

Entering financial dire straits

In the wake of the global financial crisis, the urgent financial challenges facing small and vulnerable states have been marginalised in the new international agenda, writes **André Broome**

Amidst last year's flurry of global policy negotiations, multilateral institutional reforms, rapid disbursement of new IMF and World Bank loans to crisis-hit countries, and a return to (temporary) fiscal pump-priming and monetary expansion among developed economies, the acute economic vulnerabilities and particular set of financial challenges faced by the world's smallest states have been all but forgotten.

With the epicentre of the current global financial crisis located in the USA – from where it quickly engulfed other developed economies before going on to wreak havoc on national economies the world over – consumer demand for developing economies' exports tumbled during 2008 and 2009. Because they lack easy access to the development elixir of external finance and suffer disproportionately from trade shocks, small states are most at risk from global financial turmoil and the balance of payments shortfalls such episodes inevitably produce for developing economies. The raw economic figures make for sobering reading. In October 2009, the IMF's World Economic Outlook projected world economic output would shrink in 2009 as a whole by 1.1 per cent, driven by an incredible 11.9 per cent contraction in the volume of world trade.

Many small island states are already buffeted by the ruinous effects

of climate change, with microstates such as Kiribati, Mauritius, Antigua and the Maldives bearing a disproportionate burden following the failure of larger and more powerful states to agree on a more ambitious multilateral agenda at the Copenhagen climate change summit in December 2009. These states had no involvement with America's subprime property bubble, bear no responsibility for the rampant exploitation of mortgage-backed securities by Anglo-American financial institutions to generate quick – and in many cases chimerical – profits, and could exercise no say over the ham-fisted deregulation of the division between investment banks and high-street banks in developed economies that contributed to the global credit crunch.

Yet it is small states that stand to suffer the most – both immediately and in the longer term. Because of their innate vulnerabilities, the global financial crisis has intensified the economic pressures they face through stimulating a precipitous decline in private capital flows, greater competition for scarce bilateral aid, less income from tourism as more wealthy travellers opt to holiday closer to home, and greater difficulty accessing – let alone servicing – public debt. In short, small states have been affected much more severely relative to the larger economies, while at the same time they have fewer policy tools and economic resources at their disposal to mediate the domes-

Facing the wrath of nature

CLIMATE

The Copenhagen outcome highlighted the sense of abandonment among small island states in the face of an apparent indifference to their plight from the developed and rapidly developing nations alike

Richard Syngé

Small island states were well represented at the Copenhagen climate change conference in December, but to no avail. In the final days of the conference, President Johnson Toribiong of Palau vainly appealed to India and China to recognise the fate of the small states and to provide them with technology and finance to help low-lying islands face “the wrath of nature”. The Prime Minister of Vanuatu, Edward Natapei, made an emotional appeal to the developed countries too, with the words: “It is a matter of survival for us.”

Member countries of the Alliance of Small Island States (AOSIS) had hoped that Copenhagen would be their salvation. No less than eight Caribbean heads of government attended the conference, having in the previous months prepared their common position in the Liliendaal Declaration on Climate Change. This specifically makes the demand that the rise in average world temperatures be limited to 1.5 degrees, while also underlining the need for a common regional approach to address the threats and challenges of climate change, and appealing for financial



Storm damage in the Caribbean will increase

support to access technologies necessary to undertake mitigation actions.

AOSIS members from the Caribbean even had their own song, “1.5 to stay alive”, composed by Barbadian performance poet Adisa ‘AJA’ Andwele, which highlighted the fears and concerns of people living on small islands. Sadly few at Copenhagen seemed to be in the mood to listen.

Looking beyond the disappointing outcome, Dr Ulric Trotz of the Caribbean Com-

tic welfare effects of the global financial crisis on their own.

