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## *What explains the success of small developed countries over the past several decades?*

Small advanced economies – developed countries with populations of less than 20 million people – have performed well over the past few decades. In general, these small countries have generated strong economic and social outcomes, and are actively engaged in the global economy. So what is the secret of their success? A few factors are often referenced.

First, the global economic and political environment over the past several decades has provided a supportive environment for small countries; globalisation, relatively strong and stable global growth, and a generally favourable security environment. However, this is better seen as the removal of a disadvantage to small size than as conferring an advantage on small countries. It has been helpful, as Singapore's economic history shows, and perhaps necessary, but it is not the full answer.

Superior policy settings are a second possible explanation. Many small countries – including Singapore – have well-deserved reputations for the quality of their policies. But my analysis suggests few systematic policy differences between large and small advanced economies. There are some; small countries tend to have smaller fiscal deficits and current account deficits, and higher government spending, for example. But in general policies in large and small developed countries are more similar than different.

A recent World Bank publication [*'Some Small Countries Do It Better'*] that examined the outstanding performance of Singapore, Finland and Ireland, emphasised the centrality of

education in explaining their success. It is hard to argue with this. These three small countries have invested heavily into their education systems. But not all successful small countries are world-leaders in education, and there are larger countries – like South Korea – that invest heavily in education.

In general, it is difficult to explain the strong performance of small countries – or variation in performance among small countries – by looking to policy specifics. If anything, small countries have slightly inferior policy settings on a range of standard measures. And policy settings vary significantly across small countries; Singapore, Denmark and Switzerland have quite different economic and social policy approaches.

But although the policy specifics vary, small countries tend to share a much more deliberate, strategic approach to policy that is focused on competing in the global economy. Small countries choose to compete in different ways, but it is the deliberately adaptation of policy to a changing external environment that is distinctive of small countries – and this has been a key driver of strong small country performance.

This finding points to the importance of a third explanatory factor: the contribution of politics, governance, and institutions to small country success. Small countries tend to have high levels of social capital and trust, well-functioning political institutions, and a well-developed sense of external orientation. These factors make it easier to sustain a deliberate strategy and to change course when appropriate. This combination of shared purpose and agility

supports the design and delivery of policy agendas that have positioned many small countries to perform well.

In short, it is the quality of collective decision-making that is critical to small country success. And variation in the quality of decision-making institutions is closely linked to variation in small country performance. Small countries that have strong institutions and capacity have done well (Singapore, the Nordics), because these governments are better able to respond appropriately to the changing global environment. In contrast, countries that lack these assets have done much less well (Greece). The World Bank analysis of Singapore, Finland and Ireland also notes the importance of a “durable political consensus...around a long-term growth strategy”.

The small country advantage is sometimes linked to speed and agility. But the advantage is better seen as decision-making based on a shared understanding of the strategic environment and a sense of shared purpose. This enables small countries to make long-term decisions as well as to respond quickly in terms of crisis – things that larger countries sometimes struggle to deliver.

So although small countries have clearly benefited from a supportive external environment, the more important success factor is the strong collective decision-making capacity common in small countries. This capacity has enabled them to respond to a changing global environment. The strong performance of small countries is largely a matter of deliberate choice and management.

But small countries need to avoid complacency. The external environment is likely to become

more challenging for small countries; increased competitive intensity, a more turbulent economic and political environment, and weakening multilateral institutions. Sustaining performance in this environment will demand a deliberate policy response. And the ability to do so will rest importantly on the effectiveness and capacity of collective decision-making institutions.

There are two related priorities for action in this regard. First, small country governments will need to invest in strategic policy capacity, to understand their exposures to a changing global context and to determine how to adapt policy settings. In a changing world, policy changes will inevitably be required, and the quality of decision-making will be a key determinant of national performance.

And second, small country governments will need to work hard to sustain the social consensus around the chosen strategic policy direction. Without a common understanding of the context and a sense of shared purpose, it will be more difficult to sustain a medium-term policy direction or to respond flexibly when needed. Policy choices clearly matter, but so too does politics.

Globalisation and open markets have benefited small countries significantly. But it is the quality of government that has shaped the extent to which small countries have reaped the benefits and managed the risks of this process. And investing in public sector capacity – the ability of countries to make sound collective decisions – will become even more important over the next decade.

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