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Asia-Pacific Small Island Developing States: Development challenges and policy solutions[+]

by

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Abstract

Asia-Pacific small island developing States (SIDS), are a diverse group, despite the broad perception to the contrary. Nevertheless, although they differ in size of landmass, population, national economies and the level of development, they share common development challenges. Those challenges can be classified as economic (small sized, undiversified economies, remotely located and exposed to external shocks), environmental (existential threats related to climate change and environmental degradation), political (ethnic conflicts and political instability) and social (violence towards vulnerable groups). Some of the challenges – such as environmental and economic vulnerabilities – cannot be addressed without concerted efforts and the support of the international community. This support is framed within the United Nations' programmes of action, and more specifically, the SAMOA Pathway for SIDS (2014-2024) and the Istanbul Programme of Action for Least Developed Countries (LDCs) (2011-2021). The solution to the development predicaments of SIDS also lies in a particular type of structural economic transformation, which does not follow the traditional path from agriculture to industry and then to services. As building a manufacturing base in remote islands located far away from global markets is not a viable option, structural transformation in SIDS must be well targeted and aimed at productive, niche services and modernised agriculture and fishery, and at utilising the resources of their exclusive economic zones. This sectoral development of both sectors, if accompanied by productivity gains, will effectively enhance the development trajectory. Subsequently, these actions must be underpinned by economic policies to build economic resilience, create productive capacities and productive employment, and to utilise new mechanisms to finance developmental advancements.

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Keywords: development, economic policies, structural transformation, small island developing States, Asia and the Pacific, UN programmes of action.

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I. Introduction

As a result of their geographic and economic features, small island developing States (SIDS), face particular development challenges, which significantly impede their developmental progress; "small but growing populations, limited resources, remoteness, susceptibility to natural disasters, vulnerability to external shocks and their fragile environment. Their growth and development are also held back by high communication, energy and transportation costs, disproportionately expensive public administration and infrastructure due to their small size, as well as little to no opportunity to create economies of scale."[1]

Despite rather common perceptions to the contrary, Pacific SIDS are a very diverse group of countries. Divided into three geographic sub-regions – Melanesia, Micronesia and Polynesia they differ in size of their national economies, size of their landmass and populations, international status and level of development. Melanesian countries usually possess the largest landmass with Papua New Guinea (PNG) standing out with 452.9 thousand square kilometres, whereas Micronesian and Polynesian states are often small atolls or groups of atolls, with Nauru having a landmass of merely 21 sq. km and Tokelau – only 12 sq. km. The populations range from 1.6 thousand in Niue to 8.6 million in PNG. The Gross Domestic Product (GDP) per capita ranges from US$ 1,625 in Kiribati to US$ 17,318 in Palau (World Bank, 2019), if one does not consider the much richer Guam and Northern Mariana Islands, which are territories of the United States. Indeed, many Asia-Pacific small island developing States are independent states, some however, are either overseas territories of larger countries (e.g. French Polynesia, New Caledonia, Wallis and Futuna, Tokelau), or associated territories (e.g. American Samoa, Niue, Northern Mariana Islands, Cook Islands).

This paper focuses on Pacific SIDS which are independent states. In that group, five states, namely, Kiribati, Solomon Islands, Timor-Leste, Tuvalu and Vanuatu face particular challenges as they belong to the category of Least Developed Countries (LDCs) and are characterised by limited productive capacities and widespread poverty. So far, Samoa is the only successful case of graduating from the LDC category (in 2014), however, more countries are scheduled to graduate in the near future, which illustrates significant progress achieved. The article argues that the solutions to SIDS' development predicaments lie in a peculiar type of structural transformation which goes against the broadly accepted theories which advocate for a transition from agriculture to industry and then to services. The structural transformation of SIDS must be supported by a strategy that identifies very specific sectors for development regardless of their broader affinity, i.e. to agriculture, industry or services. This structural transformation must be, nevertheless, underpinned by broader economic policies and the support of the international community. Section One identifies development vulnerabilities specific to SIDS. Section Two examines the framework of international engagement and support provided to SIDS. Section Three analyses sectoral

[1] Wikipedia: https://en.wikipedia.org/wiki/Small_Island_Developing_States (accessed: 17/07/19).

targeting therein as part of structural transformation. Section Four lists the necessary economic policy recommendations.

