTD SS, at the request of the developing countries and or LDCs concerned: i) would approve the “Development Situations” and indicate special trading or development needs characterizing each of them; ii) would agree the criteria and indicators to be used to draw up the list of countries eligible for each Situation and iii) based on the agreed criteria and indicators, and taking account of the arguments of the developing country members concerned, would define the relevant list of eligible countries. The LDCs would automatically be included in the eligibility lists of any Situation agreed.

**Approval of the additional benefits corresponding to each situation**

Likewise the CTD SS (or other WTO body as appropriate), at the request of the developing country and/or LDC members concerned, would agree the S&DT additional benefits (to be granted to the list of eligible countries for each Situation) subject to the rules and provisions of each Agreement under which the additional benefits were requested.

**Monitoring progress on Situations and periodic revision of the eligibility lists**

Every five years, the CTD SS will assess progress in overcoming the special trade and development needs of each Situation, with a view to contributing to progressive compliance of the beneficiary countries with the general rules of the multilateral trade system. The assessment will be based on a report commissioned by the CTD SS from a special group of advisors, including two experts
designated by the developing country members and LDCs on the relevant eligibility list, and four specialists from international organizations, one for UNCTAD, one for the UNDP, another for the World Bank and another for the WTO Secretariat. As a result of this assessment, the CTD SS would decide whether or not to change the list of eligible countries, in view of the eligibility criteria corresponding to the situation and the progress made in terms of the indicators by the countries on the relevant list. Any developing countries excluded from an eligibility list as a result of the assessment, would automatically be entitled to a 3-year transition period to phase out the use of the relevant additional benefits. Countries on the list that were included in it when they were LDCs may only be excluded if they ceased to be LDCs at least three years before the assessment.

Initial lists of Situations, additional benefits and eligible countries

Until new lists of Situations and additional benefits are agreed or the first assessments are produced, the Initial Lists of situations, eligible countries and additional benefits at Annex "A" will be considered valid. Annex "B" contains the technical details showing how the Initial Lists were made up.

1.5 A Synoptic View of the Competitiveness and Vulnerability Situations studied in the ICTSD Project on the Situational Approach to S&DT

Six development situations related to competitiveness of developing countries and vulnerability of small developing economies were studied in the ICTSD project dedicated to the Situational Approach, to serve as a basis for identifying additional S&DT benefits. Two of these situations refer particularly to vulnerability and remoteness of small developing countries (SVE and SRE situations).

However, the assessment of the four competitiveness situations (COM-1 through COM-4 situations) draw a series of conclusions that are highly relevant to small developing countries, given the fact that many developing countries in the list of the SVE and SRE situations are also part of the COM-1 and COM-3. It must be taken in account that any developing country may be part of the lists of various development situations, therefore being eligible to the sets of additional benefits associated to the latter.

Developing countries altogether: empirical evidence on trade and development characteristics

To begin with, it is important to note that while the developing country category used in the WTO is composed of "self-selected" members (as compared with the LDC category that responds to objective criteria defined by the UN), there is empirical evidence of common trade and development features amongst members of the self defined group. However, it is also useful to understand the empirical evidence found on the differing competitiveness levels within the group of developing countries.

If we look at the median of the distribution of all WTO member countries in relation to per capita GDP, export concentration indices, and GDP volatility indices (i.e. the value of the indicator dividing the statistical population in two groups with the same size, 50 percent), we can identify two statistical classes according to each feature: the "worst half" and the "best half".

Three very broad, yet interesting conclusions derive from the analysis of the resulting classes. Figure 1.1 shows the boundaries of the three classes as circumferences surrounding the lists of developing countries falling in each class.
The first conclusion is that the universe of WTO member countries can be subdivided in two clearly-cut groups (developed and developing countries), almost exactly reproducing the list of self defined “developing” countries by putting together the three worst-off classes.  

The second conclusion refers to the very low correlation existing between the features that apparently reproduce the developing country list, on the one hand, and the revealed competitiveness of countries, in the other. In other words, being a developing country according to the three features used to define the list of developing countries in Figure 1.1 says very little about the competitiveness of the countries involved.  

The third conclusion would be that variability instead of homogeneity would be a reasonable (condensed) statistical description of the trade-development links within the developing countries’ list.  

The three conclusions, taken together, led the researchers to further explore indicators of revealed competitiveness to shed additional light to the empirical evidence commented on common trade and development features of developing countries. An additional exercise was therefore conducted to explore broad circumstances and commonalities amongst developing countries regarding revealed competitiveness and level of success in the integration to the global markets.
International market share levels, export concentration and per capita GDP were used as indicators to identify those broad circumstances. Sub-groups E, F, G and H shown in Figure 1.2 cluster countries according to decreasing levels of revealed competitiveness and apparent economic success, basing the characterization on the systematic application of the mentioned indicators.\(^\text{13}\)

There are clear differences between groups E and F in Figure 1.2 on the one hand, and groups G and H on the other, regarding revealed competitiveness, as developing countries in Groups E and F have market shares above the world's average (higher than 0.68 percent), while market shares of countries in group G are placed between 0.08 percent and 0.68 percent, and the rest of developing countries (Group H) have market shares below the median (below 0.08 percent).

To conclude this part of the analysis, it is important to note that if the same commented criteria were to be applied to those countries that have not opted for WTO developing country status (by excluding "developed countries"), in the equivalent E’ and F’ groups (market shares above 0.68 percent), 18 of those 37 economies (48.6 percent) would be included. The rest of "developed countries" belong to groups G’ and H’, including those 8 economies that apparently share with developing countries the trade-development features that reproduce almost perfectly the developing countries’ list, as discussed in previous sections.

It seems to be clear, from the perspective of revealed competitiveness, that developing countries in groups E and F would be competing globally with developed countries in classes E’ and F’ (Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Ireland, Italy, Japan, Netherlands, Poland, Spain, Sweden, Switzerland, the United Kingdom and the United States).

A map of development situations studied, related to competitiveness and vulnerability

As part of the ICTSD project on the Situational Approach to S&DT, six situations related
to vulnerability and competitiveness that could entail additional S&DT benefits were assessed in terms of their economic, social and environmental features. Policy actions that could be implemented to cope with the development needs, problems and constraints involved in each situation were also studied. The main purpose of these illustrations was to show how a great variety of characteristics frequently present in developing countries tend to cluster and may be addressed with context-specific policy packages.

Table 1.3 offers a "map" showing features that are present in each of the situations studied on competitiveness and vulnerability.

The first situation (COM-1) is characterized around economic problems frequently faced by weak economies in the process of joining the international economy. Countries that find themselves in this situation show a very high export concentration on a few agricultural products and/or manufactures with low added value, a very small international market share, low attractiveness to foreign investment except in the exploitation of a few natural-resource based commodities, and a serious difficulty in complying with international standards (e.g. SPS).

In the second and third situations (COM-2 and COM-3) the main problems and objectives are related to complementarities and knowledge-technology strategies but both have social and environmental features. COM-2 refers to economies dependent on non-renewable resources and COM-3, to economies that have tried to change their export specializations into manufactures but feature important deficiencies in internal linkages and technological capabilities.

Situation COM-4 is featured around environmental problems and objectives, and strategies for learning combined with environmental sustainability strategies play an important role. This Situation incorporates many features of the environmental problems in developing countries in general but also has features related to the lack of productive linkages.

Finally, situations SVE and SRE relate to vulnerability and remoteness issues in small economies. These situations are the main object of this paper and will be discussed in greater detail in chapter 3, which will also comment on competitiveness situations COM-1 and COM-3. Actually, an interesting finding of the studies conducted is that a large proportion of small and vulnerable countries, i.e. developing countries in the lists of situations SVE and SRE are also included in the lists of competitiveness situations COM-1 and COM-3. Situation COM-1 implies very low productivity and weak productive linkages between exporters and the rest of the economy; a high level of growth volatility and a strong trend of deteriorating terms of trade. Situation COM-3 occurs in developing countries that have already engaged in an industrialization process but have nonetheless been unable to overcome «shallow integration of production» circumstances, which in some extreme cases can be limited to assembly of imported parts.
### Table 1.3 Features in Situations Studied on Competitiveness and Vulnerability

<table>
<thead>
<tr>
<th>FEATURES IN THE SITUATIONS STUDIED</th>
<th>COMPETITIVENESS</th>
<th>VULNERABILITY</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>COM 1</td>
<td>COM 2</td>
</tr>
<tr>
<td>Economic features</td>
<td></td>
<td></td>
</tr>
<tr>
<td>High dependence on a few export lines or markets</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>High Volatility of export revenues, Terms of Trade or GDP</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>High vulnerability/low resilience to external shocks and disasters</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>Abnormally high transportation costs to access international markets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commercial presence in international markets</td>
<td>Not necess. low</td>
<td>x</td>
</tr>
<tr>
<td></td>
<td>Very low; fragile</td>
<td>x</td>
</tr>
<tr>
<td>Export specialization other than agriculture</td>
<td>Mining and/or hydrocarbons</td>
<td></td>
</tr>
<tr>
<td></td>
<td>High-tech manufactures</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Other manufactures</td>
<td>x</td>
</tr>
<tr>
<td></td>
<td>Services</td>
<td></td>
</tr>
<tr>
<td>Low technological and innovative capacity</td>
<td>Low capacity to comply intl stds</td>
<td>x</td>
</tr>
<tr>
<td></td>
<td>Low-tech X specialization</td>
<td>x</td>
</tr>
<tr>
<td></td>
<td>Apparent high-tech X spec</td>
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<tr>
<td></td>
<td>Maquila type low-tech X</td>
<td></td>
</tr>
<tr>
<td></td>
<td>NNRR–based quasi–enclave</td>
<td>x</td>
</tr>
<tr>
<td>Low complementarities and presence of linkages</td>
<td>High NNRR-based export specialization</td>
<td>Renewable low envtl practices</td>
</tr>
<tr>
<td></td>
<td>Non renewable</td>
<td></td>
</tr>
<tr>
<td>Environmental features</td>
<td></td>
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<tr>
<td>High export specialization in potentially contaminating products</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Low capabilities to comply with internat environmental standards in exports</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Low domestic supply capacity in environmental services &amp; technology</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Opportunities in sustainable bio–trade not taken advantage of</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>Social features</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Need to increase quality and quantity of human resources</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Precarious connection of informal actors to “modern” economy</td>
<td>x</td>
<td>x</td>
</tr>
<tr>
<td>Per capita Income or GDP</td>
<td>Not necess. low</td>
<td>x</td>
</tr>
<tr>
<td></td>
<td>Low</td>
<td>x</td>
</tr>
<tr>
<td>High poverty levels</td>
<td>x</td>
<td>x</td>
</tr>
</tbody>
</table>
2. THE NEGOTIATIONS UNTIL 2006: CONVERGENCE AROUND A “CHARACTERISTICS” APPROACH

To understand the difficulties encountered in fulfilling the Doha mandate, it is essential to track the progress of the negotiations since the agreement in November 2001 on the paragraph 35 mandate. This chapter will review the history of the talks on small and vulnerable economies at the WTO, highlighting the ways in which SVEs have been characterised and the linkages that have been made to requested flexibilities in WTO rules (ICTSD; WT/COMTD/SE/M/1-14). We see that the process in advancing the interests of SVEs has been anything but smooth, and while they have had relative success in garnering the attention of WTO Members, moves to craft actual rules have been closely tied up with the question of eligibility for their special and differential treatment.

The Doha Declaration gave the General Council responsibility for the carrying out of the SVE mandate, and it was not until 25 January 2002 that informal consultations began amongst Members speaking on behalf of the SVEs and other countries on the creation of a framework to carry out the SVE work programme. After that consultation and one held on 5 February, both under the auspices of the Chair of the General Council, and others held by Deputy Director-General Mr. Ouedraogo between 11 and 25 February, WTO Members agreed to a framework to carry out negotiations at a 1 March 2002 meeting of the General Council (WT/L/447).

2.1 The Main Scenario: Talks in the CTD–DS

Based on revisions to a draft proposed by the proponents of the SVE work programme (hereafter the PSVEs) (WT/GC/W/468) submitted by Deputy Director-General Ouedraogo (WT/GC/W/469), the framework calls for the CTD to be responsible for the SVE work programme, to regularly report to the General Council on progress, and to hold dedicated sessions of the CTD (“CTD–DS”) on the mandate under the Chairmanship of the Chair of the CTD. As early as the General Council meeting, tensions were evident regarding how the mandate was to be fulfilled; while all the PSVEs stressed the importance of the work programme to their countries and the integrity of the multilateral trading system overall, several of them noted that creative approaches to addressing the problems of small economies would be necessary to avoid defining a sub-category of countries, as per the mandate for negotiations and the political sensitivity of differentiation amongst developing countries. Other PSVEs called for “realistic differentiation which provided meaningful S&DT treatment to address their demonstrated development needs”. The framework thus also calls for the Secretariat to undertake studies on impact of WTO rules on small economies; on the constraints faced by small economies; and on the effects of Trade Liberalization on small economies.

