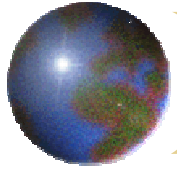


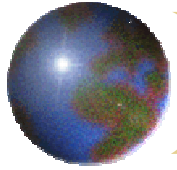
*SELF GOVERNMENT IN FRENCH  
POLYNESIA: HOW  
DECENTRALIZATION CAN BE  
DETRIMENTAL TO GROWTH*

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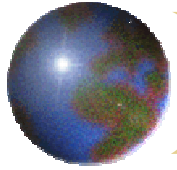


1. Introduction
2. A stagnating economy in need of structural reforms
3. Polynesian self-government within the French republic: a dream institutional arrangement ?
4. Bad governance
5. The future of FP: reform or decline



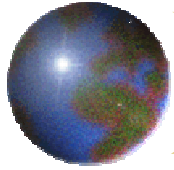
# *1. INTRODUCTION*

- Etats-généraux de l'outre mer: following the turmoil in French Caribbean territories
  - The effects of institutional arrangements at the core of the debate
  - Jego (French Ministry): open to new institutional arrangements
  - Temaru (President FP): Tahiti Nui Agreement ?
  - Fritsch (President, Assembly FP): the current institutional arrangement offers a perfect framework for growth policy.



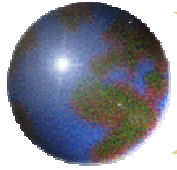
## *(Introduction )*

- ✚ General acknowledgement that institutions and governance matter for growth (although with much confusion about what is good and what is bad)

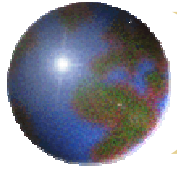


● The institutional arrangement existing in French Polynesia has the two following main characteristics:

- The territory remains within the French republic boundaries and keep the basic legal and institutional framework from the « patron country »
- However, the political status provides many attributes of local self government
  - Especially relating economic rules and policies, including tax policy, foreign trade policy, competition policy (or rather the lack of it), regulation policy, local fiscal policy,...



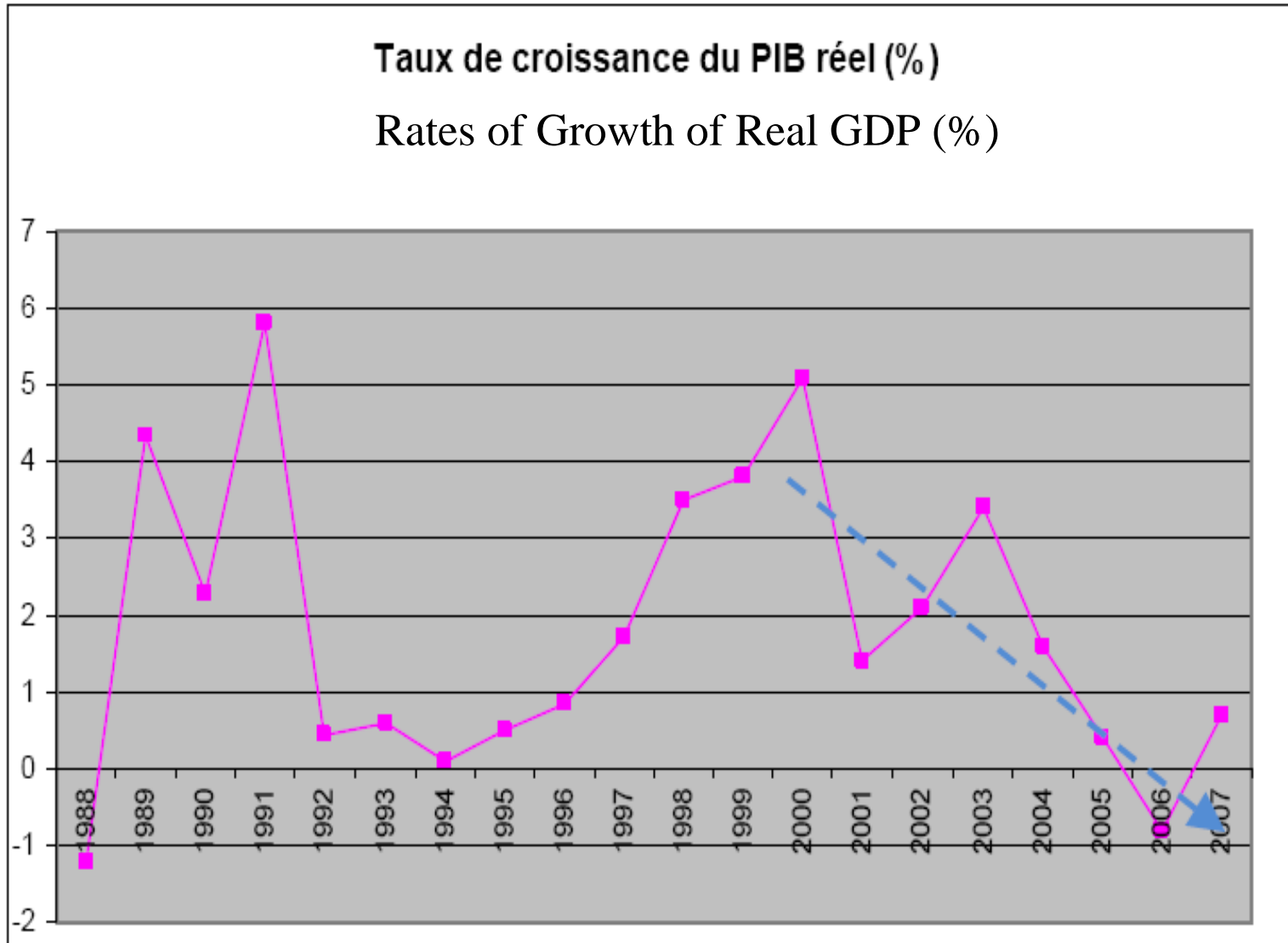
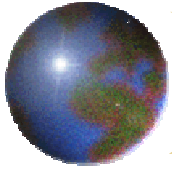
- ✦ We will use Economic theory (New Institutional Economics) and accumulated empirical studies to assess the advantages and drawbacks of the current status as a framework for sustained growth.
- ✦ We will see that the status of self-government has been so far more an impediment of growth than a factor of it.
- ✦ Some proposals of reform will be suggested, without which a prolonged decline could result.



