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Australian Government

AusAID

GOVERNANCE FOR GROWTH

Mid term Review

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GLOSSARY AND ACRONYMS

ADB	Asian Development Bank
CEWG	Core Economic Working Group
EC	European Commission
GfG	Governance for Growth
GoA	Government of Australia
GoV	Government of Vanuatu
IMF	International Monetary Fund
MDG	Millennium Development Goals
MFEM	Ministry of Finance and Economic Management
NGO	Non Government Organisation
O-based	Overseas-based staff
OECD	Organisation for Economic Co-operation and Development
PEFA	Public Expenditure and Financial Accountability Program
PFM	Public Financial Management
PIPP	Pacific Institute of Public Policy
SPC	Secretariat of the Pacific Community
UN	United Nations

2. Acknowledgements

This review of the ten year Governance for Growth (GfG) program was envisaged as part of the original 2007 design at the four year mark to make recommendations on the future direction of the program. Research for this report was primarily carried out during a mission to Vanuatu on May 9-13 2011. The review team comprised of the Governor of the Central Bank of Vanuatu, Odo Tevi representing the Government of Vanuatu, and Vincent Ashcroft, Assistant Director General (AusAID) and Robert Christie, Director (AusAID) representing the Government of Australia.

We, as the review team wish to thank all those who made the time to meet with us and who provided us with invaluable information during the in-country mission. Those we met with include various ministries and departments within the Government of Vanuatu, the private sector, regulatory bodies, other donors, and the Governance for Growth Unit and Port Vila AusAID team.

3. Executive Summary

The Governance for Growth program was set up in 2007 as a partnership program between the Governments of Vanuatu (GoV) and Australia (GoA) with GoV taking the lead, supported by an AusAID team. The program was conceived on the back of a strong bilateral relationship, relative political stability and identified reform possibilities. The program design drew from past lessons about flexibility, longer term approaches, and the need for partner government ownership. The program's purpose was to **generate broad-based economic growth and to improve service delivery through good governance**, with a particular focus on rural areas.



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Many of the development challenges that faced Vanuatu when GfG began in 2007 remain today. Although progress to overcome these challenges has been steady, the global financial crisis has meant that economic growth has been solid rather than spectacular.

The key short and long-term drivers of growth identified in the initial GfG program design have only been partially addressed, notwithstanding notable successes in some cases.

In spite of ongoing development challenges, there have been significant positive developments in Vanuatu since 2007. Governance for Growth has had a number of high profile successes and is highly regarded by the Governments of Vanuatu and Australia. While many recent reforms have been very successful, maintaining momentum in a fluid political climate will present challenges for the program.

Some of the key successes of the program include:

- Recent telecommunications reforms introducing competition to the sector have led to an unprecedented increase in mobile coverage and access. Increased access to affordable telecommunications has had significant flow-on benefits across many sectors, including the development of new innovative initiatives such as mobile banking (PiPP, 2008).
- Macroeconomic management has generally been sound, providing a platform for broad reforms. The Ministry of Finance and Economic Management has been a standout government agency in terms of economic management and planning (ADB, 2009:b; IMF, 2011).
- Management of public expenditure is also sound, although the quality of public spending is not improving as quickly as might have been hoped, particularly in line ministries (Pretorius, 2009; IMF, 2011). Vanuatu's budget process is generally regarded as an effective policy tool, supporting evidence-based decision making on national policies.

GfG's flexible design has largely been successful, allowing the program to capitalise on opportunities for GoV-led reforms as they arise. Ultimately, it is relationships built on

trust that lie at the heart of the program's success. The relationships remain strong, and the level of commitment by both the GoV and the GoA has been crucial. There is a high degree of goodwill in and around the program.

While the GfG program has had a very successful four years since its inception in 2007, and is by any measure performing well and adding significant value for its level of investment, there are a number of areas where there is potential for improvement. To build on its successes, further thought needs to be given to the design of the next phase of the program in order to maintain its momentum and plan for successful future reforms. Below, the review team outlines some broad areas for consideration in the design process that will map the next phase of the program.

Recommendation 1

- GfG should consider ways to promote a national discourse on the importance of economic growth and complementary policy reform priorities.

Recommendation 2

- GfG's current excellent level of informal contact with GoV counterparts should be supplemented with regular scheduled Management Committee meetings.

Recommendation 3

- Consider creating a GfG Steering Committee (possibly with high-level representation from across GoV) to provide guidance on priorities and strategic directions. This might sit within existing processes.

