

# **Pacific Islands Economies: Trade Patterns and Some Observations on Trade Policy Issues**

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### **Pacific Islands Economies: Trade Patterns and Some Observations on Trade Policy Issues**

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East-West Center, Honolulu As in other developing regions, international trade plays a particularly crucial role in the economic life of small Pacific island countries. All these countries are dependent, to an unusual degree, on imported goods and services, including foodstuffs, fuel, equipment and industrial material as well as a wide range of manufactured products. Exports are a vital source of foreign exchange earnings and cash income generation, employment and growth.

Export activity is generally viewed as a major source of growth, particularly through its dynamic and catalytic effects on the rest of the economy. Unusually high trade-GDP ratios prevail throughout, making these small economies among the most open (and externally vulnerable) in the world.

A major challenge facing these island countries is to strengthen their export sectors as a basis for accelerated growth. However, the recent experience shows that few of these countries have succeeded in meeting this challenge - in many cases, export activity remains stagnant and, in some cases, has suffered serious decline. Among the major obstacles to trade expansion have been

persistently low world prices for traditional exports from the region (especially for coconut products), failure to adapt to changing international market conditions and, in some cases, the adoption of policies and strategies that effectively penalise export activity.

The main purpose of this paper is to examine some of the major trade characteristics of Pacific island countries. Particular attention is given to the export activity - structure, destination, recent trends and intra-regional patterns. The paper also focuses on a number of issues affecting the export performance of Pacific island countries, particularly the widespread emphasis on export production as a major development goal. The paper ends with a discussion of some of the dangers inherent in an uncritical pursuit of export-oriented development strategies.

## Overview

The 22 island countries and territories of the South Pacific region are scattered over a vast area of the Pacific ocean and differ greatly in size. Papua New Guinea, with a total land area of 462,200 km<sup>2</sup> (equal to 83% of the region's total land area of just over 500,000 km<sup>2</sup>) is the largest, followed by Solomon Islands with an area of 28,520 km<sup>2</sup> (Appendix A). The remaining island countries are small to very small, with at least four - Tokelau, Tuvalu, Pitcairn Island and Nauru - each being 30 km<sup>2</sup> or less. The majority of these countries are widely dispersed, a handicap which gives rise to difficulties over transportation, administration and the provision of other basic services.

The population of the region is currently around 6.2 million, with Papua New Guinea accounting for 60 per cent. The rate of population increase of around 2.2 per cent per annum, is one of the highest in the world and is the result of a combination of high birth rates (with a number of exceptions) and unusually low mortality rates. Several of the larger countries, notably Papua New Guinea, Solomon Islands and Vanuatu, are experiencing particularly rapid population growth, but for some of the smaller countries (notably those with ease of access to the United States and New Zealand), a sustained process of emigration has been a major factor in containing high rates of (natural) population growth. Population densities vary widely but are particularly high for the very small island countries.

Papua New Guinea, together with Solomon Islands, Fiji and New Caledonia, is relatively well endowed with natural resources - arable land for tropical agriculture, forestry, fisheries and minerals. These countries, which account for over 80 per cent of the region's population, have a considerable potential to achieve sustainable growth, and, in fact, they have already made notable progress in developing their natural resources. The resource base of the middle-level island countries, such as Western Samoa and Tonga, is more modest, while the very small countries have extremely limited resources, largely restricted to the fisheries potential contained in their Exclusive Economic Zones (EEZs). (However, several of these small countries enjoy special advantages deriving from the fact that they have been substantially compensated for the lack of resource diversity. Nauru with phosphate, and American Samoa with its strategic advantage for fish processing are examples.)

By the standards of developing countries, levels of national income are relatively high. While a number of these countries have GNP per capita well below \$1,000, exceptionally high levels of income are being received by such countries as French Polynesia, New Caledonia and Nauru. GNP per capita ranges from a low of around \$500-700 for Tokelau, Kiribati and Solomon Islands to around \$20,000 for Nauru and French Polynesia. Underlying the high income received by many of these countries, are high levels of official development assistance (ODA), substantial personal remittances from overseas, and large tourism sectors. High levels of income are also the result of special advantages such as are found in Nauru and New Caledonia with access to phosphate and nickel deposits respectively.

