Policy brief

Sustaining development in Small Island Developing States

A reform agenda

Emily Wilkinson, Michelle Scobie, Courtney Lindsay, Jack Corbett, George Carter, Rachid Bouhia and Matthew Bishop

July 2021

Series

Resilient Islands

Key messages

Small Island Developing States (SIDS), or Large Ocean States as some prefer to be known, are at a critical juncture: they are reliant on reforms in global institutions that need to happen quickly.

SIDS have immense potential to innovate and adapt to global conditions, but they are highly vulnerable to climate change impacts and other external shocks and face significant structural challenges in managing these risks.

Younger generations of SIDS citizens face the triple jeopardy of crippling debt, a degraded natural environment and frequent, devastating disasters.

SIDS have a high need for climate finance – particularly for adaptation and resilience – but they often have the weakest capacity to access it and are far from obtaining the volumes they need.

UN Member States have acknowledged that the SIDS are a special case for sustainable development, but this needs to translate into greater support and coordination of climate and development cooperation.

Reforms are needed across development assistance, debt and climate finance, using common definitions and criteria for eligibility and towards the common goals of honouring commitments made under the Paris Agreement and SAMOA Pathway and to improving aid effectiveness.

Acknowledgements

The authors would like to thank Rebecca Nadin, Annalisa Prizzon and Wassim Dbouk for reviewing this policy brief, as well as participants in the expert roundtable 'Small Island Developing States (SIDS): Are we reaching a viability tipping point?' (2 June 2021), who commented on the working paper that is the basis of the policy brief.

About the authors

ORCID numbers are given where available. Please click on the ID icon next to an authors' name in order to access their ORCID listing.

Emily Wilkinson is a Senior Research Fellow in the ODI Global Risks and Resilience Programme and Chief Scientific Adviser to the Climate Resilience Agency for Dominica (CREAD).

Michelle Scobie[ID] is a lecturer and researcher at the Institute of International Relations at the University of the West Indies, St. Augustine.

Courtney Lindsay is a project development consultant with the Inter-American Development Bank.

Jack Corbett[ID] is Professor of Politics at the University of Southampton.

George Carter is a Research Fellow in Geopolitics and Regionalism at the Department of Pacific Affairs at the Australian National University.

Rachid Bouhia is an economist in the United Nations Conference on Trade and Development.

Matthew Bishop[ID] is a senior lecturer in International Politics at the University of Sheffield.

How to cite: Wilkinson, E., Scobie, M., Lindsay, C., Corbett, J., Carter, G., Bouhia, R. and Bishop, M. (2021) *Sustaining development in Small Island Developing States: a reform agenda*. Policy brief. London: ODI (www.odi.org/en/sustaining-development-in-small-island-developing-states).

Sustainable development constraints in SIDS

Small Island Developing States (SIDS) have faced pivotal moments when policy agendas have undergone a marked shift in emphasis and direction – for example, the loss of trade preferences for exports to Europe under the Lomé Convention (Girvan, 2010; Heron, 2011; 2013). The confluence of increased attention being paid to climate change adaptation at the 26th UN Climate Change Conference of the Parties (COP26) in Glasgow, post-Covid-19 'green' recovery and debt restructuring, and shifting donor agendas (notably in the United States and United Kingdom) may well constitute one of these pivotal moments.

UN Member States have affirmed that SIDS are 'a special case for sustainable development' due to their unique characteristics and needs. But for this designation to have meaning, significant reforms are needed to avoid debt defaults and deterioration in income levels and living standards in SIDS due to the devastating impacts of the pandemic, environmental degradation and extreme weather events. SIDS urgently need financial support to transform their economies and strengthen their resilience to future shocks. These reforms need to be undertaken simultaneously to avoid siloed approaches and with a view to addressing the long-term structural vulnerabilities and challenges that many SIDS face in managing risks.