## *2.A STAGNATING ECONOMY IN NEED OF STRUCTURAL REFORM*

### **1. Relatively poor economic performances**

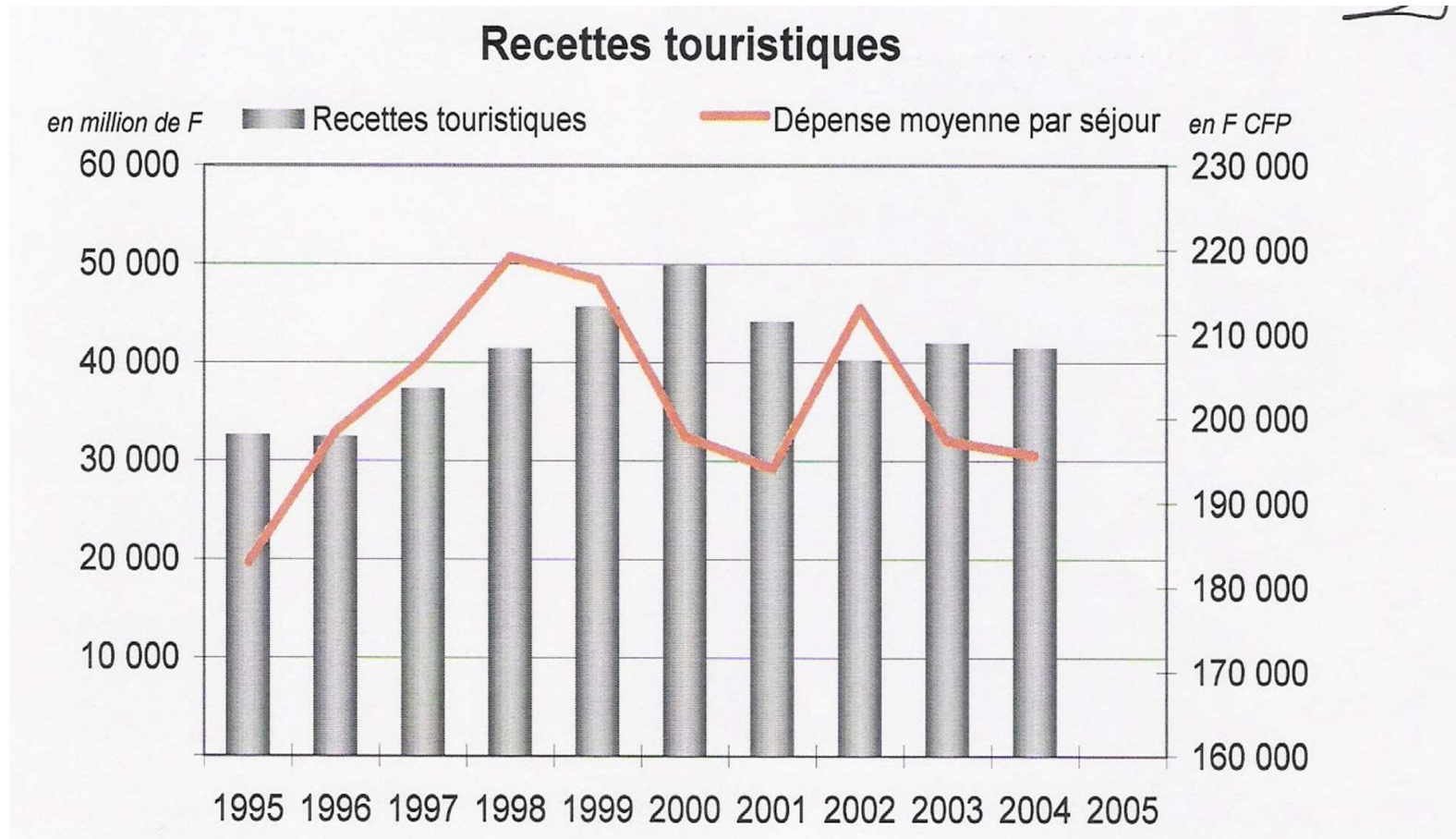
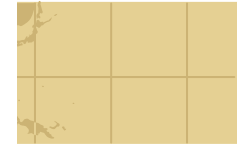
- ❖ The economy of FP is of course suffering from the international crises
- ❖ But we can observe a constant deterioration since the years 2000-2001



