

Commentaries and Applied Research for  
Practitioners and Educators

2. Financial Management

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FINANCIAL MANAGEMENT PROBLEMS IN  
SOUTH PACIFIC ISLAND ECONOMIES

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R.H. Juchau

The low-income island states of the South Pacific region may be characterised to a greater or less degree by limited natural resources, limited and or difficult land size, undiversified economies with a low range of economic opportunities, geographic isolation with relatively long distance to external markets, and dependence on imported goods and services. In addition they are economically vulnerable due to their limited export product range with high price volatility of major export items. Balance of payments problems, underemployment and high unemployment in urban centres, restricted access to finance markets and dependence on bilateral and multilateral aid further compound their economic problems. They are all preoccupied with economic development as the most effective means of raising income and employment and reducing dependence on foreign aid.

Economic development requires resources to be committed to public and private sectors to afford capital formation in such a way that balanced development occurs and efforts are made to ensure that natural and human resources, savings and capital are used economically and efficiently. Long term-permanent gain in development will depend on whether this efficient use of labour, capital and managerial resources is secured and maintained.

In large part the conduits for securing economic development are the public and private sector enterprises whose activities, if managed efficiently and effectively, will secure beneficial outcomes for the combination of labour, capital and management. Successful enterprises provide opportunities for expanded trade, growth in per-capita income and employment and reduced demand for foreign aid.

All of the island nations require the performance of their enterprises to be raised to reduce dependence on external aid and to assist the economic growth process. For some of the small economies (Tuvalu, Niue, and Kiribati) profitable enterprise diversification and foreign aid independence are unlikely prospects. The larger economies (e.g. Papua New Guinea, Fiji, and Solomons) however, have scope for their public and private sector enterprises to raise their profitability, diversity and efficiency levels.

**PACIFIC ISLAND STATES - SOME BASIC INDICATORS<sup>a</sup>**

	GNP 1983 (US\$m)	GNP per head (US\$)	Population 1983 (000s)
Fiji	1,190	1,790	670
Solomon Islands	160	640	254
Tonga	80	780 <sup>b</sup>	104
Vanuatu	40 <sup>b</sup>	350 <sup>b</sup>	127
Western Samoa	119	770	161
Papua New Guinea	2,510	790	3,197
Kiribati	30	460	61
New Caledonia	1,140	7,790	146
French Polynesia	1,260 <sup>b</sup>	8,190	154
Cook Islands	20 <sup>b</sup>	1300	18
Nauru	70 <sup>b</sup>	9090	7
Tuvalu	4 <sup>b</sup>	570	7

a. Source World Bank Atlas 1985.

b. 1981 Figures.

While these economies are enjoying the benefits of some enterprise success, there are signs that they are plagued by inefficient and unprofitable enterprises. Their financial management problems are, in large measure, attributed to their low accounting, budgeting and auditing capacity and the generally low financial management skills possessed by their personnel. Such low performing enterprises seriously jeopardise economic development, and, for many economies, resources, which can never be renewed, are wasted.

Past research investigations and reports on financial management in South Pacific economies allude to the problems of inefficient accounting systems, unsound internal control procedures, poor audit technology and ineffective budget systems [Juchau 1973, 1976, 1978]. These problems are also evident among other low-income countries where poor finance management skills and practices and inadequate staffing levels are cited as contributing factors [GAO, 1979]. There is also agreement for the South Pacific that its past and current problems can be attributed to the very low manning levels of skilled manpower in financial management and ineffective accounting systems and practices. These problems have been further documented by an Asian Development Bank report\* on accounting education for development (hereafter referred to as ADB, 1984).

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\* Proceedings - Asian and Pacific Conference on Accounting Education for Development - Manila 1984. Sponsors - International Federation of Accountants, Asian Development Bank and World Bank.

