

**STRENGTHENING PUBLIC FINANCIAL MANAGEMENT (PFM):
THE CASE OF TUVALU**

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Statement of Originality

I hereby certify that the intellectual content of this thesis is entirely my own work. Any assistance received in its preparation and all sources used have been appropriately acknowledged. This thesis has not been submitted for any other degree or purpose.

Katoa (Toa) P. Sailusi

Acknowledgement to the Traditional Owners of the Land

I would like to acknowledge the Indigenous people of Australia, recognizing their enduring connection to land, water, and culture, and express my solidarity with their ongoing struggle for justice and equality. I pay tribute to the traditional owners of the lands where this work was undertaken: the Gadigal people of the Eora Nation, as well as the Gadigal, Wangal, and Bediagal clans of the Dharug Nation.

I also acknowledge the traditional owners of the lands where this work was conducted in Tuvalu, including the Government, island communities, and especially the people of Niutao Island. I extend my gratitude to the experts who have contributed to the quality of data, analysis, and evaluation of public financial management and sovereign debt.

I pay my respects to the elders, leaders, and advocates for freedom, fairness, and equity past, present, and future in both Australia and Tuvalu. Their dedication has illuminated many complex public issues that demand greater attention and action.

Abstract

Recent studies on public financing, budget deficits, and debt sustainability in the Pacific region have emphasized the centrality of public financial management (PFM) theory and systems. Aid donors and financial institutions argue that PFM, as a component of good governance, can not only improve financial transparency and accountability but also fosters growth and financial stability. Literature on PFM highlights the crucial role of regulatory and normative institutions in strengthening financial mechanisms within the budgetary process, planning, and execution.

This thesis investigates the role of public financial management systems in Tuvalu, with a focus on how institutional elements – regulative, normative, and cognitive – shape fiscal outcomes, resilience, and sustainability in a small-island context. Regulative institutions offer legal enforcement and fiscal discipline; normative institutions embed social values like shared ownership (*kaitasi*), strategic choices (*kai filifili*) and inclusive dialogue (*fakapotopoto*); and cognitive institutions shape how communities understand and engage with fiscal systems. While global donors and financial institutions have traditionally emphasized regulatory and normative systems, this study finds that in Tuvalu, cognitive institutions such as kinship networks, community councils, and churches exert equally powerful influences on fiscal discipline, budget planning, and execution. These institutions help embed local social norms, belief systems, and communal values into financial practices, ensuring that fiscal policies align with culturally rooted approaches to sustainability and collective well-being. Blending old and new institutional economics (OIE and NIE) through collaborative fiscal strategies, participatory audits, and community-driven governance can enhance both local legitimacy and national resilience.

This study highlights the importance of integrating Tuvalu’s traditional governance systems, particularly the *maneapa* and *Falekaupule* systems, into modern public financial structures and processes. While modern governance relies on formal laws, audits, and international standards, Tuvalu’s indigenous systems rely on relational accountability, oral traditions, and communal trust. The thesis argues for hybrid strategies that combine formal and informal mechanisms in institutional pillars – regulative, normative and cognitive institutions – creating multi-layered accountability (communal accountability and scorecards) that enhances fiscal legitimacy and reduces financial risks. Such integration ensures that PFM reforms are not only administratively effective but also socially and culturally resilient, fostering stronger local engagement and long-term sustainability.

The contribution of the thesis is showing how ecological and shared ownership between regulative, normative and cognitive institutions can reshape Tuvalu's PEFA (Public Expenditure and Financial Accountability) assessments. It argues that climate-related risks, environmental sustainability, and non-market contributions, often overlooked in standard PFM models, must be integrated into fiscal planning and budgeting. Traditional governance structures and ecological thinking can strengthen PEFA's pillars on budget reliability, resource allocation, and fiscal risk management, ensuring that Tuvalu's PFM system is prepared to address both economic and environmental vulnerabilities.

Together, these findings conclude that meaningful PFM reform in Tuvalu must weave together formal and informal systems, structures, and processes that recognize the critical role of cultural, social, and ecological factors in reducing financial risks, and also in improving governance, and ensuring the long-term sovereignty and sustainability of small island economies like Tuvalu.

Key Terms: public financial management, sovereign debt, budget, public expenditure and financial accountability (PEFA), traditional institutions, institutional arrangement

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I would like to acknowledge the use of artificial intelligence tools, specifically AI-assisted language models, in the preparation of this thesis. These tools were employed exclusively for grammar checks, clarity improvements, and refinement of sentence structure. All substantive content, analysis, interpretations, and conclusions presented herein are entirely my own work.

The AI functioned solely as an aid to ensure proper grammar, coherence, and academic writing style, without contributing to the generation of original research material or ideas.

List of Abbreviations

ADB	Asian Development Bank
AUD	Australian Dollars
CBAR	Community-based Audit Reviews
CPU	Central Procurement Unit
DBT	Development Bank of Tuvalu
DDC	Development Coordination Committee (DCC)
DSA	Debt Sustainability Analysis
FTF	<i>Falekaupule</i> Trust Fund
GFC	Global Financial Crisis
GFS/COFOG	Government Finance Statistics/Classification of the Functions of Government
GDP	Gross Domestic Products
IMF	International Monetary Fund
ISSAI	International Standards Supreme Audit Institutions
ISAI	Supreme Audit Institutions (duplicate of SAI, clarified)
LMS	London Missionary Society
MFED	Ministry of Finance and Economic Development
MIRAB	Migration, Remittance, Aid, and Bureaucracy
MPUI	Minister of Public Utilities and Infrastructure
MTEF	Medium-Term Expenditure Framework
NAFICOT	National Fishing Corporation of Tuvalu
NBT	National Bank of Tuvalu
OAG	Office of Audit General
OECD	Organization for Economic Co-operation and Development
PEFA	Public Expenditure and Financial Accountability
PERMU	Public Enterprise Reform and Monitoring Unit
PBB	Performance-based Budgeting
PFM	Public Financial Management
PFTAC	Pacific Forum Technical Assistance Centre
PIC	Pacific Island Countries
PPP	Public-Private Partnerships
RFP	Requests for Proposals
ROE	Return on Equity
SAI	Supreme Audit Institutions
SIDS	Small Island Developing States
SOPs	Standards of Operating Procedures
SOE	State-Owned Enterprises
TEC	Tuvalu Electric Corporation
TNPF	Tuvalu National Provident Fund
TTF	Tuvalu Trust Fund
ZBB	Zero-Based Budgeting

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CHAPTER 1. INTRODUCTION

Improving our understanding of public financial management is crucial as nations seek to correct fiscal imbalances stemming from the global economic and financial crisis. – Clay West, senior editor, International Public Management Review (2021)

In the context of institutional theories and world-wide discussions, this thesis acknowledges the common challenges of public financial management (PFM), while highlighting the particular challenges of public finances and sovereign debt in Tuvalu that impact its effectiveness. The key issues of public financial management in Tuvalu stem from its unique characteristics as a small, aid-dependent, and climate-vulnerable Pacific Island economy. The major issues include limited institutional and human resource capacity, weak budget credibility and execution including investment management deficiencies, inadequate internal controls and oversight, and challenges in state-owned-enterprises (SOEs). All these issues have questioned the effectiveness and efficiency of PFM in Tuvalu and the value for money. This study explores whether PFM can strengthen fiscal discipline and reduce financial risks in Tuvalu.

What is value for money and public financial management?

In order to understand the role of PFM and how it strengthens fiscal discipline and reduces financial risks, we ought to understand the idea of value for money. The idea of value for money (VFM) frequently refers to the optimal use of resources to achieve a desired outcome. It often conveys the financial story of whether public funds are spent efficiently, effectively, economically, and equitably. Understanding how public funds are used and managed is difficult unless we have a predicated measurement. According to H.M. Coombs and D.E. Jenkins, VFM can be classified into three main components:

Economy: The practice of management of sound housekeeping and the virtue of ‘thrift.’ An economical operation acquires resources of appropriate quality and quantity at the least cost.

Efficiency: Making sure that the ‘maximum useful output’ is gained from the resources devoted to each activity or, alternatively, that only the ‘minimum level of energy’ and work necessary is used for a given level of output.

Effectiveness: Ensuring that output from any given activity is achieving the ‘desired result’ (Coombs & Jenkins, 1994, p. 2).

Recently, the World Bank Group has defined value for money as the means for achieving the optimal combination of benefits and costs in delivering services users want (World Bank, 2024).

Public financial management is a tool that attempts to effectively manage VFM through cost-benefit analysis (CBA) of public service delivery towards the most useful of outputs. Value for money directly impacts personal well-being, societal stability and the overall economic health of a country. It ensures efficient public spending, promotes evidence-based decision-making, as well as transparency and accountability. Value for money resonates not only in developed countries like Australia, New Zealand and the United States (US) but also in many developing countries in the Pacific such as Tuvalu.

Because Tuvalu has a small economy with limited resources such as fishing licenses, aid, dot.tv domain, and its Tuvalu Trust Fund (TTF), ensuring every dollar spent is worthwhile is critical. This means reducing waste, inefficiency, and unnecessary expenditure to deliver tangible results such as functioning schools, accessible health facilities, safe drinking water and disaster-ready infrastructures. The promotion of VFM also means a fair distribution of limited resources so that all Tuvaluans, regardless of location can benefit from public spending.

Threatened by sea-level rise, government spending in Tuvalu must create lasting value through climate-resilient infrastructure and sustainable agriculture initiatives that benefit future generations. In this context, VFM must also involve robust systems of monitoring, evaluation, and inclusive community participation. Such mechanisms not only safeguard against mismanagement and corruption but also reinforce public trust that limited resources are being used for the ‘common good’.

Moreover, VFM should integrate equity considerations, ensuring that investments reach vulnerable outer islands and marginalized populations. Strengthening local institutional capacity is equally critical so that public investments can be planned, implemented, and maintained by Tuvaluans themselves, rather than relying solely on external technical assistance. Thus, VFM must be linked to long-term fiscal and environmental sustainability, ensuring that today's spending does not compromise future resilience or create hidden liabilities, such as maintenance burdens or maladapted infrastructure.

Effective PFM frameworks, particularly on robust budget management and expenditure controls, are essential for sustainable public financing, especially in the management of public debt. Weaknesses in these areas often lead to excessive borrowing and fiscal instability, where public money is wasted and mismanaged. Richard Allen, Richard Hemming and Barry H. Potter have highlighted the importance of government, either developed or developing, in seeking ‘best practices’ that can effectively resolve the current unpredictable global crises and improve the value of money, by correcting fiscal imbalances and sovereign borrowing risks that weaken their institutions and sovereignty (Allen, Hemming, & Potter, 2013).

Despite the good intentions of PFM reforms, they cannot compensate for the long-standing fiscal deficits and their cumulative impacts on institutions and governance (Allen, Hemming, & Potter, 2013). Alternative approaches for effective management of public resources and funds are required. Indigenous knowledge and institutions fill these missing gaps. Through traditional institutions, particularly cognitive institutions in Tuvalu, we can find ideas, practices, and shared knowledges that can enhance the current public financial management systems.

However, the unique features and institutions of the Tuvaluan context has not been fully recognised in PFM. In this thesis, I respond to this gap by proposing the significant roles of regulative, normative and cognitive institutions. It argues that elements of cognitive institutions, such as shared beliefs, values and cultural norms, particularly influence the effectiveness and efficiency of public financial management.

Reality of Public Financial Management Reform

Ensuring the efficient and transparent use of public resources to achieve government objectives is a difficult task. Proponents argue that PFM is framed and communicated as a reform tool through accountability and transparency of institutions, fiscal stability, improvement of service delivery, and sovereign debt management (ADB, 2011; Allen, El Rayess, Doherty, & Goel, 2020; Allen, Hemming, & Potter, 2013; World Bank, 2018; World Bank, 2013). PFM matters because it is the backbone of fiscal responsibility, good governance, and economic development, ensuring that public funds are used effectively to improve the lives of citizens.

PFM initiatives are shaped by the realities of accountability and transparency through ‘regulative institutions.’ (Acemoglu & Robinson, 2013). Douglass North (1991) defined

‘regulative institutions’ as laws, organizations, systems, and procedures that are available to governments to secure and use resources effectively, efficiently and transparently (Allen, Hemming, & Potter, 2013, p. 2). Effective regulative institutions reduce uncertainty, enhance accountability, and support sound macroeconomic outcomes (North, 1991; Andrews, 2013). Scott (1995) categorizes regulative institutions as the coercive power of laws and formal structures such as constitutions, government regulations, judiciary systems, audits and penalizing institutions that enforce mechanisms for formal rules, sanctions, and rewards (Palthe, 2014).

PFM also shapes reform quality through ‘budgeting’ (AusAID, 2023). Through budgeting, Tuvalu requires strategic alignment of limited resources and funds with the country’s top priorities. Given Tuvalu’s unique economic and physical features such as small revenue base, geographic isolation, and vulnerability to climate change, the implementation of regulative and normative institutions can link resource allocation and measurable outcomes and performance indicators (Allen, Hemming, & Potter, 2013; Visser & Erasmus, 2002). This would help direct funds toward programs such as education, healthcare, and infrastructure that can deliver tangible results, increasing accountability and efficiency.

PFM quality can also be envisioned and articulated through normative and cognitive institutions. Normative institutions are financial norms and values that are acceptable in Tuvaluan society. Normative standards are driven by societal approval (Niuatui, 1991; Palthe, 2014). These norms and values are also defined by professional standards that are regulated by the government and other regulative institutions. For example, adopting participatory budgeting where individuals and local communities have a say in resource allocation, effective approaches to budget allocation, distribution and management of limited resources can prevent wasteful spending.

In contrast to normative institutions, the ‘Pacific Way’ is the set of informal rules, norms, beliefs and institutions such as kinship, island communities, churches and meeting venues that constitutes the ‘cognitive institutions’ of shared values, beliefs and cultural norms in the context of Tuvalu (Palthe, 2014; Niuatui, 1991). The Pacific Way refers to a concept of governance, diplomacy, and community interaction that is deeply rooted in the traditions and cultures of Pacific Island nations. It emphasises cooperation, consensus-building, mutual respect, and a shared commitment to collective well-being, drawn from the region’s indigenous values and social structures (Kabutaulaka, 2021; Larmour, 2005). These are the institutional

economic features that Hodgson (2000; 2006) argues have significant impacts on growth and economic development.

The transformation in the conceptualization of PFM reform represents a complex and conditional process between informal rules and norms (i.e., the Pacific Way) versus more formal and modern regulative institutions (Hodgson G. , 2004; Hodgson G. , 1998). The manner in which PFM reform is currently framed as an opportunity for change has the potential to either facilitate or hinder the realization of meaningful outcomes. However, reform efforts have largely been constrained by a narrow emphasis on the management of public expenditure, which may limit the broader objectives of systemic improvement (Allen, Hemming, & Potter, 2013). Surveying the context of Tuvalu's institutions can dig a little deeper to explain the constraints of its current regulative, normative and cognitive institutions and the existing lack of PFM capacity to achieve positive results.

Institutional elements – regulative, normative and cognitive – can constitute obstacles or enablers for achieving effective public financial management between the informal and formal shared values, beliefs and norms that affect economic behaviours of public managers in Tuvalu. The original contribution of this thesis is the emphasis on how the specific crossing of regulatory and cognitive institutions is a significant factor in PFM and its capacity to reduce financial risks for a vulnerable economy like Tuvalu. The following proposals are the premises of my investigation:

Regulative institutions play a critical role in reducing financial risks in Tuvalu by enforcing legal and procedural frameworks that ensure transparency and accountability. These institutions, such as the Auditor General's Office and the Ministry of Finance, provide mechanisms for oversight, compliance, and sanctions that discourage fiscal mismanagement. By strengthening enforcement of public financial management systems, including budgeting, procurement, and debt control, Tuvalu can improve fiscal discipline and reduce vulnerabilities linked to corruption or inefficient use of public funds. This enhances donor confidence and ensures more predictable and responsible financial planning.

Normative institutions contribute to risk reduction by reinforcing ethical standards and values that guide the behaviours of public officials and institutions. In Tuvalu's community-based culture, traditional leaders, churches, and social norms play a key role in promoting responsible financial conduct and discouraging malpractice. When professional codes of conduct and moral

expectations align with national financial goals, it leads to greater public trust and accountability. Moreover, embedding participatory practices into budget processes ensures that fiscal policies are more inclusive and reflect collective values, reducing resistance to reform and improving implementation outcomes.

Cognitive institutions support financial stability by shaping how individuals and communities perceive and internalize economic and governance systems. In Tuvalu, where traditional knowledge and communal ways of thinking influence behaviours, financial policies must resonate with local understandings of stewardship, responsibility, and sustainability. Educating citizens about fiscal matters and integrating indigenous values into financial decision-making can create long-lasting cultural shifts. When financial policies are cognitively accepted as meaningful and legitimate, they are more likely to be followed and sustained over time, reducing risks associated with policy failure or poor adaptation.

Research Method

Given the lack of a universally optimal research methodology in the social sciences and political economy (Benton & Craib, 2011), it is essential for scholars to transparently justify their methodological approaches in ways that are comprehensible to both technical audiences and broader stakeholders. In the case of Tuvalu, the assessment of public financial management effectiveness and institutional resilience necessitates an interdisciplinary perspective, incorporating insights from economics, political science, and development studies. As Tuvalu navigates an increasingly volatile global economic landscape, the strengthening of its fiscal policy frameworks becomes not only a technical imperative but also a foundational strategy for safeguarding its economic sovereignty and long-term viability.

Building on the interdisciplinary framework outlined above, this study investigates whether public financial management can serve as a mechanism for reducing financial risks in Tuvalu. In this context, institutional analysis plays a critical role. Theoretical constructs such as regulative, normative, and cognitive institutions drawn from across the social sciences offer valuable lenses through which to examine formal rules, social norms, and shared belief systems (Scott, 2014). To ground this inquiry, the study conducts a comprehensive review of the PFM literature using academic databases from the University of Sydney, the University of Hawai‘i, and Brigham Young University–Hawai‘i (BYUH) Pacific Studies Library. Integrating these sources, the research adopts a *kaitasi*-informed approach, rooted in Tuvaluan principles of

collective responsibility and integration. This methodological choice underscores the importance of institutional interaction and synthesis across diverse knowledge systems in addressing complex fiscal governance challenges.

Furthermore, reviewing institutional models developed by both old and new institutional economic scholars such as Geoffrey Hodgson, Thorstein Veblen, John R. Commons, Douglass North, W. Richard Scott, and Elinor Ostrom offers valuable theoretical grounding for this study. These institutional perspectives help generate new insights into the effectiveness of public financial management in Tuvalu. By combining financial data and institutional analysis, this research evaluates the relationships between Tuvalu's government officials, international donors, kinship networks, churches, and local communities. It also examines how different economic assumptions, and financial terminologies influence the discourse and practice of financial governance. As noted by the Asian Development Bank (2019), misalignments in PFM frameworks can undermine effective communication, stakeholder engagement, and policy implementation challenges that are particularly relevant in the Tuvaluan context.

The research has been informed by background interviews with key stakeholders such as the Government of Tuvalu, public managers, aid donors, and academic experts, which has been vital in building the foundation of this study. Simplification of technical language has been crucial, particularly for engaging local public managers and understanding their perspectives on managing public finances in Tuvalu (Morgan et al., 2017). Additionally, observing how communities, kinship groups, and local governments make decisions with limited resources provides important insights into grassroots financial governance and how regulative, normative and cognitive institutions influence financial behaviours in PFM systems.

To assist with the presentation of data, this study has used Python programming and the Pandas library to clean, transform and analyse financial statements and raw data obtained from the Government of Tuvalu and aid donors. Key performance indicators such as government debt, fiscal deficits, public expenditures, and aid inflows are analysed, alongside indicators from previous PFM assessments and Public Expenditure and Financial Accountability (PEFA) statements, such as budget reliability, transparency of public finance, asset management, fiscal strategy and budgeting process, control and predictability, accounting and reporting including scrutiny and audit (McKinney, 2010; World Bank, 2024; PEFA, 2023). Furthermore, the application of the PEFA method enables a structured analysis of Tuvalu's fiscal governance

against international standards such as International Standards of Supreme Audit Institutions (ISSAI) as well as traditional structures and sustainability practices.

This research therefore brings together institutional insights and public finance analysis to better understand the ongoing challenges of fiscal and PFM systems in Tuvalu. In doing so, the research contributes to more transparent, inclusive, and resilient financial systems in Pacific Island Countries (PICs), offering evidence-based guidance for institutional reform and climate-responsive financial governance as many developing countries combat financial risks and unpredicted economic crises.

Research Framework

According to Scott (2014), institutional pillars – regulative (formal rules and enforcement), normative (values and norms), and cognitive (shared understandings) – shape financial and economic behaviours. In the context of Tuvalu, this tri-dimensional perspective is crucial because it explores formal financial policies that operate alongside strong cultural norms and community-based governance. Adopting this framework allows for a nuanced exploration of regulative institutions and public financial management realities as the study looks at various relationships of fiscal policies and sovereign debt both domestic and external, the budget processes, revenue collection and expenditure management (ADB, 2015).

Scholars like Hands (2001) and Dow (2021) have recognized that there is a significant transformation in economic methods and methodologies, highlighting a major shift from traditional normative approaches to a broader philosophical base that challenges established scientific rules and emphasizes analysing and understanding the science itself. This shift has led to the emergence of the ‘heterodox economics approach,’ (King J. E., 2013), which moves away from orthodox or conventional economics in favour of alternatives that focus on institutions, history, and social structures. More importantly, these approaches address real-life issues such as inequality, financial instability, unemployment, and climate change. As Dow (1996) highlights, the use of alternative methodological approaches is often crucial for uncovering effective solutions and fostering diverse perspectives in improving PFM.

This principle resonates with traditional Tuvaluan wisdom, where elders commonly explain that preparing the most flavourful taro (see Figure 1.1), a staple root crop in the Pacific, is not necessarily achieved by simply boiling it. Instead, incorporating ingredients such as sugar, salt,

and coconut milk enhances its taste and appeal. This culinary analogy reflects a broader critique of orthodox economic methodologies, suggesting that conventional, one-dimensional approaches may overlook the complexity of real-world economic dynamics, particularly in the case of Tuvalu where traditional ecological sustainability practices continue to govern strategic goals.

From a Pacific Islands perspective, mainstream economic models are akin to taro boiled in plain water – functional but lacking depth and richness. Consequently, adopting heterodox approaches, informed by multidisciplinary, evolutionary, and context-sensitive perspectives, may provide more effective responses to fiscal instability. In addition, they also emphasize power dynamics and the role of institutions in shaping economic outcomes.



Figure 1.1 Taro Roots. Source: Jenny Gensler (2021).

Historically, the role of institutions in reinforcing fiscal policy has often been underemphasized in broader discussions of governance and development (ADB, 2021; Acemoglu & Robinson, 2013; Chambers & Munro, 1980; Hodgson, 2006). Institutional theory offers a valuable lens for PFM research, as it highlights the influence of institutional structures, behaviours, and norms on financial governance and fiscal sustainability. This perspective helps to explain how public resource allocation, fiscal responsibility, and policy implementation are shaped by institutional dynamics and PFM elements such as regulative, normative and cognitive.

Institutional components such as regulative, normative and cognitive provide stability and meaning to social life and include symbolic systems, relational networks, and social routines embedded within government structures, non-governmental organizations, and community practices. Such elements are crucial in understanding the broader environment in which PFM operates. Palthe (2014) extends this framework by proposing a model for operationalizing these institutional elements from a micro-level perspective, offering practical insights into how institutions function in specific settings (see Figure 1.2).

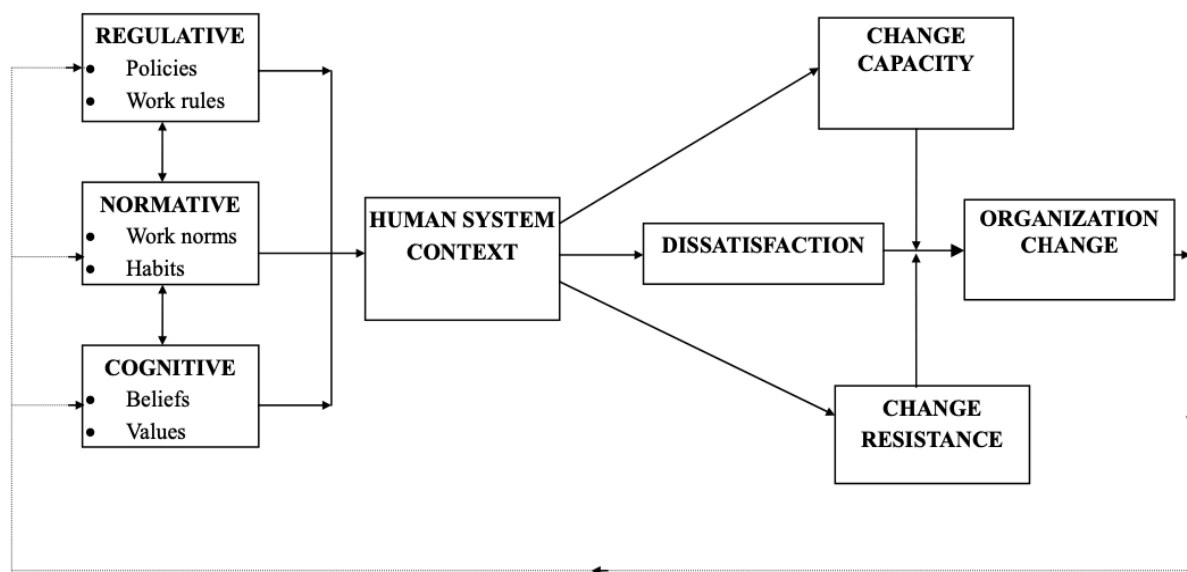


Figure 1.2 Institutional Theory and Change. Source: Palthe (2014).

Palthe’s framework highlights the three main elements of institutions and their impact on changing institutional behaviours. However, incorporating additional elements of institutionalism, such as interdisciplinary, evolutionary, and open systems approaches, can provide a deeper understanding of how PFM may influence financial risks in small Pacific Island Countries like Tuvalu. She also explains the flow of institutional elements: regulative, normative and cognitive elements interact in the process of changing organization behaviours through a ‘pluralistic approach’ (Heise, 2016).

When humans are dissatisfied with the status quo, Palthe (2014) argues that there are often two reactions to it: changing of capacity or resistance. Higher levels of resistance often lead to organizational behavioural changes as illustrated in Figure 1.2 above. The process of ‘deinstitutionalization’ (Oliver, 1992), linked to dissipation, may result from factors such as inadequate socialization, the intrusion of individual interests, or shifting circumstances that

render existing beliefs or practices obsolete (Scott, 1995). Consequently, dissatisfaction serves as a catalyst for organizational change, as depicted in Figure 1.2 above, the erosion of support for modern and colonial institutions norms or rules.

Hodgson (2006) states: “Institutions are the kinds of structures that matter most in the social realm; they make up the stuff of social life.” In ‘open structural systems’ (Krugman, Obstfeld, & Melitz, 2018) like Tuvalu, Hodgson (2004) argues that institutional economics reveals the key factors that can shape and constrain human behaviour. In the case of Tuvalu, institutions such as traditional structures (i.e., *Falekaupule, Kaupule*), land tenure systems, and cooperative systems in kinships, provide a lens to understand why programs like foreign aid, or sovereign funds, don’t easily plug into Tuvaluan economy and society.

The lessons learned from the exploration of these institutions and how they influence PFM and financial risks in Tuvalu not only provide guidance for more effective PFM but also how modern systems can interact with traditional structures. Looking into institutional characteristics such as social culture, language, beliefs, attitudes, ethnicities, and monetary and managerial practices provides a means to understand the effectiveness of PFM in allocating, distributing and managing Tuvalu’s limited resources.

Thesis Structure

This study is structured into three main parts that demonstrates how PFM is failing to reduce financial risks in a vulnerable developing country like Tuvalu. Part I focuses on the background of the study, definitions, history and emergence of public financial management (Chapter 1-2). Part II focuses on the institutional theory and its elements (Chapter 3-5). Part III addresses the incompatibilities of public financial management and lessons learned (Chapters 6-8).

The primary objective of **Chapter 1** has been to introduce and give background to the study. It explains the significance of making great decisions from good information in order to fully capture any value for money (VFM). This chapter has outlined the thesis’ method and framework, drawing on key arguments by old and new institutional economists Geoffrey Hodgson, Elinor Ostrom, Richard Scott, Douglass North and other contemporary institutionalists such as Allen, Hemming & Potter (2013), Schick (1998), DiMaggio, P.J & Powell (1983).

Chapter 2 aims to investigate the relationship between debt, public financial management, and regulative institutions in the delivery of public services to the citizens of Tuvalu. The chapter begins by drawing on Visser and Erasmus (2002) to define PFM and underscore its significance in achieving fiscal sustainability and effective governance. The analysis also considers the compounded effects of the COVID-19 pandemic on public finances and service delivery in the region (Bertram & Watters, 1984; Macdonald, 1998; World Bank, 2024).

Chapter 3 offers a regulative framework to analyse public financial management by focusing on regulative institutions – formal rules, enforcement mechanisms, and institutional accountability systems – that govern fiscal behaviour. PFM is conceptualised as a modern mechanism for strengthening public expenditure and ensuring financial accountability (Allen, 2013; Pollitt & Boukaert, 2000; Visser & Erasmus, 2002). This framework underscores the role of regulatory structures in addressing fiscal sustainability and promoting inclusive economic growth through transparent budgeting, effective debt management, and compliance with fiscal rules. The integration of these regulative elements is thus vital to mitigating financial risks and fostering a rules-based culture that upholds fiscal discipline in Tuvalu.

Chapter 4 develops a normative framework where normative institutions play a critical role in strengthening public financial management systems by embedding moral obligations, ethical routines, and professional codes of conduct into institutional frameworks. The integration of traditional values enhances rule-based governance, fosters fiscal discipline, and promotes transparency, particularly in budgeting, procurement, and audit processes (Udofia, 2017; USAID, 2024; UNESCAP, 2009; Transparency International, 2023; Tkachenko, 2020 ; Weber, 1947). These institutions shape individual and organizational behaviour, thereby increasing compliance, trust, and efficiency across the public sector. The adoption of normative frameworks is especially vital for improving the governance of state-owned-enterprises (SOEs) and education in reducing financial risks and aligning operations with the public interest as pointed out by IMF, World Bank and ADB.

Chapter 5 explains how cognitive institutions in Tuvalu such as kinship networks, churches, and island-based communities deeply influence economic behaviour and public financial management practices by shaping shared cultural values, beliefs, and expectations. Traditional systems are not merely social constructs but vital frameworks through which fiscal decisions such as taxation, savings, and public spending are interpreted and acted upon (Wood, Otor, & Dornan, 2021; Vallier, 2021; Niuatui, 1991). These institutions can either support or obstruct

the implementation of formal fiscal policies, depending on their alignment with communal norms and collective identities. As such, the effectiveness of PFM reforms in Tuvalu depends largely on how well they engage with and are informed by these cognitive systems, structures and processes. Understanding the role of informal institutions is therefore essential for designing socially embedded and culturally responsive financial systems that promote legitimacy, compliance, and sustainable governance outcomes.

Chapter 6 explores how the current Public Expenditure and Financial Accountability (PEFA) assessments in Tuvalu have proven ineffective in strengthening PFM due to the different approaches through regulative, normative, and cognitive institutional dimensions. From 2007 to the present, PEFA's seven core pillars have helped institutionalize fiscal discipline by reinforcing formal rules, legal compliance, and external oversight key features of regulative institutions. Simultaneously, ADB, World Bank, and the IMF argue that PEFA has supported normative development by promoting transparency, ethical standards, and accountability within the civil service. Fostering professionalism and shared moral expectations in cognitive institutions can improve PFM (PEFA, 2001) (PFTAC, 2010) (PFTAC, 2024). It has also influenced cognitive institutions by reshaping how Tuvaluan officials and communities perceive financial governance, aligning technical reforms with local cultural understandings of responsibility and stewardship. Thus, PEFA serves as a comprehensive framework that bridges global standards with local realities, advancing sustainable and socially responsive PFM in Tuvalu.

Chapter 7 offers insights to the *Kaitasi*, a traditional Tuvaluan institution rooted in communal cooperation and shared responsibility, which offers a culturally grounded framework for harmonizing modern public financial management practices with indigenous governance values. Peter Larmour, Barrie Macdonald, Geoffrey Hodgson, Elinor Ostrom, and others believe that bridging formal fiscal systems and traditional socio-economic structures enables a more contextually relevant and inclusive approach to managing public finances (Ostrom, 2000; Macdonald, 1998; Larmour, 2005; Hodgson 2005). *Kaitasi* strengthens fiscal discipline by promoting shared accountability at both national and community levels, while also mitigating financial risks through its emphasis on cooperation and equitable resource distribution (Niuatui, 1991). Integrating *kaitasi* into PFM reform efforts not only enhances policy legitimacy and social cohesion but also creates a more resilient and adaptive financial governance model suited to Tuvalu's unique institutional landscape.

Chapter 8 concludes that effective public financial management in Tuvalu requires a balanced integration of regulative, normative, and cognitive institutional dimensions. *Kaitasi*, as a traditional framework, provides a valuable means of integrating communal values with modern PFM practices. Altogether, these institutional elements can create a resilient, context-sensitive, and socially embedded PFM system capable of managing financial risks more effectively in Tuvalu.

**PART 1 – THE HISTORY AND EMERGENCE OF PUBLIC
FINANCIAL MANAGEMENT**

CHAPTER 2. THE EMERGENCE OF PUBLIC FINANCIAL MANAGEMENT

Men make their own history, but they do not make it just as they please; they do not make it under circumstances chosen by themselves, but under circumstances directly encountered, given, and transmitted by the past - Karl Marx (1952)

Introduction

This chapter examines the critical role institutions play in shaping public financial management. It defines what is PFM and why it matters for Tuvalu. It also describes its brief history and main drivers. Further, it explains the nature of PFM, the features or innovations and how it may be different from the usual public financial practices that have advocated in developing countries in the pursuit for economic growth and fiscal discipline.

The second section explores how institutional frameworks influence the development and implementation of public financial management systems that deals with sovereign debt - both domestic and external in Tuvalu. This section also highlights how sovereign debt shapes the governance structures, the budgetary processes, and fiscal policy. Institutions provide the rules, norms, and coordination mechanisms that guide the behaviour of public officials and stakeholders, which in turn affects the effectiveness of financial reforms and debt sustainability (Friel, 2017).