Compared with other developing countries, Pacific island countries have made notable progress in education, health and related social services. Most of these countries have achieved near universal adult literacy, high primary school enrolment rates, and many have succeeded in extending life expectancy (typically to the high 60s) and reducing infant mortality rates (as low as 23 per 1,000 live births in Tonga). Nonetheless, in many cases, there is considerable room for improvement. This is particularly true of the larger Melanesian countries - Papua New Guinea, Solomon Islands and to a lesser extent Vanuatu - which lag considerably behind the rest of the region. For these countries, the adult literacy rate is only around 50 per cent; primary school enrolment around 60-70 per cent; and, for Papua New Guinea and Solomon Islands, life expectancy is a low 55 years. In these cases, the need to improve social services remains a key development priority.

Pacific island countries face many difficult problems in their quest for economic growth. Among the most familiar are the barriers imposed by distance from the main trading centres (and from each other); small physical size (other than Papua New Guinea); vulnerability to external shocks and natural hazards; and small domestic markets. Other major constraints are the shortage of development capital and manpower skills; limited development options; and inadequate infrastructure facilities. Among the very small island countries, the capacity to overcome many of these problems remains particularly weak .

Regional cooperation is relatively advanced in the South Pacific and regional organisations, led by the South Pacific Forum and the South Pacific Commission, provide a forum for political, economic, social and cultural cooperation. In the economic and trade fields, regional cooperation has been particularly notable in the areas of fisheries, shipping, the environment, information exchange, and technical training. Strong links have been established with a large number of bilateral and multilateral donors for purposes of securing financial and technical assistance, and on a per capita basis, the region is among the highest aid recipient in the world. While trading channels with traditional partners (primarily Australia, New Zealand and France) are well established, economic relations with the Asia-Pacific rim have, to date, been limited.

#### International trade: major patterns

Trade patterns among the Pacific island countries are characterised by narrow export sectors and a high dependence on imports (Appendix B). Exports are dominated by natural resource-based products, both processed and unprocessed. Among the smaller island countries, export production is virtually confined to one or two traditional products, such as copra and handicrafts. However, in several cases, for example Fiji and Western Samoa, relatively large manufacturing and assembly-type operations are in place and contribute significantly to foreign exchange earnings, employment and gross domestic product (GDP). The main markets are the industrial countries and trade between the island countries themselves is very limited and largely concerned with the transshipment of goods.

As noted, the level of import dependence is high and this is particularly striking for the very small island countries (e.g. Tuvalu and Kiribati) which lack both an agricultural and industrial base. Four categories of imports are dominant - machinery and transport equipment, fuel, foodstuffs, and manufactured goods - with these groups usually accounting for over 70 per cent of the region's total imports. Australia is the leading source of supply followed by France, the United States, Japan and New Zealand. For almost all Pacific island countries, import demand appears to have grown rapidly over the recent period. (See Appendix C for principal commodity imports by selected countries and Chart 3 for main sources of imports.)

Almost without exception, Pacific island countries have, over the last few decades, recorded substantial trade deficits with the rest of the world - a situation that reflects, among other things,

high import demand relative to a capacity to generate export earnings. Recent (1989) trade statistics for the region as a whole show that exports (including re-exports) totalled just over \$4.0 billion (or \$680 per capita) against imports of \$6.7 billion (or \$1,100 per capita), resulting in a regional trade deficit of \$2.6 billion - equal to 63 per cent of total export earnings (South Pacific Commission 1992, p. 9). To offset such deficits, these countries have relied heavily on non-commodity sources of foreign exchange, chiefly in the form of earnings from services, private transfers, migrant remittances, official development assistance, and capital inflows. A notable feature of the trade accounts is that, with the exception of Nauru, all South Pacific island countries registered trade deficits. Nauru has consistently recorded large trade surpluses (estimated at \$80 million in 1989) as a result of substantial earnings from the shipment of phosphate.

Agricultural-based products, including forestry and fisheries products, are next in importance. The leading exports and producers are sugar from Fiji, palm oil from Solomon Islands and Papua New Guinea, and processed fish from American Samoa, Solomon Islands and Fiji. There are several major producers of coconut products (e.g. coconut oil and cream), while Papua New Guinea and Solomon Islands have been the largest exporters of forestry products, notably logs.

#### Chart 1: Import by source, 1989

For many of these countries, export earnings represent a very low proportion of GDP. This is particularly so for the very small countries. For example, in the case of Kiribati, export earnings in 1989 equalled less than one per cent of GDP (versus 77% for imports), and for Western Samoa the corresponding figure was nine per cent (and 60% for imports) (AIDAB 1962). Comparable data for Tonga and Vanuatu show much the same results as for Western Samoa. The export earnings to GDP ratio is considerably higher for the larger countries that have succeeded in building up more substantial export sectors. Thus for Fiji, in 1987, export earnings equalled 27 per cent of GDP (and retained imports 60%). (World Bank 1990).

