

Chapter 14

Economic management and state institutions

14.1 Careful and sound management of a country's financial affairs and business environment is central to its economic development. Good policy coupled with its effective implementation can maximise benefits to the economy by ensuring that opportunities for growth are fully exploited and the adverse effects of external shocks, such as natural disasters, are kept to a minimum.

14.2 In this chapter, the committee looks at the ability of both the bureaucracy and the policy makers in Pacific island countries to manage the economic and business affairs of their state. The committee looks at a number of key aspects to good government—its effectiveness in providing necessary services; managing a budget, including the collection and allocation of government revenue; and creating an environment conducive to enterprise and development.

Public administration and economic performance

14.3 Governance and the performance of state institutions is an important factor in economic growth.¹ A 2005 Joint Report to the Pacific Islands Forum Secretariat estimated that poor governance in PNG, Fiji, Solomon Islands, and Nauru 'had resulted in nearly US\$75 billion in forgone income in those countries since independence'.² It stated that human capacity constraint is 'becoming increasingly important as modern requirements of business and government become more complex'. It went further to indicate that faced with policy and capacity constraints, the governments of Pacific Island Forum countries experience difficulties meeting two essential sovereign functions:

- formulating and enforcing effective and appropriate national policies; and
- providing essential services.

14.4 As shown in the following table, recent statistics produced by the World Bank on matters of governance support these observations.

1 AusAID, *Pacific 2020: Challenges and opportunities for growth*, May 2006, p. 3. The World Bank defines governance as 'the traditions and institutions by which authority in a country is exercised. This includes the process by which governments are selected, monitored and replaced; the capacity of the government to effectively formulate and implement sound policies; and the respect of citizens and the state for the institutions that govern economic and social interactions among them', <http://info.worldbank.org/governance/wgi/index.asp>.

2 Asian Development Bank–Commonwealth Secretariat Joint Report to the Pacific Islands Forum Secretariat, *Toward a New Pacific Regionalism*, Pacific Studies Series, 2005, p. xiv.

Table 14.1: Aggregate governance indicators for selected Pacific island countries, 2005–2007³

Country	Voice and accountability			Political stability and absence of violence			Government effectiveness			Regulatory quality			Rule of law			Control of corruption		
	per cent rank			per cent rank			per cent rank			per cent rank			per cent rank			per cent rank		
Year	'05	'06	'07	'05	'06	'07	'05	'06	'07	'05	'06	'07	'05	'06	'07	'05	'06	'07
Cook Islands	..	..	..	..	..	..	68	56	44	69	68	55	88	84	67	71	73	83
Fiji	56	32	32	61	45	47	54	52	36	40	36	34	52	53	46	36	46	42
Kiribati	57	70	69	98	98	98	36	36	34	17	16	14	74	78	76	62	61	61
Nauru	78	80	81	87	88	88	38	9	35	..	..	23	71	80	62	..	..	50
PNG	43	50	52	24	23	23	15	22	25	19	24	30	16	20	21	14	13	9
Samoa	66	68	67	88	89	89	64	58	49	53	54	52	84	82	82	61	63	64
Solomon Islands	52	54	54	55	54	58	30	17	20	14	12	13	19	22	24	58	49	33
Tonga	46	47	46	71	64	59	36	29	32	24	22	23	64	66	64	6	5	13
Tuvalu	70	72	72	98	98	98	57	45	41	34	21	20	89	85	84	55	57	54
Vanuatu	60	67	60	98	98	98	45	40	45	55	52	33	64	64	68	64	62	63

14.5 These governance indicators are based on statistical compilation of responses on the quality of governance given by a large number of enterprises, citizen and expert survey respondents in industrial and developing countries. They show that, consistently, a number of Pacific island countries rate poorly on some performance indicators, notably government effectiveness, regulatory quality, rule of law and control of corruption. Again performance varies greatly between Pacific island countries, with Samoa outshining most other countries in the region. The Cook Islands and to a lesser extent Vanuatu also achieved solid rankings in these areas of governance compared with other Pacific island countries. PNG and Solomon Islands

3 Statistics are taken from the World Bank data base, *Aggregate Governance Indicators 1996–2007*, <http://info.worldbank.org/governance/wgi/index.asp> (accessed 2 December 2008) <http://info.worldbank.org/governance/wgi/pdf/wgidataset.xls>; (accessed 2 December 2008).

