

## **Small state diplomacy and global competitiveness**

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**Abstract:** Competitiveness is not only an economic matter; it is also a foreign policy issue. It requires the coordinated action of the state, business community and civil society. Global economic institutions now confront a new challenge to design strategies and roadmaps for reform that will build on the achievements of the past, and cope with an increasingly new set of ripples that poses risks to the orthodox practice of development and ignite a search for a new kind of diplomacy. A global dialogue on competitiveness and economic development is in the making, and small economies have a vested interest to be part of that dialogue. While small states have fewer resources to devote to the tasks of diplomacy and effective interaction with other states, this shortcoming can be reduced by alliances and networks, given the large number of small states with common interests. Small states in Europe are strategically placed to recalibrate that continent's approach to regional and international diplomacy in its quest to promote competitiveness, and sustain growth and equity in its development goals. As such, it can bring important lessons to the attention of other small states in the world and add considerably to the expectations of this exercise in global analytical leadership.

**Keywords:** competitiveness; diplomacy; European Union; small states

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## **Introduction**

In the new geopolitics of today, there has been an “outpouring of anxiety over the future of the liberal order” (Acharya, 2017). The spillover of this anxiety has opened a dialogue on the “new globalisation” in a period of protectionism, weakening multilateralism, and a political assault on global competitiveness. Acharya (2017, p.271) sums up the political architecture of the emerging multiplex world order as follows,

[I]nternational relations scholars should be wary of conventional wisdom and be open to new concepts and theories, and hence to new possibilities of world order that have no precedent in history... where scholars and practitioners alike will have to embrace the complexities of this new system.

The latest Global Competitiveness Report states that “governments, businesses, and individuals are experiencing high levels of uncertainty as technology and geopolitical forces reshape the economic and political order that has underpinned international relations and economic policy for the past 25 years” (The Global Competitiveness Report, 2018, p. v). These insights provide the setting for discovering new possibilities for small state diplomacy in improving small state competitiveness and economic advancement in an uncertain economic order.

Competitiveness is not only an economic matter; it is also a foreign policy issue. The Global Competitiveness Report (2018) affirmed that “improving competitiveness requires the coordinated action of the state, the business community and civil society.” Further, the report explains that uncertainty among government, business and individuals is being driven by geopolitical forces which have reshaped the economic and political order with implications for international relations and economic policy. Competitiveness determines a country’s global influence and its ability to shape the international dialogue, and is the set of institutions, policies and factors that determines the level of productivity of a country (Global Competitiveness Report, 2018). A competitive economy is productive, and productivity leads to growth and higher incomes and improved standards of living for all. Global economic institutions must now confront a new quest to design strategies and roadmaps for reform that will build on the achievements of the past, and cope with an increasingly new set of ripples that poses risks to the orthodox practice of development and ignite a search for a new kind of diplomacy. A global dialogue is in the making, and small economies have a vested interest in being part of that dialogue.

In 2015, the United Nations General Assembly adopted the 2030 Sustainable Development Agenda, along with the 17 Sustainable Development Goals (SDGs) and 169 targets which cover the economic, social and environmental aspects of sustainable development (United Nations 2015). While all countries and stakeholders are expected to act collaboratively to implement this roadmap, with a central theme of “no one left behind”, small states face their own unique challenges that threaten the achievement of the SDGs (United Nations, 2015). Alicia Barcena called for “revitalising multilateralism” to promote the 2030 Agenda, and it is at the cornerstone of small states voice and influence in accepting collective responsibility for global challenges (Bárcena, 2017). The World Bank in their recent presentation “Small States: A Roadmap for World Bank Group engagement” has explained that these challenges include building resilience to climate change, diversifying their economic base, and developing new systems to generate and attract public and private finance (World Bank, 2017).