The section three explores how the current PFM systems have influenced the current budgetary processes, systems, and structures. As argued by March and Olsen (1989), institutions operate through a 'logic of appropriateness' (e.g., institutional norms, cultural expectations, formal rules and procedures) that shapes decisions and behaviours, playing a pivotal role in either enabling or constraining progress in PFM. In the context of Tuvalu, the emergence of structured public finance practices and evolving debt management strategies cannot be understood without recognizing the foundational role of these institutional dynamics: regulative, normative and cognitive.

Defining Public Financial Management

Public financial management has become increasingly important in Tuvalu, especially in light of rising debt and the management of public finances. Since Tuvalu entered the global stage in the 1980s, the country has been heavily reliant on foreign aid from its former colonial rulers,

including the United Kingdom (UK), Australia, and New Zealand, to supplement its annual budgets. In response to financial constraints, international institutions such as the Asian Development Bank (ADB), the International Monetary Fund (IMF), and the World Bank have provided technical assistance to support public reforms and promote PFM as a vital mechanism for ensuring fiscal stability and managing financial risks (World Bank, 2016).

While there is no universally accepted definition of PFM, scholars like Visser and Erasmus (2002) have offered insightful perspectives on the concept. According to Visser and Erasmus, PFM can be seen as an approach that integrates private sector budgeting practices into public sector financial management. They define PFM as a process involving multiple specialized aspects, including budgeting for anticipated revenues and costs, accounting for the receipt and disbursement of funds, purchasing goods and services, investing idle funds, managing financial risks, and ensuring legal compliance through audits and reviews. For Visser and Erasmus (2002), PFM is an inclusive process that manages the complexities of public financial operations, from revenue planning to long-term debt management.

Cangiano, Curristine, and Lazare (2013) further argue that PFM is a comprehensive system of information, processes, and rules designed to support fiscal policymaking and its implementation. They stress that PFM encompasses not only budgeting but also all aspects of managing public resources, including revenue generation, expenditure management, and debt management. The authors emphasize that effective PFM is integral to understanding and managing the medium- to long-term fiscal risks associated with policy decisions. This holistic approach to financial management helps governments address fiscal instability and contributes to sustainable economic development, particularly in small economies like Tuvalu.

Public financial management is a comprehensive system of laws, processes, and financial tools designed to manage public resources effectively. It encompasses key functions such as budgeting, revenue mobilization, expenditure management, accounting, auditing, and risk control, all aimed at translating national strategies into measurable outcomes and ensuring public accountability. PFM also adopts private-sector budgetary practices to enhance efficiency and transparency within the public sector. In managing both fiscal and non-fiscal risks, it maintains strong financial controls and promotes accountability among leaders, involving a broad range of stakeholders including political parties, civil society, auditors, and government officials who collectively influence short- and long-term financial outcomes.

PFM in Tuvalu represents a critical framework for managing the country’s finances, ensuring fiscal discipline, and promoting sustainable economic development. Through PFM, Tuvalu can address its fiscal challenges, mitigate risks, and make strategic decisions to ensure that public resources are used effectively and efficiently, contributing to the nation's long-term financial resilience. These key elements of PFM are summed up by Andrew Lawson (2015) (see Figure 2.1).

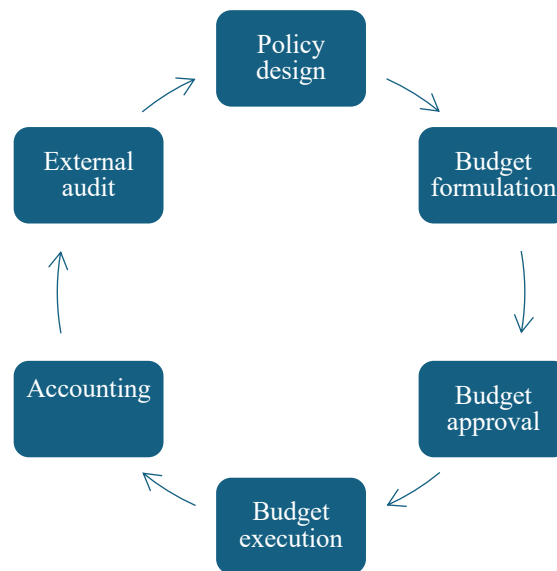


Figure 2.1 Public Financial Management Cycle. Source: Lawson (2015).

PFM promotes efficiency in the allocation, distribution and management of public resources. PFM can be traced back to the early 19th century when the need for formal financial governance grew. In European countries, the advent of ‘centralized budgeting’ (Shah, 2007) and expenditure control systems set the groundwork for modern PFM. The British Treasury, for instance, laid down foundational financial structures, with an emphasis on expenditure control and revenue management. This early system was largely designed to fund military and administrative costs (Allen, 2009). However, this approach to central budgeting can lead to lack of responsiveness of local needs.

During the mid-20th century, particularly following the World Wars, the importance of formalized financial management became even more apparent. As state functions expanded, especially with the rise of ‘welfare states’ (Esping-Andersen, 1990), the need for transparent and accountable financial systems grew. The United States (US) and United Kingdom (UK) implemented important budgeting reforms, which introduced formalized budgeting processes

and expenditure controls. These reforms included centralized budgeting mechanisms and the introduction of concepts such as budgetary reforms, financial accountability, and debt management (Fozzard & Simson, 2002).

By the 1980s and 1990s, the adoption of Public Sector Reform Programs (PSRPs) globally gained momentum, driven by the need to improve efficiency and reduce fiscal deficits. This period saw the rise of ‘New Public Management (NPM)’ (Hood, 1991), which sought to inject private-sector principles like efficiency, performance measurement, and outcome-based budgeting into the public sector. International financial institutions, such as the World Bank and the International Monetary Fund (IMF), played a key role in promoting these reforms in developing countries (Hood, 1995). The emphasis on efficiency and performance became central to PFM during this time.

In the 21st century, the focus of PFM shifted towards improving governance, transparency, and accountability. Globalization and the rise of civil society demanded greater openness in financial management systems of developed countries. The international standards such as the ‘Public Expenditure and Financial Accountability (PEFA)’ (PEFA Secretariat, 2016) and International Standards Supreme of Audit (ISSA) frameworks were introduced to help countries evaluate and improve their PFM systems. These standards encouraged countries to adopt reforms aimed at enhancing public financial management and reducing mismanagement of public resources (PEFA, 2005).

Today, public financial management plays a critical role in promoting fiscal discipline, efficient resource allocation, and long-term economic sustainability particularly in vulnerable economies such as Tuvalu. In the Pacific region, and especially in Tuvalu, the need for sound PFM is heightened by persistent budget deficits, rising debt distress, and the chronic mismanagement (e.g., corruption) of scarce financial resources. Effective PFM is not only a technical necessity but a fundamental pillar for achieving national development goals, reducing poverty, and maintaining macroeconomic stability. For these reasons, PFM has become a central theme in national development strategies and policy frameworks across (e.g. *Te Kete*, Public Finance Act). Regional and international partners, including development agencies and financial institutions, have increasingly focused on strengthening PFM systems as a pathway toward human development and institutional resilience (e.g., provide evidence).

External Characteristics of PFM

Public financial management is anchored by three foundational characteristics identified by Schick (1998), which collectively form the basis of an effective and accountable fiscal governance framework. These characteristics aggregate fiscal discipline, strategic allocation of resources (see Figure 2.2), and efficient service delivery are especially crucial for small, vulnerable economies such as Tuvalu, where resource constraints and exposure to external shocks make sound financial management essential.

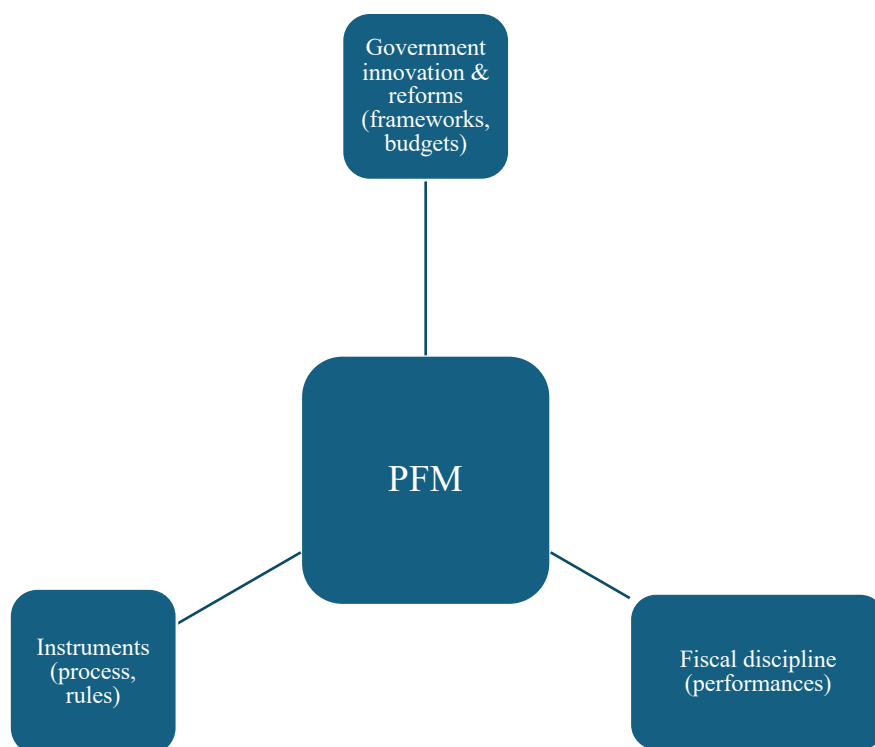


Figure 2.2 Characteristics of Effective Public Financial Management. Source: Allen Schick (2013).

Public financial management, as outlined by Schick (1998), is characterized by the government innovations and reforms, fiscal disciplines (i.e., performances), and instruments (i.e., process and rules). Budget instruments comprising formal rules, procedures, and institutional frameworks are essential for translating policy goals into equitable fiscal outcomes, particularly in Tuvalu where they support national development priorities such as education, healthcare, and climate resilience. These instruments enable transparent resource allocation and targeted investment in underserved areas, fostering inclusive development in rural communities.

Additionally, PFM emphasizes operational efficiency through robust monitoring and evaluation systems that ensure public funds are used effectively, build institutional

accountability, and encourage adaptive learning (ADB, 2015; Allen, Hemming, & Potter, 2013). In Tuvalu, where fiscal capacity is constrained, such mechanisms are vital for achieving value for money and sustaining trust in public institutions. Collectively, these PFM characteristics strengthen fiscal governance and resilience, which are crucial for addressing persistent budget deficits, rising debt, and external aid dependency in small island developing states.

In Tuvalu, the application of Schick's characteristics through Lawson's PFM cycle is not only theoretical but practical. Development partners such as the Asian Development Bank (ADB), International Monetary Fund (IMF), and World Bank have supported the strengthening of Tuvalu's PFM systems precisely to improve these aspects ensuring fiscal discipline, aligning spending with national goals, and enhancing public service outcomes, yet unfit to where local public managers can adopt.

The Economy and PFM

A small economy and limited revenue base are a reality in Tuvalu. Tuvalu's economy heavily relies on external revenue sources such as fishing license fees, remittances, and international aid, with limited domestic tax capacity. Tuvalu's persistent fiscal challenges reflect structural constraints rooted in its smallness and limited economic base. As economics and public finance researchers such as Peter Larmour, Barrie Macdonald, and Doug Munro argue, the small scale of Tuvalu's economy restricts the diversification of economic activities and increases vulnerability to external influences (Munro & Munro, 1985; Macdonald, 1998; Larmour, 1998).

The reliance on external aid and borrowing to manage fiscal deficits further underscores Tuvalu's dependence and highlights a significant vulnerability in its fiscal architecture. As the World Bank (2013) notes, such dependency reflects a structural imbalance between expenditure obligations and domestic revenue capacity. This dynamic not only challenges fiscal autonomy but also exposes the country to the conditionalities and volatility of external funding sources. During periods of heightened fiscal stress, this reliance can hinder strategic planning and reduce the government's ability to allocate resources based on national priorities. This 'structural limitation' fundamentally weakens the government's capacity to generate sufficient and stable domestic revenue, a core requirement for effective public financial management. As a result, Tuvalu's fiscal planning and budgeting processes are constrained by

a narrow and unpredictable revenue base, making long-term fiscal sustainability difficult to achieve.

In addition to structural limitations, Tuvalu’s economy is highly susceptible to ‘exogenous shocks,’ including global economic fluctuations and natural disasters. The COVID-19 pandemic (IMF, 2023) was one of the unpredictable events that encapsulates the danger of financial crises. This vulnerability, as noted by Iulai (2010), exacerbates fiscal instability by causing sudden revenue shortfalls and unanticipated expenditure demands. These disruptions create critical moments within the PFM system, requiring responsive and adaptive mechanisms that are often underdeveloped or externally dependent. The absence of robust fiscal buffers or countercyclical tools, such as monetary instruments - austerity, limits the government’s ability to mitigate these shocks through domestic means.

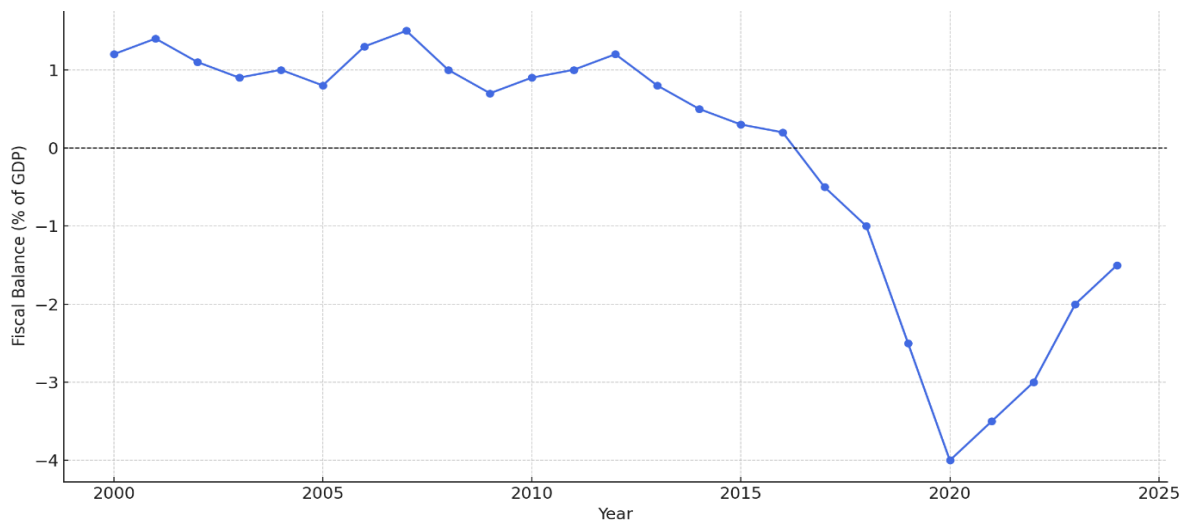


Figure 2.3 Tuvalu’s Fiscal Balance from 2000-2024. Source: International Monetary Fund (2024).

The policy responses adopted by Tuvalu in recent years particularly in response to external shocks such as the COVID-19 pandemic, climate-related events, and global economic downturns mirror the broader global strategy first deployed during the 2007–2008 U.S. financial crisis. Austerity responses often emphasize such as fiscal stimulus, external financial assistance, and state-led liquidity support, which are typically underpinned by capitalist market-oriented frameworks promoted by global financial institutions such as the IMF and World Bank (Diamond, 2013; Allen, Hemming, & Potter, 2013). Tuvalu’s reliance on development aid, concessional loans, and externally designed PFM frameworks such as PEFA reflects this repetition and limitations of PFM.

In this light, Tuvalu's repeated application of market-oriented, externally guided fiscal responses demonstrates the 'inflexibility of global capitalism' (Chang, 2008) to accommodate alternative development pathways for small and vulnerable economies. Yakovleva (2020) discusses the necessity of transitioning from a consumption economy to value preservation, where nation should protect their ecosystems and natural capitals. Furthermore, she argues that system thinking and collaboration among stakeholders to achieve long-term sustainability is essential. The result is not transformative reform but 'cyclical adaptation' (Yakovleva, 2020) (i.e., known as business cycles) within a constrained and externally defined economic paradigm.

Chang (2002) critiques the historical hypocrisy of advanced economies that now advocate strict market liberalization, despite having relied on protectionist policies during their own development. Sen (1999), while not rejecting capitalism outright, emphasizes its narrow focus on income and consumption, arguing instead for a development model grounded in capabilities and freedoms. Klein (2007) further underscores how crises are strategically exploited to push through inflexible capitalist reforms often without public consent thereby deepening structural inequalities and disempowering local institutions.

The COVID-19 pandemic significantly impacted the public finances of Tuvalu, which manifested as rising sovereign debt. This was caused by the decline in remittances, a fall in fisheries revenue, tourism halt, and global supply chain disruptions as shipping delays caused shortages and increased costs of imported goods, especially on commodities such as fuel and food. The reduction of government revenues due to the pandemic have caused fiscal strain and reduced the government's ability to finance key social programs such as healthcare and education.

The combined realities and impacts of the recent COVID-19 pandemic have posed a question on whether public financial management is effective in tackling some of the major economic challenges in Tuvalu such as sovereign debt and climate change? The overall impacts of the global pandemic have sent not only a negative impact on marginal population but also a linear downward sloping trend on key revenues sources of the Government from 2018 to 2022.

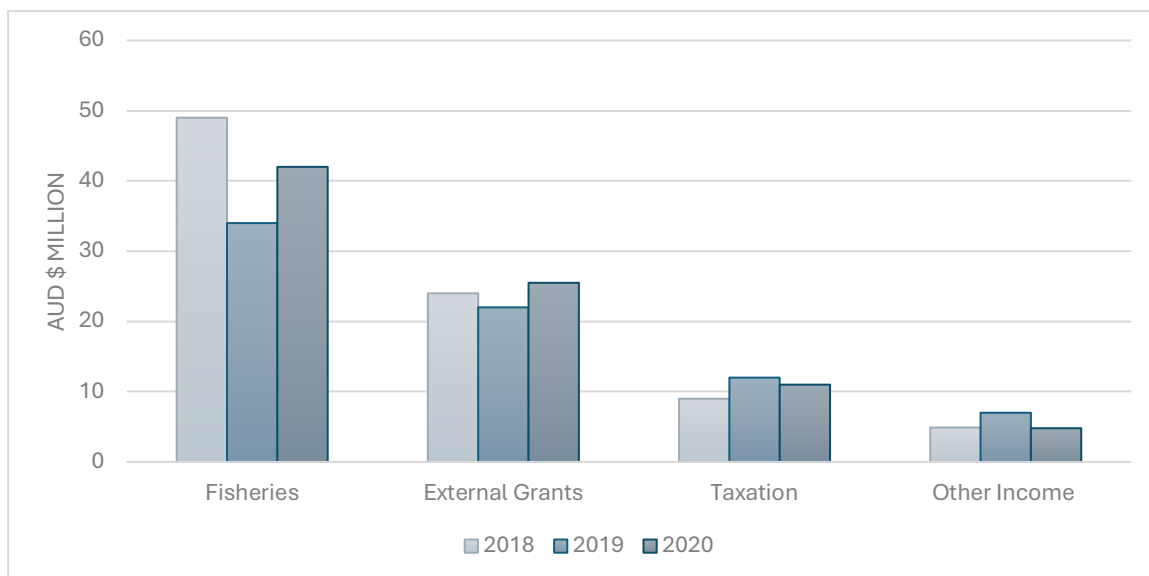


Figure 2.4 Revenues for Fisheries, Tourism, and Remittances. Source: Government of Tuvalu (2024).

The case of Tuvalu illustrates the critical need for contextually grounded PFM reform. The country’s administrative capacities, cultural frameworks, and political structures differ markedly from those of larger economies. When alternative reform models overlook these institutional realities, they risk becoming ineffectual or even counterproductive. In Tuvalu’s context, where governance is closely interwoven with community structures and traditional norms, PFM reform must be designed in a manner that is not only technically sound but also politically and culturally feasible.

Processes and Budgeting

The emergence of public financial management comes with the significant of role of the ‘budgetary process’ (Allen, Hemming, & Potter, 2013). It is a fundamental pillar, structure and system of PFM that serves as the primary mechanism through which governments plan, allocate, and monitor the use of public resources. It is also the process that is typically structured into several key phases, each serving a distinct purpose in ensuring fiscal responsibility, policy coherence, and institutional accountability (Allen, Hemming, & Potter, 2013).

The first stage, ‘budget formulation’, involves the strategic planning and preparation of the government’s financial blueprint for a given fiscal year. During this phase, ministries and agencies develop expenditure proposals based on projected revenues and national priorities. The Ministry of Finance plays a coordinating role, consolidating these submissions into a comprehensive budget plan. This phase is underpinned by macroeconomic forecasting, fiscal

policy frameworks, and alignment with national development strategies (Schick, 1998; Visser & Erasmus, 2002). Legal instruments, such as the Government of Tuvalu ‘Public Finance Act’ (Government of Tuvalu, 2008) and accompanying budget guidelines, provide structure and discipline to this process.

Following formulation, the ‘budget approval’ phase involves submission of the draft budget to the legislative body, such as Parliament, for deliberation and enactment. This stage embodies democratic accountability, as elected representatives scrutinize the allocations, debate their alignment with public needs, and may introduce amendments. Upon approval, the budget becomes a legally binding instrument authorizing public expenditure for the fiscal year (Allen et al., 2013; Goldsmith, 2005).

The third phase, ‘budget execution’, pertains to the implementation of approved financial plans. Ministries and public agencies begin disbursing funds to carry out public programs and services. This stage requires effective financial controls, procurement procedures, and cash management systems to ensure that spending is efficient and compliant with legal provisions. Monitoring mechanisms such as commitment controls and financial reporting help mitigate risks of overspending or misallocation (Schick, 1998).

‘Monitoring and control’ mechanisms operate concurrently with budget execution to assess performance and adherence to the approved budget. This involves comparing actual expenditures and revenues against forecasts and analysing variances. Governments may also undertake mid-year reviews and propose supplementary budgets where necessary. These practices are vital for maintaining fiscal discipline and responding to unforeseen economic conditions (Allen et al., 2013; Iulai, 2010).

The final stage is ‘evaluation and audit’, which ensures that public funds have been used effectively and for their intended purposes. Independent institutions, such as the Office of the Auditor General, are responsible for evaluating financial and operational performance. Audits provide critical insights into efficiency, effectiveness, and compliance, feeding back into future budget cycles to improve planning and decision-making. This stage enhances transparency and bolsters public trust in government institutions (Visser & Erasmus, 2002; New Zealand Auditor-General, 2022).

Throughout all phases, the ‘legal and institutional frameworks’ are essential for enforcing budgetary rules and maintaining accountability. The budget process integrates the roles of the executive, legislature, judiciary, and independent oversight institutions. Together, these ensure that the budget functions not just as a financial tool, but also as a strategic policy instrument for sustainable development and good governance.

The budget document, known in Tuvalu as *Fakasoaga o Tupe* literally translating to ‘financial plan’ functions as the primary policy tool reflecting the government’s fiscal position and strategic intent. It outlines total revenues and expenditures, performance metrics (i.e., KPIs), and economic forecasts. Embedded within this budget is also the concept of *Te Kete*, a traditional metaphor for knowledge storage and foresight, which captures the ‘forward-looking strategic orientation’ of national planning. *Te Kete* reinforces the idea that budgeting is not only a matter of fiscal calculation but also a ‘value-laden process’ (Ward, 2021) that considers societal well-being and long-term development.

By surveying the effectiveness of PFM tools such as budget management, financial controls, value management and governance to evaluate the financial sectors, systems, operations, and policies, we can find answers to how Tuvalu can reduce financial risks and improve fiscal discipline: careful budgeting, spending control, transparent financial practices and effective debt management.

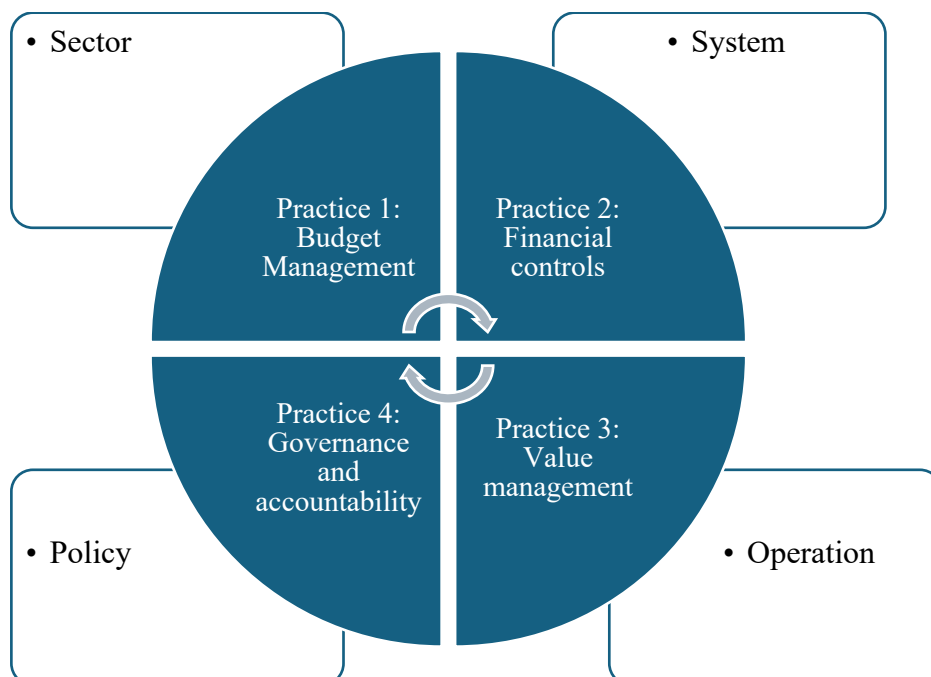


Figure 2.5 Effective Public Financial Management Model. Source: New Zealand Government Auditor General report (2012).

In the case of Tuvalu, the budget formulation is designed to align with its overarching development goals, particularly those set out in the '*Te Kakeega*' (Government of Tuvalu, 2016) national development plans. These plans highlight priorities such as infrastructure, climate resilience, education, and healthcare. The Ministry of Finance and Economic Development (MFED) plays a central role in coordinating the process, ensuring that ministerial budget submissions reflect national priorities. However, the limited technical capacity across ministries hampers effective translation of these policy goals into financially realistic plans.

Given Tuvalu's narrow economic base, budget formulation relies heavily on uncertain revenue sources like fishing licenses and the Tuvalu Trust Fund (TTF) as previously discussed. While the Trust Fund offers some financial stability, unpredictable income streams make accurate forecasting difficult. The MFED attempts to incorporate medium-term expenditure frameworks, but limited analytical capacity restricts the reliability of these forecasts, creating fiscal planning challenges and increasing vulnerability to external shocks.

Tuvalu uses expenditure ceilings to guide ministries during budget submissions. While this helps control spending, weaknesses in cost estimation and data availability often lead to unrealistic or under-costed budget proposals. The Budget Department reviews these submissions, but inconsistencies and poor data quality undermine the credibility and efficiency of expenditure plans, reducing their alignment with actual service delivery needs.

As a donor-dependent country, Tuvalu's budget formulation process is significantly influenced by development partners. Although joint donor coordination meetings are held, integrating donor-funded activities into the national budget remains challenging. Off-budget support can distort national priorities and weaken the comprehensiveness of fiscal planning, calling for improved coordination mechanisms and transparency in aid flows.

Debt Distress in Tuvalu

One of the key relationships that acquire details is the link between PFM and sovereign debt. With the shift of many developed and developing economies to capitalist systems where the increasing dominance of financial motives, market and economic actors and new institutional economics (NEIs) in the economy, traditional profit-making industries have focused only on

margins without much consideration on sustainability and ecology. This trend transforms corporate and public strategies with institutions – regulative and normative institutions prioritising financial engineering over sustainable investments in their operations.

This shift in financial engineering over sustainable has also shift in public management practices in Tuvalu by rather focusing on promoting sustainable and ecological approaches, market forces and sovereign debt has been the essential debate of fiscal discipline and financial risks. For instance, the 2018 World Bank report by Hassan Zaman, Manuela Francisco, and Nada Choueiri emphasized that economic threats and financial risks, such as high levels of ‘debt distress’ and deficits, are crucial challenges to economic development and growth (Zaman, Francisco, & Choueiri, 2018). The increasing concern over ‘debt distress’ has led to growing scrutiny and criticism of the effectiveness of Tuvalu’s fiscal policies.

In the case of Tuvalu, sovereign debt and PFM challenges are deeply embedded in structural economic vulnerabilities, limited institutional capacity of old institutional economics (i.e., churches, communities, kinships, etc.), dependence on external financing, and political pressures of copying globalisation. Addressing these issues will require not only strengthening PFM systems and institutional capabilities but also enhancing economic resilience through ‘diversification’ (Imbs & Wacziarg, 2003) and strategic thinking of how cognitive institutions and old institutional economics can interact with modern or outside institutions such as banks, investment firms, insurance companies including state-owned-enterprises (SOEs) in Tuvalu.

Debt distress and weak fiscal discipline has been a recurring theme for many Pacific Island Countries (PICs) including Tuvalu. Almost every global crisis, small economies like Tuvalu often experienced the worse financial impacts of any kind. For instance, the Asian Financial Crisis of the late 1990s triggered a notable rise in average debt levels across the Pacific, underscoring the region’s vulnerability to external shocks. Though, Tuvalu was very isolated to Asia’s markets and many developed countries such as the US, Australia and New Zealand, it has an impact on its sovereign fund, Tuvalu Trust Fund (TTF).

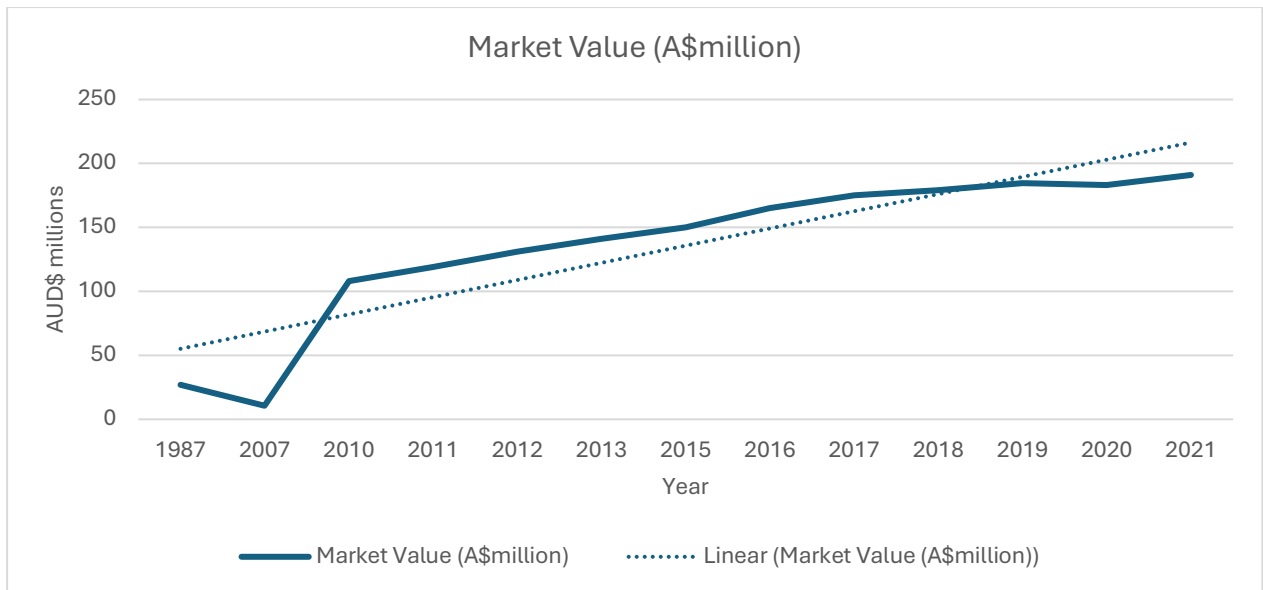


Figure 2.6 Tuvalu Trust Fund from 1987-2021. Source: Government of Tuvalu (2024).

From 1987 to 2000, the fund (i.e., TTF) was noticed that it's generated a marginal revenue at 2.9% with an average dollar value at A\$2.9 million per year. However, without a crisis the fund has better average return performances at 6.2%. The outperforming of revenue against government expenditures, which often lead to recurrent deficits is a major PFM challenge for Tuvalu.

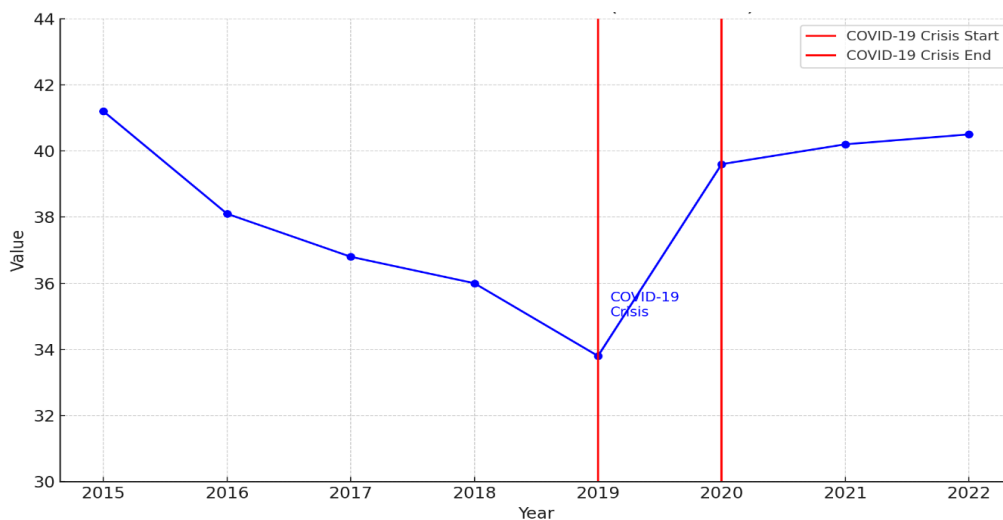


Figure 2.7 Aggregate Public Debts to Income (DTI) in Percentages for Pacific Island Countries. Source: Source: World Economic Outlook Database and IMF Staff estimates (2022).

According to the study carried out by Nada Choueiri, Manuela Francisco, and Hassan Zaman of the IMF and International Development Association (IDA) of the World Bank, Tuvalu has remained at risk of debt distress, with debt sustainability analysis projecting continued risks

over the next 10 years due to global shocks and climate change debt dynamics (Choueiri, Francisco, & Zaman, 2023).