Similarly, among many small Pacific island countries, exports as a source of foreign exchange earnings appear to play a minor role in the overall balance of payments. This is clear from a comparison between total export earnings and total net receipts from current account sources of income (exports, services and private transfers). Thus, the evidence for Kiribati, Tonga and Western Samoa - to take a few examples - shows that export earnings are of the order of 13-15 per cent of total receipts on current account. (The comparable figure for Fiji is 75%.) The relative insignificance of exports has to be viewed against the commonly held view that exports act as the engine of economic growth.

The region's exports are mainly composed of minerals, agricultural and other natural resource products (Chart 2, Table 1, Appendix B). Minerals are dominant, with export earnings an estimated \$2.0 billion in 1991, equal to around half of total exports earnings. Production is restricted to three large island countries - Papua New Guinea, New Caledonia and Fiji - and Nauru. The leading producer is Papua New Guinea which, in 1991, exported gold valued at \$900 million, copper at \$450 million, and silver at \$16 million, while in 1992, oil was exported for the first time and was valued at \$560 million (AIDAB 1993). Regarding the other producers, New Caledonia shipped nickel and non-ferrous metal valued at \$540 million, Fiji gold at \$70 million, and Nauru phosphate at \$100 million.

As would be expected, export diversification is greatest among the large countries (Table 1). This is particularly so for Papua New Guinea which, in addition to minerals, also produces and exports coffee, palm oil, and forestry products. Similarly for Fiji, the range of non-gold exports covers sugar, garments, ginger, canned fish, forestry products, and a number of manufactured products (as well, Fiji plays a major role as a re-exporter). Solomon Islands has also succeeded in broadening its export base - copra, palm oil, canned fish, and logs. The degree of export diversification achieved by these

countries contrasts with the situation in the very small island countries where exports are usually limited to one or two products. Nauru with phosphate, Tuvalu with copra and handicrafts being examples.

Chart 2: Exports - Principal domestic products, 1989

Source: SPC 1993, p. 36-55

Table 1: Total Exports and Principal Export Products by Country 1991 (A\$m)

Manufactured products are prominent only in a few cases with the export of such products largely restricted to Fiji and Western Samoa. Over the last few years, Fiji has succeeded in establishing a substantial export-oriented garments industry which is now second only to sugar as an industrial export. Fiji has also succeeded in exporting a range of other manufactured products - albeit on a modest scale - including biscuits, paint, beer, and cement. In Western Samoa, the production of automotive wire harnesses for export has been a recent initiative and this activity has expanded substantially to the point of being the dominant export item.

Many of the middle-level and small Pacific island countries depend on a narrow range of traditional products, such as copra, cacao and handicrafts. However, several of the smaller countries have had some success in developing new lines of activity that have allowed a degree of diversification. Tonga is a notable example, with the recent development of squash and vanilla as leading export industries. The development of the pearl industry in the Cook Islands and automotive parts manufacture in Western Samoa are other notable examples. In general, the problem of developing viable export activities and achieving significant sectoral diversification remains a major challenge for these countries.

Exports from the region have been dominated by Papua New Guinea, New Caledonia and Fiji. These countries contribute close to 80 per cent of total regional exports, with Papua New Guinea accounting for around 50 per cent of this total, New Caledonia 20 per cent and Fiji around 13 per cent. Except for Fiji, this dominance is largely due to the export of mineral products - gold, copper and oil in the case of Papua New Guinea and nickel for New Caledonia. For Fiji, sugar remains the leading export, but gold, forestry products, processed fish are also important. Among the remaining countries, American Samoa, Nauru, Northern Mariana Islands and Solomon Islands are the main contributors.

Regarding the destination of the region's exports, the principal markets are Japan, the United States and Europe (Chart 3). Exports to Japan have expanded rapidly over the last decade and in 1989, amounted to around \$1.0 billion or 24 per cent of total export earnings. The United States and Europe (mainly France and the United Kingdom) account for 12 and 15 per cent of export earnings respectively, while Australia and New Zealand, nine and three per cent. As noted, intra-regional trade is insignificant, accounting for around two per cent of total regional exports.