The initial meetings: the opposition to perceived intents of further differentiating developing countries

At the first meeting of the CTD–DS on 25 April 2002, held under the Chairmanship of Ambassador Toufiq Ali of Bangladesh, the focus was on the draft work programme submitted by the PSVEs (WT/COMTD/SE/W/1). Produced in reaction to post-Doha queries regarding the definition of a SVE, W-1 suggested that “small developing economies” share most or all of a list of characteristics. These included insignificant share of international trade; island or landlocked status; small populations; prevalence of natural disasters; limited land availability; physical isolation; and export concentration. The proposal, which was to set the stage for years of negotiations, suggested that “small developing economies” share most or all of a list of characteristics. These included insignificant share of international trade; island or landlocked status; small populations; prevalence of natural disasters; limited land availability; physical isolation; and export concentration. The proposal, which was to set the stage for years of negotiations, suggested that these characteristics have “implications” -- a term that was later to be replaced with “problems” -- that adversely affect their trade and development status, including high trade openness; export dependency; imperfect, small markets; economic rigidity; and vulnerability to economic shocks. W-1 also noted that because of their characteristics, they are classified as high risk by international financial markets, which
in turn makes foreign investment difficult to attract. At the same time, the PSVEs suggested that they have very limited trade policy-making capacity which adversely impacts on their ability to promote and defend their interests at the WTO.

In a reaction that would be echoed repeatedly in following years, the US, with the support of New Zealand and Chile, suggested that many of these characteristics and implications were not unique to small economies, but rather applied to most developing countries, and asked whether certain parts of the proposal did not amount to a demand for the creation of a separate sub-category of small developing economies. The US asked the PSVEs to clarify further the difference between SVEs and other developing countries, and several of the PSVEs suggested that it was the combination of factors that affected SVEs uniquely.

At the second meeting of the CTD-DS, on 1 July 2002, a proposal from Macao, China was tabled that suggested that smallness is reflected in a small market, population and geographical size and leads to inefficient resource allocation and inability to access economies of scale (WT/COMTD/SE/W/2). The proposal suggests that small economies have a small share in world trade and are reliant on their major trading partners, and notes that small economies are more vulnerable to changes in trade rules and regulations, technological changes and shifts in trade flows. A second proposal, from the PSVEs, contained concrete proposals for S&DT for SVEs in specific WTO Agreements along with explanations of why they are necessary to address the needs of SVEs.

In response, the US reiterated that it was not willing to consider the creation of a new category of Members. A number of Latin American developing countries also raised concerns that elements of the proposal would provide too much flexibility away from the rules set out in the WTO rules on, for example, subsidies and anti-dumping. Instead, along with the US, they called for “factual analysis” on the “state of play” and “description of problems” in SVEs that was driving the demands for special rules.

A review of the literature on small economies was presented by the WTO Secretariat at an informal meeting of the CTD-DS on 10 September 2002 (WT/COMTD/SE/W/4). The report concludes that economies with small populations have higher GDP volatility, are more open to trade, have higher international aid and more concentrated production and export structures. However, it notes that small-population states do not as such have lower GDP, growth rates, development indicators or policy-making capacity. While all Members welcomed the document, the PSVEs suggested that it relied too much on a population-size definition of smallness, and argued that it would be more appropriate to define smallness based upon share of world trade, as supported by a 2001 Michael Davenport study.

The third session of the CTD-DS was held on 4 November, and featured a presentation of a document from the PSVEs containing their responses to US questions on W-3 (WT/COMTD/SE/W/7) and two new reports from the Secretariat. The questions, for the most part, asked for more specificity on the problems experienced by the SVEs, questioned whether the problems were not also experienced by other developing countries, and suggest that the proposals for agreement-specific changes to the rules should be taken up in the relevant negotiating group. While many of the specificity questions were averted, the question of uniqueness of SVE problems was addressed by the statement that the SVE problems are not the “same” as those facing other developing countries.

The first report from the Secretariat, entitled “Trade and Economic Performance: the Role of Economic Size?” (WT/COMTD/SE/W/5), builds on the literature review and attempts to provide more analytical depth on the relationship between smallness and key economic indicators. However, it continues to use population size as the indicator of economic size as it is “the approach most frequently taken in the literature”. It finds that small economies face restrictions in diversifying exports owing to lack of access to economies of scale; that economies are unlikely to face higher transport costs owing to their small size, but rather owing to their location; that small economies do not experience higher volatility in export earnings; that small economies
experience more variation in their GDP; that countries with smaller populations do not have smaller GDP per capita growth; and that small economies may have more problems adjusting to changes in trade policy. It also finds that as Members’ share in world trade grows, transport costs decrease and GDP per capita increases. During the meeting, the PSVEs suggested that the document was an improvement on the literature review, but reportedly expressed surprise at the findings that small economies do not systematically experience higher volatility in their export earnings than large economies. The PSVEs did however say that overall the paper “vindicated” the arguments made by the PSVEs over the years. The second paper, entitled «WTO Provisions Potentially of Particular Interest to Small Economies» (WT/COMTD/W/6), was a first attempt at compiling some provisions that could be of interest to or impact small economies.

At the meeting, delegates clashed on whether they had completed the first stage of negotiations mandated by paragraph 35, namely of identifying the trade-related issues relating to small economies, and if the talks had advanced enough to take the second step, that of framing responses to those trade-related issues. While the PSVEs thought the two steps had been completed, and they were ready for the third step of asking the General Council to make recommendations for action, the US and EU suggested that more work was necessary on the first step. The US once again noted that Members would have to “walk a fine line” in coming up with solutions to SVE problems that did not amount to differentiation.

At the following fifth meeting of the CTD-DS on 13 July 2003, the PSVEs under the leadership of Mauritius chose to highlight the vulnerability of SVEs to natural disasters in the interventions. Compounded with their other characteristics, such as lack of economies of scale, high transport costs, export concentration and poor natural resources, they noted that the trade of SVEs was so small that changes in rules to favour their growth trajectories would not cause market distortions. Based on informal consultations held by the Chair on 3 July, the Chair noted that he had put together document W-9 as a report to the General Council, and delegates adopted the report. The PSVEs suggested that timely action was needed on the second phase of the negotiations.

A number of informal consultations were held in the months directly before and after the failed September 2003 Cancun Ministerial Conference in which the PSVEs met with other delegates to look directly at the proposals for changes to rules in W-3. At the sixth CTD-DS meeting, held on 17 October 2003, delegates simply encouraged the PSVEs to continue to make revisions to their proposals and asked them to come back with new text. Paraguay, Mongolia and Bolivia also briefly highlighted a statement they had made at Cancun on the needs and characteristics of landlocked countries WT/MIN(03)/W/23 The Chair suggested that the land-locked countries come up with concrete proposals aimed at addressing their concerns to complement W-3.

In the proposal submitted by the three countries at the subsequent meeting, held on 12 May 2004, they call themselves “landlocked and small economies” and set out specific proposals for treatment of small economies (WT/COMTD/SE/W/9).16

At the same meeting the PSVEs tabled a document elaborating on and refining the proposals for some of the changes to WTO rules suggested in W-3 (WT/COMTD/SE/W/11).17

The reactions to the papers followed the usual trends, with Canada, Australia, the US and Chile repeating that they did not support the creation of a new sub-category of Members, as per the paragraph 35 mandate, and that they were concerned that the two proposals “effectively serve” to create a new sub-category. Similarly, Japan questioned why the proposals tabled were only relevant for small economies, and with the EU and others also asked whether W-10 was aimed at addressing problems unique to landlocked countries, when the proposal nonetheless called for special treatment for SVEs overall. Overall, however, the meeting thus continued the focus of the negotiating group on the particular S&DT that the SVEs were demanding, rather than on the specific needs for the flexibilities or how...
such S&DT would be targeted at SVEs, however defined.

The eighth session of the CTD-DS, on 3 November 2004, was a short meeting in which the PSVEs, under the leadership of Barbados, said they were happy with the mention given to the SVE mandate in the WTO General Council decision on 1 August 2004 (the July Package, WT/L/579, 2004), and urged Members to build on the momentum generated by the Package to meet the end-2005 deadline for the work programme. That text says that "the trade-related issues identified for the fuller integration of small, vulnerable economies into the multilateral trading system, should also be addressed, without creating a sub-category of Members, as part of a work programme, as mandated in paragraph 35 of the Doha Ministerial Declaration."

Discussions were largely focused on procedural issues, wherein the PSVEs suggested once again that the first two steps of the negotiations had progressed to a point where Members were prepared to make recommendations for actions, while the US and other suggested such a move would be hasty. As a new member of the PSVE group, Cuba shared a description of SVEs similar to that stated earlier. It noted that export concentration and dependency; vulnerability to natural disasters; inability to affect terms of trade owing to low share of world trade; limited foreign investment; and geographical positioning led to a particular situation that demanded recognition, greater flexibility and treatment that responded to their specific developments needs. In reaction to earlier questions about the need for special rules for SVEs, which was linked to the issue of whether SVEs were "unique", the PSVEs noted that it was a combination of the disadvantages and the inability to deal with them that made small economies worthy of special consideration. The US stressed that it was important to not duplicate the work being done in other negotiating bodies, such as the CTD special session on S&DT. Reportedly, at this time the PSVEs began to consider the use of a "characteristic-specific" approach to link the needs of small economies with special rules at the WTO. Although they hoped this would enable them to surmount the ban on the creation of a sub-category, there was little clarity at this time on how such an approach would be operationalised.

A major turning point in the negotiations: the "characteristic-specific approach"

A major turning point in the negotiations came on 25 January 2005, when CTD-DS Chair Trevor Clarke tabled a new approach to the negotiations in an informal meeting of the group. Formally taken up at the official ninth meeting of the dedicated session on 21 February, the Chair’s approach essentially reframes the process to be used by the group to address the paragraph 35 mandate. Before the meeting, it was understood that the talks were to follow a three-step process, namely (1) the identification of issues or problems constraining the trade of small economies; (2) the framing of responses or solutions to those constraints; and (3) the formulation of recommendations for action to address the trade-related issues. Clarke, in his last session as Chair, proposed a new three-step process, namely (1) consideration of the use of characteristics to identify what can be accepted as small, vulnerable economies; (2) the consideration of the trade-related problems that could reasonably be attributed to those characteristics; and (3) framing responses to those trade-related problems that these countries could use.

Although the Chair’s approach gained broad support and would drive negotiations for some time, the distinction between the first two steps -- and their importance for determining eligibility for the new rules -- quickly came under fire. Brazil, Colombia, Ecuador, Egypt, Costa Rica, Mexico, India, Hong Kong and Peru suggested that the problems facing small economies should be dealt with first, while Cuba, El Salvador, Canada and the Dominican Republic preferred to first deal with the characteristics of small economies. Guatemala, Jamaica, Argentina, Sri Lanka, St Kitts and Nevis were interested in looking at both issues at the same time. The US, EU, Switzerland and Paraguay said they were flexible one way or the other.
The first group, composed mainly of larger developing countries, repeated their assertion that some characteristics of small economies probably applied to other developing countries. In informal talks, they told the PSVEs that it might not be in their interests to open up the issue of characteristics because it could open up a time-consuming, contentious debate about differentiation amongst developing countries. The second group of countries, who were largely PSVEs, said it made sense to start with the underlying causes of the problems facing small and vulnerable economies.

As such, they presented a paper (WT/COMTD/SE/W/12) affirming the Chair’s approach and setting out a list of indicative characteristics and problems of SVEs that continues to be considered as the standard description from the PSVEs. These included:

- Physical isolation, including as island or landlocked developing countries;
- Inadequate infrastructure;
- Insignificant participation in the MTS and minimal share in world trade;
- High degree of vulnerability;
- Small, fragmented and highly imperfect markets;
- Low competitiveness;
- Very open economies;
- Low productivity and insufficient supply;
- Domestic markets with imperfect and highly polarized structures;
- Economic rigidity with high adjustment costs;
- Export concentration;
- Undiversified production;
- Low supply of export services;
- Difficulty in attracting foreign investment;
- Dependent on very few export markets;
- Lack of adequate market access opportunities;
- High transport and transit costs.

Focusing on the characteristics, they argued, would help Members better understand the structural handicaps that prevent small economies from reaping the full benefit of the multilateral trading system. After lengthy negotiations, Members agreed to move forward by taking up steps one and two simultaneously, and then move on to the framing of systemic responses. On the heels of the mention of the SVE mandate in the July Package, the new three-step process injected new energy into the negotiations and launched a new, more intensive phase of the talks.

By making explicit mention of the importance of identifying the “characteristics” of SVEs, the PSVEs thus intended to try to address the concerns raised in previous sessions by developed countries such as the US, Canada and EU regarding how the new rules would be applied only to SVEs. By defining the characteristics and problems of SVEs, and linking them to solutions, they hoped it would strengthen the perceived link between the new rules and the concrete needs of SVEs that arose owing to their particular “situation” or “characteristics”, and also possibly give a concrete tool for triggering eligibility for the new rules. However, in so doing, they elicited a backlash from large developing countries, who questioned the uniqueness of the SVE’s situation as a result of fears that such a definition of uniqueness, triggered through characteristics, would exclude their relatively large economies from S&DT that had hitherto been shared amongst all developing countries.