Small economies lack adequate financial resources for achieving the SDGs, while at the same time there have been new challenges for them in accessing development finance from the international community (World Bank, 2017). Additionally, the World Bank’s ‘ease of doing business’ index is a key indicator in attracting international investment and countries including small states are ranked against each other. The appropriateness of the index in measuring competitiveness in small states, and the amount of information provided by the index on small states has been questioned (Commonwealth Secretariat, 2007) and, more recently, the integrity of the index has come under scrutiny (The Economist, 2018). Moreover, small nations are generally more sensitive to and more impacted by international developments, but at the same time have benefitted more from globalisation (Spolaore, 2018).

Recently, there are indicators that the international economic and political environment has become less supportive of globalisation, which may negatively impact small states (Spolaore, 2018; Dookeran, 2018). It is therefore not only a technical dialogue to come up with solutions to these challenges, but also a diplomatic dialogue, since diplomatic interventions are necessary, within global institutions and in the global policy frameworks that are being developed. Diplomatic intervention is an important tool available to small states that can improve their global competitiveness standing (Dookeran, 2018). While small states have fewer resources to devote to the tasks of diplomacy and effective interaction with other states, this shortcoming can be reduced given their large number and common interests through the formation of alliances and networks (Estevadeordal & Goodman, 2017). Further, European small states are strategically positioned in regional and international diplomacy to promote a global competitiveness and growth agenda where small states are not left behind (Dookeran, 2018) with special conditions for their participation in international affairs, and years of experience in participating in international institutions (Pedersen, 1984).

This paper explores small state diplomacy in affecting international competitiveness with reference to European small states. The concept of small state diplomacy is defined and three current issues affecting competitiveness and diplomacy are explored: small states access to development finance; competitiveness measures; and threats to globalisation and small state alliances and networks. The paper comprises four sections, including this introduction. Section 2 defines and outlines small state diplomacy. Section 3 looks at the three current issues in international diplomacy and small states. Section 4 concludes the paper.

### **Small State Diplomacy**

Small states operate in the same political and economic environment as large states, and in their foreign policy pursue the same objectives of security, prosperity, and wellbeing of their citizens and conduct their diplomacy using the same diplomatic toolbox as large states. The international system contains many small states, which form an integral part of the international order (Keohane, 2009). The number of small states increased significantly in the twentieth century, with the end of both World Wars, the decolonisation process in the 1960s and the collapse of the Soviet Union in 1991 (Veenendaal & Corbett, 2014; Kassimeris, 2009). About two-thirds of the member states of the United Nations are small states. In the European Union (EU), there are (at the time of writing) 28 members and 7 are small states (Thorhallsson & Wivel, 2006). In other words, small states make up 25 percent of EU membership. Small states are here defined as states with a resident population of three million or less. In the European Union, they include Cyprus, Estonia, Latvia, Lithuania, Luxembourg, Malta and Slovenia (Thorhallsson & Wivel, 2006). Small states are, therefore, well represented within the EU and the international community, and can influence regional and world politics (Henrikson, 2008). Diplomatic means can transform the smallness of small states into an asset when promoting national and international interests (Dookeran, 2018).

Small states have fewer resources to devote to the tasks of diplomacy and effective interaction with other states (Henrikson 2008). This includes resources required for gathering and analysing relevant information, for elaborating and projecting positions and points of view, and for organising and deploying alignments and circumstances in support of their positions. Although their limited resources can put small states in a weaker bargaining position in their interactions with large states, this disadvantage can be reduced, given the large number of small states with common interests (Estevadeordal & Goodman, 2017). This may require reliance on collective solidarity and the rule of law, strict focus on limited objectives, and the adoption of

creative solutions (Dookeran, 2018). The role of small states in various multilateral negotiations confirms that small and cohesive groups can have an important effect. For example, the Neutral and Non-Aligned (N+N) countries in the Conference on Security and Cooperation in Europe (CSCE), the Alliance of Small Island States (AOSIS) in climate negotiations, and the Small and Vulnerable Economies (SVEs) group in the World Trade Organisation DOHA round (Panke, 2012).