Source: Government of French Polynesia

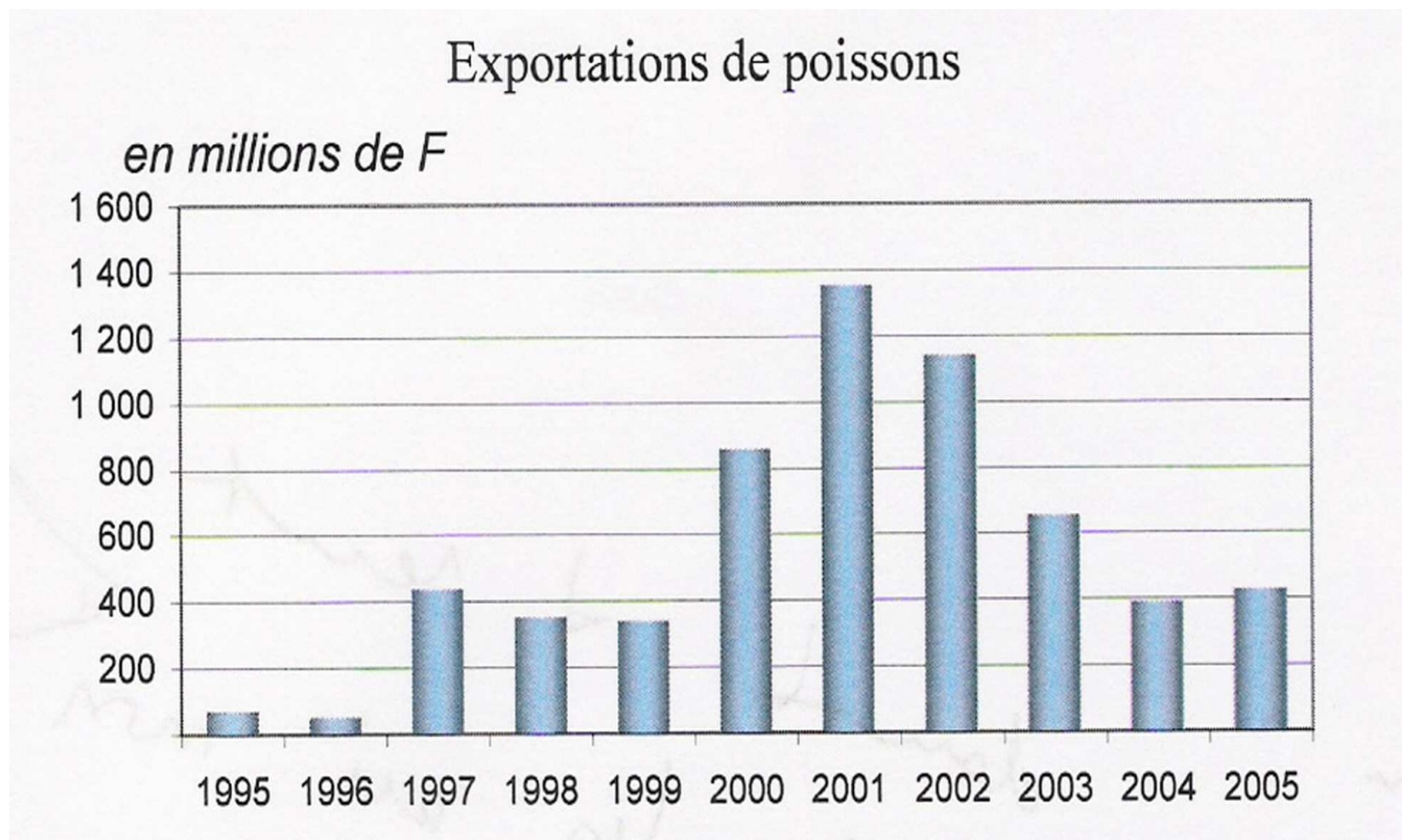


# Tourism receipts FCFP



Source: CEROM (IEOM, ISPF, SPPE, AFD)