Over the past decade, export performance among the Pacific island countries has been mixed, but generally disappointing. In general, the larger countries have done reasonably well, while many of the middle-level and smaller island countries have performed poorly. An inspection of trade data over the 1985-92 period shows that the value of exports more than doubled for Papua New Guinea, Fiji and Solomon Islands (NCDS 1994, pp. 67-100). Largely responsible for this outcome was the expansion in minerals exports in the case of Papua New Guinea, and similar expansion in fish canning and log production in Solomon Island and garments manufacturing in Fiji. The expansion in exports in Tonga has also been impressive and can be attributed to the developments in squash and vanilla production.

### Chart 3: Exports - main region of destination, 1989

Source: SPC 1992, p. 13

For most of the remaining countries, export activity has remained stagnant and in a few cases, declined fairly sharply. Over the recent period, export earnings have remained little changed in the case of Vanuatu, Kiribati, and Tuvalu, but for Western Samoa, they have suffered a steep decline. For Samoa, over the period 19 to 1993, export earnings have fallen from a level of around \$20 million to \$6 million - a decline that reflected severe cyclone damage to the country's productive base.

#### Intra-regional trade

Intra-regional trade is very small and appears to have contracted over the last decade or so. Trade data for 1989 show that intra-regional exports (equal to imports), including re-exports, totalled \$82 million, equal to around two per cent of total regional exports (\$4.0 billion). The corresponding figures for intra-regional export of domestically produced products were \$32 million and less than one per cent. Fiji was dominant by far, contributing over 70 per cent of total intra-regional exports (including re-exports) with Solomon Islands, French Polynesia, Papua New Guinea and Western Samoa following some way behind. (Note that round 66% of re-exports were accounted for by Fiji.) Detailed data on the composition of this trade are not available. However, apart from the dominant re-export element, which probably includes the transshipment of fish products for processing at regional canneries, the main products involved include the shipment of sugar and a range of manufactured items from Fiji to island neighbours, and mainly fresh produce from Western to American Samoa.

Pacific island countries have, in the past, shown considerable interest in expanding trade among themselves. This has been evident among island members of the South Pacific Forum which have tended to view intra-regional trade as a possible mechanism for strengthening their balance of payments and promoting economic growth as well as further promoting the process of regional cooperation. However, despite several studies of intra-regional trade possibilities, no major breakthrough has been made. Progress has been blocked by a number of constraints including the fact that the economic structures of these island countries and the kind of export activities they can sustain are broadly similar. Examples are the production of traditional staples such as copra, bananas, and a variety of root and vegetable crops. Other leading constraints appear in the form of often large distances between these island countries and the persistence of special trade and transport arrangements (not to mention tariff and related barriers to trade) between individual island countries and their former colonial mother countries. Where external aid contains a significant tied element this also contributes in some degree to reducing the potential for more trade between these countries.

Re-exports totalled \$50.0 million in 1991, equal to 1.2 per cent of total exports from the region, or 0.7 per cent of imports. Fiji accounted for over 60 per cent of re-exports, with Papua New Guinea, French Polynesia and Solomon Islands being the other notable players. Fiji owes its dominance to its central location and longstanding entrepot status, especially in relation to such neighbours as Tonga, American and Western Samoa, Kiribati and Tuvalu. A large proportion of Fiji's re-exports relates to the distribution of petroleum for shipping and airlines. Information on the composition and direction of re-exports for Solomon Islands and Papua New Guinea is not available, but for French Polynesia, re-exports relate principally to the shipment of goods imported from France.

Interest in promoting greater intra-regional trade has remained somewhat subdued in recent years. The South Pacific Forum Secretariat stands ready to play a coordinating role in this area but, in

practice, much greater emphasis is given to promoting stronger trade links with the major industrial markets where the potential for trade expansion is much greater. Such an emphasis is embodied in the South Pacific Regional Trade and Economic Cooperation Agreement or SPARTECA initiative adopted during the 1970s and designed to provide non-reciprocal preferential entry for products of Forum island countries of island products into the Australian and New Zealand markets. Examples of special trade arrangements between Pacific island countries themselves are few and largely restricted to a sugar scheme between Fiji and a number of island neighbours and preferential market access provided by Fiji for handicrafts from several of the smaller countries including Tuvalu.

### Service activities

Service industries have become major sources of foreign exchange earnings for many Pacific island countries. Such activities are dominated by tourism although international tax haven facilities are important in a number of countries. For most, if not for all of these island countries, tourism represents one of the best prospects for attaining economic growth and diversification. Such prospects are based on a generally favourable world outlook for tourism expansion combined with the many favourable features that almost all Pacific island countries have to offer, including interesting cultures, the natural beauty of islands, the availability of space and relatively unspoilt natural environments.