Recommendation 4

- As per the original GfG design document, the GfG program would benefit from a clear design process for its next phase.
- The design should map the Government's capacity constraints, identify priorities, and outline the means to address these institutional constraints, particularly in key line agencies (This has worked well in infrastructure but now needs to expand to health and education). The design should outline the processes, resources and timelines for GfG expanding its capacity building work.

Recommendation 5

- The design team for GfG's next phase should clarify the balance in its focus between work supporting urban centres versus rural areas.
- Australia's bilateral program should consider supporting research into the drivers of migration and urbanisation in Vanuatu, and assessing relevant current systems and policies. This may be something GfG could undertake.

Recommendation 6

- GfG needs to ensure that it understands private sector and civil society views in order to effectively support GoV to identify and address constraints to growth and development. This would best be achieved through assisting and participating in GoV-private sector and civil society dialogue.

Recommendation 7

- A model to improve dialogue with the major donors in Vanuatu on economic and PFM issues should be considered. The Core Economic Working Group model is one possible approach.

Recommendation 8

- GfG's projects in the infrastructure sector complement and benefit from GfG's work in other sectors. While the expansion of the infrastructure component was not envisaged in the original design, the review team found the work to be broadly consistent with the objectives of the program.

4. Country context: trends and challenges

Vanuatu shares many characteristics with its Pacific Island neighbours— its small and highly dispersed population of 245,000 means it cannot realise economies of scale in manufacturing or agriculture, while its remoteness from international markets ensures high costs for inputs and exports (OECD, 2009). Given its archipelago geography and scattered population, the cost of service provision to the majority of its citizens who live in rural areas is particularly high.



Vanuatu's relatively high fertility rate and its increasing life expectancy mean that population growth is comparatively high for the Pacific region. In particular, 25 per cent of the population now live in the urban centres of Port Vila and Luganville (Vanuatu National Statistics Office, 2009), up from 22 per cent in 2003 (UN, 2003). The informal sector comprises an estimated 85 per cent of Vanuatu's economy. The rural population are primarily engaged in subsistence farming and fishing. Although Vanuatu's relative abundance of natural resources means that most ni-Vanuatu are able to live in 'subsistence affluence', the rural majority experience 'poverty of opportunity', or a lack of access to services (Cox et al., 2007).

A period of relative political stability under one Prime Minister from 2004-2008, and progressive reforms saw Vanuatu experience a period of sustained high economic growth; in general, Vanuatu is a good performer compared with some of its Pacific Island neighbours. However, there remain constraints to growth that hamper longer term development such as a limited human resource base, low capacity in line ministries, the high cost of service delivery (through constrained infrastructure in land, sea and air transport, communication, water and electricity), and the absence of a tradition of evidence-based policy-making (ADB, 2009:a; IMF, 2011).

The AusAID-commissioned *Drivers of Change in Vanuatu* study, undertaken during a period of relative political stability and growth in Vanuatu, suggests that a 'medium case' scenario for Vanuatu's future would see a continuation of positive trends, including political stability and macroeconomic management, and continued strengthening of the budget (Cox et al., 2007). However, as remains largely true today, resources are concentrated in Port Vila, and there is still limited state capacity to support development in rural areas. Income differentials between urban and rural areas sit five times higher for urban households (ADB, 2009:a). This reality has increased the appeal of urban centres, and the subsequent increasing urbanisation and growth of peri-urban areas has seen an associated rise in social and environmental challenges (World Bank, 2008).

As in many other societies, economically active women in Vanuatu suffer from a dual workload, combining responsibilities for home and family with their economic activities (World Bank, 2009). Although female enrolment rates are growing faster than male

enrolment rates and girls now make up, for the first time, the majority of those enrolled in secondary education (52 per cent), women remain less likely than men to undertake tertiary education and are less likely to be awarded government scholarships (Vanuatu Rural Development and Training Centres Association, 2007).

In terms of Public Financial Management (PFM), Vanuatu's latest Public Expenditure and Financial Accountability (PEFA) Report (2009) found that the Government of Vanuatu has shown steady progress in several areas of PFM, though in most cases it receives the same score as at the previous 2006 Report. Weaknesses of Vanuatu's PFM system concern policy-based budgeting and the articulation and alignment of some sectoral policies with national priorities. External scrutiny and audit, and effective tax collection are also key concerns for the Government, particularly as they may adversely affect service delivery outcomes through non-competitive tendering processes. However, through its centralised payment and control system and prudent approach to cash and debt management, GoV has maintained aggregate fiscal discipline and the predictability of funds for line ministries (Pretorius, 2009).