According to this analysis, the researchers have used the Debt Sustainability Analysis (DSA) approach, which they used the present value (PV) of external debt measured against the threshold of 55% of gross domestic product (GDP) in developing countries. According to this approach, the PV of the debt-to-exports ratio should not exceed 240%. DSA also measured the ability of a developing states to sustainable level of borrowing at 21% of exports, with a debt-to-revenue ratio of 23%. These are the benchmarks.

At current PV, Tuvalu’s total debt-to-GDP was assessed to be at 35%, which led to an assessment that Tuvalu’s debt carrying capacity is extremely weak. International financial institutions, including the IMF, suggest that small island nations in the Pacific Region should maintain lower debt thresholds to account for their heightened risk exposure and weaker financial systems. Exceeding these levels increases the risk of ‘credit downgrades’ (Backer & Gosman, 1980) and higher interest rates, making future borrowing more expensive and less accessible (IMF, 2021) for Tuvalu.

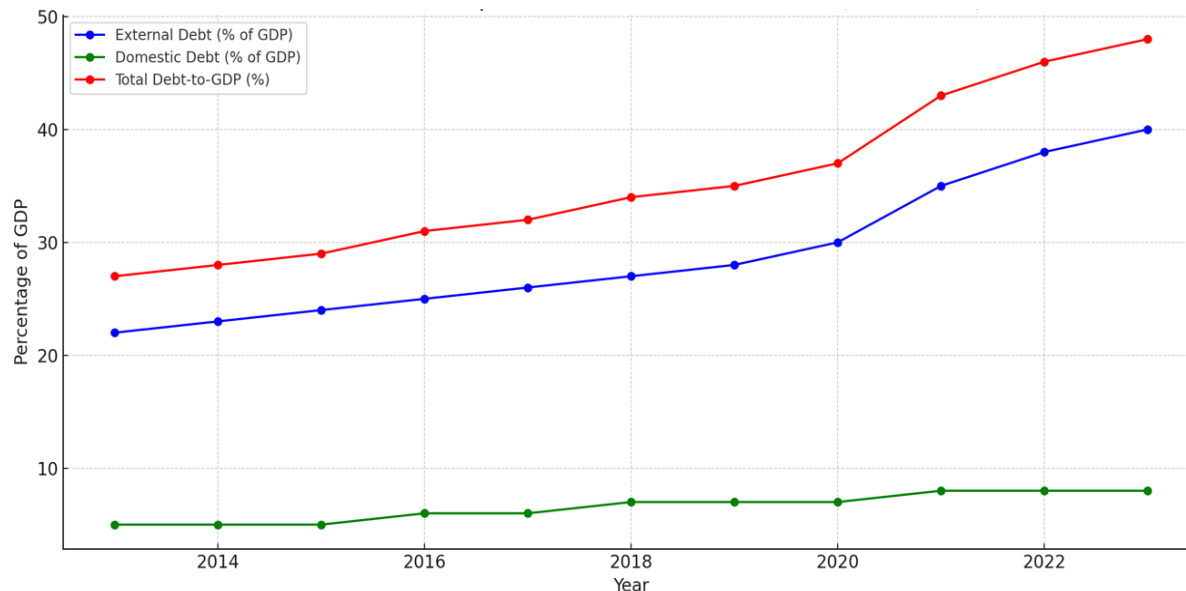


Figure 2.8 External versus Internal Debts in Tuvalu (AUD\$). Source: IMF and Government of Tuvalu (2023).

Though the Government of Tuvalu debt content is estimated below 50% of GDP, the rising debt levels of both domestic and external reduce the government’s ability to invest in long-term development and essential infrastructure. As more funds are diverted toward debt repayment, less is available for critical areas such as education, health, and climate resilience.

This ‘crowding out’ effect limits Tuvalu’s ability to build the capacity needed to respond to current and future challenges. In the long run, underinvestment in development will slow economic growth and reduce the government's ability to generate revenue, creating a negative cycle (Allen et al., 2013).

While public debt in absolute terms is small at USD\$4.26 million to USD\$5.66 million compared to developed countries, their impacts can be insurmountable in Tuvalu (see Figure 2.8).

Lender	Contract date	Loan Details	2016	2017	2018	2019
ADB	1990	Establishment of Falekaupule Trust Fund (FTF)	1.53m	1.39m	1.13m	0.90m
ADB	2003	Upgrade of Tuvalu Maritime Training Institute (TMTI)	1.27m	1.27m	1.17m	1.09m
ADB	2005	Upgrade TMTI	1.46m	1.47m	1.35m	1.27m
ICDF	2019	Tuvalu Convention Centre				2.4m
TOTAL			\$4.26m	\$4.13m	\$3.65m	\$5.66m

Figure 2.9 Gross Nominal Public Debt (2016-2019) (Outstanding Balance in US Dollars). Source: Government of Tuvalu (2020).

According to the Public Debt Bulletin reported by the Government of Tuvalu and the Ministry of Finance, external borrowings from multilateral institutions have been the primary source of public financing for several decades. However, the economic impact of COVID-19 has led to a decline in borrowing. Currently, Tuvalu’s main creditors are the Asian Development Bank (ADB) and the International Cooperation and Development Fund (ICDF) of Taiwan (Government of Tuvalu, 2021). Much of this debt is contracted at fixed interest rates and consists primarily of medium- and long-term obligations. Additionally, approximately 58% of Tuvalu’s debt has been acquired on ‘concessional terms’, providing more favourable borrowing conditions (Komai, 2024).

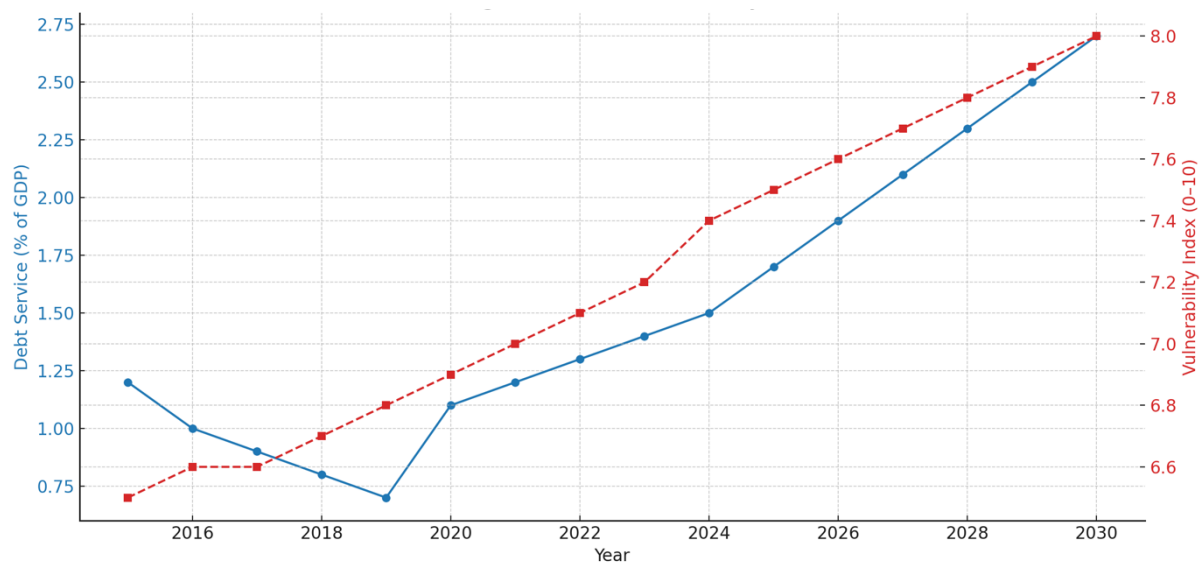


Figure 2.10 Tuvalu Debt Servicing Cost and World Bank’s Vulnerability Index Projections (2015-2030). Source: Government of Tuvalu & Ministry of Finance (2022), International Monetary Fund (IMF) (2023) and Asian Development Bank (2023).

World Bank’s vulnerability index further complicates its fiscal outlook (see Figure 2.10). As a Small Island Developing State (SIDS), Tuvalu remains highly susceptible to external shocks, including climate change impacts, global market fluctuations, and natural disasters. The IMF/World Bank Debt Sustainability Framework (DSF) vulnerability index reflects this persistent vulnerability, capturing dimensions such as environmental risk, economic openness, and institutional fragility (ADB, 2023).

If the index remains elevated or increases, it suggests that structural weaknesses remain unaddressed, limiting the country’s ability to absorb shocks and sustain long-term development. The interconnection between Tuvalu’s rising debt servicing costs and its vulnerability index reveals a feedback loop. Increased vulnerability often necessitates borrowing to manage emergencies or invest in resilience, while growing debt obligations constrain fiscal space for future adaptation measures (World Bank, 2018; World Bank, 2024). This cycle creates a compounding effect, where fiscal instability and external vulnerability reinforce each other.

From a policy perspective, these trends highlight the urgent need for a comprehensive debt management strategy that integrates fiscal prudence with climate adaptation priorities. International cooperation remains essential, especially in mobilizing climate finance tailored to the needs of vulnerable states. Strengthening domestic resource mobilization and institutional capacity can also mitigate future debt stress and enhance resilience (Palthe, 2014).

For a small island nation like Tuvalu, the presence of outstanding public debt presents a range of fiscal and economic vulnerabilities, despite the relatively modest amounts shown in the debt table for 2016 to 2019. The data reveals that Tuvalu's gross nominal public debt declined steadily from USD\$4.26 million in 2016 to USD\$3.65 million in 2018, largely due to consistent repayments on earlier loans contracted with the Asian Development Bank (ADB). These included a 1990 loan for the establishment of the 'Falekaupule Trust Fund' and two subsequent loans in 2003 and 2005 for upgrading the Tuvalu Maritime Training Institute (TMTI). The reduction in outstanding balances for these loans indicates disciplined fiscal management.

Regulative Institutions

As rising costs and recurring deficits continue to trouble small economies like Tuvalu, regulative institutions play a soothing role in managing public finances by establishing legal frameworks, legal processes, and financial systems that govern the national budgeting, taxation, public expenditures, and debt management. According to Hallet and Ventresca (2006), rules, norms, and values emerge through social, political and economic interactions and the modification of human behaviour in the management of public finance.

The first significant role of regulative institutions in the economy is to promote and design a legal framework that can lead to 'good governance' (Kaufmann, Kraay, & Zoido-Lobaton, 2000). A regulative institution refers to the 'formal structures', rules, and mechanisms that guide and control behaviour within a society or organization to promote the effective allocation of public money through collective choice (Schick, 2013). Regulative institutions have two key features: 'enforcement and punishment' that can improve the lack of fiscal discipline. They are designed to ensure that citizens adhere to established laws, regulations, and standards, thereby maintaining order and economic stability (Palthe, 2014). Barnett and Carroll (1993) argue that regulative institutions are fundamentally a product of market forces and regulative elements such as policies driven through coercive means (Palthe, 2014). Without enforcement and punishment, regulative institutions cannot establish public confidence and economic sustainability.

Regulative institutions can be structured as legal processes that guide and control behaviour within the public and private sector that promotes transparency, responsibility, accountability, participation and responsiveness (UN, 2023). By promoting public transparency, accountable,

participatory and responsive government, it can establish higher standards that can lead to effective public financial management. Furthermore, it also promotes integrity and ensures effective government spending and revenue collection that are aligned with societal behavioural reasoning from ‘want to’ to ‘have to’ (Palthe, 2014).

Another role of regulative institutions is the establishment of an effective financial system that can fundamentally improve public finances. The IMF defines a financial system as a ‘system that consists of institutional units and markets that are interacted in a complex manner for the purpose of mobilizing funds for investment and providing facilities for payment systems in financing commercial activities’ (IMF, 2006, p. 1).

Regulative institutions play a vital role in public financial management by establishing legal frameworks, enforcing fiscal discipline and promoting transparency, accountability, and economic stability. Scholars emphasize that these institutions require continuous human interaction to function effectively, ensuring compliance through enforcement and penalties (Hallet & Ventresca, 2006; Palthe, 2014).

They support good governance by structuring financial processes that enhance responsible government spending and revenue collection while shifting societal behaviour from voluntary to mandatory compliance. In addition, they also facilitate efficient financial systems that mobilize funds, investments, and credit, contributing to economic growth and stability (IMF, 2006). Ultimately, regulative institutions are essential for sustaining economic governance, maintaining public confidence, and ensuring effective PFM.

In the context of Tuvalu, regulative institutions are crucial for maintaining effective public financial management, especially amid rising costs and fiscal deficits. These institutions establish legal frameworks and formal processes that govern budgeting, taxation, expenditure, and debt, promoting transparency, accountability, and fiscal discipline. By enforcing rules and applying sanctions, they shift public behaviour from voluntary compliance to mandated responsibility, supporting good governance and economic stability (Palthe, 2014; Hallet & Ventresca, 2006).

Additionally, regulative institutions facilitate efficient financial systems that mobilize funds and credit, enabling sustainable economic management (IMF, 2006). Their effectiveness

depends on continuous human interaction and the incorporation of social norms and agency, reinforcing their role in shaping fiscal outcomes in small economies like Tuvalu.

Normative Institutions

Normative institutions (NI) are essential for public financial management because they establish social norms, code of conduct, and professionalism that shape how financial resources are managed within a society. Normative institutions are institutions that are influenced by written and unwritten rules, and they determine the patterns of appropriate behaviour (Gartland, 2009). This normative aspect refers to the formal and informal rules, laws, regulations, customs and traditions that guide and constrain behaviour within institutions. Normative can be explained by the following different forms: social norms, ethics, and traditions.

Social norms are often underestimated in their influences on institutions; however, they can also affect consumer habits, labour market participation, and market efficiency as demonstrated by normative institutions. Douglas North (1990) argues that social norms such as *everyday customs, taboos, common daily dos* affect labour market participation, particularly regarding gender roles. Elinor Ostrom also adds that social norms especially in developing institutions can be positively influence the management of shared resources effectively in small communities. Ostrom found that informal norms can build strong relationships of trust that enhance sustainable economic growth in resource-dependent communities (Ostrom, *Collective Action and the Evolution of Social Norms*, 2000). Social norms can be classified as financial regulations that regulate taxation, labour and business practices on daily basis.

Scholars have argued that ethics or codes of conducts are the foundation of the ‘moral economy’. This argument goes back to Aristotle’s era. Ethics examine the basic obligation for people in society. For example, the ‘Pacific Way’ in the Pacific Region often spelled out the code of conducts of its people and leaders. *Consensus-based decision making, respect for the elders and tradition, communalism over individualism, peaceful conflict resolution* are some key examples of how island managers conduct themselves in financial management (Besnier, 2009; Goldsmith, 2005; Chambers & Munro, 1980).

Andrew Sayer expands on this by emphasizing that a ‘moral economy’ is not just about abstract principles but is deeply embedded in social relationships and cultural contexts that shape economic behaviour (Sayer, 2000). Sayer argues that economic actions cannot be fully

understood without considering the moral values and social norms that govern them, as these influence what is seen as just or unjust in economic exchanges. In the Pacific Region, the 'Pacific Way' exemplifies this integration of ethics and economy, guiding leaders and communities alike. These practices demonstrate how financial management is conducted not merely by technical rules but through moral commitments that reinforce social cohesion and accountability (Besnier, 2009; Goldsmith, 2005; Chambers & Munro, 1980; Sayer, 2000). This highlights the importance of understanding local ethical frameworks to appreciate how public resources are managed in Pacific Island societies.

With modern insertion of modern financial practices, competing norms codes may be at play. This can lead to different answers to fundamental questions such as: how can people lead a good life? What gives true meaning to a good life? What is right and wrong? These questions are fundamental to what are the right or proper financial management practices that are ethical in the management of public finances. What are the current norms for ethical standards, compliance and accountability that encouraging professionalism, and strengthening public trust in public institutions of Tuvalu?

Furthermore, formal institutions such as the Ministry of Finance, Education, Attorney General, Churches, etc. are also normative because they promote ethical standards as a mechanism for effective financial management. Ethics in financial management is often referred to the 'moral code of conduct' that guides and governs the behaviour of professionals or managers. It promotes integrity, credibility and fairness among public stakeholders (LPC, 2023). Ethics in financial management prevents unethical practices such as financial fraud and corruption, theft or embezzlement, insider trading, conflicts of interests, wealth manipulation, accounting frauds, or stealing funds (Larmour, 2012).

Besides the moral code of conduct, the idea of 'professionalism' is often central to public reform agendas (Hassall, 2017). Professionalism guides the overall standards within economic institutions and shapes how clients, government, and stakeholders interact. According to Penfold (2013), professionalism is key to improving the 'rule of law' in many Pacific Island Countries, including Tuvalu. It upholds the values, ethics, and codes of conduct for public leaders and managers, ensuring adherence to shared beliefs, traditions, and cultural expectations that influence the management of public finances. Encouraging professionalism can improve public financial management at both central and local government levels.

Normative institutions play a vital role in PFM by shaping social norms, ‘ethics and professionalism’ which influence financial decision-making and governance. According to Gartland (2009), these institutions are guided by formal and informal rules that dictate appropriate behaviour. Social norms, as argued by North (1990), impact labour market participation, consumer habits, and economic stability, while ethics provide moral foundation for financial management, ensuring integrity and preventing corruption (Lamour, 2012). Furthermore, professionalism upholds ethical standards and strengthens public trust in financial institutions, fostering accountability and efficient resource management (Penfold, 2013). Therefore, enforcing the rule of law and professional conduct are vital in Tuvalu and other PICs to enhance fiscal disciplines.

In Tuvalu, normative institutions are fundamental to effective public financial management as they shape behaviour through shared social norms, ethics, and professionalism. Guided by both formal and informal rules, these institutions influence financial practices by promoting ethical conduct, trust, and accountability in both central and local governments (Gartland, 2009). Social norms, as emphasized by North (1990) and Ostrom (2000), affect labour participation, market efficiency, and resource management, particularly in close-knit island communities. Additionally, traditional values such as consensus decision-making and communal responsibility commonly seen in the ‘Pacific Way’ enhance ethical governance (Besnier, 2009; Goldsmith, 2005). Institutions like the Ministry of Finance and the Church instil moral and professional standards that deter corruption and reinforce public confidence (Lamour, 2012; Penfold, 2013). Upholding professionalism and ethical codes within Tuvalu's public sector are therefore essential for fostering fiscal discipline and sustainable governance.

Cognitive Institutions

Cognitive institutions (CI) can be seen as the most influential institutions in the Pacific Region and in Tuvalu. As public leaders in Tuvalu are conscious about the vitality of their beliefs, values, and social systems (known as chiefly systems), cognitive institutions are influential institutions not only in Tuvalu but also in the Region. Peter Larmour (2005) pointed out that the role of cognitive institutions can be seen in governance and leadership, social organization and identity, and through land and resource management.

According to Richard Scott, a cognitive institution is an institution that deeply engrained mental frameworks, shared understandings, and belief systems that shape how individuals and

society perceive, interpret, and respond to their environment. Scott (2008) emphasizes that cognitive institutions operate at an ‘involuntary level’, where it influences human behaviour by providing taken-for-granted economic assumptions that guide actions. Daniil Frolov states that economic theory is enhanced when it considers the role of cognitive institutions (Frolov, 2024).

In the studies of international business (IB), cognitive institutions have been characterized by how managers use mental frameworks to perceive economic opportunities, assess risks and navigate unfamiliar environments. According to Buckley, Devinney and Louviere (2007), public managers often use mental frameworks that have been heavily drawn from disciplines such as economics, sociology, and psychology from a modern perspective, yet they have not recognized the traditional views of the islanders or the Tuvaluans.

The role of cognitive institution influences how ‘big-man leadership style’ (Feinberg & Watson-Gegeo, 2021) and customer leadership influences the budgeting planning, processes and financial decisions, which could lead to economic growth and sustainability. For example, the ongoing interactions and feedback loop between kinship, island community, and churches have a significant influence on thinking patterns. These thinking patterns consist of the so called ‘extended mind thesis’ (Clark & Chalmers, 1998), the practical integrated systems (the abilities of individuals in the institution to control and coordinate) (Dengso & Kirchhoff, 2003), and external environment that influences ‘outsiders’ or ‘foreigners.’

According to Goldsmith (2005) and Chambers & Munro (1980), institutions such as kinship, churches, and island communities are considered as cognitive institutions that influence policy and law (e.g., regulative institutions). In Tuvalu, these institutions are the agents that create a ‘shared understanding’ of how the world works, influencing how individuals and organizations make decisions. Institutions such as these, ‘cognitive economic institutions’, are the agents that maximize functions of the principal (e.g., individuals and citizens in society) (Bourguine, 2004). Therefore, the shared understanding of institutions and individuals can be heavily influenced by kinship, churches and island communities’ practices.

By promoting shared values, beliefs, and norms, normative institutions help align societal goals with governance actions. In doing so, these agents are expected to operate in ways that maximize the welfare and interests of the people they represent, particularly in areas such as

public financial management. For Tuvalu, where communal life and traditional structures remain strong, these institutions help interpret complex financial matters and influence decision-making in ways that reflect the collective interest of society.

In the context of public financial management in Tuvalu, the influence of cognitive institutions through ingrained beliefs and thinking patterns can significantly shape financial decisions. These mental frameworks, rooted in cultural norms and traditional practices, often guide public leaders and institutions in budgeting and resource allocation. However, reliance on familiar ways of thinking can also lead to cognitive biases, resulting in conservative or irrational financial choices that may hinder innovation and economic progress. When decision-makers prioritize customary approaches over new or evidence-based methods, it can limit adaptability and prevent the exploration of more effective financial strategies. Therefore, while cognitive institutions provide valuable cultural context and stability, integrating critical reflection and openness to new ideas is essential for sound and forward-looking financial management in Tuvalu.

In Tuvalu, cognitive institutions play a profound role in shaping public financial management by embedding shared belief systems, values, and mental frameworks that influence decision-making across all levels of society, particularly ‘indigenous groups’ (Palthe, 2004). These institutions such as kinship networks, churches, and island communities guide how Tuvaluans perceive leadership, economic opportunity, and public accountability (Larmour, 2005; Goldsmith, 2005; Chambers & Munro, 1980). Palthe (2004) believes that shared beliefs are engrained from antecedents of adjustments to personality traits, pre-training, mentoring, host-country assistance, stress and delay adaptation, cultural differences, family policies and so forth.

As already mentioned, Richard Scott (2013) explains that cognitive institutions operate at an ‘involuntary level’ (Scott W. R., 2013), shaping behaviour through deeply held assumptions. In Tuvalu, these assumptions influence budget planning, governance structures, and financial behaviour, often reflecting traditional leadership styles and community norms. As Bourguine (2004) notes, these institutions act as cognitive agents that shape and maximize societal functions. However, relying too heavily on established thinking patterns may inhibit innovation and lead to cognitive biases in financial decision-making. Therefore, while cognitive institutions are essential for grounding Tuvalu’s financial practices in local culture and identity,

they must be integrated thoughtfully with modern economic frameworks to promote adaptability and sustainable development.

In summary, cognitive institutions are agents that promote the idea of ‘how the world is’ instead of ‘what it should be.’ Unlike normative and regulative, cognitive institutions operate at a deeper psychological level on how people perceive, interpret and make sense of reality. These consist of cultural beliefs, language, national identity, and fundamental economic principles.

Conclusion

The emergence of public financial management in Tuvalu and other Pacific Island Countries (PICs) is increasingly significant in public financing. PFM opportunities are increasing consistent with the rapid growth of globalization that ensure that public funding is properly allocated, distributed and managed for the benefits of all citizens. According to modern public financial management scholars such as Allen Schick (2013), Visser and Erasmus (2002), Brigham and Huston (2010) and Lawson (2015) have been proposed implementing strong budget frameworks such as PFM Cycles and characteristics to strengthening revenue collection, enhancing public expenditure management, strengthening transparency and accountability, and controlling public debt and deficit. These scholars above also emphasized that PFM is the tool for economic growth and stability for small economy like Tuvalu.

In Tuvalu, effective PFM is deeply reliant on the strength of regulative institutions, which provide the legal and procedural foundation for fiscal discipline, budgeting, taxation, and debt management. These institutions such as the Parliament, Ministry of Finance, Budget Committees, and others uphold formal rules, enforcement mechanisms, and financial systems necessary for transparency, accountability, and stability. As outlined by scholars such as Schick (2013) and Palthe (2014), these frameworks shape fiscal behaviour by shifting societal conduct from voluntary to obligatory compliance and good governance.

For small states like Tuvalu where rising costs, recurring deficits, and external shocks are persistent threats to regulative institutions as they strive to become critical in maintaining governance standards and ensuring public confidence in financial decision-making. The IMF highlights the importance of such institutions in creating a sustainable financial system that supports investment, development, and the mobilization of credit, even as Tuvalu faces weak debt-carrying capacity and growing vulnerability to climate and global economic shocks (UNESCAP, 2009).

Normative institutions in Tuvalu reinforce PFM through shared ethics, traditions, and professional standards that guide financial behaviour across government and civil society. Rooted in both formal frameworks and unwritten social rules, these institutions such as the Ministry of Finance, churches, and traditional governance bodies promote ethical conduct, moral responsibility, and professional integrity in resource allocation and budget execution.

The Pacific tradition of communalism, consensus-based leadership, and respect for elders often referred to as the “Pacific Way,” contributes to a moral economy where accountability and trust form the bedrock of financial governance (Besnier, 2009; Sayer, 2000). These institutions influence not just financial policies but also the behaviour of public officials and community leaders, reducing the risk of corruption and mismanagement. Emphasizing professionalism and adherence to ethical codes of conduct is essential for addressing the fiscal risks associated with debt distress, as normative institutions serve as cultural anchors for sound financial practice.

Cognitive institutions in Tuvalu represent the deeply embedded belief systems, mental models, and cultural logics that influence how public finance is understood and practiced. These include kinship networks, churches, and island communities that shape perceptions of leadership, financial responsibility, and national identity (Scott, 2008; Larmour, 2005). Unlike regulative institutions that enforce rules or normative institutions that set ethical expectations, cognitive institutions operate at an unconscious level, guiding economic reasoning and decision-making through cultural narratives and traditional knowledge systems.

In Tuvalu, this manifests in how budgeting, debt decisions, and investment strategies are interpreted through communal values and local leadership structures. While these institutions ensure financial policies resonate with social norms and foster legitimacy, over-reliance on traditional cognitive frameworks may hinder innovation and adaptability. Thus, integrating local cognitive institutions with modern economic approaches is essential to building financial resilience, reducing bias in fiscal decisions, and ensuring sustainability in the face of rising debt servicing and climate-induced vulnerabilities.

In summary, the interplay of regulative, normative, and cognitive institutions forms a comprehensive framework essential for mitigating financial risks in Tuvalu’s small economy. Regulative institutions ensure legal order and fiscal discipline; normative institutions embed ethics and social trust; and cognitive institutions provide cultural context and shared understanding. Together, they reinforce each other to promote good governance,

accountability, and resilience in public financial management. For Tuvalu to achieve sustainable economic stability, it is imperative to integrate these institutional dimensions thoughtfully, respecting cultural traditions while embracing innovative and evidence-based financial strategies.

The next three chapters explore the relationships and interactions between regulative, normative and cognitive institutions with public financial management cycles and characteristics. This holistic approach can strengthen the country's ability to manage financial challenges and support long-term development.

**PART II – INSTITUTIONAL THEORY: REGULATIVE, NORMATIVE
AND COGNITIVE**

CHAPTER 3. REGULATIVE INSTITUTIONS AND PUBLIC FINANCIAL MANAGEMENT

Individual behaviour conditioned by instinct, habit, belief as well as rationality
- Thorsten Veblen (1899)

Introduction

This chapter explores the relationships and interactions between regulative institutions and public financial management. This chapter puts forth key arguments that regulative legal structures such as the Westminster System, formal structures (i.e., good governance), and fiscal models (i.e., MIRAB) affect budget frameworks, revenue collection, public expenditure management, strengthening transparency and accountability, and control public debt and deficits.

The first section is focused on how the legal structures of Tuvalu can influence the outcome of PFM. It demonstrates key interactions between legal structures such as the Constitution, Parliament, the role of the Prime Minister (PM), and other formal structures such as state-owned-enterprises (SOEs) in management of public finance. It also argues how the functions and capacities of these structures can influence financial decision-making in many aspects – micro and macro levels in both local and central governments.

The second section explores the roles of regulative institutions and good governance frameworks – accountability, responsiveness, transparency, consensus, equity, rule of law, participation and effectiveness – in connection to PFM. The good governance agenda has been one of the most common legal frameworks that proposed by the World Bank and IMF to strengthen compliance, accountability and financial transparency in Tuvalu. Good governance has been an enforcement mechanism for institutional accountability systems that govern fiscal behaviour by international institutions such as the World Bank and IMF.

The last section of this chapter explores how regulative institutions established revenue collection through migration, remittances, aid, and bureaucracy (MIRAB) (Bertram G. , 2007; Bertram G. , 2006; Bertram & Watters, 1986). Series of study by Geoff Bertram and Ray Watters on income structures and my observation of small island states like Tuvalu highlighted the important role that MIRAB model plays in Tuvalu's economy.

Legitimacy and Formal Structures

According to Scott (1995), legitimacy arises when rules, laws, and norms are consistent with cultural values and receive broad normative support. In modern sovereign states, the primary role of regulative institutions is to create a legal framework that govern political and economic actors to follow established processes and procedures for the benefit of all citizens (Palthe, 2014). This legal framework can be established through various means. Within these various legal frameworks, Tuvalu has adopted the Westminster democratic structure as their formal structure.

Tuvalu's formal structure is the Westminster Parliamentary system. This structure came when Tuvalu established its parliamentary democracy on October 1st, 1978. By the virtue of the United Kingdom (UK), the Tuvalu Independence Order 1978 was issued as the legal order by Her Majesty Queen Elizabeth on 25th July 1978. Queen Elizabeth II approved the Tuvalu Constitution as the 'supreme law of Tuvalu' (Government of Tuvalu, 2023) that prescribed the power and duties of the executives. Prior to this declaration, Tuvalu had used a 'traditional system' (Taafaki & Oh, 1995), where the executive was constituted by chiefs (e.g., *ulu-aliki*) and elders (e.g., *toeaina*) (Goldsmith, 2012).

The Tuvalu Constitution of 1978 established Tuvalu's new rules, laws, norms as a sovereign state. The Constitution outlined the country's new legal framework, governance structures, and the functions of power from Britain to Tuvaluan authorities. It confirmed Tuvalu's status as a constitutional monarchy within the Commonwealth, with Queen Elizabeth II as the Head of State, represented by a Governor-General, and a Prime Minister (PM) elected as the Head of Government (Taafaki, 1996). Although this formal structure has been in place since the 1970s, opposition parties have, over the years, contested the idea, advocating for its replacement with a republic. The painful experience of colonialism has not been forgotten, as many current political leaders recall those times from their youth.

During data collection, one of the most meaningful conversations I had while collecting information on Tuvalu's path to independence was with Sir/Dr. Tomasi Puapua, former Prime Minister (PM), former Governor-General, and former Speaker of Parliament. Dr. Puapua was appointed a Knight Commander of the Order of the British Empire (KBE) in 1998 and later a Knight Grand Cross of the Order of St. Michael and St. George (GCMG) in 2002.

Born in 1938, prior to World War II, Dr. Puapua came from a humble background and lived through some of the most difficult events in Pacific history. He witnessed the conflict between Japanese and American forces during WWII and how these events had played an instrumental role in Tuvalu's journey to becoming a sovereign state. Moreover, these events created an opportunity for colonial masters such as the United Kingdom to share their public and financial management principles with Tuvalu. As a result, the 'mixed capitalist system' was adopted in 1978, where Tuvalu would agree to use Australian dollars as their pegged exchange currency at a 1:1 rate with Australian dollar (AUD).

During our conversation, Dr. Puapua shared that the formulation of Tuvalu's initial government and the process of separating from the British colony was one of the most difficult projects he had ever been involved in. He clearly recalled the days of February 13–17, 1978, when the delegation arrived at Buckingham Palace, the Queen's residence. They were nervous and scared. Dressed in *lavalava* without socks, and in freezing temperatures, all they could think about was the pain felt by many Tuvaluans working under the colonial administration and their collective desire to return home (Puapua, 2018).

When the Queen asked how they would manage their affairs if they left the colony, they answered 'yes' to everything. Their determination to achieve independence meant they received no financial assistance to begin their government. During the separation and even after independence in 1978, they discovered that fisheries and copra were Tuvalu's most significant economic resources. However, these two sources of revenues did not purge the initial costs of starting the country. There were a lot of tears and hardship as Dr. Puapua reflected on it.

He also noted that the first official Constitution was simply a piece of paper, a proposal drafted by the original eight members elected to represent Tuvalu in 1975. Although the proposal contained only a few ideas, the key objective was clear: to ensure that Tuvalu could independently make sovereign decisions. The draft included provisions for the prohibition of slavery, the right to life, and the dignity of the human person. This Constitution was later ratified by both the British Parliament and the Tuvalu House of Assembly in June 1978, and formally approved by Queen Elizabeth II (Puapua, 2018).

Reflecting on the brief history of Tuvalu and in light of current efforts to promote public financial management, the key question I must ask is: Does PFM uphold the same values that Dr. Puapua and his colleagues fought for democratic values and beliefs such as equal rights,

the right to life, and human dignity? Do we seek these fundamental values/beliefs as we pursue economic growth, reducing financial risks and not forsaking our democratic values and principles?

According to North (1990), institutions reduce uncertainty by structuring human interaction, and in Tuvalu, this structuring must occur in tandem with indigenous norms and practices. Perhaps, North (1990) may have used this argument in a well-established institution, however, in the case of Tuvalu, regulative institutions such as the Westminster model have not yet provided that stability and certainty thus far (see Figure 3.2: List of Prime Minister, 1978-present). Did the Westminster model structure provides the individuals ownership and promote equal opportunities, utility, fair shares for Tuvaluans? According to Dr. Puapua, the stability of the Government and society is rooted in Tuvalu's governance system that operate informally and, in the community-based level.

Scott (1995) contends that legitimacy stems from three institutional pillars: regulative, normative, and cognitive, and Tuvalu's institutions must reflect all three to maintain trust and effectiveness (Scott, 1995). For instance, while the Governor General serves a ceremonial function rooted in constitutional functions, the role continues to hold legitimacy due to its alignment with traditional expectations and symbolic neutrality – respect, fairness, and love for others (Baba, 1985; Besnier, 2009; Chambers & Chambers, 2008). Likewise, the PM and Cabinet Ministers derive their authority not only from parliamentary procedure but also from their perceived adherence to communal values and their accessibility to constituents. This has been the missing gaps in modern structures.