The two-track approach to negotiations and the “combination and accumulation” argument

At the next meeting of the CTD-DS, held on 6 and 12 April 2005 under the new Chairmanship of Ambassador Gomi Tharaka Senadhira of Sri Lanka, Members began going through the different characteristics. Once again, the large developing countries said that the characteristics are not unique to small economies, and the PSVEs argued that small economies are different in the extent to which these characteristics affect them as well as their capacity to respond.

In an attempt to echo the categorisation under use in the CTD special session, Ambassador Senadhira proposed to divide the characteristics/problems into three categories, namely those where WTO solutions can be found; areas where WTO solutions may be available but
perhaps only in combination with action from other organisations; and areas where solutions lie elsewhere. Senadhira’s approach came in reaction to suggestions from some Members that the session focus on trade-related problems, where they said the WTO could be more useful. Some of the characteristics raised in the list, they argued, could be addressed at a national level through competitiveness, export diversification, or productivity policies, rather than at the WTO. Other problems, such as the geographical isolation of small economies, did not lend themselves to WTO solutions, they added.

However, Senadhira’s categorisation was rejected by the meeting largely owing to the PSVEs’ insistence that the WTO could respond to all of the characteristics/problems identified. Dismissing from the start all problems assumed to not have a WTO solution would be “putting the cart before the horse”, and would compromise the agreed three-step process, they argued. Instead, the PSVEs went in some detail through W-12, noting that it was the “combination and cumulation of all seventeen elements that enhance the vulnerability of small economies,” and that as a result a “combination and cumulation of responses” was needed to reduce the vulnerability of SVEs. Highlighting the cross-linkages between the problems, they responded to criticisms that they were not trade-related by highlighting that the listed characteristics and problems have “systemic implications on the capacity of small economies to integrate fully into the global trading system”, and that as such solutions should be found in the WTO.

The session switched to informal mode, examining the first four characteristics/problems in W-12. The remaining thirteen items were discussed at an informal session on 12 April 2005.

At the next formal meeting of the CTD-DS, on 25 May 2005, the PSVEs decided to table a “bridging” document that marked an attempt to frame responses to the trade-related problems and characteristics that had been discussed in the formal and informal April sessions (WT/COMTD/SE/W/13). Citing that agreement on solutions was the highest priority for negotiations scheduled to finish by the end of 2005, the paper suggests twelve “elements of responses” to the characteristics and problems outlined in W-12. In a new response to questions regarding the uniqueness of the SVE’s situation, and a new analysis of the relationship between characteristics, problems and solutions, the PSVEs said that while the characteristics may not be unique to small economies, it was “the combination and intensity with which small economies face problems deriving from them, coupled with their lack of resilience, that was particularly challenging for these countries.”

The proposal points to other instances in WTO rules where S&DT was targeted at countries meeting certain criteria -- to net food importing developing countries in the Uruguay Round Agreement on Agriculture or to “developing countries that allocate almost all de minimis support for subsistence and resource poor farmers” in Annex A of the July Package -- as evidence of the precedent in the WTO for what they called their “characteristic approach”. The paper calls broadly for S&DT for small economies in several issue-areas, including services in its first appearance in a PSVE submission. Other issues raised were relatively broad, calling for the agricultural and NAMA negotiations ”to be addressed satisfactorily” for SVEs, for priority to be given to services and products of export interest for SVEs, to ensure the trade facilitation negotiations address the “specific needs” of SVEs and to make sure acceding SVEs are not required to undertake commitments greater than those of other WTO Members.

According to the submission, S&DT would be agreed upon by the CTD-DS and then forwarded to the General Council which would then “direct relevant subsidiary bodies to frame responses”, that is, tell other negotiating groups to work on creating such S&DT. In response, the EU, New Zealand and Japan urged the PSVEs to table specific proposals directly in the relevant negotiating bodies in current months to save time in the run-up to the Hong Kong Ministerial Conference in end-2005. The US warned that unless they did so, the proponents could “miss the train” in other negotiating fora, and China repeated concerns that the paper seemed to
define a new category of developing countries.

In response, in another major turning point in the negotiations, on 29 July the PSVEs issued a press release saying that they would be pursuing a two-track approach to the negotiations according to which they would be making proposals on how to address their particular problems directly in the relevant WTO negotiating group, while the CTD-DS would monitor the progress of these proposals. Essentially conceding that the developed countries had been correct at the May meeting on the need to go directly to the relevant negotiating body, in a formal submission to the 17 October 2005 meeting of the CTD-DS the PSVEs restated the two-track approach and pointed out a number of different negotiating groups where they had already tabled proposals (WT/COMTD/SE/W/14). Noting once again that "no one characteristic and problem by itself" was unique to SVEs, the proposal nonetheless emphasises "the cumulative effect" of these characteristics and problems on SVEs and reaffirms the "characteristic based approach" as the three-step way to fulfil the paragraph 35 mandate. It also highlights the submissions made to the negotiating group on agriculture (JOB(05)/161, 27 July 2005), non-agricultural market access (NAMA) (JOB(05)/165, 29 July 2005) and WTO rules (TN/RL/GEN/57, 13 September 2005) by some or all of the PSVEs (see following section for a brief review of these submissions and negotiations).

From that meeting thereon, the focus of the SVE negotiations was in the other negotiating groups, with the CTD-DS largely given a monitoring role. However, at the next meeting of the CTD-DS, on 16 November 2005, three submissions were tabled which delegates have supported for sending to the General Council for adoption.

However, a proposal on the accession of SVEs to the WTO (WT/COMTD/SE/W/17) was much more controversial and owing to broad scepticism about the feasibility of its operationalisation was dropped at the meeting. The proposal called for the terms of reference for working parties on accession of SVEs should make clear that membership-seekers "will only be required to undertake commitments commensurate with their level of development". It also proposes allowing Working Party members to request the establishment of a special panel of experts appointed by the Director-General if it believes that these terms are not being observed. Notwithstanding the controversy on this proposal -- which was largely submitted at the behest of Vanuatu, who has faced particular difficulties in the accession process -- delegates easily adopted Chair Senadhira’s report to the General Council (WT/COMTD/SE/19).

At next session of the CTD-DS, held in informal mode on 21 February 2006, along with the 26 April and July sessions, the negotiating group took up in full its role as a monitoring body for negotiations held elsewhere on S&DT for SVEs. At the February session, the PSVEs noted they were happy about the mentions of the situation facing SVEs in the December 2005 Hong Kong Ministerial Declaration, not only in the lengthy paragraph about the talks in the CTD-DS, but also in the ongoing negotiations in NAMA and services. Given that the deadlines for NAMA, agriculture and services negotiations were closely approaching in April and July, they stressed that the proponents of the small economies work programme would focus on promoting their concerns in the relevant committees.

As such, they tabled a paper (WT/COMTD/SE/20) that listed the PSVEs, repeated the list of indicative characteristics/problems, and listed the various proposals that were on the table in the CTD-DS and other negotiating groups. At the April session the PSVEs tabled a new proposal which compiled the relevant sections of the PSVE proposals made to other negotiating groups (WT/COMTD/SE/W/20). However, at the
meeting some delegations, including Brazil and China, suggested that it was not clear in all the relevant negotiations on SVEs which WTO Members would qualify for the rules being sought for SVEs. Overall, they said that the methodology for determining eligibility for the new rules needed to be elaborated; but, at the same time, they insisted that to preserve the rules-based nature of the WTO, and to avoid creating a new category, they opposed limiting eligibility to a list of countries. While the PSVEs said at the meeting that they would take up this challenge in a submission to be made shortly to the NAMA negotiating group, in the corridors some suggested that they would use a list of criteria; others suggested that they address the concerns by either using over-inclusive criteria or granting all developing countries eligibility, with the trust that the large developing countries would use the “honour system” and not actually use those flexibilities (see relevant section on NAMA negotiations below).

In their proposal and their intervention, the PSVEs suggested that the CTD-DS, through its monitoring role and also through the persuasive powers of new Chair Faizel Ismail of South Africa, should step up political pressure in other negotiating groups to address the SVE-related S&DT in their particular issue area.

At the July 2006 session, delegates reviewed once again the so-called “administrative” proposals, that is, the submissions calling for the recognition of regional bodies as responsible for assisting Members with notification and implementation of the Sanitary and Phytosanitary (SPS), Technical Barriers to Trade (TBT) and TRIPS Agreements. In addition, they considered an updated document outlining progress in other negotiating bodies on SVE proposals (WT/COMTD/SE/W/20/Rev.1). Although the PSVEs commended the progress in the NAMA group, many delegates noted that detailed criteria for eligibility had not yet been tabled in the Ag and Services negotiating groups, and urged these groups to give priority to their concerns. However, given the decision at the end of July to suspend the negotiations for some time, delegates recognised that this was unlikely to happen in coming months. Instead, the PSVEs expressed hope that the momentum generated in recent months, including the progress in the NAMA group, would not be lost.

2.2 Proposals and Progress in Other Negotiating Bodies

The PSVEs have also made submissions, and engaged in talks, in the negotiating groups on non-agricultural market access (NAMA), agriculture, services, rules (on fisheries and on subsidies and countervailing measures), trade facilitation and the working party on domestic regulation. While they have been very active in the NAMA negotiating group, where they are led by El Salvador, there has been relatively less progress on their proposals in the other negotiating groups. In the NAMA and agriculture groups they have called for SVEs to be exempted from the obligation to reduce tariffs according to the formula being negotiated for other WTO Members. Instead, they have called for smaller cuts to their tariffs. In the other negotiating areas, and for special products in the agriculture negotiations, they have asked for special flexibilities to the rules to accommodate their particular situation.

However, in all of the different groups they have been reminded that given the lack of agreement on core elements of the market access formula for all Members and special and differential treatment for developing countries, it is difficult to consider the details of exemptions for SVEs. Nonetheless, a relatively significant amount of progress has been made in framing the modalities that would eventually apply to these countries.

Negotiations in NAMA

Consideration of S&DT for the SVEs in the NAMA negotiating group has centered around two different opinions on how such special treatment should be delivered. According to the framework for NAMA negotiations set out in the 2004 July package, there are two sorts of S&DT available to depart from the normal tariff reduction formula. The first type, known
as "paragraph 6 flexibilities", allows developing country WTO Members who have not previously agreed to limit a certain percentage of their tariff lines at their current rate ("binding") to do so as part of the Doha Round at an average that is the same as the overall average for bound tariffs for all developing countries. The second type, known as "paragraph 8 flexibilities", allows developing countries to apply less-than-formula tariff cuts to a certain percentage tariff lines and to exempt a percentage of tariff lines from reduction entirely. While the PSVEs want to use the paragraph 6 flexibilities, relatively large developing countries would prefer that they use paragraph 8-type flexibilities.

In their first submission to group, on 11 November 2005 (TN/MA/W/66), the PSVEs said that SVEs -- defined as developing countries whose average share in total world merchandise exports was less than 0.10 percent between 1995-2004 -- should be exempt from the formula and should make tariff reductions between 10 and 15 percent. In addition, they would bind all their tariffs, though newly bound tariffs would not need to be reduced. In negotiations on the SVE's proposal in early February 2006, however, some delegates criticised the single criteria for determining eligibility, arguing for identification criteria based on indicators of the degree of vulnerability in addition to market size. Others suggested that the proposal was not sufficiently detailed to be a constructive contribution to the debate, and called for the eligibility criteria as well as S&DT requested to be improved.

As a result, in a major breakthrough in the negotiations, and partly in response to comments made in the CTD-DS in early 2006 (see above), the PSVEs tabled a revised proposal on 10 May 2006, in the form of an informal room document, that set out three criteria for the identification of potential developing country non-LDC beneficiaries of S&DT for SVEs in NAMA. These criteria were a share of world merchandise trade not more than 0.16 percent; world NAMA trade not more than 0.10 percent; and world agricultural trade not more than 0.40 percent. These countries would be, like for the paragraph 6 countries, exempted from the tariff reduction formula. Instead, they would be required to bind a to-be-determined percentage of their tariff lines according to a series of five bands of tariff rates. The SVEs also asked for a longer implementation period than other developing countries, and said that countries with less than 50 percent bindings would have to bind 95 of them.

Several developed and developing countries criticised the proposal, including Canada, Chile, Colombia, Costa Rica, Korea, Norway, Pakistan, Peru, and Singapore. They argued that the proposed definition of SVEs rested on arbitrary criteria. Many Members believed that the identification of SVEs for the purpose of industrial tariff liberalisation should depend exclusively on NAMA trade; some criticised the proposal for including farm trade but not trade in services. Taiwan noted that some of the paper’s sponsors had relatively high GDPs. Many of these Members also suggested that a paragraph 8-type approach would be better, that is, that the SVEs should be subject to the same tariff reduction formula as other developing countries but that they could be allowed to exempt more tariffs from the formula. In informal consultations held on 7 June, Norway suggested in a submission a compromise that uses a paragraph 6 approach, like the PSVEs, but would require them to bind all their tariff lines at a single target tariff average with minimum cuts on individual tariff lines. They would also have to make a minimum, to-be-negotiated reduction to each of their individual tariff lines.