SIDS have long pursued unconventional economic development strategies, often with great success. Equally, because of their pronounced susceptibility to exogenous shocks, their progress remains fragile and can be set back suddenly and dramatically. Nonetheless, this vulnerability–resilience framing, which has commonly been used to analyse SIDS, has focused too much on intervening variables – exogenous shocks and endogenous capacity to mitigate them. In doing so it misses the wider enabling environment on which the relative economic success of these countries has been based: namely a geopolitical context in which interstate conflict has been rare, borders porous, openness and interconnectedness prized, and the natural environment relatively well preserved. This context has provided stability and opportunities for SIDS to identify and exploit niches (Bishop et al., forthcoming). The immediate post-independence era was one in which aid, trade preferences and relatively open migration schemes underpinned agricultural commodity exports and labour mobility (Heron, 2013). This gave way to a neoliberal era typified by distinct niche strategies associated with globalisation (Payne and Sutton, 2007), during which SIDS were able to sustain relatively high levels of growth compared to other developing regions by harnessing financial services, unlocking the potential of global tourism and tapping into large inflows of remittances.

We are now entering a new era characterised by global economic upheaval (wrought by the 2008–2011 global financial crisis and the Covid-19 pandemic) and greater external surveillance of offshore finance, the secondary impacts of the pandemic, cracks in the multilateral system, rapidly degrading natural environments and accelerating climate change.

This represents a turning point for SIDS. As the global context changes, so too does their ability to achieve genuinely sustainable development – that is, development which is socially and ecologically viable and sustained and enduring over time. Successfully exploiting new economic niches as they emerge to achieve new development goals via innovation and entrepreneurialism – such as the new opportunities presented by the blue economy – will be crucial in generating development that is both sustainable and sustained.

But this is not dependent simply on judicious national policy and action: the global context is crucial too. Just as traditional avenues for national development shrink and the challenges deepen, there may be a window of opportunity for SIDS to shift global priorities as donors and international organisations seek to make good on the international community's pledge, articulated in the 'Small Island Developing States Accelerated Modalities of Action – SAMOA Pathway,' to treat these states as a special case for sustainable development (UNGA, 2014).

This policy brief outlines three intersecting routes to creating more favourable conditions for SIDS' climate resilience and sustainable development:

- revisiting eligibility criteria and improving access to official development assistance (ODA)
- a fairer share of – and improved access to – climate finance
- more debt relief and long-term debt restructuring.

Coordinated reforms across these three agendas could help redress some of the challenges faced by SIDS in a changing geopolitical context and a warming world.

Revisiting eligibility for concessional finance

SIDS encounter a number of difficulties in accessing the development assistance that they need. Most SIDS are middle-income countries (MICs) and many are not eligible to receive concessional finance from multilateral financial institutions. While the World Bank (2019) has extended special treatment to small states in terms of access, financing volumes and concessionality, the evidence suggests that as countries approach or join the MIC group, donor governments scale down their development cooperation programmes (Jalles d'Orey and Prizzon, 2019).

Some SIDS are high-income countries (HICs) and therefore ineligible for ODA (after three consecutive years of being a HIC, countries are removed from the list of ODA-eligible countries). Many more SIDS will graduate in the coming years – including Antigua and Barbuda, Palau, and Panama, which will graduate in January 2022 instead of 2021 as expected because of the Covid-19 crisis (Prizzon and Pudussery, 2020).

It has long been argued, however, that gross national income (GNI) per capita is a poor or even deeply misleading measure of developmental progress in SIDS (Bishop and Murray-Evans, 2020). This is for the following reasons:

- Dividing the sum of national income among a small population inherently overstates living standards in the community.
- Taking a snapshot in time tells us little about changes in growth rates (many SIDS have suffered real-term stagnation for decades).
- GNI per capita tells us little about the distribution of income levels (most SIDS are extremely unequal, with small elites capturing most gains).
- SIDS are generally dependent on external finance and enclave forms of development, such as tourism or offshore finance, so rents often accrue to outside actors (Bishop, 2013).

Recent studies suggest that SIDS' graduation from the Least Developed Country (LDC) category happens through a combination of limited diversification towards services, in particular tourism, and investment in human capital (Quak, 2019). This concentration on a few service sectors heightens vulnerability to external shocks. Added to this, as SIDS transition, private capital flows – such as foreign direct investment and remittances – do not increase as fast as for other countries, and levels of debt increase. This makes it increasingly difficult for SIDS to make the capital investments necessary to buttress themselves against climate change impacts.

SIDS at all levels of per capita income will require substantial external assistance to adapt to climate change.[1] Meanwhile, signatories of the Paris Agreement have committed to looking at all financial flows (public and private, domestic and international) and ensuring that these support a transition to a low-greenhouse gas emissions, climate-resilient world.[2] ODA allocations to SIDS are thus not only an issue of development effectiveness and financial stability but also fulfil a global commitment to help climate-vulnerable states transform their economies and strengthen their resilience.