II. Development challenges

Pacific small island developing States, due to their small nevertheless diverse populations, limited landmass and small economies (see Table 1), as well as geographic locations and remoteness from international markets, are among the most vulnerable countries in the world. They are exposed to a variety of external shocks and internal predicaments that constitute development challenges and can be classified as economic, environmental, social and political.

Table 1. SIDS in nutshell

States	Population* (in thousands)	Landmass (in sq.km.)**	GDP*(current) (US$ in millions)	GDP per capita* (current) (US$)	LDC category
Fiji	833.5	18,274	5,479.5	6,202	
Kiribati	115.9	811	188.3	1,625	Y
Marshall Islands	58.4	181	211.5	3,621	
Federated States of Micronesia	112.6	02	344.5	3,058	
Nauru	12.7	21	114.7	9,030	
Palau	17.9	459	310,1	17,318	
Papua New Guinea	8,606.3	452,869	23,431.6	2,723	
Samoa	196.1	2,821	861.5	4,393	
Solomon Islands	652.9	27,986	1,411.9	2,163	Y
Timor-Leste	1,268	14,919	2,581	2,036	Y
Tonga	103.2	717	450.4	4,364	
Tuvalu	11.5	26	42.6	3,701	Y
Vanuatu	292.7	12,189	887.8	3,033	Y

Sources: * World Bank 2019
** Wikipedia https://en.wikipedia.org/wiki/List_of_countries_and_dependencies_by_area

In terms of economic vulnerabilities, small domestic markets, undiversified economies, usually limited endowment in natural resources, and remoteness form the global markets, renders those economies unattractive from the perspective of international capital and hence as a destination for foreign direct investment (FDI). Thus, they are unable to become a part of global and regional value chains and this impacts their ability to advance development efforts, as engagement with the global economy (through, for example, international trade and sharing global production processes) is of particular importance for any contemporary development model. UNCTAD's World Investment Report (2019) emphasizes the fact that Pacific SIDS are a marginal destination for FDI (Table 2 and 3).

Table 2. FDI inflows in Pacific SIDS (2013-2018) (in US$ millions)

Country	FDI inflows					
	2013	2014	2015	2016	2017	2018
Fiji	243	380	205	390	386	344
Kiribati	1	3	-1	2	1	1
Marshall Islands	33	-8	-6	-3	5	-1
Federated States of Micronesia		20				
Palau	19	41	36	36	27	22
Papua New Guinea	18	-30	28	-40	-180	335
Samoa	14	23	27	3	9	17
Solomon Islands	53	22	32	39	43	12
Tonga	51	56	12	9	14	8
Tuvalu	0.3	0.3	0.3	0.3	0.3	0.3
Vanuatu	-19	-18	29	22	24	38

Source: UNCTAD World Investment Report 2019.

Table 3. FDI inward stock in Pacific SIDS (2013-2018) (in US$ millions)

Country	FDI inward stock		
	2000	2010	2018
Fiji	356	2,978	4,781
Kiribati		5	14
Marshall Islands	20	120	186
Federated States of Micronesia		7	235
Palau	173	232	442

Papua New Guinea	935	3,748	4,563
Samoa	77	220	90
Solomon Islands	106	552	557
Tonga	19	220	446
Tuvalu		5	8
Vanuatu	61	454	607

Source: UNCTAD World Investment Report 2019.

In the times of globalisation and economic opening up, as well as integration of production processes through the international value chains, economies also become more vulnerable towards external shocks, as economic crises are swiftly transmitted from one corner of the world to another. Even those whose role in the international economic interaction is limited are inevitably affected. Their small size and undiversified economic structures make SIDS particularly vulnerable to these external economic shocks – global and regional financial and economic crises, fluctuations of global prices of certain goods and commodities and trade volumes, as well as shifts in global demand for certain services (e.g. tourism), due to, for example, a global recession.

Environmental vulnerabilities in SIDS relate to climate change and environmental degradation. Climate change is responsible for rising seas levels, unpredicted weather patterns, natural disasters (e.g. droughts, floods, etc.) and an overall change in environmental conditions. These occurrences impact SIDS' abilities to develop the agricultural sector, services (such as tourism) and necessary infrastructure. Natural disasters often deplete significantly the available resources and accumulated economic assets, reducing the overall GDP, as was the prominent case, for example, with cyclone Pam which devasted Vanuatu in 2015 and reduced its GDP by almost 65 per cent (ILO, 2015). Environmental degradation impacts the availability of resources, particularly for development of the so-called "Blue Economy" or the "Ocean Economy", which relies on the natural environment and biodiversity, as it reduces fish stock, pollutes sea water and degrades the overall natural habitat, which otherwise could have served as an important economic asset. It affects services such as tourism and contributes to the depletion of human capital due to deteriorating living conditions and the spread of diseases. In addition, addressing external environmental shocks related to global climate change is predominantly beyond the capacity of any given SIDS, making their degree of vulnerability even greater. Global changes in the natural environment can only be addressed by large polluters (which are also big economies) and concerted efforts by all the states. No matter the degree of their engagement, SIDS' unilateral actions will not avert the process of climate change and worldwide environmental degradation.

