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Vision or fiction? Prospects of regional integration in the South Pacific

Stephan Freitag

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- Following the formation of the European Union, regional economic integration has been sought as path to rapid development by several groups of developing countries. The Pacific Forum has now joined groupings of Caribbean, Latin American and African countries in turning to mutual rather than global trade to put behind it three decades of stagnation in the Pacific. But the European Union was created in unique economic and political circumstances and the experience of developing country regional integration groupings is sobering.
- Analyses of Pacific development widely agree that despite large aid inflows, living standards for most islanders have only improved slightly, if at all, since independence. This paper considers whether or not economic integration could play a role in raising living standards in the Pacific. Two main models for integration are distinguished: 'top-down integration', requiring a heavily interventionist program as opposed to more organic 'bottom-up' integration development based on island initiatives.
- Australasian, European and North American preferential trading schemes protected the South Pacific from global competition, notably in sugar and clothing. These arrangements failed because they tended to protect inefficient investments, restricted international competitiveness and lost relevance in an internationally liberal trade environment.
- The South Pacific islands also signed several inter-island trading arrangements. But the inter-island trade remains negligible not because of trade barriers but because of the limited and similar export range and the diversified imports of the islands.
- Expectations of economies of scale led to sectoral collaboration in the South Pacific. Successful integration efforts in education, business and fishing are widely agreed to be beneficial for the islands. The South Pacific urgently needs to pay attention to its transport—airlines and shipping—and telecommunication linkages. Tourism especially could be significantly expanded.
- The efforts of a huge number of foreign aid sponsored regional organisations seeking to improve collaboration among the islands lack coordination and are highly inefficient. Duplicative endeavours, notably in the form of meetings, report writing and planning of integration are incredibly wasteful.
- The facts support bottom-up integration initiated by the islands themselves. The experience of countries such as Botswana, Mauritius, Iceland and Norfolk Island are evidence that small economies can be prosperous. Focusing on their international comparative advantages these countries succeeded in exploiting the trend towards the freeing up of global trade and investment.
- Lagging economic growth can only be tackled by economic reforms in each island, such as in Samoa, to increase agricultural production and create private sector jobs. Without rising incomes and greatly improved social conditions, the Pacific is not only in grave danger of further instability but it could become a locus for international crime, and drug and arms trafficking.

Stephan Freitag is a research assistant and PhD student at the Institute for Economic Policy at Leipzig University, Germany. He spent six months researching regional integration in the South Pacific while a research intern at The Centre for Independent Studies after he had graduated in economics from Bremen University, Germany.

1. Introduction

Proposals for economic and political integration in the South Pacific are seen by some as central to the future of the Pacific. Discussion of prospects for regional trade, currency and political integration forms a large component of the academic literature devoted to the South Pacific. Multilateral and bilateral donors and Australian-Pacific business groups have also turned their attention to Pacific economic integration. Preferential market access by former colonial powers followed independence. More recently, inter-island trade agreements have been signed. The islands have attempted sectoral initiatives in air transport, shipping, fisheries and the environment, and a currency union has been mooted. The discussion of economic integration gained momentum at the launch of the *Pacific Plan for Strengthening Regional Cooperation and Integration* at the South Pacific Forum meeting in Port Moresby in October 2005. But basic questions remain. How would economic integration be achieved? And do the proposed models provide a basis for positive future growth?

Analyses of Pacific development widely agree that despite large aid inflows, living standards for most islanders have only improved slightly, if at all, since independence.[1] This paper considers whether or not economic integration could play a role in raising living standards in the Pacific. Two main models for integration are distinguished: 'top-down integration' requires a heavily interventionist program as opposed to more organic 'bottom-up' integration development based on island initiatives.

This paper looks at approaches to economic integration against the reality in trade, present examples of sectoral integration and regional organisation to evaluate whether proposals for economic integration in the South Pacific are a vision of the future or a fiction.

Analyses of Pacific development widely agree that despite large aid inflows, living standards for most islanders have only improved slightly, if at all, since independence

Top-down integration

The 'top-down' approach to regional integration is based on foreign aid and strong external ideological support. It is favoured by many academics, consultants, Pacific leaders and multilateral organisations such as the World Bank, the Asian Development Bank, United Nations organisations, the European Union and the South Pacific Forum. There are five principal and linked arguments for 'top-down' integration:

- The small and disparate nature of the South Pacific island states, compounded by limited natural resources, myriad languages and distance from external markets, is said to be a hindrance to their development. It is argued that regional integration could help overcome these difficulties.[2]
- Economies of scale and scope could be achieved by trade integration and sectoral integration. Trade liberalisation among the Pacific islands would extend the domestic market and lower prices for consumers and producers through higher scales of production. Cooperation in sectors, such as education, transport and telecommunications would reduce overhead costs and lead to greater efficiency.[3]
- Regional economic integration could act as a 'stepping stone' to global liberalisation, giving time for policy changes and reducing adjustment costs. Protecting domestic infant industries for a specified period would give them the time to become internationally competitive.[4] This follows the inward-oriented, protectionist model of regional integration.
- The Pacific islands' lack of development has created a dearth of good economic management. This could be overcome by economies of scale in integrated governance.
- Regional economic integration would lead to endogenous growth through positive multiplier effects. It is argued that while the European Union could not initially fulfil all preconditions for a currency union, it has achieved some degree of success. A similar logic would apply to the Pacific.[5]

Bottom-up integration

The 'bottom-up' approach is mostly favoured by academics. It is a development process based on island initiatives. Economic integration is not regarded as an inevitable outcome of this process. Rather, it emphasises the importance of letting the South Pacific find its own way to economic development. Four arguments oppose the above assertions:

- South Pacific islands are viable and able to be independent from aid despite their smallness and remoteness. Most Pacific islands are richly endowed with agricultural and forest land, marine resources and tourist sites. Being located in the 'rim of fire', several islands have mineral resources. The Pacific is also well located with respect to the burgeoning markets of Asia. Education is seen as the key to overcoming the economic disadvantage of hundreds of languages. Several small countries that face comparable geographic settings, such as Botswana, Iceland, Mauritius and Norfolk Island have overcome similar alleged disadvantages.[6]
- The economies of scale effects in small blocs of developing countries are not large enough to permit inward oriented market strategies.[7]
- Several studies make it clear that most regional trade integrations among developing countries have not resulted in growth but decline. All these attempts were based on foreign financial and ideological aid. The integration policies failed because they supported inwardly oriented trade that merely excluded trade with other markets.[8] Successful integrations, such as the European Union, the North American Free Trade Agreement and the Closer Economic Relations agreement between Australia and New Zealand were based on already successful economic units and their trade.
- National political stability and sound micro and macroeconomic performance are essential to successful economic integration.

