

# The role of regionalism in financing development in the Pacific



by Raymond Prasad

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Financing for sustainable development remains the biggest challenge for the **Pacific Islands Forum** countries. We have recorded mixed outcomes in reaching the Millennium Development Goals, and it is crucial that we are well equipped to deliver on the Sustainable Development Goals (SDGs). Financing options determine how we can effectively invest in people, institutions, technology and infrastructure, which are necessary for development, and have a critical role to play in meeting development challenges. The SDGs are expected to bring profound transformation in sustainable development. To deliver on them effectively will require vast mobilisation of resources with associated funding, organisation and allocation, and the strengthening and building of genuine partnerships and institutional capacities.

The development finance landscape varies significantly from country to country, reflecting the economic size and structure, political relationship with development partners, sources of revenue generation, and the nature of inherent vulnerabilities and fragilities. For instance, the Forum's Smaller Island States (Cook Islands, Federated States of Micronesia, Kiribati, Nauru, Niue, Palau, Republic of Marshall Islands, and Tuvalu) are dollarised economies and rely heavily on the grant arrangements with their respective metropolitan donors. The relatively larger economies in the Pacific have a comparatively broader economic base, and are able to generate independent sources of financing.

The Forum Economic Ministers at their 2015 Meeting in the Cook Islands approved the concept of a Regional Finance Facility, noting the mounting challenges in financing development both nationally and regionally to achieve the SDGs. The concept of the Facility presented at the meeting proposed the mobilisation on a voluntary basis of around 10-20 percent of the regional long-term savings for long-term investment in the region. A preliminary survey of the Provident/Superannuation Funds, Trust Funds, and Sovereign Wealth Funds in the region highlighted that Forum Island Countries in total own around US\$7 billion in financial assets. There is

a critical need for Forum Island Countries to consider a regional model for development financing, largely to overcome the non-existent or underdeveloped national financial markets and diseconomies of scale, and to stimulate and sustain economic growth and development in the region.

The quest for sustained positive economic growth in the region requires sustained flows of development finance. The demographic and economic transition of Pacific economies has put additional demands on financing for new and/or upgraded social and economic infrastructure as enablers of conducive economic conditions. These social and economic financing needs are exacerbated by the vulnerability to climate and disaster risks. Based on these qualitative estimates, it is imperative that the required development finance is significantly more than a proportional increase in economic activity, to maintain a sustained economic growth path over time. Unfortunately, domestic capital markets in Forum Island Countries are underdeveloped and rarely serve as a major source of development and investment financing. Correspondingly, most domestic credit market currently do not, and likely will not, have the capacity to finance these development needs on their own.

A regional solution, that addresses the barriers to robust, deep, and economically functional financial market development for Forum Island Countries, especially the Smaller Island States, is a clear way forward. This is evident even in the case of larger emerging and developing economies with relatively larger and complex domestic financial markets, which have supported regional solutions in pursuit of their national goals. The Asian Bond Market Initiative, Africa50 Infrastructure Fund, and Regional Governments Securities Market in the East Caribbean countries are admirable examples of how regional solutions can overcome national financing gaps and challenges. Regional collaboration, solidarity, political will and commitment can transform common challenges into shared prosperity.

A regional solution will enable Forum Island Countries to mobilise funds regionally and will be an essential strategy in mobilising excess liquidity and investable funds, such as excess windfall revenues and savings, to those that need it. This approach will ensure a minimisation of systematic risks and diversification of unsystematic risks (that is, geographical, country, market, credit, interest rate and political risks), and elevate the Pacific region's credibility in managing its financial resources.

A regional financial arrangement is the best alternative for an insurmountable national option. It is the optimal policy option for improving development financing for regional and national public goods and services, with spill-over regional benefits. The proposed Regional Finance Facility will amplify economic and political gains by transforming national markets into a combined regional market for financial assets. As such, countries will be able to fully benefit from the *"Integration Dividend"* by

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overcoming diseconomies of small national market size, limited financial market participants and investable/loanable funds, high domestic transactions costs, varying degrees of country risks, and limited competition for public and private financing needs. This will benefit the Smaller Island States in particular which have very limited options and probabilities to develop a national capital market for public and private investors. The Regional Finance Facility can be a catalyst for the region to take control of our development agenda and financing for regional public goods and services, development of economic sectors, and broadening the economic base.

The Forum Economic Ministers will meet on 3-6 April at the Pacific Islands Forum Secretariat in Suva to consider options for development financing.

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