

Chapter 16

Private sector—driver of economic growth

16.1 In large part, governments are responsible for creating an environment that fosters, not frustrates, enterprise. In this chapter, the committee builds on its consideration of economic infrastructure and government effectiveness to explore further the major impediments to economic growth. Its main focus is on the business environment and the extent to which governments in the region create an environment that encourages economic growth and development.

Encouraging private enterprise

16.2 A number of witnesses observed that economic growth depends on the private sector which, in their view, has much scope to grow in Pacific island countries.¹ For example, the Australia Fiji Business Council emphasised how a vibrant and sustainable small/medium enterprise (SME) sector would be the key to employment growth.² In AusAID's assessment, the private sector could be 'the generator of growth'.³

16.3 The Pacific 2020 report noted, however, that 'the private sector requires a competent government, but is discouraged by an overbearing one'. It argued that governments 'need to facilitate private investment, not crowd it out by being directly involved in commercial activities or by imposing burdensome regulations or excessive taxation'.⁴ They need to reduce the climate of risk and provide policy certainty for business. The Australian Chamber of Commerce and Industry argued similarly that excessive red tape and an inefficient bureaucracy strangle growth.⁵

16.4 These observations that link the performance of the bureaucracy, the regulatory environment and private sector activity are particularly apt for many Pacific island countries. A recent UN report noted that governance arrangements in most Pacific island countries make foreign and private sector investors wary of investing.⁶ Another report published by the Pacific Islands Forum Secretariat used the tuna industry to show how the business environment, with its high cost of production and short-sighted macroeconomic policies, hindered development. In its view, Pacific island countries make it 'difficult for foreign and even locally based companies with long-term visions to be successful'. It argued that 'for domestic tuna development to

1 See also Austrade, *Submission 61*, p. 9.

2 *Submission 58*, p. 5; *Submission 60*, p. 4; *Submission 70*, p. 2.

3 *Committee Hansard*, 20 November 2008, p. 26.

4 AusAID, *Pacific 2020, Challenges and Opportunities for Growth*, May 2006, p. 43.

5 *Submission 29*, attachment, p. 8.

6 ESCAP, *Enhancing Pacific Connectivity*, 2008, p. 73.

work, the economic and policy environment has to enable private-sector development'.⁷

Ease of doing business

16.5 Statistics on regulatory quality taken from a World Bank data base and reproduced in Table 14.1 (chapter 14) support these observations about Pacific island countries having 'a difficult business environment'. They indicate that governments in most Pacific island countries have a long way to go to improve their ability 'to formulate and implement sound policies and regulations that permit and promote private sector development'. From a top score of 100, Fiji (34), Vanuatu (33), PNG (30), Nauru (23), Tonga (23), Tuvalu (20), Kiribati (14), and Solomon Islands (13) were unimpressive with ratings below the 35th percentile. Samoa (52) and the Cook Island (55) were just above the 50th percentile.

16.6 The results of another more targeted survey are consistent with the statistics showing that Pacific island countries do not rate highly on a scale measuring the ease of doing business. Although the order of merit differs from that cited above, the rankings still show Pacific island countries performing poorly. From a total of over 180 countries, they received the following rankings on the ease of doing business, with number 1 being the highest:

Table 16.1: Rankings on ease of doing business (number 1 being the best)⁸

Country	2010 rank (rankings from 183 economies)	2009 rank (rankings from 181 economies)	2008 rank (rankings from 178 economies)
Tonga	52	43	47
Fiji	54	39	36
Samoa	57	64	61
Vanuatu	59	60	62
Kiribati	79	79	73
Solomon Islands	104	89	79
Palau	97	91	82
Marshall Islands	98	93	89
Papua New Guinea	102	95	84
Micronesia	128	126	112

Between 2007–2009, Singapore, New Zealand and Australia, which were rated at no. 1, 2 and 9 respectively, were among the countries identified as good-practice economies.⁹

7 Kate Barclay with Ian Cartwright, *Capturing Wealth from Tuna: case studies from the Pacific*, Asia Pacific Press, Australian National University, 2007, pp. 22 and 38.

8 Information taken from Tables 1.3 in World Bank, *Doing Business 2009* and *Doing Business 2010*.

9 The International Bank for Reconstruction and Development/the World Bank, *Doing Business 2009 East Asia and Pacific–Pacific Islands*, Washington, 2008, p. 2.