The authors advised users of the limitations of these measures of governance, 'which are shared by virtually all efforts to measure governance across countries and over time'. They stated, 'aggregate indicators we construct are useful for broad cross-country and over time comparisons of governance, but all such comparisons should take appropriate account of the margins of error associated with the governance estimates'.

lag well behind. The committee looks at these governance categories, starting with government effectiveness.

Capacity to deliver essential services

14.6 According to the researchers involved in compiling these statistics, government effectiveness measures the quality of public services, the quality of the civil service and the degree of its independence from political pressures. It also measures the quality of policy formulation and implementation and the credibility of the government's commitment to such policies.⁴ For 2007, most Pacific island countries registered below the 50th percentile for government effectiveness. In comparison, Australia scored 97, Japan 89 and New Zealand 96.

14.7 In its discussion on resources management, the committee highlighted some of the problems created by under-resourced and under-skilled bureaucracies. While it noted the potential for Pacific island countries to increase economic productivity through sustainable development, it also drew attention to governance and institutional gaps that undermine their ability to do so. This lack of capacity to manage and develop their resources extended to conservation, data gathering, reporting, monitoring and enforcement, administration, consultation, marketing, negotiation and quarantine matters. For example, it noted the prevalence of illegal or unreported activities in areas such as fishing and forestry.⁵

14.8 Such unauthorised activities, which often result in a loss to government revenue, are not confined to these two sectors. The Australia Papua New Guinea Business Council observed that a large number of illegal foreign workers were in PNG, many running small trade stores, and it seemed likely that some companies were operating without appropriate permits and licenses. It urged the Australian and PNG governments to ensure the Papua New Guinea Internal Revenue Commission was fully resourced to protect revenue collection.⁶

14.9 The failure of PNG to monitor the movement of goods and their carriers effectively also creates the potential for loss of revenue. Ms Wimmer, Australian Customs Service, said that Australian Customs had been 'trying to get the relevant agencies in Papua New Guinea to work together to do patrols of the border, with assistance from Australia'. She cited an example where one of those [maritime border]

4 Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, *Governance Matters VI: Aggregate and Individual Governance Indicators 1996–2006*, World Bank Policy Research Paper 4280, July 2007, pp. 3–4.

5 See paragraphs 4.26–4.36; 5.14–5.27; 5.37. Also see, Andreas Schloenhardt, *The illegal trade in timber and timber products in the Asia-Pacific region*, Research and Public Policy Series, No. 89, Australian Institute of Criminology, 2008, p. 75. An IMF mission to Solomon Islands found anecdotal evidence indicating that only 30–40 per cent of log shipments in Solomon Islands are inspected, resulting in foregone tax revenues of nearly 4 per cent of GDP in 2007. IMF, Solomon Islands: 2008 Article IV Consultation—Staff Report; Staff Supplement; Public Information Notice on the Executive Board Discussions, IMF Report No. 08/358, November 2008, p. 11.

6 *Submission 70*, p. 7.

patrols identified an oil tanker that 'had not paid the relevant duties or royalties...which in PNG was a significant amount of money'.⁷

14.10 In some cases, the causes of lost revenue to government are difficult to determine. Dr Lake, AusAID, referred to leaks in Kiribati's current budget system. She informed the committee that the policy and regulatory frameworks around its state-owned enterprises are really unfortunate to the extent that the government itself incurs quite considerable losses that are 'both uncontrolled or poorly controlled'.⁸ A weakness in administrative capacity resulting in loss of revenue can also be found in the judicial system in PNG. Ms Lucinda Atkinson, Attorney-General's Department, explained that 'PNG has an entrenched lack of capacity within its judicial system, so there are large numbers of backlogged cases and claims against the state'. She explained:

Often people take advantage of the fact that judges do not have the time or the resources to properly hear cases, and also the Solicitor-General's office is under-resourced in terms of being able to actually attend court hearings. Often people will take advantage of that and make vexatious claims against the PNG government and, when the Solicitor-General's office litigators cannot get to a court because they are booked in five other courtrooms at the same time, the court has no choice but to award in favour of the claimant.⁹