The current formal structure of Tuvalu (see Figure 3.1) reflects a minimalist adaptation of the Westminster parliamentary system and how the Executive Branch is structured. Formal institutions are operated under a codified constitutional framework, providing legal legitimacy, executive authority, and mechanisms intertwined with interior and external regulative institutions for accountability. It is complex and not as simple as the *Aliki* or Chiefly system that many Tuvalu used to it. However, the effectiveness and legitimacy of these institutions in Tuvalu cannot be fully understood without considering their alignment with local cultural and social contexts.

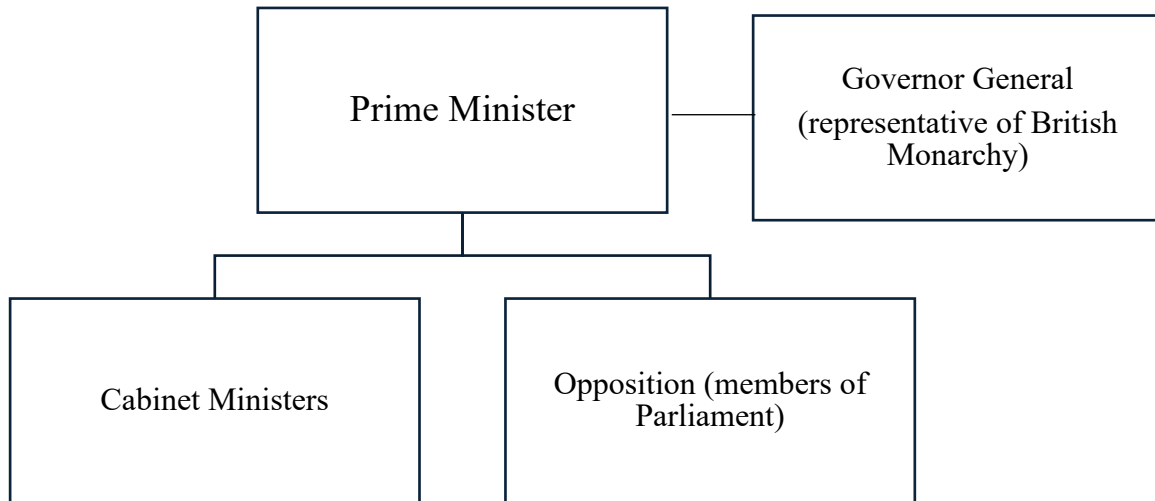


Figure 3.1 Post-Colonial Structure (1978-present). Source: Government of Tuvalu & Tauaasa Tafaaki (2007).

In such close-knit communities, ‘institutional trust’ often depends on social proximity and the ability of leaders to engage directly with citizens in Tuvalu is paramount. This localized form of legitimacy is where public figures are held accountable through both formal procedures and communal feedback (i.e., *Maneapa* System) that may underscore the unique political environment in which Tuvalu operates. Hodgson (2006) reinforces this by asserting that institutions are socially embedded and evolve in response to their environments. Thus, Tuvalu’s formal structures must remain flexible and adaptive to local traditions, ensuring that their authority is not only legally grounded but socially accepted.

In sum, while Tuvalu’s political system is formally structured along Western parliamentary lines, its legitimacy is largely sustained through culturally embedded practices and communal expectations (i.e., *Kaitasi*). The interplay between formal institutions and indigenous governance models (i.e., Chiefly System or *Aliki*) creates a distinctive political landscape one that requires constant negotiation between legal frameworks and traditional norms to achieve institutional stability and societal trust. Figure 3.1 above shows the current formal institutions and elected members of Parliament (MPs) in Tuvalu and how ‘vote of confidence’ short-lived many Government’s ambitions and long-term goals (Taafaki, 1996; Tafaaki, 2016).

Took Office	Left Office	Name
1 st Oct. 1978	8 Sept. 1981	Sir Toaripi Lauti
8 Sept. 1981	16 Oct. 1989	Dr. Tomasi Puapua
16 Oct. 1989	10 Dec. 1993	Bikenibeu Paeniu

10 Dec. 1993	24 Dec. 1996	Sir Kamuta Latasi
24 Dec. 1996	27 Apr. 1999	Bikenibeu Paeniu
27 Apr. 1999	8 Dec. 2000	Ionatana Ionatana
8 Dec. 2000	24 Feb. 2001	Acting, Lagitupu Tuilimu
24 Feb. 2001	14 Dec. 2001	Faimalaga Luka
14 Dec. 2001	2 Aug. 2002	Koloa Talake
2 Aug. 2002	27 Aug. 2004	Saufatu Sopoaga
27 Aug. 2004	14 Aug. 2006	Maatia Toafa
14 Aug. 2006	29 Sept. 2010	Apisai Ielemia
29 Sept. 2010	24 Dec. 2010	Maatia Toafa
24 Dec. 2010	1 Aug. 2013	Willy Telavi
1 Aug. 2013	19 Sept. 2019	Enele Sopoaga
19 Sept. 2019	26 Feb. 2024	Kausea Natano
26 Feb. 2024	Present	Feleti Teo

Figure 3.2 List of Tuvalu Prime Minister (1978-present). Source: Government of Tuvalu (2024).

The frequently changing nature of government in Tuvalu has cast doubt on the ability of regulatory institutions to maintain lasting reforms. Tauaasa Tafaaki (2016) reports that between 2000 and 2016, the country's economy and fiscal management were poorly handled. Consequently, formal institutional frameworks often clash with the cultural values and norms of the Tuvaluan people, undermining their effectiveness. Moreover, this misalignment extends into financial practices persistent budget deficits and rising public expenditure have gone unchecked despite increases in using modern key performance indicators like Gross National Income (GNI).

Monetary policy and fiscal discipline were bewildering and unfamiliar to many public managers. With the introduction of monetary instruments such as interest-rate decisions by the Australian Reserve Bank and macroeconomic tools - including taxation, inflation control, deregulation, and market privatization local financial officials often lacked the fiscal capacity to fully understand how these modern mechanisms could influence Tuvalu's fiscal and macroeconomic policies. Consequently, this deficiency in fiscal capacity is consistently reflected in development outcomes, economic growth trends, and numerous public financial management debates (see Figure 2.3 below). As highlighted in the ADB's 2012 report, these systemic weaknesses continue to undermine effective policy implementation.

The concept of worldview functions as a vital dimension of legitimacy that is too often overlooked in scholarly discourse. A worldview - a coherent set of beliefs, values, and assumptions profoundly shapes our perceptions of reality, institutional significance, and contextual awareness. In Tuvalu, it is especially striking that numerous political figures have fallen victim to fraudsters, an occurrence that signals a critical gap in both global and local system comprehension. Several public managers, wishing to remain anonymous, have expressed concern that this lack of foundational insight compromises the resilience and integrity of institutional structures.

For instance, they shared that many high-ranking government officials and managers have lost significant amounts to financial fraud due to a limited understanding of global monetary and financial systems. Like outsiders, they often lack insight into local structures and processes that are essential for adapting modern investment models to new conditions (Public Manager1, 2023). Without this foundational knowledge, proposed systems and formal procedures risk undermining key investments. As a result, fears of incurring further losses have made Tuvalu increasingly cautious about making swift financial decisions.

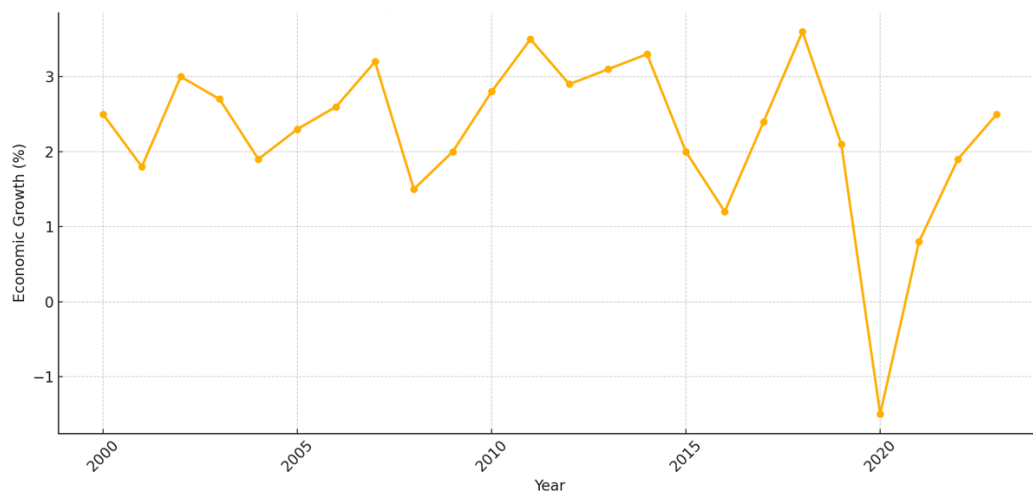


Figure 3.3 Economic Growth (2000-2023). Source: World Bank data and Government of Tuvalu (2023).

In order for PFM to be effective in Tuvalu, new formal rules, regulations and processes should be effectively and reduces any resistance from local public managers, they must build on common grounds. Digging deeper into traditional ways such as the *Aliki*, *Maneapa* or *Kaitasi* systems for legitimacy and improving aspects of formal processes in accountability, transparency, and management that strike equal voices and structures cohesion between regulative and cognitive institutions need to encourage.

Good Governance Framework

According to Barrie Macdonald (1998), the World Bank developed a concept from their assessment of the Sub-Saharan Africa on governance issues as known as the ‘good governance.’ The focused on good governance is to ‘formulate and implement sound economic policies and to manage both the country’s resources and any fund provided by the donors’ (Macdonald, 1998, p. 22). In more specific areas, the Bank focused on formal structures and the process in which country’s economic and social resources were managed, and how policies were formulated and designed is much similar to PFM. Both good governance PFM focused on improving government systems, structures and processes in managing public resources.

Since the early 1990s, the ‘good governance agenda,’ led by institutions such as the World Bank and the Organization for Economic Co-operation and Development (OECD), has become a central global initiative aimed at advancing development in regions like the Pacific. This agenda emphasizes transparency, accountability, the reduction of corruption and inefficiencies, and the promotion of effective public spending and budgeting (Macdonald, 1998). It also reinforces the importance of legal enforcement and the capacity of regulatory institutions to function effectively. In Tuvalu, good governance policies have played a crucial role in strengthening the legitimacy of the parliamentary system, positioning it as a central framework for national development and institutional modernization.

The World Bank (1992) defines ‘good governance’ as the way power is exercised in managing a country’s money (or finances) and social resources toward accomplishing positive financial growth. Good governance is a framework for exercising authority over economic resources, and the ability to design, implement, and execute policies and government functions (Macdonald, 1998, p. 23). The framework (see Figure 3.4) is characterized by eight main principles: accountable, transparent, responsive, equitable and inclusive, effective and efficient, rule of law, participatory and consensus oriented (UNESCAP, 2009). The promotion of good governance can strengthen the rule of law and strengthen the institutional drivers that improve stability, predictability and continuity.

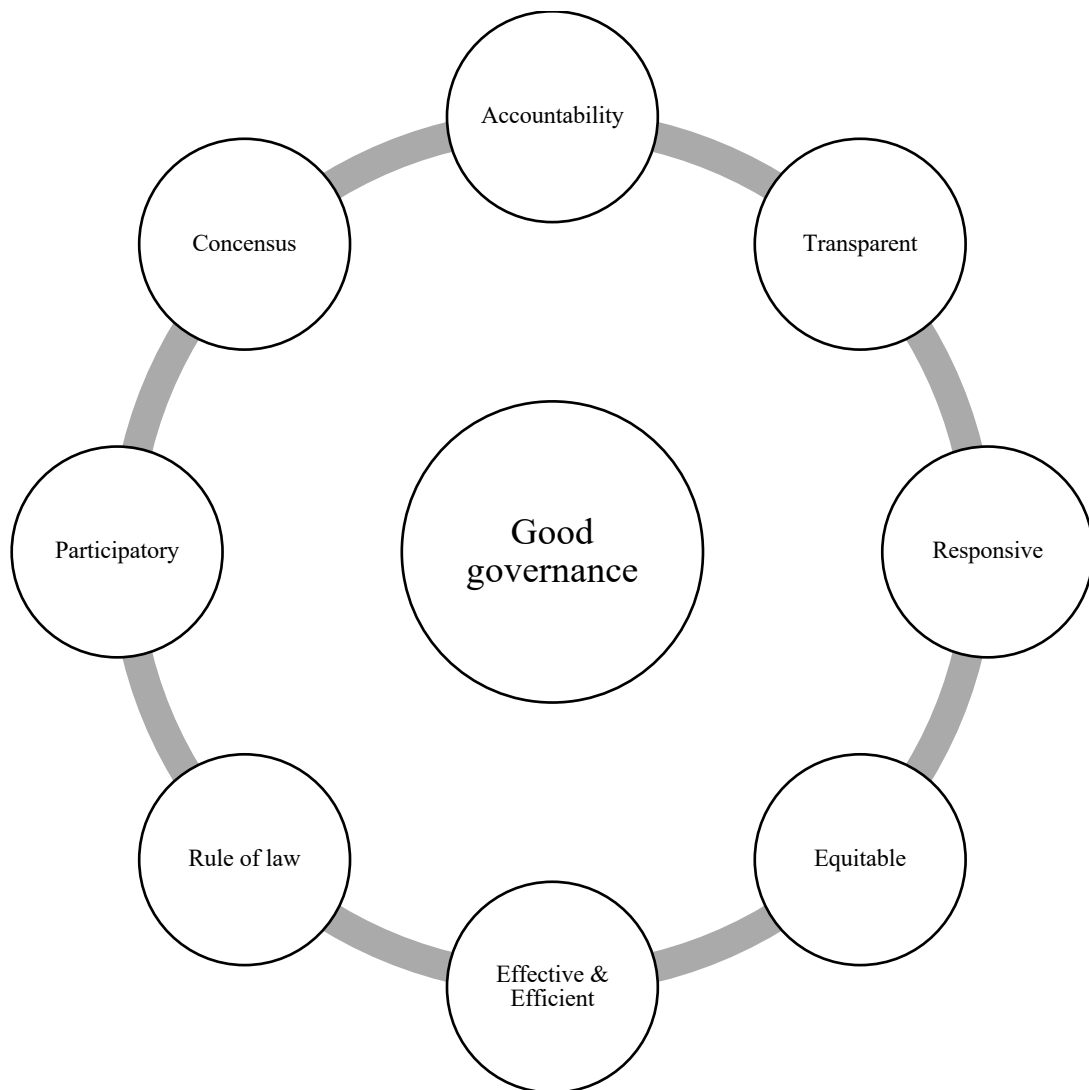


Figure 3.4 Characteristics of Good Governance. Source: ESCAP (2009) based on Collier (2007).

The National Strategy for Tuvalu 2016-2020 reported that improving governance and PFM should concentrated on accountability and transparency, equity, and participation in order to improve social well-being of all Tuvaluans (Tafaaki, 2016). In Tuvalu, this theoretical framework began to take practical shape in 2005, when the government launched *Te Kakeega II*, its second national development strategy, which prioritized building institutional capacity and what can be understood as ‘neoliberal policies’ to serve the public interest with competence, integrity, and fairness, yet without surveying the local context. A key pillar of this strategy was fostering collaboration, deregulation, and privatisation between Federal Government ministries and state-owned enterprises (SOEs), but it has ignored the effectiveness of accountability and transparency in the *Maneapa* system that have been practiced for centuries.

A useful way to identify weaknesses in regulatory and formal structures and PFM is by examining Tuvalu’s state-owned enterprises (SOEs). Key SOEs in this initiative include the National Fishing Corporation of Tuvalu (NAFICOT), National Bank of Tuvalu (NBT), Tuvalu Post Limited (TPL), Tuvalu Electricity Corporation (TEC), Tuvalu Telecommunications Corporation (TTC), and Vaiaku Lagi Hotel (VLH). These partnerships reflect the government’s efforts to apply good governance principles such as institutional accountability, strategic coordination, and public sector efficiency though their outcomes have been mixed due to persistent capacity constraints and structural problems. Since 2000, many of these SOEs have struggled to grow though ‘neoliberalism policies’, as shown in the snapshots below. This suggests the good governance agenda is more of checklist over real change.

Tuvalu Post Limited’s Consolidated Profit & Loss Account for First Quarter Ending 31 March 2017

Sales	\$24, 303. 64
Less Cost of Sales	\$26, 198. 43
Gross Profit/Loss	(\$1,894.79)

Figure 3. 5 Tuvalu Post Limited Financial Position in 2017. Source: Government of Tuvalu (2023).

In the Tuvalu Auditor General’s reports from 2016 to 2021 and other public reviews, they have highlighted that weak corporate governance, the lack of financial discipline and poor internal controls have made it difficult for both the Tuvalu Post Limited (TPL), and the Development Bank of Tuvalu (DBT) improve their financial positioning (Government of Tuvalu, 2017; PFTAC, 2024; Government of Tuvalu, 2023). In 2016, the Government reported that internal control issues were rooted in poor record keeping, unplanned expenditures due to climate change, and inefficiency (Government of Tuvalu, 2016). Thus, this formal structure has failed at core because it is superficial compliance, yet without recognizing local realities.

The snapshot below demonstrates continuation negative retained earnings of TEC or accumulated deficit, where the company has lost more over time than it has earned. TEC consistently relied on Government’s annual subsidies to reinvest in daily operations.

Share Capital 1 Jan.	AUD \$2,335,016 (Actual)
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Plus Additional Capital	(\$0)
Total Share Capital	\$2,335,016
Other Contributed Equity 1 Jan.	\$22,602,302
Plus Additional Other Contributed Equity	\$328,345
Other Contributed Equity 30 Sep.	\$22,930,647
Retained Earnings 1 Jan.	(\$23,948,750)
Plus Net Profit (Total Income) after tax	(\$353,876)
Less Dividends Paid	(\$0)
Retained Earnings/Deficit) 30 Sep.	(\$24,302,626)

Figure 3.6 Tuvalu Electricity Corporation (TEC) Statements of Changes in Equity in 2017. Source: Government of Tuvalu (2023).

For the DBT, the lack of commercial incentives to improve performance or innovative financial solutions is a major problem for the Bank. With small population and the intense competition between other financial institutions such as the National Bank of Tuvalu (NBT) and the Tuvalu National Provident Fund (TNPf), personnel incentives are more appealing. As a result, it is difficult to retain qualified personnel at DBT compared to NBT and TNPf (Government of Tuvalu, 2023; Government of Tuvalu, 2016).

Many SOEs in Tuvalu, such as DBT, PTL, NAFICOT and TEC, have weak accountability frameworks even though modern regulative structures of proposed strategic oversight, fiduciary duty and a balance of power by employing board of directors and C-suite roles, SOEs have not live up to their potential. Continuation of insufficient performance audits, and blurred reporting structures between boards, management, and government ministries continue. When SOEs lack proper reporting and are not held accountable for financial or service outcomes, inefficiencies persist without corrective action. However, the challenge of weak performance lies in the promotion of cultural bias (i.e., Western economic models and practices) as pointed out by Barrie Macdonald (Macdonald, 1998).

Good governance relies on a regulatory framework that is applied fairly and consistently with Western economic models that are unfamiliar with local executives of DBT, PTL, NAFICOT and TEC. Under such legal and formal structure, public managers are operating under

conditions that new economic models don't fit as SOEs in Tuvalu have different social, political and economic conditions. Therefore, establishing clear legal mandates and enforcing them uniformly across all public enterprises is different for improving institutional discipline and sustainability in Tuvalu due to local SOE practices of close-knit and communities' relationships. PFM practices are much different when operated on close-knit and communities' conditions.

Because of the different conditions and environment that are required for Western models to thrive, many of the formal rules have not effectively worked in translating economic performance (i.e., KPIs) of many SOEs into profit maximisation. Government raw data provided a few snapshots above (in Figure 3.5 and Figure 3.6) of the failures of SOEs in achieving their financial goals that could contributed to the overall economic performance of the country.

In 2016 the Government engaged in Technical Assistance (TA) which reviewed the effectiveness and efficiency of the Government's legal processes. The TA has found the need to improve personnel and the establishment functions of government posts, organizational structures within ministries, agencies and organizations (Tafaaki, 2016). The TA also proposed the need to establish the General Administrative Orders, policy for recruitment, and other personnel management responsibilities. Conversely, the lack of a work measurement system that assigns specific job descriptions and holds public servants accountable for completion of their tasks according to administrative functions and policies was identified as needing strengthening (Tafaaki, 2016, p. 9).

In contrast to General Administrative Orders, in traditional management and practices, the division of labour specialities or specialisation were given to kinships (i.e., *puikaiga*) or tribes. Each kin have their own specialty (Nia, 2021; Sogivalu, 1992). There are kins who specialized in fishing, nurturing plants/agriculture, combats, mortuary, physical and spiritual healers, orators, and many others. All these administrative responsibilities have been practiced in each Tuvalu's island communities for centuries. With the promotion of formal structures, however, it is required a curricular learning or western ways of executing such functions. And for such implementing new functions and structures, it is increased labour costs and education. Thus, we see adding new formal structures and functions can be costly and also increase Government expenditures in regulative institutions.

Furthermore, other regulative institutions such as the Ministry of Finance, Auditor-General, Attorney-General, Ombudsman, Public Accounts Committee (PAC), anti-corruption agencies or units (see Figure 3.7) also carried out the same mantra – to improve financial accountability and transparency in managing public resources. They worked together in formulation of new systems, structures and processes that ensure proper financial auditing and reporting on public financial matters that could reduce financial risks. In addition, they supported the mission and legal guidelines established under the revised Tuvalu Constitution 2023 (UN, 2023). Nevertheless, these established rules and regulations sound great, yet they never reach their potential.

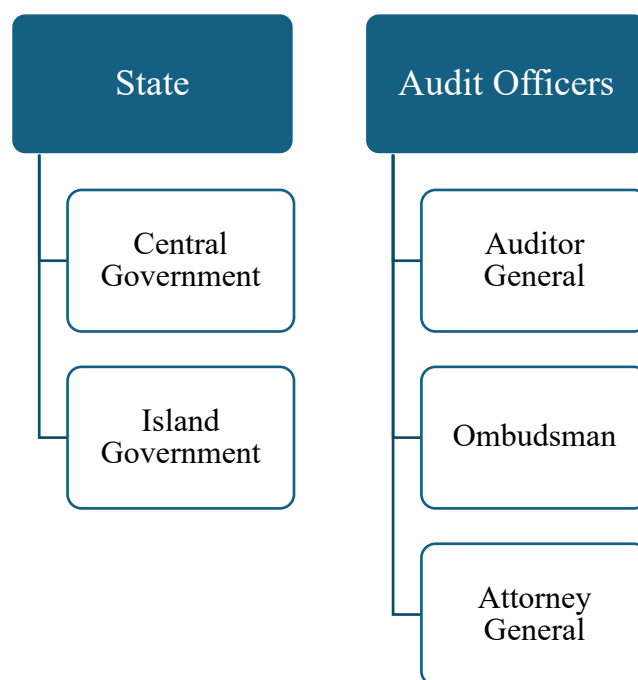


Figure 3.7 Separation of Power in Tuvalu. Source: Macdonald (1998) and Government of Tuvalu (2023).

In the push for increasing financial accountability and transparency under the good governance agenda, Tuvalu also established its Office of the Chief Ombudsmen in 2014 under the Leadership Code Act. The first Chief Ombudsman was Saaga Talu Teafa, appointed in October 2014. When Chief Teafa decided to run for Members of Parliament (MP) in Niutao Island on June 6th, 2022, his post as an Ombudsman officer was closed. According to one of the public managers in Tuvalu, there was not enough funds and budget to fill the Chief Ombudsman Office at this time (Public Manager2, 2023). Perhaps, the idea of PFM reforms can improve financial accountability and transparency, however, it is required money for functionality to work.

The Ombudsman Office, which was formally established in 2014 to act as an independent oversight body, has failed to deliver measurable improvements in public sector accountability or legal redress mechanisms (Tafaaki, 2016). Despite its potential role as a non-partisan auditor of executive behaviour and a defender of citizen rights, the Ombudsman Office in Tuvalu remains inactive, with no current representative appointed, largely due to budgetary shortfalls and internal accusations of favouritism and islandism the preferential treatment of certain island communities over others (Commonwealth Ombudsman, 2009). The absence of such a mechanism in Tuvalu weakens the oversight of executive actions and contributes to limited accountability in public service delivery.

With the missing of actions from the Attorney General Office and the Ombudsman, institutional cooperation between the executives of public corporations and ministries is ineffective. As a result, the informal institutions for empowering marginalized citizens (e.g., children's organizations, women organizations, non-profit organizations) have been ignored. This also led to a weak parliament system and other legal structures. The failure to achieve cooperation among government ministries and enforcement of financial accountability and transparency under this new formal structure, good governance, has not been the answer to the quest that PFM is searching (Estevao, Kanani, & Berger, 2021; ADB, 2005; ADB, 2015).

The MIRAB Model

Characterised with a unique formal systems, structures and processes, the MIRAB structure has found extremely significant for public financial management in Tuvalu. The MIRAB model is an economic framework first developed by Geoff Bertram and Ray Watters to explain the development dynamics of many small Pacific Island Countries (PICs) including Tuvalu in 1980s. It is an acronym representing four key sources of government revenues: migration (MI), remittances (R), aid (A), and bureaucracy (B). Migration (MI) and remittances (R) signifies the important relationships that creates a transnational link between Tuvalu communities and developed countries such as Australia, New Zealand or the United States (US) (Boland & Dollery, 2005; Tisdell C. A., 2014; Bertram & Watters, 1986).

The relationship between MIRAB and PFM creates many challenges and complexities. The relationship between the MIRAB and PFM can have multiple effects in the processing of foreign aid. According to Tisdell (2014), the interactions between MIRAB and PFM's

processes is vital to shape economic and fiscal decisions. Tisdell (2014) reveals that there are two distinct processes that are worth noting: Process I-the provision of foreign aid funding government spending, and Process II-the sending of remittances from Tuvaluans migrants from metropolitan cities to relationships at home (see Figure 3.8). These processes can have ‘multiple effects’ on macro and micro revenues in the country (Tisdell C. , 2014). They can improve national growth and household incomes, that could lift them out of poverty.

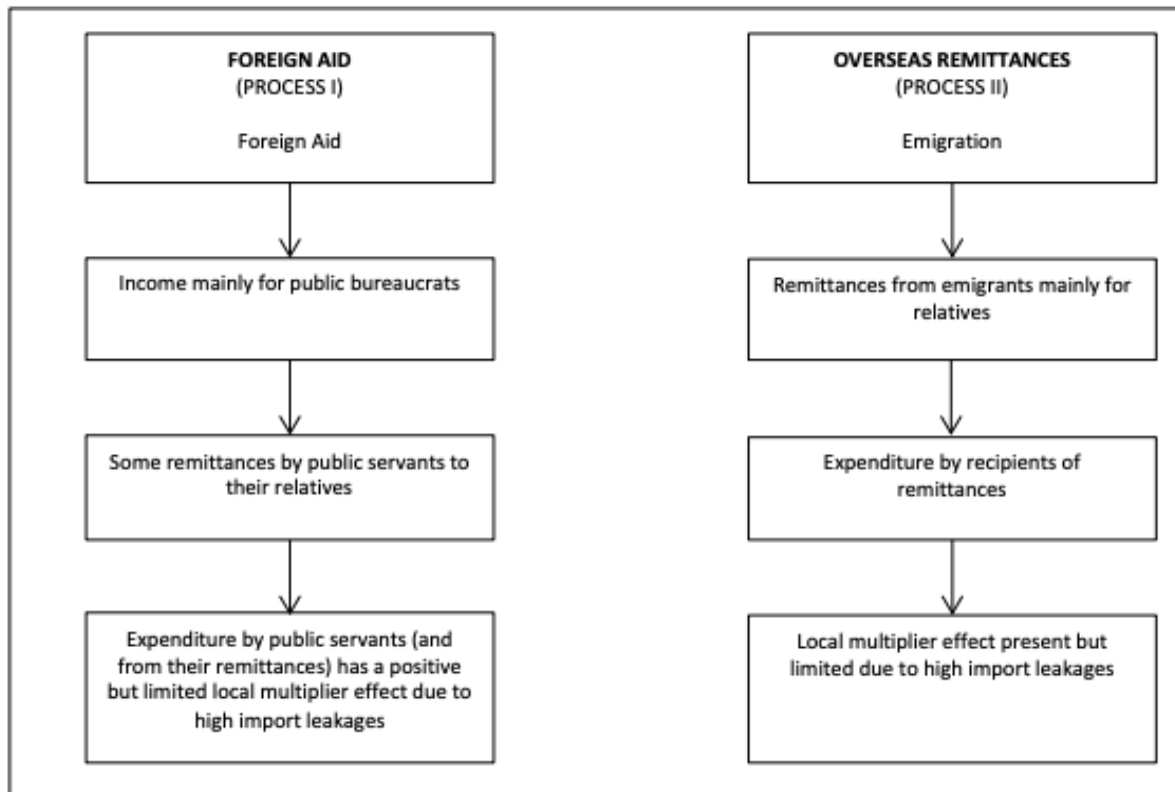


Figure 3.8 Foreign Aid Processes. Source: Tisdell (2014).

MIRAB can create institutional aid dependency and less competitive capitalist systems, structures and processes. For instance, main components of MIRAB such as remittances (R) and foreign aid (A) were significantly affected by it (Choueiri, Francisco, & Zaman, 2023). As a result of the global pandemic, Tuvalu had ‘structural dependency’ on bilateral and multi-lateral aid from developed neighbours such as Australia, New Zealand, including the United States (US) for financial assistances (Abbott & Pollard, 2022; ADB, 2021), which also can be a setback for innovation and growth.

For instance, Tuvalu’s heavy reliance on foreign aid and migration policies to developed countries tend to bolster the public bureaucracy. In turn, it shapes contemporary economic policy and regulative institutions in sustaining aid flows rather than nurturing domestic sectors.

This dynamic often diminishes incentives for local ownership and the use of heterodox economic approaches. The use of ecological, institutional and community-oriented perspectives could further lift them out of poverty.

Another imbalance is caused when many families in Tuvalu have heavily relied too heavily on remittances from families who are working short-term overseas, rather than engage in domestic economic activity. These examples show the importance of understanding the processes of foreign aid and remittances and how they relate to domestic economic growth and budget management (Tisdell C. A., 2014). Furthermore, understanding the impacts of external shocks and vulnerabilities of foreign aid and remittances is also key to making national and household decisions. Understanding these complex processes allows the Government to think of other economic opportunities and diversification (Tuvalu Fisheries Department, 2022; Government of Tuvalu, 2017).

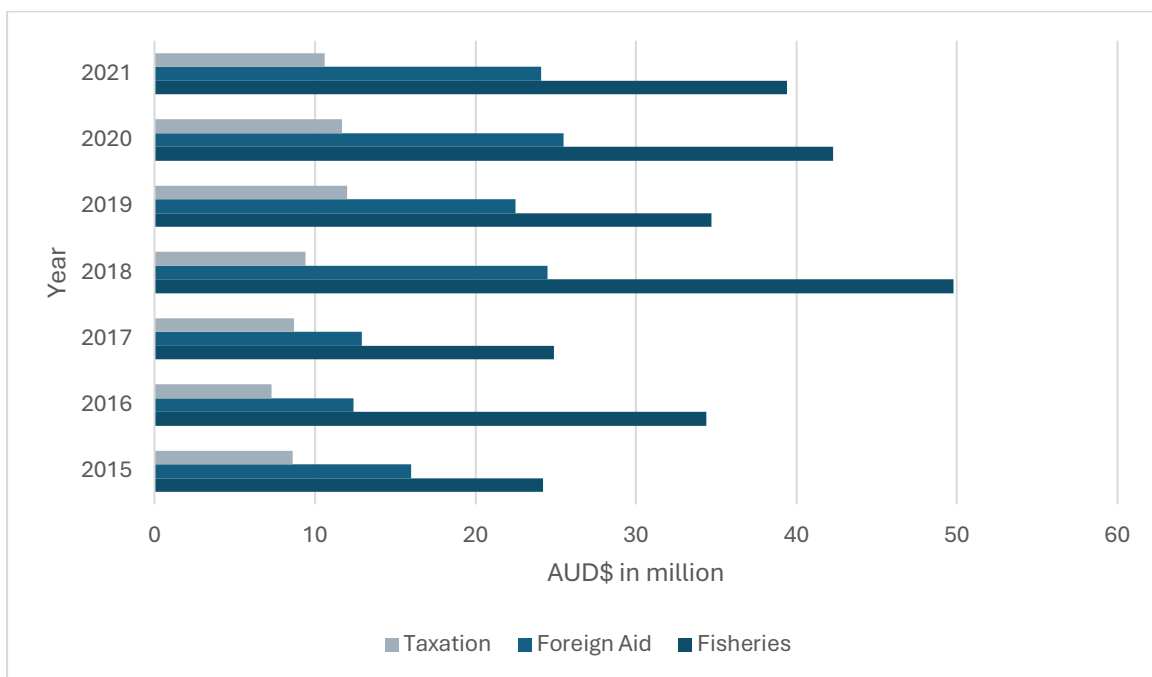


Figure 3.10 Top 3 Main Sources of Revenues in Tuvalu. Source: Government of Tuvalu (2022).

From 2015 to 2022, the Government of Tuvalu have consistently identified the following three as main sources of incomes: fisheries, foreign aid and taxation but the need for economic diversification is necessary (see Figure 3.10). One way Tuvalu can expand its economy is to explore carefully its ocean resources. As Professor Epeli Hauofa (1994) beautifully states, underscoring that the Pacific Ocean as both the best economic resource and the lifeblood for long-term sustainability:

“We are the sea, we are the ocean, we must wake up to this ancient truth.”

This enduring insight urges Tuvalu to transcend its modest landmass and embrace the true breadth of its maritime domain, a perspective championed by Professor Epeli Hau’ofa. The ocean bounty from fisheries to coastal and deep-sea minerals, holds immense economic promise. Through the framework of the 2050 Blue Pacific Strategy, Tuvalu is called not only to harness these oceanic assets but to manage with care, ensuring their continued vitality for generations to come.

This enduring insight invites Tuvalu to look beyond its limited land area and recognize its vast ocean assets, as highlighted by Professor Epeli Hau’ofa. Ocean resources from fisheries to coastal and deep-sea minerals offer significant economic potential. Through the lens of the 2050 Blue Pacific Strategy, Tuvalu is encouraged not only to exploit these oceanic riches but also to steward them responsibly, ensuring they remain sustainable for future generations. Hau’ofa reminds that the Pacific Ocean is a ‘seas of islands’ and that with the Ocean as both our resource base and lifeblood.

