

Structural transformation in Asia-Pacific small island developing States

Asia-Pacific small island developing States (SIDS) face various challenges concerned with their structural economic transformation and indeed their overall development trajectory. The *Asia-Pacific Countries with Special Needs Development Report: Structural Transformation and its Role in Reducing Poverty* examines those development challenges and offers policy recommendations.

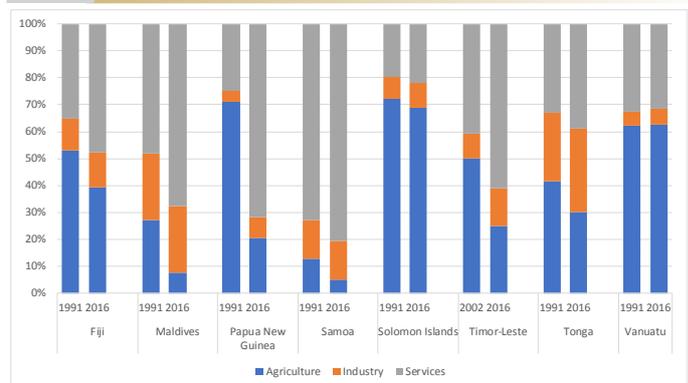
The dominance of the services sector characterizes the employment structure of SIDS. This is partly due to their large government sector and efforts to establish tourism as the basis of their economies. However, it is also a reflection of the difficulty that most SIDS face in promoting viable industrial activities. Because of their geographical isolation and small size, which translates into lack of economies of scale and high costs to reach international markets, the potential for developing a large manufacturing hub or for the integration into global value chains (GVCs) is severely limited.

Some SIDS, such as Solomon Islands and Vanuatu, remain structurally underdeveloped as agriculture still accounts for the largest share of employment. While most others have transformed their economies from agriculture-based to services-based, they have bypassed, in the course of the process, the dynamism of the manufacturing sector. In Papua New Guinea, for example, the employment share of agriculture declined from 71 per cent in 1991 to 21 per cent in 2016. Over the same period, the share of the industry sector increased only marginally from 4 per cent to 7 per cent. Similarly, in Samoa, more than 80 per cent of the labour force works in the services sector today, while the agriculture and industry sectors account only for 5 and 14 per cent, respectively.

One concern with this pattern of structural transformation is the increasing informality in the services sector. While there is no denying that the informal sector plays an essential role in providing jobs and reducing poverty in the short run, it tends to provide only low-wage, low productivity jobs.

Furthermore, the informal sector reduces resources available for governments' redistributive policies and can end up locking workers into poverty in the long run. A lack of policy actions to address informality also has a particularly detrimental impact on gender equality, as women are more likely to be employed in the informal sector than men in most developing countries. Productivity enhancements within the services sector must therefore be examined in greater detail, with a view to expanding high-productivity services. This is especially relevant in SIDS, where immutable factors such as distance and lack of economies of scale are likely to limit the potential of manufacturing to serve as the backbone of economic development.

Figure 1. Trends in employment shares in the Asia-Pacific small island developing States, 1991-2016



Source: ESCAP, based on data from ILO-STAT.

Note: Data for 2002 and 2016 were used for Timor-Leste.

Blue Economy, tourism and agriculture

In SIDS, targeting specific subsectors (or even products) for development is more relevant than targeting entire sectors because the lack of economies of scale limits the potential of these small economies to spur economic diversification. Yet, policy considerations for aligning structural transformation with poverty reduction differ, depending on the subgroup of SIDS. The *Asia-Pacific Countries with Special Needs Development Report: Structural Transformation and its Role in Reducing Poverty* acknowledges this and proposes various

policy solutions that are related to SIDS' natural advantages and the necessity to develop productive services, modernize the rural economy and preserve the natural environment.

While small land masses constrain the economic growth of SIDS, the vast area of ocean that falls within their jurisdiction can provide them with extensive revenues. For 12 Asia-Pacific SIDS, the total area of their exclusive economic zones (EEZs) amounts to 16.8 million square kilometres, 31 times their landmass. Many governments of Pacific SIDS have already started to focus on sustainable ocean management, programmes and policies (Keen and others, 2018). This concept, known as the "Blue Economy", focuses on the potential of the fishery sector for small-scale fisheries, urban fish markets and onshore tuna processing. This approach, however, must ensure that the interests of local populations are adequately served, the natural environment is protected, and that the sector's development is sustainable. At the moment, there is a significant disparity between the license fees paid to SIDS for using their EEZs and the value of fish caught. In 2014, the 12 small island developing Pacific Governments' revenue received from access fees was approximately \$331 million, whereas the value of the extracted tuna therein was approximately \$2.5 billion in 2016. Sustainable fishery is more relevant for States in Micronesia and Polynesia, such as Kiribati, Marshall Islands, Nauru, and Tuvalu, whose small landmass and geographic isolation prevent the development of other sectors.

Second, environmentally sustainable tourism may be the main sectoral target among larger Asia-Pacific SIDS. Tourism is already a key component of several national development plans, and a number of States have increased their tourism capacity significantly. Despite their remoteness and isolation, which translates into costly transport and development, revenues from tourism account for up to 30 per cent of GDP in Fiji, Samoa and Vanuatu, while in Palau

they reach 58 per cent. However, in the other Pacific SIDS, tourism is still in a relatively early stage of development. Structural transformation towards tourism as the main sectoral target must ensure productivity gains, hence the necessity to make the tourist industry a high-value, high-end focused, and environmentally sustainable endeavour, similar to that in the landlocked and mountainous Bhutan.

Third, for the larger of the Pacific SIDS based in Melanesia, commercialized, high-value agricultural niche products for export could further be explored, hence the call for rural modernisation. Good examples include beef production in Vanuatu and sugarcane in Fiji. However, the environmental aspects need to be better mainstreamed into agricultural practices to ensure sustainability of production. Increased investments in irrigation infrastructure and soil fertility conservation are also urgently needed.

The role of the international community

Development challenges in SIDS cannot be addressed without an active engagement of the international community. SIDS are particularly susceptible to the impacts of climate change, which can hamper their efforts directed at achieving sustainable development and undergo structural transformation. As climate change threatens the very existence of many SIDS, the international community therefore has an obligation to help.

Concerted actions to address the consequences of climate change must be taken. Actions can include the introduction of carbon pricing instruments and energy subsidy reforms, promoting public and private partnerships for low-carbon, climate-resilient infrastructure investments, and improving transboundary climate data collection. The international community must also assist SIDS in mitigating and adapting to climate change by scaling up available resources climate action and providing disaster risk transfer and financing instruments.

The MPFD Policy Briefs aim at generating forward-looking discussions among policymakers, researchers and other stakeholders to help forge political will and build a regional consensus on needed policy actions and pressing reforms. Policy Briefs are issued without formal editing. The content of this issue, prepared by Andrzej Bolesta and Yusuke Tateno, and, is in part based on material from *Asia-Pacific Countries with Special Needs Development Report: Structural Transformation and its Role in Reducing Poverty* (Sales No. E.19.II.F.5). This policy brief benefited from comments by Oliver Paddison, Jose Antonio Pedrosa Garcia and Nyintob Pema Norbu. For further information on this issue, please contact Hamza Ali Malik, Director, Macroeconomic Policy and Financing for Development Division, ESCAP (escap-mpdd@un.org).