16.7 This scale is based on a set of regulations affecting ten stages of the life of a business—starting a business, dealing with construction permits, employing workers, registering property, obtaining credit, protecting investors, paying taxes, trading across borders, enforcing contracts and closing a business. Based on analysis, the survey highlighted how these various regulations can impede economic growth. For example, it argued that:

...burdensome entry regulations do not increase the quality of products, make work safer or reduce pollution...they constrain private investment, push more people into the informal economy; increase consumer prices and fuel corruption.¹⁰

16.8 It observed that investors worry about their money and rely on laws to protect their interests. Thus, the legal and regulatory protections offered to investors influence their business decisions.¹¹ It also noted that 'in the absence of efficient courts, firms undertake fewer investments or business transactions'.¹² The late Secretary General of the Pacific Islands Forum Secretariat, Mr Greg Urwin, noted:

...good governance, apart from the savings it generates, can also be a powerful leverage on foreign investment—investment is ultimately an act of faith, and quite evidently, without investors being convinced that the governance procedures of a country are of a quality to ensure a future for their efforts, they will go elsewhere, and we have seen them do so.¹³

16.9 Some witnesses identified areas where substantial work was required in Pacific island countries to remove barriers to enterprise and foreign investment. The Australia Pacific Business Council referred to 'slow bureaucratic processes and excessive regulation'.¹⁴ The Australian Chamber of Commerce and Industry suggested that red tape is a particular problem in some Pacific countries. It informed the committee that AusAID had indicated that 'the average cost of recovering a debt in Pacific countries is equal to 86 per cent of the debt and takes more than 500 days'.¹⁵ The Australia Fiji Business Council noted:

10 The International Bank for Reconstruction and Development/the World Bank, *Doing Business 2009 East Asia and Pacific—Pacific Islands*, Washington, 2008, p. 3.

11 The International Bank for Reconstruction and Development/the World Bank, *Doing Business 2009 East Asia and Pacific—Pacific Islands*, Washington, 2008, p. 17. It cited a study that found, 'the presence of legal and regulatory protections for investors explains up to 73 per cent of the decision to invest'.

12 The International Bank for Reconstruction and Development/the World Bank, *Doing Business 2009 East Asia and Pacific—Pacific Islands*, Washington, 2008, p. 26.

13 Greg Urwin, Secretary General, Pacific Islands Forum Secretariat, 'Regional cooperation and economic growth', Pacific 2020 Conference, Hilton Hotel, Sydney, 10–12 May 2006.

14 *Submission 60*, p. 6.

15 *Submission 29*, attachment, p. 8.

There is an excess of bureaucracy to be traversed at all levels of starting and operating a business, with increased burdens if the business requires access to land and/or if it is a foreign business investment.¹⁶

16.10 The governments of the Pacific island countries have made commitments to reduce the costs of doing business. International organisations, including the World Bank and the OECD, are working with them to foster an investment climate that would enable their private sector 'to flourish and fulfil its role as the main engine of growth'.¹⁷ Although Pacific island countries are taking positive steps to improve their business environment, progress is patchy and even those with better business environments could do more. The most recent ratings on the scale of ease of doing business show clearly that most Pacific Island countries are losing ground. Economies such as Macedonia, United Arab Emirates, Colombia, Kyrgyz Republic, Armenia and Taiwan improved significantly in the last year to secure places ahead of all the Pacific Island countries.¹⁸

Tonga

16.11 Tonga recognises that the time is ripe for it 'to increase the momentum of private sector reform' and is undertaking reforms.¹⁹ For example, it introduced regulations to its building code which effectively decreased the number of procedures for dealing with construction permits from 14 to 11, and with administrative improvements, the process was reduced by 12 days.²⁰ It also implemented new regulations on business licensing, which cut the time to start a business by one week, and has reduced the time required to enforce a contract from an estimated 510 days to 350 days.²¹ Tonga has also achieved major accomplishments in trade liberalisation and revenue reforms, for example, it has reduced its reliance on trade taxes. The ADB was of the view, however, that more could be done to improve the environment for private sector development by reform of state-owned enterprises and by better public service delivery.²²

16 *Submission 58*, p. 6.

17 OECD, *Promoting Private Investment for Development: the role of ODA*, DAC Guidelines and Reference Series, 2006, p. 7.

18 World Bank, *Doing Business 2010*, Table 1.3, p. 4.

19 Media Release, <http://www.pmo.gov.to/releases-mainmenu-29/english-mainmenu-30/286-prime-minister-of-tonga-launch-private-sector-assessment.html>.

20 The International Bank for Reconstruction and Development/the World Bank, *Doing Business 2009, Country Profile for Tonga*, 2008, p. 51.

21 Asian Development Bank, *Asian Development Outlook 2008*, p. 256.

22 Asian Development Bank, *Asian Development Outlook 2008*, p. 256.

Fiji

16.12 The Australia Fiji Business Council believed that Fiji has the potential to become a type of Singapore of the Pacific. Its central position in the region, the size and diversity of its economy, the skills and talents of its people and the presence of pre-eminent educational institutions provide the foundations for it to become the region's business hub. Nonetheless, the Council maintained, that even though Fiji rates relatively well on the ease of doing business scale, substantial work remains to be done to remove barriers to its trade and foreign investment. It explained that despite the rhetoric, Fiji 'is not an especially welcoming environment for foreign investors'. It cited a number of existing impediments to the development of a vibrant economy. They included a restricted industries list (which excludes selected business types from any foreign investment), a reserved industries list (which requires a minimum Fiji domestic equity in the business and/or a minimum foreign investment level), a restrictive fiscal and foreign exchange policy and an opaque taxation system.²³