In his 2010 study of foreign aid, Iulai observed that aid to the education sector has delivered measurable human capital gains. He also highlighted fisheries as another sector benefiting from aid, noting that growth in fisheries revenues has become an important source of income for Tuvalu (see Figure 3.10). However, sectors like energy, transport, and infrastructure have remained unstable as demonstrated by SOEs such as Tuvalu Electricity Corporation (TEC) and Tuvalu Post Limited (TPL), largely due to fluctuations in global oil prices and technological shifts (Iulai, 2010, p. 388).

Despite annual increases and more stable budget allocations, the roles of education and fisheries in building resilient human capital continues to face significant volatility due to the unexpected and volatility of Tuvalu to external shocks. The impacts of recent global pandemic, geopolitical conflicts in Europe and the Middle East, interest hikes in the United States (US), they have affected all sources of incomes: fisheries, foreign aid and taxation as demonstrated in Figure 3.10 and Figure 3.11. Therefore, relying on traditional practices that have worked for decades to sustain national goals and communities can be an alternative solution (Kitara, 2020; Niuatui, 1991).

Item	2011 (\$AUD)	2013 (\$AUD)	2015 (\$AUD)	2017 (\$AUD)
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Education	6,039,416	6,167,994	10,715,291	10,169,803
Fisheries	446,818	555,232	822,586	819,929
Total	\$6,486,234	\$6,723,226	\$11,537,877	\$10,989,732

Figure 3.11 Recurring Expenditures for Education and Fisheries Sectors Source: Government of Tuvalu (2017).

Tuvalu’s economic vulnerability to external shocks is one challenge, climate change is another major factor. Climate change is not just another environmental issues, it is an existential threat. Because Tuvalu is one the lowest lying countries in the World, routine high tides and storm surges have created ongoing adaptation and mitigation costs that difficult to meet within the budgetary process on annual basis. Destructive tropical cyclones and winds brought heavy rainfalls and severe damages that inflicted economic losses sometime worth over 25% of the national’s gross domestic product (GDP) (Barton, Kadir, Robinson, Jimenez-Ontiveros, & McGrann, 2022; Falefou, 2017). Given the impacts of external shocks and climate changes, it is difficult to account and fairly manage the reporting of government expenditures.

According to the World Bank (2025), climate-related events in Tuvalu result in annual economic losses equivalent to approximately 7% of the country’s GDP. The Deputy Prime Minister and Minister of Finance and Economic Development, Hon. Panapasi Nelesone, emphasized that enhancing the country’s capacity to manage, account for, report on allocate funding for disaster response and climate adaptation is essential for Tuvalu’s resilience (World Bank, 2025). The pledge by the Deputy PM enforces the significant of proper accountability and the need for transparency on climate and government limited funds.

Without sufficient revenue, Tuvalu faces serious fiscal vulnerabilities due to climate mitigation and adaptation. Adjusting of formal structures to resilient informal structures is essential in the case of Tuvalu through enforcing the role of communal ownership instead of private ownership (see Figure 3.11). It means that reinvigorating traditional ecological and resource-management practices (i.e., *kaitasi*) can offers culturally grounded strategies for confronting unexpected and negative climate challenges. Thus, it makes international cooperation and foreign aid essential to protect its economic stability.

The MIRAB model also overlooks how ‘economic strategic value’, and ‘geostrategic services’ can generate rent at a national scale. This trend is especially visible today in the Pacific, where the United States and China are engaged in a fierce battle for regional influence. In the aftermath of the global pandemic and rising debt among low- and middle-income nations,

developed countries have initiated debt relief programs (Aljazeera, 2024; Chen, 2023). While accessing aid is essential for balancing budgets, relying solely on traditional financial methods without embracing new financial innovations may prove more sustainable.

China, as one of the largest bilateral creditors to Pacific nations, has been at the forefront, providing both debt relief and substantial financial assistance to support climate resilience and infrastructure programs (Lowy Institute, 2025; AP, 2023). Consequently, Pacific Island Countries (PICs) including Tuvalu have become cautious about disclosing financial details, balancing these new inflows with the need to maintain diplomatic relations. This cautious stance presents significant challenges for financial transparency and accountability, as the shifting nature of donors and their strategic motives can obscure public oversight.

The MIRAB model abandons the analysis of production and exported-oriented ventures. As pointed out by Boland & Dollery (2005), MIRAB shows that market forces are pushing production sectors to the periphery in Tuvalu. Mainstream development policies aimed at promoting domestic production without diverting resources and energy away from foreign aid (A) and remittances (R) to the production of other resources beside tuna fisheries such as sea cucumbers, coconut oil, and seabed mining. These are some of the business concepts that have proven working in other parts of the Pacific region.

The MIRAB framework doesn't response to fiscal strategies that control the rapid impacts of climate changes. In the Fifth Assessment Report of the Intergovernmental Panel on Climate Change (IPCC) in 2013, it projected that sea level will rise between 0.17m and 0.82m by 2100 (Balesh, 2013). As a result, Tuvalu initiated the Tuvalu Coastal Adaptation Project (TCAP) to protect against sea-level rise, assess population displacement, provide pathway for immigration and preserving of its people's rights and culture. This perspective has aimed to retain Tuvalu's statehood, marine boundaries and limited land. However, the fiscal burden to adapt and mitigate these impacts has been enormous.

For instance, according to the United Nations Development Program (UNDP), the TCAP has accumulated the total of US\$36 million on Green Climate Fund (GCF) for strengthening Tuvalu's institutions, human resources, awareness and knowledge for resilience coastal management. In addition, these GCF assistances have also rebuild homes, schools, hospitals and other infrastructures that have reduced the Government's ability to deliver effective public services.

In 2015, Tuvalu was stroked by Cyclone Pam and accumulated the total damages that was estimated at US\$92 million, including the damages to the crops, animals, and water supplies. In the Cyclone Pam assessment, 90% of crops were damaged in Niu and Nukufetau Island. Taro and pulaka (main staple foods) pits in many areas were inundated and require significant time to reestablish. Roads, hospitals, rams for harbours in few of the outer islands were also damaged (OCHA, 2015). With the frequent storm surges, the impacts of climate costs on the Government budgetary process and revenues can be unpredictable.

The development of strong accountability and transparency for SOEs has been explored by development partners as a tool to alleviate fiscal pressures and enhance operational efficiency, the model has proved difficult to implement in Tuvalu. Given the lack of investor interest, a limited market base, and the essential public roles played by SOEs, alternative approaches such as strengthening corporate governance frameworks, introducing performance-based management, or leveraging public-private partnerships (PPP), may offer more sustainable pathways for economic reform and service delivery.

Aspect	Private Ownership	Communal Ownership (<i>kaitasi</i>)
Legal Basis	Formal, individualized title	Customary, collective tenure
Decision-Making	Individual autonomy	Collective agreement and consensus
Transfer/Sale	Freely transferrable or sellable	Restricted; land cannot usually be sold to outsiders
Resource Use	Profit-oriented or development-driven	Subsistence-based, culturally and ecologically sensitive

Figure 3.12 Private versus Communal Ownership. Source: Author’s analysis (2024).

Thus, we see the limitations of the MIRAB and how current regulative institutions including monetary systems have impacted Tuvalu’s fiscal discipline and economic sustainability, Tuvalu also need to recognize the significant role of traditional systems, structures and processes in pursuing fiscal stability, creating the value for money (VFM) and fiscal discipline.

Conclusion

Regulative institutions have paved the road for Tuvalu to participate in globalization, the frequent government instability and no-confidence motions revealed the challenges of modern systems, structures and processes. Between 2000 and 2021, Tuvalu experienced a repeated shifts in leadership marked by frequent votes of no confidence. Government turnover was

common in Prime Minister Paeniu in 1999, Sopoaga in 2003-2004, and multiple turns overs in the 2010s were precipitated by narrow parliamentary coalitions and elite rivalries rather than policy failure (Tafaaki, 2004). This pattern of political flux fostered gradual public trust building and perceptions of political unpredictability.

A constitutional crisis is another new challenge of political instability under these new regulative institutions in Tuvalu. In the late 2012 and mid-2013, during the constitutional crisis under PM Willy Telavi, the government delayed the by-election for the Nukufetau seat for six months (Tafaaki, 2016). This incident promoted a high court intervention. The governor-general intervened to dismiss Telavi and install Enele Sopoaga as caretaker PM. This episode exposed deep institutional vulnerabilities, eroded procedural legitimacy and public scepticism about the institutional and regulative norms on these modern institutions.

While the Government of Tuvalu's governance model places Ministers in charge of SOEs within their portfolios, creating a dual role as both owners and regulators have been a failure. This setup generates conflicts of interest and limits effective oversight by the Ministry of Finance, which often lacks full visibility into SOE operations. As a result, accountability and transparency is diluted and poor governance and good governance continue to persist unchecked. Therefore, relying on a stronger accountability and transparency approach such as the *maneapa* system, a traditional system, structure and process

Despite the strengths and weaknesses of regulatory institutions in advancing good governance agenda, weak oversight, and substandard service delivery persist, largely shaped by deeply rooted social norms, beliefs, and communal structures. In Tuvalu, private and public leaders in government ministries and SOEs are more attuned to scrutiny by their own communities with the '*maneapa* system' than to external oversight, emphasizing communal visibility over procedural compliance. To bridge this divide, it is crucial to integrate traditional social accountability with formal mechanisms. Therefore, our observations support the Government of Tuvalu's push to embed the *maneapa* framework within financial audits, budgeting processes, and broader transparency initiatives ensuring that formal standards align with culturally accepted, community-drive accountability.

While the MIRAB framework can sustained Tuvalu's economy in the short-term, it is structurally unsustainable. Reliance on fluctuating external flows (e.g., remittances and foreign

aid) are consistently distorted by economic external shocks (e.g., pandemic crisis, financial crisis, geopolitical wars). The rising of sea level, storm surges and frequent cyclones as a result of climate changes impose environmental fragility. The urgent need for economic diversification, build stronger regulative institutions that can withstand climate resilient conditions and environment for Tuvalu would drive a more sustainable economy.

In the next chapter, I discuss the impacts of normative institutions as they interact with public financial management practices.

CHAPTER 4. NORMATIVE INSTITUTIONS AND PUBLIC FINANCIAL MANAGEMENT

Institutions are the rules of the game in a society, or more formally, the humanly devised constraints that shape human interaction – Douglass North (1991)

Introduction

The failures of regulative institutions to maintain sound fiscal management leads this study to explore normative institutions and their relationships with public financial management. Philip Selznick (1948) an American sociologist, argued that normative institutions evolve beyond their formal structures and take on deeper ‘economic and moral significance.’ This economic and moral significance is the institution’s ability to evaluate wrongs and encourage moral obligations to address fiscal discipline. Selznick believes that moral obligations are not just bureaucratic systems for changes but also the ‘carriers’ or leaders for changing social norms, ethics, and traditions.

According to Selznick’s views, normative institutions can be the technical tools that achieve specific objectives. Selznick (1948) argues that dynamic conservatism highlights how normative institutions can adapt to change without compromising their core values (Youvan, 2024). This challenge is clearly demonstrated in the case of Tuvalu, where institutional routines, practices and processes may adjust to modern systems, structures and processes but not to their conservatism core values. Because of this, institutional standards, social reality, and social conditions have not changed totally to new formal or regulative institutions.

In this chapter, the study explores the roles of institutional norms that carriers or leaders use to guide their financial decisions. Factors such as leadership codes of conduct and professionalism financial management practices that create institutional standards, social reality and social conditions in normative institutions. Looking at leadership functions and responsibility inside the Tuvalu’s modern system is the essence to draw the line between ‘what is ought to be’ by comparing to global financial norms (Palthe, 2014). Therefore, observing the budgetary process and procedures at the federal or macro-level is essential. The role of the Government through enhancing human capital and building their capacities to perform at the institutional standards and meet economic realities is key for this chapter.

These factors such as institutional norms code of conduct and professionalism practices play a vital role in improving normative institutions and PFM systems to reduce financial risks.

Institutional Norms

Institutional norms encompass the routines, habits, and practices embedded within organizations, governments, and societies shaping their operations in today's interconnected world. March and Olsen (1984) argue that the "logic of appropriateness" is deemed proper within their institutional roles and contexts to significantly improve financial and management efficiency. Hodgson (2000, 2004, 2006) extends this by arguing that habits, agreements, and norms serve as institutional economic factors that lend consistency and coherence to behaviour within many economic systems. He specifically notes that these social logics and structures foster routines and habits that underpin institutional stability. Effective budget processes and organizational frameworks at both federal and local levels are essential for enhancing institutional norms and PFM.

In the realm of public financial management, these institutional norms materialize through established financial management practices in normative institutions (e.g., Government of Tuvalu both local and federal) such as rigorous budget formulation, systematic assessment of financial market and non-market risks, and regular reporting of fiscal positions. These activities adhere to globally (i.e., modern) and domestically (i.e., traditional) recognized procedural standards, exemplifying how institutional conventions operationalize within modern PFM frameworks. The challenge of these PFM practices that they are not clearly defined in contemporary institutions.

The Budget Process in the Federal Government

One of the most foundational procedural standards in public financial management is the 'budget' (i.e., *fakaso*) and its associated 'budgetary process' (i.e., *fakasoasoaga*). Serving as the primary tool for allocating finite resources across competing priorities, especially in developing Pacific Island Countries (PICs) such as Tuvalu, the budget process delivers several essential benefits. Firstly, it enhances financial control by setting clearly defined limits on spending, which helps prevent overspending and strengthens fiscal discipline (Visser & Erasmus, 2013). It also supports more informed decision-making by public managers, offering a systematic structure for prioritization and performance assessments (NZ Centre for Public Impact, 2019). Furthermore, budgeting reduces costs and inefficiencies by identifying wasteful expenditures and anticipating financial risks (Schick, 2013).

Ultimately, the budgetary process is recognized as a ‘critical governance instrument’ that governs public revenues, debt levels, and expenditures. By enforcing accountability and transparency, it ensures that governments adhere to legally mandated fiscal outcomes (Visser & Erasmus, 2002). Thus, in PFM, the budget is not merely a financial plan, it is an institutional instrument that underpins many systems, structures, and processes where sound governance, prudent risk management, and effective resource allocation is at the centred.

In Tuvalu, the budgetary process (*fakasoasoaga*) is manifested in two distinct forms: informal and formal. The informal process is consisted of traditional norms, which rooted in community customs, where the budget is orally formulate, design, and unwritten. These are the unofficial actions and interactions that exert significant influence even undermining formal rules and procedures. Politicians and official are engaged in backroom deals, pushing or dropping items based on power and interests rather than transparent criteria (Rakner, Ngwira, Smiddy, & Schneider, 2004). However, such essential element of the budget has not effectively used in the budgetary process in the case of Tuvalu.

The formal practices of budgeting that often including the structures, methodical process – typically by government, businesses, or organizations in planning, implementing, monitoring and evaluating financial resources over a set period (described in Chapter 2). This is the formal budget that is carefully prepared in financial plans, where revenues, expenditures and expected returns (or deficits) for a future period is recorded. This document is approved by top executives or legislative bodies of the Government (see Figure 4.1) and remains as an official reference throughout time. Such formal practices can be shaped by formal financial routines, habits and regulatory frameworks that govern public finance.

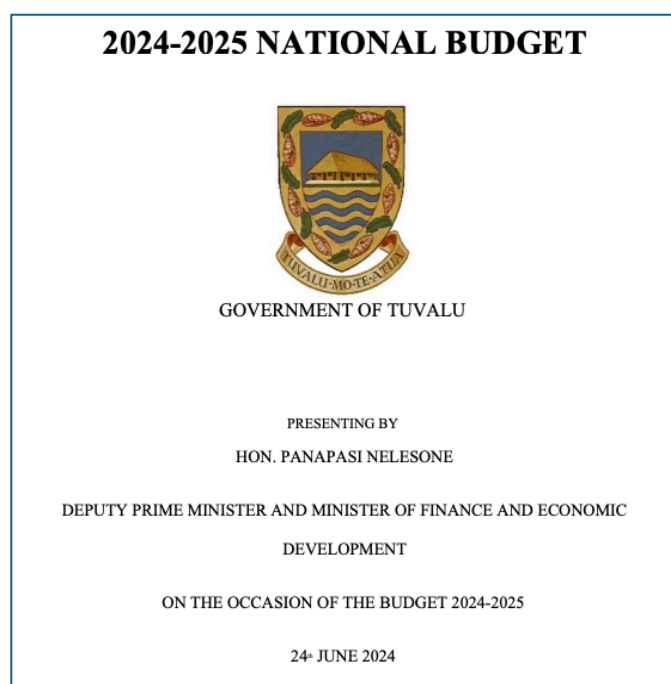


Figure 4.1 2024-205 National Budget document. Source: Government of Tuvalu (2024).

In contemporary practices, according to the ‘Government of Tuvalu Budget Handbook’ (2014), the budget is a financial plan outlining expected government revenue sources and expenditure for the year. Regardless of its size, effective budgeting requires careful decision-making to ensure optimal use of available funds. This involves prioritizing programs and projects, determining which can be funded, and identifying those that cannot (Government of Tuvalu, 2014). Several key documents guide the budgetary process: Governments Medium Term Fiscal Framework (MTTF), *Te Kakeega II* (National Strategy for Sustainable Development), Policy Reform Matrix and Government Roadmap, Tuvalu Trust Fund (TTF) Act, Public Finance Act, Government Borrowing and Guarantee Act, and Appropriation Act.

Although these key documents have provided support and guidance in prioritizing the allocation of funds, the economic data has shown the government continues to spend beyond budget projections, which has led to continuing recurring deficits. This data only represented the most consistent by the World Bank and IMF from 2010 to 2019.

Year	Domestic Revenue (AUD\$ million)	Expenditure (AUD\$ million)	Budget Balance
2014	\$24.9	\$33.2	(\$8.3)
2011	\$26.3	\$29.7	(\$3.4)
2012	\$32.5	\$28.9	\$3.6
2013	\$42.7	\$32.2	\$10.5
2014	\$41.9	\$41.9	\$0

2015	\$52.12	\$60.6	(\$8.48)
2016	\$71.1	\$76.4	(\$5.3)
2017	\$63.50	\$68.3	(\$4.8)
2018	\$59.2	\$54.4	\$4.8
2019	\$55.7	\$84.6	(\$28.9)

Figure 4.2 Recurring Deficits. Source: World Bank/IMF (2024).

According to the World Bank and ADB, pre-grant fiscal deficits have averaged 29.1% of GDP. This means that before accounting for grants and bilateral aid, Tuvalu's budget was chronically in deficit by approximately 30% of GDP on an annual basis. Although with surpluses in year 2012 and 2013, Tuvalu has a persistent structural deficit from climate mitigation and adaptation and also government spendings which required the Government to draw from Tuvalu's sovereign fund, Tuvalu Trust Fund (TTF) to balance the budget (ADB, 2021; World Bank, 2025). With this financial condition, the fiscal health remains acutely sensitive to revenue volatility.

The Budget Process in the Local Government

The establishment of the *Falekaupule* Act (1997) created the traditional council (i.e., *Falekaupule*) and its executive *Kaupule*. Each *Kaupule* or Island Council consisted of six members with a Council President and Treasurer. The *Falekaupule* Act defines as the traditional assembly in each island, where it formulated by respected men aged 50 years and above, who organized customs and laws for managing resources and governing members of the communities (Government of Tuvalu, 2023; Government of Tuvalu, 2020).

Under this Act, the Island Council (*Kaupule*) should draft its annual budget and development plan known as the Island Strategic Plan (ISP). Both the budget and ISP propose their budget drafts to the Ministry of Home Affairs and Rural Development (MHARD) and Ministry of Finance's Planning and Budget Division for funds approval (see Figure 4.3). An average budget allocation is usually AUD\$200,000 per annum. There are locally raised fees and taxes levied on citizens to finance local projects and enhance public services approved by MHARD.

Stage	Description
Drafting & Committees	<i>Kaupule</i> forms budget plan and committee reviews
Public Engagement	Community input & approval during quarterly assemblies
Revenue Planning	Combines national grants, trust fund disbursements, local taxes

Final Approval	<i>Kaupule</i> resolution, oversight from ministries and Auditor-General
Execution & Monitoring	Ongoing implementation with quarterly reporting and oversight mechanisms

Figure 4.3 Local Government (*Falekaupule*) Budgetary Process. Source: Government of Tuvalu (2024).

National bodies such as the Auditor-General, MHARD’s internal auditors, and the Ministry of Finance are responsible for reviewing local government budgets and ensuring they comply with national regulations (Government of Tuvalu, 2023; 2014). However, despite their formal oversight role, these bodies have largely unsuccessful to enforce meaningful accountability and have been notably ineffective in practice (ADB, 2005; ADB, 2011). Therefore, seeking an alternative that can improve financial accountability is key to improve oversight in local government budgets.

Organisations and Structures

In the budget process, the Planning and Budget Department within the Ministry of Finance and Economic Development (MFED) has the primary responsibility for developing the Budget (see Figure 4.3 below). First, the budget is presented to the Development Coordination Committee (DCC) and Cabinet before approval. This process includes scrutinizing the Ministry’s submissions, advising on expenditure priorities, negotiating with development partners for funding support, providing advice on the fiscal outlook, revenue forecasts and expenditure trends and undertaking regular reviews of this information throughout the year as economic and development priorities change (Government of Tuvalu, 2014, p. 3). The weak institutional capacity to present realistic forecasts due to the lack of quality and consistent of data is still a large issue in the budgetary process.

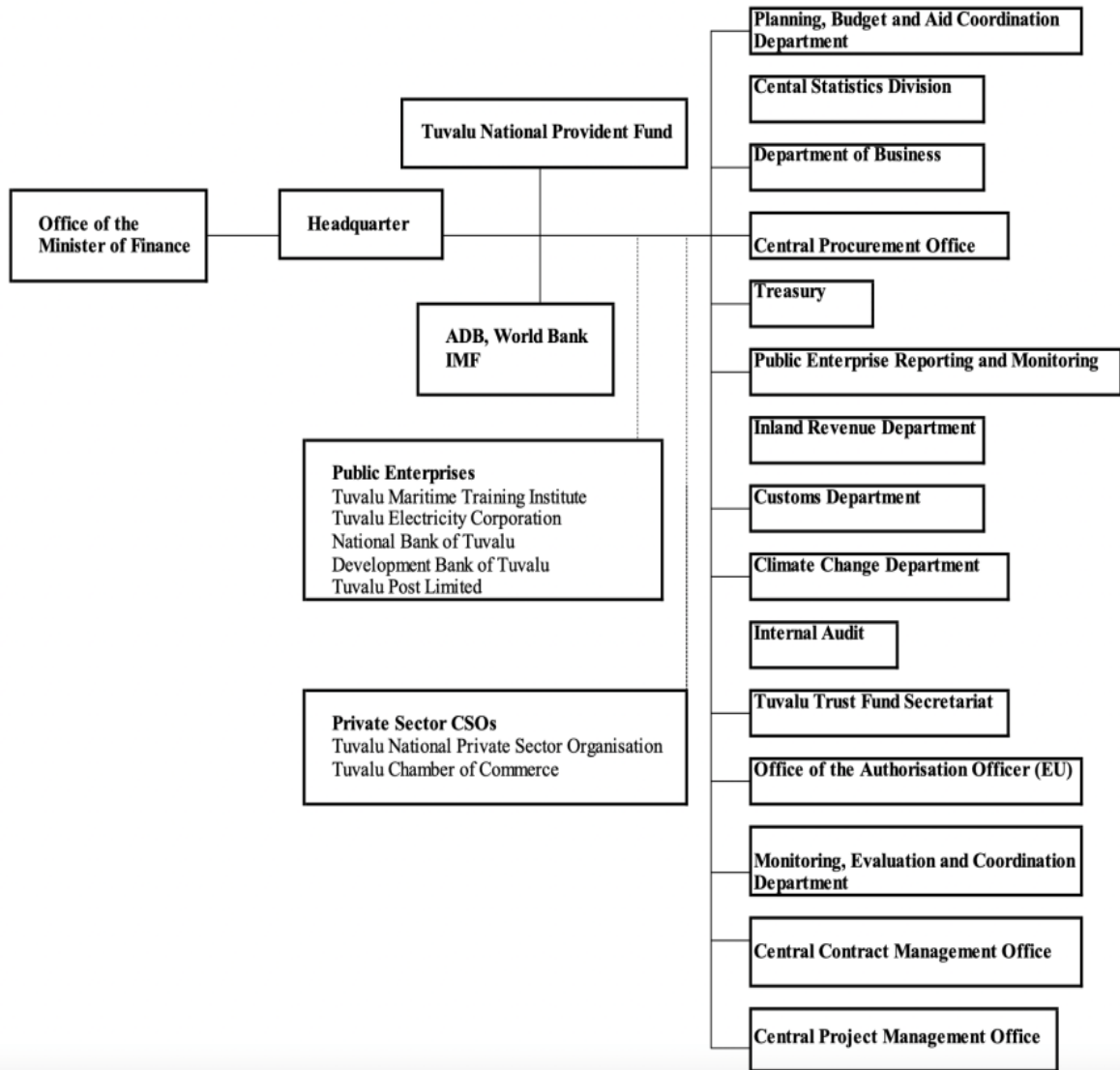


Figure 4.4 Structure of the Ministry of Finance. Source: Ministry of Finance website (2024).

Additionally, the Planning and Budget Department defines the budget process and circulates the National Budget Memoranda to all government ministries and agencies each year. These memoranda detail the submission deadlines, guidance on adjustments to the proposed overall budget ceiling, sector-specific ceilings, a timeline for budget preparation, and scheduled meetings to review budget proposals. Figure 4.5 illustrates the annual submission schedule (Government of Tuvalu, 2014). Although numerous tools exist to scrutinize the Budget prior to its final approval, Tafaaki (2016) argues that there is insufficient critical engagement with the Budget.

One of the central concerns in Tuvalu’s budgeting system is the tightly packed and overlapping schedule of key timetable (see Figure 4.5). Ministries are notified of their budget ceilings and

guidelines by mid-August, yet their detailed budget proposals are due by late August leaving them with only a narrow window for preparation. This compressed timeframe severely restricts ministries' capacity to perform thorough internal assessments, engage stakeholders, and ensure their submissions reflect sectoral priorities and national objectives.

The pressure continues into early September with the commencement of ‘budget rounds,’ followed by Cabinet's review by mid-October. These episodes are scheduled in quick succession, raising the risk that decision-making becomes rushed, undermining detailed analysis and strategic prioritization (see Figure 4.5). In a small public administration like Tuvalu’s, where both staff and technical resources are stretched thin, such compression increases the likelihood of superficial reviews and misaligned funding allocations.

Month	Description
Early July	Budget submission template circulated to Ministries
Late July/Early August	MTFF and Budget Ceilings set by Cabinet
Mid-August	Budget Guidelines issues to Ministries along with Individual Budget Ceilings
Late August	Budget Submissions due to be submitted
Early September	Budget Rounds
Late September	Budget Consideration by DCC
Mid-October	Cabinet Consideration of Budget
Late October	Budget Appropriation Bill submitted to Parliament
Mid-November to Early December	Parliament Debate the Budget

Figure 4.5 Budget Submission Timetable Source: Government of Tuvalu Budget Manual (2014).

The second challenge is the ‘limited flexibility’ for stakeholders (i.e., local governments, island communities, non-governmental organizations, etc.) to inputs and revised the budget once the budget process advances beyond the initial submission stage. For instance, after ministries deliver their proposals, there is little room built into the timeline for iterative feedback, public consultation, or major adjustments before the Appropriation Bill is submitted to Parliament by late October.

Given Tuvalu’s fiscal landscape, the lack of ‘adaptive space’ in the calendar can make the budget process overly rigid. This rigidity potentially leads to budget outcomes shaped more by administrative expediency or political preferences rather than evolving evidence or national consultations. For Tuvalu to strengthen the effectiveness and resilience of its public financial

management, it will need to improve not only the technical quality of submissions but also the institutional processes that allow for more inclusive, transparent, and flexible budget planning.

Building on the foundational role of procedural standards in Tuvalu's budgeting framework, these guidelines acquire profound importance when embedded within the country's broader institutions and public financial management systems. They underscore the moral responsibility of all participants in financial decision-making spanning recruitment, budget development, and expenditures reinforcing governance through accountability and trust.

The Code of Conduct

In the budgetary process, moral obligations for the carriers (i.e., leaders) for changes is vital for financial efficacy and integrity. By delineating acceptable conduct, carriers for changes can prevent mismanagement and abuse of power, fostering 'ethical leadership' across all levels of government. In a small place like Tuvalu, the challenge of 'conflict of interest' can easily intrude the fair, just, and management of limited resources. Thus, improving the budgetary process through ethical leadership and improving the procurement process are vital elements for normative institutions.

Ethical leadership

In normative institutions, ethical leadership (i.e., *takitaki amiotonu*) means that leaders and managers make decisions guided by what's right for the common good not just what benefits themselves or boosts profits. They inspire their teams to follow suit, creating a workplace built on transparency, collaboration, and inclusion, where everyone feels empowered to speak up. Beyond fostering a positive culture, ethical leaders also attract and retain top talent. This echoes core definitions of ethical leadership, which emphasize moral conduct, integrity, and accountability not only among leaders but throughout the organization (Harvard Professionals, 2024).

Ethical leadership embodies these six main principles: respect, accountability, service, honesty, justice, and community. Many empirical studies and meta-analyses have shown positive effects of ethical leadership on individual and organizational outcomes especially on work attitudes and job performance (Brown & Trevino, 2006; Chen & Hou, 2016; Zheng, Olga, Graham, & Caveney, 2021). According to More at al., (2019), ethical leadership is the ideal for an excellent

leadership model, trustworthy, and social exchange aspects that associate with ethics and morality.

The significant role of ethical leadership can illustrate by key performances in the public sector such as budget reliability, transparency of public finances, management of assets and liabilities, policy-based fiscal strategy and budgeting, predictability and control in budget execution, accounting and reporting, and external scrutiny and audit. These factors reflect a core function of good financial governance, systems and process. Together, they help both federal and local government improve accountability, build public trust, and reduce financial risks (Chulu, 2015; Davies, Joshi, & Naidu, 2010; Dunleavy & Hood, 1994)

According to Eli Lopati, Tuvalu's former General Auditor, the country's Code of Conduct & Ethics now be evaluated using contemporary benchmarking tools. For example, reforms to the Office of the General Auditor were implemented to strengthen financial accountability and oversight. Central to those changes was the adoption of modern accounting standards, as reflected in the preamble to the Code of Conduct & Ethics, which explicitly references international norms:

‘To encourage and ensure a professional work environment, which emphasises the work of an individual values tolerance, diversity and flexibility. Integrity is the core value of a Code of Ethics. Integrity can be measured in terms of what is right and just’ (Lopati, 2016).

Tuvalu has placed a strong emphasis on enhancing financial oversight to reduce financial risks and aligning with international accounting frameworks such as PEFA as part of modern benchmarking practices to evaluate and strengthen its public financial management.

The Public Expenditure and Financial Accountability framework commonly known as PEFA was launched in 2001 by seven international development partners: the European Commission, IMF, World Bank and France, Norway and the UK. It establishes a standardised methodology for evaluating public financial management systems, using quantitative KPIs across areas such as budget reliability, transparency, asset and liability management, fiscal strategy, execution control, accounting, reporting and external audit (PEFA, 2001; PFTAC, 2011).



Figure 4.6 Public Expenditure and Financial Accountability Framework. Source: PEFA (2019).

PEFA provides a standardised, widely accepted approach to evaluating financial systems, but it has limitations in capturing real-world effectiveness, institutional realities, and local nuances. This study will detail PEFA limitations in Chapter 6.

Another foundational element closely linked to the Code of Conduct for leaders is the ethical principle of doing ‘what is right and just’ during the procurement process. In the context of Tuvalu, procurement can be particularly challenging due to the close-knit nature of kinship ties and small island communities. These relationships often give rise to conflicts of interest, which may lead to unfair and unethical practices. This is a common issue of ‘social network’ cannot only be found in Tuvalu and many other Pacific Island Countries (PICs) (Dornan & Pryke, 2016; Larmour & Wolanin, 2001; Larmour, 2012).

The Procurement Process

In normative institutions, public procurement is a crucial element of services delivery. It plays an important role in building trust with citizens and contributing to the implementation of key government’s priorities. The procurement process is a vital part of the budgetary process. It helps institutions to effectively manage their financial resources in a manner that benefits its members, is cost effective and can deliver sustainable profitability for long-term survival.

Effective procurement process can directly impact the government’s ability to deliver quality services and achieve policy objectives at all levels of government: central and local. Premchand from the IMF states that procurement should be transparent, accountable, and practical, even when the procurement of fund is small or large. This process should be a tender that is public for any bidder. It should include the procedures, the contract (rules), and changes to the rules, as summarise in the procurement cycle (Premchand, 1989).

In the case of Tuvalu, the Public Procurement Act 2013 became effective in January 2014 as the legal document that prescribed the process and rules. There are two forms of procurement: minor and major. The Minor Procurement is any government procurement that is total at AUD\$500 (Australian dollars-AUD) and between AUD\$5000. A Major Procurement is any procurement that is estimated more than AUD\$5000 and is undertaken by the Central Procurement Unit (CPU) under the Ministry of Finance and Economics. Figure 1.16 shows the current procurement process in Tuvalu (Government of Tuvalu, 2014).

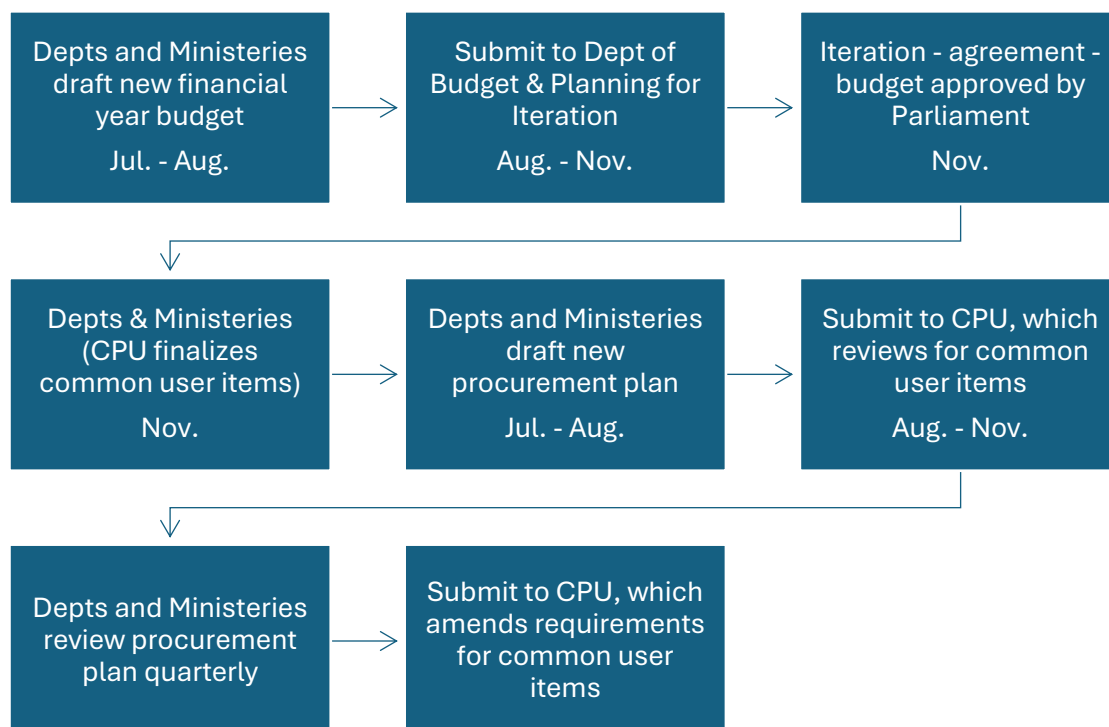


Figure 4.7 Procurement Process. Source: Government of Tuvalu Department of Procurement (2014).

