

VII Conclusion

The message of this report is robust and stark. For micro and very small economies, the competitive challenges are huge. These economies will not be suitable locations for industry or even tourism unless they have very specific advantages that allow them to charge higher prices than the median country. For hotels and tourism the attractions of small tropical islands are plausible and we do, indeed, see viable tourist industries on them. Our results merely indicate that they will need to manage costs carefully and will never achieve mass market penetration.

For manufacturing, on the other hand, the barriers look very high indeed, and if we expect such industries to develop, the international community will have to provide compensating advantages. Merely subsidising capital will not be sufficient – there are too many other disadvantages. One superficially promising route is via some sort of preferences for small countries' exports, allowing them to sell at tariff-inclusive prices in industrial country markets rather than world prices. But as these markets are liberalised the benefits of preferences erode and very small economies will face large income penalties. A second route could be to subsidise small country trade explicitly – either their exports or their imports or both. This would require conscious policy-shifts in the major capitals and also derogations from the WTO, but the cost of subsidies and their consequences for other nations would be limited by the smallness of the recipients' economies. A third route would be straight income transfers, which again would be small.

Explicit subsidies to micro and very small economies raise their own challenges. Specifically, many of the cost disadvantages we have identified must also apply to insular or isolated parts of larger countries. These may be subsidised via regional policies now, but if small economies were permitted to have export subsidies, one would need to argue why this privilege should not be extended to parts of larger economies. The reason is not hard to formulate, but it may be uncomfortable: within a country, people can move out of uneconomic locations. Ultimately we must face the possibility that if the current preferences that small countries receive are eroded and we do not somehow support their incomes in other ways, many of their inhabitants may seek to migrate.