14.11 Weak, inefficient or poorly resourced government agencies also impede economic growth through their inability to deliver essential services effectively. The poor state of infrastructure and education services in the region, discussed earlier, are key indicators of this failing. Indeed, numerous witnesses spoke of the lack of institutional capacity in Pacific island countries and their inability to deliver services as a major constraint to economic development.¹⁰ Palms Australia identified a lack of administrative capability and weak internal linkages without organisational structures as core impediments to development in PNG. As an example, it cited the inordinate delays in PNG for a teacher to be placed on the payroll and stated further:

Such examples are common across sectors, from business owners waiting for hours in bank queues to international governments and agencies waiting for financial reports from local communities or NGOs which would justify ongoing funding.¹¹

14.12 Australia's High Commissioner to PNG suggested that there had been a 'hollowing out of the capacity and a lack of leadership' in PNG. In his view, while

7 *Committee Hansard*, 21 November 2008, p. 58.

8 *Committee Hansard*, 12 March 2009, p. 28.

9 *Committee Hansard*, 21 November 2008, p. 64.

10 See for example, Mr Ian Clarke, Australia Papua New Guinea Business Council, *Committee Hansard*, 25 March 2009, p. 53 and 61; Professor Clive Moore, *Committee Hansard*, 26 March 2009, p. 10; AusAID, *Tracking Development and Governance in the Pacific*, 2008, p. 18.

11 *Submission 44*, p. 3. There are skills shortages that reach across all sectors of the economy for example in border management. See DIAC, *Submission 36*, p. 5.

there are competent officers in the public service who provide leadership, others simply do not have the capacity and are challenged. He informed the committee:

Some who are able and brought in to fix it are just defeated by the chronic incapacity and unwillingness of their senior managers to respond because there are entrenched interests at play.¹²

14.13 This inefficiency and lack of capacity to deliver services permeates administrations throughout the region.¹³ Mr Brian Anderson, Australia Fiji Business Council, noted that the bureaucracy in Fiji needs to be streamlined and strengthened: that in many cases it is a roadblock.¹⁴ More generally, AusAID observed that many Pacific countries have 'difficulties attracting, developing and retaining skilled staff'. It explained further:

Low levels of investment in human resources has led to many public servants lacking basic skills (for example, literacy and numeracy), including at senior levels. Skills at provincial levels of government are, on average, substantially weaker than at the national level. Key public sector skills urgently require development, especially for improved service delivery.¹⁵

14.14 Mr Ian Clarke, Australia Papua New Guinea Business Council, argued strongly for the need to 'reinvigorate and assist the bureaucracy'. In his view, if the bureaucracy is efficient and effective, 'the rest will look after itself'.¹⁶

14.15 A number of witnesses agreed with the view of the Australian High Commissioner that there are intelligent and committed people in the public service but that other factors undermined their work including inadequate resources.¹⁷ Mr Hodgson, Australia Pacific Islands Business Council, added that most Australian public servants would not work under the conditions prevailing in some places in Pacific island countries. He said they would 'not walk in the front door' of those

12 *Committee Hansard*, 19 March 2009, pp. 11–12.

13 World Vision Australia, *Submission 47*, p. 7. World Vision Australia noted that in the government sector, 'Insufficient numbers of well-educated and skilled people are available to run governments at all levels, resulting in failures of service delivery and accountability'. A recent Asian Development Bank evaluation report found that a lack of synergy between central and local agencies and improving management competencies remain a challenge in PNG. ADB, *Performance Evaluation Report, PNG: Public Service Program*, Operations Evaluation Department, December 2008, p. 17. Ms Hayward-Jones suggested that the governments of both PNG and Solomon Islands lack the capacity to deliver the services they promise, *Committee Hansard*, 24 March 2009, p. 10.

14 *Committee Hansard*, 25 March 2009, p. 72.

15 AusAID, *Tracking Development and Governance in the Pacific*, 2008, p. 14.

16 *Committee Hansard*, 25 March 2009, p. 71.