In response, the PSVEs tabled a revised room document on 15 June that reiterated their support for a paragraph 6-type approach, and changes their scheme to a four-band reduction obligation. It also would incorporate Norway's requirement of SVEs to make a minimum, to-be-negotiated reduction to each of their individual tariff lines.

However, Uruguay and Costa Rica said they preferred a paragraph 8 approach that would have the percentage of tariff lines slated for lower reduction and exemption be higher for SVEs than whatever is eventually agreed for all developing countries, allowing them to shield relatively more industrial products from tariff cuts. Apart from these products, SVEs would be
subject to the overall tariff reduction formula. Other Members said that SVEs could, along these lines, both exempt some products entirely from tariff cuts and subject other to partial tariff cuts.

However, in marked contrast to earlier meetings, the question of the eligibility criteria drew less fire, suggesting that the relatively inclusive trigger -- which would include some 103 WTO Members -- had brought on board the relatively large developing countries and particularly Latin American Members who had earlier been afraid of being excluded from access to the new rules. This marked a significant step forward for the PSVEs, who had for years been battling about how to trigger their S&DT. While the decision to halt WTO negotiations at end-July 2006 put a damper on plans to clarify the exact nature of the S&DT in NAMA, or extend the criteria to other negotiations, the meeting left a relatively promising note to end the eligibility debate.

**Negotiations in agriculture**

The PSVEs have submitted two proposals to the Committee on Agriculture Special Session -- one on 11 November 2005 (TN/AG/GEN/11) and one on 31 May 2006 (JOB(06)/164). The former defines SVEs as non-LDC WTO Members with an average share of world merchandise exports of less than 0.10 percent, while the latter uses the three trade share criteria mentioned in the NAMA proposal and explicitly says that the criteria for identifying SVEs should be the same in both negotiating areas. As regards the S&DT to be delivered, the former says that SVEs would cut their tariffs at least 10 percent and not more than 15 percent per tariff line, and that SVEs would be able to self-designate special products that would then be exempted form tariff reductions and tariff rate quota commitments. The May 2006 proposal repeats the S&DT modalities from the previous proposal, and explains that SVEs need this treatment because, amongst other things, the size of their economies, exposure to natural shocks, dependence on a limited number of goods or markets and geographical disadvantages.

**Other negotiations**

**Negotiations on fisheries**

A sub-set of PSVEs calling themselves the "small vulnerable coastal states” on 13 September 2005 submitted a proposal on fisheries subsidies disciplines being negotiated in the Negotiating Group on Rules (TN/RL/GEN/57/Rev.2) that says that development assistance to developing coastal states, assistance to artisanal or small-scale fisheries, fees as part of fisheries access agreements and ‘fiscal incentives’ to develop the capacities of small vulnerable coastal states should be exempted from any future disciplines on fisheries subsidies. Since that time, when some Members criticised the proposal for not sufficiently defining the exemptions being requested, they have engaged with the LDCs and others to better define the exemptions to the fishery subsidy disciplines, most notably for artisanal, small-scale and/or subsistence fisheries (see ICSSTD paper on the issue, forthcoming).

**Subsidies and Countervailing Duties**

On 12 April 2006, the PSVEs made a submission to the Committee on Subsidies and Countervailing Measures requesting that Article 27.4 of the relevant Agreement, which allows extensions to exemptions from the disciplines on subsidies, be changed to allow such extensions until 2018 (G/SCM/W/535). Their request was granted.

**Services**

In November 2005, the PSVEs tabled a broad, generalised proposal to the Council for Trade in Services Special Session calling for issues of concern to SVEs to be addressed satisfactorily in the services negotiations. As a result, in the Hong Kong Ministerial Declaration of December 2005, the Services Annex says that “due consideration shall be given to proposals on trade-related concerns of small economies”.

**Domestic Regulation**

Building on the mentions of specific services-related flexibilities the submission made to the CTD-DS in May 2005 (WT/COMTD/SE/W/13), on 2 May 2006 the PSVEs made a detailed proposal
to the Working Party on Domestic Regulation that lists specific recommendations for the disciplines to be developed for measures relating to qualification requirements and procedures, licensing requirements and procedures and technical standards. For the most part, the rules suggested would apply to all WTO Members, though suggested flexibilities aimed at development objectives (such as implementation periods and technical assistance) would be targeted directly at (as yet undefined) SVEs.

**Trade Facilitation**

On 6 July 2006, a sub-set of the PSVEs submitted a proposal to the Negotiating Group on Trade Facilitation, underscoring their repeated mention of the importance of these talks to the interests of SVEs (TN/TF/W/129). The proposal, similarly to the administrative proposals considered in the CTD-DS, seeks explicit recognition that a regional enquiry point for a group of countries would fulfil trade facilitation obligations, notifications and information provision requirements. It also calls for longer implementation time periods and technical assistance.
In previous sections of this paper we have seen how the SA has been conceived to pursue a development-oriented improvement of the S&DT regime, responding to the Doha mandate on S&DT in general, avoiding further differentiation amongst developing countries and aiming at maximising access to relevant S&DT for all developing countries and LDCs.

We have also seen how the negotiations on the SVEs programme of work mandated in paragraph 35 of the Doha declaration started showing some progress in NAMA and the CTD -DS. This progress is to a certain extent associated to the proponents progressively leaning towards a Characteristic-based Approach (CBA) which aims at addressing the SVEs problems of competitiveness and vulnerability with targeted solutions. These solutions would be triggered by means of thresholds established on the bases of statistic indicators that should represent smallness and vulnerability. However, although the CBA has gained some support, there are still claims about coherence and alleged arbitrariness of the indicators, as well as about the links between characteristics and problems, on the one hand, and between problems and proposed S&DT solutions, on the other.

Although the SA is different from the CBA adopted by the SVEs - most notably, the first aims to provide a framework for all S&DT at the WTO, while the latter focuses on the SVEs - they share in common the principle of delivering specific S&DT through data-based triggers to address a particular set of characteristics that create a particular development situation.

The studies on the SA conducted by ICTSD address in a systematic manner the characteristics of 155 developing countries and LDCs and the relations existing between those characteristics and the problems they face in relation to agricultural trade and rural development, vulnerability and competitiveness. The studies led to defining nine different situations and to conducting simulation exercises on the corresponding lists of eligible countries; i.e., the countries that would access the additional S&DT benefits associated to each situation. The possible solutions to the problems and constraints in each situation, which involve S&DT in trade rules, were also systematically studied. The conclusions of the studies point at the value that could be added by the SA to the arguments of developing countries in the negotiations on S&DT in general and the SVEs programme of work in particular.

This chapter is dedicated to discussing the results of the S&DT studies conducted on the vulnerability of small economies, as well as on competitiveness situations which affect many developing countries, including the SVEs, for which it is organised in four sections.

Section 3.1 discusses the relationships existing between characteristics and development problems of the SVEs, using evidence from the literature and from systematic assessments and statistical tests conducted directly by ICTSD, based on a battery of trade and development indicators that the centre prepared for this purpose. The conclusions of this section have two focuses. The first is clarifying the extent to which the SVEs conform a group of countries that have relevant common features in terms of development and trade. The second is how to best define the lists of countries that should have access to additional S&DT benefits in situations on vulnerability and competitiveness of small economies (Situations SVE and SRE).

Section 3.2 discusses the lists of eligible countries resulting from the simulations initially made on the SVE and SRE situations. It shows that all SVEs participate in the lists of eligible countries of these two situations, and that most SVEs also participate in the lists corresponding to other situations on competitiveness (namely situations COM-1 through COM-4). This means in practical terms that the SVEs would also have access to the additional benefits involved in the latter situations.

Section 3.3 is dedicated to the additional S&DT benefits involved in the SVE and SRE situations.
These benefits are explicitly derived from the consideration of policy actions that countries in the situations could implement to cope with their particular constraints and problems. In other words, this section discusses the links between problems and S&DT solutions.

Finally, conclusions and recommendations on future policy-research activities related to SVEs are given in section 3.4. The recommendations point at undertaking further research that would help improving the basic data, secondary indicators and analytical instruments that could be useful to enhance the knowledge on vulnerability and the links between trade, competitiveness and resilience of the SVEs. They also suggest conducting case studies in various small and vulnerable countries, aiming at learning lessons of experiences, and identifying opportunities for Aid for Trade support, addressing the reduction of vulnerability and the enhancement of resilience through trade and competitiveness-related measures. A cooperation programme between the SVE group, the International Strategy for Disaster Reduction (UN-ISDR) and the ICTSD is suggested as a means to implement the recommendations.

3.1 Links Between Characteristics of Situations and Trade-Related Development Problems in the SVEs

One of the main issues for both the CBA and the SA in the case of the SVEs is to clearly demonstrate the links that exist between the characteristics of these countries, such as smallness or remoteness, on the one hand, and the development constraints that they allegedly experience for fully benefiting from their integration in global trade, on the other. Two questions are repeatedly asked about these links: to what extent SVEs face trade-related development problems that differ from those of other developing countries; and what are the explanatory connections between the characteristics of the SVEs and the existence of the problems they experience.

The arguments of the PSVEs have evolved from the linear relationship between smallness, on the one hand and competitiveness or volatility problems, on the other, to a more comprehensive explanation on the combined and cumulative influence of several characteristics which are unique of the SVEs on the trade and development outcomes of their integration. However, robust proofs of the existence of these links have been missing so far, particularly proofs of the non-existence of equivalent links between characteristics of the rest of the developing countries and competitiveness problems that they - as the SVEs- face.

Almost all arguments and evidence on these kinds of links found in the literature are based on analysis of the variables taken one-by-one, and not considering wholesets of characteristics or variables determining the problems of competitiveness, trade marginalization, etc... Both the arguments in favour and those against SVEs allegations are usually supported in this manner.

This section shortly discusses evidences on the commented links, including the results of statistical tests of hypotheses that the ICTSD conducted, arriving to three fundamental conclusions.

The first conclusion is that using a rational combination of indicators (various and not just one determinant) leads to a robust statistical confirmation of the existence of a particular disadvantaged situation of the SVEs. The counterpart of this conclusion is that analyzing variables in an isolated way does not allow properly assessing the issues of smallness, vulnerability and remoteness in the context of trade and development.

The second conclusion, derived from the first, has very practical consequences: the definition of the lists of countries in the situations of smallness and vulnerability must be based on combining thresholds on various characteristics and problems, and not on only one or a few characteristics.

Finally, the third conclusion refers to the fact that development situations involve relative
disadvantages of countries in the particular situation vis-à-vis the rest of the countries. The thresholds must not be arbitrarily defined but take into account the relative position of the country under analysis in the whole set of developing countries and/or the whole WTO membership according to the variables considered.

The lack of explanatory power of variable-by-variable intents of explanation of the comprehensive trade and development constraints of SVEs

Without claiming to be exhaustive, the information in Table 3.1 is a summary of the main problems that proponents of the SVE programme of work (PSVEs) claim the SVE face, which in turn is a kind of X-ray of its main distinctive features in accordance with their approach.

Table 3.1 Features Characterizing Small, Vulnerable And Remote Economies According To The Proponents Of The SVE Work Programme (PSVEs)

<table>
<thead>
<tr>
<th>FEATURES</th>
<th>01 SMALLNESS</th>
<th>02 VULNERABILITY</th>
<th>03 REMOTENESS / ISOLATION</th>
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<tbody>
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<td></td>
<td>LMS</td>
<td>LSIC</td>
<td>ETRS</td>
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<tr>
<td>1 Exposure to economic conditions in rest of the world</td>
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<td>x</td>
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<td>2 Small domestic market and high dependence on exports</td>
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<td>3 Limited diversification possibilities</td>
<td>x</td>
<td>x</td>
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<td>4 Dependence on a narrow range of products</td>
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<td>5 High volatility of prices</td>
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<td>6 Market thinness</td>
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<td>7 Peripherality / Physical isolation and remoteness</td>
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<td>8 High per unit transport costs</td>
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<td>9 Marginalization</td>
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<td>10 Uncertainties of supplies</td>
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<td>11 Need to keep large quantities of stocks</td>
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<td>12 Trade vulnerability</td>
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<td>13 High dependence on trade taxes</td>
<td>x</td>
<td>x</td>
<td>x</td>
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<tr>
<td>14 Vulnerability of domestic industries</td>
<td>x</td>
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<td>15 Dependence on trade preferences</td>
<td>x</td>
<td></td>
<td></td>
</tr>
<tr>
<td>16 Proneness to natural disasters</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>17 Limited ability to exploit economies of scale</td>
<td>x</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>18 Limitations on domestic competition</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>19 Difficulties in absorbing foreign direct investment</td>
<td>x</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>20 Limited investment opportunities</td>
<td>x</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>21 Limited possibilities for investment in communication services</td>
<td>x</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>22 Dependence on external finance</td>
<td>x</td>
<td></td>
<td></td>
</tr>
<tr>
<td>23 Dependence on Remittances</td>
<td></td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>24 Legal problems caused by rights of passage over the territory of coastal transit states</td>
<td>x</td>
<td>x</td>
<td></td>
</tr>
<tr>
<td>25 Legal problems caused by the access to marine resources under the International Law of the Sea</td>
<td>x</td>
<td>x</td>
<td></td>
</tr>
</tbody>
</table>


Notes: LMS = Limited Market Size; LSIC = Limited Saving and Investment Capacity; ETRS = Exposure to trade-related shocks; ENH = Exposure to natural hazards; LER = Low economic resilience; ETLC = Extreme transport and logistic costs.
In addition to the list of problems and characteristic features set out in Table 3.1, an argument put forward by the PSVEs is the cost of access to and participation in the WTO which, according to Langhammer and Mathias (2001), should not be underestimated but rather regarded as an important limiting factor for the small economies. On the other hand, as argued by McKellar et al (2000) low economic growth is a problem characteristic of the SVEs.