5. About Governance for Growth

The Governance for Growth program was set up in 2007 as a partnership program between the Governments of Vanuatu and Australia, with GoV taking the lead, supported by an AusAID team (including locally engaged and Australian staff). The program was conceived on the back of a strong bilateral relationship, relative political stability and identified reform possibilities. The program design drew from past lessons about flexibility, longer term approaches, and the need for partner government ownership. The program's purpose was to **generate broad-based economic growth and to improve service delivery through good governance**, with a particular focus on rural areas. This was to be achieved through two objectives: a national policy framework that is more supportive of broad-based growth; and improved quality of Vanuatu's public expenditure.

Central to Governance for Growth's program design was the Vanuatu Government's ownership of and involvement in GfG. The GfG Unit, which comprises five AusAID staff and three sector advisers (who are a joint resource for AusAID and GoV), is housed in GoV office space adjacent to the Prime Minister's Office and the Department of Strategic Policy Coordination. GfG's Program Director sits on the GoV-chaired GfG Management Committee, and works closely with GoV decision-makers to identify and support the Vanuatu Government's own reform agenda.

The GfG program has grown significantly in response to the 2009 'Australia-Vanuatu Partnership for Development' priorities of infrastructure and economic governance. This expansion is reflected in the growth of GfG's budget resources, which have more than doubled since GfG began (initially budgeted at \$35 million over its first 4 years to actual expenditure of \$60 million over that period).

6. Previous Reviews of the Program

An external peer review by US Treasury department in 2009 provided an overall positive assessment of GfG, noting the high level of engagement and consistency with the Vanuatu government's strategic objectives. The report noted that "counterparts consider that support provided through GfG is quicker and more efficient than [other projects]" and that:

"co-location also appears effective in building the capacity of government counterparts, through a daily, close working relationship and systematic knowledge sharing. The programme also allows AusAID to have a deep knowledge of how the system functions and where it is possible to rely on domestic procedures."

The Treasury review concluded that Australia's commitment to Vanuatu is sufficiently robust and long term to be effective (US Treasury, 2009).

A number of other papers and studies on Vanuatu's development context and economic situation more broadly have been used in the preparation of this review, in particular the comprehensive 2007 'Drivers of Change in Vanuatu' paper prepared for AusAID, ADB

reports, and the 2011 IMF Article IV Consultation Staff Report, in addition to GfG program documents¹.

7. Development Challenges

Many of the development challenges that faced Vanuatu when GfG began in 2007 remain today. Although progress to overcome these challenges has been steady, the global financial crisis has meant that economic growth has been solid rather than spectacular.

The key short and long term constraints on growth identified in the initial GfG program design have only been partially addressed, notwithstanding some notable successes.

- Infrastructure coverage and quality remains poor, adding to the cost of many economic and social activities.
- Electricity, gas and water are all still very expensive and have limited coverage in rural areas.
- Access to basic services in rural areas is still poor.
- Education and health outcomes are low for a country at Vanuatu's stage of development.
- Informal employment is very high (only 15 per cent of the population is engaged in the formal economy) and there is evidence that rural to urban migration is resulting in increased instances of peri-urban slums.

Similarly, the key governance obstacles to achieving growth and service delivery identified at GfG's inception are still features of Vanuatu's economic and political landscape today. These include:

- Lack of a clear and coherent national economic policy with many initiatives reflecting short-term political expedience rather than long-term national interest.
- Poor outcomes on policy implementation – short-lived and political initiatives rather than evidence-based advice.
- Weak public expenditure management, despite sound budget processes and financial management— expenditure is not well prioritised and the budget does not have a strong policy basis.
- Limited policy and regulatory settings, and inadequate investment in infrastructure (Cox et al., 2007).

Despite these ongoing challenges, there have been significant positive developments in Vanuatu since 2007.

- Recent telecommunications reforms introducing competition to the sector have led to an unprecedented increase in mobile coverage and access. Increased access to affordable telecommunications has had significant flow-on benefits across many sectors, including the development of new innovative initiatives such as mobile banking (PiPP, 2008).

¹ The latest Vanuatu Household Income Expenditure Survey was carried out in 2009, but it has not yet been made publicly available. When they met in May, the Review team encouraged the National Statistics Office to publicly release the Survey.

- Macroeconomic management has generally been sound, providing a platform for broad reforms. The Ministry of Finance and Economic Management has been a standout government agency in terms of economic management and planning (ADB, 2009:b; IMF, 2011).
- Management of public expenditure is also sound, although the quality of public spending is not improving as quickly as might have been hoped, particularly in line ministries (Pretorius, 2009; IMF, 2011). Vanuatu's budget process is generally regarded as an effective policy tool, supporting evidence-based decision making on national policies.