17 See also Mr Hodgson, Australia Pacific Islands Business Council, *Committee Hansard*, 25 March 2009, p. 73.

places, 'let alone sit there all day and try to do a job'.¹⁸ Professor Clive Moore cited the use of today's technology to highlight the difficulties facing public servants in providing service:

The Solomon Islands subdepartment of statistics, for instance, really does not have a clue what is going on or how to collect data. Neither does it have equipment that does not break down. When a bank of computers breaks down or a single computer breaks down, often there is not the money available to replace them.

...

Air-conditioning systems break down in the Pacific constantly.¹⁹

14.16 He noted that the level of technical sophistication required in today's bureaucracy is not only very expensive but also hard to maintain if technicians are not available. He added 'there are a lot of dead computers out in the Pacific'.²⁰ Mr Clarke suggested that public servants may not 'even have a typewriter let alone a computer' and that the services to their buildings are 'in some disarray'.²¹

14.17 These ill-equipped bureaucracies are often called upon to deliver services that require both technical skills and advanced technology. In particular, Pacific islands countries with the potential to earn significant income from large commercial enterprises require the support of a sound and effective government bureaucracy if they are to seize opportunities for growth.

14.18 Mining projects provide a good case study. Although they tend to be large scale and well resourced, these operations still require a business environment that facilitates business activity and investment. Gladstone Pacific Nickel Ltd noted that one of the major impediments to the progress of a major project to mine lateritic nickel ore in Solomon Islands was 'the absence of bureaucratic efficiency'.²² It detailed its unsuccessful efforts to overcome bureaucratic logjams, including delays and missing documents, to obtain prospecting licences through an international tender process. According to the company, such obstacles are experienced by 'other Australian companies and to a lesser extent other overseas companies trying to do business there'.²³

14.19 The Australia Papua New Guinea Business Council indicated that the lack of capacity in the PNG government sector to deal with permits, regulation and

18 *Committee Hansard*, 25 March 2009, p. 72. Mr Chris Gaskell, APRA, also mentioned computer problems. *Committee Hansard*, 25 March 2009, p. 49.

19 *Committee Hansard*, 26 March 2009, p. 11.

20 *Committee Hansard*, 26 March 2009, p. 11.

21 *Committee Hansard*, 25 March 2009, p. 72.

22 Presentation Memorandum to the Australia Pacific Islands Business Council, attachment to *Submission 60*.

23 Presentation Memorandum to the Australia Pacific Islands Business Council, attachment to *Submission 60*.

compliance was 'a major impediment to development'.²⁴ Mr Peter Graham, Esso Highlands Ltd, informed the committee that the proposed PNG LNG project poses 'significant challenges for prudential government'. In his view, the legislative, financial, commercial and practical implementation matters would place substantial burdens 'on the currently limited resources of the various levels of government'.²⁵

14.20 As noted earlier, the proposed PNG LNG project presents a major challenge for the PNG administration, including finding the capacity to analyse and assess critically the 5,000 or so pages of the environment and social impact statement and the accompanying 36 independent studies. It must also deal with licence applications that already number 26. Quarantine and immigration matters pose another major task for the administration such as processing the anticipated 10,000 third country national visa applications from workers all over the world, and having in place arrangements for the importation of 550,000 tonnes of steel pipe. The government also needs the capacity to reach agreement with landowners on the benefit-sharing arrangement; to provide the necessary economic infrastructure; and to develop and implement policy concerned with the training and development of local people to work in the industry. According to Mr Graham, government policies should seek to encourage and facilitate local businesses to meet the requirements of the project and become suppliers over its 30-year life.²⁶

14.21 Although Pacific island countries such as the Cook Islands, Vanuatu and Samoa have achieved relatively high scores on the scale of government effectiveness compared to PNG and Solomon Islands, the evidence suggests that all Pacific island countries would benefit from improved bureaucracies.