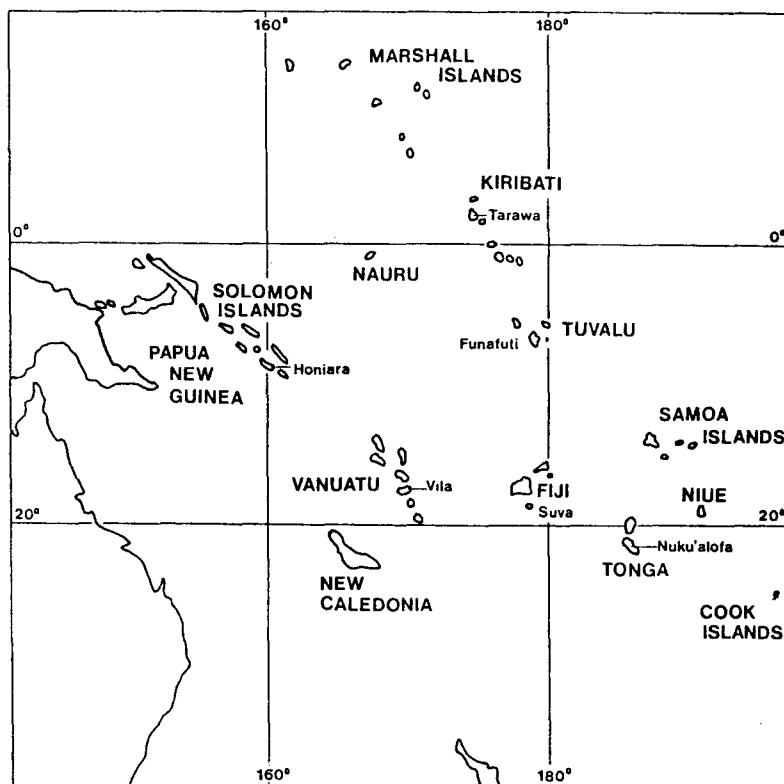
In most low-income countries (including those in the South Pacific) government enterprises are especially disadvantaged by inadequate financial management skills and practices. Numerous instances of fraud, debt mismanagement, and asset wastage abound and do much to sabotage the processes of securing permanent gains in national product. This plight of government financial management has been documented by Wesberry [ADB, 1984, p.132]. He claims that the following are typical and recurring problems in government financial management and reporting.

- Government financial statements, when they exist at all, are inadequate, fragmentary and untimely.
- Governments do not use financial information in making managerial decisions.
- Government financial management personnel are usually poorly qualified and little trained.
- Governments place little emphasis upon the importance of sound financial information.
- There is no agreement as to what constitute proper government financial statements.
- Accounting principles and standards have not been generally accepted by governments.
- Undue emphasis upon legal and budgetary controls defeats the purpose of sound financial management in government.
- The accountancy profession has rarely been accepted by government as authoritative in the field.

It is now over a decade since accounting manpower supply and financial management problems in the South Pacific were examined by the author. At that time evidence suggested that growth of enterprises and economies was being hampered by financial manpower shortages and failings in

accounting services and management skills. Since then almost all the economies have achieved independence, expatriate manpower in many of the professions has been substantially reduced, and localisation of senior executive management positions (marketing, administration, and finance) has moved on apace. The number of graduates from the post-secondary education system has increased and, in certain skill areas, the local talent pool has made some notable gains. Yet, despite these outcomes, the problems of enterprise failure and financial mis-management continue to dog the fortunes of these low-income economies.

To provide one picture of the continuing financial management problems within the South Pacific, press reports of these problems were gathered, for the period December 1984 to February 1986, from the South Pacific news media, in particular, items reported in the authoritative news journals, *Island Business* (IB) and *Pacific Islands Monthly* (PIM). The reports reveal a number of financial management problems, many of which continue to drain valuable financial resources and to frustrate the achievement of target growth rates in national product and income. The sections below summarise and discuss these reports. It is assumed that press reports are faithful representations of the events evidencing these problems. Of course reports focus on the misadventures and failings in financial management; successes are rarely reported! Undoubtedly there are a number of enterprises throughout the South Pacific which are prospering and, in their own way, have secured effective financial management practices.



### Crash Landing of Airlines

"Air Nauru has cut its fleet from seven to two, sacked or retired 26 pilots plus supporting crew, abandoned many services and reduced the remainder."  
PIM, Aug. 1985, p.7.

The period of this review witnessed a number of financial difficulties among many of the South Pacific region's airlines. Financial mis-management had a significant role in contributing to these difficulties. Airline operations in all regions of the world face major finance difficulties but generally astute financial management has enabled many of the airlines to survive, albeit with government subsidies and protection. Yet, in the case of the majority of airlines of the region it appears that government support was not sufficient to overcome difficulties arising from financial mis-management.



The region's airlines have faced and may continue to face the problems of over-provision and under-utilisation of aircraft and have failed to exploit economies of scale. Backgrounding this has been a trail of financial losses which have been attributed in part, to poor asset acquisition and deployment decisions and, in part, to poor funding management.