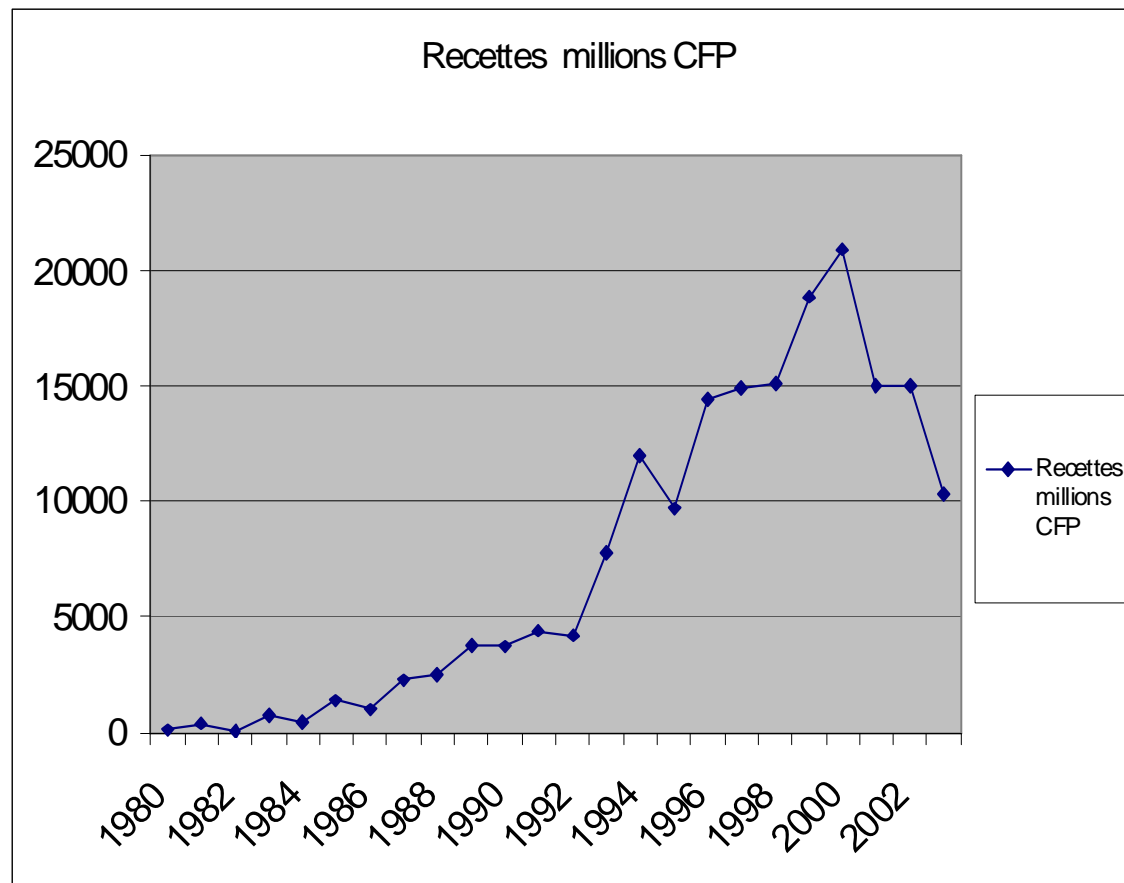
## Fish exports, millions FCFP



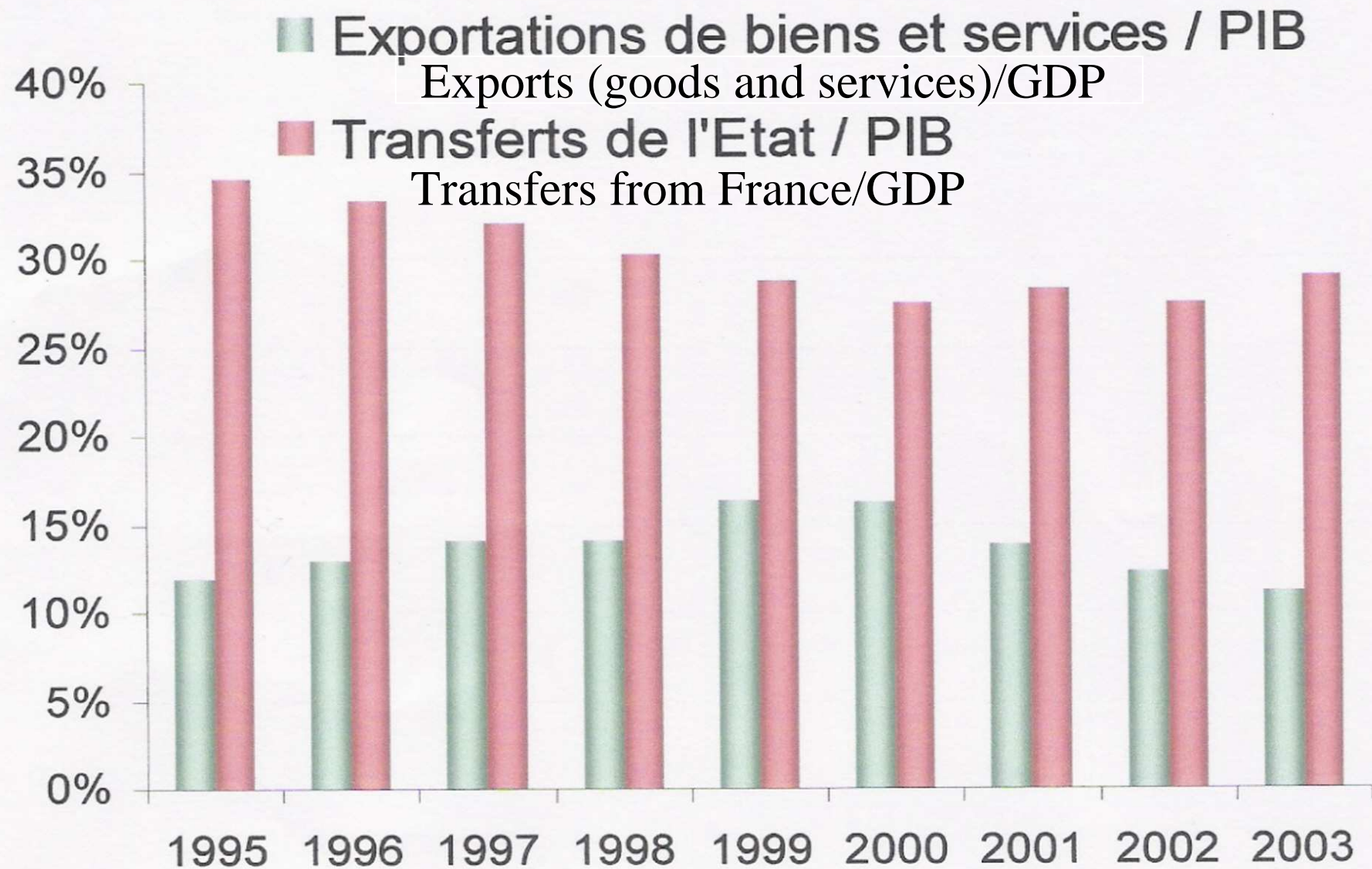
Source: CEROM (IEOM, ISPF, SPPE, AFD)



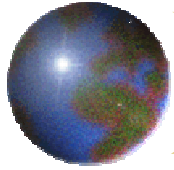
# Black Pearl exports (millions FCFP)



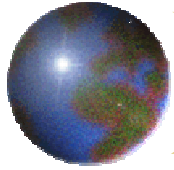
Source: données service de la perliculture



Source: CEROM (IEOM, ISPF, SPPE, AFD)

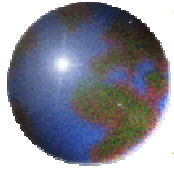


- ❖ Population has increased at a rapid path especially in the 1980s and 1990s
- ❖ Consequently, relative stagnation of the GDP per head:
  - ❑ An average growth of 1,1% between 1995 and 2003 (acceleration between 1995 and 2000 and stagnation since then).



## **2. Weak performances in terms of public management :**

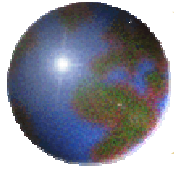
- As can be testified by the Chambre Territoriale des Comptes through their auditing of public budget, finance and policies see numerous reports online: [www.ccomptes.fr](http://www.ccomptes.fr) (then go to CRTC)
- Among numerous exemples of waste of resources: management an regulation of telecommunications, power generation and electricity distribution, human resources management of the public sector (president office, GIP,...)



### **3. Low productivity**

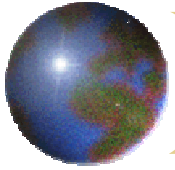
- ❑ Labor productivity decreases (see CEROM, 2007)
- ❑ TFP negative (work in progress)

### **4. A structural mix of oligarchic and state-guided capitalism** (a bad specie according to Baumol, Litan and Schramm, *Good Capitalism, Bad Capitalism and the Economics of Growth and Prosperity*, Yale University Press, 2007)



- ❁ Need of structural reform:
  - ❁ Increase productivity
  - ❁ Increase entrepreneurship
  - ❁ Increase private investment, innovation and risk taking
  - ❁ Increase competition
- ❁ To summarize: need to move from a form of capitalism (oligarchic and state-guided) to a form of good capitalism (entrepreneurial)
- ❁ Can the status of self government change from a support of a bad form of capitalism to the support of a good one ?

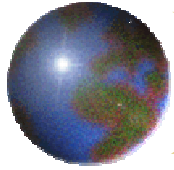




### *3. SELF GOVERNMENT AS A DREAM INSTITUTIONAL ARRANGEMENT ?*

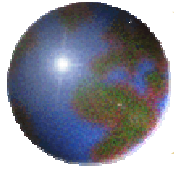
#### ✚ The current status

- ✚ Provides institutions and mode of governance of a European country
- ✚ Offers the economic advantages of the backing of a large and developed country
- ✚ Responds to the local demand for public goods and externalities
- ✚ Avoid (temporarily ?) separatism which may bring impoverishment.



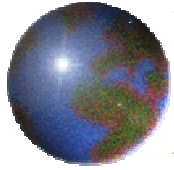
# **1. Institutions of a European country:**

- ❑ Judicial system
- ❑ Definition and protection of property rights
- ❑ Business laws
- ❑ Political democracy: parliament, free voting, etc...
- ❑ Trust (lowering transaction costs)

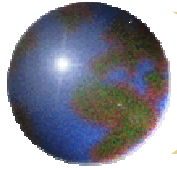


## **2. Advantages of a large country**

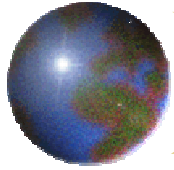
- ❑ Scale economies in the provision of public goods: national defense, monetary and financial system, courts, police, diplomatic representation,...
- ❑ Increased security facing external aggressions



- ❑ Increased efficiency to internalise externalities between regions
- ❑ Insurance against localised shocks (recession or natural catastrophes).
- ❑ Size of the market as a factor of growth

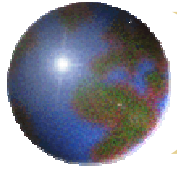


- ✪ Although some of these advantages are less clear with globalisation (see Alesina 2003)
  - ✪ Openness of international trade allows a small country to benefit from large markets
  - ✪ On the other hand, global problems of public goods and externalities require international arrangements: climate, financial markets, crime,...