Samoa

16.13 Since the early 1990s, Samoa has embarked on major reforms including tax reforms, civil service changes to reduce the public debt, structural reforms to promote competition and encourage the private sector and privatization of state-owned enterprises.²⁴ Recently it lowered rates of corporate and capital gains taxes.²⁵ The ADB observed that growth forecasts for Samoa rely on the government refocusing on economic and public sector reforms. It noted in particular measures that would reduce the costs of doing business including 'reform of the commercial legal framework and facilitation of leasehold access to customary land, and ensuring access to reliable utility services at reasonable prices'. Even so, the bank noted that 'revamping state-owned enterprises has generally been slow and the enterprises have often failed to comply fully with new regulatory requirements'.²⁶ The IMF recommended that Samoa continue to deepen its reform program that, in its view, would 'yield a much higher real per capita growth'.²⁷ Samoa was one of only two Pacific island countries to improve its rating on the 2009 scale for the ease of doing business. It jumped 7 places from 64 to 57.

23 *Submission 58*, p. 8.

24 IMF, *IMF Executive Board Concludes 2007 Article IV Consultation with Samoa*, Public Information Notice (PIN) No. 07/62, 1 June 2007, p. 4.

25 The International Bank for Reconstruction and Development/the World Bank, *Doing Business 2009, Country Profile for Fiji*, 2008, pp. 50–51.

26 Asian Development Bank, *Asian Development Outlook 2008*, p. 254.

27 IMF, *IMF Samoa: 2007 Article IV Consultation—Staff Report; and Public Information Notice on the Executive Board Discussion for Samoa*, Country Report no. 07/185, *IMF Executive Board Concludes 2008 Article IV Consultation with Samoa*, Public Information Notice (PIN) No. 07/62, 1 June 2007, p. 8.

Vanuatu

16.14 Vanuatu is also making progress with structural reform. It has upgraded financial sector supervision, and, according to the IMF, is taking measures 'to improve utility pricing and increase competition in the telecommunications'. Even so, the IMF indicated that more needs to be done to create a climate conducive to investment. It cited the need to improve the land registration and titling process; to ensure that public enterprises operate efficiently; and to eliminate infrastructure bottlenecks by encouraging private sector involvement.²⁸ Professor Rod Duncan suggested, however, that the regulatory environment in Vanuatu could have declined in absolute terms in the past few years and, in relative terms, fallen behind other countries that have been reforming.²⁹

PNG

16.15 PNG is one of the countries falling behind in implementing reforms. A recent IMF report described the investment environment in PNG as 'unattractive'. It was blunt in asserting that the structural reform agenda 'to improve the investment climate has seen little progress'—that PNG ranks poorly in areas such as enforcing contracts, dealing with licences, getting credit, trading across borders and the quality of the bureaucracy.³⁰ In its assessment, the recent economic performance was 'an improvement relative to the recent past, however, the growth performance gap relative to peers continues to grow'. It urged the government to 'accelerate progress on structural reform, without which the outlook for more rapid non-mineral sector growth, job creation, and poverty alleviation is dim'.³¹ A World Bank study explained:

To stimulate private sector investment, particularly outside mining, the critical priority is improvement in the business climate, especially by opening more markets to competition, reducing the regulatory and licensing

28 IMF, Statement at the Conclusion of an IMF Staff Mission to Vanuatu, Press release No. 08/29, 22 February 2008.

29 Rod Duncan, Lecturer, School of Marketing and Management, Charles Sturt University, 'Solomon Islands and Vanuatu: an economic survey', *Pacific Economic Bulletin*, vol 23, no. 3, 2008, p. 8, http://peb.anu.edu.au/pdf/PEB23_3_DUNCAN_WEB.pdf (accessed 14 October 2008).

30 IMF, Staff Report for the 2007 Article IV Consultation, prepared by the staff representatives for the 2007 Consultations with Papua New Guinea, 18 January 2008 and IMF Country Report No. 08/93, Papua New Guinea: Selected Issues and Statistical Appendix, <http://www.imf.org/external/pubs/ft/scr/2008/cr0893.pdf> (accessed 9 October 2008).

31 IMF, Staff Report for the 2007 Article IV Consultation, prepared by the staff representatives for the 2007 consultations with Papua New Guinea, 18 January 2008, Executive Summary, p. 4.

burden, clarifying property rights (especially for land), and maintaining law and order.³²

16.16 A recent economic survey of PNG supported this assessment. It found that the country ranks poorly on the ease of doing business because of the lengthy delays and large number of bureaucratic procedures involved in business activities. It used modelling to show the substantial savings to be made from simple reforms that would reduce the number of procedures to obtain construction licences and permits. It also looked at reforms that would reduce the required number of documents, and the time taken, to export and to enforce a contract. It concluded:

Whilst other barriers to growth remain, lifting the performance of Papua New Guinea's regulatory environment in a number of key areas to regional averages—a modest goal—could have a large impact on income growth.³³

16.17 Table 16.1 shows that PNG dropped eleven places on the ease of doing business scale between 2006–07 and 2007–08 and a further 7 places in 2009.