The characteristics of small states influence how they operate in the international system. The characteristics of small states including their small size, openness and proneness to natural disasters and vulnerability to climate change influence the issues they deem important (World Bank, 2018). The effects of small state actions on the international order tend to be more focused (Kassimeris, 2009). Small states are attracted to the notions of legitimacy and the rule of law (Pollard, 2007). They recognise the valuable role that multilateral diplomacy plays in enhancing their engagement and amplifying their voices on regional or global issues, thus levelling the playing field (Henrikson, 2008). Nevertheless, the many complex structures and processes of multilateral diplomacy strain their resources.

## **Diplomatic Issues in Global Competitiveness**

### *Accessing Development Finance*

Financial vulnerabilities are a threat to competitiveness, and threaten a nation's ability to finance innovation, spread the benefits of technological adoption and provide worker protection in a flexible labour market (World Bank, 2017). The World Bank Roadmap for small states specifically linked financing to competitiveness by carefully identifying seven priority action areas, in which there is need for the development of a global practice: inclusion of vulnerability as a criterion for concessional financing; predictability of affordable financing; debt sustainability; access to new and existing climate financing; capacity building and technical assistance; diversification of small state economies; and access to financial markets (World Bank, 2017). Diplomatic interventions for the benefit of small states can play an important role here within the global dialogue, global institutions and the global policy frameworks that are being framed on development finance (Dookeran, 2018).

In July 2015, at the Third International Conference on Financing for Development, development finance entered a new era when the international community agreed to the Addis Ababa Action Agenda (AAAA): a framework and set of commitments for financing the SDGs, which require far more funding than aid can provide. Meeting the SDGs will require an additional US\$ 2.5 trillion in private and public financing per year and an additional US\$ 13.5 trillion to implement the 2015 United Nations Climate Change Conference (COP21) Paris climate accord (UNCTAD, 2014). The World Bank, together with other multilateral development banks and the International Monetary Fund (IMF), committed to use billions in investment funding, aid, and grants, in innovative ways to increase development finance (World Bank 2017). It is imperative that small nations including EU states are able to access these funds successfully, and diplomatic channels can play a key role here (Dookeran, 2018).

In seeking development finance, small states – including European small states – may consider taking into account their vulnerability and seek preferential access to concessional finance (Dookeran, 2018). Given their small populations, limited geographies and the difficulties to diversify, small states are particularly vulnerable to external shocks. This vulnerability hinders small states' capacity to progress towards the SDGs. Small states must also seek the

predictability of affordable financing. Despite acute vulnerabilities to shocks, small states are ineligible for concessional financing because of their high per capita incomes. Debt sustainability is another urgent matter facing small states (Bustillo et al., 2018). Vulnerability to natural disasters, with high costs of recovery, contributes to small states' indebtedness. In addition, limited fiscal space, narrow potential for domestic revenue generation, and the high costs of public services typically exacerbate debt burdens (Bustillo et al., 2018). Because of these debts, small states may not be able to access concessional or market financing (Dookeran, 2018).

Small states would do well to invest in building resilience and diversify their economies to lessen their vulnerability, manage their debt burdens and attract private sector financing (Bustillo et al., 2018). Accessing new and existing climate financing is also recommended. Although the international community is giving high priority to climate adaptation and mitigation, small states have difficulty accessing the vast pool of climate funds (World Bank, 2017). Additionally, capacity building and technical assistance in small states must be developed. Many small states face limited human, institutional, and implementation capacity to carry out tasks needed to absorb development finance and implement the investments necessary to address their vulnerability and lack of resilience. Donor fragmentation in small states hinders the effective use of financing for achieving development outcomes (World Bank, 2017).

The World Bank Roadmap identified financial deepening of the private sector – the cascade approach and blended finance approaches – as relevant to enhancing competitiveness strategies in small states in Europe, designed to support progress towards the SDGs at the Third International Conference on Financing for Development in 2015 (World Bank, 2017). Blended finance is described as the strategic use of development finance and philanthropic funds to mobilise private capital flows to emerging and frontier markets resulting in positive results for both “investors and communities” (World Bank, 2017, p.16). It offers the possibility to scale up commercial financing for developing countries and to channel such financing toward investments with development impact. The increasing emphasis on blended finance approaches evokes the need to increase the understanding and transparency of these flows.