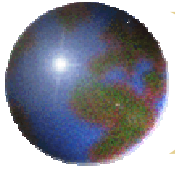


### **3. Management of local public goods and externalities:**

- Heterogeneity of populations and of geographic situations create different tastes for public goods and also specific (local) external effects
- Economic theory (fiscal federalism) teaches that decentralization is the best way to deal with these issues

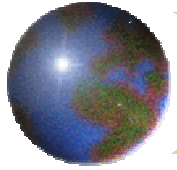


- ✦ France/FP: obvious heterogeneity (geography, culture, history,...) : different tastes for public goods and different problems of major external effects.
- ✦ Economic logic to have these issues dealt with at the local level, which may require various adaptations of french laws and regulations.



- ✦ **Examples:**
  - ✦ Protection of natural resources (sea, coral,...)
  - ✦ Coordination with neighbour countries (especially other Small Pacific Islands)
  - ✦ ...





## **4. Avoid separatism ?**

- ✚ The proliferation of sovereign states has not brought economic performances as expected (see Braun et al.)

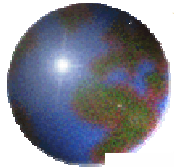


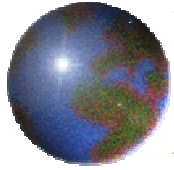
Table 4: Differences in growth rates between newly independent and other countries

Gained Independence from:		N	10 year			20 year			Maximum available years		
			Growth of newly independent countries	Difference:		Growth of newly independent countries	Difference		Growth of newly independent countries	Difference	
				OECD (tw)	Independent		OECD (tw)	Independent		OECD (tw)	Independent
France/Belgium	average	18	1.2%	-2.9%	-1.0%	0.9%	-2.3%	-0.8%	-0.1%	-2.4%	-0.9%
France/Belgium	median	18	0.8%	-3.2%	-1.5%	1.0%	-2.3%	-0.9%	0.1%	-2.3%	-0.8%
UK	average	27	3.1%	0.4%	1.7%	2.2%	0.1%	1.4%	1.8%	-0.2%	1.2%
UK	median	27	2.7%	0.2%	0.6%	2.0%	-0.2%	1.3%	1.6%	-0.3%	1.0%
Other	average	7	1.0%	-1.0%	-0.2%	1.2%	-0.9%	0.6%	1.2%	-0.9%	0.6%
Other	median	7	-0.6%	-2.0%	-1.3%	0.8%	-1.6%	0.1%	0.8%	-1.6%	0.2%
All	average	52	<b>2.1%</b>	<b>-0.9%</b>	<b>0.5%</b>	<b>1.6%</b>	<b>-0.9%</b>	<b>0.5%</b>	<b>1.1%</b>	<b>-1.1%</b>	<b>0.4%</b>
All	median	52	<b>1.8%</b>	<b>-0.9%</b>	<b>-0.1%</b>	<b>1.7%</b>	<b>-1.1%</b>	<b>0.3%</b>	<b>0.7%</b>	<b>-1.6%</b>	<b>-0.2%</b>
<b>Using different sample of countries and data</b>											
All	Average	61	<b>2.2</b>		<b>-0.6</b>						
All	Median	61	<b>2.8</b>		<b>-0.7</b>						

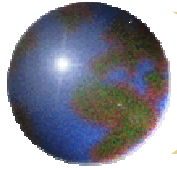
Source: Appendix 1.

<b>Niveau de PIB par habitant dans la Caraïbe (US\$ 2000)</b>					
<b>Pays encore dépendants</b>		<b>Pays devenus récemment indépendants</b>		<b>Pays indépendants depuis plus longtemps</b>	
<b>Pays</b>	<b>PIB par tête en parité de pouvoir d'achat</b>	<b>Pays</b>	<b>PIB par tête en parité de pouvoir d'achat</b>	<b>Pays</b>	<b>PIB par tête en parité de pouvoir d'achat</b>
Anguilla		Antigua			
Antilles Néerlandaises	8 200	Bahamas	8 200	Cuba	1 700
Aruba	24 400	Barbades	15 000	Haïti	1 800
Bermudes	28 000	Bélize	14 500	Rep. Dominicaine	5 600
Guadeloupe	33 000	Dominique	3 200		
Guyane française	9 000	Grenades	4 000		
Iles Cayman	6 000	Guyane	4 400		
Iles vierges	24 500	Jamaïque	4 800		
Iles vierges britanniques	1 6 000	St Kitt	3 700		
Martinique	15 000	Ste Lucie	7 000		
Porto Rico	11 000	St Vincent	4 500		
	10 000	Surinam	2 800		
		Trinidad	3 400		
			9 500		
<b>Moyenne</b>	<b>16 827</b>		<b>6 538</b>		<b>3067</b>

Source : Braun, M., Hausmann, R. et L. Pritchett « The Proliferation of Sovereigns : Are There Lessons for Integration ? », Document de travail, Harvard University, Décembre 2002



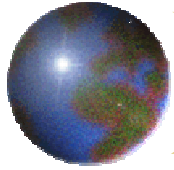
- ➊ Summary: in many respect the current political arrangement offers the potential of economic efficiency:
  - ➋ Advantage of a strong link with a large and developed European country (including aid and support of pro growth institutions)
  - ➌ While keeping the power to deal locally and originally with problems of local public goods and externality and postponing (?) the issue of separatism.