The process has to be at least six months long. The process begins in July, with draft budgets submitted to the Department of Budget and Planning for iteration between August and November. Once the Department of Budget and Planning approves the draft then it would go

to Parliament for approval. Then the Departments and Ministries draft a new procurement plan according to the Government needs, then it is submitted to the Central Procurement Unit (CPU) for final review before the bidder receives the result (see previous Figure 4.3 for organisational structure in the Ministry of Finance).

The Central Procurement Unit (CPU) Annual Report 2018 acknowledged that despite overcoming significant challenges in establishing the Procurement Process and Act in 2013, staffing shortages remain a critical issue. Currently, the CPU operates with only five staff members, including the Head of the Unit, three Operational Procurement Officers, and a Policy Procurement Officer. A major challenge is the submission and recording of procurement plans from line ministries and departments (CPU, 2018). Addressing the shortage of certified officers has become a key priority to enhance the department’s effectiveness and efficiency.

Procurement planning remains a significant challenge in the procurement process. The lack of proper planning often results in last-minute major procurement transactions and reviews due to insufficient personnel. For example, in 2018 there were 119 out of 181 major procurement transactions conducted through Direct Contracting, while approximately 36% of major procurements could not be completed (CPU, 2018). The single-year budgeting system at the Federal Government level further complicates the process, leaving limited time for the CPU to conduct final reviews before parliamentary approval. Adopting a ‘medium-term budget forecasting (MTBF) approach’ would enhance the budgeting process and improve the efficiency and effectiveness of procurement (CPU, 2018; Visser & Erasmus, 2002).

The prequalification standards for major procurement currently follow established guidelines. When hiring contractors, relevant background and experience are essential; however, no formal legal procurement standards exist. According to the Procurement Manual, the prequalification questionnaire for major procurement includes company details, structure and organization, resources, experience, and financial capacity. A similar questionnaire is provided to companies planning a joint venture for the same procurement. Applicants have 30 days to submit their prequalification documents to the CPU.

Minor Procurement

Indicator	2016	2017	2018
Total transactions	476	565	689

Value Total \$AUD	\$878,935	\$1,005,139	\$1,457,473
Competitive Bid (no)	396	555	432
*Directing contracting	80	10	257

Major Procurement

Indicator	2016	2017	2018
Total transactions	192	142	181
Value Total \$AUD	\$11,557,636	\$6,278,143	\$8,427,957
Competitive Bid (no)	36	57	59
*Directing contracting	156	85	122

Figure 4.8 Minor versus Major Procurement Statistics (2016 – 2018). Source: Government of Tuvalu (2018).

* Note: Direct Contracting is also known as ‘single-source procurement’. It is a non-competitive procurement method where a contract is awarded directly to selected supplier without a formal bidding process. It is typically used where competition is impractical, unnecessary or not feasible.

The procurement evaluation process is guided by the Public Procurement Act 2013 and its subsequent regulations. For major procurements, an evaluation committee of at least three members is appointed to assess proposals based on criteria outlined in the Request for Proposals (RFP). The evaluation focuses on aspects such as company details, organizational structure, resources, experience, and financial capacity. Introducing new criteria not specified in the RFP during the evaluation is prohibited. While the process is designed to be straightforward, the scoring matrix can be complex due to the lack of formalized standards.

For minor procurements, bid evaluation committees are appointed by the respective procuring entities. These committees consider only the evaluation criteria specified in the procurement documents. Additionally, the regulations prohibit automatic disqualification of bids priced above or below a predetermined estimate. If a bid appears abnormally low, the evaluation committee is required to seek clarification from the bidder to ensure the bid's viability. Overall, while Tuvalu's procurement evaluation process is structured to promote fairness and transparency, the absence of formalized scoring standards can introduce complexities in the evaluation process.

In conclusion, addressing the shortages in staffing, planning, and standards is crucial for strengthening the Procurement Department's capacity. Improving these areas would enhance

procurement regulations and promote best practices. Currently, the procurement process is lengthy and challenging for many bidders, particularly for major procurements, as the timeline follows an annual framework rather than mid-term budget forecasting. Limited competition among bidders is another issue, as the public remains largely unfamiliar with the procurement process. As noted, most procurements between 2016 and 2018 were conducted through Direct Contracting, where contracts were awarded to single bidders due to a lack of competition.

Professionalism

In normative institutions, professionalism can shape and improve public financial management practices systems, structures and process. In the Pacific, the term professionalism is interchangeably with custom and tradition, which essentially pivot to ‘what we’ve always done’ as opposed to ‘what we’ve done prior to colonisation’ (McLeod, 2007). In 2005, Pacific leaders endorsed the ‘Pacific Plan’ in Port Moresby that emphasise the ‘what is ought to be.’ This Plan encourages regional cooperation and integration to improve economic growth, sustainable development, good governance and security of Pacific countries. Furthermore, the Plan promotes regional reforms to improve budgeting, auditing, procurement and reporting standards across PICs including Tuvalu. However, the challenge of professionalism is the different between new versus old definitions, characteristics and practices. Emphasising the role of education to communicate such differences can synchronize the new and old management practices.

Professionalism: New versus Old Management Practices

The new standards and definitions of professionalism may be different around the world. However, the sentiment of ‘professionalism’ (i.e., new practices) can be defined in simple terms by the U.S. Department of Labour. They describe this term as a professional or someone who consistently demonstrates a combination of qualities: punctuality and effective time management, accountability for their actions, ability to collaborate well with others; adherence to high-quality work standards, honesty, neat appearance and appropriate attire. These traits collectively embody professionalism (DOL, 2020). Such expectations of professionalism have been standardised throughout as a one size fit all.

In Tuvalu and across the Pacific, professionalism is shaped not only by standard work traits mentioned above like integrity, reliability, courteous dress, but also deeply influenced by local cultural values. These distinctive qualities that define professionalism can be consistently

demonstrated in the ‘Pacific Way’ (i.e., old practices), faith in God (*fakatuʻanaki*), respect for the elders (*ava*), community leaders and members of kinships; contribute to the collective good of the kin and community (*fesoasoani*); and generosity (*alofa*) (Kitara, 2020; Kabutaulaka, 2021; Joseph, 2015). With these traits, collaboration and collective efforts are required to contribute to the betterment of the society and community.

Promoting harmony and fostering professional relationships among managers and employees in any normative institution is essential for strengthening PFM. It can also reduce risks and uncertainty. For Tuvalu to reduce financial risks, the Pacific Plan provides access to technical assistance from the Pacific Technical Assistance Centre (PFTAC) and other development partners in the region. It also facilitates collaborative efforts between the IMF, 18 Pacific Island Forum (PIF) members countries, IMF and World Bank, and bilateral donors such as Australia and New Zealand (PFTAC, 2024). The Plan supports Tuvalu in strengthening institutional capacity, regional training, and the design and implementation of sound macroeconomic and financial policies.

For examples, in 2023 the PFTAC TAs have focused on PFM, Revenue Administration, Financial Sector Supervision, Real Sector Statistics, Government Finance Statistics and Macroeconomic Analysis as key Actual Outturn workshops in the region. In 2022, Debt Management was a key workshop that was stressed its importance in PICs public finance and management. For Tuvalu, PFM workshops were narrowly focused on two key PFM initiatives: agile PEFA assessment and the development of PFM Roadmap. Tuvalu’s PFM roadmap was incorporated with Tuvalu’s Strategy for Sustainable Development 2021-2030 (Government of Tuvalu, 2020; PFTAC, 2021).

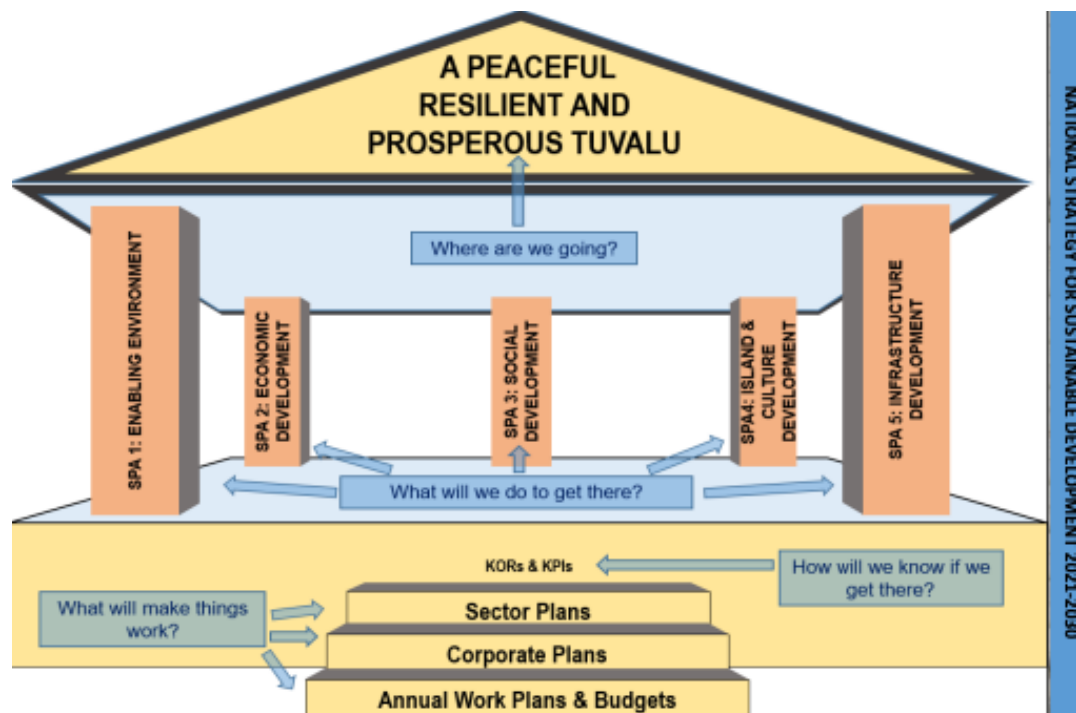


Figure 4.9 National Strategy for Sustainable Development 2021-2030. Source: Government of Tuvalu (2024).

According to Seve Paeniu (2020), the former Minister of Finance, this PFM roadmap (i.e., Te Kete) will be an important framework as Tuvalu is living through a paradigm shift of the ‘new normal’ unexpected pandemic crisis, geopolitical crisis, or financial crisis. This roadmap allows Tuvalu to look back at their ancestors’ management practices like ‘*kai filifili*,’ a ‘pragmatic approach’ in high level planning and professionalism to address real economic challenges of today.

For instance, with ‘*kai filifili*’ or pragmatic approach, Tuvalu is shifting its focus on the important of technology as the main factor for enabling their constraints environment. Recently, the Government of Tuvalu has prompted to digitise most of their services online, issuing passports, payments and licensing online. In addition, the Government of Tuvalu has focused on improving professionalism to meet digital problems from cybercrime and e-commerce. Furthermore, the Government also encouraged the role of e-learning and e-government services. The focus on enabling environment allows Tuvalu to meet the rapid changes in our global world and meet international norms and standards (Government of Tuvalu, 2020).

In strengthening institutional capacity and reinforcing PFM, the Development Bank of Tuvalu (DBT) plays a critical role in supporting private sector growth and small business development (IMF, 2023) especially within key government mechanisms such as state-owned-enterprises (SOEs). As of 2017, DBT reported net assets of AUD\$1.7 million, which reflected a sound financial footing. However, the historical records of high proportion of ‘non-performing loans’ (NPLs) have been consistently reported by the World Bank and IMF as an enormous challenge.

In 2017, the Ministry of Finance reported that DBT has an accumulated loss of equity from \$3.8 million to \$3.7 million, a \$1 million improvement on the previous year. In 2019, the Government of Tuvalu made a total payment of \$64,281 to DBT, an increase of \$34,281 from the previous year, 2018. In 2018, DBT EIB loan reached the total of AUD\$107,198 and the Bank couldn’t service it since its conception in 2003. As a result, the Government of Tuvalu committed to guarantee the entire amount in case of default since they have the largest net shares of the company. Such institutional behaviours display the lack of professionalism and the challenge of profitability not only by DBT but also by other public enterprises such as TEC and TPL (ADB, 2021).

The liquidity ratios in Figure 4.10 demonstrates the financial concerns the ADB (2021), World Bank and IMF (2023) and PFTAC (2024) on Tuvalu’s public enterprises. According to the Whole-Statements of the Government of Tuvalu from 2020 to 2023, TEC quick ratio of 0.73 indicates unhealthy benchmark, where quick ratio often considered healthy at 1.5 to 2.0 on average standards. The rise of energy prices of fuel around the globe due to COVID-19 and conflicts in Europe and the Middle East had caused a rise in concerns about solvency of TEC from \$1.54 in 2020 to \$4.38 per litre in 2022 while not counting the inflationary prices of commodity and fuel globally.

The lack of increasing TEC and TTC profitability is extremely concerning for the Government as they relied too much on Government’s supports and subsidies to continue current operations. Thus, improving the level of professionalism, where public enterprises’ managers and executives take full responsibilities on how to ride their ships is essential. In particular, the vulnerabilities of SOEs require careful attention and remediation. The lack of completing corporate plans, enhancing governance and performance, and lack of service quality often demonstrated the lags behind Government’s expectations.

Types	Ratio	TEC			TTC	
		2020	2021	2022	2022	2023
Liquidity	Current Ratio	1.33	1.37	1.21	2.81	3.65
	Quick Ratio	0.73	0.77	0.62	2.72	3.57
Solvency	Debt-to-Equity	1.54	1.88	4.38	2.54	2.15
Profitability	EBITDA Margin	0.04	-0.10	-0.17	0.31	0.42
	Return on Assets	0.001	-0.08	-0.13	0.12	0.12

Figure 4.10 Tuvalu's State-Owned-Enterprises (SOEs) Key Ratios. Source: Government of Tuvalu (2024).

It has been 47 years since Tuvalu became a sovereign nation and the challenges of adopting a new way of doing business in the public sphere has not been easy. As financial institutions such as the ADB, World Bank and IMF advocate for the changes of structure or governance from traditional governance to market-economy, it is not simply an overnight project. Given centuries of embracing, living, and practicing an indigenous social order, political and economic norms will not just vanish. Rather it takes time to adjust to new fiscal and monetary disciplines.

Education System

Some of the ways we can address institutional norms, code of conduct and being professional in normative institutions is through education. Nelson Mandela (1990), a former UN General Secretariat and former South Africa President said this on the significant of education:

‘Education is the most powerful weapon in which you can use to change the world.’

In the same light, Oscar Wilde (1890) appears to be polished the important of education as well. He said, ‘you can never be overeducated.’ In the midst of over aceturate ideas and philosophies floating around on how to be a professional, learning to understanding how new and old practices intersect can be key to build effective PFM practices for Tuvalu. Providing knowledge, skills and opportunities where modern PFM and indigenous are compromised can synchronise systems, structures and processes in many levels of the federal and local governments including public enterprises.

The study by Dr. Konai Helu Thaman titled ‘Learning to Think in the Language: Indigenous Education in a Colonized and Globalized Pacific’ spoke to the challenge many Pacific Island Countries including Tuvalu face, including how difficult it is to integrate Western knowledge and economic systems to indigenous systems (Thaman, 2019). Two main tensions have limited the integration of Western and indigenous education systems (e.g., *poto mua*). First, it is the ‘tension between group and individual, and second is the tension between traditions and modernity’ (Thaman, 2019, p. 4).

Traditional professions in Tuvalu each revolve distinct skill sets known as *pologa*, which were typically inherited within families and often considered sacred (*tapu*). As identified by Taafaki (1983), these include roles such as ‘*tufuga*’ (canoe builders or house builders), *tagata ote moana* (fishermen), *te koso* or *uanuu* (farmers), *mafi* (warriors), *amoamo* (healers), among others. Much like today, these vocational skills were deeply interwoven into day and social life in Tuvalu. Their legacy lives on in the songs and dance that narrate about their stories, difficulties and innovations in life (Taafaki, 1996). These skill sets are used for collective purposes and the sustainability of the entire community or society without monetary fees (see chapter 5).

For instance, when I was young and sprained my ankle playing sports, my mother would take me to a traditional healer for treatment. In the evenings, I often saw villagers gathering around 6pm at the healer’s house whenever someone fell ill. Later, when my father decided to remodel our home, he asked the local *tufuga* (home builder) to assist our family without monetary compensation. In gratitude for his time and expertise, we offered him a large fish such as tuna, as a form of barter. Such practices are common traditional systems, structures, processes most in community settings continue today.

In creating modern labour force, Thaman (2019) argues that the compartmentalization of knowledge and skills between Western educational systems compared to PICs or indigenous educational system is totally dissimilar (Thaman, 2019). For instance, indigenous’ educational systems are based more on holistic, interconnected, experiential and context-specific compared to Western. For instance, in the Ministry of Finance, having a degree in Accounting, Finance, and Economics are essential for work and manage public funds. This is quite the contrast to traditional structures, where the expert doesn’t earn modern education, but they inherited from their ancestors.

The challenge between the new and old practices is synchronisation. New education methods, approaches, and philosophies often undermine the effectiveness of communal practices that formulated for centuries and decades. New education approaches also don't have the curiosity of questioning the premises of why such small communities uphold those social norms, habits and practices. Thaman (2019) argues that though indigenous people are now bounded by different laws, regulations, policies and practices developed by Western experts, they are not the same laws, regulations and policies nor practices that operates for centuries.

Perhaps the idea of foreign domination or colonialism has negatively overwhelmed the right and freedom for education. Goldsmith (2009) presented an argument that: 'there is no better way to destroy a people than to undermine their education system (Goldsmith, 2009, p.3). The view of colonial development was that of disregarding old education, religious beliefs, values and political orientations - meaning on who or what they are or think they 'ought to be.' Thaman (2019) reported that indigenous education often focused on origins, history, customs, traditions and languages. In addition, the indigenous/old educational system embraces and encourages compassion, respect, humility, loyalty, and spirituality as educational values and norms.

In solving ecological challenges such as food security and climate changes, the elders play a major role in traditional education. Since *pologa* or skill sets are inherited, it created a division of labour and specialisation in an 'ecological approach.' In the case of Niutao Island, an island located in the northern groups of islands in Tuvalu, the elders who have accumulated knowledge, skills and values from life experiencing itself (Nia, 2021). The elders' specialisation in traditional knowledge come from the learning various educational approaches such as observation, imitation, and participation in practical activities. The elders teach young people in their own trait using shared language and in real life situations. In contrast, formal agriculture degrees require young Tuvaluans to leave their islands and attend the University of the South Pacific (USP) or somewhere else.



Figure 4.11 Pulaka Roots. Source: Ioane Sitaake (2016).

Furthermore, the elders are expected to model sustainable outcomes that were being taught by judging their learner's appropriate behaviour and community's performances when members of the community requested for their help in any related to their skill sets (Nia, 2021). For instance, farmers (*uaniu*) will be judged their knowledge and skills on community competitions like the '*pulaka* competition' on whom grew the fastest and largest *pulaka* root (*cyrtosperma merkusii*) in the island. This is often the long process of learning an inherited skill set or *pologa*.

Thaman (2019) contends that indigenous education is deeply rooted in ecological and cultural contexts, embracing 'non-market values,' where knowledge is passed on by those who have already learned to understand, act, and be within their environment (Thaman, 2019). This framework applies equally in Tuvalu: to become a skilled healer, one must apprentice under a master healer who has experienced, treated, and witnessed a wide range of ailments. Healing is intricately linked to one's surroundings, diet, and ecological conditions so, for coastal communities, marine-based foods become central to both their nourishment and their healing practices (Sogivalu, 1992). Culturally, these forms of learning demand extensive dedication countless hours and many years to attain mastery, mirroring the thousands of hours and roughly 15 years it often takes to complete medical school and training to become a doctor.

Because of the compartmentalization of modern education, there are not many Tuvaluan students are interested in monetary subjects and concentrations such as Accounting, Finance and Economics. Many students since the 1970s have preferred medical schools, Theology, and Political Sciences. Thus, there are very limited institutional capacity in Public Finance nor Financial Management subject matters. Tuvaluans are gravitated to majors that familiar with them and also have cultural meanings. With the economic challenges that Tuvalu is currently facing on deficits, lack of exports, and debt there are limited learning and capabilities for

Government of Tuvalu to compensate to the demand of such subject matters because of the costs associated (Public Manager1, 2023).

With limited opportunities for Tuvaluans to study the role of ‘market values and structures’ in specific academic disciplines such as commerce, accounting, finance and management, the Ministry of Education mentioned that very few in Tuvalu had exposed to financial management practices in developed countries. Such experience is worthwhile and could make a positive impact on PFM reforms.

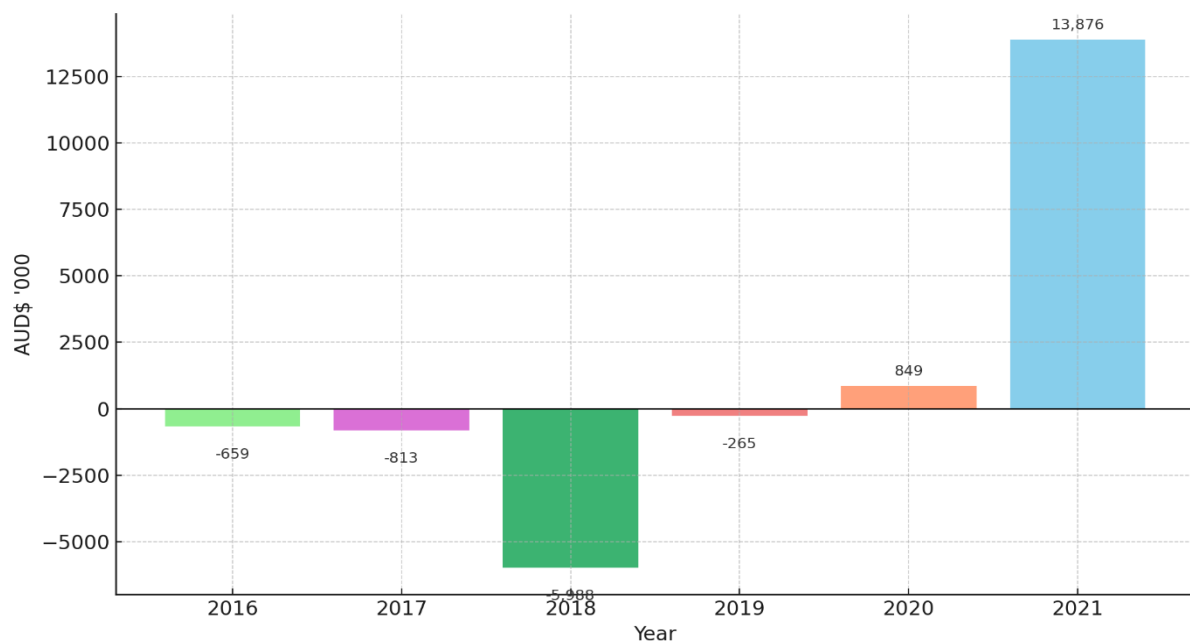


Figure 4.12 National Budget Surplus/Deficits (2016 – 2021). Source: Government of Tuvalu (2021).

During our data collection, it became evident that limited technical capacity poses a significant challenge to effective public financial management in Tuvalu. Several local experts highlighted an over-reliance on external consultants, which has undermined local ownership and hindered the sustainability of PFM systems, structures, and processes. Furthermore, the absence of adequate incentives has contributed to high staff turnover within key institutions such as the Ministry of Finance, the Department of Planning and Budgeting, and the Internal Audit Office. This has weakened institutional memory and caused delays in the implementation of PFM reforms (Public Manager4, 2023). Capacity constraints have also disrupted record-keeping processes, resulting in frequent delays. These limitations in skills, knowledge, and experience

are reflected in broader macroeconomic challenges, including persistent budget deficits and trade imbalances (see Figure 4.12).

The contrast between traditional (ecological approach) and modern education systems (economic approach) reveals significant differences in pedagogical approaches. However, integrating elements of both systems, structures and processes can meaningfully address the limited human capacity within local and national governments. Thaman (2019) argues that revitalizing traditional management knowledge and sustainability practices within contemporary Pacific education frameworks can strengthen cultural identity and support local economic resilience, as old system once did in the past.

Professionalism in Tuvalu is shaped by a combination of traditional cultural values and modern normative expectations. Punctuality, accountability, competence, ethical conduct, and effective communication are all essential components of strong public financial management systems, structures, and processes. These values are often influenced by social norms, relational accountability, and formal education. The interplay between formal and informal systems: traditional and modern, emphasizes the need to foster trust, leadership, and social harmony within Tuvalu’s governance framework. Therefore, integrating ecological and economic approaches from both indigenous knowledge and modern education is crucial to strengthening PFM capacities across normative institutions.

Aspect	Indigenous Education System (Ecological Approach)	Modern Education System (Economic Approach)
Focus	Environment & ecosystems	Money, trade & financial growth
Goal	Sustainability & conservation	Profit & resource efficiency
Concern	Natural balance & biodiversity	Market stability & development
Example	Climate change policies	Stock market performance

Figure 4.13 Old versus New Education Models. Source: Author’s comparison analysis (2024).

Conclusion

Tuvalu’s institutional norms reflect a unique blend of traditional values and modern bureaucratic expectations. These norms shape how public leaders and managers behave, how decisions are made and how normative institutions function across both at federal and local

government. Traditional norms emphasise communal values, respect for the elders and collective responsibility, while modern administrative norms promoted PEFA framework and modern Acts that regulate public finances. However, the major problem is the interaction between traditional and modern norms often creates tension that has led to weak PFM systems, structures and processes. This issue is created many weaknesses for PFM reforms.

As a result, this fragility stems largely from high staff turnover, limited technical capacity through the budgetary process is important element for Tuvalu's PFM system. This lack of continuity disrupts the implementation of public policies and reforms, particularly in key areas such as budgeting, auditing, and planning. Additionally, poor documentation practices and the absence of compliance and oversight further erode the government's ability to draw on past lessons to inform future decision-making. The role of ethical leadership and improving education in both new and old systems is vital for PFM reforms and normative institutions.

To address these challenges, Tuvalu must strengthen institutional norms by investing in long-term capacity development, improving record-keeping systems, and formalizing procedures for documentation and knowledge transfer from old and new management knowledge. Encouraging mentorship between senior and junior staff, digitizing important records, and establishing standard operating procedures can help preserve organizational knowledge in key normative institutions such as the Ministry of Education. Moreover, blending modern administrative practices with traditional governance structures such as the *maneapa* system, can foster a culturally relevant model of knowledge of transparency, retention and institutional learning. Strengthening institutional memory is essential not only for effective Code for public managements' conduct, but also for the resilience and sustainability of Tuvalu's public financial management systems.

The use of pragmatic approach (*kai filifili*) to jerry picks advantage methods and principles between Tuvalu's old and new management practices such as respect public funds, love your neighbours, do what is right for the people can uphold high standards of behaviour across government institutions. It can also reinforce professional values such as honesty, fairness, and diligence. These principles are essential for ensuring that public servants act in the best interest of the people, particularly in the management of public finances.

All these values can strengthen professionalism and the Code of Conduct for leadership and normative institution in Tuvalu. As pointed out previously, professionalism is not only

measured by individual behaviour in the workplace but also by one's cultural commitment to communal responsibility, respect (*fakaaloalo*), and service to the collective good. Traditional leadership structures, such as the *falekaupule* (local council of elders), still exert strong moral influence over local governance and professional conduct. This interplay of formal and informal systems reinforces a unique Pacific model of professionalism, where trust, relational leadership, and social harmony are critical. Thus, the need for promoting both traditional and modern education, management practices and normative institutions that build resilient economy for Tuvalu is essential for moving forward.

The next chapter will discuss how cognitive (i.e., informal) institutions, cultural norms and non-market values can influence public financial management mission and implementation.

CHAPTER 5. COGNITIVE INSTITUTIONS AND PUBLIC FINANCIAL MANAGEMENT

A famous Song of Niutao Island demonstrates the beauty of cognitive institutions:

*Ko aku pese
Mo aku vii
Mo aku fatele
Ne fatu ki muna o toku fenua
Toku gau galeo
E tagitagi fakaNiutao
Toku fenua ne fanau ai*

Translation of the Song:

*My songs
My lullaby
My dance
Have been composed by the sincerity and
sweetest words of my Island
It is the sounds of my language
It is the cries of my Niutao accent
It is the Island where I was born.*

Introduction

The traditional Niutao song, or *fatele*, illustrates the crucial roles of institutional memory, behavioural biases, and communal accountability as shaped by cognitive institutions. The interaction between public financial management principles and cognitive institutions such as kinships, island communities, and religious organizations, can drive both meaningful progress and ongoing challenges in PFM development. These elements collectively reveal how cognitive institutions shape the way PFM systems, structures and processes operate.

This chapter also examines how elements of institutional memory such as history, institutional experiences, and traditional practices, serve as a vital reservoir of knowledge that informs decision-making and everyday operations. In Tuvalu, much of this memory has been preserved through community-constructed narratives such as songs, stories, and dance - which, as Barbara Czarniawska (1997) suggests, act as alternative forms of remembering and institutional continuity.

In addition, behavioural biases such as loss aversion, anchoring, and overconfidence - can distort objective decision-making by influencing public managers in processing information, emotional decision-making, and under social pressures from others. As a result, such biases can affect predictions and decisions across various domains, including public finance, labour markets, and development. In Tuvalu, *mafaufau* (e.g., mental processes) may override

economic reasoning, as decisions are frequently guided by social norms and expectations rather than purely rational economic incentives.

Furthermore, this chapter investigates forms of social responsibility or communal accountability, where collective or group effectively accounted for their actions. Peter Larmour and Barrie Macdonald believe that cultural authority, informal sanctions, and collective oversight are key characteristics that can enforce PFM's transparency and accountability. Social responsibility frames by duty to community and collective welfare, where Peter Larmour (2005) suggests that 'people are not accountable *upwards* to government or donors, but to their *inwards* community.' Understanding institutional memory, behavioural biases and communal accountability can strengthen weaknesses of PFM.

Institutional Memory

To understand the influence of cognitive institutions on public financial management systems, structures, and processes, research highlights that elements of institutional memory including history, experience, and established practices serve as vital sources of sustainable knowledge. Memory is the action of remembering, recollection, and perpetuating knowledge or recollection of things of the past (Byrne, 2015; Corbett, Grube, Lovell, & Rodney, 2018). Elements of memory such as institutional history, experiences and practices from the past that guide public managers in making informed decisions that promote continuity, stability, and the long-term wellbeing of communities can shape PFM systems, structures and processes.

In the theory of organization and management (O&M), Chester Barnard (1938), Nonaka and Takeuchi (1995) and Peter Drucker (1993) evolved the modern thinking for institutional memory by promoting collective knowledge through 'tacit' and 'explicit' knowledge based on standard operating procedures (SOPs), technical manuals, scientific data and interpretations, and so forth. Institutional memory is understood as the process of retaining knowledge, practices, and experiences within cognitive institutions such as kinship, community, and churches (Byrne, 2015). On the other hand, tacit knowledge is based on personal experiences, insights, and learning through trial and error, observation, or mentorship.

Institutional History

The history of Niutao Islands and its economy including sustainable models have passed down through narratives in songs, stories, or dances. Niutao Island is a reef island in northern Tuvalu

the main executive authority into two factions: the Uta State and the Tai State. The Uta State followed the royal lineage of Paramount Chief Papauoatua VIII, while the Tai State was led by Paramount Chief Valavala I. This bifurcation of leadership caused a rupture within the royal bloodline, intensifying rivalries and competition over authority and resources among the chiefly elite.

However, in the 18th century, the creation of Sixth Chiefly Houses of Uta State and Fifth House of Chief in Tai State was created to reduce hatred and corruption and rather built a more peaceful community. The creation of local community court and ruling functions of chiefs to settle disputes was also created – *Te Malie o Fuatia* (Fuatia’s Goodwill). This was a great transformation of structure, processes from a hierarchy to a more of circular structural system.

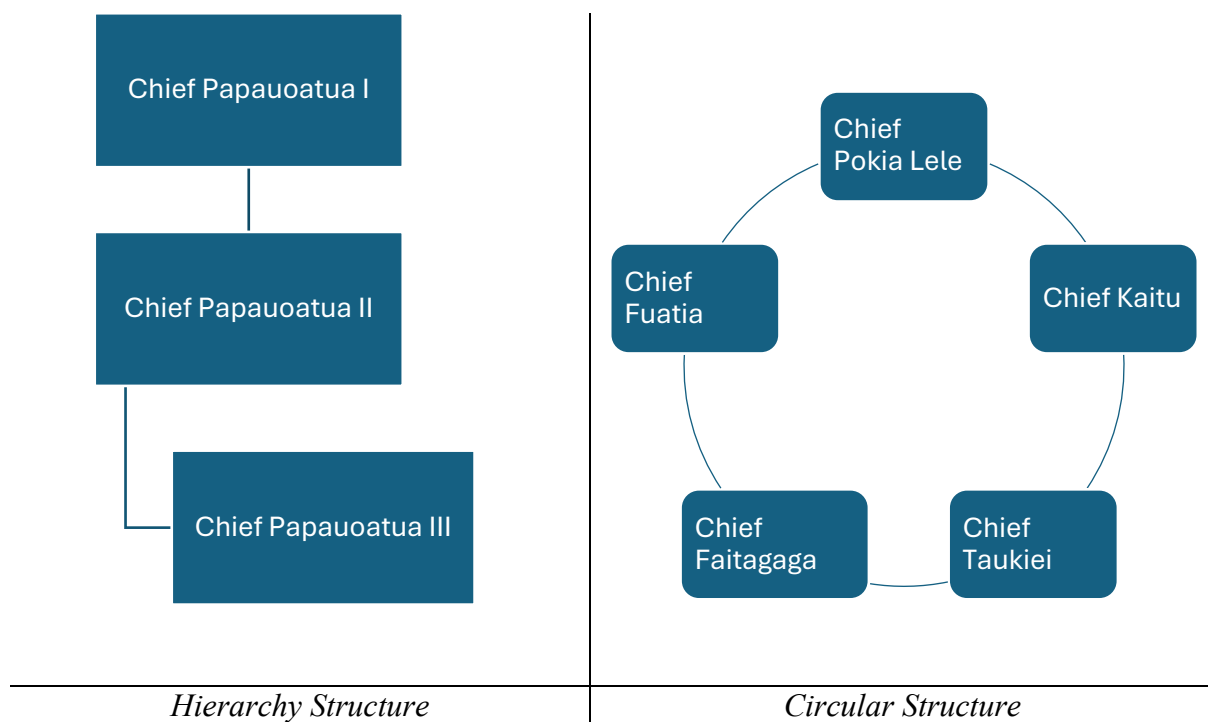


Figure 5.2 Transformation of Niutao Island Chiefly Structure. Source: Sogivalu (1992).