The World Bank adopted the cascade approach as a concept to guide its effort to leverage the private sector for growth and sustainable development. The guidelines on how to implement the cascade are very clear. When a project is presented, ask: is there a sustainable private sector solution that limits public debt and contingent liabilities? If the answer is yes, promote such private solutions. If the answer is no, then ask whether it is because of policy gaps, regulatory gaps or their weakness. If so, provide World Bank support for policy and regulatory reforms, then assess the risks and see whether World Bank instruments can address them. If you conclude that the project still requires public funding, only then pursue that option (World Bank, 2017).

The mandate of the International Finance Corporation, an affiliate of the World Bank Group is to enhance financial flows for small economies. Capital flows, and their direction and sustainability, are key to building resilience for the economies of small states around the world. Some of the criteria to be considered here include: the predictability of affordable financing; debt sustainability; access to financial markets; and economic diversification. With respect to deepening private sector involvement, the report says,

International Finance Corporation is committed to helping expand the limited set of economic opportunities leveraging the full weight of resources of the World Bank group. Ensuring obstacles for the poor and the bottom 40 percent of the population to access these economic opportunities are reduced (World Bank, 2017, p. 16).

Small state economies tend to suffer from limited export diversification and productive capacities (World Bank, 2017). A lack of economic diversity leaves small states dependent on the economic and political situations of neighbouring transit countries, and vulnerable to economic and climate shocks. Small states must enhance their capacity to attract, manage and invest with both concessional and private sector resources. Access to financial markets poses a risk to small states (World Bank, 2017). Large financial entities are effectively cutting ties between banks in small states and global finance. A decline in correspondent banking relationships is having damaging results at the individual and community levels, particularly by affecting remittances and complicating the provision of domestic and cross-border payments (Alleyne et al., 2017; Alwazir et al., 2017).

At the 17<sup>th</sup> annual Small States Forum held in October 2017 in Washington DC, 50 small states banded together and were able to successfully increase their development finance allocation from the World Bank four-fold after active diplomacy. Members of the Forum welcomed the World Bank's May 2017 Roadmap for engagement with small states (Small States Forum, 2017). The challenge now is to find transformative projects that can absorb and make the most of these extra resources. The Forum also highlighted the importance of mobilising public and private sector financing for renewable energy, the green and blue economy, and technology development in building resilience and reducing vulnerability in small countries.

Some small states which are vulnerable to natural disasters, such as Nauru and Palau, do not qualify for the small states exception from the International Development Association because they are classified as high income countries, or meet the International Bank for Reconstruction and Development's credit standards and are therefore unable to access resources for clean-up and relief. The 2017 Small States Forum successfully lobbied for the World Bank to explore financing solutions for countries in this category (Small States Forum, 2017).

Financial institutions are seeking to 'de-risk', and are leading to the withdrawal of correspondent banking relationships in small states, resulting in financial exclusion from the international community. The 2017 Small States Forum proposed establishing a working group to address the development challenges of de-risking in small states and to provide a systematic and comprehensive response and to explore possible solutions, including Blockchain technology (Small States Forum, 2017). Malta, now dubbed 'Blockchain Island' (Holotescu, 2018), has an opportunity to play a leadership role here for other small states. At the same time, it has been recently accused by the EU of failing to correctly supervise financial institutions and ensure their compliance with anti-money laundering rules. In November 2018, the European Commission required the Maltese Financial Intelligence Analysis Unit to: improve its methodology to assess money laundering and terrorist financing risks; enhance its monitoring and supervisory strategy; ensure that the authority is able to react in an appropriate time when a weakness is identified; ensure that its decision-making is properly reasoned and documented; and adopt systematic and detailed record-keeping processes (European Commission, 2018).