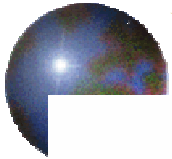
## *4. BAD GOVERNANCE*

### **1. Not so good legal origins**

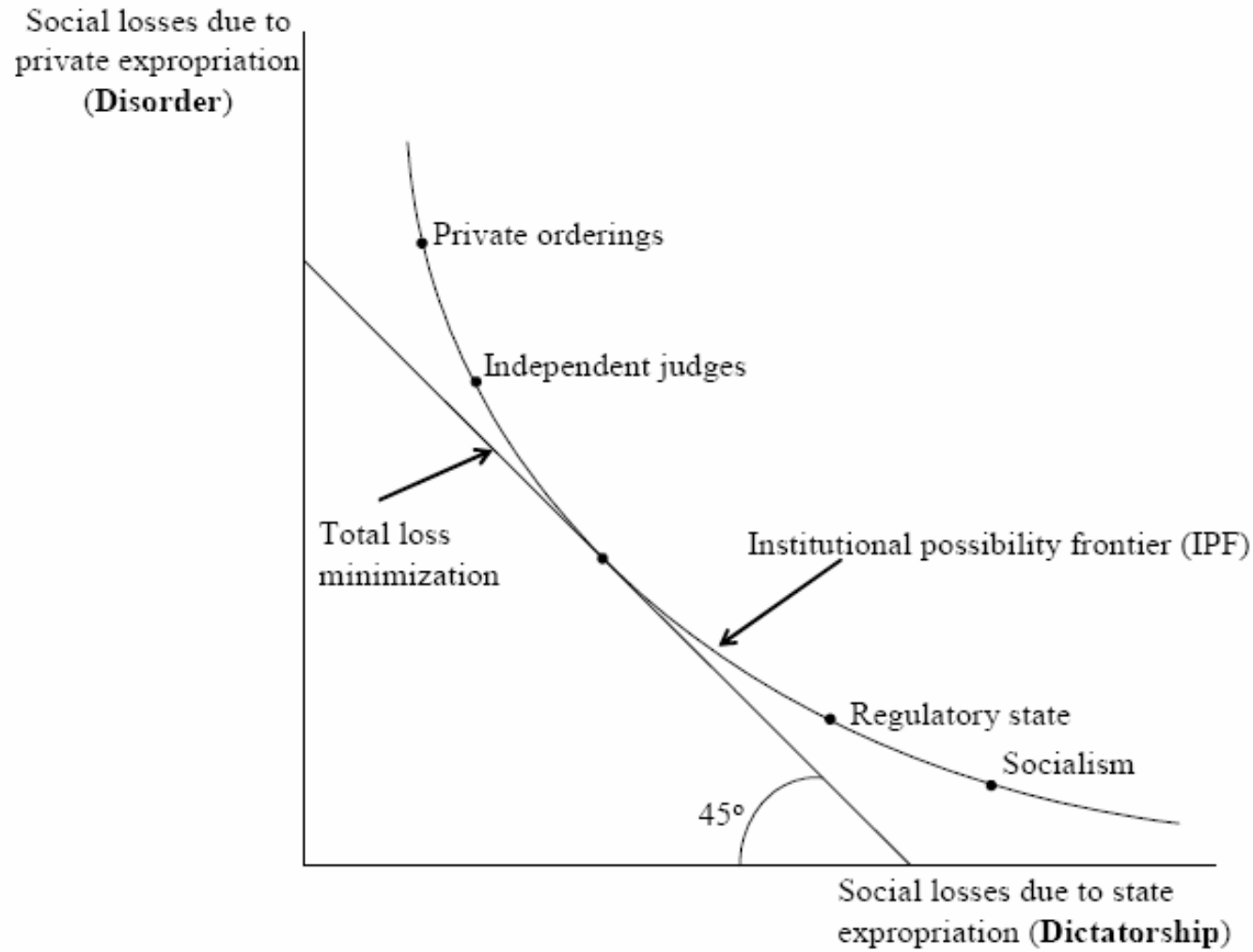
- ✚ France is not among the best rated country in terms of efficiency and quality of its institutions as a support of growth (see Djankov et al. and La Porta et al.)

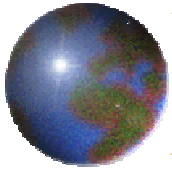


- According to Djankov and his colleagues efficient institutional arrangements minimize the social losses due to the risks of expropriation by private interests and expropriation by the State.
- In this respect France has chosen, through the system of civil law, to rely more heavily on regulation than say Great Britain which uses common law (see the two figures below).

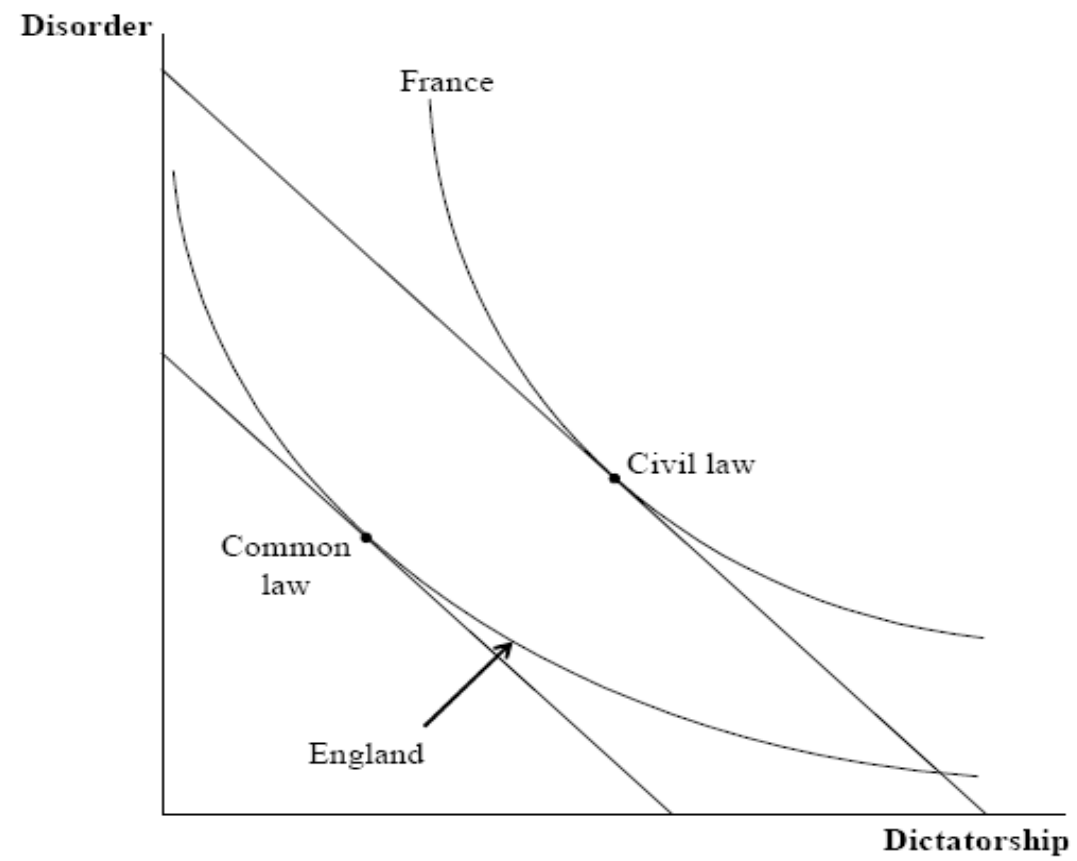


**Figure 1: Institutional possibilities**

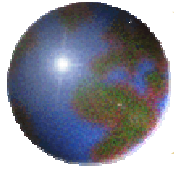




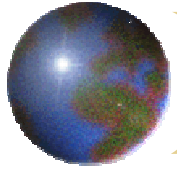
**Figure 2: Legal origins**





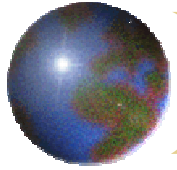


- ✚ In the end, a system less efficient seems to result in France.
- ✚ This conjecture is verified by the empirical study conducted by La Porta and his colleagues:
  - ▣ The quality of government is significantly lower in countries, especially developing countries, which have been influenced by the French system of civil law and corresponding regulations.