It has been referred above that several other developing countries have pointed out that most of these characteristics are hardly specific to SVEs - indeed, most developing countries have such problems. The SVEs argue that they face a combination and intensity of several of these factors, making them particularly vulnerable.

As pointed out by UNCTAD (2006), "...probably no category of countries has ever been more commonly misunderstood than Small Island Developing States". This could perhaps be extrapolated to the case of landlocked countries.

In general terms it would seem that everyone shares the conception that the proponents of the SVE programme really do have certain disadvantages and that they really require S&DT, but in practice they have been trying in vain for long time to have their particular characteristics and limitations understood. To a large extent it is possible that this situation is due to the evidence of a cause-effect relationship between size, vulnerability, remoteness and economic and trade performance not being at all conclusive. On the contrary, the evidence tends to be ambiguous or contradictory.

Two studies conducted by the WTO secretariat contradict many of the arguments presented in Table 3.1 (see WTO, 2004a and WTO, 2004b). In WTO (2004b), using population size and market share as indicators, a set of isolated tests are presented, the results of which are summarized in Tables 3.2 and 3.3.

### Table 3.2 Some Evidence In Favour Of The PSVEs' Arguments Found In The Literature

<table>
<thead>
<tr>
<th>SOURCE</th>
<th>RELATIONSHIP STUDIED</th>
<th>EXPECTED EFFECT BASED ON ARGUMENTS OF SVE PROPONENTS</th>
<th>CONCLUSION ON ARGUMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>WTO (2002b)</td>
<td>CIF/FOB ratio: Geographic disadvantages (Islands, Landlocked, Others)</td>
<td>Islands or landlocked countries show higher CIF: FOB ratios in comparison with the other countries in the world.</td>
<td>Supports the argument but does not prove whether the difference in the variables (CIF: FOB ratio, openness) is significant between the groups of countries analyzed or the ranges of market share and population compared.</td>
</tr>
<tr>
<td></td>
<td>CIF–FOB ratio: Market share</td>
<td>Small economies (assessed by market share) show higher CIF:FOB ratios in comparison with the other countries in the world.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Openness: Population</td>
<td>Small economies (assessed by population size) are more exposed to international trade (greater openness).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>CIF/FOB ratio: Market share</td>
<td>Small economies (assessed by market share) tend to have higher transport costs.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Openness: Population</td>
<td>Small economies (assessed by population size) tend to be more open to international trade, and are therefore more exposed.</td>
<td></td>
</tr>
<tr>
<td>Jansen (2004)</td>
<td>Trade concentration: Population</td>
<td>Small economies (assessed by population size) have a high concentration on their export lines, so they are more fragile.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Number of exported products: Population</td>
<td>Small economies (assessed by population size) tend to depend significantly on a small number of exported commodities.</td>
<td></td>
</tr>
</tbody>
</table>

**Source:** Baritto (2007), Table 6.
An initial observation to be made on the information set out in Tables 3.2 and 3.3 is precisely that these cannot in any way be regarded as sufficiently robust proofs of the conclusions offered by the authors on the issues under analysis. On the one hand, because they are simply a set of analyses of isolated variables on issues that would seem to be characterized by adverse combinations of factors and, on the other hand, because the tests are not accompanied by a systematic analysis of the statistical significance of the differences found (to what extent a difference can be considered important).

It must be added to these comments that there is not even a consensus on the meaning of the “size” of an economy, regardless of the fact that various indicators have been proposed (population, GDP, share of international trade, surface area, etc.). On this point, for an appropriate definition of size, consideration should be given to what was stated in the literature review conducted by WTO (2002a): "... an appropriate definition of size should take account of a variety of factors, including: population, per capita income and income distribution. Indeed, a very poor country can have a very large population and be a small market owing to its limited potential demand" (WTO 2002a).

The variable-by-variable analyses carried out by ICTSD for SIDS and landlocked countries confirm some apparently distinctive features of these groups. The most striking differences were found in the concentration of their exports, which confirms that to a large extent these countries are highly reliant on very few export lines and very few market destinations, compared with the rest of the world. This could make them particularly fragile. In line with the information reported in several studies (Jansen 2004; WTO 2002a; WTO 2002b), the analyses also demonstrate that transport costs (expressed in terms of shipping costs = CIF:FOB ratio -1) are another distinctive feature, especially for landlocked countries. The most significant differences found refer to the proportion of services in gross domestic product, particularly marked in the case of SIDS.

However, as Table 3.4 shows, the results obtained suggest that many of the ambiguities found when comparing the arguments of the SVR countries with the information reported persist.
### Table 3.4 Empirical Evidence Assessed By ICTSD In Relation To PSVEs Arguments

<table>
<thead>
<tr>
<th>FEATURE</th>
<th>VARIABLE / PROXY</th>
<th>HYPOTHESIS BASED ON ARGUMENTS OF SVR PROPONENTS</th>
<th>RESULTS / CONCLUSIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Exposure to economic conditions in the rest of the world</td>
<td>Openness to trade (X+M)/GDP</td>
<td>SIDS and landlocked countries are more exposed to international trade (they would therefore be more vulnerable to changes in the world economy).</td>
<td>Contradictory – On average, SIDS are more open, but the difference is not significant.</td>
</tr>
<tr>
<td>2. Dependence on a narrow range of products</td>
<td>Herfindahl–Hirschmann Index by export lines</td>
<td>SIDS and landlocked countries tend to depend on very few export lines and their basket of exports is therefore highly concentrated.</td>
<td>Confirmed – There are no appreciable differences between SIDS and landlocked countries, but the difference between them and the rest of the world is significant. Proponents tend on average to have medium to high concentration values (HHx &gt; 0.4).</td>
</tr>
<tr>
<td>3. Dependence on a few market destinations</td>
<td>Herfindahl–Hirschmann Index by market destinations</td>
<td>Exports by SIDS and landlocked countries tend to be concentrated in very few market destinations.</td>
<td>Confirmed – The behaviour is similar to the concentration of export lines. Proponents tend on average to have medium to high concentration by destination (HHmd &gt; 0.4).</td>
</tr>
<tr>
<td>4. Transportation costs</td>
<td>Shipping Costs SC = CIF:FOB – 1</td>
<td>Since SIDS and landlocked countries are more remote, they have higher transport costs, so limiting their competitiveness.</td>
<td>Confirmed – There are very significant differences between both groups and the rest of the world. However, landlocked countries have a fairly wide range of variation (some have very high values and other very low ones).</td>
</tr>
<tr>
<td>5. Proneness to disasters involving natural hazards</td>
<td>Exceedance Annual Probability of disasters producing D+H+I ≥ 0.04percent of total population (D=Deaths; H=Homeless; I=Injured)</td>
<td>Based on historical records, SIDS and landlocked countries are more prone to natural disasters.</td>
<td>Contradictory – No significant differences are observed in the probability associated with SIDS and landlocked countries and the rest of the world. The variation is very wide in each case.</td>
</tr>
<tr>
<td>6. Highly volatile prices</td>
<td>Purchasing power of exports volatility as standard deviation of annual relative changes (1980–1997)</td>
<td>SIDS and landlocked countries are subject to very high volatility of exports’ purchasing power.</td>
<td>Contradictory – No significant differences are observed. The variation is very wide, especially for SIDS and landlocked countries.</td>
</tr>
<tr>
<td>7. Export volatility</td>
<td>Export volatility as the standard deviation of annual relative changes (1980–1997)</td>
<td>SIDS and landlocked countries have very high export volatility.</td>
<td>Contradictory – No significant differences are observed. In this case SIDS have the highest variation. On average the rest of the world tends to have higher export volatility, but the differences observed are not significant.</td>
</tr>
<tr>
<td>8. Income volatility</td>
<td>Income volatility as the standard deviation of annual relative changes (1980–1997)</td>
<td>SIDS and landlocked countries have very high income volatility.</td>
<td>Contradictory – SIDS tend to have higher income volatility than landlocked countries, and they have a higher value than the rest of the world. However, the range of variation observed in the first two means that the differences are not significant.</td>
</tr>
<tr>
<td>9. Output volatility</td>
<td>Output volatility as the standard deviation of annual relative changes (1980–1997)</td>
<td>SIDS and landlocked countries have very high GDP volatility.</td>
<td>Contradictory – As for income, SIDS tend to have higher GDP volatility than landlocked countries, and they have a higher value than the rest of the world. However, the differences observed are not significant.</td>
</tr>
<tr>
<td>10. GDP reliance on services</td>
<td>Services as percentage of GDP</td>
<td>SIDS tend to be more reliant on services.</td>
<td>Contradictory – There are very significant differences between SIDS, landlocked countries and the rest of the world. SIDS are the group most reliant on services (63.1percent ± 4.05percent). This behaviour is characteristic of all islands viewed as a whole.</td>
</tr>
</tbody>
</table>

Source: Baritto (2007) Table 8.
The expounding power of a set of variables acting together: the Situational Approach

With the aim of examining the explanatory power of a set of variables acting together on the countries in the SIDS or landlocked categories, statistical tests were conducted by ICTSD on 155 developing countries and LDCs for the two cases under study, using binomial probit models. The test consists, in simple terms, in trying to reproduce the list of the SIDS, on the one hand, and the list of the landlocked countries, on the other, making use of a set of variables.

The results of the tests can be considered conclusive in both cases: Both lists can be reproduced within acceptable limits of error using several characteristics of the countries studied. In the case of the landlocked countries the quality of the results is affected by the lack of data of an important number of countries.

For the SIDS the best global binomial probit model has an explanatory power of 88 percent. Applied to the 155 countries, only 11 countries are wrongly classified as SIDS and 8 are wrongly classified as non-SIDS. All the variables report a direction (sign of coefficient) which is coherent with the hypotheses stated initially.

The factors having a significant or very significant impact in confirming the SIDS situation are: i) proportion of services in GDP; ii) exceedance annual probability of natural disasters producing (Death +Homeless +Injured) over 0.04 percent of total population; and iii) population (number of inhabitants). The rest of the variables studied, although their behaviour coincides with the expected direction, do not have a significant effect. Incorporating the EVI composite index by Briguglio (2003) into the model, the explanatory power increases significantly, from 88 percent to 95.7 percent. However, the EVI is only available for 69 countries, for which it was ruled out of the model.

For the landlocked countries, although the model as a whole shows a significantly high goodness of fit (accuracy of estimates 93 percent), we also observe that the human development index appears as the most relevant explanatory factor, which prevents drawing more concrete conclusions in terms of cause-effect relationships. However, the model reproduces the list of landlocked countries with only 3 out of 87 countries wrongly classified as landlocked and 4 out of 13 wrongly classified as non-landlocked.

How to best address the preparation of lists of countries in the situations

On the basis of the above commented results, some general conclusions can be drawn to support the selection of variables to be applied in the definition of lists of countries in the situations related to smallness, vulnerability and remoteness.

In the first place, it is clear that analyzing variables in an isolated way does not allow properly assessing the issues of smallness, vulnerability and remoteness in the context of trade and development. However, from the variable-by-variable assessments, four factors appear with a large influence in characterising the SIDS cluster of countries, namely: i) concentration by export lines; ii) concentration by destination; iii) shipping costs and, iv) the proportion of services in GDP.

Additionally, from the analysis made of the SIDS using a binomial probit model, population, exceedance annual probability (DHI ≥ 0.04 percent) and the proportion of services in GDP result factors of most relevance. Landlocked countries present serious problems of data, limiting the possibility of reaching more solid conclusions with the same ease as for the SIDS.

Considering these findings, it is judged advisable to use a sufficiently rational combination of the indicators mentioned previously, and others commented below, in a systematic method which would lead to defining the lists of eligible countries in these situations. The list of countries in these situations should be prepared combining three lists (a combination of the three main characteristics so far highlighted), those representing the circumstances associated to smallness (σ), vulnerability (ϖ) and remoteness (ρ). Considering that there are robust links between these factors and other specific variables representing trade circumstances,
in preparing each the three lists $\sigma$, $\varpi$, and $\rho$, various indicators should be considered.