8. Program Successes

Governance for Growth has had a number of high profile successes and is highly regarded by the Governments of Vanuatu and Australia. While many recent reforms have been very successful, maintaining momentum in a fluid political climate will present challenges for the program.

GfG's flexible design has contributed to this success, allowing the program to capitalise on opportunities for GoV-led reforms as they arise. However, this flexibility involves a greater level of risk than more conventional aid programs. As the Government highlighted in meetings with the review team, flexibility and responsiveness work best when there is an active, high-level appetite for reform. GfG manages this uncertainty by building relationships across GoV and progressing longer term projects such as capacity building initiatives that can continue when the higher-level imperative for ambitious reforms loses momentum. The underlying premise of direct engagement through an AusAID staff member managing a flexible program which supports Government-led reforms has proven sound.

Ultimately, it is relationships built on trust that lie at the heart of the program's success. The relationships remain strong, and the level of commitment by both the GoV and the GoA has been crucial. There is a high degree of goodwill in and around the program. While there are particular risks associated with such a broad and flexible model, GfG's major achievements have been the result of its strategic and well articulated development strategy based on an understanding of the local context, its constraints and a degree of 'strategic opportunism' taking advantage of opportunities that arise.

Key achievements:

Initiatives in the **telecommunications and energy sectors** are standout and important structural reforms. There have also been less obvious but encouraging steps forward in **public financial management**.

- **Telecommunications:** GfG played a key role in supporting the Government of Vanuatu to liberalise its telecommunications sector and allow market competition. With GfG's support, in 2007, Vanuatu's Telecommunications Act was amended to open the market to competition, and Caribbean based company Digicel was granted a licence to provide mobile telecommunications in Vanuatu. With the entry of Digicel to the market, the sector has seen tangible benefits in terms of reduced prices and improved service quality (ADB, 2009:b). National coverage of the mobile network also increased dramatically, from around 25 per cent of Vanuatu in 2006 to over 90

per cent in 2010. Further, declining costs have seen the use of mobiles in Vanuatu rise dramatically, from 11 per 100 people in 2007 (PiPP, 2008) to 71 per 100 people in 2010 (AusAID 2011:b).

The Pacific Institute of Public Policy's 2008 study into the impact of the telecommunications reforms suggests a positive impact for social capital and economic activity by small and medium enterprises (PiPP, 2008), supporting GfG's objective of broad-based economic growth. The introduction of competition in the telecommunications sector is "reducing the cost of doing business (incremental benefits) and expanding business opportunities (transformational benefits)" (PiPP, 2008). The study also found that increasing access to telecommunications "is leading to more contact with family and friends, improving information regarding family events, reducing cost of travel, and increasing speed of communication. There is a positive relationship between perceived access to telecommunications and perceived livelihood improvements." This reform remains a key success story of the GfG program, generating considerable goodwill for the program across government.



- **Mobile banking:** With the opening of the telecommunications market in Vanuatu, the National Bank of Vanuatu launched a mobile banking initiative which has allowed customers from across Vanuatu to transfer money quickly, easily and affordably without having to make difficult and expensive phone calls to the Bank of Vanuatu in Port Vila. The Bank set up solar-powered satellite banking hubs on remote islands, vastly improving access to banking services for the 75 per cent of the population living in rural areas. While credit has been available for Vanuatu's commercial sector and larger businesses, rural enterprises and small businesses have found administrative costs for small amounts to be high. Mobile banking is one technology-based initiative that should help address this challenge (ADB, 2009:b). Internet services in Vanuatu have also expanded, with the entry of several new service providers into the market; uptake of these services is rising quickly (Vanuatu National Statistics Office, 2008; IMF 2011).
- **Energy:** Since 2006, the Government of Vanuatu has undertaken reforms in the energy sector to help lower the high cost of electricity in Vanuatu, increase access, and improve services. Vanuatu's 2009 census found that only 33 per cent of the population had access to electricity. With the Government identifying the sector as a priority, GfG supported the establishment of the now-operational independent Utilities Regulatory Agency (URA) to ensure power and water services were provided at a fair price and with improved access. The URA has since undertaken an Electricity Tariff Review which made recommendations for an overall 6.9 per cent reduction in the price of utilities², and a 49 per cent reduction for low income consumers. With GfG's support, the Government has now also announced the entry of a new electricity

² A subsequent High Court decision lowered this overall reduction in cost to 4.7 per cent.

supplier, Pernix, into the market this year. This will effectively end Vanuatu's electricity monopoly and, it is hoped, will put further downward pressure on prices and increase access.