Moreover, some Pacific SIDS, particularly Fiji, Papua New Guinea and Solomon Islands are sometimes affected by political instability and ethnic conflict (ESCAP, 2018). Papua New Guinea comprises of various ethnic groupings which speak around 850 different languages and dialects. Historically, the main ethnic conflict therein was related to the Bougainville civil war (1988-1998).

The immigrant population in Bougainville, recruited mainly from representatives of Papua New Guinea's "mainlanders" increased as a result of the mining sector development in the 1960s. As the new jobs were mostly awarded to the immigrant population and the benefits for the local population remained limited, by late 1988 tensions over the mining sector led to violence. The government deployed the military and fought against the rebels of the Bougainville Revolutionary Army (BRA). The conflict developed into a separatist insurgency. The estimated number of casualties among the local population was between 15,000 and 20,000. Papua New Guinea continues to be plagued by tribal unrests, tensions and conflicts, in particular in the mountainous interior, following largely tribal lines. The November-December 2019 referendum, in which over 98 per cent of Bougainvilleans voted for independence from PNG may add to the ethnic tensions, since the subsequent political process is not clearly defined, due to the referendum's non-binding character. In the Solomon Islands over 120 different languages and dialects are spoken. The main ethnic conflict (1999-2003) took place between the Gwale (inhabitants of Guadalcanal island) and the more recent immigrant population from the island of Malaita, and concerned access to land and resources. The conflict abated with the intervention of foreign troops in 2003, but tensions continue to simmer. Fiji's population comprises indigenous Fijians who are mostly Melanesians (54 per cent of the population) and Indo-Fijians (38 per cent of the population) – descendants of immigrants from the Indian Subcontinent who arrived at the time when Fiji and the Subcontinent were part of the British Empire. The ethnic conflict between the indigenous Fijians and Indo-Fijians dates back to the early twentieth century and accelerated after Fiji's independence from Britain in 1970. Ethnic divisions were used, for example, as the motives for both the 2000 and 2006 coup d'états.

Social vulnerabilities concern growing populations of the Pacific and related social pressures on the labour market and beyond. The geographic dispersion and the remoteness of the populations impede effective delivery of social and public services. Some SIDS also face significant issues concerning gender inequality, with a significant prevalence of domestic and other violence against women. One of the most worrying cases is Papua New Guinea, where the majority of women have experienced some sort of violence. Indeed, particularly in conflict affected areas in SIDS the situation is precarious. For many women and girls, conflicts place greater restrictions on their choices, opportunities, movement and access to resources. Women and girls in conflict settings face an increased risk of violence – physical, sexual, economic and psychological.

III. International response

The international community has paid significant attention to the development challenges of SIDS. Although some vulnerabilities can effectively be addressed through internal means and politics, many require broader, international engagement. Indeed, various vulnerabilities may need to be addressed through domestic/national policies and institutional arrangements. Some, however, will require sub-regional and regional coordination, cooperation and integration. Others, will need the international transfer of knowledge and best practices. In particular, building resilience against broadly defined external shocks will necessitate the support of the international community and concerted international efforts.

Although it is clear that in view of environmental and climate catastrophes the response by the international community to SIDS development predicaments is by no means adequate, it is important to single out two particular action plans which fully or partially focus on addressing the development challenges of SIDS, namely, the SIDS Accelerated Modalities of Action (SAMOA) Pathway, which specifically focuses on small island states and the Istanbul Programme of Action, which concerns those Pacific islands which belong to the category of the Least Developed Countries (LDCs), as defined by a low level of development, high degree of economic vulnerability and limited human capital (see: LDC Handbook, UNCTAD, 2018a). Both programmes of action are intricately linked to the United Nations' 2030 Agenda and the Sustainable Development Goals (SDGs), a collection of 17 global goals set by the United Nations General Assembly in 2015 for the year 2030, reflecting priorities and urgent areas which need to be addressed by the international community.