Solomon Islands

16.18 Progress on structural reform also remains slow in Solomon Islands.³⁴ The IMF found that the cost of doing business is relatively high by regional standards. It argued that an acceleration of structural reforms that would reduce the costs of doing business could help Solomon Islands to 'unlock the vast growth potential in the agriculture, fisheries (including canning) and tourism sectors and expedite production in the mining sector'. Mining provides an example of where bottlenecks repeatedly cause delays. These delays apply to both gold and nickel operations.³⁵ Professor Duncan suggested that in the last few years the regulatory environment in Solomon Islands could have declined in absolute terms and certainly was not keeping pace with other countries that have been reforming.³⁶ Table 16.1 shows that Solomon Islands

32 The World Bank, *East Asia: Testing Times Ahead*, East Asia and Pacific Update, April 2008, p. 49,

http://siteresources.worldbank.org/INTEAPHALFYEARLYUPDATE/Resources/550192-1207007015255/EAPUpdate_Apr08_fullreport.pdf (accessed 14 October 2008).

33 Aaron Batten, Jonathan Gouy and Ron Duncan, 'Papua New Guinea economic survey: from boom to gloom?', *Pacific Economic Bulletin*, vol. 24, no. 1, 2009, p. 21.

34 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. 3.

35 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.

36 Rod Duncan, Lecturer, School of Marketing and Management, Charles Sturt University, 'Solomon Islands and Vanuatu: an economic survey', *Pacific Economic Bulletin*, vol 23, no. 3, 2008, p. 8. http://peb.anu.edu.au/pdf/PEB23_3_DUNCAN_WEB.pdf (accessed 14 October 2008).

dropped ten places on the ease of doing business scale between 2006–07 and 2007–08 and a further 15 places in 2009.

Capacity to reform regulatory environment

16.19 The Pacific Islands Forum Secretariat noted that even with adequate and appropriate legislation, many Pacific island countries do not have the human resources to implement reforms. In its view, the lack of skilled personnel creates an administrative impediment to foreign investment.³⁷ Indeed, evidence demonstrates clearly that most Pacific island countries are yet to reach a stage where the quality of their bureaucracy and regulatory framework instil confidence in investors. By failing to create an enabling environment for economic growth, poorly performing bureaucracies and a burdensome regulatory regime inhibit, even prevent, the private sector from capitalising on economic opportunities. In effect, bureaucratic inefficiencies and regulatory bottlenecks in Pacific island countries stifle their productivity.

Control of corruption

16.20 All investors, from the smallest enterprise to multinational companies, base their investment decisions on anticipated risk-adjusted returns. As discussed above, these risk factors include unpredictable or burdensome government regulations, delays, excessive start-up and transaction costs, and complexities in establishing and doing business.³⁸

16.21 Corruption is another significant deterrent to business and investors and ultimately to sustainable economic growth. Often a manifestation of poor governance, corruption is 'the misuse of entrusted power for private gain by government officials as well as individuals in the private sector'.³⁹ A UN report explained that corruption may distort the pattern of public expenditure; weaken infrastructure by diverting funds; reduce the quality of investment; corrode the ideals of public service; and encourage a system where those entrusted to protect rights may be the source of harassment, extortion and fear. Corruption may even exacerbate the effects of natural disasters such as landslides associated with illegal logging. With regard to sustainable development, the report noted:

37 *Submission 69*, p. 9.

38 The Development Assistance and Investment Committees and the OECD's Development Co-operation Directorate and the Directorate for Financial and Enterprise Affairs. 'Mobilising Private Investment for Development: Policy Lessons on the Role of ODA', *the DAC Journal* 2005, vol. 6, no. 2, p. 14.

39 Definition based on United Nations Development Programme, *Tackling Corruption, Transforming Lives, Accelerating Human Development in Asia and the Pacific*, 2008, p. 18. http://hdr.undp.org/en/reports/regionalreports/asiathepacific/RHDR_Full_per_cent20Report_Tackling_Corruption_Transforming_Lives.pdf (accessed 22 December 2008).

Many developing countries in the Asia Pacific region are rich in natural resources, but, thanks to corruption, much of this natural wealth is being drained away. Companies may bribe public officials to get permits for cutting timber, for example, or they may pay to get away with logging in protected areas. Public officials themselves can also join in by running their own 'off-the-book' business. Similar problems arise with mineral extraction or unregulated fishing, and with systems of land registration and administration, or the capturing of protected species.⁴⁰

16.22 In chapter 5, the committee discussed corruption in the forestry industries in PNG and Solomon Islands. Table 14.1 (chapter 14) indicates, however, that corruption is a problem in a number of Pacific island countries. It shows that from a top score of 100, PNG (9), Tonga (15), Solomon Islands (33) and Fiji (42) all scored below the 50th percentile on the scale of control of corruption. Nauru and Tuvalu scored on or slightly above 50. Kiribati (61), Vanuatu (63), and Samoa (64) were deemed to be better able to control corruption including both petty and grand forms of corruption, and their administrations less likely to be captured by elites and private interests.⁴¹