- **Public financial management:** Ongoing GfG support in economic and financial management has helped GoV to improve fiscal discipline and strengthen the links between government policy, resource allocation and donor funding. GfG support to this area involves long term flexible funding to the Ministry of Finance and Economic Management to support their role in developing, implementing and leading sound financial management practices within government (at a national and provincial level).

In addition, GfG support enables operational grants to go directly to schools from the Ministry of Finance, laying the foundations for reforms in other sectors. GfG played an integral role in helping the government to develop and establish its initiative to phase out school fees as a means to support the achievement of Universal Primary Education. GfG support to the Ministry of Finance helped set up direct funding arrangements between the Ministry and individual schools, avoiding the inefficiencies and bottlenecks of distributing funds through a line agency and then multiple layers of Government (many of which face serious capacity constraints) before arriving at individual schools. GfG's work with GoV in the education sector has resulted in improvements in access to primary education as some school fees are phased out and individual schools have the ability to plan and fund their own needs, whether it is teachers, classroom repairs, or purchasing materials.

Other achievements:

GfG has numerous other achievements spanning multiple sectors including infrastructure and transportation, research and statistics, and tourism. In the infrastructure sector, one of the most visible and important components of the program, one of GfG's key achievements is building on and deepening – through practical cooperation – the level of partnership with key GoV counterparts. GfG's strong relationships in this sector ensure that AusAID's infrastructure programs are based on open dialogue, and they are responsive and able to effectively address emerging constraints. Recently, GfG has also supported GoV to open its aviation sector to international competition, and to design the new cargo terminal and implement various ports management reforms.

More broadly, GfG has demonstrated to the Government of Vanuatu, other donors and AusAID that development partners, can deliver support and structure themselves in a way which is responsive to the political and capacity realities in-country. GfG has also shown that governments in a low human resource capacity environment are capable of bringing about rapid positive change through reform if provided with ready access to quality technical support, particularly for significant or first-time reforms. Telecommunications and Energy are the two key sectors in which GfG's impact in this responsive, 'mobilising' role can be seen, both through immediate outcomes of lower prices and higher access, and improved governance of the sectors with the establishment of independent regulators.

It is also important to recognise the bilateral relationship which makes a program like GfG possible. The strong sense of partnership within the program clearly reflects a strong broader bilateral relationship between the Governments of Vanuatu and Australia. This

has allowed space for the program to have strong ownership by GoV. As such, Governance for Growth has quickly become a core part of not only the aid relationship between Vanuatu and Australia but the broader bilateral relationship.

9. Looking Ahead

While the GfG program has had a very successful four years since its inception in 2007, and is by any measure performing well and adding significant value for its level of investment, there are a number of areas where there is potential for improvement. To build on its successes, further thought needs to be given to the design of the next phase of the program in order to maintain its momentum and plan for successful future reforms.

The review team has examined GfG's progress to date, and below we outline some broad areas for consideration in the design process that will map the next phase of the program.

1. **Economic Policy Development** - there is a need to ensure that Government policies are driven by strategic growth objectives, and are underpinned by up-to-date economic information and advice. One opportunity to promote broader discussion and understanding of economic issues might involve a whole-of-government or expanded GfG Management Committee meeting where invited guests present on economic issues of relevance to Vanuatu. Guests would stimulate discussion on economic issues that should inform policy direction and planning, and would be relevant to all service delivery portfolios, central agencies, and the National Statistics Office, for example. Whatever form it takes, there is a need for whole-of-government dialogue on the economy and other issues affecting the budget and policy environment of Vanuatu.

The promotion of a wider understanding of economic issues would feed into several of GfG's original objectives, as set out in its design paper (see Annex 1), such as:

- supporting the Government to develop and implement policy decisions to remove constraints to broad-based growth;
- ensuring policy decisions are increasingly informed by sound research, evidence and analysis; and
- improving public financial management outcomes by fostering discussion on priorities for service delivery and tying this to the budget process.

Such a forum would seek to promote greater dissemination of information and public debate about economic growth and the role of government. It need not add to the number of meetings already convened, but could take place on the sidelines of a regular GfG Management Committee meeting, with the flexibility to invite guests and other interested agencies.

Recommendation 1

- GfG should consider ways to promote a national discourse on the importance of economic growth and complimentary policy reform priorities.