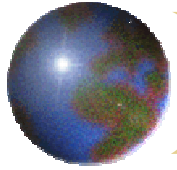


## **2. Loopholes in the institutional heritage**

- ✪ Antitrust laws: competition is one of the key elements of dynamic forms of capitalism; the French modern competition law of 1986, revisited several times until the recent creation of the « Autorité de la concurrence », has never been implemented, nor even adapted.

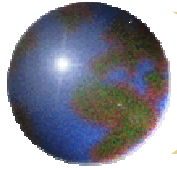


- ❖ Trade policy: could have been oriented in a modern way
- ❖ Relationships between the local government and the towns and villages administration; towns and villages depend on the territorial government for their budgets.

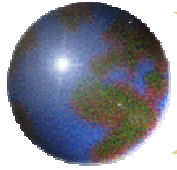


### **3. Local factors of bad governance**

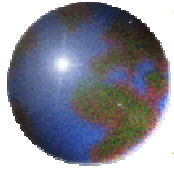
- ✚ Governments often institute policies which are bad for growth



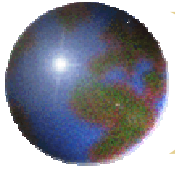
- ❖ « The abuse of public office for private gain –either by the head of government or by lower level officials – reduces growth by eroding the rule of law, among other things. Similarly, the desire to stay in power may conflict with actions that would promote economic growth » « D. Weil, *Economic Growth*, Pearson Addison Wesley, 2005.



- ❁ In FP, as in many other small countries, all the conditions are in place for bad effects of government action on economic growth
  - ❁ Small number of active firms
  - ❁ Many « natural monopolies » due to the high level of fixed costs with regard to the small market, justifying various types of regulations
  - ❁ Capital in the hand of a few number of families
  - ❁ Small number of lobbies with strong connections with politicians
  - ❁ High level of inequalities of income, wealth and human capital



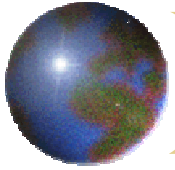
- Relative importance of the public transfers from France (around 30% of GDP, see above slide 12) with a considerable amount of discretion in their use by the politicians
- An important part of demand on different markets coming from the public sector
- All the conditions are met for having a high return of rent seeking behavior instead of a good returns of entrepreneurship and risk taking.



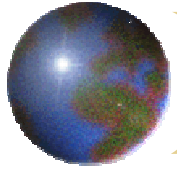
## ✦ **Capture of local governments (Bhardan and Mookherjee, 2000, and Bardhan, 2005)**

- ✦ The extent of capture of local governments relative to that of central government is a critical determinant of the welfare impact of decentralization.
- ✦ If local governments are equally or less vulnerable to capture than the central government, decentralization is then likely to improve both efficiency and equity.
- ✦ But the opposite may be the case when capture at the local level is much greater than at the central level



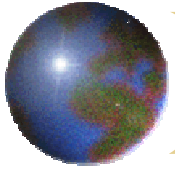


- ➊ Factors influencing the relative capture of governments at the central and local levels:
  - ▣ Levels of social and economic inequalities
  - ▣ Tradition of political participation and voter awareness
  - ▣ Fairness and regularity of elections
  - ▣ Transparency in decision-making and government accounts
  - ▣ Media attention

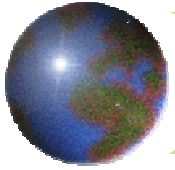


## 🌐 Bardhan: «

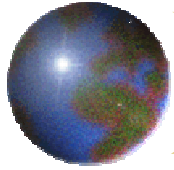
- ❑ In large heterogeneous societies, the elites are usually more divided at the national level, with more competing groups neutralizing one another.
- ❑ At the local level, in situations of high inequality, collusion may be easier to organize and enforce in small proximate groups (involving officials, politicians, contractors and interest groups);



- Risks of being caught and reported are easier to manage, and the multiplex interlocking social and economic relationships among the local influential people may act as formidable barriers to entry into these cozy rental havens. »



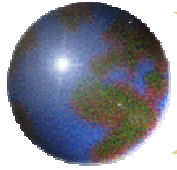
- At the central level in democratic countries more institutional mechanisms for checks and balances are usually in place:
  - these include various constitutional forms of separation of powers and adjudicatory systems in some countries,
  - more regular auditing of public account, more vigilance by public media, etc..
  - Much of which are absent or highly ineffective at the local level ».



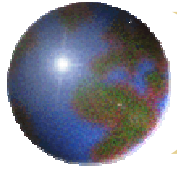
## ❁ Inequality: much higher in PF compared to France (mainland):

### ❁ Gini index :

- FP close to 0.5 (own calculations from the ISPF data, Etude Budget des familles, 2000-2001, p. 88))
- France mainland: between 0.26 and 0.33 (depending on the way it is estimated estimation 2004, source INSEE, OECD)
- Comparisons: average OECD: 0.31
- High levels: USA: between 0.36 and 0.45; Mexico around 0.5; Brazil:

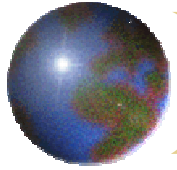


- ⊕ Political participation and voter awareness: evolving positively, but still dubious behavior (election of a Mayor still in jail)
- ⊕ Media attention: only a recent phenomenon (before 2004, only Tahiti Pacific and Toere as a sources of diversified information)
- ⊕ Close relationships between influential people (politicians, officials, interest groups,...)