The economies of scale effects in small blocs of developing countries are not large enough to permit inward oriented market strategies

Outline

Section 2 reviews economic theories of customs unions. The measures already taken toward trade integration are outlined in section 3. Sections 4 to 6 review sectoral and organisational integration, the *Pacific Plan* and further proposals for integration, including integration with Australia and New Zealand. Section 7 concludes by considering the economic integration strategy in relation to the needs of the majority of islanders.

Table 1 gives key indicators about the South Pacific islands as well as for Botswana and Mauritius, two small successful African developing countries.

Table 1: Selected key indicators

Countries	Population ('000)	Land area (km^2)	GDP per Capita (in US$)
Papua New Guinea	5,671	462,840	523
Fiji	906	18,270	2,281
Solomon Islands	552	27,550	541
Vanuatu	209	12,200	1,138
Samoa	177	2,900	1,484
Micronesia, Federated States of	108	702	1,864
Tonga	115	718	1,347
Kiribati	105	811	530
Marshall Islands	60	181	2,008
Cook Islands	21	240	2,651
Palau	21	458	NA
Nauru	13	21	NA
Tuvalu	11	26	345
Niue	2	260	NA
Botswana	1,640	581,730	3,010
Mauritius	1,241	2,040	3,860

Sources and Notes: Population and land area figures are for 2006, *CIA—The World Fact Book*; GDP per capita figures for 2003, Asian Development Bank, 2004; *Key Indicators 2003,* purchasing power parity data are not available for the Pacific; GDP per capita figures for Botswana and Mauritius are for 2002, World Bank, 2004, *World Development Indicators*.

By opening markets under Most Favoured Nation (MFN) rules, multilateral trade liberalisation contributed markedly to developing and transitional countries' access to markets and hence to their growth potential

2. Theory of integration: Customs unions

Economic theory indicates that trade increases welfare. Given reasonably competitive markets, all parties benefit from trade liberalisation by being able to exploit their comparative advantage. This theoretical understanding underpinned the post-World War II multilateral trade liberalisation GATT (General Agreement on Tariffs and Trade) Rounds that laid the foundations for a strong rise in per capita incomes, first in developed countries and then, mainly, in Asian developing countries. By opening markets under Most Favoured Nation (MFN) rules, multilateral trade liberalisation contributed markedly to developing and transitional countries' access to markets and hence to their growth potential.

The economic success of European integration stemmed from its participation in multilateral trade liberalisations that simultaneously opened up markets within Western Europe and to the outside world. Political imperatives also led to the eventual formation of the European Union to secure peace in Europe. Political as well as economic forces were also important in driving the enlargement of the European core—the Benelux states, France and Germany—to include the United Kingdom, Ireland and Denmark. Subsequent enlargements in the 1980s—Greece, Portugal and Spain—extended market access for sensitive exports such as clothing and footwear to take advantage of capital and labour mobility. In 1995, Austria, Finland and Sweden joined the European Union. The recent European Union expansion to encompass ten Central and Eastern European states was also predicated on market access, labour and capital mobility as well as political considerations.

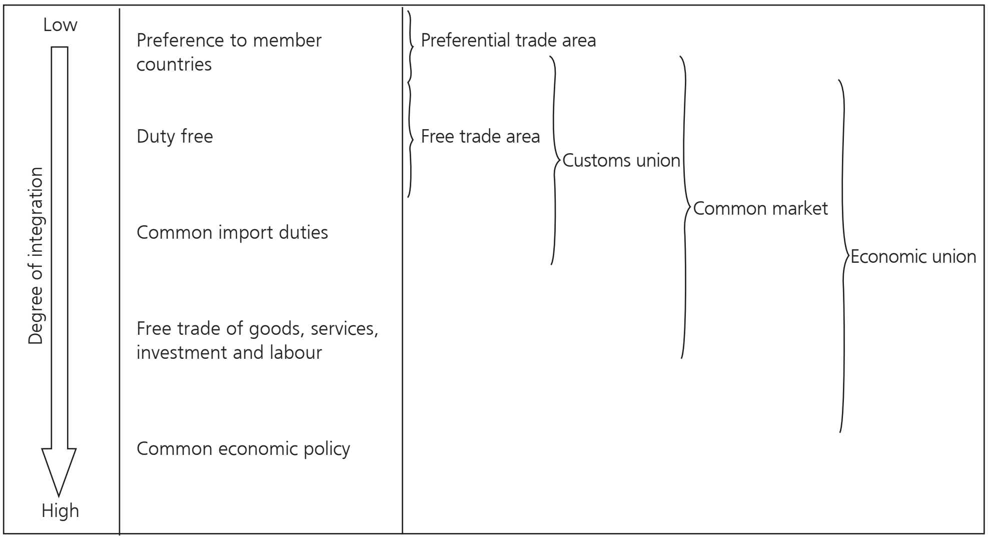
Support for European integration led to GATT Article XXIV, a provision that exempted free-trade areas from Most Favoured Nations (MFN) conditions. The United Nations Conference on Trade and Development (UNCTAD), following Prebisch and Singers's theory of import-substitution for developing countries,[9] seized on the European Community's exemption from Article XXIV to advocate protectionist regional integration among developing countries. UNCTAD argued that protection failed individual developing countries because they lacked economies of scale in production. But although integration increased market size it did not create markets that had large enough economies of scale for manufacturing.