2. **Communication** – formal and informal – as GfG transitions to its next phase and new management teams replace the original proponents of the program, there is a need to ensure that communication is maintained. Regular scheduled meetings of the Management Committee should supplement regular informal contact.

When GfG was first established, the four year period under one Government allowed strong informal relationships between GfG and central agencies to overtake the need for regular formal Management Committee meetings. However, with new management teams in place for the Government of Vanuatu and in AusAID, there is a need for the formal meetings that were envisaged in the original GfG design to convene. This regular formal contact would complement the informal networks that are developing over time, and is no less important for GfG's ability to support GoV in realising its reform and development objectives.

Recommendation 2

- GfG's current excellent level of informal contact with GoV counterparts should be supplemented with regular scheduled Management Committee meetings.

3. **Governance** – The GfG Management Committee has provided excellent leadership of the GfG program. Central agencies should consider the precise composition of the Committee, and consider broadening it to include key GfG line agency representatives.

The original program design also envisaged a Director-General level Steering Committee that has never in practice been a part of the program. There is merit in considering some form of Steering Committee – not to take decisions on the program but to, every six months or so, assess GfG's priorities and strategic directions, and to provide guidance on key initiatives. These Committee meetings would provide an important forum for a broader discussion on program objectives with other agencies. One option is for the Steering Committee to sit within or alongside established mechanisms (such as the weekly meeting of Directors-General, the Development Committee of Officials (DCO), or the annual Australia-Vanuatu Partnership for Development talks). This would enable a Steering Committee to convene without adding to the number of existing meetings within GoV. We would suggest that a member of AusAID senior management could attend to highlight the importance of the program to AusAID.

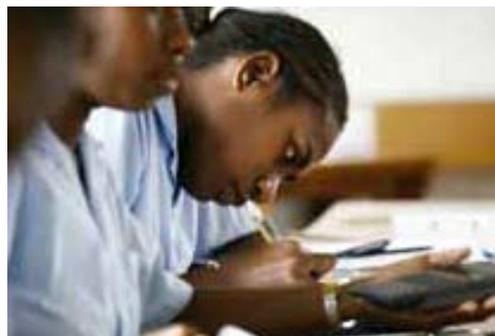
Recommendation 3

- Consider creating a GfG Steering Committee (possibly with high-level representation from across Government) to provide guidance on priorities and strategic directions. This might sit within existing processes.

4. **Capacity Building** – while the program has been extremely successful at supporting reforms and undertaking specific activities, there is a need for ongoing improvement of line ministry capacity. This will require more leadership from GoV and more dedicated and concerted resources from GfG.

The design of the next phase of GfG activities should explicitly address capacity constraints and identify priorities for addressing those constraints. The design should involve a refocus on GfG's potential to support the central agencies to engage more

effectively with line agencies, while also supporting line agencies directly to improve their public financial management. Clear priorities for capacity building remain infrastructure, education and health.



GfG is already taking action on this objective, for example they are assisting GoV to engage a PFM specialist to assist the Ministry of Education with public expenditure. Improving public expenditure systems in major spending agencies remains a sizable and challenging task, and GfG will need to develop a strategy on the best way to move forward with limited resources.

The provision of support directly to schools by the Ministry of Finance has created significant momentum within the Ministry that should be capitalised on. At the same time, GfG should consider what quick wins are possible in key service delivery agencies, including encouraging consideration of public expenditure reviews. This might also help to garner interest from the multilateral development banks who have a wealth of experience and knowledge to provide and are providing important assistance to other Pacific countries in this space that Vanuatu has not yet capitalised on.

Recommendation 4

- As per the original GfG design document, the GfG program would benefit from a clear design process for its next phase.
- The design should map the Government's capacity constraints, identify priorities, and outline the means to address these institutional constraints, particularly in key line agencies (This has worked well in infrastructure but now needs to expand to health and education). The design should outline the processes, resources and timelines for GfG expanding its capacity building work.

5. **Rural focus** - the GfG program was designed to assist rural areas where most of the population live and where access to services is most constrained. While most GfG-supported reforms benefit the rural population, several GfG projects have an increasing focus on urban areas, particularly in infrastructure. GfG envisages that “existing levels of support to rural areas would be maintained and the expansion into urban areas would be accommodated through expected growth in the program budget as the agency scales up” (AusAID, 2011:a).

