Notes for Commentary on John Gibson and Karen Nero, "Pacific Island Economies"

New Zealand-Pasifika Interactions and Perspectives Symposium
Wellington 8 February 2007

Geoff Bertram
School of Economics and Finance
Victoria University of Wellington

This is excellent work in a genuinely inter-disciplinary framework. The integration is incomplete, however, and the chapter comprises three almost independent chunks, with Karen providing the middle one.

Karen has not managed to find any decent quantitative measures that John could use for his analysis other than GDP per capita, so the economic work remains trapped in the national-accounting frame of reference.

John has been unable to discipline Karen into formalising her arguments in an operationally-tight way, so the anthropological sections are unsatisfyingly qualititative and don't function as a seamless extension of the economics (and vice versa).

So my feeling was that the chapter needed the attention of a rigorous editor aiming for a more integrated overall result.

Having said that, here we have an economist who understands tapa wealth, and an anthropologist who sees value in working constructively with economists. This has to be a good start!

My detailed comments come under a series of headings, each largely self-contained.

Data and Econometric Analysis

John's regressions follow a path that is by now well-trodden in the growth literature, using OLS to find explanatory relationships by successively including and excluding particular variables or groups of variables, to find which coefficients remain robust over a variety of experiments. The law of large numbers is on his side, and there are some valuable and interesting results reported, but I have a number of concerns:

- Coverage is unnecessarily patchy, being confined apparently to countries covered by IMF or similar sources. The former US territories in Micronesia are missing, as are French Polynesia and New Caledonia. In general, sub-national jurisdictions are excluded.

- Population is measured on a *de-facto* basis, but the Pacific is pre-eminently a region where *de jure* is a better concept to start with. In the comparative population charts and tables, Polynesia looks smaller (relative to Melanesia) than it actually is, because the Melanesians are all stuck at home *de facto* whereas a big proportion of the Polynesians are *de jure* types out in the

diaspora. If we think that development is about people (and peoples) rather than about physically bounded territories, then the politically-delimited units of analysis forced upon us by "national accounts" are likely to miss much of the interesting action. The Pacific peoples' economies are networks operating across transnational space, and there is a need for economic analysis to start from a recognition of this – don't leave it to anecdotal anthropology!

- John's dependent variable is GDP per capita which is notoriously problematic. In particular, remittances don't fit – and GNI is an imperfect way to correct for this (it captures some but not all varieties of remittance flows).

- The use in the equations of the first difference of GDP (that is, the growth rate over some period) seems to me unwise given the extremely poor quality of time-series GDP data in the region. In my own regression work I always use levels, not growth rates, of income, because I don't believe that existing data sources enable us accurately to compare two GDP estimates a decade or so apart. Over that period statisticians have come and gone, assumptions have changed, different interpretations have been placed on accounting concepts, and varying ad-hoc adjustments to the numbers have been made to deal with things such as subsistence agriculture and remittance incomes. Some figures are based on production estimates, some on expenditure estimates. The margins of error over a decade seem to me likely to be of the same order of magnitude as John's calculated rates of growth, which means that his dependent variable (the "growth rate") may be simply an accidental artefact. This reinforces my point above that wider country coverage would be useful - the more economies we can get into the regressions the more confidence we can have in the diagnosis.

Conceptual Basis of National Accounting

Faced with the poor fit between Pacific reality and the standard national-accounting frameworks used by international agencies, it is worth stepping back and recalling some of the original conceptual foundations of national accounts. Long ago John Hicks, one of the founding fathers of the field, defined income in terms of the change in wealth over time. The correct way to measure income is to take wealth at the start of the period and compare it with wealth at the end of the period, plus consumption during the period, minus depreciation.

If we can get the stock measurements of wealth at beginning and end of the period correct, then the only flow we have to estimate is consumption (plus, I suppose, depreciation whatever that means!) – the rest falls into place by arithmetic. All the complicated procedures of SNA accounting, with its attempts to estimate flows directly, are ultimately no more than an operational alternative to working from wealth stocks. As our work moves away from large, modern economies dominated by a fully-commercialised modern sector, towards more loosely-organised economies with large informal sectors and unrecorded transactions, it is increasingly a good idea to work with stocks rather than flows. Karen, therefore, is absolutely correct in her emphasis on measuring wealth – and on including things like tapa in that wealth, given that the acquisition and holding of tapa is something that islanders observably treat as being of value to them. Woe to the economist who refuses to acknowledge

parts of the utility functions of individuals just because they are not those of economists themselves!

Defining Wealth is Critical

The real wealth of island communities lies in their resilience, and whatever assets contribute to resilience and flexibility in the face of outside economic forces need to be recognised as wealth. This means we need to take stock of

- Physical capital (familiar stuff)
- Financial capital (still familiar though harder)
- Human capital (education, skill acquisition and so on)
- Social capital (here things get sticky)
- Metaphysical capital (don't underestimate it! – check out the differing economic performance of religious communities)

Plus other things.

Basically, wealth is anything at all that is durable and fungible into future command over goods and services that are valued. So a relationship established today, that enables me ten years hence to make a phone call and get something done for me by the other party, is a form of wealth. Denying that something is wealth because it looks "unmeasurable" is myopic. Even intangible wealth in the present converts ultimately to something that is measurable *ex post*, and anything that is measurable *ex post* can be theorised about *ex ante*. The accountancy profession has an entire category- "goodwill" that is about this sort of wealth in relation to firms, and which can be a big part of the market value of a firm's shares.

Spatial Autocorrelation

Assuming that the intention here is not to blind people with ostensible science but to say something substantive about the Pacific, I found the discussion of the autocorrelation results unsatisfactory. The autocorrelation result provides an alibi for individual countries within the region, but it does not provide an alibi for an entire region. There really is something about Africa, and it's not helpful to dismiss it just because individual countries' performance is highly correlated with that of their neighbours.

Similarly (taking John's regression results as given for this discussion) there does seem to be something about the Pacific as a whole, such that individual countries suffer rather than gain from being in the cluster.

So what is this regional something that drags growth back? Here John's regressions don't help, but his airfare data are suggestive. Market power seems more pervasive in the Pacific than in other potential comparator regions. The Caribbean is a much more competitive market environment – airfares are lower, telecommunication pricing is lower, remittance transfer costs are lower, shipping freight rates are lower on a per-unit per-km basis, retail margins on imported goods seem lower…… Given the increasing emphasis in the literature on institutional barriers to economic development, I suspect it is time to look much harder at the industrial-organization aspects of Pacific economies.