Accordingly, the relevant combinations for the purpose of preparing the lists of eligible countries would be: i) small and vulnerable ($\sigma\varpi$); ii) small and remote ($\sigma\rho$); and iii) small, vulnerable and remote ($\sigma\varpi\rho$). The first combination is meant to reflect the special situation of the SIDS and other developing countries and LDCs living similar circumstances mainly associated to smallness; the second the landlocked countries and other developing countries and LDCs living circumstances associated with very high transportation costs, while the last is what has been termed the "worst case", i.e. the one in which all three adverse factors and their circumstances are present at the same time.

Figure 3.1 Basic Logic Followed In Identifying The Lists Of Countries In The Situations

Applying this method implies individually defining the three main sets indicated in Figure 3.1 as \{$\sigma$, $\varpi$, $\rho$\} and then identifying the intersections referred to above.

From the outset, it is important to stress that all the subsets of countries to be defined as eligible to additional S&DT benefits should share the common criteria of including limitations associated with market share, in order to ensure that no large distortions in international trade were generated by the use of flexibilities in rules by the beneficiary countries. Market share, on the other hand could be used as one factor expressing the size of the economy.

Population should be used as the main indicator to characterize the size of the economy (as is normal practice in the literature), but introducing combinations with per cápita income (or with per cápita GDP) in various ranges, to incorporate the concept of purchase power. These combinations would allow considering the extremely small economies regardless of the per capita income, and at the same time prioritizing social vulnerability associated to low incomes and limitations of scale in the case of medium size countries. Three ranges were chosen for the simulation exercises of the two situations that followed (SVE and SRE), and a similar approach in which population and per cápita GDP are combined is suggested for conducting other simulation exercises: (i) population not exceeding 15 million referring strictly to countries with low income; (ii) population not exceeding 10 million, referring only to countries with medium and low incomes; and (iii) population not exceeding 5 million.

Since concentration of exports (by market destination and export lines) individually show certain significant differences in relation to
the rest of the world, ideally it should also be reflected in the characterization criteria, but rather amongst the factors determining vulnerability, in this case in terms of the fragility associated with economic conditions beyond the control of the countries.

Indicators of other trade-related problems faced by these countries may be associated in clusters around the three main characteristics (smallness, vulnerability and remoteness), in order to initially identify the $\sigma$, $\varpi$ and $\rho$ subsets, which would be combined in a later stage (see Box 3.1 in the following section).

### 3.2 Lists of Countries in the Situations: Results of the Initial Simulations

Multiple simulation exercises involving vulnerability and competitiveness problems of small economies (SVE and SRE situations) were conducted in the studies, from which some results are commented below. The simulations made use of models and a battery of 139 indicators that were developed by the ICTSD, which cover 155 countries. These models and indicators are at the disposal of any WTO delegations that would be interested in simulating additional sets of criteria to explore new situations or fine-tune the lists of eligible countries. The results presented below show that all the LDCs would be covered by the additional benefits of the SVE and SRE situations; that 37 of the countries eligible to the two situations would also benefit from at least one situation on competitiveness and 23 would benefit from at least two of them.

**Empirically-supported lists of countries in the SVE and SRE situations**

Two situations involving the characteristics and problems of the SVEs have been considered using the following criteria:

- **Small and Vulnerable Economies SVE** ($\sigma\varpi; \varpi\rho$ and $\sigma\varpi\rho$): a situation combining smallness ($\sigma$) – ordinarily associated with high volatility and low resilience – with high vulnerability to external shocks and/or natural disasters ($\varpi$), including or not the circumstance in which high transportation costs (remoteness $\rho$) are implied; and

- **Small and Remote Economies SRE ($\sigma\rho$):** a circumstance combining both smallness ($\sigma$) and a remote location (remoteness $\rho$) which implies high transportation costs.

---

**Box 3.3 Criteria And Indicators Used In Defining Lists Of Developing Countries In The Basic Simulation of Situations SVE and SRE**

The process used to define the lists of the two situations was to formulate partial lists of small countries ($\sigma$), vulnerable countries ($\varpi$), and remote countries ($\rho$) in order to then combine them to form the lists of small and vulnerable economies ($\sigma\varpi; \varpi\rho$ and $\sigma\varpi\rho$) and of small and remote economies ($\sigma\rho$).

**The Smallness list**

The size of the population and the economy, and the participation in global export markets are taken as a basis for statistically defining Smallness. A total of 63 developing countries and LDCs are included in list $\sigma$ of small countries.

**The list of vulnerable countries**

The list of vulnerable countries ($\varpi$) comprises 70 developing countries and LDCs. It is formed from the union of four partial lists $\chi; \delta; \epsilon$ and $\gamma$, each of which focuses on groups corresponding to particular vulnerable circumstances. Thus, list $\chi$ incorporates countries with low or middle income
In addition to the basic list formulated as described in the Box, during the course of the study many sensitivity tests were conducted, two of which introduced an additional restriction of only considering those countries that have shares below 0.12 percent of the international export market. These are economies in which the scale factor seriously affects the institutional and economic capacity to respond effectively to high-risk situations, or to recover on their own from the damage of major disasters, or to diversify exports or undertake comprehensive disaster risk management programs in the areas of productivity, trade, competitiveness or infrastructure policies.

**Countries in the remoteness list**

List ρ of remote countries, that is countries characterized by remoteness from markets in terms of transportation costs, includes 46 developing countries and LDCs.

**Some comments on data related to remoteness and vulnerability factors**

The phenomenon of vulnerability - also associated with resiliency or capacity to recover - can have many different causes and manifestations (e.g. risk of disaster related to natural factors; exposure to external trade shocks; impact of disastrous events of any kind on GDP; volatility of the terms of trade, of revenues from exports or of GDP), and there are no standard data covering the countries in all of the situations, a problem which is more acute for smaller countries. This requires the use of several different indicators and sources in order to treat vulnerability satisfactorily. With respect to remoteness, the ICTSD studies have relied primarily on data on the quotient of CIF and FOB prices, an indicator which does not exist for some small economies, so forcing the analysts to make hypotheses and indirect inferences for those landlocked countries that are affected by the lack of data.

In addition to the basic list formulated as described in the Box, during the course of the study many sensitivity tests were conducted, two of which introduced an additional restriction of only considering those countries that have shares below 0.12 percent of the international export market. One of them, represented in Figure 3.2, maintains the maximum population of 15 million; the other -represented in Figure 3.3- reduces the population ceiling to 10 million.

In principle, from the simulations performed, we believe that these two sensitivity tests are good representations of the combination of criteria that would have an opportunity for consensus amongst the developing countries and LDCs in WTO. Note that of the 32 LDCs, only eight are excluded from the list. Of them, seven have populations above 15 million and for one (Guinea) the necessary information is not available. In other words, all the LDCs can really be considered to be in the situation.

The sectors shown in Figures 3.2 and 3.3 correspond to the following situations:

- **Small and Vulnerable Economies (SVE):** In the option that limits the population to a maximum of 15 million inhabitants (Figure 3.2), 57 countries qualify as SVEs. They are those listed in intersections $\sigma\nu\nu^*$ (22), $\omega\nu^*$ (2), $\sigma\omega\nu\nu^*$ (30) and in sector $\omega^*$ (3). It can be appreciated that the majority of remote countries are also vulnerable (32 countries in intersections $\omega\nu^*$ and $\sigma\omega\nu\nu^*$). If the upper limit for population is lowered to 10 million instead of 15 million, countries in the list are reduced from 57 to 44 as shown in Figure 3.7.

- **Small and Remote Economies (SRE):** Five countries located in sectors $\sigma\nu^*$ (4) and $\nu^*$
(1), which do not show high vulnerability levels. This total is reduced in one country when limiting total population to 10 million inhabitants.

The remaining five countries (Brunei-Darussalam, Guinea, Georgia, Namibia and Uruguay, in sectors $\sigma^*$ and $\sigma^{**}$) can only be considered small, and would not qualify as either remote or vulnerable countries and would not be included in the lists of the situations studied here.

Given the fact that Figures 3.2 and 3.3 only include small countries (populations under 15 million and 10 million, and shares under 0.12 percent of world exports) all countries in sectors $\rho^*$ and $\rho^{**}$ must be considered small and remote, and all countries in sectors $\omega^*$ and $\omega^{**}$ must be considered small and vulnerable.

Figure 3.2 Small, Vulnerable And Remote Developing Countries With Population Under 10 Million Inhabitants And Exports Market Share Under 0.12%
SVEs in other competitiveness-related situations’ lists

Four situations on competitiveness and three on agriculture and rural development were studied in addition to situations SVE and SRE. From these seven situations we highlight the competitiveness situations designated COM-1 through COM-3 as their respective lists include many countries also included in the SVE and SRE list.

Of 39 developing countries on the list shown in Figure 3.2, 30 (77 percent) are also on the list of competitiveness situation COM-1 “Severe supply-side constraints found in low-income countries”, 15 (38 percent) are on list COM-2 "Diversifying exports and strengthening technological capabilities in mineral-dependent economies", and 19 (49 percent) are on list COM-3 "Deepening shallow productive-sector development in manufacture”. Thirty-seven (95 percent) would benefit from at least one of the situations COM-1, COM-2 or COM-3; twenty-three (59 percent) would benefit from at least two; and four (10 percent) would be eligible to benefit from all three.

**Situation COM-1: severe supply-side export constraints found in weak economies**

Countries that find themselves in this situation show a very high export concentration on a few...
Box 3.2 List Of Developing Countries In Situation COM-1 “Severe Supply-Side Exports Constraints In Weak Economies”

Combining three partial lists K, L and M produces the comprehensive list of countries in the situation characterized as “severe supply-side exports constraints in low-income countries”

**List K: A broad combination of constraints and problems.**

List K includes countries (with no limitation as to population size) simultaneously subject to a wide variety of constraints, namely a low per capita income; a low share of international export markets; and a high dependency on a few export lines with very low or no manufacturing content.

**List L: Extremely low market shares**

List L focuses on countries with a very low share of the international export market. Limits on income levels are the same as in list K and no condition is imposed on population size.

**List M: Small size of economy limits opportunities for diversification**

Finally list M concentrates on very small developing economies, a characteristic which seriously limits their capacities to diversify or to improve their market shares.

**Comprehensive list of countries in the situation (35 countries)**

Albania; Antigua & Barbuda; Barbados; Belize; Bolivia; Botswana; Cuba; Dominica; Dominican Republic; Ecuador; El Salvador; Fiji; Gabon; Ghana; Grenada; Guyana; Honduras; Jamaica; Kenya; Kyrgyzstan; Macedonia; Mauritius; Moldova, R. of; Namibia; Nicaragua; Pakistan; Paraguay; Peru; Sri Lanka; St Kitts & Nevis; St Lucia; St Vincent & the Grenadines; Swaziland, and Zimbabwe.

**Situation COM-2: “Diversifying exports and strengthening technological capabilities and linkages in mineral-dependent economies”**

This situation refers to countries that have a high specialization in commodities exports of mineral or hydrocarbons. Their indicators often exhibit trade specializations in the export of these mineral resources and in low-technology manufactures based on them.

Two more or less generalized characteristics of these economies are that the main export sectors (i.e. hydrocarbons and mining) show a very high apparent productivity in comparison with other productive sectors, which explains a permanent tendency towards the overvaluation of the domestic currency and serious difficulties on the part of manufacturing sectors to become internationally competitive; they also generate a very small number of direct and indirect employment opportunities, due to the scarcity of the backward and forward linkages they establish with the rest of the economy. Consequences of these features are a high dependence on imports of all kind of goods and services to supply volatility and reduced power in international negotiations. Additionally, these circumstances are usually correlated to very low productivity and weak productive linkages between exporters and the rest of the economy, thus limiting trade spillovers for job creation and income distribution.

Thirty-five countries are found to be in the situation, as shown in Box 3.2, which also summarizes the combination of criteria employed.
domestic demand (therefore resulting in a severely negative balance of non-mineral trade, which becomes serious in the low-price sector of the cycles); high levels of unemployment and informal employment; and highly skewed income distribution. Box 3.3 shows the list of countries resulting from the simulation of this situation, as well as the criteria employed.

**Box 3.3 List Of Developing Countries In Situation COM-2 "Diversifying Exports And Strengthening Technological Capabilities And Linkages In Mineral-Dependent Economies"**

Combining the criteria of four lists O, P, Q and R produces a comprehensive list of 32 countries in this situation.

**Four partial lists**

Criteria for inclusion of countries in the partial lists are a very high proportion of exports made of hydrocarbons, minerals and their manufactures (List Q) and high concentration on a few non-agricultural export lines (List R). Countries with low or middle incomes according to the World Bank are grouped in list O, and high-income countries are grouped in List P. In consequence, two subsets can be identified in the list of eligible countries of this situation. Countries in subset PQR have the trade specialization characteristics plus high income levels; countries in subset OQR have the same specializations and medium or low income levels.