Financial management

14.22 The management of the financial affairs of a country is critical to economic development. In this regard, a number of Pacific island countries have greatly improved their performance. For example, ANZ noted that the Government of PNG had done a sound job establishing macroeconomic stability with its economy experiencing consecutive years of positive growth. It attributed this turn around to the implementation of prudent fiscal policy.²⁷ It concluded:

...there is now greater transparency and consultation with the private sector and the wider population around the preparation of the budget. Notwithstanding, more work is needed to ensure greater headway is made.²⁸

14.23 Solomon Islands has also improved its financial management but again weaknesses remain. Mr Motteram, Treasury, observed:

24 *Submission 70*, p. 6.

25 *Committee Hansard*, 26 March 2009, p. 39.

26 *Committee Hansard*, 26 March 2009, pp. 39–42 and 46–48.

27 *Submission 51*, p. 3.

28 *Submission 51*, p. 4.

In the case of the Solomon Islands a shock like the massive civil war that they had must have made a huge impact on their middle management capacity, so there is some work that needs to be done. At the end of the day most of the tasks are quite achievable for them to build their indigenous capacity.²⁹

14.24 A number of witnesses were particularly concerned about the capacity of governments to manage revenue windfalls from large commercial enterprises. They recognised the difficult challenge facing governments in devising and implementing policies that would ensure that these proceeds 'translate into generalised wealth and economic prosperity in the host country'.³⁰ The Commission on Growth and Development pointed out, however, that history generally indicated that the reverse tended to happen:

Sometimes the state sells extraction rights too cheaply or taxes resource revenues too lightly. Sometimes the money it raises is stolen or squandered by rent-seeking elites and vested interests. When the money is invested, it is not always invested wisely or transparently. And by providing a ready source of foreign-exchange, natural resources can also reduce incentives for diversifying exports, a predicament known as 'Dutch disease'. States will improve on this sorry historical record only if they capture an appropriate share of the resource rents; save a judicious amount overseas; and set clear, growth-oriented priorities for absorbing the remainder at home.³¹

14.25 The Pacific Islands Forum Secretariat also referred to experience that suggested that 'resource booms often give rise to difficult economic and governance problems'.³²

Managing income from large commercial operations

14.26 PNG stands out as a country grappling with the task of harnessing revenue earned from the proceeds of commercial undertakings and feeding it back into productive areas of the economy. The Australia Papua New Guinea Business Council commented on the nature of this challenge:

These funds [from current and projected resource projects] need to be directed at economic infrastructure, health and education services and sustainable small business development...it is important that appropriate

29 *Committee Hansard*, 20 November 2008, p. 6.

30 *Committee Hansard*, 26 March 2009, p. 39.

31 Commission on Growth and Development, *The Growth Report, Strategies for Sustained Growth and Inclusive Development*, The International Bank for Reconstruction and Development/the World Bank, 2008, pp. 8–9, <http://cgd.s3.amazonaws.com/GrowthReportComplete.pdf> (accessed 27 October 2008). Dutch disease refers to the adverse consequences that may follow large increases in a country's income. The term was coined after Holland's poor performance in managing wealth generated from its natural gas reserves in the 1960s.

32 *Submission 69*, p. 5.

frameworks are put in place promptly to manage these flows for long term sustainable purposes.³³

14.27 The proposed PNG LNG project underscores the urgency for the PNG Government to meet this challenge. In Mr Graham's view, the project would act as a catalyst in putting PNG 'on the pathway towards achieving its full potential'.³⁴ He informed the committee that 'the true potential of PNG goes well beyond the oil and gas reserves that form the basis of our project'. He cited an economic impact assessment by independent economists ACIL Tasman which found that the project has the potential to transform the PNG economy, potentially doubling the GDP.³⁵

14.28 Esso Australia was of the view that the PNG Government would 'need to grow both its size and its governance capacity significantly if it is to properly support the Project [LNG] and truly reap the community rewards possible from a major project like this'.³⁶

14.29 Mr Motteram, Treasury, also expressed concern about the ability of PNG's administration to use the large amount of money that the government has in trust funds for their intended purposes (building roads, education and so forth) and to fully expend them. In his view, 'Capacity constraints within the public services are a critical issue for them'.³⁷ Professor Clive Moore was of the view that 'at the mining royalty level a lot of advice needs to be given to Pacific governments about how to involve the community in that distribution'.³⁸ He noted that money intended for local landowners may go instead to building 'an ever richer and more powerful Papua New Guinea elite—creating a new one, too, because a lot of these projects are in rural areas'.³⁹

33 *Submission 70*, p. 2. See also Mr Clarke, Australia Papua New Guinea Business Council, *Committee Hansard*, 25 March 2009, p. 65.