### *Competitiveness Measures and Integrity*

One of the flagship economic reports that measures business competitiveness rankings is the World Bank's 'ease of doing business' index. A higher ranking (lower numerical value) indicates that the regulatory environment is more conducive to starting and operating a local business. These indicators carry considerable attention in investment attractiveness, and include regulatory hurdles, tax and exchange rate issues, and other measures that make a "better" business environment and improve competitiveness (Dookeran, 2018). The index attracts extensive international media coverage and its findings are used by countries against each other to improve their competitiveness standing (Dookeran, 2018). It may however be argued that the 'ease of doing business' index is inappropriate for measuring competitiveness in small states, provides limited information on competitiveness in small states, (Commonwealth Secretariat, 2007), and most recently has been accused of political interference bringing the integrity of the index into question (Dookeran, 2018; Morck & Shou, 2018).

The 'ease of doing business' index has been criticised on technical grounds, with flaws in its definition of competitiveness, model specification, variable choice, causal relationships and use of data. Focus on particular sectors rather than the economy as a whole using a smaller number of critical variables may be more appropriate in small states (Commonwealth Secretariat, 2007). The rankings are determined via a methodology which sorts the aggregate distance to frontier scores on 10 topics (starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts and resolving insolvency) (The Global Competitiveness Report, 2018). Each topic consists of several indicators, giving equal weight to each topic. The method entails answering measurable questions, and the answers determine a country's score, and its score, relative to those of other countries, determines its global rank and bragging rights.

Critics argue that the index is limited in scope since it focuses on 10 topics, with the specific aim of measuring the regulation and red tape relevant to domestic small to medium-size firms (Morck and Shou, 2018). Accordingly, the index does not measure all aspects of the business environment that matter to firms and investors and all factors that affect competitiveness. The index does not for instance measure security, macroeconomic stability, corruption, quality of institutions and infrastructure, and foreign investment regulations. As an alternative, the Commonwealth Secretariat developed the Small State Manufactured Export Competitiveness Index (SSMECI) (Commonwealth Secretariat, 2007). The SSMECI focuses on basic economic fundamentals including macroeconomic stability, outward oriented trade policy, high levels of human capital and efficient infrastructure and is deemed more appropriate than the 200 sub-indices in the 'ease of doing business' index. It emphasises the ability to produce manufactures competitively in small economies. The SSMECI however does not have the same international recognition as the 'ease of doing business' index.

The 'ease of doing business' index covers around 190 jurisdictions, but includes less than twenty small states; while the SSMECI covers 47 small states, including the 7 EU small states. A large number of small states are excluded from this index, largely because the data requirements for calculating the index are huge and the data simply do not exist in these countries. Small states have small populations and often underdeveloped national statistical systems and institutions; they therefore can lack the capacity and demand to collect the extensive data required. Having an appropriate index to measure competitiveness in small

states allows for proper benchmarking of small states against each other (that is, countries with similar characteristics) and provides a yardstick to measure performance. Small states at the lower end of the ranking could then emulate and learn from the experience and policy strategies implemented by small states at the higher end of the ranking. The SSMECI is constructed taking into account the data availability in small states and realistic data requirements. Malta and Estonia top the rankings because of their greater access to markets and the positive effect of sustained competitive pressure from their large European members, and as such provide appropriate benchmarks for small countries seeking to improve their competitiveness.

An article in *The Economist* (2018) calls into question the integrity of the ‘ease of doing business’ index and its accompanying reports. The article explains that the compilation of the ‘ease of doing business’ index may have been tainted by the political motivations of World Bank staff (The Economist, 2018). The story was based on an interview with Paul Romer, the World Bank’s Chief Economist, who pointed out that Chile’s ranking in the yearly report had dropped sharply during the presidency of President Michelle Bachelet, a left-leaning politician who took office for the second time in 2014 (Reuters, 2018; The Economist, 2018; Zumbun & Talley, 2018). In small states, with weaker institutions and institutional frameworks and lack of data, the possibility of political interference may be even larger.