The drivers of the new focus on urban areas include increasing urbanisation and poverty in peri-urban areas (30 per cent of the 60,000 people living in Port Vila are reported to live below the poverty line, a higher rate than in rural areas), as well as growing tourist numbers and economic activity in urban areas. While there are obvious and increasing development needs to address in the urban areas of Vanuatu, there is also a need to clearly articulate GfG's objectives in terms of its focus, given the core tenet of the original design was to increase growth and service delivery in

Recommendation 5

- The design team for GfG's next phase should clarify the balance in its focus between work supporting urban centres versus rural areas.
- Australia's bilateral program should consider supporting research into the drivers of migration and urbanisation in Vanuatu, and assessing relevant current systems and policies. This may be something GfG could undertake.

rural areas. Considering this shift, there may be value in GfG coordinating some research work into the drivers of migration and urbanisation in Vanuatu, and the efficacy of current systems in dealing with these issues. These urban-rural issues should be a priority consideration in the design of the next phase.

6. **Engaging the private sector and civil society** - GfG has successfully engaged the private sector and civil society (including the media) in a number of initiatives, but there is potential for GfG to further extend this support, and for it to prioritise the development of linkages between GoV and non-Government sectors. This support has been identified by the Government as an area of need. Greater dialogue between GoV and the private sector would promote a greater understanding of constraints on the private sector, and foster a positive environment for business-conscious policy making, ultimately adding to the Government's drive for reform. The GfG program would also benefit from greater insight into private sector and civil society views including, for example, more regular engagement with think-tanks such as PIPP, and NGOs. Greater levels of discussion and interaction with non-government sectors would assist GfG to more clearly understand the constraints to growth and the broader challenges to development facing Vanuatu. This would best be achieved through GfG assisting and participating in government-private sector and civil society dialogue. GfG's support for more regular engagement with non-government sectors should begin with any existing GoV mechanisms to consult with these sectors.

Recommendation 6

- GfG needs to ensure that it understands private sector and civil society views in order to effectively support GoV to identify and address constraints to growth and development. This would best be achieved through assisting and participating in GoV-private sector and civil society dialogue.

7. **Donor coordination** - there is potential for GfG to further strengthen its relationships with other donors to maximise impact and avoid duplication. There are fora for donor coordination to take place in Vanuatu, but in spite of this, there is some uncertainty amongst other donors about what projects GfG is currently involved in, or is planning for the future. Given the number of bilateral donors and development banks operating within multiple sectors and projects in Vanuatu, it is important that the GfG Unit works with these parties to plan and coordinate activities, focusing on alignment with Government objectives. GfG and GoV should consider the merits of a 'Core Economic Working Group' (CEWG) for Vanuatu, which has worked well in the Solomon Islands (amongst other countries around the world). In the Solomon Islands, CEWG's quarterly meetings are led by the Ministry of Finance, supported by key government agencies and the donors most involved in economic issues. The CEWG supports the government's own reform agenda, and engages donors (including the World Bank and ADB) in a policy dialogue around reforms promoting economic growth. The CEWG has a number of features that would be of benefit to GfG in terms of donor coordination, and to GoV in terms of improving dialogue and facilitating coordinated responses to key economic and fiscal challenges, as the model has done in the Solomon Islands.

Recommendation 7

- A model to improve dialogue with the major donors in Vanuatu on economic and PFM issues should be considered. The Core Economic Working Group model is one possible approach.

8. **Breadth of work** - there was a broad consensus that the suite of work being undertaken by GfG covered the major areas for reform and was within a manageable range for the program's team. While there are not clear 'easy wins' for the next phase of GfG such as the successful telecommunications reforms early in GfG's life, this does not take away from the need for more challenging but no less important reform tasks.