Almost all Pacific island countries are making efforts to boost tourism and to realise its development potential. Those that have made the most progress are Fiji, French Polynesia, the Cook Islands, Vanuatu and the U.S. associated countries. In Fiji, the Cook Islands and French Polynesia, tourism has provided a considerable momentum for growth and it ranks among the leading two or three industries. The main sources of tourists are the United States, Australia, Europe, New Zealand and Japan.

Many Pacific island countries, including Fiji, Papua New Guinea, Western Samoa and Tonga, have been cautious in their approach to tourism development. In framing their development strategies, these countries have opted for a system of controlled tourism so as to minimise the possibly adverse impact on local cultures. They have also been influenced by the need to avoid tourism approaches that involve damaging the natural environment. Development strategies based on eco-tourism has evoked considerable interest among these countries in recent years.

Particularly among the smaller countries, much remains to be done to overcome existing constraints and to realise the growth potential of this industry. An important common need is to channel more resources into improving basic infrastructure and to upgrading accommodation and related services. Also important is the need to upgrade overseas promotion and train support staff. For many, too, the high cost of air flights and infrequent air services remains a serious problem.

### Future prospects

Medium to longer-term prospects for exports from the region are far from bright. The international trade environment appears to be fraught with difficulties and uncertainties. The decline in the strategic significance of the South Pacific region with the end of super power rivalries means that the Pacific island countries will have to face more difficult conditions in establishing marketing links, while for a variety of reasons, many of the traditional products supplied by these island countries will be facing more intensive international competition (Elek 1994). Additional uncertainties stem from signs of increasing trade protectionism as a result of rising tensions between major trading powers, for example, Japan and the United States.

Commodity prices for many of the leading exports from the region are likely to remain depressed (Appendix D). For major agricultural products such as coconut and palm oil, any possibility of significant increase in prices is being threatened by such factors as pressure from substitutes, increased production from low-cost Asian producers, and inelastic demand for traditional exports. Pacific island suppliers will face increasing competition in many of their traditional markets as a result of the general trend toward the dismantling of trade barriers. At the same time, the importance of special trading arrangements, such as SPARTECA which accords preferential entry of island products to the markets of Australia and New Zealand, will decline, thereby further exposing Pacific island countries to more intense competition in these markets.

These developments call for major efforts to strengthen national capacities to earn foreign exchange and to take advantage of new trading opportunities. Key areas that need to be considered are more vigorous efforts to achieve more efficient and competitive economic structures and policies, improve labour productivity through training and research efforts, and promote greater flexibility in the allocation of resources at the sector level. Similar efforts are needed to promote suitable processing and related downstreaming activities for maximising local value-added and income and employment generation. Further processing possibilities in relation to coconut and forestry products are particularly worthy of investigation. Further efforts should also be made to develop tourism which appears to hold considerable promise for most of these island countries. Considerable scope also exists for the extension of regional cooperation, especially in the development of major resources and services, such as fisheries and tourism, agricultural research, and harmonisation of taxation incentives.

Pacific island countries - especially through the South Pacific Forum - need to make stronger efforts to strengthen their trading links within the wider Asia-Pacific region. Present trade with Asia is significant - equal to around 27 per cent of exports and 17 per cent of imports - and dominated by Japan. A significant potential exists for these island countries to increase their trade with Asian countries by taking advantage of opportunities presented by dynamic growth taking place in the Asian sub-region and rising demand for mineral and other natural resource items produced in the South Pacific.

Through both regional and individual country efforts, Pacific island countries should be encouraged to play a more active role in current Asia-Pacific initiatives, notably the Asia Pacific Economic Cooperation forum, or APEC, and the Pacific Economic Cooperation Conference, or PECC, aimed at building up a more open trading (and investment) framework and at promoting more collaborative approaches to the solution of common development problems and issues. The South Pacific Forum enjoys observer status at ministerial-level meetings of APEC, but so far no Pacific island country is a full member of either APEC or PECC. Nonetheless, these island countries are free to participate in the task forces and working groups established by these organisations and this provides a potentially valuable mechanism for constructive participation. Through such involvement, combined with the South Pacific representation at APEC, Pacific island countries can participate in regional work programs concerned with the development and management of key resources, for example, fisheries, forestry and the marine environment; benefit from the exchange of technical information; and, in general, the opportunity to advance a clearer understanding of their needs and development problems.