16.23 Also, allegations of corruption are not confined to the forestry industry. An AusAID report on governance cited a commission of inquiry into corruption in PNG's Finance Department which is 'now uncovering details of more than K1 billion (A\$400 million) gone missing in the last few years'.⁴² A study by Australia's Office of Development Effectiveness noted that corruption was a 'major development problem in PNG'. It cited the growing influence of Asian crime syndicates in that country. While it could not assess the overall importance of this trend, it was led to conclude that 'corruption is taking a decided turn for the worse, with potentially serious implications for political governance and stability'.⁴³ According to ANZ:

While many of PNG's legal, structural and policy frameworks to prevent and address corruption are adequate, weaknesses lie in implementation, including lack of political will and limited capacity (financial and human) to fight corruption. Further assisting PNG to implement effective, broad-based reforms and improve the management of these resources will contribute significantly to reduced levels of corruption and tolerance for it.⁴⁴

40 United Nations Development Programme, *Tackling Corruption, Transforming Lives, Accelerating Human Development in Asia and the Pacific*, 2008, p. 7.
http://hdr.undp.org/en/reports/regionalreports/asiathepacific/RHDR_Full_per_cent20Report_Tackling_Corruption_Transforming_Lives.pdf (accessed 22 December 2008).

41 See definition of corruption used as a governance indicator in Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, *Governance Matters VI: Aggregate and Individual Governance Indicators 1996—2006*, the World Bank, Policy Research Paper 4280, July 2007, pp. 3–4.

42 AusAID, *Tracking development and governance in the Pacific*, August 2008, p. 13.

43 AusAID Office of Development Effectiveness, *Approaches to anti-corruption through the Australian aid program: lessons from PNG, Indonesia, and Solomon Islands*, 2007, p. 19.

44 *Submission 51*, p. 7.

16.24 It should be noted that some business representatives informed the committee that they do not necessarily agree with assumptions made about the level and extent of corruption in Pacific island countries. They suggested that a bureaucracy unable to process requests, applications and claims encourages people to seek assistance outside the normal due process giving rise to perceptions of corruption. Mr Clark was of the view that often corruption and bureaucratic inefficiencies get confused. He said:

When you have a strong bureaucracy or a strong public service you get a much better deal done with foreign investors; otherwise investors get very frustrated that they cannot get their approvals through and then they invariably resort to a discussion with the minister of the day. When you have a discussion with the minister of the day you do not follow due process, and corners are cut. It chases its own tail.⁴⁵

16.25 For example, Mr Hodgson explained that he was aware of situations in Pacific island countries where the frustration, generated after months and months of waiting for a decision, drives people involved in the negotiation to resort to the minister. He said 'permission is granted very quickly and, of course, people make assumptions'.⁴⁶ These observations underline the importance of Pacific Island countries improving the performance of their bureaucracies and the regulatory environments in which they operate.

16.26 The Pacific Islands Forum Secretariat also drew attention to the cultural context in which business is conducted. It noted that Pacific societies have a strong tradition of patronage 'which favours those with influence and connections, particularly in the exploitation of natural resources and penalizes those without'.⁴⁷ Mr Sanjesh Naidu from the Forum Secretariat, informed the committee that 'a number of our mandates and documents from various meetings and policy dialogues recognise that corruption is definitely a big constraint to our development in the region and a quite significant drag to our economic prospects'.⁴⁸ He was of the view that the functioning and operation of customs and border agencies could be improved 'to tackle the problem of malpractice and corrupt behaviour'.⁴⁹ Mr Rick Nimmo, Forum Secretariat, concluded that at every level—the audit, policing and broad governance level—'corruption is an issue that the region acknowledges, accepts and tries to address'.⁵⁰ He explained that the nature of corruption in the region would be no

45 *Committee Hansard*, 25 March 2009, p. 65. The ACCI also noted that excessive regulations promote corruption because businesses have an incentive to use any means to bypass the unnecessary red tape. *Submission 29*, attachment, p. 8.

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

47 *Submission 69*, p. 2.

48 *Committee Hansard*, 19 June 2009, p. 11.

49 *Committee Hansard*, 19 June 2009, p. 11.

50 *Committee Hansard*, 19 June 2009, p. 12.

different from that found elsewhere and involves 'misuse of public money, people taking bribes and developers giving people backhanders'.⁵¹

16.27 The Australian Chamber of Commerce and Industry noted that 'potential investors in the region need meaningful assurance that corruption is not endemic'.⁵² But once assumptions regarding corruption are made about a country, they can be difficult to shift. Indeed, regardless of facts, perceptions of corruption are equally effective at deterring foreign investment and undermining confidence in the government. According to Transparency International, perceptions of corruption may persist, even though in some cases unwarranted, 'in spite of attempts to clean up'.⁵³ It has produced a set of statistics that rank countries on the perception of corruption. Again Pacific island countries do not rate highly. From a total of 180 countries, Denmark, Sweden and New Zealand, all at number 1, showed the lowest levels of perceived corruption. Australia was placed 9th. Samoa ranked 62; Kiribati, 96; Solomon Islands and Vanuatu both 109; and Tonga, 138. PNG at 151 was deemed to have the highest levels of perceived corruption among the Pacific island countries. Fiji was not included in the index but the Interim Government in Fiji understands that 'Corruption and the abuse of positions and privileges have long been features of Fiji's economic and political landscape'.⁵⁴

16.28 These statistics suggest that many Pacific island countries have a problem with the perceived level of corruption within their borders.