Trade barriers between the EU and other countries were reduced but maintained or raised against other countries in regional arrangements in the Caribbean, Latin America and Africa. The resulting inward orientation led to a loss of economies of scale effects and hence to economic failure. As Viner's customs union theory predicted,[10] as well as reducing global efficiency, trade diversion swamped trade creation within the integrated areas leading to economic stagnation.[11]

More recent theoretical literature adds little precision to Viner's original 'trade creation' versus 'trade diversion' insights. Lipsey and Lancaster in 'The General Theory of the Second-Best' argued that because customs unions only lowered internal trade barriers, they were unlikely to raise global welfare.[12] Meade and others focused on the impact of integration on members. They highlighted the importance of specific trade volumes and prices but did not draw general conclusions. Wonnacott and Wonnacott argued that much of the customs union literature had little relevance for gains and losses from actual integration.[13]

Most countries begin the integration process with tariff preferences for members and move to free trade with one another while maintaining tariffs toward the rest of the world. In a customs union a common external tariff is adopted. When a customs union moves toward a common market, not only trade in goods and services, but capital and labour flow freely within the integrated area. An economic union is identified by common economic policies. If the economic union adopts a common currency, monetary policy passes to the union's central bank. This means that fiscal policies—public revenues and expenditures—must be harmonised if not unified.

Chart 1: Regional integration steps



Based on A Sell (2003): *Einfuehrung in die internationalen Wirtschaftsbeziehungen*, 2. Ed., Munich.

Economic theories of integration indicate that the Pacific islands are unlikely to form an efficient integration area. According to Krugman, successful trade integrations are between '"natural" trading partners who would have done much of their trade with another even in the absence of special arrangements' and that '"unnatural" free trade areas are highly likely to cause trade diversion rather than trade creation'.[14] The South Pacific islands are not a natural trading bloc; most of their trade is with major industrial economies as well as emerging Asian economies. The islands now export primary products to Australia, New Zealand, the United States, Europe and Japan, and import fuel, manufactures and services from traditional colonial suppliers, with Australia as a major provider.

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3. Trade integration in the South Pacific

The Pacific islands established open trading economies with low tariffs at independence. In the 1970s, ideas of planned economic development influenced the Pacific. This lead to selective increases in tariffs and the introduction of quantitative import restrictions on locally manufactured products with high effective production on products such as processed food and drinks (sugar, flour, canned food, cooking oil, processed coffee, soft drinks and beer) and some building materials (corrugated iron, paint, cement). As Fiji's tourism industry was developed as a leading export earner, the high costs of tariffs became evident. But many islands relied on customs revenues so they were reluctant to reduce tariffs.[15] The Pacific islands, nevertheless, began to turn towards trade liberalisation with Papua New Guinea, Fiji and Samoa becoming World Trade Organisation (WTO) members around 1995.

Industrial countries gave the Pacific islands reciprocal preferential access to their domestic markets. Soon thereafter, the Pacific islands signed several inter-island trade arrangements.

Extra-island arrangements

The Generalised System of Preferences

The Generalised System of Preferences (GSP), a creation of UNCTAD, was approved as another exemption to GATT's MFN rule in 1971. Industrialised countries gave preferential access to manufactures from developing countries because it was argued that it would stimulate growth by promoting their employment, skill creation and economic diversification. GSP schemes were developed with lists of tariff reductions. These were, however, limited by quotas on 'sensitive' products such as clothing, textiles, footwear and leather goods. The GSP lists interlocked with Multifibre Agreement lists that prescribe relatively high tariffs and 'voluntary export restrictions' to limit imports of products in which developing countries have the greatest comparative advantage. Australia, Canada, the European Union, Japan, New Zealand and the United States all introduced versions of the GSP in the South Pacific and elsewhere.[16] Additional preferential regional arrangements were added with developing countries of special interest. Administrative mechanisms, such as negative and positive product lists and quantitative restrictions, further complicated exports.

Lomé to Cotonou to EPAs

In 1964, the United Kingdom granted trade preferences to some of its smaller colonies for sugar, beef, veal and bananas as compensation for ending British preferences when it joined the European Economic Community (EEC) in 1973. These were incorporated in the first EEC agreement with the African, Caribbean and Pacific (ACP) states at Lomé in 1975 (Table 2). The EEC gave ACP producers annual sugar quotas at a price aligned to the EEC's internal sugar price, which was much higher than the world price. Fiji benefited greatly from the sugar protocol and Vanuatu profited from the 90% tariff reduction on beef and veal.

When the Cotonou sugar protocols ran out, ACP producers such as Fiji lost their privileged access to the European market

The Lomé agreements were marked by 'rules of origin' conditions: inputs into products such as clothing had to be sourced in partner developed countries if they were not produced locally. Fish, for instance, had to be caught in boats skippered by ACP mariners or those from partner countries. The STABEX (stabilisation of export receipts from agricultural products) and SYSMIN (stabilisation of export earnings of mining products) schemes were introduced to compensate ACP countries for lost export incomes as a result of market declines or bad weather. The Lomé Conventions also had a broader agenda to promote human rights, democratic principles, ecological compatibility, and private sector and regional cooperation.

Table 2: The South Pacific and the ACP

	Lomé I 1975	Lomé II 1979	Lomé III 1984	Lomé IV 1990	Cotonou 2000
Pacific island states signed	Fiji, Samoa, Tonga	Lomé I and Kiribati, Papua New Guinea, Solomon Islands, Tuvalu	Lomé II and Vanuatu	Lomé III	Lomé III and Cook Islands, Niue, Marshall Islands, Micronesia, Nauru, Palau

Source: European Commission, 2005, http://europa.eu.int/comm/development/body/cotonou/ overview_en.htm.

Lomé preferences on manufactured goods were eroded as tariffs on manufactures declined after the Uruguay Round of trade negotiations in 2000. More importantly, when the Cotonou sugar protocols ran out, ACP producers such as Fiji lost their privileged access to the European market.[17] The focus of the Cotonou Agreement in June 2000 shifted from trade preferences to the reduction of poverty with support for economic, social and human development, regional cooperation and integration. The Cotonou Agreement will run for 20 years but is to be reviewed at least every five years, or more often if required.