The Multidimensional Vulnerability Index (MVI) being developed for SIDS by the United Nations offers great potential for developing additional (or exceptional) eligibility criteria for

1 At present, SIDS receive very small amounts of external financial assistance relative to their needs. The Organisation for Economic Co-operation and Development (OECD) estimates that Total Official Support for Sustainable Development to all SIDS in 2017, which includes ODA, concessional and non-concessional finance, amounted to $4.1 billion (OECD, 2020a).

2 Article 2.1c of the Paris Agreement (2015).

concessional finance that align with commitments under the Paris Agreement. The MVI could be used to improve resource allocation across all international financial institutions and help SIDS that graduate in the future to access concessional finance. This would support a transition to more sustained models of development in SIDS in combination with increased climate finance and debt reduction.

In parallel to discussions about eligibility criteria, development partners also need to create more systematic and longer-term approaches to strengthening national capacities and overcoming absorptive constraints (Quak, 2019). High transaction costs are a structural problem for small administrations and are not easily avoided (Corbett and Veenendaal, 2019). There are, however, forms of assistance, such as budget support and long-term capacity development programmes, that can help ensure that it does not prevent SIDS from accessing and absorbing external finance for resilient development programmes. These types of development assistance should become more prominent in the sector and should focus on the needs of SIDS.

Improving access to climate finance

SIDS have some of the highest needs for climate finance – particularly for adaptation and resilience – but they often have the weakest capacity to access it (Robinson, 2019) and are far from obtaining the volumes they need. This is even though scientific reports (IPCC, 2019) and the United Nations Framework Convention on Climate Change (UNFCCC) recognise the particular vulnerability to climate change of low-lying coastal, arid and semi-arid areas or areas with fragile mountainous ecosystems (UNFCCC, 1992). Article 9.4 of the Paris Agreement states that SIDS and LDCs are particularly vulnerable to the adverse effects of climate change and therefore need public and grant-based resources for adaptation because of their significant capacity constraints (UNFCCC, 2015).

Responding to this vulnerability, the Green Climate Fund (GCF), which was established within the framework of the UNFCCC, committed to prioritising SIDS and LDCs in adaptation efforts and providing 50% of its funding to adaptation, of which half is to be spent in LDCs, SIDS and African states (GCF, 2020).

However, developed countries' commitment to scaling up their climate finance to at least US$100 billion per year by 2020 has not been met. In addition, most public climate finance is provided in the form of loans and other non-grant instruments: in the period 2017–2018, around half of climate finance to SIDS was non-concessional (a higher proportion than for public climate finance overall – at 40%) (Oxfam, 2020).

A new climate finance goal, which is on the agenda for COP26, will need to be quite different from its predecessor in both content and complexity. Unlike development or humanitarian finance, climate finance is based on an explicit historical responsibility for climate change, in addition to a moral imperative to support those most severely affected. Yet, to meet the targets in the Paris Agreement, climate finance must also be used effectively to drive the transition to low-carbon, climate-resilient economies and societies. This is especially important for SIDS, and in particular for those islands whose very existence depends on this transition.

Now is the time for a robust debate on appropriate levels of concessionality for climate finance – particularly for adaptation – and what a 'fair share' of climate finance should be for SIDS given their high vulnerability to climate change impacts and low contribution to global warming. SIDS have been acknowledged as a special case for sustainable development, so should there be a climate finance goal for SIDS to help realise this?

Reducing the debt burden

The collapse in tourism revenues and the economic slowdown caused by Covid-19 have aggravated the debt positions of SIDS, putting them at greater risk of defaulting. But these debt problems have deeper roots than the recent crisis. Even before the pandemic, in 2019 external debt in 2019 accounted for 62% of gross domestic product on average in SIDS, compared with 29% for all developing countries and economies in transition (UNCTAD, 2020). Large-scale borrowing from public and private foreign creditors, particularly after disasters, has narrowed these countries' fiscal space, limiting their options to invest in adaptation and resilience (Bouhia and Wilkinson, 2021).