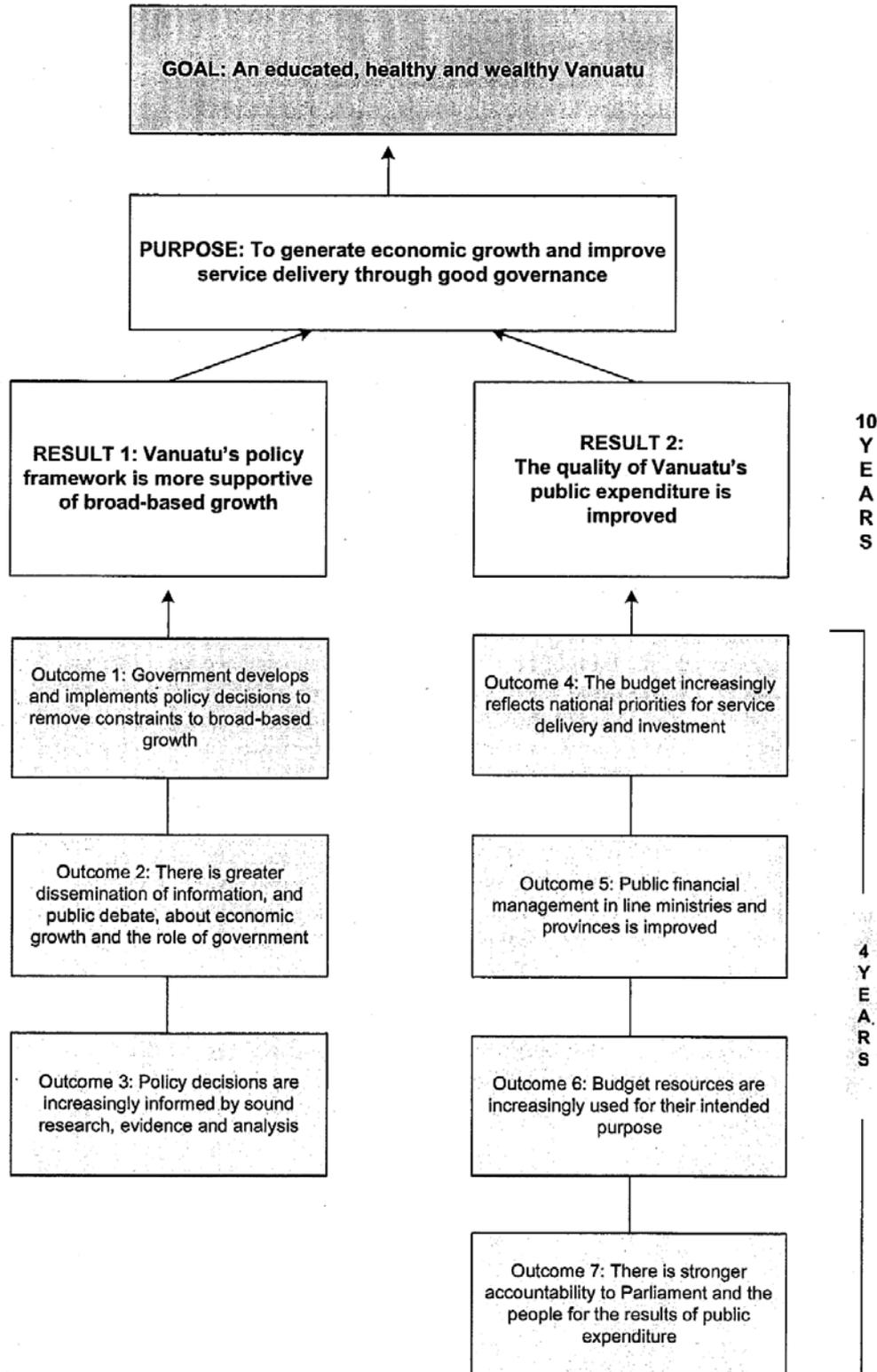
Regarding GfG's focus, a question was raised about the possibility of splitting off the infrastructure component from the program. The review team feels that the work in the infrastructure sector has benefited from the use of the GfG partnership model, particularly the placement of an AusAID Adviser working on the infrastructure sector from within the GfG Unit. This has been important given that the Ministry responsible for infrastructure also covers many of the reform areas that GfG is otherwise engaged in. GfG's support to the infrastructure sector also builds on a history of successful support. It follows on from the successful telecommunications reforms, building on GoV's and the program's objective of increasing rural connectivity, and which was also based in the Ministry of Infrastructure and Public Utilities.. Further, the program will benefit from having the in-house experience of working in one line agency while it moves to improve public financial management in others. On balance therefore, the strategic advantages combined with the benefits of continuity and stability appear to outweigh any streamlining that removing the infrastructure component may bring.

Recommendation 8

- GfG's projects in the infrastructure sector complement and benefit from GfG's work in other sectors. While the expansion of the infrastructure component was not envisaged in the original design, the review team found the work to be broadly consistent with the objectives of the program.

Suggestions for further work:

- A design mission for the next phase of the program should be undertaken. The design should again balance flexibility with a strategic framework that clearly sets out the practical objectives of the program. It should articulate, in quantifiable terms, the results GfG is hoping to achieve and will be assessed against at the end of the program in 2017.
- Appraisal of the status of GfG's current reform initiatives – this should be undertaken by a reform specialist with the possible involvement of the ADB or World Bank
- Assessment of the most effective way for GfG to support GoV in its public financial management reforms - this should be undertaken by PFM specialists.



Annex 2

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