The Cotonou Agreement is to be replaced by EPAs (Economic Partnership Agreements) between individual states and groups of countries.[18]

PACTRA/SPARTECA

The Papua New Guinea-Australia Trade and Commercial Relations Agreement (PATCRA), giving Papua New Guinea free or low tariff entry for its exports to Australia, came into force in February 1977 and was renewed in September 1991 (PACTRA II). The aim, as in the other GSP schemes, was to stimulate exports of labour intensive manufactures from recipient countries. PACTRA also includes lists of exempted goods that include Papua New Guinea's principal export goods, notably gold, petroleum and timber. These carry standard, albeit low, import duties.[19] Provisions for suspending PACTRA privileges in the case of export surges that would lead to balance of payments difficulties have not been invoked.

A complementary South Pacific Regional Trade and Economic Cooperation Agreement (SPARTECA) was signed in July 1980 at the South Pacific Forum's meeting in Kiribati and came into effect in January 1981. It was subsequently incorporated into PATCRA. SPARTECA aimed to foster economic growth by providing duty and quota free access to Australian and New Zealand markets to stimulate exports and support employment and investment.

Australia and New Zealand allowed access to goods that fulfilled the 'rules of origin' except for sugar exports to Australia. 'Unmanufactured raw products' (Australia) and 'goods wholly obtained' (New Zealand) attracted preferential rates of duty and no further conditions. Wholly or partly manufactured goods had to meet two conditions: the last process of manufacture had to be performed by an island member manufacturer and not less than 45% (until 1994 it was 50%) of the total manufacturing cost had to be in the Pacific. The 'rules of origin' were criticised as being harmful because the islands' manufacturing industries relied heavily on external materials to be competitive, making it difficult to remain under the 45% threshold.

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Further trade agreements followed. An Australian-Fiji Trade and Economic Relations Agreement was signed in March 1999 as well as a Caledonia Trade and Economic Relations Agreement between Australia and New Caledonia in March 2002.[20]

Compact of Free Association

The United States entered into a Compact of Free Association with the Federated States of Micronesia and the Marshall Islands in 1986, and with Palau in 1994. The Compact was renewed in May 2004 to run until 2023. Trade preferences for exports to the United States were embedded in the initial compacts. Associated Pacific islands' goods entered the United States duty free if they were imported directly and if at least 35% of the import value was produced in the Pacific. Some items of clothing, agricultural products and some technical products were excluded. Tuna and skipjack imports from Pacific signatories, for example, were restricted to no more than 10% of the previous year's US consumption. These provisions and restrictions were similar to those that apply to other US associated states such as Puerto Rico.

Within a general framework of improving economic development, self government and national security in the Pacific, the United States also committed itself to defence and economic assistance. Importantly the associated states received privileged immigration access to the United States.[21] The Free Association Compacts specify aid to Micronesia of US$90 million, to the Marshall Islands of US$60 million a year and to Palau of US$450 million over 15 years. In return, the United States is permitted to deploy troops, undertake field exercises and test missiles until 2066 with an option to extend to 2086. All claims arising from US nuclear tests at Bikini and Enewetak Atolls from 1946 to 1958 were deemed to be settled. The island governments are not permitted to act contrary to these security and defence responsibilities.[22]

Inter-island arrangements

Many trade arrangements have been signed among the Pacific islands. There are reciprocal trade agreements among Fiji, Vanuatu and Papua New Guinea and there are non-reciprocal trade agreements between Fiji and the islands of Tonga, Tuvalu, the Cook Islands, Kiribati and New Caledonia. The Solomon Islands have also begun to negotiate a bilateral agreement with Fiji. Fiji and Tonga signed a handicraft duty free agreement in 1986.

The most notable inter-island trade arrangements are covered below.

The Melanesian Spearhead Group

The Melanesian Spearhead Group Trade Agreement (MSG) was initiated and developed by the leaders of Papua New Guinea, the Solomon Islands and Vanuatu. Although the MSG Trade Agreement negotiations were overshadowed by the civil conflict on Bougainville that nearly caused military confrontation between Papua New Guinea and the Solomon Islands, the agreement was nevertheless signed in July 1993, with Fiji joining in 1998. Initially the products falling under the agreement were tea from Papua New Guinea, beef from Vanuatu and canned tuna from the Solomon Islands. After Fiji joined in 1996, more products were covered. The agreement consisted of a positive list of more than 150 commodities on which trade barriers were to be reduced. Escape clauses permitted the suspension of the agreement to defend a country's balance of payments and to protect new industries. It is claimed that trade in beef, coffee and kava slightly increased among the MSG members.[23] When the Solomon Islands and Vanuatu had sizeable trade deficits with Papua New Guinea and Fiji, they temporarily withdraw from MSG.[24]

The Pacific Island Countries Trade Agreement claims to reduce and finally eliminate tariffs on all goods imported from member states, but exemptions are rife

The Pacific Island Countries Trade Agreement

A region-wide trade organisation was formed by the Pacific Island Countries Trade Agreement (PICTA). PICTA aimed 'to improve the economic and social living standards of all people in the region'.[25] Ten countries—Papua New Guinea, Fiji, Solomon Islands, Samoa, Tonga, Cook Islands, Kiribati, Vanuata, Nauru and Niue—signed PICTA as well as an umbrella agreement, the Pacific Agreement on Closer Economic Relations (PACER), with Australia and New Zealand in August 2001. The treaty has been ratified by the ten member states. The three countries in Free Association with the United States, the Federated States of Micronesia, the Marshall Islands and Palau will be permitted to enter PICTA and PACER if 'they make reasonable efforts to secure a waiver of their obligation to provide MFN treatment to the United States'.[26] Tuvalu is yet to sign the agreement.

PICTA claims to reduce and finally eliminate tariffs on all goods imported from member states, but exemptions are rife. The tariffs were to be lowered in two-year-steps to zero by 2010 for most members, and by 2012 for 'least developed' members (Kiribati, Samoa, Solomon Islands, Vanuatu and Tuvalu) and small island states (Cook Islands, Nauru, Niue and the Republic of Marshall Islands). PICTA also contains a negative list that allows for a slower reduction of tariffs for 'sensitive' industries. In addition most countries claim agricultural products and clothing as exempted imports. All rights to other trade agreements of its members including the Cotonou Agreement, SPARTECA and Agreements of Free Association are accepted by PICTA.