Air Pacific, which by November 1984 had accumulated losses of F\$38million, did not have the manpower skills and resources to salvage itself from its financial and managerial morass and was hampered both by inaccurate financial information and an accounting reporting system that was up to six months late. Airlines of the Marshall Islands has also suffered. Both the lack of cost control and the imprudent use of funds have placed its operations in jeopardy. Poor judgements on financing and on aircraft usage have also put Air Niugini and Air Nauru into severe financial difficulties.

To counter these difficulties Air Pacific (Qantas), Air Niugini (KLM) and Polynesian Airlines (Ansett) have all entered management arrangements with other airlines (bracketed) to put their operational and financial management into better shape. Longer term remedies have been proposed for the region's airlines. For example, a proposal has been made for a regional based aircraft leasing pool to outfit and supply aircraft. Part of the benefits

from such a proposal would be to integrate air and maintenance services both to raise utilisation and reduce major operational costs.

Whatever the financial outcomes are for the management and ownership schemes for the region's airlines, their financial expertise and systems require improvement if these high business and finance risk enterprises are to provide their countries with transportation services which will assist, not burden, their already much too fragile economies.

Public Financial Administration Awry

"... a monster with fifteen heads (Ministries) feeding off the country's revenues, providing diminishing services, and leaving little for development."

Solomon Islands Finance Minister,  
George Kejoa, PIM, Dec. 1985, p.55.

World-wide, public sector financial management has generally achieved some notoriety with respect to its ineffectiveness and inefficiency. In the context of some of the Island States of the region evidence indicates that this notoriety remains unchallenged. Public sector activity has been adversely affected by fraud, asset wastage, poor budgeting and inadequate financial controls, all of which illustrate the presence of low financial management performance.

An obvious concern is that of the shortage of skilled finance accounting manpower which thwarts efforts directed to raising the financial performance of the public sector. Governments throughout the region report difficulties in recruiting local and expatriate qualified accountants to fill critical vacancies in financial administration. The Central Bank of the Solomons, when commenting on the parlous condition of financial administration in their Government, argued that manning levels were critically low and that financial planning and management had to be strengthened as a matter of urgency. The tax authority in Papua New Guinea cannot recruit technical officers to administer taxation and is currently losing 50 million Kina a year in uncollected tax revenue. In Western Samoa there are continuing problems of filling key financial management positions in public sector trading enterprises which continue to experience major difficulties with accounting and internal control procedures.

Apart from shortages of manpower, more detail of which has been documented by the ADB (1984) report, accounting systems and procedures in many public authorities are not being employed to great effect. Island Business regularly reports embezzlements, mis-appropriations, theft, and misuse of funds in government departments and enterprises. Recent reports have focussed on Western and American Samoa, the Solomon Islands, Papua New Guinea and the Marshall Islands. These reports imply that controls and accountability were

astray. Furthermore, a number of the financial problems earlier referenced by Wesberry (1984) continue to bedevil many of the Government administrations and have been echoed in the ADB (1984) report.

Government administrations are limited by the amount of financial management skills that they can fund and supply. Their tax revenue base is narrow with limited scope for growth. Consequently limits are placed on the amounts of resources available for the development of effective financial management practice, especially where resource management is concerned. Also, financial controls and policies of administration are limited by the actions of politicians whose private and patronage goals often force procedures which by-pass prudent financial management practice.

Privatisation of government activity, international manpower aid programmes, external contract services (audit services), improved reporting systems and computerisation and more professional training and development have all been proposed as solutions to these difficulties. Governments, however, frequently lack the frameworks to capitalise on such initiatives and the resources sufficient to sustain the benefits and changes introduced through such initiatives. Further, while politicians fail to accept the discipline and consequences of efficient and effective financial management in government, those resources, directed to financial management improvement, will simply be wasted.

Private Sector Difficulties

"Papua New Guinea is desperately short of experienced and trained accounting and financial management personnel at both the professional and sub-professional levels." ADB 1984, p.157.

Throughout the South Pacific private enterprises are more competitive in the labour market and have relatively greater success in recruiting local and expatriate financial manpower. Further, these firms have accounting systems which are often inherited from or supported by international parent or associated firms. These factors confer advantages which public sector enterprises do not enjoy. Press reports of financial management difficulties among these firms appear less frequently. Their privacy and self interest concerns limit the reporting of adversities and losses arising from ineffective financial management. It is difficult, therefore, to secure a representative picture of the financial problems besetting firms within the private sector.

Comments by key accounting personnel (ADB 1984) operating from major urban centres throughout the South Pacific provided some indication of the state of financial management within the private sector. Shortage of skilled manpower continues to frustrate management even though they continue to out-compete the public sector for existing manpower and currently employ 80% of the qualified accounting manpower. As also reported (ADB 1984), the success of accountants and accounting systems continues to be hampered by:

(a) Attitudinal Factors

Cultural and social forces shape value systems which eschew accountability and accord low status to the accounting function and accountants.