All SIDS except Antigua and Barbuda have since 2020 benefited from the International Monetary Fund's Covid-19 Financial Assistance and Debt Service Relief, and 13 SIDS have benefited from the G20 Covid-19 Debt Service Suspension Initiative (DSSI) (World Bank, 2021), but official support is needed to address the short- and longer-term debt problem in SIDS.

First, SIDS need to be given more 'breathing space'. Given the looming debt crisis, more comprehensive measures are needed – and fast. In particular, the G20 DSSI eligibility criteria should be extended so that SIDS with relatively high per capita income levels can also benefit from 'debt standstills' (OECD, 2020b). The DSSI also needs to cover all creditors (OECD, 2021) – bilateral, private and multilateral. Given the alarming levels of debt distress in SIDS, private creditors should be encouraged to join temporary debt repayment suspension programmes (Prizzon et al., 2021) to allow time for economic recovery and avert huge financial losses in the future (should the country default or require debt restructuring).

Second, an urgent assessment of the long-term debt sustainability of SIDS is due. Debt repayment needs to be compatible with restoring and maintaining sustainable and inclusive growth beyond the Covid-19 crisis, as well as balanced fiscal and trade trajectories. SIDS need to be able to invest to build the resilience of their economies to climate change and other external shocks. Some type of debt relief or restructuring initiative that goes beyond a temporary standstill is therefore needed (Humphrey and Mustapha, 2020).

One option being considered by SIDS' governments as a solution for heavy indebtedness is swapping debt for climate change adaptation and mitigation measures. So-called 'debt-for-climate swaps' offer debt forgiveness to countries that commit to funding conservation and natural resource management, resilience and renewable energy projects. These need to be applied at scale – and without the kind of conditionalities that hinder countries' own climate change agendas. Implementation may be challenging, involving time-consuming negotiations and extensive monitoring of funds.

Conclusions

SIDS are at a critical juncture in their relatively short post-independence histories, and reliant on urgently needed reforms in global institutions. Building resilience to climate change and other shocks means tackling both debt and climate crises simultaneously. This will allow SIDS to use different sources of external finance to invest in resilience, diversify their economies and develop skills and capacities so they can be flexible in responding to climate change impacts and other shocks in the future.

SIDS have immense potential, but they also face significant structural challenges in managing risks because of their size, openness and other factors. They have successfully pursued niche development opportunities in service sectors such as tourism, which has generated income but resulted in environmental degradation and increased exposure to natural hazards, high levels of debt when disasters occur (due to lack of diversification) and limited options for reducing that debt.

This presents a triple jeopardy for young people in SIDS, who will inherit crippling debt, a degraded environment, and frequent and destructive disasters. There is a historical and moral obligation for development partners to help SIDS overcome the structural challenges that they face – even if these cannot actually be removed.

The SAMOA Pathway adopted by the UN on 14 November 2014 acknowledges the SIDS' special case for sustainable development, but this needs to translate into greater support and improved coordination of climate and development cooperation. Reforms are needed across development assistance, debt and climate finance, using common definitions and criteria for eligibility and towards common goals of honouring commitments under the Paris Agreement and SAMOA Pathway and improving aid effectiveness.

References

Bishop, M.L. (2013) *The political economy of Caribbean development*. London: Palgrave.

Bishop, M.L., Bouhia, R. and Carter, G. et al (forthcoming) *Towards sustained development in small islands: why we need to reshape the global governance architecture to support long-term post-pandemic recovery and solutions to the climate crisis in SIDS*. London: ODI.

Bishop, M.L. and Murray-Evans, P. (2020) 'Five little B(R)ICS: huffing and puffing, but not blowing your house in' *New Political Economy* 25(5): 691–702.

Bouhia, B. and Wilkinson, E. (2021) 'Small-Island Developing States need urgent support to avoid debt defaults' 30 March, ODI (https://odi.org/en/insights/small-island-developing-states-need-urgent-support-to-avoid-debt-defaults).

Corbett, J. and Veenendaal, W. (2019) 'Why small states are beautiful' *Political Insight* 10(1): 4–8.

GCF – Green Climate Fund (2020) 'Climate action during the pandemic. Green Climate Fund Annual Results Report' (www.greenclimate.fund/sites/default/files/page/gcf-annual-results-report-2020_0.pdf).

