Policy dialogue

# Managing volatile fishing licence revenues in the Pacific

Ron Duncan

Executive Director, Pacific Institute of Advanced Studies in Development and Governance, University of the South Pacific and Emeritus Professor, School of Economics, The Australian National University

For some Pacific island governments, fishing licences that allow distant water fishing nations access to the Pacific's tuna stocks are an important source of revenue. But these revenues are highly volatile because of fluctuations in the fish catch and in the price of tuna. While such fees are presently not a large component of government revenue in Fiji, there is the potential for them to become much larger. Therefore, consideration should be given to coping with the volatility. Running a country is difficult enough without having to manage large fluctuations in components of government revenue.

Kiribati is the Pacific country most dependent upon fishing licence fees for government revenue. Over the period 1991 to 2001, fishing access fees earned by Kiribati averaged $23 million in Australian dollars. However, during this period the revenue received ranged from a low of A$6.2 million in 1996 to A$46.6 million in 2001. In 1996 fishing revenues made up only 9.9 per cent of total Kiribati government revenue, while in 2001 they accounted for 54 per cent of total government revenue. It is extraordinarily difficult to have good fiscal management when the revenue side of the budget is so unstable.

Kiribati is the extreme example at present. However, if arrangements between the Pacific nations and the distant water fishing nations can be improved to the benefit of the Pacific—as they should—the share of government revenue from fishing will become a larger share of revenues for all governments. Therefore, the management of this volatility will become of great importance for all.

There are basically two ways in which the volatility of revenue streams such as fishing licence fees (or logging and mining revenue streams) can be managed to reduce the instability of government revenue. One measure is to place the revenues in a separate account and to try to transfer a (reasonably) stable amount from this separate account to the government budget each year. This is what Botswana does with its revenue from diamonds, which also have highly volatile prices. The Botswana government protects these revenues by holding them offshore in an independently managed trust account, thus making it harder for politicians to get at them. It is no accident that Botswana has been one of the fastest growing countries in the world for many years.

## Policy dialogue

The temptation of holding the revenues on-shore was obvious from the experience of the PNG Mineral Resources Stabilisation Fund. In that case the government revenues from mining were held by the Central Bank. However, through one means or another the government's draw-down on these funds was such that the revenues collected in each year were mostly spent in that year. So effectively there was no stabilisation of the government budget revenue.

Kiribati and Tuvalu can manage the volatility of their fishing revenues in the same way as Botswana by placing them directly into their country trust funds (the Kiribati Revenue Equalisation Reserve Fund and the Tuvalu Trust Fund). The moneys held in these trust funds are invested offshore in government securities and equities by commercial fund managers. The governments could then draw out a more stable amount from the fund each year for the national budget. There are two major problems with this means of managing the fluctuations in the fishing revenues. First, the trust fund is subject to the volatility of exchange rates, bond markets and stockmarkets and therefore it is impossible to have a stable drawdown from the fund. Second, by managing the volatility of fishing revenues in this way, the country bears all the risk.

A better way to manage the risk in the volatility of the fishing licence fees is to devise a means whereby the country does not have to bear any, or only a small part, of the catch and price risk and the risks of managing the reserve fund. This can be done by passing the risks back to the major fishing companies, which are in a better position to manage these risks than the small Pacific island countries. One means of doing this is to negotiate multi-year contracts with the distant water fishing nations that involve a fixed yearly payment over the term of the contract. However, this form of contracting has an in-built problem in that the distant water fishing nations has more information about the likely catch and the likely price than the country owner of the resource.

A means of overcoming this 'information asymmetry' problem is to auction quota rights to access the fishing grounds. By forcing fishing firms to bid against each other through an auction, they have to be more 'truthful' about their likely catch and the expected fish prices. In exchange for, say, a five-year fishing contract, firms could be asked to bid a fixed 5-yearly stream of payments. This form of controlling access to the fishing grounds would maximise the revenue from the resource while minimising the extent of under-reporting of fish catches as well as minimising the costs of monitoring under-reporting and illegal fishing. By forcing the fishing firms to pay the maximum access fees, they will be more likely to monitor illegal fishing activity that could interfere with their own performance than at present where the licence fees are estimated to be well below the true 'resource rent'.

Under these arrangements the Pacific Island governments would know five years in advance what their fishing licence revenues would be. This would introduce the desired stability into the governments' consolidated revenue and budget planning.

As with all auction systems there is bound to be some concern about collusion in tendering. However, with something like 1,300 vessels from up to 10 countries fishing Pacific waters, it is hard to imagine that the bidding process cannot be made competitive. Indeed, the auction system can be used to introduce much greater competition than the existing system, with its accompanying suspicion of 'side payments' to ensure the allocation of licences to particular interests.