(b) Technical - Functional Factors

Inadequate accounting reporting systems, poor formal training systems and the lack of financial reporting standards constantly threaten the maintenance of a minimal and acceptable accounting provision.

(c) Institutional Factors

Insufficient legislation and inadequate provision of university/institute education limit the control and supply of accounting skills.

Many private sector enterprises in the South Pacific have adopted accounting policies which endeavour to accommodate the difficulties of manpower shortages, unsympathetic value systems and low accountability. For example, credit sales in the retail and wholesale sectors have been minimised and or abandoned, credit review is more tight and systematic, internal control has been strengthened through more low level scrutiny of supervisor activity and financial documentation, computerised systems are more devolved with accent on mono-purpose functions and reports, external agencies - banks, audit firms, warehousing and transportation operators - have assumed a greater role in providing support financial services and advice, and the treasury and controllership functions have adopted a more interventionist role at lower levels of operations for various asset and equity decisions.

Despite these accommodations the private sector has its share of difficulties. In Fiji, many Fijian sponsored companies which were floated in the last decade have lost hundreds and thousands of dollars from a plain lack of management and financial knowhow. White collar crime is on the increase and this has been attributed by the Fiji Police Commissioner to the lack of proper internal audits and supervision. Many of the international subsidiaries operating in Papua New Guinea, Fiji and Western Samoa report inadequate returns on capital because of high operating costs, low product prices, and problems with accounting and control operations arising from accounting staff difficulties - turnover, quality, recruitment and deployment. These companies and other operators continue to report difficulties of securing acceptance amongst staff of the value of timely and accurate accounting information for improving decisions relating to working capital management and new investment.

Prospects of the private sector enjoying the benefits of a larger pool of qualified manpower depend on the efforts of governments and educational institutions to improve resources for manpower development. Government regulatory departments - taxation, audit, finance, attorney general - also need to insist on better financial reporting and accounting in their own undertakings and in the private enterprises they review and regulate. Through this action the public's conscience may be raised about the crucial role

good financial management can play in low-income economies. Long term, the partnership of the public and private sectors in effecting manpower improvement and securing attitudinal and behavioural changes empathetic with accountability, productivity and profitability is clearly critical to the process of economic development.

### Summary

The presence of ineffective financial management in the low-income nations of the South Pacific is an obstacle to the optimal use of resources available to improve national income and living standards. Effective financial management is critical. Its absence leads to resource wastage and inhibits economic development. To improve financial management all sectors need to embark upon a proactive financial management development programme. Some of the key elements in such a programme are summarised in the matrix below. These action proposals have been drawn from a survey (ADB 1984) of countries participating in the conference on accounting education in Manila. All have relevance, to a greater or less degree, to the principal island states of the South Pacific. On the limited evidence gathered from the principal news journals in the South Pacific, continued action is necessary if economic development is not to be hampered by ineffective financial management.



**SUGGESTED ACTION PROPOSALS FOR ACCOUNTING DEVELOPMENT**  
SOME KEY ELEMENTS (AFTER ADB 1984)

ACTION CATEGORY  TIME SCALE	TRAINING	PERFORMANCE	REGULATORY	PROMOTIONAL
SHORT TERM	Planned & well designed on-the-job training. Compulsory continuing education for accountants.	Introduce accounting and auditing standards. Press for improved accountability in the public sector.	Enforce application of accounting & auditing standards. Simplify regulatory laws, including taxation reporting requirements.	Programs to increase public awareness of the role of accounting in national economic development. Improve compensation & benefits to retain indigenous staff.
MEDIUM TERM	Upgrading of trainers & facilities. Develop state-of-the-art courses in educational institutions as part of continuing education.	EDP to be fully integrated in systems & auditing work. Establish review panels for quality control of accounting & auditing performance.	Require all practising accountants to hold specified qualifications & be registered. Legislate public finance & audit requirements particularly for control of capital markets, public sector & business generally.	No proposals
LONG TERM	Promote foreign accounting scholarships. Plan to match supply of trained personnel with demand by specified date(s).	Development of pertinent local standards derived from & compatible with international & other national standards. Expand the scope of work accountants & auditors to cover economy, efficiency, & effectiveness to provide more effective management tools.	Legislate the establishment & roles of professional bodies. Establishment of autonomous professional institute.	No proposals

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