Law and order and political stability

16.29 Law and order, political stability and absence of violence are also key factors that influence business decisions. The economies of countries renowned for political instability and for break-downs in law and order struggle to attract investment.⁵⁵ Numerous witnesses referred to the damage that political instability has done to

51 *Committee Hansard*, 19 June 2009, p. 12.

52 *Submission 29*, Speech by Peter Anderson, Chief Executive, ACCI, attachment pp. 3–5.

53 Peter Larmour and Manuhia Barcham, *National Integrity Systems: Pacific Islands, Overview Report 2004*, Transparency International, Australian National University, 2004, p. 7.

54 Government of Fiji, *Sustainable Economic and Empowerment Development Strategy (SEDS) 2008–2010*, November 2007, p. 40.

55 See for example, Address by Mr Bob Lyon, President of the Australia Fiji Business Council, at the launch of the *AusAID 2020 Report*, Sydney, 11 May 2006, 'Why good political governance is so essential for a dynamic private sector and investment' [http://www.afbc.org.au/Speeches_20060511_Bob per cent20Lyon per cent20to per cent20AusAID per cent202020.htm](http://www.afbc.org.au/Speeches_20060511_Bob_per cent20Lyon_per cent20to per cent20AusAID per cent202020.htm) (accessed 14 January 2009) and ESCAP, *Economic and Social Survey of Asia and the Pacific 2008: Sustaining Growth and Sharing Prosperity*, p. 73, http://www.unescap.org/survey2008/download/01_Survey_2008.pdf (accessed 1 October 2008).

economic development in the Pacific.⁵⁶ Mr Peter Anderson, Chief Executive, Australian Chamber of Commerce and Industry (ACCI), noted:

It is well known that states in the region have had a diverse experience with political stability. A challenge for commerce in the region...is ongoing stability and ensuring our laws, including laws governing labour and commerce, are made by politically stable elected representatives.⁵⁷

16.30 Recent events in Solomon Islands, Tonga and Fiji show the extent to which political uncertainties damage the prospects for economic growth.

16.31 In November 2006, riots destroyed a large part of the business district of Tonga's capital, Nuku'alofa. A state of emergency, which was declared for the main island of Tongatapu, was still in force in March 2008.⁵⁸ A number of sectors suffered setbacks including commerce, hotels and restaurants, transport and communications, financial and real estate services and manufacturing. According to the ADB, tourism receipts dropped by 10.4 per cent in financial year 2007.⁵⁹ The Government of Tonga acknowledged that the civil disturbance in 2006 'resulted in negative growth in 2006/07'.⁶⁰

16.32 Fiji has had four coups since May 1987, all of which have had a negative effect on the economy. For example, the coup in May 2000 ushered in a period of political instability, economic decline, significant loss of jobs and migration of skilled and professional workers. Following the military coup in December 2006, all major sectors of the economy weakened—'Export income and business confidence fell and macroeconomic policies were tightened, resulting in an estimated 3.9 per cent contraction in the economy'.⁶¹ In particular, the uncertainty led to a decline in tourist arrivals, worker layoffs, 'a fall in wholesale and retail trades and a freeze on private-sector investment projects'.⁶² According to Mr Anderson, Australia Fiji Business

56 See for example, Department of Immigration and Citizenship, *Submission 36*, p. 6.

57 *Submission 29*, attachment, pp. 3–5.

58 Asian Development Bank, *Asian Development Outlook 2008*, p. 255.

59 A number of sectors suffered a setback including commerce, hotels and restaurants, transport and communications, financial and real estate services and manufacturing. According to the Asian Development Bank, tourism receipts dropped by 10.4 per cent in financial year 2007, Asian Development Bank, *Asian Development Outlook 2008*, p. 255. See also ESCAP, *Economic and Social Survey of Asia and the Pacific 2008: Sustaining Growth and Sharing Prosperity*, p. 72.

60 Media Release, 'Economic Update: July 2008', <http://www.pmo.gov.to/releases-mainmenu-29/231-economic-update-july-2008.html> (access 14 February 2009).

61 Asian Development Bank, *Asian Development Outlook 2008*, p. 235.

62 ESCAP, *Economic and Social Survey of Asia and the Pacific 2008: Sustaining Growth and Sharing Prosperity*, p. 70.

Council, there is no confidence in the country and the investment that usually stimulates growth no longer exists.⁶³

16.33 The Australia Fiji Business Council had no doubt that the economy and domestic stability in Fiji were inextricably linked. It stated that the 2006 coup has had 'a deep and prolonged economic effect'.⁶⁴ The Governor of the Reserve Bank of Fiji explained:

...there are so many other countries...that investors can put their money into just as readily, if not easily, than in Fiji. We are already offering all kinds of enticements to lure tourists and investors to our shores: reduced hotel rates and airfares, tax breaks of various kinds for investors and so on. But these types of 'carrots' won't be effective if the environment is unstable.⁶⁵