Girvan, N. (2010) 'Technification, sweetification, treatyfication: the politics of the Caribbean-EU Economic Partnership Agreement' *Interventions: International Journal of Postcolonial Studies* 12(1): 100–111.

Heron, T. (2011) 'Asymmetric bargaining and development trade-offs in the CARIFORUM-European Union Economic Partnership' *Review of International Political Economy* 18(3): 328–357 (https://doi.org/10.1080/09692290.2010.481916).

Heron, T. (2013) *Pathways from preferential trade: the politics of trade adjustment in Africa, the Caribbean and Pacific*. London: Palgrave.

Humphrey, C. and Mustapha, S. (2020) *Lend or suspend? Maximising the impact of multilateral bank financing in the Covid-19 crisis*. ODI Working Paper 585. London: ODI (https://cdn.odi.org/media/documents/Lend_or_suspend_Maximising_the_impact_of_multilateral_bank_financing_in_the_Covid.pdf).

IPCC – Intergovernmental Panel on Climate Change (2019) 'Summary for policymakers' in H.-O. Pörtner, D.C. Roberts, V. Masson-Delmotte et al. (eds) *IPCC Special Report on the Ocean and Cryosphere in a Changing Climate*. Intergovernmental Panel on Climate Change.

Jalles d'Orey, M.A. and Prizzon, A. (2019) *Exit from aid: an analysis of donor experiences*. London: ODI (www.odi.org/publications/11297-exit-aid-analysis-donor-experiences).

OECD – Organisation for Economic Co-operation and Development (2020a) *External financing to Small Island Developing States (SIDS): where we stand*. OECD Factsheet.

OECD (2020b) *Policy responses to Coronavirus (COVID-19): a "debt standstill" for the poorest countries: How much is at stake?* Paris: OECD (www.oecd.org/coronavirus/policy-responses/a-debt-standstill-for-the-poorest-countries-how-much-is-at-stake-462eabd8).

OECD (2021) COVID 19: Debt Service Suspension Initiative (www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative).

Oxfam (2020) *Climate finance shadow report 2020: assessing progress towards the $100 billion commitment*. Oxford: Oxfam.

Payne, A. and Sutton, P. (2007) *Repositioning the Caribbean within globalisation*. CIGI Caribbean Paper No. 1. Ontario: Centre for International Governance Innovation (www.cigionline.org/sites/default/files/1._repositioning_the_caribbean_within_globalisation.pdf).

Prizzon A. and Pudussery, J. (2020) *From aid to development partnerships: lessons from the literature and implications of the Covid-19 crisis*. London: ODI (https://cdn.odi.org/media/documents/Aid_final2.pdf).

Prizzon, A., Mustapha, S. and Steel, I. (2021) 'Four priorities for the G20 meeting of finance ministers and central bank governors' 1 July, ODI (https://odi.org/en/insights/four-priorities-for-the-g20-meeting-of-finance-ministers-and-central-bank-governors).

Robinson, S-A. (2019) 'Mainstreaming climate change adaptation in small island developing states' *Climate and Development* 11(1): 47–59.

Quak, E.-J (2019) *How losing access to concessional finance affects Small Island Developing States (SIDS)*. K4D Helpdesk Report, DFID.

UNCTAD – United Nations Conference on Trade and Development (2020) *External debt sustainability and development. Report of the Secretary-General*. United Nations General Assembly. Seventy-fifth session. July 2020. Geneva: UNCTAD.

UNFCCC – United Nations Framework Convention on Climate Change (1992) United Nations Framework Convention on Climate Change. Geneva: UNFCCC (https://unfccc.int/files/essential_background/background_publications_htmlpdf/application/pdf/conveng.pdf).

UNFCCC (2015) Paris Agreement to the United Nations Framework Convention on Climate Change. Geneva: UNFCCC (https://unfccc.int/sites/default/files/english_paris_agreement.pdf).

UNGA – United Nations General Assembly (2014) A/RES/69/15 Resolution adopted on 14 November 2014.

World Bank (2019) *World Bank Group support to small states*. Washington DC: World Bank (https://thedocs.worldbank.org/en/doc/340031539197519098-0290022019/original/WorldBankSupporttoSmallStatesbooklet.pdf).

World Bank (2021) 'COVID 19: Debt Service Suspension Initiative' 18 June, World Bank brief (www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative).