COVID-19 Makes the Case for Our Trade Vulnerability Index

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"We are concerned about the impact of COVID-19 on vulnerable developing and least developed countries, and notably in Africa and small island states. We are also concerned about the daunting challenges facing workers and businesses, particularly the most vulnerable ones. We will ensure our collective response is supportive of micro, small and medium-sized enterprises, and recognize the importance of strengthening international investment."

G20 Trade Investment Ministerial Statement, March 30, 2020

"We need global leadership similar to what we had post-World War II … a plan that protects not just the strongest among us, but also the most vulnerable … The [Commonwealth Secretariat's] vulnerability index has, in fact, settled on a framework since 30 years ago… We believe it needs to be revisited".

Prime Minister of Barbados, Hon. Mia Amor Mottley, in interview with CNN international journalist Christiane Amanpour, April 29, 2020

Introduction

Recent global events are making us all feel vulnerable. Plunging oil prices, upended global trade and disrupted international supply chains all contribute to the general sense of trepidation and uncertainty. Economists at the World Trade Organization (WTO) predict that the trade slump precipitated by COVID-19 will be deeper than the global financial crisis of 2008-2009. As wealthy and poor countries alike strive to "keep their heads above water", the strain is being felt most by those with limited health infrastructure, high levels of poverty, limited fiscal space and access to credit. Amidst this shared experience of COVID-19 madness, what are we to make of claims that some are "more" vulnerable than others, and why should the world care?

Vulnerability has been the subject of international trade literature in the past and more recently, a research project by the present authors working under the auspices of the Shridath Ramphal Centre (SRC) of the University of the West Indies. Specifically, the authors have constructed a framework – the SRC Trade Vulnerability Index (TVI) – that aims to detect, measure and ultimately quantify the degree of trade vulnerability of countries. The global health pandemic of COVID-19 gives credibility to – and ultimately validates – the relationship we have explored between vulnerability and trade using our TVI. It also justifies and directs a response by the international community to COVID-19 that prioritizes the allocation of global resources to the most vulnerable.

The SRC Trade Vulnerability Index in a Nutshell

We first proposed the TVI as an objective basis for guiding country eligibility for preferential treatment – Special and Differential Treatment (S&DT) – at the WTO. It was developed to steer the focus away from income-based criteria for assessing development – like GDP- or GNI-per capita – as recently proposed, for instance, by the United States at the WTO, to structural characteristics of an economy which can impact its development outcomes. The original United States proposal of February 15, 2019 has since been slightly revised, with the latest revision being November 25, 2019. Country vulnerability could be measured based on a composite index score relative to a threshold, rather than simply on income, which is not a complete measure of a country's level of development.

We wanted a framework that could provide a sense of a country's coping capacity (not only in times of crisis) but which also pointed to the kind of assistance necessary to more seamlessly integrate vulnerable countries into the international trading system. After careful review of the literature on economic vulnerability and international trade, the authors developed a set of "proxy indicators" relating to structural, environmental and institutional vulnerabilities. These "proxy indicators" were: export concentration, concentration of export destination, trade openness, susceptibility to trade shocks, dependence on strategic imports like food and fuel, reliance on external finance, market share of global trade, remoteness, limited economic diversification, small size, susceptibility to natural hazards and climate change, market inflexibility and weak political, social and environmental governance. The proxy indicators were indicative and not verified for significance with econometric or statistical approaches. They were also grouped according to, and mapped against, current types of World Trade Organization Special and Differential Treatment, (S&DT), provisions so that it could be used as a practical tool to guide decision making and negotiations related to eligibility for S&DT in the WTO context.

While the TVI contemplates that the majority of countries which fall under the "vulnerable" category would be small economies, unlike the United States' proposal, it is not preclusive and captures a variety of new features of vulnerability that are more closely linked to the trade capabilities of countries. Moreover, itis sufficiently malleable to be used in a sector- or agreement-specific way; on a stand-alone basis; or together with other criteria such as per capita income.

COVID-19 Exposes Caribbean Vulnerability

While extraordinarily beautiful, the Caribbean region is comprised of economies that are small, debt-ridden, export dependent, disaster prone, and reliant on external finance. With these characteristics, it is little surprise that COVID-19 has further exposed the Caribbean’s vulnerability. Further, what it has also made patently obvious is the *degree* of that vulnerability.

We have just begun to empirically assess the possible impact of COVID-19 on the economies of the Caribbean region. Take, for example, the TVI proxies of export concentration and limited diversification. For the majority of islands, tourism is the main economic activity, representing approximately 45 per cent of GDP, contributing an average of 29,208 persons to employment (per island); and serving as a major source of foreign exchange with the main tourism source markets being the United States, United Kingdom and Canada.

The tourism sector arguably will be one of the hardest hit by COVID-19, with spillover effects into other sectors including the wholesale and retail, real estate, agriculture, construction and transportation sectors. Tourism will experience a sharp economic decline due to closed borders, grounded flights, interrupted cruises, shut hotels and other accommodations, supply disruptions and social distancing and state of emergency measures (domestically and abroad). Instead of a V-shaped recovery by 2021, experts are saying it will be more W-shaped one, that is still dependent on recovery of consumer confidence to travel.

Take another proxy: dependence on strategic imports. For many years, leaders of the Caribbean Community (CARICOM) have lamented the region’s increasing dependence on critical imports such as food, fuel, machinery and transport and other manufactured goods. With COVID-19, this dependence has become debilitating with the region scrambling to ensure that its access to critical produce, health related goods and equipment such as personal protective equipment, medical supplies and ventilators is secured.

The COVID-19 pandemic has served as a stark reminder of our susceptibility to disasters and exogenous shocks. While not a “natural” disaster to which the region has become accustomed, COVID-19 is just as incapacitating in terms of its economic impact. Conservative economic growth projections suggest that most of the Caribbean’s economies will experience single-digit economic declines in 2020. However, the trend towards more protracted “lock-downs” and significant unemployment fall-off due to closed businesses may point towards double-digit economic contractions in these island economies. To shore-up economic activity and provide some social support to its citizenry, governments across the region have implemented fiscal stimulus packages ranging from between 1 to 4% of GDP. While this will provide some easement, it will also contribute to the heavy debt burden in one of the most highly indebted regions of the world. Moreover, its compounding effect in the Caribbean is real since these islands are already feeling the adverse impacts of climate change, including more frequent droughts and increasingly ferocious weather systems. With the hurricane season quickly approaching, concerns are heightening, but hopefully we will be spared another natural disaster onslaught this year.

The Lessons to Learn About Vulnerability

As it unravels, the pandemic is teaching us as much about our Trade Vulnerability Index as about the concept of vulnerability itself.

While, admittedly, a health crisis of the magnitude of COVID-19 was not contemplated when the TVI framework was conceptualized, it can certainly be accommodated within the existing proxies and has deepened our understanding of them. It has validated our belief that inherent characteristics of certain countries, like those of the Caribbean, predispose them to less favourable outcomes in severe crises like this one: high concentration of exports (and particularly tourism services); high dependence on other nations for their imports of food, fuel and medical equipment and services; a small proportion of global trade and as such may not be prioritized given scarcity of supply; deep fiscal constraints and limited access to capital markets – which is often connected with weak governance and institutions; heavy reliance on external trade and foreign investment to overcome their inherent resource limitations; market rigidities which can restrict the economy’s ability to recover after being affected by the shock and have higher levels of poverty and inequality. All of these characteristics are reflected in the proposed “proxy indicators” of the TVI - and COVID-19 gives added legitimacy to it.

But beyond just inputs for our Index, COVID-19 allows us to reflect on the very concept of vulnerability, as a more human and lived experience. First, it shows that the potential causes of vulnerability are not static. Health pandemics, like climate change, which now feature prominently in discussions, were hardly, if at all, on global radars 15-20 years ago. Although they operate in different realms and at different paces, both COVID-19 and climate change are equally halting in their global impact and reach and demonstrate that in an increasingly global world. Secondly, the globalization and interconnectedness of the world in economic, social and environmental dimensions demonstrates how – to varying degrees – we are all vulnerable to each other. Thirdly, the pandemic has broadened our understanding of who the vulnerable people are which should preoccupy the world's attention. While we typically understand this group to comprise women, children, the elderly, disabled, the poor, marginalized and displaced, we may now include as well those without health care or health insurance, and those facing job losses and economic hardship which could result in mortgage and rental arrears and evictions.

Conclusion

The opening quote taken from the G20 Ministerial Statement is a welcome acknowledgment by the most powerful that some countries and citizens lay greater claim to the title of "vulnerable" than others. However, it is not enough. Prime Minister Mottley's clarion call for global leadership in this area and application of the vulnerability index is one we have wholeheartedly embraced. Through our TVI, we are proposing tangible and effective ways to cater to the patent vulnerabilities of countries in regions like the Caribbean and Africa. While some answers undoubtedly lie in our own hands – regional solutions, redirecting supply to domestic markets, diversification into higher value-added exports, and strengthened logistics – many more hinge on the willingness of the international community to do more. The TVI can help provide a sound and evidential basis for decisions taken by international institutions to allocate limited resources to the most vulnerable.

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