16.34 Solomon Islands is another Pacific island country whose economy has suffered because of recent upheavals. During the late 1990s, long-standing tensions and land disputes between the peoples of the two main islands, Guadalcanal and Malaita, surfaced. Escalating organised violence and militant activity forced the closure of important export industries and crippled the economy.⁶⁶ In June 2000, the government was overthrown and, despite attempts to restore peace and stability, conflict continued, the economy faltered and government structures were rendered ineffective. Law and order issues remained unresolved, with ethnic violence dissolving into widespread criminality, violence and lawlessness. The national GDP decreased by a full quarter between 1998 and 2002 and formal government debt increased by more than 40 per cent in 2002 alone.⁶⁷

16.35 In June 2003, the Pacific Islands Forum foreign ministers endorsed an assistance mission to Solomon Islands and Solomon Islands formally requested regional help 'to restore law and order, security and economic sustainability'.

63 *Committee Hansard*, 25 March 2009, p. 59. Mr Nimmo, Pacific Islands Forum Secretariat, used tourism, which he suggested was a very good barometer of attitudes toward countries, to indicate the damage being done to Fiji's economy. In his view, the countries surviving the global economic crisis best are those that are stable such as Vanuatu and Samoa. In contrast, he argued that the 'political instability in Fiji has significantly hurt its ability to deal with the global downturn in tourism numbers'. *Committee Hansard*, 19 June 2009, p. 14.

64 *Submission 58*, p. 2.

65 Keynote address at the National Micro, Small, Medium Enterprise (MSME) Forum by Governor of Reserve Bank of Fiji, Mr Savenaca Narube, Lami, Suva, 22 May 2008, p. 8, http://www.reservebank.gov.fj/docs/Keynote_per_cent20Address_per_cent20National_per_cent20MSME_per_cent20Forum.pdf (accessed 27 October 2008).

66 For background see Dr Michael Fullilove, Lowy Institute for International Policy, *The Testament of the Solomons: RAMSI and International State-Building*, 2006, p. 5; Dr Elsina Wainwright, ASPI, *Our Failing Neighbour, Australia and the Future of the Solomon Islands*, 2003, pp. 18–27.

67 Dr Michael Fullilove, Lowy Institute for International Policy, *The Testament of the Solomons: RAMSI and International State-Building*, 2006, p. 6.

According to the IMF, since the restoration of peace in 2003, economic performance has been robust due in large measure to logging and increased aid.⁶⁸

16.36 PNG has also experienced economic setbacks because of political uncertainty but shows the success that can be achieved with domestic stability. ANZ noted:

PNG's economic growth has also coincided with a period of relative political stability that is unprecedented in PNG's history since independence. The Government under Sir Michael Somare (first elected in 2002) was the first to complete its term in office without suffering a vote of no-confidence. Work within that Government on improving PNG's economic policy framework and related governance structures have helped improve the country's economic fortunes.⁶⁹

16.37 A return to political stability has not, however, brought with it certain peace and security for communities. ANZ was of the view that law and order remains a major constraint on the country's economic and social development.⁷⁰ In its view, PNG 'suffers from a level of lawlessness that is disproportionate to its population and economic size'. This situation, according to ANZ, impacts 'significantly on quality of life of its citizens and seriously restricts investment and private sector development'.⁷¹ Mr Steven Noakes, Pacific Asia Tourism, informed the committee that PNG is perceived as a dangerous place, which has a negative effect on the market for tourism.⁷² As noted in chapter 12, one of the key law and order concerns is the growing number of unemployed young men in PNG.

16.38 ANZ monitors law and order developments closely to ensure the safety of its staff and operations. It informed the committee that 'its geographic footprint in the country is guided in large part by security considerations'. As an example, it explained that ANZ's ability to roll out its "'Banking the un-banked" program in regional areas is constrained by law and order considerations'.⁷³ Mr Tunstall, ANZ, noted that the cost

68 IMF, *IMF Executive Board Concludes 2008 Article IV Consultation with the Solomon Islands*, Public Information Notice No. 08/139, 29 October 2008, p. 1.

69 *Submission 51*, p. 3.

70 *Submission 51*, p. 5. See also the IMF which noted that in PNG political risks stemming from corruption and ethnic tensions are still a disincentive to investment. It estimated the direct costs of security at 3 per cent of total business cost on average. It also noted that 'overall labour costs are increased to compensate employees for the added personal insecurity'. Security concerns also 'generally lead to reduced intensity of capital equipment' and they 'occupy management's time, thereby reducing overall productivity'. IMF, *Papua New Guinea: Selected Issues and Statistical Appendix*, Country Report No. 08/93, p. 44, <http://www.imf.org/external/pubs/ft/scr/2008/cr0893.pdf> (accessed 9 October 2008).

71 *Submission 51*, p. 5.

72 *Committee Hansard*, 26 March 2009, p. 59.