4. Sectoral integration in the Pacific

Expectations of economies of scale in tertiary education led to the first effective sectoral collaboration in the Pacific. The Pacific islands also have common interests in aviation, shipping and communication infrastructures to minimise the costs of their transactions with principal markets. Maintaining fish and other marine product stocks in a sustainable environment received early recognition. Several specialised agencies have been formed to promote regional cooperation.[27]

Education

The founding of the University of the South Pacific (USP) in 1968 was one of the earliest and most successful Pacific-wide activities. It cooperates with the Fiji School of Medicine which was founded in 1885 to provide medical training. The university has a main campus in Suva and additional campuses in Samoa, Tonga and Kiribati. It complements the University of Papua New Guinea in Port Moresby and the Papua New Guinea University of Technology in Lae. A South Pacific Board for Education Assessment was created in 1980 to introduce region wide educational standards. The Pacific island development programme, an initiative of the East-West Centre of the University of Hawaii, works on development cooperation with the United States.[28]

Transport

The Pacific airlines are maintained by country restrictions on landing rights

Low population density and long distances make South Pacific air transport costly. A pre-independence effort by Australia, Great Britain, New Zealand and Fiji in the late 1960s created Air Pacific as a regional carrier by expanding Fiji Air services. Great Britain's Solomon Islands and Tonga, New Zealand's Western Samoa and Australia's Nauru joined as shareholders. However, it soon became obvious that Fiji was the only Pacific island interested in the further development of Air Pacific, which eventually became Fiji's national airline. The other countries were intent on their own separate national airlines.[29]

The Pacific islands have been preoccupied with air transport since independence because it dominates passenger traffic and provides a substantial component of goods transport. The French territories are serviced by Aircalin (a subsidiary of Air France) and the American associated territories by United Airlines. Papua New Guinea, Fiji, Samoa and Tonga opted for publicly operated national airlines. Some later formed partnerships with Qantas and other international airlines. Most of these national airlines have consistently made financial losses. The Tongan airline collapsed in 2004.[30] Nauru established its own airline. It was losing $40 million a year during the 1980s and 1990s, squandering Nauru's phosphate earnings; it now operates with aid from Taiwan. Some national airlines run intra-island services and there are also small private independent operators. The Pacific airlines are maintained by country restrictions on landing rights. They create the framework for an inefficient oligopoly that limits services and charges high prices to the detriment of island travellers and tourism. Virgin Blue's recent entry to routes from Australia and New Zealand to Fiji, Vanuatu, Samoa, Tonga and the Cook Islands has markedly reduced prices.

The Pacific Islands Air Services Agreement (PIASA) was signed by Vanuatu, Samoa, Tonga, the Cook Islands and Nauru to overcome air service problems; Fiji has not yet joined. PIASA aims to liberalise the South Pacific aviation market incrementally but no such progress has been made.[31]

Shipping

The Pacific Forum Line was established in 1977 and is owned by 12 Forum member governments. It was established to insure shipping transport in the South Pacific when containerisation emerged in the late 1970s. It owns a fleet of eight vessels linking Australia, New Zealand and the South Pacific islands. Nauru has its own government owned shipping line but it has never made a profit.[32] It operates seven vessels on nearly the same routes as the Pacific Forum Line. In the early period, mismanagement led to substantial losses. Since the late 1980s the Pacific Forum Line has become profitable but private shipping would almost certainly operate more efficient services.

Telecommunications

Cooperation in telecommunications in the South Pacific is limited. Several plans for the common regulation of telecommunication services have been released by Forum meetings and sector organisations since 1999. The Pacific Islands Telecommunications Association and the APT Telework-P are the two dominant regional players among several organisations involved in telecommunications in the Pacific. Improving telecommunication services by establishing cooperation among the national telecommunity entities or by standardisation is a common objective.[33] But thus far the many plans put forward have amounted to nothing.

Fishing

The Forum Fishing Agency, founded in 1979, supports the management of island fisheries and their future development. The Agency assists member countries negotiate the substantial incomes they receive from the sale of fishing licences to the United States, Japan, Taiwan and other countries. The Agency also has a vessel monitoring program to prevent poaching and illegal catches. Its support for publicly owned national fleets has been less successful. The Forum Fishing Agency was reviewed at New Zealand's request in 2005, leading to a marked increase in member contributions. The Agency cooperates with the South Pacific Community in fostering scientific work on fish resources and the Pacific Forum on trade and investment.[34]

Several plans for the common regulation of telecommunication services have been released but thus far the many plans put forward have amounted to nothing

Environment

The South Pacific Applied Geoscience Commission was established by the United Nations in 1972 and became autonomous in 1984. There are 18 island members plus Australia and New Zealand but it is largely donor funded. The Commission was initially interested in offshore mineral exploration, including petroleum, but has broadened its range of geoscience interests to include water management and community natural disaster risk management. The Commission's interests overlap with the South Pacific Regional Environment Programme which was founded the following year, in 1973. This is a much smaller programme that monitors island ecosystems, environment and climate change and the interaction between human activity and the environment.[35]

Business development

The South Pacific Tourism Organisation (SPTO) was founded to assist the development of the potential for tourism in the region. The organisation focuses on the marketing of the South Pacific. It regularly publishes analyses of tourism and is engaged in coordinating regional Pacific marketing and representing South Pacific tourism in the United Kingdom, Germany and the United States. The SPTO's website provides a comprehensive listing of accommodation and other tourist news. It is private enterprise oriented and less dependent on donor funding than other Pacific organisations.[36]

5. Regional Pacific organisations

Regional organisations date back to the colonial period when the colonial powers saw merit in exchanging information and experience. Table 3 summarises the most important Pacific-wide organisations in three categories. The first category, 'the core group', includes organisations interacting with national and international governments and NGOs. A second category covers the commercial support organisations, notably the South Pacific Tourism Organisation. The third group includes the educational organisations.