34 *Committee Hansard*, 26 March 2009, p. 38.

35 The ACIL Tasman report concluded 'Appropriately handled, PNG LNG will provide the government of PNG with an opportunity to maintain a responsible program of expenditure on social programs and productivity-enhancing infrastructure development yielding long-term improvements in quality of life and economic stability for the people of Papua New Guinea'. *Submission 34*, p. 2 and *Committee Hansard*, 26 March 2009, pp. 38–39. See also statements by ANZ, *Committee Hansard*, 24 March 2009, p. 53.

36 *Submission 34*, p. 2. An economic impact study by ACIL Tasman on the proposed PNG LNG Project suggested that: 'One effective approach to ensure that future generations of Papua New Guineans benefit from the LNG project would be to invest a substantial part of government revenues from the project into an offshore fund. The interest on this fund would provide a perpetual source of revenue...[and] help to smooth out the effects on revenue of commodity price cycles', ACIL Tasman, *PNG LNG Economic Impact Study*, 6 February 2008, p. viii.

37 *Committee Hansard*, 20 November 2008, p. 9.

38 *Committee Hansard*, 26 March 2009, p. 10.

39 *Committee Hansard*, 26 March 2009, p. 12.

Smaller Pacific island countries

14.30 In some Pacific island countries the requirement for sound financial management of government revenue is magnified because of their limited ability to absorb the effects of poor decisions. Those without significant natural resources, in particular, have few policy options to help them counter the adverse effects of their small size, remoteness and susceptibility to natural disasters. The tiny scattered atoll nation of Tuvalu is a case in point:

Despite a long-standing record of sound economic management, Tuvalu has failed to achieve sustainable growth due largely to constraints imposed by the paucity of land-based resources, extreme isolation, smallness, and dispersion over vast ocean spaces.⁴⁰

14.31 In June 1987, the Tuvalu Trust Fund was established to help the country achieve financial stability by providing government with an additional and reliable source of funds. It was intended to finance chronic budget deficits, underpin economic development and achieve greater financial autonomy. The fund was initially capitalised with contributions from the UK, New Zealand, Australia, Tuvalu, Japan and the Republic of Korea. Some commentators regard it as the most successful public fund in the Pacific which provides a model for the effective use of such funds for small-state economic development.⁴¹ In the view of the Tuvalu Trust Fund Board, the agreement has provided Tuvalu with:

...a level of financial security not thought possible at Independence. It has provided an additional source of government revenue that underpins the Budget and so the whole economy.⁴²

14.32 Kiribati is another of the small Pacific island countries with a revenue base that is 'highly volatile and narrow'. It has a Revenue Equalization Reserve Fund that was established in 1956 from phosphate mining royalties.⁴³ With sound financial management, the funds have steadily increased.⁴⁴ Even so, a more recent ADB Update registered concerns about the heightened risk that the fund's value 'could be entering a long-term period of decline if management is not improved'.⁴⁵ In chapter 2, the

40 Te'o I. J. Fairbairn, Review Essay: 'Economic Vulnerability and Resilience of Small Island States', *Island Studies Journal*, Vol. 2, No. 1, 2007, pp. 133–140, <http://www.islandstudies.ca/system/files/u2/ISJ-2-1-2007-Fairbairn-pp133-140.pdf> (accessed 24 October 2008).

41 Benjamin Graham, Asian Development Bank, *Trust Funds in the Pacific: Their role and future*, 2005, p. 39; and Tuvalu Trust Fund Board, *Tuvalu Trust Fund, 20th Anniversary Profile, 1987–2007*, p. 3.

42 Tuvalu Trust Fund Board, *Tuvalu Trust Fund, 20th Anniversary Profile, 1987–2007*, p. 3.

43 Catriona Purfield, *Managing Revenue Volatility in a Small Island Economy: The Case of Kiribati*, IMF Working Paper, WP/05/154, p. 3.