The SAMOA Pathway acknowledges the existing and existential threats to SIDS related to environmental vulnerabilities such as climate change and violent weather patterns and calls for building resilience and the capacity to mitigate the effects of climate change and to improve monitoring and sectoral awareness. It mentions marine pollution and degradation of the natural environment, including its biodiversity. It calls for more efficient efforts at disaster risk reduction through technology transfer, increased sectoral investment, and adopting, mainstreaming and harmonizing adequate policies based on rigorous planning. However, it also goes further and specifically mentions that inherent development models need to be put in place to address SIDS development challenges – alluding to the necessity for a particular type of structural transformation – and these models need to underscore the need for sustainable, inclusive and equitable economic growth and the policies aimed at generating decent employment, creating an enabling business environment to attract investment, and improving economic resilience. It also alludes to the concept of the "Blue Economy" (see: Chowdhury, 2019; ESCAP, 2019), which focuses on the sustainable management of oceans and seas, its eco-systems and coastal zones. Finally, SAMOA Pathway emphasizes the importance of international cooperation and efforts in addressing the challenges and providing financial resources. International partnerships, institutional support and more efficient connectivity are of key importance to improving the means of implementation of policies to address development challenges, enhancing capacity building and statistics systems and enabling technology transfer.

As far as the Istanbul Programme of Action is concerned, the LDC category was first introduced in 1971 and included one Pacific state, Samoa. The idea behind this was that countries characterised by low income[2] and structural impediments were identified and awarded a special international status with privileges. These privileges have included:

[2] Low income status is not equal to belonging to the LDC category. In fact, none of the Pacific LDCs are low income economies; all are lower middle-income countries.

a) trade related support measures – preferential market access for goods through a duty-free, quota free (DFQF) mechanism as well as preferential tariffs and preferential and more flexible rules of origin for goods – the concept in itself being a response to the growing importance of the regional and global value chains and subsequent difficulty in identifying where a given product comes from; preferential treatment for services and service suppliers or the so-called “LDC services waiver”, which essentially allows a non-reciprocity based approach for WTO members; special treatment regarding obligations and flexibilities under WTO rules to facilitate LDCs’ compliance in view of limited institutional capacity and to protect policy space, as well as addressing supply-side constraints and supporting LDCs’ broader engagement in international trade, as part of a development strategy;
b) development cooperation, which concerns commitments as far as bilateral overseas development assistance (ODA) flows to LDCs are concerned, multilateral cooperation and exclusive mechanisms, as many donors, national and international alike, define their obligations and legibility and make decisions on their support based on a country’s status and its membership of the LDC category. Exclusive mechanisms include access to technology through LDC Technology Bank, access to funds for mitigating climate change through LDC Fund and climate change related expertise through LDC Expert Group, Aid for Trade through Enhanced Integrated Framework (EIF) to ease trade related constrains, United Nations Capital Development Fund to provide access to microfinance and investment capital, as well as an Investment Support Programme for LDCs by IDLO and UNOHRLLS to provide capacity to LDCs;
c) support for participation in the United Nations and other international forums, which include caps and discounts in contributions to the UN system budgets, support for travel, capacity building for participation in negotiations and flexibility in reporting requirements (LDC Handbook, UNCTAD, 2018a).

There are currently seven SIDS which are also LDCs; five of which are in the Asia-Pacific region. The recent success stories of SIDS graduating from the LDC category include Cabo Verde (2007), Maldives (2011) and, from the Pacific – Samoa (2014). Most of the current Pacific LDCs have already met the graduation criteria; during the 2018 triennial review; Kiribati did so for the third consecutive time (2012, 2015, 2018) and Timor-Leste and Solomon Islands for the second consecutive time. However, although Vanuatu (which met the criteria in 2006 and 2009 and then deferred graduation, on one occasion due to cyclone Pam) is scheduled to graduate in 2020 and Solomon Islands in 2024, Timor-Leste was not recommended for graduation and this case will be reviewed again in 2021.

SIDS’ development vulnerabilities have prompted a debate as to the criteria for graduation from the LDC category. All SIDS LDCs have been recommended for graduation based on the GNI per capita criterion and human assets criterion and not on the economic vulnerability criterion (the three criteria define the eligibility for graduation; see: LDC Handbook, UNCTAD, 2018a). In fact, it is unlikely that despite the graduation from the LDC category, SIDS will meet the economic vulnerability criterion in the foreseeable future, due to economic and environmental reasons. First, they are small and undiversified economies whose budget revenue and thus capacity to spend will be affected by global price fluctuations and global income fluctuations (which affect tourist flows). Second, natural (e.g. extreme weather conditions) and man-made disasters (environmental degradation) will affect their capacities to grow and can cause extensive loss of economic stock and assets.