Te Malie o Fuatia continued to impact how Niutao’s treated foreigners in the 18th century even till to this day. In the 18th century many new settlers from Kiribati travelled to Niutao and were welcomed, treated kindly and were offered land titles in Niutao. As a result, these new settlers from Marakei, Maiana, Beru and Tabitouea Islands of Kiribati gifted their sacred knowledge of black magic and the supernatural upon the people of Niutao, known today as the ‘Lagai fakaola fenua’ or Land lifesaving power (Sogivalu, 1992, p. 18).

Te Malie of Malaefono played a central role in shaping a shared identity among many Niutao people throughout Tuvalu, widely known as *Te Noti*. *Te Noti* represents an informal, yet recognizable, cultural identity that distinguishes young Niutaoans across the islands. They are often identified by certain traits commonly associated with Niutao culture such as possessive love (*alofa valea*), abundant patience (*onosai*), and playful or foolish humour (*lagia*). According to Sogivalu (1992), these traits are not accidental but emerge from the island's unique institutional environment. As elders in Niutao often say, '*A fuataga o tamaliki e mafai o iloa mai fuataga a matua mo kaiga*,' meaning '*The fruits of the children (their behavior) can be traced back to the seeds planted by their parents, families, and communities.*' This reflects how deeply personal identity is shaped by collective values, traditions, and social norms.



Figure 5.3 Ariel Photo of Niutao Island. Source: Wantech Design (2024).

Perhaps the positive impact of strong communal loyalty and care for others can foster strong collective ownership of resources in Niutao, it also can lead to more inclusive planning and spending decisions. However, there is a risk these above traits can also fit uneasily with modern systems of government and finance as it can blur the lines between public and private interest. It may result in nepotism, favours, or emotional decision-making in allocating funds to family or close kin rather than to projects based on objective need or merit (Barcham, 2007).

Institutional Experience

The experience of local leaders plays a critical role in shaping the effectiveness of public financial management in Tuvalu. Their accumulated knowledge and experience of governance

processes in traditional systems can influence public resources are planned, managed and accounted for. With institutional experience, the Government of Tuvalu formulated the traditional assembly (i.e., *Falekaupule*) or council of elders on Niutao Island as the highest institutional structure that the govern local community (Firth, 2004; Goldman, 1970; Government of Tuvalu, 2023).

In the 18th century, the circular structure of the Chieftainship in Niutao Island became clearer on how their functions and special responsibilities were delivered. So, the new structure of the *Falekaupule* is made up of chiefs (e.g., *aliki*), elders and other respected community members who represent the voice, values, and interests of the people of Niutao. At the same period of time, Sione and Tapu, both Samoan pastors sent by the London Missionary Society (LMS) began to influence the way Niutao people managed their limited resources. The salutation chant composed by the people to honour the ‘Good News’ (*Tala Lelei*) demonstrated another layer of transformation to the power structure of the Chieftainship system.

<p>Chant:</p> <p><i>Ko Muna ite Mamalu</i></p> <p><i>Kote Mata ote Alik</i></p> <p><i>Io me ko te suipou Alik</i></p> <p><i>Kote Malu o Fenua</i></p> <p><i>Ote Tala Lelei</i></p>	<p>Translation:</p> <p><i>Behold the Sacred Voice</i></p> <p><i>They are the Eyes through which the Chief sees the</i></p> <p><i>people</i></p> <p><i>They carry the Honor and Pride of the Island</i></p> <p><i>They are the Bearers of Glad Tidings</i></p>
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Figure 5.4 Salutation Chant of the Good News. Source: Sogivalu (1992).

This salutation chant demonstrated how the London Missionary Society (LMS) pastors’ status on par with the Niutao Island Paramount Chief was essentially restructured from the 18th century (Goldsmith, 1989; Sogivalu, 1992). As a result, contemporary cultural protocols and norms in Niutao continue to mandate the highest respect be shown to both LMS pastors and the ceremonial Chief – selected from the various chiefly houses spanning the Uta and Tai States. This dual authority structure, deeply embedded within the maneapa system, persists as an enduring legacy of that historical transition.

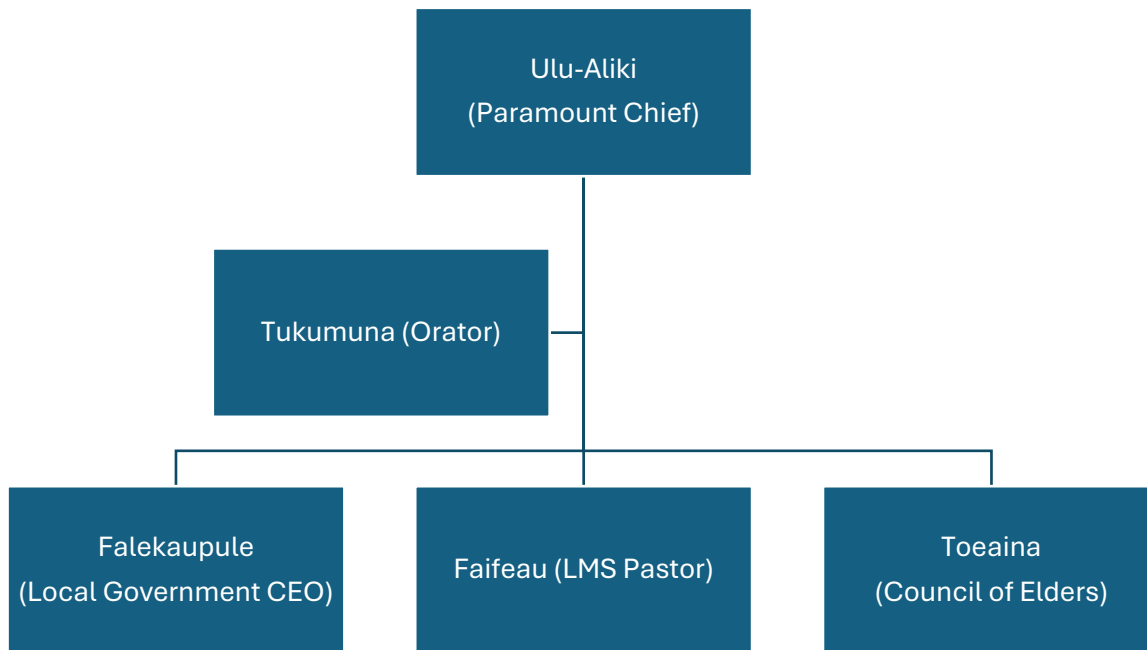


Figure 5.5 Postmodern-Chiefly Structure. Source: Author’s Analysis (2023).

For many indigenous groups like Niutaoans, salutations and blessings hold profound and multifaceted importance in cognitive institutions. It demonstrates experience of consistency and alignment to ancient knowledge. According to Katoto Fikau, these practices reinforce the reciprocity with the natural and the spirit world. It also connects the living to their ancestors and community. Furthermore, it enforces the respect for the elders and social order that was installed in honouring the memories of the past (Fikau, 2023). Thus, reinstating salutations and blessings is part of reclaiming the spirit of elders and ancestors. It acknowledges the reciprocal circle between the past and present believe to interweave the spirits of the living, the dead, and their lands.

On Niutao Island, the chief retains traditional responsibilities as custodian of land, culture, and the community, roles that have endured over time (see Figure 5.4). The Paramount Chief (*ulu-aliki*) exercises ultimate authority in communal decision-making, following consultation with elders (*toeaina*), orator (*tukumuna*), the *Falekaupule* (council of elders), and broader community members. In contrast, the *Kaupule* (elected island council) and its officers receive formal salaries and allowances from the central government, while chiefs do not benefit from such monetary compensation. This dual structure - combining the traditional chiefly system with elected local governance within the ‘maneapa framework’ - characterizes the institutional configuration of power and authority in Niutao, as in other Tuvaluan communities (Paeniu, 1995).

Byrne (2015) argues that for Indigenous Australians, deeply embedded ‘cognitive institutions’ such as traditional ownership, the use of Indigenous protocols, honouring elders, and fostering connections between past and present are essential elements of institutional memory. These practices sustain authentic dedication and continuity within Indigenous systems (Byrne, 2015, p. 259). Sogivalu (1992) believes is the same sentiment and narratives that was found in a tiny, small indigenous group of people in the archipelago of Tuvalu, Niutao Island. The honouring and paying respect to their ancestors’ methods and ways of sustaining life is essential element that intertwine with present sustainable practices – ecological and agricultural production.

Byrne (2015) and Sogivalu (1992) highlight that institutional experience, comprising collective knowledge, shared histories, and experiences cultivated within cognitive institutions is a vital normative resource that Indigenous institutions frequently draw upon to address economic and social challenges. These experiences encompass the cumulative ‘know-how’ derived from historical decisions, both successful and unsuccessful practices, and evolving norms. They include explicit forms such as written records, manuals, and standard operating procedures and implicit or tacit dimensions such as unwritten rules, experiential judgment, and cultural behaviours that are not readily codified. Thaman (2019) emphasizes the importance of preserving these tacit dimensions, noting their role in sustaining institutional memory and guiding adaptive governance.

The systems, structures and processes in Niutao Island is much similar to other eight islands of Tuvalu: Nanumea, Nanumaga, Nui, Vaitupu, Nukufetau, Nukulaelae, and Funafuti. Indigenous experiences and cultural wisdom have passed down through generations, often without formal documentation or written. Examples include traditional fishing techniques that applies tidal patterns, fish migration and the use of handcrafted nets and traps. It also involves the knowledge of canoe building, navigation and weather prediction using wind patterns, cloud formation and ocean currents. It also considers wisdom of community chiefs and elders to resolve conflict and disputes. Other forms of tacit knowledge are traditional medicine and healing, weaving and handicrafts (Shiu R. N., et al., 2024; Sogivalu, 1992).

Application	Explicit	Tacit
Nature	Formal knowledge Books or documents knowledge	Personal and subjective knowledge Individual experiences, intuition, insights

Transferability	Easily shared through written or digital means	Require personal interactions and hand-on experience
Accessibility	Readily available Stored in computer database	Difficult to access because team need to watch and learn

Figure 5.6 Tacit versus Explicit Knowledge. Source: Author’s Analysis and Jen Avelino (2023).

Understanding this dynamic is crucial for policymakers and development practitioners to capture the essential nature of explicit knowledge and tacit knowledge in Tuvalu. Interventions that overlook the significance of cognitive institutions risk undermining the very social structures that contribute to the community’s cohesion and sustainability. Therefore, development strategies should aim to engage with and build upon existing cognitive institutions, ensuring that new systems are adapted to fit within the established social fabric rather than displacing it.

Institutional Practice

Traditional economic subsystems in Tuvalu have the potential to create a virtuous path for resource management through subsistence and ‘communal economy’ or communal economic system. Elinor Ostrom (1993) found that economic activities in communal economic systems are organized around ‘communal well-being’ of the collective society rather than individuals’ profit on the mode of production such as – land, labour and capital. The production, distribution, and resource allocation are made through processes or consensus rather than by market forces or central authorities (Macdonald, 1982; Larmour, 2005). Since life circumstances are volatile and unpredictable, collective needs are more important than individuals.

With the establishment of the Westminster model of governance since 1978, traditional local governance in Niutao and throughout Tuvalu has historically been structured around a hybrid structure, where the *Falekaupule* (council of elders) and the *Kaupule* (their executive body) are two main structures in local governance. This arrangement was formally reinforced in December 1997 when the Parliament enacted the *Falekaupule Act 1997*, providing statutory recognition and regulatory authority to these institutions. In 2018, Feue Tipu, Graham Hassall, Matthew Kensen, Sara Mecartney, Rikiaua Takeke, and Karibaiti Taoba have recognized that

local governance has statutory recognition it was more established for ‘customary authority’ with very limited ‘fiscal decentralisation’ roles (Hassall, et al., 2018).

Under Section 40 (supported by Schedule 3), *Falekaupule* and *Kaupule* were explicitly assigned oversight responsibilities across various local sectors, including agriculture, livestock, fisheries, land management, public health, public order, trade, communication, and public utilities. This legislative empowerment enabled island councils to adopt a comprehensive approach to community governance and resource management. Section 41 further requires both bodies to allocate their own financial and human resources to assist police operations in crime detection and prevention within their communities. Additionally, the Act empowers them to enact bylaws and plan environmental stewardship initiatives such as marine conservation plans aimed at safeguarding Tuvalu’s limited natural resources.

The *Falekaupule* Act of 1997 fundamentally reconfigured customary leadership structures, transforming the traditional *Falekaupule* and its executive counterpart, the *Kaupule*, into legally recognized local government entities. This hybrid governance framework grants these institutions both customary legitimacy and statutory accountability, thereby enabling Niutao’s *Falekaupule* and *Kaupule* to effectively oversee public resources, drive local development initiatives, and safeguard community well-being (Oppong, 2015). Despite these advancements, significant challenges persist namely, the disconnect between tacit cultural knowledge and formal regulatory systems, which has hindered the alignment of cognitive and regulatory institutions and stalled the articulation of clear sustainability and development objectives. It was only in subsequent years that the national government fully acknowledged the pivotal role of empowered local councils in promoting holistic national growth.

Local government in Tuvalu, embodied by the *Falekaupule* (traditional island councils), consistently struggles with chronic revenue shortages and is frequently unable to keep pace with infrastructural and innovation demands at the local level. As Hassall and Tipu (2008) observe, national governments in the Pacific region including Tuvalu’s face their own fiscal pressures and are often reluctant to allocate additional funding to sub-national entities, especially when confronted with concerns regarding limited financial expertise and instances of mismanagement at the local level (Hassall, et al., 2018).

In response to these challenges, Tuvalu established the *Falekaupule* Trust Fund (FTF) in 1999, with the support of development partners such as the Asian Development Bank (ADB, 2019).

Initially capitalized at approximately AUD\$12 million and structured with a reserve buffer to stabilize disbursements, the FTF reached an estimated market value of AUD\$25.3 million by mid-2007, from which around AUD\$4.7 million in payouts were made to support island council (*Falekaupule*) operations. These distributions have supplemented the *Falekaupule*'s own modest revenue streams which include user fees, business and land licenses, head taxes, and land taxes as well as sporadic national grants. Such combining of revenue sources has provided a more stable financial foundation for local development initiatives.

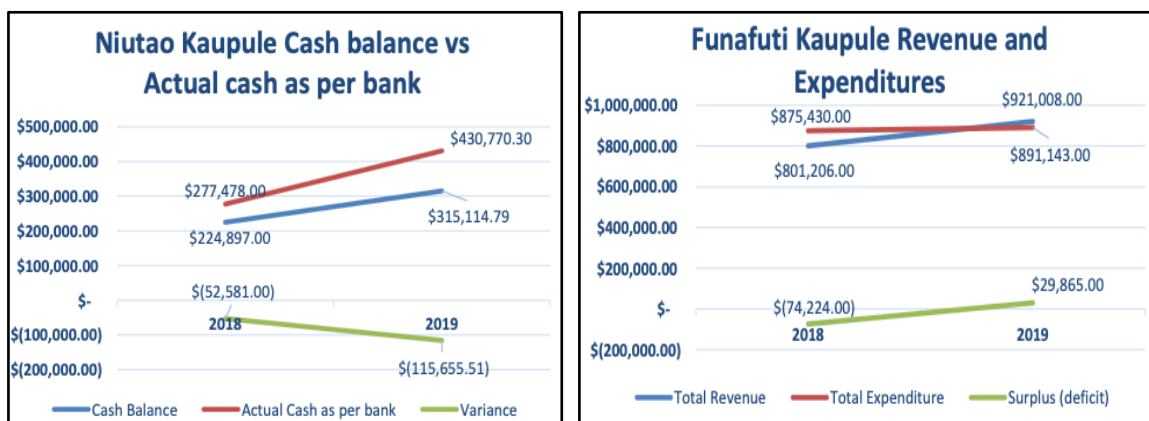


Figure 5.7 Niutao & Funafuti Kaupule's Cash versus Actual Cash in 2018-2019. Source: Auditor General (2019).

Despite the fact that *Falekaupule* in Tuvalu struggles with limited own-source revenues and insufficient transfers from the national government, the *Falekaupule* Trust Fund (FTF) has emerged as a vital and innovative mechanism that strengthens island councils' ability to finance essential infrastructure and public services (see Figure 5.6). Scholars such as Nunn (2007) and Kirch (1984) argue that Pacific Islanders have historically “learned how to cope” with shifting environmental and social conditions. Traditional land-and-sea tenure systems - like Hawaii's *ahupua'a*, the Cook Islands' *raui*, Micronesia's *mehen*, and Vanuatu's *noho*, demonstrate how small-island societies, including Tuvalu, have long navigated ecological variability through integrated resource management (these concepts will be expounded more in Chapter 7) (Delavaux, 2018; Nunn, et al., 2023).

Despite limited fiscal capacity at the local government level, communities in the Pacific have sustained resilient traditional knowledge systems and institutional memory in ecological and agricultural production, enabling them to adapt to environmental changes, including those driven by climate variability. As Nunn et al. (2023) report, cyclone impacts over the past decade including damage to subsistence crops, increased salinization of freshwater supplies, and

destruction of infrastructure, continue to threaten local livelihoods. Nonetheless, these communities demonstrate enduring capacity to recover and adapt, drawing on time-honoured practices to cope with recurrent adversity.

While institutional memory often enhances organizational learning, there remains a critical need to integrate traditional and modern knowledge systems within Tuvalu's cognitive institutions. Pollitt and Bouckaert (2000) argue that repeated waves of public-sector reform including frequent restructuring, staff turnover, and evolving information systems - have diminished institutional memory (Pollitt & Bouckaert, 2000). By explicitly incorporating both the tacit knowledge embedded in traditional practices and the explicit knowledge associated with contemporary fiscal discipline, Tuvalu's local governments could strengthen their cognitive frameworks and improve financial performance.

Several decades ago, my cousin and I had the privilege of caring for his grandmother, Tagoga, who was highly regarded as one of the foremost experts on Niutao Island due to her extensive indigenous knowledge and expertise in traditional fishing techniques, known as 'Mulivaka.' At the time, she was approximately seventy to seventy-five years old. One afternoon, feeling a strong craving for fish, she instructed us to visit Muli, a well-known reef in Niutao Island, which had been bombed by the Australians during the 1990s to facilitate access to the Niutao harbor.

She was aware that it was the time of the 'lunar perigee,' a period she associated with favourable fishing conditions. With great precision, she directed us to gather hermit crabs (*uga*) for bait, advising that we could find them within the roots of pandanus trees (*fala*). She emphasized the need to act quickly, as we would miss the opportunity of the 'low tide running.' Furthermore, she explained that when the tide approaches its extremes, either high or low, fish are less likely to bite, showcasing her profound understanding of tidal patterns and their impact on fishing success, though not educated in modern or formal education (see Figure 5.6).

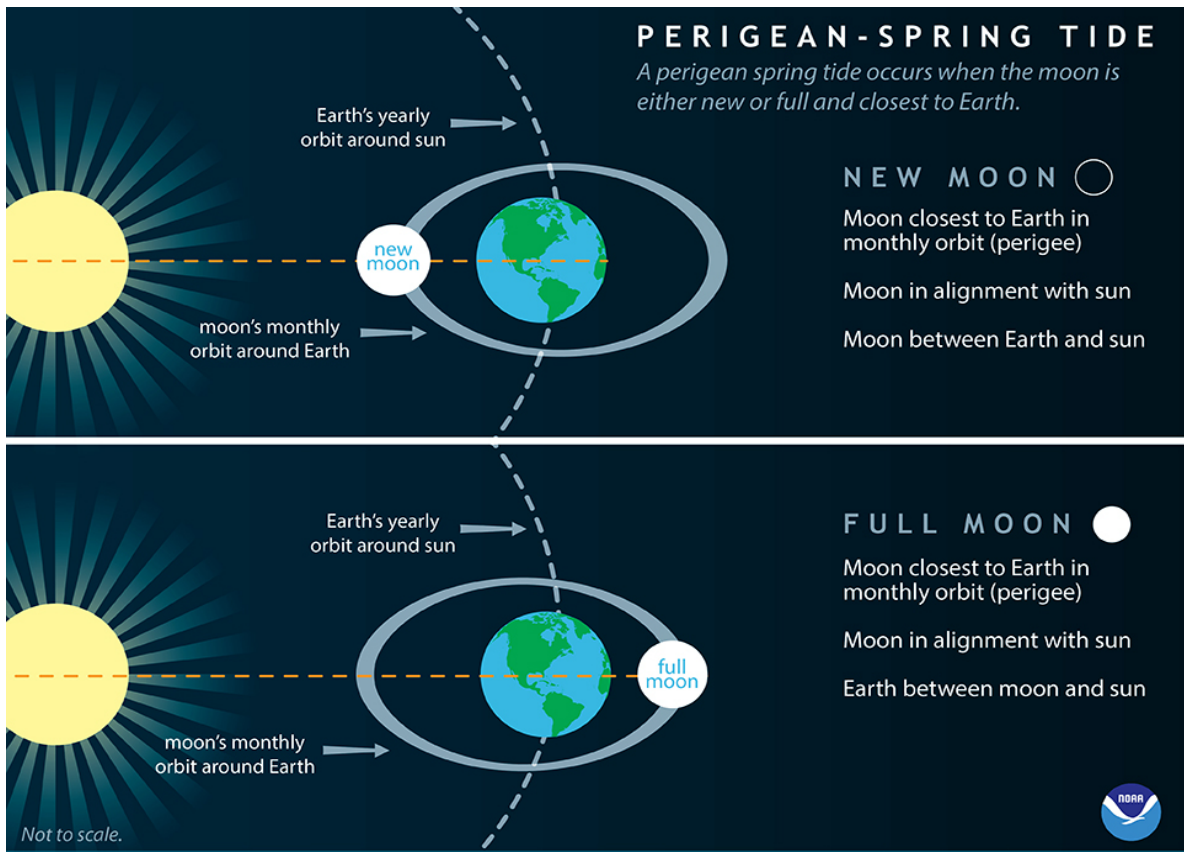


Figure 5.8 Perigean Tide Patterns Source: NOAA (2024).

She further instructed us to use the smooth tails of the larger hermit crabs (*uga*) for bait. She explained that the bigger tails would be more suitable for attracting the larger peacock grouper fish (*gatala*), emphasizing the importance of using the larger crabs rather than the smaller ones. Additionally, she suggested that we should catch enough fish to fill the ‘falai,’ a term often used in Tuvalu to refer to catching enough only for a meal and not too much, so we would not waste. We carefully adhered to her instructions, and as a result, we successfully caught plenty of peacock groupers that day. Institutional knowledge is demonstrated here as a vital part of indigenous community that has lived on through tacit approaches.

Although Grandma Tagoga may not be formally recognized in modern academic journals on marine and ecosystem studies or oceanic and atmospheric research, her expertise in fishing techniques was deeply rooted in tacit knowledge passed down through generations. She inherited this wisdom from her ancestors, who had been esteemed members of the Niutao community for centuries. The traditional fishing techniques, known as *Mulivaka*, were carefully preserved by the *Mulivaka* ‘kinfolk’ (Carsten, 2024; Shiu R. N., et al., 2024) and played a central role in communal activities and celebrations. This indigenous knowledge emphasized sustainability and food security, particularly during challenging times. Moreover,

it ensured that extra food was available for visitors and temporary residents, allowing the community to extend hospitality to strangers and foreign guests without direct family connections in Niutao.

As fiscal literacy and monetary management become increasingly vital for the resilience of small economies, it is equally imperative to recognize the value of non-monetary knowledge such as indigenous agricultural and ecological wisdom given by Grandma Tagoga.

Behavioural Biases

As modern economic approaches increasingly becoming more dominant in Tuvalu, there is resistant and biases toward the demise traditional knowledge and skills for sustainability. These behavioural biases can be found in loss aversion, simplicity bias, and familiarity tendencies in the development of public financial management. Daniel Kahneman and Amos Tversky (1979) pioneered research on ‘cognitive biases’ and ‘heuristics’ in decision-making, they found that ‘behavioural economics’ can be an instrument in shaping economic decisions (Kahneman, 2011; Ostrom, 1990). Kahneman and Tversky (1979) offered strong critiques of the ‘utility theory’ with the ‘prospect theory’ behaviour because of the theory’s lack on how people’s actually make decisions under risk (Kahneman & Tversky, 1979). They believe that irrational behaviour are biases toward information that supports their pre-existing beliefs, norms and values while ignoring contradictory evidence. This bias can lead to poorly designed policies rather than data-driven analysis.

Loss Aversion

According to Kahneman and Tversky, loss aversion refers to the psychological tendency in which individuals perceive the pain of losses more intensely than the pleasure of equivalent gains. In other words, the emotional distress associated with losing a certain amount of money tends to outweigh the satisfaction derived from gaining the same amount (Kahneman, 2011; Kahneman & Tversky, 1979). This cognitive bias is a key factor behind risk-averse behaviour, resistance to change, and often irrational financial decisions. In the context of Tuvalu, such tendencies can be traced back to the transitional period between its pre-colonial structures and the onset of British colonial rule, which introduced new uncertainties and disruptions to traditional socio-economic systems.

One of the enduring oral traditions frequently shared with children on Niutao Island is the prophecy once declared by Chief Galiga. Before the arrival of Christianity, Chief Galiga warned the people of Niutao about the coming of a new religion. He firmly stated that he would not convert, as his faith remained with the god who resided in the ‘seven heavens.’ He cautioned the community not to embrace the new religion, foretelling that doing so would lead to immense suffering. In recent times, many elders have come to reflect on this prophecy, recognizing the deep cultural and spiritual disruptions caused by the introduction of Christianity and its impact on their ancestral belief system (Macdonald, 1982; Nia, 2021).

Chief Galiga’s deep devotion to the ancestral religion ultimately led to open resistance against Chief Kapui, who had welcomed and supported the arrival of Christianity. This ideological conflict escalated into violence, culminating in Chief Galiga stabbing Chief Kapui. Following this confrontation, Christianity was widely embraced across Niutao Island (Fikau, 2023; Sogivalu, 1992). To this day, the descendants of Chief Kapui continue to honour his legacy, commemorating his pivotal role in introducing Christianity and transforming traditional beliefs. However, a growing number of young Niutaoans have begun to sympathize with Chief Galiga, as they question the burdensome financial demands tied to religious obligations and church-based development activities (Maega, 2021).

External efforts to implement public financial management reforms on Niutao have frequently met resistance not because islanders reject modern systems out of hand, but because these ‘new frameworks’ – perfect competition, materialism, ‘Garbage In & Garbage Out,’ which clash with deeply rooted cognitive institutions: traditional norms around communal resource management and shared decision-making (Fuechsel, 1950; Alibo, 2010). Small Pacific nations like Tuvalu often face capacity constraints: low population and limited skilled personnel mean that importing ‘best-practice’ PFM tools can overwhelm government systems rather than strengthen them. In Pacific Island Countries (PICs), including Tuvalu, PFM reforms have shown mixed results, achieving gains in areas like budgeting and accounting, yet struggling in procurement, revenue forecasting, and audits due to insufficient capacity and political commitment (IMF, 2006). The simplification of these methods can improve PFM systems, structures and processes.

On Niutao, traditional local governance is structured around the *Falekaupule* (council of elders) and the communal *maneapa*, which rely on consensus and habit rather than individualized accountability. Thus, externally imposed PFM systems, which is emphasizing standardized

or coins as the first form of monies for exchange by the Bank of England instead of cowrie shells (see Figure 5.7).

During World War II, American forces used Tuvalu (especially Funafuti) as a strategic base, which temporarily brought infrastructure development and increased contact with the outside world. However, post-war development remained slow. The cultural and administrative differences between the Gilbertese and Ellice Islanders eventually led to growing Ellice dissatisfaction with the GEIC arrangement (Paeniu, 1995; Macdonald, *Cinderellas of the Empire*, 1982). This culminated in a 1974 referendum in which the Ellice Islanders voted overwhelmingly to separate from the colony. The Ellice Islands officially became Tuvalu in 1978, achieving full independence while maintaining a constitutional monarchy within the Commonwealth, with Queen Elizabeth II as Head of State.

The prolonged period of British colonial rule in Tuvalu - first as part of the British Western Pacific Territories (1892–1916) and later within the Gilbert and Ellice Islands Colony (GEIC) until 1975 left the islands economically underdeveloped and politically sidelined in decision-making processes (Macdonald, 1982). These experiences fostered a profound wariness toward Western governance models and economic philosophies. In the aftermath of independence (1978), Tuvaluans placed great value on reaffirming their cultural traditions and local self-governance which have seen, for example, in the constitutional amendments of 1986 that underscored community values over individual Western-style entitlements (Kofe & Marinaccio, 2023).

This historical backdrop has shaped a collective form of ‘loss aversion,’ where any external proposal, especially those from Western countries is met with scepticism. It reflects a fear that embracing outside frameworks may erode traditional authority structures (like the *Falekaupule/Kaupule* councils) and undermine national identity (Larmour, 2005; Macdonald, 1982; Taafaki, Tuvalu, 2007). In essence, Tuvalu’s colonial legacy didn’t just leave structural scars, but also it seeded a deeply ingrained protective instinct against cultural or political losses, regardless of potential short-term economic gains from modern approaches to growth and development sustainability.

Simplicity Bias

The simplicity bias is a preference of people for simple explanations, ideas or solutions over complex ones. Preferring simpler economic models, Brian Albrecht (2021) suggests that

mainstream economists often favour frameworks where markets function smoothly such as perfectly competitive models over those that explicitly model market breakdowns, like those characterizing Tuvalu's market failures (Albrecht, 2021). Jon Steinsson (2021) notes that this 'simplicity bias' can result in models that systematically leave out vital aspects of real-world complexity and realities in Tuvalu. Of course, no model captures everything. Yet Albrecht (2021) warns that relying on an oversimplified benchmark such as applying indicators from developed Western economies to a struggling market system like Tuvalu is misguided preconception analysis and can lead researchers astray.

The simplicity of life in Pacific Island communities reflects a deep-rooted belief in living in harmony with nature. This is another significant bias of many elders in Tuvalu including Niutao Island (Nia, 2021). Community members engage in sustainable resource management by fishing only when necessary, cultivating small gardens, and relying on forest and marine ecosystems to meet their essential needs compare to modern lifestyle of working from 8am to 5pm (Niuatui, 1991; Nunn et al., 2023; Iese, et al., 2021). The lifestyle was made possible because of land tenure systems are both collective and private, with most Tuvaluans inheriting land from their ancestors. This arrangement ensures widespread access to land and sea resources, enabling communities to maintain subsistence livelihoods. While cash income is used to purchase imported goods and services, subsistence activities serve as a critical 'social safety net,' particularly during periods of economic hardship or global food price shocks.

Comfort bias, a form of simplicity bias, often discourages community leaders from engaging in English-speaking settings or interpreting written financial reports. Instead, they tend to rely on verbal communication, especially when interacting with 'outsiders'- typically referring to non-Tuvaluans or foreign financial experts. Informants in Government of Tuvalu departments reported that they to express their opinions in meetings with public financial management experts from abroad. This discomfort was particularly noticeable during virtual conferences or Zoom calls, where unfamiliar faces intensified their reluctance to participate.

Another example of simplicity bias in Tuvalu is the continued reliance on the 'barter system' over formal market mechanisms. In many island communities, economic life remains rooted in traditional, subsistence-based exchanges, where goods and services are traded without money and low economic volume (Kennedy D. G., 1953; Knapman, Ponton, & Hunt, 2002). In bartering, there is no fixed value but goods and services can be negotiable their prices. This cultural familiarity with barter is rather limited to domestic trade only than the complexity of a

monetized free market shapes, which may shape small businesses and households’ operations in a complex manner as it is today.

This simplicity bias significantly affects public financial management, as it limits the scope of revenue collection, weakens the effectiveness of monetary policy, and reduces financial data available for planning and forecasting as island communities engage in barter system (Helbling, 2024). It also challenges efforts to formalize the economy (i.e., market system), introduce taxation systems, and expand financial inclusion based on price, all of which are vital for sustainable fiscal governance and global trade.

Feature	Market System	Barter System
Medium of Exchange	Money	Direct goods/services
Efficiency	High (transactions)	Low (time-consuming)
Valuation of Goods	Based on price	Negotiable, no fixed value
Global Trade	Easy and widespread	Limited to local exchanges

Figure 5.10 Market versus Barter System. Source: Author’s Analysis (2024).

Simplicity bias in Tuvalu affects both federal and local governments by encouraging reliance on familiar, low-effort practices and resistance to complexity. At the federal level, this leads to dependence on foreign consultants, avoidance of structural reforms, and underutilization of modern financial tools. Locally, *Falekaupule* and *Kaupule* often prefer verbal communication over written records, favour traditional customs over formal regulations, and maintain subsistence or barter-based economies. These behaviours contribute to weak institutional capacity, gaps in accountability, and delays in adopting modern public financial management practices, ultimately hindering transparency and sustainable development.

Familiar Tendencies

As discussed in our previous points, familiarity tendency is referred to tendency for people to prefer things, people or options they are familiar with even when unfamiliar options might be better. This bias can strongly influence decision-making in finance, consumption and risk management including governance (Kahneman & Tversky, 1979). Some of the familiar tendencies found in Tuvalu are product choices and favourism over political representatives.

In Tuvalu, many everyday product choices made by individuals and communities reflect cultural norms, subsistence lifestyles, and a preference for simplicity, which often conflict with the principles of effective public financial management. For instance, the widespread use of barter and informal exchange such as trading fish, coconuts, or handicrafts, means that a significant portion of economic activity goes unrecorded and untaxed. This weakens the government's ability to generate local revenue and accurately monitor economic performance. Similarly, while imported foods like rice and canned meat are widely consumed, they contribute to a growing trade imbalance and increase dependence on imported goods, straining the national budget and diverting resources from local agricultural development.