To move the pendulum forward, the technical analysis will need to build a momentum for effective results. The Global Competitiveness Report recently developed a proposal on “the future of competitiveness benchmarking” which offers an opening for technical negotiations and conceptual innovations in the design challenges (Dookeran, 2018). This index is a valuable measure of how a country is progressing to build structures and processes to support policy initiatives on a global competitiveness framework. As such, the search for diplomatic interventions becomes necessary, within global institutions and in the global policy frameworks that are being framed, and small states have a role to play.

A global dialogue is in the making with regards to the ‘ease of doing business’ index and measuring competitiveness, and small economies have a vested interest to be part of that dialogue. Small states could coordinate to improve the appropriateness, integrity and objectivity of international competitiveness indices. It is therefore not only a technical dialogue, but also a matter of diplomacy. In an often cited publication, Long (2017) argued that “small states can influence institutional rules and procedures....just as for rules shaped by greater powers”. Many scholars argue that “small states can “punch above their weight”, and “Luxembourg has been a founding model member of European institutions, and it has used this to pressure for favourable EU policies, while seeking to strengthen institutions as a bulwark against historic German French rivalry” (Long, 2017). Allegrezza (2017) draws attention to the “competitiveness observatory” set up by the social partners in Luxembourg and the measurement of the competitiveness scoreboard which was discussed in “a special parliamentary session” on competitiveness and growth.

#### *Threats to Globalisation and Alliances and Networks*

Small nations are generally more sensitive to and possibly more affected by developments in the international system, which can impact their competitiveness (Spolaore, 2018). Small nations are more vulnerable, and the economics of their situation is precarious. The workings of the global system, particularly the globalisation of business, may harm their competitiveness even while promoting their freedom. After several decades of an international economic and political environment that has been highly supportive of globalisation, there are indications of



meaningful change (Spolaore, 2018; Rodrik, 2018; Llundji, 2015). There are threats to globalisation, a rise of populist policies and increased geopolitical pressure (Dookeran, 2018). This new international environment is likely to pose a challenge to small economies and their international competitiveness. The international community, a large part of which is now made up of small states, should be prepared to act, for the global public good, as well as out of sheer political and also environmental self-interest, to help safeguard the livelihood of the world's many and varied small states. Small state diplomacy can play an important role here.

In Europe, there is political backlash against international integration both globally and within the EU as demonstrated by Brexit and the rise of anti-European political movements (Rodrik, 2018; Inglehart and Norris, 2016). Critics have argued that institutional integration in Europe has gone too far and that the euro has failed, and Brexit is seen as the first step towards European disintegration (Spolaore, 2018). Furthermore, the immigration crisis may lead to the return of permanent barriers within Europe (Goodwin and Milazzo, 2017). On the other hand, supporters of European integration attribute the current economic, financial, and political crises to incomplete integration, and seek further integration through a banking union, fiscal union and full political union (Spolaore, 2018). The European integration dilemma involves high economies of scale from commercial integration, common immigration policies, common legal system, common defence and security, but also high heterogeneity from different preferences, beliefs, and values in large and diverse populations (Spolaore, 2018).

Small nations have benefited from increasing international openness. They thrive in an economically integrated world, while they are disproportionately hurt by international barriers. Alesina and Spolaore (2003) empirically demonstrate that conditional correlation between international openness and economic growth for larger countries is 0.150 as against 0.641 for smaller countries. This suggests that while international openness is beneficial on average for countries of all sizes, it is especially beneficial for small countries. The Commonwealth Secretariat, with small states as the majority of its members including Cyprus and Malta, carries out policy analysis, consultations and global advocacy to promote the international trade interests of these countries. As a result, trade between Commonwealth countries has seen phenomenal growth termed the "Commonwealth effect", rising from US \$200 billion in 2000 to more than US \$600 billion in 2015 and projected to surpass \$1 trillion by 2020 (Commonwealth Secretariat, 2015).