#### Export orientation and related policy issues

Reference to the national development plans of many Pacific island countries - large and small - indicate that trade expansion figure prominently in current efforts to achieve growth and related development objectives. Export-orientation in production is widely viewed as a key development strategy essential for promoting the role of trade as the so-called engine of growth. This emphasis is



based on the benefits that can accrue from gaining access to larger external markets; to the opportunity to achieve greater product specialisation and lower unit costs through economies of scale and from various externalities that trade can bring, including learning and inter-industry linkage effects. The need to boost export production has been a prominent element in recent efforts to achieve more open and efficient economic structures through, for example, labour market deregulation and public sector reforms.

Many of these countries have gone out of their way to provide special investment inducements for export-oriented ventures as a means of stimulating export production. These include a range of tax concessions, such as income tax holidays, exemption from the payment of import duties on raw materials and equipment, and accelerated depreciation allowances. These are usually provided on top of other more direct forms of assistance, for example, the provision land and factory space at reduced rentals, access to subsidised credit, special training schemes, and financial assistance on the promotional and marketing sides. Some of these inducements - whether considered individually or as part of a total package - appear very generous.

Export incentives provided by Fiji to boost export-oriented manufacturing are particularly liberal and appear to have succeeded in their objectives, especially in relation to the export of garments. These include the provision of a range of tax concessions for which manufacturing operations designated as a tax free zone (TFZ) or factory (TFF) are eligible. (A major eligibility criterion is that at least 95% of total output of a company is sold overseas.) Such concessions include a tax holiday of up to 13 years, duty free imports of raw materials and components, and exemption from excise duty. Another notable example is Western Samoa which provides a tax holiday of up to 15 years for a major export activity along with other financial inducements. (In a recent case, namely the establishment of an automotive components assembly operation, the government not only provided generous tax concessions but also constructed a building for the investor concerned.)

It appears therefore that export-orientation is firmly entrenched in the growth strategy of many Pacific island countries, and, in general, this has been backed up by a range of taxation incentives and more direct and practical measures of assistance that often appear to be very generous. The question I would like to pose is this - Is this seemingly heavy emphasis on export-orientation overdone? Is it a realistic option for the small island countries? And what are the dangers and risks inherent in such an approach? Should these countries exercise more caution in trade policy? The remainder of this paper will seek to provide some light on these issues and specifically, to offer a few caveats that should be heeded by those countries that see export-orientation as road to their economic salvation.

## 1. Trade and growth

Export-orientation, as a potentially dynamic strategy for promoting economic growth, needs to be viewed with some caution when applied to the economic circumstances of the small island countries of the South Pacific. The plain fact of the matter is that these small countries have little potential for building up substantial export industries. With the possible exception of fisheries, the resource base is not there, while other key constraints are present in the form of a chronic shortage of capital and technical know-how and remoteness from the major markets. Such constraints underpin present trade patterns among these small countries, as for example the very small export sectors that have developed to date. As noted, for many of these small countries, export earnings represent no more than 10 per cent of GDP, and less than 15 per cent of current account receipts in the balance of payments.

It is apparent therefore that export production plays a minor role in overall production and foreign exchange earnings and, for many of these small island countries, the potential for major expansion is

difficult to envisage. Far more important has been income received in the form of services, private transfers, official development assistance and other 'rent' sources of income. Reference to the balance of payments of Kiribati, for example, shows that, in 1991, export earnings of \$4 million were well below receipts from net services of \$18 million, net private transfers of \$5 million, and official assistance of \$23 million (AIDAB 1992, p. 57). It also appears that over the recent period, export production did not contribute to Kiribati's growth. While GDP (in current terms) rose by 43 per cent between 1985 and 1991, export earning declined by around 43 per cent. Much the same applies for Tuvalu whose economic growth of between five and six per cent per year over the recent period took place within a stagnant export sector (AIDAB 1993).

On the basis of the recent experience, therefore, it appears that the economies of the small island countries have been predominantly shaped, not by export production, but by the external rent flows in the form of private transfers, migrant remittances, official aid and, in some cases, fishing license fees. It can be argued - as have Bertram and Waters in recent works on the so-called MIRAB economies - that these economies are largely driven by rent income rather than by income from productive export-oriented activities (Bertram and Waters, 1986 and Bertram, 1986). According to these authors, the future sustainability and prospects for increasing living standards in these small islands hinge on their capacity to maintain and enhance access to future sources of rent income, including official aid. Export production is of minor importance and may even undermine rent entitlements (e.g. in the sense that conventional productive projects can crowd out aid and remittance entitlements (Bertram 1986)).