Enter a revitalised and flush IMF. In contrast to its lending of approximately \$143 billion from 2000 to 2007, in the seven months from November 2008 to May 2009 the Fund approved large new loans to 12 countries that totalled over \$153 billion. These loans went hand-in-hand with more flexible policy conditionality, easier access to more money up-front, and a greater tolerance of unorthodox policy instruments (such as temporary capital controls in the case of Iceland).

For especially vulnerable economies, the IMF provides access to its 'exogenous shocks' facility, which is designed to tailor policies to local circumstances with more flexible conditionality. One small state in dire straits that recently sought an exogenous shocks facility loan is the Maldives. With estimated current account deficits of 51 per cent of GDP in 2008 and 29 per cent of GDP in 2009, and facing a fiscal blowout with a projected budget deficit of 28 per cent of GDP in 2009, the Maldives is hardly in a position to strike a hard bargain with the IMF. Accordingly, when the Maldives borrowed \$79.3 million under a 3-year IMF standby arrangement and \$13.2 million under a two-year exogenous shocks facility arrangement in December 2009, these loans incorporated tough conditions that mandated wide-ranging macroeconomic policy reforms.

On the face of it, the IMF has modified its rules for crisis management since episodes like the Asian financial crisis of 1997-98. But it is one thing for the IMF to relax loan conditionality for large emerging market economies and quite another to loosen policy constraints across the board. In comparison to larger economies, small states that have turned to the IMF for essential financial support during the current crisis have had to agree to a comparatively stricter set of conditions.



Economic storms loom for small island nations

The case of the Maldives illustrates the limits of the IMF's new-found tolerance of temporary unorthodox measures in economies that are experiencing severe financial distress. The sticking point for the world's most vulnerable states is whether governments' existing economic policy settings are deemed by the IMF to be 'sound'. When current economic policies are judged to be unsustainable, IMF loan conditionality remains an uncomfortable straitjacket, regardless of the financial vulnerabilities the small states face. ⑨

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munity Climate Change Centre (CCCCC) says that Caribbean countries are not just faced with the constant threat of hurricanes but also that of drought associated with the El Niño phenomenon. "In addition to the projections coming out of our research that extreme events will be more severe, our projections are for a warmer and drier Caribbean. Indeed, some countries are already suffering serious water shortages."

The CCCCC remains committed to undertaking local actions, but Dr Trotz notes: "One of the restricting factors is the question of resources." In recent years the Centre has set about monitoring changes in sea levels and climate, improving access and availability of data on coral reefs and other threatened forms of life. The Centre helps countries to articulate their adaptation policies and has set up a network for regional harmonisation with assistance from Canada's Climate Change Development Fund. But such assistance seems both hard to access and insufficient to meet the challenges ahead.

With only a handful of isolated and small projects aimed at harnessing renewable

energy sources, the Caribbean states have few sustainable strategies for surviving long-term damage from climate change.

Perhaps one of the small states best equipped to face up to the challenge is Guyana. Capitalising on the country's

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massive forest endowment, the government of President Bharrat Jagdeo has been able to formulate a low-carbon development strategy based on the principle of Reduced Emissions from Deforestation and Forest Degradation (REDD). This calls for investment in organic agriculture, sustainable forestry and ecotourism, as well as in

hydroelectric power to cut fossil fuel use.

Guyana has signed a partnership deal with Norway, providing \$30 million for forest conservation and up to \$250 million by 2015, based on its success in limiting emissions. The idea is to use the money to protect the rainforests and implement its low-carbon strategy.

As a follow-up to the REDD deal with Norway, Guyana has also signed up for a collaborative project on avoided deforestation with Conservation International (CI). Agriculture Minister Robert Persaud says Guyana's leadership role in this area is now being recognised and the new project could be counted as "one of the positive and enduring features coming out of the Copenhagen talks". CI's vice-president Lisa Famolare also describes Guyana as "in the position of leadership globally on climate change" because of its low-carbon strategy.

With little else of cheer coming out of Copenhagen, it is good to know that at least some of the world's small and vulnerable states can see a way forward.