44 Catriona Purfield, *Managing Revenue Volatility in a Small Island Economy: The Case of Kiribati*, IMF Working Paper, WP/05/154, p. 3.

45 Asian Development Bank, *Country Strategy and Program Update, Kiribati (2006–2007)*, January 2006, p. 7.

committee noted that the global economic downturn is eroding the value of the assets held in these trust funds.

14.33 Nauru stands as a stark reminder of the need for the prudent and capable management of a country's finances. The Nauru Phosphate Royalties Trust was established to build up funds from phosphate royalties in order to generate income once the mineral reserves were exhausted. The country accumulated substantial offshore assets that peaked at approximately \$1 billion but, according to an ADB report, a decline in phosphate mining, combined with poor management of the country's offshore assets and public expenditure, led to 'a dramatic deterioration in its economic and fiscal position'.⁴⁶ Another ADB study stated that the management of the fund 'broke almost every rule in the book':

...its trust fund governance structure was weak and not transparent, it made poor trust investments, it raided its funds and used them as collateral, and it maintained an unwarranted expansionary fiscal position.⁴⁷

14.34 Nauru is now heavily indebted and relies on income from fishing licences and foreign aid, especially from Australia. An ADB project has been approved to establish a 'well managed Nauru Trust fund on par with the Tuvalu Trust Fund'.⁴⁸ The country, however, has severe capacity constraints in its financial management. Mr Motteram, Treasury, indicated that a generation of people 'have missed out on comprehensive education' and noted further:

There are a number of people within the finance ministry who are possibly going to be going forward, but I was talking to our manager there recently and he sees it as possibly another five years before there will be an indigenous capacity to have a local secretary of finance there.⁴⁹

14.35 The current global financial crisis has elevated the importance of sound and prudent financial management to a new level. Fiji exemplifies the difficult task facing Pacific island countries as the global economic crisis worsens. Mr Peceli Vocea, Governor of the Bank for Fiji, said:

It adds to the already precarious situation we face in managing the risks related to commodity price increases. Policy making as a result, has become more challenging with the trade-off between inflation and growth whilst ensuring financial stability is at the forefront of policy makers' consideration. As such, the current crisis calls for more urgency in strengthening surveillance.⁵⁰

46 ADB, *Country Economic Report, Nauru*, November 2007.

47 Benjamin Graham, Asian Development Bank, *Trust Funds in the Pacific: Their role and future*, 2005, p. 48.

48 ADB, 'Nauru Trust Fund: Republic of Nauru', TA No. 7183, approval 2 December 2008.

49 *Committee Hansard*, 20 November 2008, pp. 6–7.

50 IMF, Statement by the Hon. Peceli Vocea, Governor of the Bank for Fiji, at the Joint Annual Discussion, Boards of Governors Meeting, Press Release No. 49, 13 October 2008, <http://www.imf.org/external/am/2008/speeches/pr49e.pdf> (accessed 14 October 2008).

14.36 The small Pacific island countries in particular have been buffeted by the global economic downturn, especially the economies that rely heavily on tourism and remittances. As mentioned earlier, those with trust funds invested in international financial markets have seen the value of their assets plunge. The ADB noted that to date, these governments 'do not appear to have reduced public spending to compensate'. It urged Kiribati and Tuvalu to 'trim government spending quickly so as to match the decline in the value of their offshore investments'.⁵¹

Conclusion

14.37 To be a constructive and productive sector of a country's economy, the public service needs to have the necessary resources, skills and commitment. A competent, professional public sector is well placed to deliver government services to a high standard. Whether providing advice or managing finances or projects, it is better able to reduce the costs of government through greater efficiencies and the elimination of waste; sound budget processes; and prudent and effective financial management, including the collection of revenue and allocation of resources. Evidence suggested, however, that the performance of state institutions in many Pacific island countries is mixed. Clearly, Pacific island countries would benefit from assistance to help them build capacity in their bureaucracies.

51 Asian Development Bank, *Asian Development Outlook 2009, Rebalancing Asia's growth*, 2009, p. 280.