IV. Structural transformation

The Istanbul Programme of Action acknowledges the importance of structural transformation in addressing the development challenges of least developed countries. Structural economic transformation – a gradual increase in value and sophistication of the output of a given economy – lies at the heart of developmental advancements. This concerns structural transformation within sectors (i.e. agriculture, industry, services) or one sustained through shifts between sectors, traditionally from agriculture to industry and then to services. Once an economy moves towards producing more sophisticated goods, it increases the demand for skilled labour. Skilled jobs are also better paid; hence, the population increases its purchasing power and wealth, and poverty is reduced. Naturally, there are additional conditions which determine the societal ability to engage with and benefit from the restructuring of an economy. Nevertheless, the level of wealth within the population is, to a large degree but with some significant exceptions, dependent on the degree of the sophistication of a national economy.

Studies reveal that in terms of poverty reduction, in the short term, it is the shift within sectors which brings better results (ESCAP, 2019) and this conclusion has indeed important consequences for small island developing States. Naturally, in the long term, the gradual intersectoral move from agriculture is, nevertheless, necessary. Moreover, research shows that greater productivity gains and employment generation, thus poverty reduction, come from transformation from agriculture to industry rather than from agriculture straight to services (ESCAP, 2016). Therefore, this conclusion creates an additional development challenge for SIDS. The relocation of the labour force from agriculture to manufacturing always means the increasing of productivity, whereas the move between agriculture to services often results in rural poverty being replaced by urban poverty.

There are various challenges to effective structural transformation. Two of them have been of particular importance in recent years. First, in terms of poverty reduction, the contemporarily observed phenomenon of an early de-industrialisation, in which economies shift from manufacturing to services at a lower level of GDP per capita and at a lower share of industry in the overall GDP, as compared to the experiences of the earlier industrialisers (Rodrik, 2018), is indeed worrying. Early de-industrialisation affects efforts at poverty reduction, as it is normally manufacturing which brings the best results in increasing wages. Second, the often observed move from unproductive agriculture to unproductive services does not reduce poverty either, as it omits the vital stage of industrial development. In other words, inhabitants of rural areas, formerly employed in agriculture, move to cities and engage in activities such as delivery services, cleaning, etc. From an economic perspective, their new jobs are as unproductive as those they left behind. Consequently, despite the change in type of employment, they remain poor.

The debate on structural economic transformation is inevitably connected to the debates on suitable economic development models. The latter have been proliferating following the global financial crisis of 2008 and the ultimate discrediting of the laissez faire neo-liberal approach favouring an unregulated market and a limited role of the state. However, the role and intensity of the state intervention and to what extent markets should play a decisive role has not been settled and will most likely continue to be debated. This debate is indeed very country specific, as each state has its own set of characteristics, a derivative of various historical, economic, geo-political and geographic factors. The most successful case of recent economic history, namely the East Asian development model – based on import substitution industrialisation followed by export-orientated industrialisation – may not be entirely relevant contemporarily, particularly for small island developing States. The successful historical cases of the model, namely, Japan, South Korea and Taiwan, and its contemporary reincarnation – China (for details see: Bolesta, 2015) have been very different economies from SIDS; they are larger, more diversified and located closer to global economic centres. Moreover, it is often argued that the interdependencies of economic processes were during the periods of Japan's, Korea's and Taiwan's high growth (see: Maddison, 2007) more limited and states could exercise more independent and interventionist economic policies than they can today. Contemporary China is altogether a separate case of structural transformation, due to the country's capabilities. Foremost, however, the East Asian development model did not consider environmental issues, and contemporarily, environmental considerations must be at the fore of development models, particularly in relation to SIDS. The degree of environmental degradation in East Asian economies is significant and a similar course could not be contemporarily sustained, be it for economic reasons – the de-acceleration of growth resulting from lost opportunities in the long term, or the fact that pollution contributes extensively to the deteriorating of well-being and is thus an antithesis of development (see: ESCAP, 2019).