Regional public goods have once again been cited as important in the context of twenty first century international relations. Heterogeneous preferences negatively affect the provision of public goods which are non-rival in consumption and must be shared by all within a jurisdiction. In contrast, diversity of preferences and traits come with benefits when considering interactions about rival goods. Egan (2017) traced the pivotal role of European public goods in the foundations of European integration. The range of these public goods include competition policy and market access, common external tariff and trade matters, transportation and cross border services, environment and negative externalities, economic convergence and income and wealth disparities, macroeconomic stabilisation and the euro, and internal security and border control (Estevadeordal and Goodman, 2017). Egan (2017, p. 256) concluded that "despite the growing chorus of disenchantment in Europe with the concerns for inequality, productivity and migration there remains a role for regional organisations to act as catalysts for collective action by providing regional public goods." But Egan (2017, p. 258) hastens to add that it "can also weaken democratic institutions and can collapse trust in European institutions."

“Small states have a greater capacity to influence the agenda in world politics and play a critical role in the evolution of European integration than is commonly understood” (Long, 2017, p. 9). Inside European institutions, small states can construct a “position of authority” through diplomacy by influencing the “rules and voting procedure” (Long, 2017, p. 9). In this sense, small state diplomacy is an essential component for advancing its interest in global competitiveness. Estevadeordal and Goodman (2017) argue that regional leadership alliances and networks fit together to link public goods with sustainability and, with Acharya (2017), called for a new conceptualisation of regionalism that will embrace more complex situations in a changing “balance of power”.

Small states can coordinate actions to counterbalance current threats to international integration and globalisation, as they have done in the past on monumental international issues, since they are less constrained by political alliances and direct national interests, championing ideas that have led to major international agreements (Súilleabháin, 2014). Further, decolonisation, the end of bipolarity, democratisation, trade liberalisation and the digital revolution are five factors that have given small states more freedom (Henrikson, 2001). In addition, small countries may find it easier to respond to citizen preferences in a democratic way (Alesina & Spolaore, 2003). Could small states shift global economic structures to favour their interest? Would small states benefit from open trade systems? How could small states overcome their ‘smallness’ and develop diplomatic leverage? These and other relevant questions addressed in the work of Henrikson (2001) and Alesina and Spolaore (2003) provide a critical body of thought that informs the agenda of small state diplomacy and competitiveness in today’s world.

## **Conclusion**

This paper has argued that competitiveness is not only an economic matter, but also a foreign policy issue. Competitiveness determines a country’s global influence and its ability to shape the international dialogue. It requires the coordinated action of the state, business community and civil society. Three global issues with implications for competitiveness, and where it is crucial for small states to have a voice, are: accessing development finance; measuring competitiveness; and a changing international political and economic environment that is not as supportive of globalisation as in the past. Small nations are generally more sensitive to and more impacted by such international developments and at the same time benefit from an economically integrated world, and are disproportionately negatively affected by international barriers. It is not only a technical dialogue to come up with solutions to these challenges, but a diplomatic dialogue is also necessary within the global institutions and global policy frameworks that are being developed.

A global dialogue is in the making, and small states are not to be left behind. Diplomatic intervention is an important tool available to small states which can improve their global competitiveness. While small states have fewer resources to devote to the tasks of diplomacy and effective interaction with other states, this shortcoming can be compensated by their large number and common interests through the formation of alliances and networks. Although it may appear that small states have failed to form alliances and networks, progress has in fact been made as shown with the Small States Forum in improving access to development finance and de-risking in small states, and the Commonwealth Secretariat with increasing international trade and developing a new competitiveness measure for small states. This progress has been made with different degrees of success or not the level of success anticipated, which makes the point that more could be done.

The fact remains that there is limited space in the global negotiating agenda for the issues that small states represent. Small states in Europe are strategically placed to bring these issues forward at the regional EU level and through the EU at the international level, and to recalibrate its approach to regional and international diplomacy in its quest to promote competitiveness, and sustain growth and equity in its development goals. As such, it can bring important lessons to the attention of other small nations in the world and add considerably to the expectations of this exercise in global analytical leadership.

## **Disclaimer**

The authors declare that this article did not benefit from research funding.

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To cite this article:

Dookeran, W. & Mohan, P. S. (2019). Small state diplomacy and global competitiveness. *Small States & Territories*, 2(1), 69-82.