## 2. Collapsible export sectors

A small narrowly-based island economy that is heavily geared to export production faces considerable risks and uncertainties. A major risk is the collapsibility of an export industry arising from external factors beyond the control of these island countries (Tisdell, 1985 and Kakazu, 1985). An export venture can collapse for several reasons, including a severe decline in world demand for a major export product, a loss of a traditional market, or the exhaustion of a non-renewable resource. As well, export activity can decline through the indiscriminate exploitation of a key natural resources such as in fisheries and forestry.

The collapse of a major export venture can have traumatic consequences on the economic life of the population. Significant adjustments may have to be made to the standard of living and economic aspirations. Population levels that were sustainable with trade may no longer be tenable and may need to contract if basic subsistence standards are to be maintained. Such adjustments may mean that, in the final analysis, these economies become no better off than they were before the establishment of export-oriented production. They may even be worse off if, in the transition toward export orientation, traditional skills are lost necessary to maintain basic subsistence production.

There are many recent examples of export industries in the region that have collapsed as a result of unfavourable external influences. One that has been most pervasive is copra whose decline has been triggered by persistently low international prices for over a decade. Other well-known cases are the cessation of banana exports from Western Samoa to New Zealand as a result of competition from South American suppliers; the export of fruit juices from the Cook Islands to New Zealand due to increasing pressure from other suppliers. The exhaustion of phosphate on Ocean Island and the near mining out of the same product in Nauru are also well-known. Increasing pressure of competition from Asian suppliers is threatening other export industries, including the processing of coconut cream in Western Samoa.

Pacific island countries need to recognise the inherent dangers of over-dependence on export production and develop appropriate policy measures to minimise the risks inherent in such

dependence. Consideration should be given to approaches that foster greater production for the domestic market, especially basic subsistence products. The aim should be to maintain a stable mix between subsistence and export production - and to foster the preservation of traditional productive skills. Moreover, an attempt should be made to develop, within possible limits, a degree of diversification in export production to avoid over-concentration on one or two export products. Allied to this is the desirability of promoting service industries as a basis for further diversification. Implicit in such an approach is a recognition that, realistically, the comparative advantage of many Pacific island countries lies in service industries such as tourism.

### 3. Resource exploitation

A further danger relates to trade in forestry products and other major natural resource-based products. Papua New Guinea, Fiji and Solomon Islands are relatively well-endowed with forestry resources and have relied heavily on foreign companies, particularly Asian ones, for development. However, almost invariably, the involvement of foreign companies has led to serious problems of resource exploitation that has brought little real benefit to the host country. In some cases, these companies have been encouraged by their governments to set up operations in the South Pacific region to gain access to supplies while conserving their own forestry resources. Many of these companies appear to engage in unscrupulous practices designed to reduce royalties, taxation and other financial obligations payable to island countries. (This often happens despite their receiving generous taxation incentives.) Furthermore, logging has taken place without regard for the sustainability of the resource, thereby undermining longer-term growth prospects. Indiscriminate logging has caused serious environmental damage - soil erosion, silting of rivers and lagoons, and impairment of water catchment areas. In purely commercial terms alone, the loss of revenue to Papua New Guinea, Fiji and Solomon Islands through transfer pricing and related practices has been estimated at around \$130 million per annum.

Both for economic and ecological reasons, it is essential for Pacific island countries to take the necessary steps to protect their forestry resources against over-exploitation and loss of sustainability. Grave concern over the extent of foreign exploitation of forestry has forced a number of island countries, notably Solomon Islands and Western Samoa, to impose a ban on the export of logs. Careful control of the export activities of commercial loggers should be maintained and efforts made to develop forestry management plans and programs that embody the essential concept of resource sustainability.

Pacific island countries control large sea areas under their EEZ jurisdiction that bring with them access to extensive marine resources. Fiji and Solomon Islands in particular have developed sizeable fisheries industries which contribute significantly to export earnings, while American Samoa is a major fish processing centre. Regional cooperation in fisheries has made much headway, largely through the work of the South Pacific Forum Fishery Agency. However, island countries have not been in a position to take full advantage of their marine resources and, as a consequence, have received minimal financial benefits. Illegal fishing by foreign fishing vessels remains a serious problem and has deprived many of these countries a fair return for their marine resources. Understatement of catches by these groups has also reduced the benefits to the island countries. Lack of effective surveillance and management mechanisms also threatens the sustainability of migratory fish stocks. Clearly, more effective regional cooperation is essential if these countries are to gain more benefits from these resources. Such cooperation is particularly important in relation to the need to improve surveillance systems, to assess stock size and migration patterns, to strengthen negotiation capabilities, and to promote the exchange of technical information.