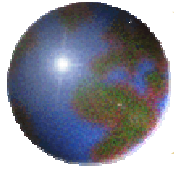
## 🌐 **Political Economy of Clientelism** (Robinson and Verdier)

- ❑ Clientelism: political exchange between a politician, a « patron », and a voter or supporter, a « client ».
- ❑ Politicians trade favors – policies – to a groups of citizens in exchange for political supports.
- ❑ Strategic issues: exchanges must be self enforcing
- ❑ Policies should generate excludable, reversible benefits

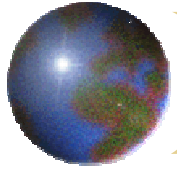


- Redistribution through jobs in the bureaucracy, or the public workforce (preferably non permanent) can work better for the politicians than spending in public goods provision or public investments





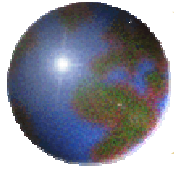
- Robinson and Verdier show that inefficient redistribution and clientelism become a relatively attractive strategy in situations with:
  - High inequality
  - Low productivity
  - Stakes from politics are high
- FP present all the conditions for effective clientelist policy



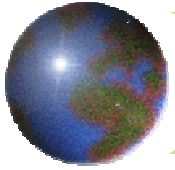
## ✦ **Economics of Kleptocracy**

(Acemoglu, Robinson and Verdier)

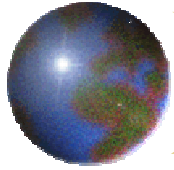
- ✦ Kleptocrats implement highly inefficient economic policies; serious impediment of development.
- ✦ How can they survive ?
- ✦ Collective action problem to depose a kleptocrat.



- This collective action problem can be exacerbated by divide and rule policy: punitive actions on some citizens and distribution of the benefits to others
- Made possible by the weakness of institutions

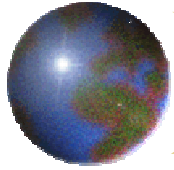


- ARV show that these policies are more likely
  - When foreign aid provide greater resources to buy off opponents
  - Opposition groups are short sighted
  - The average productivity in the economy is low.
- Again, FP offers a perfect example.
- Local politicians are not Mugabe or Mobutu and FP is not the Dominican Republic, however lots of cases of corrupt politicians disclosed by the medias (recently) and punished by the courts (very recently).

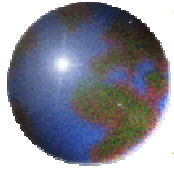


## **4. Local accountability mechanisms and political discretion in decision making**

- ✿ Bardhan (2005): « When the potential of capture of local governments is serious, decentralization programs have to focus a great deal of attention on strengthening local accountability mechanisms.

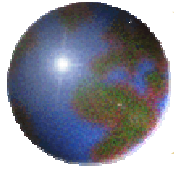


- ✦ Owing to the risks of bad governance the political status of self government should have tried to strengthen local accountability mechanisms and to avoid political discretion.



## 🌐 Quite the opposite is true:

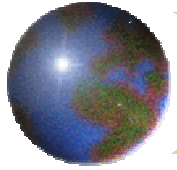
- 🗄 Accountability mechanisms have been weakened
- 🗄 Political discretion in decision making is systematically organised in the status
  - Fiscal advantages (« defiscalisation »)
  - Various authorizations: buying land; private occupation of the public domain; purchase of assets; entry on a market
  - Subsidies to subterritorial divisions
  - Subsidized employment (there is no unemployment benefit in FP)



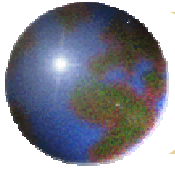
## ☉ Outcomes of bad governance:

- ☒ Mismanagements analysed by the Chambre Territoriales des Comptes (CTC); but it goes much farther than that
- ☒ Overcrowded bureaucracy and public or semi-public agents
- ☒ Heavy and inefficient regulations and political management of the economy
- ☒ Heavy barriers to new businesses
- ☒ Predatory monopolies
- ☒ Costly taxation



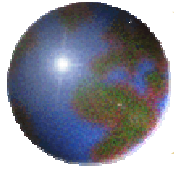


- ❖ The lack of competition only may cost more than 5% of GDP, that is at least 25 billions of FCFP in social welfare
- ❖ The bigger costs may be in the distorted incentives:
  - ❑ Efforts put in seeking rents
  - ❑ Disincentives to take risks



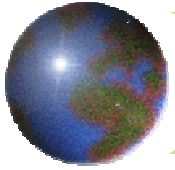
## *5. THE FUTURE OF FP: REFORM OR DECLINE*

- ❖ Predatory politicians have deliberately implemented bad policies in order to stay in power
- ❖ Most of the risks of bad governance are inherent to the institutions
- ❖ Where do we go from now ?



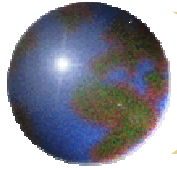
# **1. Two ways out the current status:**

- ❑ Further move towards independence (Temaru): impossible without an enormous impoverishment
- ❑ Return to a closer link with France (« departementalisation »): difficult to imagine at this stage of the process of political autonomy.

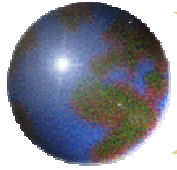


## **2. Reform within the boundaries of the current status**

- Take advantage of self government to implement the best institutions adapted to the local conditions:
  - Example of antitrust laws:
    - Why not imagine an optimal system inspired from Iceland, Malta, New Zeland, Jamaica, Papua New Guinea, ... ?
    - An original body (independent from the politicians and the local business) managing both competition issues and regulation of utilities.

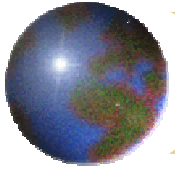


- ✪ But as in the case of Iceland, Papua New Guinea, it has to be imposed from outside the oligarchic/politician interests (EU in the case of Iceland, Australia in the case of PNG, WTO for the Carrabean countries).
- ✪ France had the opportunity before giving the self government status; now it is too late.
- ✪ Problem: the incentives to change.

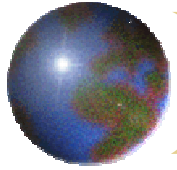


### **3. Reform by changing parts of the status of self government**

- ✪ Increase the constraints on politicians and the accountability mechanisms
  - ▣ Increased role of the CTC
  - ▣ Severity of courts
  - ▣ Promote competition and transparency in exchange for aid



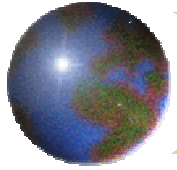
- ✚ Change the incentives of the politicians by changing the electoral rules
  - ▣ FP currently has the more corruption prone electoral system: proportional election with closed lists defined by the political parties.



✚ Most fundamentally and deeply: change the incentives of people (voters, middle class, poor people,...):

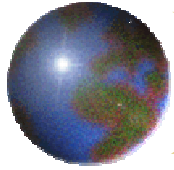
- ▣ Information
- ▣ Education
- ▣ Reduction of inequalities





## *Conclusion*

- ✦ FP an ideal laboratory for applying New Institutional Economics.
- ✦ Design of better institutions is not too difficult
- ✦ Polynesians must learn and decide.



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