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Economic Populism: End of The Small State?

By Joel Ng

Synopsis

If the 'belle époque' of the small state is over, then the world is in for some dangerous times. Middle-sized and aspiring powers should be concerned about what this entails, but small states still have something to offer.

Commentary

A RECENT [commentary in the Financial Times](#) laid out a foreboding case that the era for small states was coming to an end. In particular it added “the conditions that allowed small nations to bloom look precarious. There is a protectionist fad that should haunt these trade-dependent economies like nothing else”. If this is true, then it is not only small states that are in trouble, but the entire world.

Much of the visible troubles relate to the expanding trade war between the United States and China, in which a rules-based order may be the collateral damage. As the political commentator Janan Ganesh argues, “Rules-based globalism was a precious equaliser for [small states],” and this is under threat as the major powers attempt to impose new rules favourable to themselves. Donald Trump has clearly stated that he believes the US got a bad deal in the trading arrangements it has and wants deals that are more favourable to itself.

Danger of Bad Deals

This is a curious reversal of the same criticism anti-globalist movements in Europe and elsewhere had levelled against the US, in protesting the trade arrangements such as the Transatlantic Trade and Investment Partnership (TTIP) and Trans-Pacific Partnership (TPP) that the US had driven until Trump's election in 2016. These arrangements, the protestors argued, had given European or Asian countries a bad

deal with the US, which was allegedly imposing its rules to benefit its corporate interests.

Can both assertions be true, that both the US *and* its trading partners got bad deals from arrangements they made with each other? The sentiments certainly suggest it, but then it leaves a puzzle how both could feel victimised, leading to a zero-sum interpretation of trading regimes. David Ricardo's 200-year-old law of comparative advantage certainly expects someone to be benefiting from this free trade, but the benefits are not being felt by the masses from which populist forces have emerged.

From Trump to Brexit to resurgent populism in Europe, there is undeniably a latent discontent in many developed nations, in which simple solutions have been touted that appear to address it. While looking only at one side of an accounts balance such as a deficit leads to skewed interpretations of the problem at hand, it provides convenient political targets.

This leads to an incentive to view interests narrowly, relying on a simple understanding of the world that reflects these populist politicians' domestic support bases' narrow understanding of their problems.

This in turn leads to a temptation for nations to act unilaterally, carving out a space in which they can enforce rules preferential to themselves. In a globalised world, however, making that space increasingly requires stepping on someone else's toes. Moreover, setting rules that are discriminatory invites retaliation, which is precisely what we have observed in the escalating Chinese-US trade war.

Major Powers in History

History is replete with examples of major powers whose minor conflicts escalated into wars and left them smaller, less able to assert themselves beyond their borders. Indeed, Britain and France may have been among the "winners" of World War II, but the ensuing retreat from their empires within two decades of that victory was a direct result of the costly war that brought their economies to their knees, requiring decades to rebuild.

While they may have recast decolonisation as an act of benevolence, it was a matter of jumping or being pushed out as they lacked the capacity to control territories thousands of miles away, that were now agitating for self-determination.

Europe's multilateral system was created after World War II as a direct response to the problem of individual nations believing they could go it alone. While it is true that small nations suffered, the major powers were wracked by the conflict and lost their global ambitions as a result. Ordinarily, Europe would stand poised to benefit from a tussle between the US and China, but it has not yet resolved its own internal problems.

Small States Still Relevant

The multilateral system may be under the most significant threat it has faced since the collapse of the League of Nations. Too many politicians are looking abroad for scapegoats, but for all of them to be right about unfair deals, it suggests the answer

lies internally: That it is domestic distribution problems – that is, unequal access to the benefits of trade – that lies at the heart of their support base’s discontent with current international arrangements.

Looking for external targets will neither solve the problem nor address their supporters’ discontent, in which case the game will soon be up if their problems remain unaddressed.

It might seem in this return to the Great Game of power politics in the international system, that small states will go back to suffering what they must. However, there is still some hope: Small states will continue to be the strongest proponents of a multilateral order regardless of the whims of major powers. Middle-sized states and aspiring regional leaders should see it in their interests to also support and strengthen this system.

Small states’ success under ‘rules-based globalism’ was not only about their nimbleness and adaptability to prevailing conditions. As smaller economies, they had to get their domestic formula correct in bringing up the levels of well-being across the board for their citizens.

As microcosms of larger economies, they may yet offer a final ace-in-the-hole as a laboratory for larger countries looking for solutions to the problem of discontent in their much larger and more complex economies. Trampling them underfoot in the name of a zero-sum trade war would only undermine that opportunity for learning.

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