### 4. Trade and possible environmental damage

Among Pacific island countries, the further expansion of trade as an integral element of the growth process can have far-reaching consequences for the natural environment. This is largely because of the unusually high trade:GDP ratios prevailing in these countries and a high level of dependence on resource-based products for export combined with generally fragile environments. As compared with countries with larger land masses, environmental resources and systems are compressed (so to speak) into a more limited area so that the scope for interaction tends to be more direct, more immediate and more devastating. This close inter-dependence is readily visible, for example, where heavy flooding, soil erosion and coastal siltation occur as a result of indiscriminate deforestation thereby destroying the fragile ecosystems of lagoons and mangrove swamps. In the case of coral atolls, a major source of environmental fragility is the vulnerability of water lenses to pollution where effective waste disposal systems are lacking. It is essential therefore, that these island countries take the necessary steps to protect their natural environments against those aspects of international trade that are potentially hazardous and destructive. Efforts to develop natural resources for export and related commercial purposes can be particularly damaging with a resulting significant and often permanent negative impact on social and economic welfare. In the case of agriculture, increased export production can lead to major damage to the natural resource and environmental base via the incursion of commercial agriculture into watershed areas, the excessive application of chemicals, and inappropriate technology. The clearing of forested areas for agriculture can lead to widespread damage to both land and marine environments through soil erosion, siltation of rivers and streams, deterioration of water quality, sedimentation of coastal waters (leading to the destruction of marine habitat and fisheries), and loss of biodiversity. Export-orientated industrialisation policies can result in the establishment of polluting industries that discharge effluent into reef, lagoon and mangrove zones. The harm that may be caused to fisheries and recreational areas can be high and irreversible. Such industries can also make a heavy demand on scarce natural resources, notably water and beach sands (not to mention imported fuel). Tourism - an industry that is widely viewed as a major growth potential - can also be a major source of environmental degradation as a result of heavy consumption of water, inappropriate location of facilities, and possible damage to sensitive environmental areas by tourists.

On the import side, increased trade can create a wide range of environmental problems. The inevitable expansion of trade means that these countries will have to cope with an increasing amount of imported waste material, including solid wastes, hazardous waste and other non-biodegradables. This poses the problem of how to dispose of these wastes in an environmentally - and hygienically - sound way - a problem that is particularly acute for the smaller countries which are disadvantaged both by lack of funds and physical space (for establishing dumping sites).

## Conclusion

Pacific island countries, regardless of size, are heavily dependent on international trade and tend to view export expansion as a potentially dynamic source of economic growth. Trade patterns are very simple - reflecting the developing status of these island countries, and, particularly for the small countries, very narrow resource bases. Mineral and agricultural-based products are dominant by far, while the export production of technically sophisticated manufactures is very limited. The larger island countries, including Papua New Guinea, contribute the great bulk of the region's exports, almost all of which are destined for the markets of the large industrial countries (there being very little intra- regional trade). Over the recent period, the large island countries have achieved fairly impressive export expansion - and a degree of diversification - but the smaller countries have generally performed poorly as a result of weak international prices for traditional staples and the basic constraints imposed by limited resource endowments. Medium-term prospects remain uncertain but generally unfavourable.

Although, particularly for the large better-endowed Pacific island countries, export expansion can provide a powerful stimulus to economic growth, the dangers inherent in an uncritical acceptance of an export-oriented strategy have to be recognised. Under the particular circumstances of these countries, an over-commitment to export-orientation carries many potential risks. In particular, adverse changes in the terms of trade can lead to the collapse of a major export industry with potentially traumatic effects on the standard of living and economic aspirations; export industries based on the commercial exploitation of key natural resources (e.g. forests) can result in very little financial benefits to the host country and may cause serious and irreparable damage to the natural environment. Furthermore, export-orientation as a major growth strategy may be misplaced given that, in some cases, comparative advantage may lie in the development of service industries such as tourism. In light of these strictures, it is essential that these island countries take it upon themselves to develop more realistic trade policies which, among other things, recognise the many risks associated with an excessive commitment to export orientation and the need for more balanced approaches.

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