**Comprehensive list of countries in the situation**

- **Subset PQR (10 countries):** Bahrain; Brunei-Darussalam; Chile; Kuwait; Oman; Qatar; Saudi Arabia; Trinidad & Tobago; United Arab Emirates; Venezuela.
- **Subset OQR (22 countries):** Albania; Bolivia; Botswana; Cameroon; Congo, R. of; Colombia; Costa Rica; Dominica; Ecuador; Egypt; Gabon; Ghana; Guyana; Kyrgyzstan; Mauritius; Mongolia; Namibia; Nigeria; Papua-New Guinea; Philippines; Suriname; Swaziland.

**Situation COM-3: deepening "shallow productive sector development" in manufacture**

A significant number of developing countries export relatively high proportions of goods in relation to their total exports. However, many of these countries have at the same time a permanent trade balance deficit in goods as well as a low contribution from export to domestic value added and to stable and well-paid job creation. This trade phenomenon occurs in developing countries of different income levels that have already engaged in an industrialization process but have nonetheless been unable to overcome «shallow integration of production» circumstances, which in some extreme cases can be limited to assembly of imported parts.

The most common examples of sectors involved in this situation are the low-technology "footloose industries", i.e., industrial processes for final assembly of traditional goods for export (e.g. that complete the final phases of clothing finishing with no vertical integration into the textile sector). But examples can also be found in specialist high-technology exports that are not supported by internal chains of component suppliers, either because these chains were never developed or because they were destroyed in the trade liberalization process (e.g. electronics assembly). Free-trade zone subsidy regimes were associated with the origins of these exporting models in many developing countries. These are to be eliminated in the near future except in LDCs and low-income countries. Additionally, in both these cases, labour costs and tax benefits would give low-income countries an advantage for the location of international assembly enterprises aiming at international markets.

The list of countries in this situation includes 27 developing economies, as shown in Box 3.4 with the corresponding explanation of the criteria employed.
Box 3.4 List of Developing Countries In Situation COM-3 "Shallow Manufacture"

Combining three lists T, U and V produces the comprehensive list of countries in the "Shallow Manufacture" situation.

**Common conditions in all lists:**
All the partial lists have to meet three conditions: trade imbalance in goods, represented by a limit on the quotient between exports and imports of goods; total share of international market under a certain ceiling; and an upper limit on the per capita GDP.

**Additional conditions used to complete List T: high technology exports**
The additional condition completing the pre-requisites for list T is a relatively high proportion of high-technology goods in total exports.

**Additional conditions used to complete List U: low technology exports**
The additional condition completing the pre-requisites for list U is similar to that of list T, but relating to low-technology manufacture exports.

**Additional conditions used to complete List V: trade deficit and low incomes**
The conditions required for list V are completed by adding to the basic conditions the simultaneous occurrence of the worst cases of a trade deficit in goods and the lowest per capita GDP.

**Comprehensive list of countries in the situation**
Albania; Armenia; Belize; Costa Rica; Cuba; Dominica; Dominican Republic; Egypt; El Salvador; Georgia; Grenada; Guatemala; Guyana; Honduras; Jamaica; Jordan; Macedonia; Moldova, R. of; Mongolia; Morocco; Nicaragua; Paraguay; Romania; Sri Lanka; Tunisia; Turkey; Vietnam.

3.3 The Links between Problems and Solutions and the Additional S&DT Benefits Involved in the SVE and SRE Situations

In this section a series of policy actions that could be useful in addressing the problems and constraints of situations SVE and SRE are illustrated, indicating in each case the trade rules where S&DT flexibilities might be necessary. However, two introductory considerations may be important, before presenting the ideas on additional benefits associated to the situations designated as SVE and SRE.

First of all, policy actions are the logic links between the development problems and the S&DT measures to be proposed. It is necessary to demonstrate that the S&DT demanded is instrumental to the policy actions and that the latter contributes to solving the problems concerned. Policy actions should be sufficiently focused in the problems in order to maximize their effectiveness; and the S&DT flexibilities should be conceived as to limit negative spill overs on trade partners.

Secondly, SVEs do have unique characteristics and special circumstances, but those related to competitiveness are not unique, they may be shared by many other developing countries and LDCs. Negative reactions against the SVE work programme must be expected from numerous developing countries if the SVEs insist in demanding special benefits on the basis of allegedly "unique" competitiveness problems. In the ideas discussed below we make an effort in differentiating commonalities and real differences or uniqueness of SVEs regarding the needs for special supports.
Commonalities and differences with other developing countries

There is clear evidence that small countries face certain particular obstacles to their benefiting from integration into the global economy, but there is also evidence that the size of the economy, its remoteness and insularity do not by themselves explain the majority of the competitiveness constraints from which countries of both proponent groups suffer (see section 3.1), since these problems are also found in many other developing countries.

Commonalities between SVEs and other developing countries in competitiveness constraints

No significant differences have been found in characteristics strongly related to competitiveness, between SIDS and landlocked countries, on the one hand, and the rest of developing economies on the other, especially those that have been characterized in this paper by the situations COM-1 and COM-3 (see section 3.1).

The problems of trade and competitiveness in which no differences are perceived are, amongst others, insufficient value added or insufficient processing of exports, insufficient links between export activities and the rest of the economy, volatility in the price of exports, advantages or disadvantages for attracting foreign investment, or difficulties in overcoming problems relating to international technical and health standards.

The real differences based on smallness, vulnerability and remoteness

Small economies usually depend more on international trade than other countries, and are more exposed to risks resulting from external shocks. In addition, due to their size relative to the volume of trade, it is more difficult for them to adapt to (or recover from) the damage they suffer from shocks in their export prices, or when they are subject to trade remedies, discriminatory access to markets or sudden changes in trade rules. Also because of their high level of dependency, their fiscal earnings depend to a great extent on import tariff revenues, which makes them more vulnerable to reductions in those tariff levels.

In small countries, external trade or finance shocks and disasters involving natural phenomena have a greater impact due to the scale of the economies, and there is empirical evidence that these countries have less capacity to recover from such damage (they are less resilient). Compared to other developing countries, small countries tend to have more limited institutional capacity to formulate and implement trade or productive development, diversification and competitiveness policies, to face an international trade dispute, or put into effect comprehensive disaster risk management plans. On the other hand, it is a statistically proven fact that SIDS and landlocked countries face greater constraints than other developing countries due to certain traits, such as dependence on few products and export markets, and transportation costs that they must absorb in order to access international markets.

The conclusion reached is that small countries have scale restrictions that can aggravate the constraints that other developing countries experience in trying to diversify or to integrate into their own economies the processing of their commodities. If, in addition, they suffer from external shocks or frequent disasters, they face even more severe constraints to preserve any improvements in competitiveness that they may have achieved and to recover from any damage suffered during disasters. The same can be said for countries whose per unit transportation costs are in fact much higher than those of the rest of the world and that in addition have economic scales that prevent them from making themselves the investments - in logistics and infrastructure - they would need to overcome their disadvantages. Worse yet is the situation in countries that simultaneously meet the three conditions - smallness, vulnerability and remoteness.

These are the real reasons that differentiate the two situations of SVE and SVR from those circumstances of limited competitiveness that most developing countries experience. It is on these traits that the policies that could be
useful and the considerations of S&DT that both situations would deserve, should be based.

**Ideas on additional S&DT benefits for countries in the SVE situation**

Due to the fact that countries in situations SVE and SRE share many supply-side constraints related to competitiveness with those in situations COM-1 and COM-3, some of the policy actions and instruments are also shared. However, international technical assistance (IA) and international development assistance (DA) are relatively more important in SVE and SRE.

The expected development of Aid for Trade programmes in WTO would provide additional resources for both purposes.

It can be seen in Table 3.6 that policy measures relative to vulnerability and remoteness, as well as to weakness of State organizations of SVEs and SREs would depend to a large extent on external support. In fact, given the small size of these economies, even those with the highest per capita GDP, they are extremely limited in addressing their needs related to vulnerability and resilience using their own resources.

### Table 3.5 Illustration Of Policy Actions Related To Competitiveness, And Trade-governed Instruments For Their Implementation In Situations SVE & SRE

<table>
<thead>
<tr>
<th>Policy actions</th>
<th>National policy instruments</th>
<th>International instruments</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>CI</td>
<td>S</td>
</tr>
<tr>
<td>LI-1; CL-1: Promote and support domestic supply capacity of goods and services incl. SME chains</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>LI-1: Negotiate improved access conditions to WTO member country markets (e.g. duty-free; quota-free access for small economies’ exports)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>LI-1; CL-1: Negotiate exemption of ASCM disciplines in sectors of particular interest (e.g. fisheries in island states)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>LI-3: Increase compliance to international (technical, health &amp; environment) standards</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>LI-3: Negotiate obligation of developed countries in WTO to provide for technical assistance when establishing new standards (e.g. SPS)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ES-3: Enforce and monitor implementation of best environmental practices</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>LI-1; CL-4: Extend X processing zones regime and flexibilities to enable coordinated transition; negotiate extension of related trade disciplines.</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>CL-4: X subsidies fade out in coordination with measures enhancing suppliers’ capabilities</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>CL-2: Build dedicated infrastructure to support improving export capabilities</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>CL-4: Negotiate limited tariff cuts in NAMA and agriculture; modulate tariffs to improve labour content in net trade balance (X-M)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SH-1: Training of personnel at all levels in productive sectors and auxiliary public agencies</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>SH2: Promote cooperation networks (e.g. cooperatives) to enhance local devt impact</td>
<td></td>
<td>X</td>
</tr>
</tbody>
</table>

CI: Conditional incentives, including incentive-based performance requirements; S: Subsidies; T: Import tariffs; PP: Preferences in public procurement. IA: International technical assistance; DA: Development assistance (net transfers); MP: Market access preferences.
### Table 3.6 Illustration Of Policy Actions Related To Vulnerability And Weakness Of Small Economies, And Trade-governed Instruments For Their Implementation In Situations SVE & SRE

<table>
<thead>
<tr>
<th>Policy Actions</th>
<th>Trade-governed instruments</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>POLICY ACTIONS RELATED TO VULNERABILITY AND REMOTENESS OF SMALL COUNTRIES</strong></td>
<td></td>
</tr>
<tr>
<td>Negotiate priority consideration to SVEs vulnerability to disasters in development cooperation schemes, including in the IF and Aid for Trade programmes, for development financing and technical assistance</td>
<td>CI, IA</td>
</tr>
<tr>
<td>Conduct recovery/reconstruction of assets damaged in disasters, incorporating standards and best practices for risk prevention</td>
<td>X, X</td>
</tr>
<tr>
<td>Incorporate best practices for risk management in all areas of planning: international finance; territorial &amp; sectoral development; infrastructure; investment projects programming</td>
<td>X, X</td>
</tr>
<tr>
<td>Establish financial mechanisms to support the recovery of priority areas, activities or services from disastrous events (funds and/or insurance)</td>
<td>X, X</td>
</tr>
<tr>
<td>In international trade and investment agreements limit exposure to risks of external shocks, and ensure prompt access to safeguards to protect international reserves in cases of shocks as well as in disasters</td>
<td>X, X</td>
</tr>
<tr>
<td>Negotiate priority consideration to remoteness of small economies in development cooperation schemes, including in the IF and Aid for Trade programmes, for development financing and technical assistance</td>
<td>X, X</td>
</tr>
<tr>
<td>Implement comprehensive institutional reforms in trade-related services such as logistics, and conduct investment in infrastructure and logistics, with the participation of international ODA and private investors</td>
<td>X, X</td>
</tr>
<tr>
<td><strong>POLICY ACTIONS RELATED TO ECONOMIC AND INSTITUTIONAL WEAKNESS OF SMALL COUNTRIES</strong></td>
<td></td>
</tr>
<tr>
<td>Negotiate and implement simplified procedures for implementing trade rules including for notification (e.g. antidumping; safeguards; ASCM; SPS)</td>
<td>X, X</td>
</tr>
<tr>
<td>Increase and deepen international technical assistance for preparation and implementation of trade–supported strategies for development, as well as for implementing logistics and infrastructure plans for trade support</td>
<td>X</td>
</tr>
<tr>
<td>Negotiate special (simplified and less onerous) conditions for dispute settlements involving SVEs and SREs (e.g. Art 4 of DSU “substantial trade interest”; negotiate rules that incentivizing the use of mediators)</td>
<td>special</td>
</tr>
<tr>
<td>Promote participation of SVEs and SREs in regional integration schemes, cooperation agreements and FTAs with other developing countries and LDCs; and negotiate flexibilities to ensure WTO compatibility</td>
<td>special</td>
</tr>
<tr>
<td>Negotiate conditions that facilitate the accession of SVEs and SREs to WTO, and that ensure smooth transition ensuring those SVEs’ accession</td>
<td>special</td>
</tr>
</tbody>
</table>

CI: Conditional incentives, including Incentive-based performance requirements; S: Subsidies; IA: International technical assistance; DA: Development assistance (net transfers).