Table 3: Pacific Organisations, 2005

	Year founded	Members	Core task	Staff	Budget ($US million)
Category 1: Organisations interacting with national and international governments and NGOs					
Secretariat of the Pacific Community	1947	22 Pacific islands, Australia, New Zealand, France, United States	Economic and social development	284	30
Pacific Islands Forum	1972	14 Pacific islands, Australia, New Zealand*	Economic, social and political development, regional integration	90	15.6
South Pacific Applied Geoscience Commission	1972	16 Forum members, plus 3 other island associates	Sustainable development, poverty alleviation	80	8.2
South Pacific Regional Environmental Program	1973	22 Pacific islands, Australia, New Zealand, France, United States	Sustainable development	70	9
Forum Fisheries Agency	1979	16 Forum members, Tokelau	Sustainable fisheries	55	4.0
Category 2: Commercial support organisations					
South Pacific Tourism Organisation	1980	11 Pacific islands, Australia, New Zealand, United States, France, Britain	Tourism	10	>0.6
Category 3: Educational organisations					
Fiji School of Medicine	1885	Fiji	Tertiary teaching and research	NA	NA
University of the South Pacific	1968	12 Pacific islands	Tertiary teaching and research	>900	NA
South Pacific Board for Education Assessment	1980	9 Pacific islands, Australia and New Zealand	Education	15	>0.6
Pacific Islands Development Program	1980	21 Pacific islands	Research on trade and development	35	NA

Notes and Source: Based on A.V. Hughes, 2005, *Strengthening Regional Management: A Review of the Architecture for Regional Co-operation in the Pacific*, Report to the Pacific Islands Forum, Consultative Draft; *: French Polynesia and New Caledonia have observer status.

The Secretariat of the Pacific Community's principal function has been to maintain contact between the Francophone and Anglophone islands by operating in both languages

South Pacific Commission to Secretariat of the Pacific Community

The South Pacific Commmission was founded in 1947 on the initiative of the Pacific colonial powers Great Britain, France, the United States, Australia and New Zealand with headquarters in Noumea, New Caledonia. It embraced all 22 Pacific island territories 'to help Pacific Island people make and implement informed decisions about their future'.[37] The Commission undertook a variety of sectoral activities, most prominently in the land resources, agriculture and health sectors. Over time, the Commission metamorphosed into the Secretariat of the Pacific Community (SPC). In the 1990s, the new SPC took responsibility for organising Pacific data with an Internet program called 'Prism' that linked island statistical offices. The SPC helped statistical offices with computers and organised seminars in Noumea for statistical staff. The SPC's principal function has been to maintain contact between the Francophone and Anglophone islands by operating in both languages. The SPC has, however, gradually been overtaken by the Pacific Forum.

The Pacific Forum

The Pacific Trade Bureau, founded in 1972, became the Pacific Forum Secretariat in 1988 and evolved into the Pacific Forum in 2000, increasingly considered the pre-eminent Pacific-wide organisation. Ministerial meetings grew into annual meetings of the heads of the governments of the independent and self-governing Pacific countries, and Australia and New Zealand. The Forum's mission is stated as 'the enhancement of social and economic living conditions of the South Pacific population' with the support and cooperation among governments and international agencies that represent the collective interests of the Forum.[38]

The decisions made at the annual meeting are implemented by the Pacific Islands Forum Secretariat based in Suva, Fiji. The Forum's management board consists of a Secretary General and two deputies. The Secretary General chairs the Council of Regional Organisations in the Pacific (CROP) that represents the principal regional organisations in the Pacific. The Forum Secretariat's activities are monitored by the Forum Officials' Committee made up of representatives of the Forum governments. The Forum Secretariat is predominantly financed by aid from donor countries as well as by member governments. The Forum Secretariat has several divisions:

- Some divisions have a more political orientation such as the Division for Development Cooperation and Coordination, the Political, International and Legal Affairs Division and the Division for Regional Coordination's. These divisions are responsible for preventing waste of resources, international relations, legal affairs and security issues.
- Other divisions are more economically orientated such as the Corporate Services Division, the Economic Analysis and Development Planning Division and the Trade and Investment Division. They act in development programs, economic analysis and trade management.

A review in 2004 of the Forum emphasised that economic growth, sustainable development, good governance and security were key to improving living standards

A review in 2004 of the Forum by an Eminent Persons Group emphasised that economic growth, sustainable development, good governance and security were key to improving living standards.[39] It noted the Secretariat's dual role in supporting Forum leaders in their endeavours and developing an agenda for the Forum.

The Council of Regional Organisations in the Pacific

The Pacific Forum replaced the South Pacific Organisations Coordinating Committee with the Council of Regional Organisations in the Pacific (CROP) in 1988 to improve cooperation, coordination and collaboration among regional groups in the Pacific. CROP meets once a year and draws together the ten most important Pacific-wide organisations in education, government and commercial support. In 2005, CROP member organisations had more than 1500 employees with an annual budget, mostly aid funded, of more than $US68 million.

6. Plans for the Pacific

The Pacific Plan for Strengthening Regional Cooperation and Integration

The Forum Leaders' April 2004 intention to 'strengthen regional cooperation and integration' culminated in *The Pacific Plan for Strengthening Regional Cooperation and Integration* presented by the Pacific Forum Secretariat to the Pacific forum meeting in October 2005 in Port Moresby.[40] The plan is 'to enhance and stimulate economic growth, sustainable development, good governance and security for Pacific countries through regionalism.' It does not imply any limitation on national sovereignty and it is not intended to replace any national programmes, only to support and complement them. The Plan argues that a regional approach should be taken only if it adds value to national efforts.

The immediate implementation for a 2006–8 timetable includes:

- extension of the trade in goods under the aegis of SPARTECA, PICTA and PACER and with non Forum trading partners;
- integration of trade in services, including temporary movement of labour into PICTA and the EPA;
- timely and effective implementation of the regional Trade Facilitation Programme;
- implementation of the Forum Principles on Regional Transport services including development of the Pacific Aviation Safety Office;
- investigation of the potential impact under PACER of a move towards a comprehensive framework for trade (including services) and economic cooperation between Australia, New Zealand and Forum Countries; and
- support of private sector mechanisms including the Pacific Islands Private Sector Organisation.

Despite some acknowledgment of the costs of regionalism, the Pacific Plan recommends regional integration, arguing that development in the Pacific must proceed through regional market integration. The priority is for the implementation of PICTA and PACER.

