The Pacific Speed of Growth
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Apia, Samoa

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Questions

• What determines growth in PICs?
• Why did PIC growth slow during the 2000s?
Growth has been slow and become slower

- Global crisis hit PICs hard
- Seven PICs below pre-crisis income
- This is the slowest decade
- Growth has fallen behind others
PICs have diverged

- PNG and SI. Have surged ahead
- Other PICs have slowed
- Growth has become less volatile
Growth constraints: theory

Smallness

High production cost

Remoteness

High transport cost

Low competitiveness
Expanded growth Convergence Model
(Sample: Cross-sectional, 45 small states, 1992-2008)

• Per capita GDP growth is a function of:
  – Initial income level (per capita GDP in 1992) +
  – Investment (in percent of GDP) –
  – Population growth –
  – Aid (in percent GNI) ±
  – Political stability +
  – Openness +
  – Growth volatility –
  – Remoteness –
  – Regional dummies Pacific –
  – Others Many are tested, but insignificant
The Pacific Speed:
Geography and policies do matter

(Average annual p.c. GDP growth, in percent)
The Role of Aid in Small States

- Helps raise living standards
- Much aid is for poverty reduction rather than growth
- Possible to increase growth in the long run, e.g., human capital
Why has growth slowed?
(Change in determinants over time)

<table>
<thead>
<tr>
<th>Determinant:</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Initial income level</td>
<td>Little</td>
</tr>
<tr>
<td>Investment</td>
<td>Little</td>
</tr>
<tr>
<td>Population growth</td>
<td>Little</td>
</tr>
<tr>
<td>Aid</td>
<td>?</td>
</tr>
<tr>
<td>Political stability</td>
<td>?</td>
</tr>
<tr>
<td>Export openness</td>
<td>↓</td>
</tr>
<tr>
<td>Growth volatility</td>
<td>↓</td>
</tr>
<tr>
<td>Remoteness</td>
<td>No</td>
</tr>
<tr>
<td>Regional dummies</td>
<td>No</td>
</tr>
</tbody>
</table>
Export openness has fallen

Goods and Services Exports (In percent of GDP)

<table>
<thead>
<tr>
<th>Year Range</th>
<th>PICs</th>
<th>PICs excluding PNG</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991-00</td>
<td>38.0</td>
<td>40.0</td>
</tr>
<tr>
<td>2001-06</td>
<td>36.0</td>
<td>38.0</td>
</tr>
<tr>
<td>2007-10</td>
<td>33.0</td>
<td>36.0</td>
</tr>
</tbody>
</table>
Exchange rates have become overvalued? (1)

REER of PICs with Central Banks

- Fiji
- Samoa
- Tonga
- Vanuatu
- Papua New Guinea
- Solomon Islands

Date:
- 1992M6 to 2010M6

Value:
- 70 to 160
Exchange rates have become overvalued? (2)

REER of PICs without Central Banks

- Kiribati
- Marshall Islands
- Micronesia
- Tuvalu
- Palau

Y-axis: 70 to 160
X-axis: 1992M6 to 2011M6
What do exports show?

Comparative groups
(Real annual average growth, in percent)

PNG and SI.
Other PICs
Small states
LICs
SSA

1991-00
2000-10
Export growth by destination
(Real annual average growth, in percent)

PNG and Solomon Islands

Other PICs
Other groups have surged
(Real annual average growth, in percent)

Small States

Low-income countries
International containerized freight
(US$/TEU, deflated by US GDP deflator)

TEU = twenty-foot equivalent unit

Data source: Containerization International

Global crisis
Policy implications (1)

• **Speed limits**: realistic expectations and prudency.

• **Macroeconomic policy consistency**: ensure competitiveness as well as stability.

• **Structural policies**: raise efficiency and supply response; competitive exchange rates may not be feasible or enough.
Policy implications (2)

• Supporting private sector: encourage investment and exploit comparative advantage in resource-based industries.

• Trade policy: look north while deepening integration with traditional markets, especially with respect to labor services.

• Transport/communication: regional approaches/integration to reduce cost and increase competition?
Thank You
PICs are small and remote

GDP Weighted Distance (km)

World
PICs
Carribeans
Population

(1k) (1m) (1bn)
What do exports show? (1)
PNG and Solomon Islands

1992-2000

2001-2010

N America + EU
Aus & NZ
China
Rest of Asia
Rest of the World
What do exports show? (2)

Other PICs

1992-2000

2001-2010

<table>
<thead>
<tr>
<th>Region</th>
<th>1992-2000</th>
<th>2001-2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>N America + EU</td>
<td>40</td>
<td>32</td>
</tr>
<tr>
<td>Aus &amp; NZ</td>
<td>35</td>
<td>23</td>
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<tr>
<td>China</td>
<td>15</td>
<td>22</td>
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<tr>
<td>Rest of Asia</td>
<td>9</td>
<td>0</td>
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<tr>
<td>Rest of the World</td>
<td>1</td>
<td>23</td>
</tr>
</tbody>
</table>
What do exports show? (3)

Small States

1992-2000

- N America + EU: 42
- Aus & NZ: 3
- China: 28
- Rest of Asia: 26
- Rest of the World: 1

2001-2010

- N America + EU: 33
- Aus & NZ: 10
- China: 27
- Rest of Asia: 28
- Rest of the World: 1
Increasing competitiveness: Policy options - macro and micro

- Garments
- Tourism

**Absolute disadvantage**: Lower living standard

**Competitive exchange rate**: Extremely difficult

**Micro efficiency**: Income penalty

Cost

- 158
- 135
- 100

World price

Income penalty
# Growth Constraints: Empirics

**Sample: 45 countries (averages over 1992-2008 subject to data availability)**

<table>
<thead>
<tr>
<th>Africa (14)</th>
<th>America (12)</th>
<th>Europe (4)</th>
<th>Pacific (9)</th>
<th>Asia (6)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Botswana</td>
<td>Antigua and Barbuda</td>
<td>Estonia</td>
<td>Fiji</td>
<td>Bahrain</td>
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<tr>
<td>Cape Verde</td>
<td>Bahamas, The</td>
<td>Malta</td>
<td>Kiribati</td>
<td>Bhutan</td>
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<td>Comoros</td>
<td>Barbados</td>
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<td>Micronesia, F.S.</td>
<td>Brunei</td>
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<td>San Marino</td>
<td>Palau</td>
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<td>Equatorial Guinea</td>
<td>Bermuda</td>
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<td>PNG</td>
<td>Qatar</td>
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<td>Gabon</td>
<td>Dominica</td>
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<td>Samoa</td>
<td>Timor-Leste</td>
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<td>Gambia, The</td>
<td>Grenada</td>
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<td>Solomon Islands</td>
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<td>Guinea-Bissau</td>
<td>Guyana</td>
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<td>Tonga</td>
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<td>Lesotho</td>
<td>St. Kitts and Nevis</td>
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<td>Vanuatu</td>
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<td>Mauritius</td>
<td>St. Lucia</td>
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<tr>
<td>Namibia</td>
<td>St. Vincent and the</td>
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<tr>
<td>Sao Tome &amp; Principe</td>
<td>Suriname</td>
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<td>Seychelles</td>
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<td>Swaziland</td>
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