However, what the East Asian development model brings as part of the "library of experiences" applicable today is the centrality of the state as the main facilitator of structural transformation and the development trajectory (ESCAP, 2019). The state exercises its powers through industrial policy. Neglected and often ridiculed during the reign of neo-liberalism, industrial policy is a broad concept encompassing state policies and institutional arrangements aimed at altering the structure of an economy. Among various classifications, one that stands out is the division between functional industrial policy and selective industrial policy. The functional policy aims at creating an enabling economic environment for the private sector to thrive through, for example, well defined and upheld property rights, as well as physical and other legal infrastructure developments. A selective policy is sustained by the process of "targeting", (Bolesta, 2015) in which the state chooses particular industrial sectors for development and then supports them through various incentives, e.g. through purpose-built special zones, financial system-based preferential access to credit (special loans), favourable interest rates and exchange rates, support of export-focused activities – promotion of products, sectoral, bilateral agreements with other countries, etc. In the case of SIDS, due to their extensive development predicaments, a more direct industrial policy is often believed to be necessary (ESCAP, 2019). Indeed, in the case of SIDS, particularly from the LDC group, a selective industrial policy may be needed to address the development challenges. Due to their small economic size, remoteness from global markets and extensive vulnerability to natural disasters and climate change, SIDS may need decisive actions as to which sectors to develop and how.

Structural transformation in SIDS must take into consideration their inherent features. Therefore, some policy recommendations towards this group must go against the broadly accepted economic theory. Moreover, SIDS are often very different from each other, hence policy recommendations concerning structural transformation must be country-specific and tailored towards particular domestic needs.

The traditional path of structural transformation from agriculture to industry and then to services is not relevant for SIDS. In most of the SIDS, particularly the remotely located Pacific islands, creating an industrial manufacturing base (focused on export) is not feasible. As discussed earlier, the costs of reaching international markets are too high. This impedes availability of FDI and thus affects capital formation and technology diffusion. Hence, often direct transformation from agriculture to services is necessary. In that case, one needs to avoid a transfer which will not have a positive influence on productivity, as has been the case in many developing Asian economies. Moreover, the solution may lie in modernisation and sustainability of the agriculture, and in particular, the fishery sector, as this may bring extensive gains in poverty reduction. It is worth noting that the size of Pacific SIDS' exclusive economic zones (EEZs) combined, which includes their exclusive rights to water areas, is 31 times bigger than their landmass. EEZs thus constitute a significant asset. Hence, the structural transformation in the Pacific must deviate from the traditional path and omit the industry development period, focusing instead on services (addressing the predicaments of the rural poor becoming urban poor due to the lack of improvements in productivity) and on (modernised and more productive) agriculture.

Indeed, a recent study by the Economic and Social Commission for Asia and the Pacific (2019) acknowledged the need for a particular genus of structural transformation in SIDS and among the sectors for targeting to overcome the development challenges in the most effective way identified productive services and modern agriculture, and more specifically:

- First, the environmentally sustainable oceanic resource management, known as the "Blue Economy", in a manner which supports development of local/indigenous micro, small and medium enterprises (MSMEs) and ensures that a significant portion of economic gains is retained domestically. As mentioned, EEZs constitute a significant economic asset. However, the fee paid for usage of the SIDS' waters by international companies and corporations and other states is still a fraction of the revenue the latter gain from these activities. For example, in 2014, 12 small island developing Pacific governments received only \$331 million in revenue from access fees to their EEZs, compared to the value of the extracted tuna therein of approximately \$2.5 billion in 2016 (Gillett, 2016; PIFFA, 2017);
- Second, despite the remoteness and high costs of reaching these islands, tourism is a viable option due to the natural richness of the region with unique and well-preserved fauna and

flora. However, for it to be environmentally sustainable and serving the purpose of generating productive employment, tourism must be a regulated low-impact, high-value industry, where impact on the natural environment is minimal;

- Third, for larger landmass SIDS, such as those based in Melanesia, commercial crop production for export markets might be suitable. This would be in line with the 2018 LDC Development Report's general suggestions on the commercialisation of LDCs' rural economies. Successful cases may be considered beef production in Vanuatu for the Australian market and the sugarcane industry in Fiji (ESCAP, 2019).

V. Policy recommendations

The task of identifying necessary sectors for development is only the beginning. The next step concerns adequate long-term economic policies, which will allow for sectoral development.