The future of regional integration is seen by the Forum Economic Ministers as 'building a relationship with the rest of the world'. Further examination of Pacific labour market issues, including labour market mobility through the region and beyond is another driver of regional integration. The Forum Trade Ministers decided to commission a joint study to investigate the potential impacts of a move towards a comprehensive framework for trade and economic cooperation between Australia, New Zealand and Forum Island countries. The *Pacific Plan* concludes: 'A successful regionalism requires larger markets to stimulate growth; partnership with Australia and New Zealand is crucial for Pacific regionalism to be viable.'

The Pacific Regional Order

Building on the Pacific Plan, Bob Sercombe, the Australian Labour Party (ALP) spokesman for Pacific Affairs, introduced the prospect of early integration of the Pacific Island countries with Australia and New Zealand into the public debate, drawing heavily on Dave Peebles's detailed prescriptions for integration in his Pacific Regional Order monograph.[41]

The Sercombe/Peebles model not only integrates Pacific Forum island countries into Oceania, but also French Polynesia, New Caledonia, Wallis and Futuna, Guam, American Samoa, the North Mariana Islands and Timor Leste. The model assumes that the PICTA and PACER programmes quickly result in a free trade area, with Australia and New Zealand assisting in the introduction of value added taxes to make up for losses in customs revenues. Sercombe and Peebles find a customs union unlikely to be workable because island governments would not wish to adopt low Australian tariffs and because Australia would not wish to adopt low New Zealand tariffs.[42]

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Nevertheless, Sercombe and Peebles continue to argue that the concept of extending the CER (Australia-New Zealand Cooperation Agreement) into a fully fledged economic community with the Pacific islands is workable. They envisage the Pacific Islands Forum becoming the Pacific Community and the Forum Secretariat being transformed into the Community's Commission. Becoming a community would mean not only the free flow of goods, services and investment, but also of labour. This is all despite difficulties with continuing rules of origin and other trade restrictions, with free trade in services and with the flow of investment into islands where individual land titles and property rights are not established.

Furthermore, the model sees the Pacific Community developing into an economic union with a common currency and monetary policies. An Oceania currency would replace the Australian, New Zealand and Fiji dollars, the Vatu, Tala, and Kina. It is argued that with a free labour market and the diversification of the Australian and New Zealand

Lomé sugar protocols protected the Fiji sugar industry from world market forces. But they also allowed domestic policies to evolve that led to lagging investment in sugar technology and processing

economies the principal economic objections to currency unions would be overcome.

The Sercombe/Peebles model sees advantages in a unified approach to security, human rights and the rule of law that would follow from the adoption of the regional integration model. Their argument culminates with an Oceanic Parliament based on a combination of the European Parliament (direct elections) and the Nordic Council (the functions and form but not the powers of a national parliament) that would initially have an advisory and supervisory role. Sercombe and Peebles consider the prospects for the Oceanic Community so attractive that they envisage it being joined in the future by a wider range of countries: Brunei, Indonesia, the Philippines and Singapore in phase two, and Japan in phase three.[43]

7. Analysis

The impact of trade arrangements

Exports have grown in most of the South Pacific Islands, but lag behind the growth rates of strongly growing developing countries. Botswana has moved from half to twice Papua New Guinea's per capita income between 1975 and 2005. During the same period Mauritius' per capita income also moved from half to twice Fiji's. Rapidly growing Asian countries also show per capita exports far exceeding Pacific islands' capital exports.

Table 4: Recent Pacific merchandise and service exports per capita, as a share of GDP and real growth rates

Countries	Exports per capita US dollars	Exports/GDP	Average real export growth rates 1975–2005*
Papua New Guinea	515	66	2.8
Fiji	1054	56	2.5
Solomon Islands	300	59	5
Vanuatu	186	12	3
Samoa	328	3	5
Tonga	313	9	2.7
Micronesia Fed Republic	169	9	NA
Kiribati	86	15	NA
Marshall Islands	155	9	NA
Mauritius	2884	55	8.8
Botswana	2113	40	10.3

Sources: The most recent available data was used (data are from various years between 2001 to 2005), from IMF for Papua New Guinea, Solomon Islands, Fiji and Vanuatu, *Statistical Yearbook 2006,* available at http://ifs.apdi.net.im; for Samoa and Tonga from World Trade Organisation, *Statistical Database*, available at http://stat.wto.org and for Kiribati and Marshall Islands from Asian Development Bank, *Key Indicators 2006*, www.adb.org; Real export growth data calculated from IMF, *Financial Statistics*, www.imfstatistics.org; *: 2005 constant US Dollars.

Table 4 also shows that the often quoted ratio of exports to GDP is not a meaningful economic indicator. It is influenced by a country's size and its export effort. Small countries tend to have higher export to GDP ratios than large countries; for small, undeveloped countries, exports have a strong influence on GDP.

The impact of the extra-island arrangements has been marginally positive. Lal and Rita argue that the Lomé sugar protocols protected the Fiji sugar industry from world market forces. But they also allowed domestic policies to evolve that led to lagging investment in sugar technology and processing. As a consequence, productivity in the Fiji sugar industry fell well behind world levels. When the Lomé protocols ended, Fiji sugar growers were unable to compete.[44] Overall the share of imports from the ACP countries to the EU dropped from 6.7% in 1975 to 3% in 1998 clearly showing that the arrangements were ineffectual in most countries.[45]

Expatriate firms attempted to take advantage of PATCRA by utilising the ample supply of labour in Port Moresby to produce clothing for the Australian market. However, the onerous local industrial relations legislation made the labour costs too high for the level of labour productivity. They did not persevere.

A New Zealand entrepreneur established a successful sweater knitting firm in Tonga before SPARTECA, substantially increasing job availability in Nuku'alofa and contributing to exports. The manufacture of clothing responded to American trade preferences in the Micronesian Federal Republic but was dependent on protection from more competitive producers in Asia. The Micronesian island producers did not move up-market to higher quality products as other established producers did to meet the competition from China. When the Uruguay Round unwound the Multifibre Agreement, these clothing exports began to collapse.

In Fiji, industrial relations legislation also kept wages above labour productivity until the political coup in 1980 led to high unemployment and a sharp increase in urban poverty. Women began to work below official wage rates, permitting local and foreign investment in clothing production for export. Some of the Fijian exports replaced those from the Cook Islands to New Zealand. Fiji, unfortunately sheltered behind the preferences that SPARTECA provided and also failed to move up market. As New Zealand and Australia reduced their clothing tariffs in the 2000s, Fiji's manufacturers have found it difficult to compete with Asian exporters.