73 *Submission 51*, p. 5.

of doing business in PNG is 'quite horrendous in terms of having...armed security guards'.⁷⁴

Summary

16.39 Clearly, the private sector is a catalyst for economic growth and Pacific states need to attract industry and investment in a highly competitive global market if they are to realise their economic potential.⁷⁵ The perception of Pacific island countries as poor economic performers and difficult places to do business is a disincentive for entrepreneurs and potential investors. It is therefore essential for Pacific island countries, where possible, to reduce the risks, real and perceived, that deter investors. They must endeavour to create an enabling domestic environment in order to make better use of their resources, encourage greater productivity, mobilise the private sector and attract and make effective use of foreign investment and assistance. The responsibility for creating an environment that attracts investment to support economic growth and sustainable development falls mainly to governments. They must ensure that business is not deterred by unnecessary barriers to entry or unacceptable risks to their investments caused through the poor delivery of essential services, bureaucratic bottlenecks, a weak regulatory system or corruption or law and order concerns. Their task is to convince business that their country welcomes and supports enterprise.

16.40 As a major donor country to the region, Australia can make a positive contribution to help Pacific island countries improve their governance and business environment.

Australia's assistance

Improving business environment

16.41 Much of the work that Australia does in the region either directly or indirectly contributes to developing a better business environment. The committee has already identified numerous programs that, by helping to promote good governance, ultimately contribute to an environment that instils business confidence. The following examples provide further indications of how Australian agencies working in

74 *Committee Hansard*, 24 March 2009, p. 54.

75 See for example, the Australian Pacific Islands Business Council, *Submission 60*, p. 4; *Submission 29*, p. 5; the Governor of the Reserve Bank of Fiji noted that investment is the 'locomotive of growth' and without it the economy would 'lose steam'. Opening address by Governor of Reserve Bank of Fiji, Mr Savenaca Narube, at the opening of Westpac's MHCC Branch, 20 June 2008, p. 2.

Pacific island countries are assisting Pacific Island countries to improve their regulatory environment.⁷⁶

16.42 AusAID cited the work being done by the Federal Court of Australia with the Supreme Court of Tonga to help identify priority areas for enhancing its court administration. As a result, court records, previously compiled manually, are now computerised allowing the progress of active cases to be monitored closely and easily. The Federal Court also helped 'to develop a regulatory framework for mediation, accreditation training for mediators, and to raise awareness amongst the legal profession and the public'. According to AusAID, these reforms have contributed to a significant reduction in the time taken to settle cases. It noted:

Tonga's Supreme Court had cut the average time to enforce contracts from 510 days to 350, earning it the title of the 2007 top reformer in the category of contract enforcement.⁷⁷

16.43 The regulatory environment for telecommunications is another area where Australia has provided assistance to Pacific island countries. Mr Oliver, Department of Broadband, Communications and the Digital Economy, noted that the work of his department focused mainly on governance matters—dealing with issues that arise as countries move to liberalise their telecommunications regime. He said:

Countries of the Pacific raise particular challenges because they do not necessarily have the sorts of resources that are available in larger countries in terms of regulatory capacity, competition law, even court systems that are able to deal with the issues, so there are particular challenges there.⁷⁸

16.44 AusAID referred to Vanuatu's decision to introduce competition into its telecommunications sector which provided AusAID with the opportunity to assist with financial support and commercial negotiations through its Governance for Growth initiative.⁷⁹

76 It should be noted that numerous international organisations are assisting Pacific island countries to improve their business environment. The Foreign Investment Advisory Service (FIAS) and World Bank, in particular, conduct numerous projects designed to address regulatory constraints and to support reform changes in Pacific island countries. The International Finance Corporation and the World Bank, 'East Asia and the Pacific', http://www.fias.net/ifcextJtias.nsf/ContentJFIAS_Projects_Asia_the_Pacific (accessed 18 December 2008). For a list of projects see http://www.fias.net/ifcextJtias.nsf/ContentJFIAS_Projects_Asia_the_Pacific_Country (accessed 18 December 2008).

77 Australian Government AusAID, Annual Report 2007-2008, p. 59.

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

79 Australian Government, AusAID, Annual Report 2007-2008, p. 59.

Creating a stable environment

16.45 In many ways political stability and law and order stem from communities free from the burden of poverty, food shortages and unemployment and that have good effective government. The committee has already considered the work that Australia is doing in the region to assist Pacific island countries with food security, natural disasters, employment, economic growth and governance. All of these activities go towards creating an environment less tolerant of corruption and more likely to promote political stability and law and order.

16.46 The Pacific Islands Forum Regional Security Committee recognised the connection between corruption and 'increasing crime and transnational criminal activity'. It stated, 'poor governance and corruption contribute to the entrenchment of transnational criminal groups.' It suggested that to be properly effective, 'we need to look at a more coordinated "whole of law enforcement" response'.⁸⁰ This matter will be considered in greater depth in the second volume of this report which covers security.

16.47 In the following chapter, the committee considers land tenure and access to finance as the final challenges facing Pacific island countries in developing their economies.

80 Pacific Islands Forum Secretariat, Opening Address by Mr Tuiloma Neroni Slade, Secretary General, Pacific Islands Forum Secretariat, Forum Regional Security Committee Meeting, 4–5 June 2009.