### 3.4 The Need for Additional Research on the Relations Existing Between Vulnerability, Resilience and Competitiveness of Small and Vulnerable Economies

Knowledge gaps must be filled to allow for appropriate trade policies and trade-supported sustainable development strategies to be implemented in small and vulnerable economies. The lack of consistent and reliable data on vulnerability, impact of disasters and the links between these two features and the capacity to recover from shocks (resilience) is more or less generalised amongst these countries. In order to put trade liberalisation to work in favour of reducing their vulnerability, strengthening their resilience and improving their competitiveness, there is a need to overcome this situation as well as to assess the experiences of particular countries to draw lessons that may help defining appropriate strategies.

Responding to the above mentioned facts, the experience gained in the project on the Situational Approach to S&DT has led the researchers to propose a group of initial ideas for a research programme.
General objectives and institutional framework of a research programme on Trade, Disasters Risk Management and Competitiveness of SVEs

The initial ideas on the objectives of the research programme on SVEs point at enhancing knowledge on the links between international trade and competitiveness of these countries, on the one hand, and their vulnerability and resilience, on the other. These ideas ultimately aim at supporting the development of better policies and strategies for sustainable development of SVEs, and to focus the attention of international cooperation agencies in priority areas, where the positive impact of their support may optimise the achievement of development goals. Disaster Risk Management (DRM) and Trade-supported Strategies for Sustainable Development (TSDS) would be two ever-present strategic considerations in implementing the research programme.

Executing the programme would need integrating the expertise and institutional networks of international organizations in the fields of trade, sustainable development and disasters risk management, as well as the political support of the beneficiary countries and financial cooperation from international donors. A core group of these organizations, which would undertake the programme’s coordination, could be integrated by the Secretariat of the United Nations International Strategy for Disaster Reduction (UN-ISDR) and the International Centre for Trade and Sustainable Development (ICTSD), with the support of the SVE group of countries.

A two-track programme of activities

Two lines of work are envisaged in the research programme, based in concrete targets: improving the coverage and quality of basic data and analytical instruments on trade, competitiveness, disasters’ impacts and recovery conditions of small and vulnerable countries; and conducting case studies in various countries.

Activities in the first track would consist of improving the quality and coverage of basic data available and preparing a battery of secondary indicators on trade, competitiveness, disaster impacts and vulnerability and resilience of small and vulnerable countries. They might also consider integrating the data bases of the UN-ISDR Secretariat and the ICTSD on the mentioned fields, to facilitate their use in research and policy formulation by all interested parties.

Activities in the second track would consist of conducting case studies in various small and vulnerable countries in Africa; Asia and the Pacific; Central America and the Caribbean; and South America. These studies would aim at assessing experiences and learning lessons on how trade and competitiveness policies, on the one hand, and programmes focused on prevention and resilience building, on the other, may be made mutually supportive. Results from these case studies may eventually identify opportunities and help preparing concrete requests for Aid for Trade support, addressing the reduction of vulnerability and the enhancement of resilience through trade and competitiveness-related measures.
ENDNOTES

1 The official mandates under the Doha Round within which the negotiations on S&DT are taking place that affect both competitiveness and the vulnerability of small economies are basically paragraph 44 of the Ministerial Declaration and the "July (August 2004) Framework", and paragraphs 35 to 39 as well as annex F of the Hong Kong Ministerial Declaration. The negotiations relating to small vulnerable economies also have specific mandates in paragraph 35 of the Doha Declaration, paragraph 1 of the July Framework; paragraphs 21 and 41 and paragraph B of Annex C to the Hong Kong Declaration.

2 That text says that "the trade-related issues identified for the fuller integration of small, vulnerable economies into the multilateral trading system, should also be addressed, without creating a sub-category of Members, as part of a work programme, as mandated in paragraph 35 of the Doha Ministerial Declaration."

3 One of the tests consisted, in simple terms, in trying to reproduce the list of the SIDS, on the one hand, and the list of the landlocked countries, on the other, making use of a set of variables. The results of the tests can be considered conclusive in both cases: Both lists can be reproduced within acceptable limits of error using several characteristics of the countries studied. For the SIDS the best model has an explanatory power of 88percent or 95.7 percent if the EVI composite index of Vulnerability is incorporated. For the landlocked countries, although the model as a whole shows a significantly high goodness of fit (accuracy of estimates 93 percent), it is also observed that the human development index appears as the most relevant explanatory factor, which prevents drawing more concrete conclusions in terms of cause-effect relationships.

4 Small and Vulnerable Economies SVE: a situation combining smallness - ordinarily associated with high volatility and low resilience - with high vulnerability to external shocks and/or disasters associated to natural hazards, including or not the circumstance in which high transportation costs (remoteness) are implied; and Small and Remote Economies SRE : a circumstance combining both smallness and a remote location which implies high transportation costs.

5 Twelve countries share the characteristics of those in the list but have populations ranging between 10 and 15 million inhabitants: Angola, Burkina Faso, Cambodia, Cuba, Ecuador, Guatemala, Malawi, Mali, Niger, Senegal, Zambia and Zimbabwe.

6 For a detailed discussion on the Trade-supported Strategies for Sustainable Development (TSDS) please refer to the paper "Developing-Country Policy Issues in Reconciling Trade Liberalization and Sustainable Development Goals" (Corrales, 2007).

7 For instance, diversifying production and trade towards higher value-added products (goods and services, including environment and energy-related services), while at the same time increasing employment spillovers and reducing heterogeneity in productivities, may help to achieve higher rates of growth and better social results with a lower intensity of natural resource exploitation.

8 The international strategy for disaster reduction (ISDR) has been testing synthetic indicators of economic vulnerability to disasters involving natural phenomena, using the ratios of the cumulative values of the damage to the Gross Capital Formation. Monitoring of the indicator shows that vulnerability is growing for many small developing economies. Indicators on resilience are also being studied by ISDR, based on comparing the saving capacity of a country with the scale of the damage caused by the typical disasters that affect it. The saving capacity can in turn be expressed in terms of the sum of investment expenditure and the trade balance (exports minus imports), highlighting a clear link between trade performance and resilience (Miqulena, 2006).

9 See section 2.2

10 Indeed, if a statistical exercise trying to reproduce the self-defined list of developing countries is undertaken, the list can be replicated almost perfectly by putting together the lists of countries that depict at least one of the following features: (i) their per capita GDP is below the average of all WTO countries; or (ii) export concentration indexes by export lines are in the worst-off half of all WTO member countries (i.e. below the median); or (iii) GDP volatility indexes are in the worst-off half of all WTO members (i.e. above the distribution median. If the developing countries’ list is taken as the target list, statistical error levels in this
exercise (i.e. that countries that shouldn’t be in the target list fall within the result list, or that the latter leaves out countries that are part of the former) appear to be very small. This is evidenced by the fact that the result list covers all 32 WTO LDC members and also covers 77 of the 81 developing countries (109 out of 113; i.e. 96.5 percent accuracy or 3.5 percent error), and would only include 8 “developed countries” (8 out of 113; i.e. 7.1 percent error).

11 The per capita GDP and the export concentration index, if taken separately, do not reflect the "revealed competitiveness" of countries. Coexistence of developing countries showing very high levels or high increase rates of export market shares (e.g. Brazil, China, India, Costa Rica, Chile) and economies in the opposite extreme are characteristic of sectors A and B in Figure 1.1. Output volatility, as an independent indicator, seems to have the lowest correlation with proxies of revealed competitiveness, as shown in sector C of the same figure, where we find 12 countries, of which 5 are "Asian tigers" and 2 are amongst the highest oil exporting countries in the world.

12 In fact, there is an apparently low correlation between the three variables, which is illustrated in figure 1.1 by the fact that the intersection of the three circles cover only 12 percent of the 81 countries and 50 percent of them are located outside any intersection (no apparent correlation).

13 See Corrales (2007b) for an exhaustive explanation of the analysis that led to this country characterisation.

14 This section draws heavily from reporting on the SVE work programme in ICTSD’s Bridges Weekly (www.ictsd.org/weekly/archive.htm), informal discussions with relevant WTO delegates and Minutes of the meetings prepared by the WTO Secretariat (WT/COMTD/SE/M/1-14).

15 Topics covered included margins of preference; regional trade agreements; the Agreement on Subsidies and Countervailing Measures; a proposal to allow regional bodies to be designated as the implementing authority for the Agreements on Sanitary and Phytosanitary Measures (SPS) and Technical Barriers to Trade (TBT); WTO rules and procedures; technical assistance and capacity building; and the graduation of small economies which were LDCs (WT/COMTD/SE/W/3).

16 These include the provision of tariff and quota-free treatment of goods and services originating from small economies; the provision of technical assistance to aid in export diversification, compliance with TBT and SPS rules and improvement of productivity; the reservation of a certain percentage of tariff quotas of each WTO Member for small economies; the incorporation of small economies into the LDC’s Integrated Framework; and to extend the special treatment granted to LDC in the accession process to small economies.

17 On preferences, the proposal suggested gradually phasing out ("grandfathering") trade preference arrangements that cover products of export interest to preference-dependent small economies and creating "adequate alternative arrangements" to offset the adverse impact of WTO-led trade liberalisation on the preference margin and market access of these countries. On investment, it calls the creation of long-term preferential investment facilities, and on subsidies it demands that small economies be exempted from disciplines on export subsidies and be allowed certain other categories of non-actionable subsidies.

18 A point-by-point analysis of each characteristic/problem listed in W-12, made by the PSVEs in their intervention at this meeting, is available online at WT/COMTD/SE/M/10.

19 The submission states that these calculations would be based on WTO data from 1999-2004.

20 On the basis of empirical evidence, these authors maintain that being landlocked reduces mean growth by approximately 1.5 percent a year.

21 Section 3 of the paper "Smallness, vulnerability and Remoteness from a Situational Approach perspective" (Baritto, 2007) offers a detailed discussion on these tests and their results.

22 In general terms, the model’s overall goodness of fit can be considered very high at a level of P = 0.0001. The countries wrongly classified as SIDS are 11 out of 121 non-SIDS: Bahrain; Bermuda; Costa Rica; Cyprus; Djibouti; Gambia; Hong Kong, SAR; Luxembourg; Macau; Nicaragua; and Panama. The SIDS countries wrongly
classified as non-SIDS are 8 out of 34: Cuba, Dominican Republic; Guyana; Haiti; Jamaica; Papua New Guinea; Singapore; and Trinidad-Tobago.

23 The countries wrongly classified as landlocked are Benin, Gambia and Mozambique, while those erroneously classified as non-landlocked are Bolivia, Paraguay, Uganda and Zimbabwe.

24 The main limitation in the case of the landlocked countries derives from the fact that there is a large group of them for which the shipping costs (based on CIF: FOB ratio) are unknown.

25 Greek symbols are used hereafter to refer to the three main characteristics: $\sigma$, equivalent to S for smallness; $\varpi$, equivalent to V for vulnerability; and $\rho$, equivalent to R for remoteness.

26 Note that when intersecting the three sets $\sigma$, $\varpi$ and $\rho$ the (+) symbol has been used to identify the “pure” circumstances, namely those in which only one adverse factor is present, where there is no evidence of the simultaneous influence of the other factors.

27 It is important to take into account that one of the main reservations in WTO against the arguments of the SIDS is that the vast majority tend to have high per cápita incomes and rather high levels of Human Development Index, facts which are also clearly highlighted in the literature.

28 Details on the statistical tests used to prepare the list presented here for the situations SVE and SRE are given in the already cited papers Baritto (2007) and Corrales (2007 b).

29 The twelve countries integrating the difference, i.e. the small and vulnerable economies with populations between 10 and 15 million inhabitants are: Angola, Burkina Faso, Cambodia, Cuba, Ecuador, Guatemala, Malawi, Mali, Niger, Senegal, Zambia and Zimbabwe.

30 The reader is referred to the papers Werner Corrales "Developing Country Policy Issues in Reconciling Trade Liberalization and Sustainable Development Goals (2007 a) and Werner Corrales "Developing Countries’ Competitiveness and Vulnerability in a Situational Approach to Special and Differential Treatment” (2007 b) for broader comments and examples on the kinds of actions that may be undertaken to implement the trade-supported strategies for development introduced in chapter 1 (innovation, linkages creation, environmental sustainability, and social and human capital formation).

31 See Table 1.1 for codes used in designating Policy Actions.

32 Refers to policy instruments that would be implemented at national level. In some cases implementing such instruments would require flexibilities granted by means of Special and Differential Treatment provisions.

33 Refers to instruments negotiated internationally and administered by third parties, either governments or international organizations.
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ABOUT ICTSD

Founded in 1996, the International Centre for Trade and Sustainable Development (ICTSD) is an independent non-profit and non-governmental organization based in Geneva. By empowering stakeholders in trade policy through information, networking, dialogue, well-targeted research and capacity building, the centre aims to influence the international trade system such that it advances the goal of sustainable development.