First, SIDS must enhance their resilience against external shocks, as indicated in the programmes of action. Building resilience is an arduous, multi-layered and multidimensional process, which requires the concerted efforts of national, international and other stakeholders. This process is, however, indispensable for ensuring inclusive and sustainable development. In terms of economic shocks, efforts cannot be limited to standard, often anticyclical, macroeconomic policies. They need to include designing a tailored development strategy, which takes into consideration comparative advantage and domestic strengths, but at the same time presents a vision beyond comparative advantage and one which considers external and internal factors which may contribute or inhibit efforts. A separate issue concerns the ability to build resilience towards global and regional financial crises. This must remain the domain of the international community and the plausible policy options must contain: more thorough regulation of international financial flows, scrutiny over the financial sectors' products and more effective monitoring of sectoral activities. The role for SIDS and LDCs to build resilience in this respect, may mean to rely, to a greater extent, on sources of financial flows from fast growing emerging economies, regulate the transfers domestically and favour, through domestic incentives, those flows which contribute to sustainable and inclusive growth, such as FDI generating positive externalities (e.g. productive employment and the development of the local business sector). What will improve resilience against the volatility of financial markets is a low level of external debt and its sustainability, hence the government's macroeconomic policies must be prudent and ensure the sustainability of its external obligations. In SIDS, public debt servicing takes up a significant share of state revenue, and those resources could be used for productive purposes. De-dollarization may give the authorities more policy options, however, it may also expose small economies to currency shocks.

Second, for LDCs and many SIDS, the biggest overall concerns in terms of progressing with structural economic transformation and developmental advancements lie with the limited productive capacities, defined by UNCTAD (2018b) as: productive resources (human, financial, natural, physical), entrepreneurial capabilities and production linkages, the latter defined broadly as networks, also within regional value chains (RVC) and global value chains (GVC), backward and forward linkages, production clusters, resource networks, links between FDI and the domestic business sector, and between firms. UNCTAD (2018b) lists the biggest challenges to building productive capacities as: limited domestic demand growth (a result of poverty), a lack of human capital (knowledge), a lack of productive employment, a lack of resources (capital) and a lack of a supportive financial system (intermediary infrastructure).

The policies aimed at building the productive capacities must therefore address those challenges, through (a) creating a necessary soft and physical infrastructure, including a well-regulated financial sector; (b) creating an enabling economic environment for the business sector to thrive and FDI to be attracted, with, however, a particular focus on domestic sector development through various linkages (e.g. GVC and RVC) to the global economy. Although, as illustrated, attracting FDI to SIDS is an arduous task, the development of the identified sectors will require the inflow of capital and know-how. Moreover, in order to implement any effective policies and build capacities, (c) an effective reporting/statistics system must be in place.

Third, in the SIDS context, one needs to focus on rural modernisation as part of structural transformation. LDC Development Report 2018 suggests aligning agricultural economy with market and economic activities and making it more business oriented and thus an integral part of the overall economy, rather than playing the traditional role of "feeding the population". This is important as rural modernisation will, in the short term, bring more extensive poverty reduction results than other efforts within structural transformation (ESCAP, 2019). This rural modernisation must encompass a broad range of policies which will incentivise and secure land property rights, mechanisation, dissemination of sectoral technology and advanced technics and most productive inputs (grains, etc.) of farming and husbandry. It also needs to be supported by targeted financial services for farmers and the rural economy.

Fourth, structural transformation itself may not contribute to employment generation. Hence it needs to lead to the development of labour-intensive sectors. This poses additional challenges for SIDS, as the most desirable sector would be manufacturing, an option not viable for them. Instead, SIDS must focus on services. In this respect, the state policy must address the binding constraints to employment creation such as infrastructure and skills. The question of productive and decent employment must be addressed from the supply and demand side. On one hand, an educational system must be created and an education strategy designed which will allow for a steady increase in the quality of human capital in the long term, ensuring a supply of skilled labour force to the market. However, the education system must also be designed to address domestic market needs (the demand side) rather than be focused exclusively on gradual improvements of skills in general. This means that what needs to be considered for the education strategy is the domestic comparative advantages of the local economy and/or the state vision as to the engaging of latent comparative advantages or indeed creating new ones. The envisaged development trajectory is determined by various economic, geo-political, geographical and historical factors, including features of the existing economy, regional and global trends, and the elites' perceptions as to the new opportunities.

Fifth, although the Addis Ababa Action Agenda stipulates that the main responsibility for financing for development lies within the national governments, it is by all accounts clear that many SIDS, particularly LDCs, do not possess and cannot domestically generate adequate resources to advance development. The problem is compounded by the stagnation of official ODA and little political prospects to avert the situation. Moreover, in terms of development of the financial markets, SIDS economies seem to be too small, hence the efforts would need to include building regional structures rather than national structures (e.g. a regional stock exchange). The solution might thus lie in other mechanisms such as remittances and South-South cooperation.