The effects of inter-island arrangements are even smaller than those of extra-island trade preferences. Trade between the Pacific islands was, and remains, very small

A more successful Japanese investment in Samoa took advantage of the SPARTECA margin to produce electrical harnesses for the Australian motor vehicle industry. This enterprise employs 2,000 workers and is incorporating technological developments to remain competitive.

In sum, most preferential trade arrangements in developing markets failed because they tended to protect inefficient investments, restricted international competitiveness and lost relevance in an internationally liberal trade environment.

The effects of inter-island arrangements are even smaller than those of extra-island trade preferences. Trade between the Pacific islands was, and remains, very small (Table 5). When re-exports from larger to smaller islands are taken into account, as for example from Fiji to Tuvalu, the remaining inter-island trade is negligible.

Table 5: Trade among South Pacific islands as a percentage of total trade, 1998–2002

	1998	1999	2000	2001	2002
Papua New Guinea	0.5	0.4	0.6	0.3	0.3
Fiji	2.1	2.8	3.4	3.7	3
Solomon Islands	5.1	4.4	8.2	4.4	5.1
Vanuatu	7.1	5.3	13.4	3.2	1.9
Samoa	11.9	12.3	13	10	14.2
Tonga	7.3	8.8	9.7	17.1	17
Federated States of Micronesia	0	0	NA	NA	NA
Kiribati	8.7	11.4	10.7	11.9	9.1
Marshall Islands	0.7	1	1	NA	NA
Cook Islands	10.8	9.8	15.7	9.7	5.6
Palau	NA	NA	NA	NA	NA
Nauru	NA	NA	NA	NA	NA
Tuvalu	58.4	57.2	56	62.5	51.1
Niue	NA	NA	NA	NA	NA

Source: K Bunyaratavej and TK Jayaraman, 2005, *A common currency for the Pacific Region: A feasibility study,* USPEC working paper.

The arrangements have clearly not contributed to export growth and hence to overall growth. Some tariffs were reduced when countries joined the WTO:[46] however, protection on domestically produced manufactures remains high. Inter-island trade is not small because of trade barriers, but because of the limited and similar export range and the diversified imports of the islands.

The impact of regional organisations

A.V. Hughes, former Governor of the Reserve Bank of the Solomon Islands, was commissioned by the Pacific Islands Forum Secretariat to review the 'architecture' for regional cooperation in the Pacific for the *Pacific Plan.* Noting that 'there are hundreds of regional organisations in the Pacific, with new ones appearing all the time and a smaller number passing away as specific regional needs wax and wane', Hughes focused on the five principal organisations.[47]

Finding egregious overlaps in the considerable output of 'reports' that occupy four of five organisations, Hughes made two main recommendations. First, increasing cooperation in place of each organisation's present autarchy, followed by rolling all five organisations into a Pacific Commission would make coordination and cooperation in the Pacific far more efficient. Second, he considered the Council of Regional Organisations overly bureaucratic, inept and in need of reform.[48]

It is appalling that after 30 years of independence, most of the senior staff of all the Pacific organisations are expatriates

It is appalling that after 30 years of independence, most of the senior staff of all the Pacific organisations are expatriates. Their duplicative report writing also calls into question whether the Pacific islanders employed by these organisations do not have high opportunity costs in terms of participating in short-staffed island administrations.

Impact of sectoral integration

Successful integration efforts in education, business and fishing are widely agreed to be beneficial for the islands. Yet, there is no integration in air transport. Against the background of the remoteness of the islands, falling international transaction costs, and the increasing importance and great potential of tourism in the South Pacific this is a serious brake on economic growth. The aims of the air liberalisation agreement PIASA are laudable and should be pursued as a bulwark against Pacific rent seeking attempts. A free skies policy would not only improve the potential for tourism, but also represent an important step towards economic integration into the world economy. Transparent subsidies for passenger, mail and freight would be much more efficient than implicit subsidies for national airlines.

Integration in shipping has only been relatively successful with the Pacific Forum Line. Government owned shipping crowds out private shipping in the South Pacific. A free market in shipping would be far more stimulating for trade with the outside world.

No integration has yet taken place in telecommunications. Telecommunication networks are absolutely necessary for economic development. It is imperative to extend the telecommunications infrastructure and to establish Pacific-wide regulation to oversee competition. Moreover, a telecommunication infrastructure serves as an essential base for development in key sectors for economic development such as education and business. A Pacific-wide regulatory authority would guarantee workable competition and would lead to price decreases in telecommunications.

To prevent egregiously wasteful duplication in the environmental sector, a reduction in the number of organistions is crucial. The South Pacific Applied Geoscience Commission overlaps with the South Pacific Regional Environment Program and several other organisations. Considerable savings to donor taxpayers would result from a rationalisation of these organisations.

8. Conclusion

The facts only support bottom-up integration initiated by the islands themselves. Falling international passenger, freight and communication costs are reducing the South Pacific's distance from its markets. The experience of countries such as Botswana, Mauritius, Iceland and Norfolk Island are evidence that small economies can be prosperous. Focusing on their international comparative advantages they succeeded in exploiting the trend towards the freeing up of global trade and investment. The Pacific islands are competitive in agricultural, tourist, timber, mineral and marine exports. The most profitable niches in world markets for these products are likely to be found in old industrial countries and in rapidly growing industrialising countries in Asia.

The Pacific market as a whole is too small for economies of scale through integration. Actual and prospective inter-island trade is extremely limited. Regional integration will therefore not work as a 'stepping-stone' to wider trade access. Increased inter-island trade would lead to trade diversion if investment is attracted by raising regional tariffs. Trade diversion would reduce growth below its low present rates.

Economy of scale effects are possible in some sectors. They have been successful in education and business, and regional cooperation in air transport and telecommunications has strong potential. But cooperation on such a scale does not necessarily imply overall political and economic integration. On the contrary country initiatives, political will, and understanding are important for the pursuit of these objectives.

Actual and prospective inter-island trade is extremely limited. Regional integration will therefore not work as a 'stepping-stone' to wider trade access

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