Remittances have traditionally been a source of financing for many SIDS with their diasporas around the world, contributing, for example, to Tonga's economy as much as over 40 per cent of GDP (table 4).

Table 4. Personal remittances received (as % of GDP) (2018)

States	Remittances (% of GDP)
Fiji	5.2
Kiribati	9.7
Marshall Islands	14.1
Federated States of Micronesia	7.1
Palau	0.8
Samoa	16.1
Solomon Islands	1.2
Timor-Leste	3.4
Tonga	40.7
Tuvalu	9.5
Vanuatu	2.2

Source: World Bank, 2019.

Indeed, these financial flows need to be maintained. However, remittances are mostly used for household consumption, and although this may incentivise an increase in domestic production, per se they contribute little if anything to building domestic productive capacities. The way to employ remittances to build productive capacities would be through regulating (e.g. taxing) the remittances flows, which in itself is a contentious issue, often politically not viable. To more effectively employ remittances for developmental advancements, one may consider building a more enabling business environment so that remittance recipients may wish to invest their resources rather than spend them on current consumption.

Moreover, in view of the emerging economic clout of some large developing economies such as China, South-South cooperation may arise as an important source of financing for development for SIDS. Although the international community is adamant about South-South cooperation being merely complementary to such efforts as ODA by advanced economies, the eagerness of economic expansion of large emerging economies, as well as their financial capacities can make South-South cooperation a potentially indispensable source of financing for development. The vehicles for such assistance already exist; for example, the New Development Bank (created by BRICS countries) and China-led Asian Infrastructure Investment Bank, which already provide loans. Some national development banks have also engaged in financing development projects in SIDS, notably the China Development Bank and China Import-Export Bank whose funds dispersion is greater than that of the World Bank. Sustainability questions aside, these new mechanisms may become the leading source of development assistance.

Finally, domestic efforts to improve financing for development must concentrate on building an efficient financial system, which will enable credit access, particularly to macro, small and medium sized domestic enterprises (MSMEs), and particularly those who target productive employment and innovation. Closing the gaps in the taxation system and eliminating informal sectors, at the same time simplifying procedures, will result in greater financial flows to governments, which can in turn use the funds for development.

VI. Conclusion

In recent decades, economic growth in the Pacific small island developing States has allowed for important developmental advancements. It is very likely that within the next decade all Pacific LDCs will graduate from the category of Least Developed Countries. All of them already belong to the group of middle-income economies.

Nevertheless, the current situation for SIDS looks precarious. This is due to external economic and environmental shocks, the latter causing threats of existential proportions, and due to other factors, examined in this article, which impede growth. Hence the pleas of SIDS governments for greater efforts to amend the situation, as indeed progress may be stalled and some of the countries may cease to exist within the next decades due to rising sea levels, the result of climate change. Indeed, SIDS development trajectories are already negatively affected by various factors, which may lead to the deterioration of economic conditions. To add to the development predicaments, external economic and environmental shocks cannot be mitigated by domestic efforts only. They require combined efforts within the international community as well as closer regional cooperation and collaboration. But the international community seems slow in acting to mitigate climate change effects and indeed in averting the process.

However, SIDS cannot sit idly and indeed they do not. SIDS' domestic policies may be seen as equally important in coping with external shocks and internal predicaments and undoubtedly may add to the pool of solutions towards addressing their development challenges. Firstly, structural economic transformation, a necessary process to reduce poverty and advance development, must be tailored to the specific needs of Pacific islands and deviate from the traditional patterns. It must be focused on modernising agriculture and building a robust "Blue Economy" focused on sustainable fishery within the SIDS' exclusive economic zones (EEZ). By skipping the development of the manufacturing sector, the process must also focus on developing services. These services must, however, be characterised by increased productivity. This can be achieved through the expansion of a particular type of tourism, one yielding high revenue not from the volume of visitors but from the quality of service, one which is tightly regulated to minimise the impact on the natural environment and ensures environmental sustainability. The Bhutan model is there to be studied and may perhaps, to some extent, be useful. The specific targeting of sectoral development must be supported by more general economic policies implemented by a capable state. Those policies include: building economic resilience and productive capacities and ensuring that, in the process, productive employment is created in the new and modernised sectors of a national economy. At the same time, one needs to utilise new mechanisms for harnessing financial resources to enhance development.

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