Moreover, many Tuvaluans prefer informal financial practices, such as saving cash at home or using community-based savings groups, over formal banking services. This limits the government's capacity to promote financial inclusion and develop reliable monetary or fiscal policies. Public services also face challenges: some households avoid paying utility fees and instead rely on traditional practices like using wells or the ocean, which undermines cost recovery for basic infrastructure. Cultural and religious commitments, such as contributions to church functions or traditional ceremonies, often take precedence over financial obligations like tax payments or school expenses. These spending patterns reduce public revenue and limit the effectiveness of government investments in education, health, and community development. As a result, these deeply rooted choices, while meaningful in a local context - create systemic barriers to sustainable and transparent financial management in Tuvalu.

The role of kinship plays a powerful and often decisive role in the re-election of incumbent politicians in Tuvalu. In small island societies where social networks are deeply rooted in family ties, clan affiliations, and extended kin groups, political loyalty is frequently shaped not by policy performance or national vision, but by relational obligations and social identity. Voters often support candidates who are their relatives or who belong to the same lineage or community subgroup, perceiving their success as a collective achievement of the family or island group.

This kin-based political culture reinforces the incumbency advantage, as once elected, a politician can use their position to 'distribute favours, resources, or government jobs' to kin members (Larmour, 1998; Larmour, 2012), further strengthening their base of support. It also discourages opposition from within the same kin network, as challenging an incumbent relative may be seen as disloyal or divisive (Eriksen, 2017; Gunson, 1997). In this way, kinship

functions as a social mechanism for political continuity, reducing the space for alternative candidates and ideas, especially from outside the dominant kin groups.

However, while kinship may foster trust and social cohesion, it can also undermine meritocracy, transparency, and accountability, as political decisions may be influenced more by family loyalty than by public interest. It can entrench elite families in power and limit political competition, contributing to governance practices that prioritize familial obligations over institutional development or national priorities.

Communal Accountability and Financial Accountability

One fundamental factor contributing to weak financial oversight in Tuvalu is the influence of ‘cognitive institutions’- including kinship networks, closely connected communities, and church organisations, which often take precedence over formal accountability mechanisms, thereby shaping how public funds are managed and scrutinised. According to Tala Simeti and Allan Mua Illingworth (2023) in their analysis of Tuvalu’s accountability ecosystem, accountability is rooted not only in service (*tautua*) but also in leadership, personal support, and relational strength (*va*), a combination that reflects core values of respect and integrity (i.e., *ava mote fai mea tonu*), underpinning everyday practices in Tuvalu (Simeti & Illingworth, 2023). This culturally embedded approach poses challenges for accountability, as decisions are often guided more by relationships than by strict governance standards.

The interplay between formal regulative institutions and informal cognitive institutions in Tuvalu such as kinship networks, communal hierarchies, church authorities, *Falekaupule*, and *Kaupule* - shapes the complexity and limits of accountability, prompting the critical question: *Who is accountable for what, and at which level - local or national?* According to Simeti and Illingworth (2023), *Falekaupule*, along with *Kaupule* and church leaders, exert substantial influence on policy decisions at the community level, effectively blurring formal and informal oversight boundaries (Simeti & Illingworth, 2023). At the national or federal level, political figures rely on the support and endorsement of these local leaders to secure popular legitimacy; they are likewise held to account by communities through these village-level mechanisms. This dynamic underscore how communal accountability that is rooted in traditional relationships and structures -functions as a primary mechanism for financial and ‘community-based’ oversight in Tuvalu.

Financial Accountability

In 2024, Reverend Alamatini Lusama of the Church of Tuvalu (i.e., Ekalesia Kelisiano Tuvalu) said in building the Accountable Civil Society Training and Workshops in Tuvalu (UNDP, 2024):

“There’s a critical need to address public financial management. We’ve seen too many projects fail due to misuse of funds. Donors get discouraged, and ultimately, communities suffer. When proper processes aren’t followed, there are no real benefits for the people. This workshop is a crucial step toward ensuring accountability and delivering positive outcomes for Tuvalu.”

The Vaka Pasifika (Te Vaka Pasefika) Project is a collaborative initiative supported by the European Union and led by UNDP, in partnership with PIANGO (Pacific Islands Association of NGOs) and La Trobe University. It aims to revitalize public financial management and strengthen Supreme Audit Institutions across the Pacific by embedding locally relevant best practices and reinforcing the principle of “the Pacific Way” as central to good governance and efficient resource management (EU, 2023; UNDP, 2024). H.E. Sujiro Seam, the EU Ambassador to the Pacific, enthusiastically endorsed the project, highlighting its commitment to citizen-focused oversight and resource stewardship. Additionally, the initiative supports modern transparency and accountability through training programs that send heads of government divisions overseas, including Fiji, to learn advanced PFM tools and systems tailored to regional contexts.

In the modified Federal Government system for Tuvalu, which adopted from the Westminster model governance, financial transparency and accountability are guided by many formal policies, laws and regulations such as the Tuvalu Public Finance Acts and Tuvalu Government Budget Manual that were passed by the Federal Government to prevent financial fraud and abuse (Government of Tuvalu, 2017). In addition, Supreme Audit Institutions (SAIs) such as the Tuvalu Auditor General, the Attorney General, and the Ombudsman offices are government agencies that are responsible for auditing public finances and monitoring financial operations to ensure compliance. Oversight committees such as the Public Account Committees, Budget Committees and external institutions such as the IMF and World Bank also provide oversight and technical assistance to assess institutional mechanisms and plans for actions. Yet, recent Auditor General reports have pointed out that Tuvalu’s financial statements have not met international standards (ADB, 2021; Government of Tuvalu, 2019).

The Pacific Association of Supreme Audit Institutions (PASAI) plays a vital role alongside Pacific nations, including Tuvalu, in promoting transparency, accountability, and the efficient

management of public resources. As outlined in its Charter, PASAI aids member Supreme Audit Institutions (SAIs) in enhancing audit quality to internationally recognized standards (PASAI, 2024). Its mission encompasses several strategic objectives:

- strengthening cooperation and coordination among SAIs;
- advocating for governance principles like transparency and SAI independence;
- building sustained public-sector auditing capacities through knowledge sharing;
- assisting member SAIs in performing audit functions - often via cooperative audits;
- acting as a regional working group under INTOSAI;
- and fostering collaboration with other regional SAIs, INTOSAI groups, and stakeholders in public governance. Through its long-term strategy for 2024–2034.

PASAI emphasises peer-to-peer mentoring, legislative advocacy, performance auditing, and quality assurance to support Supreme Audit Institutions (SAIs) in delivering timely, high-quality audits that enhance public accountability across the Pacific. However, improvements in financial accountability have been modest the 2023 Accountability and Transparency Report acknowledges strides in audit quality and PFM systems but notes that deeper progress on financial oversight remains limited (PASAI, 2024). Strengthening accountability mechanisms, especially through targeted reforms in public financial management systems, structures, and processes could meaningfully elevate PASAI’s work in this area.

Various issues have impeded PASAI’s efforts in Tuvalu, including capacity shortfalls and staff turnover, audit delays, incomplete reform implementation, and persistent political and cultural constraints. While PASAI’s interventions through legal empowerment, technical capacity building, and peer support have been significant, actual improvements in financial accountability have been modest. Core problems remain - insufficient independence and autonomy of the Supreme Audit Institution (SAI), internal control weaknesses, failure to fully implement audit recommendations, and enduring political barriers (ADB, 2015; PASAI, 2024; Simeti & Illingworth, 2023). Moreover, kinship-based and communal networks continue to influence staff recruitment and operational decisions, a challenge commonly observed across the Pacific region.

Perhaps other issues such as capacity shortfall and staff turnover, delayed audit execution, insufficient implementation of reforms, and political and cultural constraints have been the problems. Most of PASAI’s efforts have focused on legal empowerment, technical-capacity and peer support, actual improvements in Tuvalu’s financial accountability have been related

to SAI independence and autonomy, internal control challenges, incompleteness of audit recommendations, and political barriers. Sometime kinship-based and communal networks exerting undue influence over staff recruitment and operations. This is a common problem in the Pacific.

As highlighted in Chapter 3 on regulatory institutions, Tuvalu continues to face challenges in combating corruption and resource mismanagement due to weak enforcement mechanisms. Key bodies - such as the Ombudsman, media, and police - lack sufficient capacity to impose sanctions, and the tight-knit nature of communities often impedes public scrutiny and formal accountability processes. Additionally, the country's longstanding oral culture means that systematic financial record-keeping and formal accounting practices remain underdeveloped, further weakening transparency and hindering effective oversight.

Communal Accountability

In contrast to Western systems above, Tuvalu's traditional governance structures have historically delivered transparency and accountability through a 'community-based approach' or community (Baker, 1983; Goldman, 1970). Central to this communal accountability are the roles of cognitive institutions such as *Falekaupule* (Council of elders) and the *maneapa* system including kinship and churches, which have long served as platforms for communal decision-making and the enforcement of collective responsibility, social offences, crimes, or misconduct.

The leadership and executive functions within the *Falekaupule*, which functioned as the 'highest local decision-making authority' - overseeing community projects, local regulations, and land management is key to understand communal accountability. However, many of these responsibilities have gradually shifted to the central government, especially in areas such as policy implementation and financial planning, it is key to re-evaluate their effectiveness. This shift of local accountability to federal accountability have seen as weaken PFM systems, therefore moving accountability back to *Falekaupule* and the *maneapa* through communal setting can improve PFM.

Despite this shift, the underlying political authority and cultural legitimacy of the traditional system remain deeply rooted. Nevertheless, these traditional leaders often lack the technical skills and institutional capacity required for modern public financial management - especially

in budgeting, procurement, and financial reporting. While the formal influence of traditional leaders is diminishing, their capacity to uphold accountability and social transparency within their communities still persists in culturally embedded forms.

Communal accountability is a subset of social accountability, where citizens actively engage in monitoring and overseeing the performance of public and private institutions. It enables stakeholders to participate in resource allocation, decision-making, and budget processes (Fox, 2015). Three key features of communal accountability that can bolster financial oversight are collective scrutiny, consensus-based authority, and social enforcement, drawing from the frameworks of Ostrom (2000), Paeniu (1995), and Goldsmith (2005). These traditional mechanisms can compensate for the absence or weakness of formal governance structures, fostering more inclusive civic engagement.

In the 1860s, missionaries from the London Missionary Society (LMS) began promoting communal accountability in Tuvalu by converting local chiefs and elders to Christianity. With support from traditional leaders, they introduced Christian principles such as truth, freedom, love, equality, forgiveness, peacemaking, and generosity (Paeniu, 1995). These ideals were enforced through customary penalties and monetary fines for offences like alcohol consumption and failing to attend church services (Munro & Goldsmith, 1987). The LMS's influence extended to displacing traditional chiefly authority and integrating church leaders into community decision-making processes. This fusion of Christian ethics with local governance practices has endured, shaping participatory communal accountability on many islands. As such, leveraging this traditional framework could be an effective approach to enhancing accountability.

A *maneapa* is an open-side building with a high roof, traditionally constructed using local materials such as coconut wood and pandanus leaves (see Figure 5.9). Its designs allow for natural ventilation, making it suitable for Tuvalu's tropical weather. The structure is versatile, accommodating various community needs – ceremonial events, traditional dances, and community discussions including land disputes (Macdonald, 1982; Paeniu, 1995; Taafaki, Tuvalu, 2009). Beside disputes, the role of the *maneapa* goes beyond resources ownership and endless social issues, governance, cultural, justice and equity, kinship and religion and sustaining economic growth. It links all aspects of the community activities – social, political and economics.

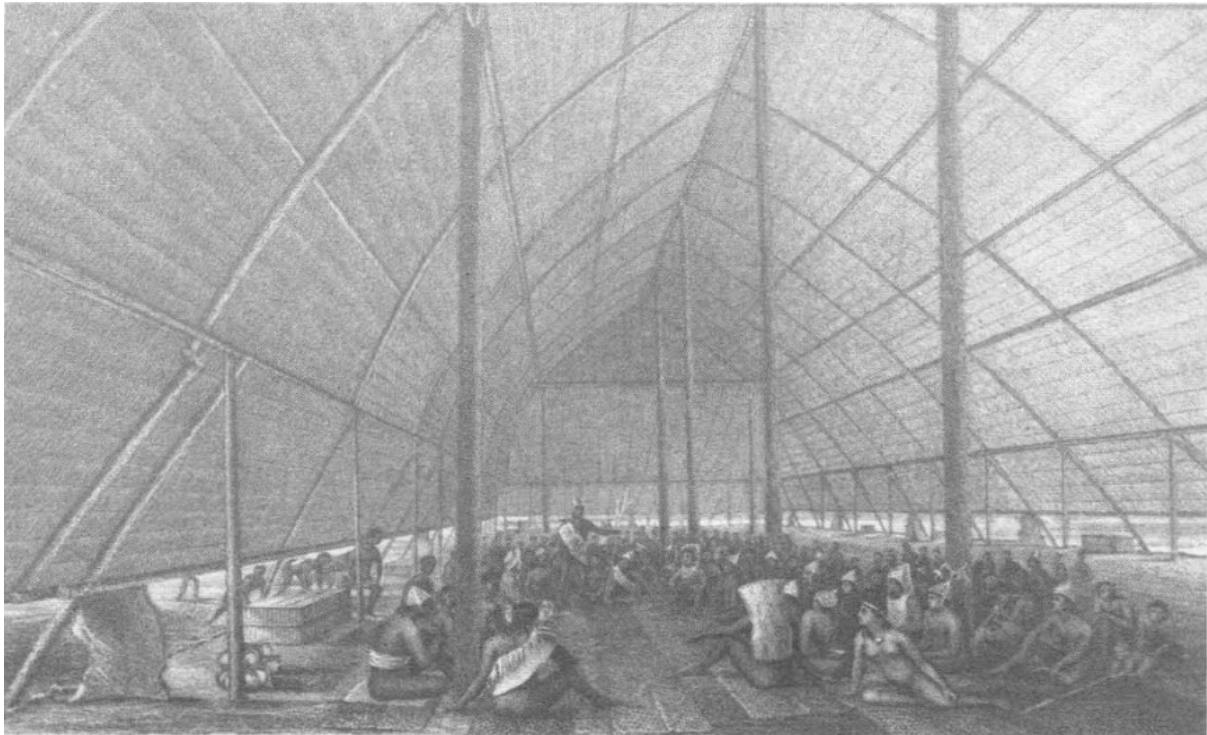


Figure 5.11 *Maneapa* Traditional Structure in Kiribati. Source: Maude (1989).

Many island communities in Tuvalu have traditionally gathered at the *maneapa*, the central meeting place for collective decision-making and social cohesion. The Paramount Chief and Island elders often initiate and oversee development projects and economic activities through discussions held in the *maneapa*. In recent years, this space has also been used to formulate Island Strategic Plans (ISPs), reflecting its evolving role in community governance. Moreover, the *maneapa* serves as a traditional classroom, where intergenerational knowledge - cultural practices, values, and oral histories is transmitted. In the case of Niutao, the Strategic Plan titled *Lagai Fakaola Fenua I* outlines below how the community envisions and implements its sustainable development goals (Niutao Island, 2016):

- incorporation of climate change mitigation and adaptation in agricultural production,
- three years Kaupule Capital Investment Plan (CIP) for budgetary supports, and
- the role of Niutao diaspora (*Te Motuokai*) in development of the Island community.

Despite the precarious existence of the barrenness of Island conditions and environments, Tuvaluans learned to cope and involved their culture in harmony with hard environments.



Figure 5.12 Modern Maneapa Structure of the Niutao Island community. Source: Simon Tuilagi (2022).

Although *maneapa* structures have been modernized for enhanced durability, their fundamental functions remain consistent. Today, the *maneapa* continues to ensure the equitable allocation, management, and distribution of land and related resources, guided by customary law through open community deliberation. These tasks are overseen by the *Kaupule* - elected island councils established under the Falekaupule Act of 1997 (the executive arm of the traditional Falekaupule assembly). Empowered by law, the *Kaupule* regulates land legislation, rental agreements, and usage rights, but always in collaboration with citizens during *maneapa* meetings. This blend of legal authority and community consensus from both cognitive and formal institutions - plays a vital role in promoting communal accountability.

The final dimension of communal accountability in Tuvalu lies in the role of *kaiga*, or kinship. Villages and islands in Tuvalu are traditionally structured into kin-based sections - typically two per island rooted in shared ancestry. These divisions coordinate collective responsibilities such as fishing, resource sharing, and community projects. Kinship also plays a vital role in organizing communal events including fundraising, shared meals, and the exchange of gifts for

weddings, funerals, and educational milestones. Through these practices, kinship networks serve as a foundational mechanism for reinforcing social responsibility and communal accountability.

Aspect	Financial Accountability	Communal Accountability
Structure	Based on laws, regulations, and formal institutions	Based on oral traditions, communal consensus, and elder's authority
Decision-Makers	Government officials, elected representatives, and financial institutions	Elders, chiefs, and religious leaders guide decisions collectively
Process	Follows a bureaucratic process with documented records	Discussions in the Maneapa (Traditional meeting house) with informal records
Financial Records	Budget, expenditures, and reports are documented and publicly available	Financial management is verbal and less documented.
Record-Keeping	Information is stored in written reports, digital systems, and government archives	Information is mainly oral, with minimal documentation.
Enforcement Body	Police, courts, anti-corruption commissions ensure compliance	Elders and community leaders enforce rules through social pressure
Punishments for Violations	Legal actions such as fines, court trials, and jail sentences	Traditional punishments such as public shaming or exclusion from community events
Oversight Mechanisms	Auditing agencies and anti-corruption bodies monitor funds	Community elders monitor and manage resources through trust.
Accountability Measures	Officials face legal consequences for mismanagement (fines, removal, imprisonment).	Social accountability through public shaming, fines, and communal labour.
Public Involvement	Citizens participate through elections, public consultations, and social media engagement	Decisions are made through community gatherings in the <i>maneapa</i> , where all voices are heard.
Trust & Transparency	Trust is built through public reporting and legal accountability	Trust is based on long-standing relationships and respect for elders.

Communication	Uses formal press releases, government websites and reports	Relies on word-of-mouth, meetings and traditional storytelling.
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Figure 5.13 Modern Decision Making versus Maneapa System. Source: Author’s Analysis (2024).

The above Figure 5.11 compares the big differences between financial and communal accountability. Knowing how financial and communal accountability principles and mechanisms build a common ground to strengthen and enforce formal systems, structures and processes can enhance the budgetary process and may lead to resilient financial and economic system.

Conclusion

Public financial management in Tuvalu has been significantly weakened by institutional memory challenges, rooted in country’s history and past experiences. A reliance driven reforms from aid donors’ institutions like the ADB, IMF, or World Bank has often resulted in superficial changes that fail to be embedded in local cognitive institutions – island communities, churches, and kinships – limited capacity and poor alignment with modern PFM systems, structures and processes.

Concurrently, high staff turnover – exacerbated by frequent changes in personnel and dependence on short-term advisors from developed countries, which led to the erosion of indigenous/traditional knowledge and internal oversight that key to sustainability of resilient traditional systems, structures and processes. The habits of behavioural biases – loss aversion, simplicity bias and familiar tendencies by public managers in decision-makings that often-required modern PFM practices create a separation and confusion on what is the best approach to improve the current PFM situation in Tuvalu.

With the strong presence of Tuvalu’s institutional memory, collective knowledge, and behavioural biases in cognitive institutions, which are deeply rooted in oral traditions, communal governance, and social accountability, overcoming financial risks is extremely difficult. Transparency and accountability in Tuvalu are socially enforced, where individuals are held responsible through public shaming, communal labour, or exclusion from community activities rather than formal legal penalties. Trust is built on long-standing relationships rather than written records or bureaucratic oversight.

The different operations of modern and market-driven systems rely heavily formal structures and processes that are documented policies, legal frameworks, and financial accountability is currently absent in Tuvalu. Public participation occurs through elections, consultations, and civic engagement, with compliance enforced by courts, anti-corruption agencies, and law enforcement have not strengthened by modern mechanisms due to the lack of trust in modern structures and their legitimacy. Tuvaluans have great biased toward familiar solutions, barter system, and oral traditions that are not easily adapted to current PFM policies.

To improve PFM, government policies must recognize and integrate the value of barter systems as part of the broader economic landscape, ensuring that non-cash economic activities are reflected in local development plans, resource allocation, and fiscal strategies. By acknowledging the real economic contributions of barter systems, the state can design more inclusive budgets and policies that support both formal and informal livelihoods, ultimately strengthening national resilience.

While modern system, grounded in formal rules, external audits, and international standards like the Public Expenditure and Financial Accountability framework (PEFA), emphasizes procedural accountability, legal compliance, and fiscal reporting (World Bank, 2013), financial accountability and transparency can be significantly enhanced in Tuvalu through strong traditional *maneapa* system. Communal accountability through the *maneapa* system, where economic participants - political leaders and financial managers - rely on collective dialogue, social accountability, and communal trust, where village elders and community members openly discuss resource use and make decisions through consensus (Lal & Fortune, 2000).

The use of the *maneapa* for enforcement and consequences can be significantly improved in Tuvalu by bridging the strengths of the modern legal system with the traditional enforcement mechanisms of the *maneapa*, creating a complementary model that enhances public financial management. Because the *maneapa* system relies on social enforcement: decisions are upheld through collective norms, communal sanctions, and reputation-based accountability, where the loss of community respect can carry significant informal penalties (Lal & Fortune, 2000).

Integrating the formal enforcement tools of the modern system with the informal, socially embedded consequences of the *maneapa* can create a more robust and culturally appropriate PFM framework. For example, when cases of public fund misuse arise, involving the *maneapa* in preliminary reviews or community-based hearings can apply immediate social pressure,

reinforcing ethical standards at the local level before or alongside formal legal procedures (Iati, 2011). This dual-track approach ensures that enforcement is not only procedural but also relational, amplifying the deterrent effect by combining legal risks with social disapproval.

While the modern system ensures compliance with national laws and international benchmarks, the *maneapa* reinforces community-level oversight, making sure that public resources address local needs and that leaders are socially answerable to their communities (Paeniu, 1995; Tafaaki, 2004). When communities have access to clear, understandable financial information and channels to question or challenge public spending, trust in both traditional and state institutions increases. This enhanced trust reduces the risks of corruption, mismanagement, and political capture, making PFM reforms more durable and effective. In sum, by combining the procedural rigor of the modern state with the relational accountability of the *maneapa*, Tuvalu can build a more transparent, accountable, and culturally resonant financial governance system.

The next few chapters (6-8) will explore how regulative and formal systems, structures, and processes can effectively intertwined with cognitive institutions.

**PART III – RETHINKING OF HOW TO MUTUALLY INTEGRATE
ALL ELEMENTS OF INSTITUTIONS TO PUBLIC FINANCIAL
MANAGEMENT**

CHAPTER 6. PUBLIC EXPENDITURE AND FINANCIAL ACCOUNTABILITY IN TUVALU

Public money ought to be touched with the most scrupulous consciousness of honour -
Thomas Paine (1795)

Introduction

Although the previous chapter on cognitive institutions demonstrated the vast difference between modern and traditional management systems, the method for measuring is designed the Europe Way, not the Pacific Way. The Public Expenditure and Financial Accountability (PEFA) approach is the most recognized method to measure the effectiveness of public financial management. In 2001, the European Commission, IMF, World Bank and the governments of France, Norway, Switzerland, and the United Kingdom (UK) adopted the PEFA framework to assess the strengths and weaknesses of PFM.

The goals of the PEFA framework is to strengthen the capacities that assess the status of country PFM systems and develop a practical sequence of reform that: encourages country ownership, reduces the transaction costs to countries, enhances donor harmonization, allows monitoring of progress of country PFM performance over time, better addresses developmental and fiduciary concerns, and leads to improvements in the impacts of public reforms (PEFA, 2023).

Facing existential threats from rising sea levels and climate change, Tuvalu's future hinges on climate risks that represent a major economic challenge that can prevent fiscal discipline and the achievement of a strong financial position. The climate threat supports Tuvalu's global advocacy for climate justice and underscores the need for climate finance and adaptation strategies. Cyclone frequency exposes Tuvalu to many ecological risks and also financial risks. Extreme wind speeds, extreme precipitation and storm surges have caused significant economic and social damages to the small vulnerable economy. The recent Cyclone Pam's cost was estimated to whoop US\$92 million for rebuilding after the cyclone destruction that damaged food crops, vegetation, water security, homes, infrastructures and other citizens' properties (Taeia, 2021).

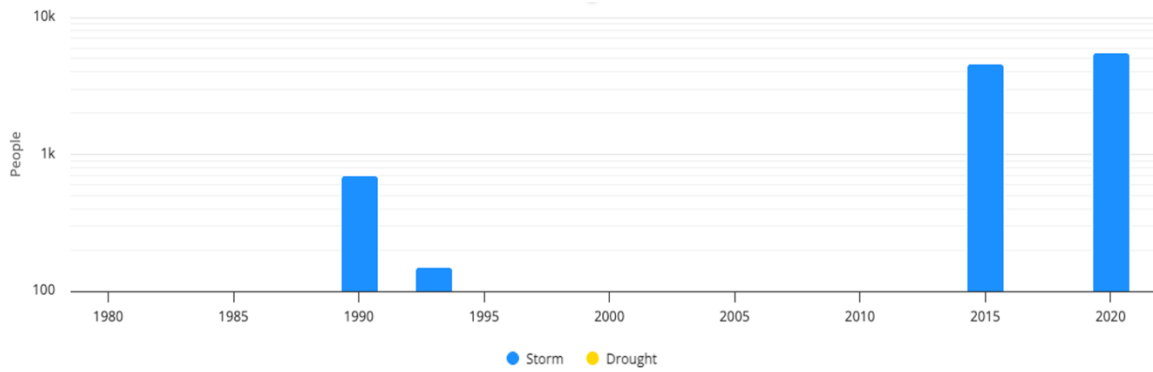


Figure 6.1 People affected by Natural Hazards (1980-2020). Source: SPREP (2023).

According to Figure 6.1, the number of people affected by storms spiked dramatically in 2015 and 2020, each time exceeding 10,000 people. For a small nation like Tuvalu, where the total population is around 11,000, this implies nearly the entire population was impacted. These events likely triggered emergency relief efforts, rehabilitation costs, and long-term adaptation investments, such as elevating infrastructure and relocating communities. Such large-scale events strain public finances, especially in a country heavily reliant on foreign aid and with limited domestic revenue.

Figure 6.1 above shows that storms account for the vast majority of natural hazard occurrences in Tuvalu over the 40-year period. Storms are often accompanied by ‘coastal flooding,’ infrastructure damage, and displacement (SPREP, 2024). These recurring climate events require frequent public spending on emergency response, rebuilding public infrastructure (such as roads, schools, and seawalls), and disaster preparedness, leading to ‘unplanned fiscal pressure’ and repeated reallocations in the national budget (Devereux, 2002).

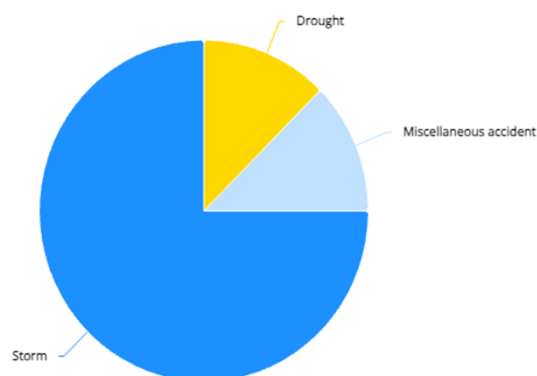


Figure 6.2 Average Annual Cyclone Frequency and Occurrence (1980 -2020). Source: World Bank (2024).

Figure 6.2 also shows smaller but recurring events such as 12.5% of droughts and 12.5% of storm surges and high wind speeds causing tremendous costs on national budgets. However, cyclones expose Tuvalu to high wind speeds, extreme precipitation, and storm surges all of which cause significant economic and social damage which often resulted more than 25% of Tuvalu's national gross domestic product (GDP). Although they may not cause mass displacement, these hazards still erode agricultural productivity, threaten water security, and require local adaptation measures, such as water storage systems and food aid programs. These expenditures, although not always immediate, build up over time and increase Tuvalu's structural fiscal vulnerability.

From an ecological view of the economy as a subsystem of the finite natural environment, economic activity must stay within planetary boundaries (Daly & Farley, 2011). In contrast, neoclassical economics assumes that natural resources are either infinite or substitutable and focuses on efficiency, utility maximization, and perpetual growth. This clash is highly relevant to Tuvalu, where rising sea levels, coastal erosion, and limited land resources impose strict physical constraints. An ecological approach recognizes that Tuvalu's economic sustainability is inseparable from environmental resilience, unlike the neoclassical focus on GDP growth as the primary indicator of progress.

As PEFA assessments indicated, PFM systems in Pacific Island Countries are very different from the sophisticated and comprehensive systems operating in larger, wealthier countries. The ongoing duration of capacity constraints is difficult to achieve 'good practice' standards (i.e., PFM practices) to be effectively implemented and sustained with limited financial resources. In this chapter I evaluate the effectiveness of four main PFM practices that are currently used to measure effectiveness in Tuvalu: budget management, financial controls, value management and governance and accountability.

PEFA Framework and Grading System

Since the introduction of the Public Expenditure and Financial Accountability framework, 155 countries, including Tuvalu and other small Pacific Island nations like Samoa, Tonga, and Kiribati, have participated. Bernard Jappah, the PFM Reforms Coordinator at the Ministry of Finance and Development Planning in Liberia, stated that PEFA has provided them with 'a realistic check of how we have been performing (financially) and where the areas of PFM improvement remain' (PEFA, 2023). Today, there have been over 700 PEFA assessments

conducted globally, with more than 1,000 officials trained each year and 65% of public assessments made publicly accessible.

The PEFA framework is built around seven key pillars and 31 common performance indicators used to assess public financial management systems. This section pinpoints key indicators that portray risks in Tuvalu from the perspective developed in this thesis. These pillars cover areas such as budget reliability, transparency of public finances, management of assets and liabilities, policy-based fiscal strategy and budgeting, predictability and control in budget execution, accounting and reporting, as well as external scrutiny and audit. PEFA serves as a valuable tool for governments by providing a structured way to measure and monitor PFM performance across institutions, systems, and processes. It also incorporates international standards and best practices, ensuring a comprehensive approach to strengthening PFM systems (PEFA Secretariat, 2016, p. 6).

One practical approach is to create ‘hybrid economic strategies’ that link barter activities with market-based initiatives, such as allowing community contributions in kind (e.g., labour, local produce, or traditional services) to count toward public projects or local development programs. This builds local ownership while reducing the strain on limited cash resources. Additionally, improving the ‘documentation and valuation of barter exchanges can help local governments better assess the full spectrum of economic activity, feeding into more accurate fiscal planning, taxation models, and service delivery (Godoy, 1985). Importantly, fostering dialogue between market actors, community leaders, and policymakers ensures that reforms are culturally sensitive and practically grounded, avoiding the imposition of purely Western market models that might undermine local social cohesion. In this way, Tuvalu can leverage the strengths of both systems to create a more adaptable, inclusive, and community-responsive PFM framework.

PEFA’s first pillar, budget reliability, focuses on the accuracy of aggregate expenditure outlays compared to what was originally approved in the budget documentation and fiscal reports. To assess this, a letter grading system from A to D is used. A Grade A is awarded when the aggregate expenditure outturn falls between 95% and 105% of the approved budget in at least two of the past three years. Grade B is given when the outturn is between 90% and 110%, while Grade C is assigned if it falls between 85% and 115%. Any performance outside these ranges receives a Grade D (PEFA, 2023).

PEFA's second pillar centres on the transparency of public finances and the quality of budget classification. Scoring for this area uses a letter grade system from A to D. Grade A is awarded when budget formulation, execution, and reporting are fully based on administrative, economic, and functional classifications in line with GFS/COFOG standards or use a classification system that produces consistent and comparable documentation (World Bank, 2010). Additionally, a program classification can substitute for sub-functional classification if it provides at least the same level of detailed information.

Grade B reflects budget formulation, execution, and reporting based on administrative, economic (at least at the 'Group' level of the GFS standard-three digits), and functional or sub-functional classifications, following GFS/COFOG standards or an equivalent system that ensures consistent and comparable documentation. Grade C is awarded when the budget is formulated, executed, and reported using administrative and economic classifications that align with GFS standards at a minimum of level 2 (two digits) or a comparable classification system that maintains consistency with international standards.

The third pillar focuses on the management of assets and liabilities, specifically measuring fiscal risks. Fiscal risks refer to potential threats arising from adverse macroeconomic conditions, the financial health of subnational governments or public corporations, and contingent liabilities linked to the central government's programs and activities, including those of extrabudgetary units. Additionally, fiscal risks encompass implicit and external threats, such as market failures and natural disasters.

Fiscal risks are assessed using a grading scale from A to D. Grade A is awarded when audited annual financial statements for all public corporations are published within six months after the fiscal year ends, along with a consolidated report on the financial performance of the public corporation sector issued by the central government. Grade B is given when audited financial statements for most public corporations are published within six months. Grade C applies when the government receives financial reports from most public corporations within nine months of the fiscal year's end. Grade D is assigned when performance falls short of the requirements for a Grade C (PEFA, 2023).

The fourth pillar emphasizes policy-based fiscal strategy and budgeting, focusing on macroeconomic and fiscal forecasting, which is essential for developing a sustainable fiscal strategy and ensuring greater predictability in budget allocations. Macroeconomic and fiscal

forecasting is assessed through specific indicators. Grade A rating is given when the government provides forecasts of key macroeconomic indicators, along with the underlying assumptions included in the budget documentation submitted to the legislature. These forecasts must be updated at least once a year and cover the budget year plus the following two fiscal years. Additionally, the projections must be reviewed by an independent entity separate from the one that prepared the documentation (PEFA, 2023).

Grade B assesses the government's ability to prepare forecasts of key macroeconomic indicators, along with the underlying assumptions, which are submitted to the legislature for approval. These forecasts must cover the budget year and the next two fiscal years. Grade C is assigned when the government prepares forecasts of key macroeconomic indicators for the budget year and the following two years, but without the same level of supporting detail. Grade D is given when performance falls below the standard required for a C score (PEFA, 2023).

Pillar five focuses on predictability and control in budget execution. This indicator pertains to the entities responsible for managing Federal Government revenues, including tax administration, customs administration, and the administration of social security contributions, such as provident funds. It also covers agencies that serve as regulators and holding companies for government interests in state-owned enterprises. Additionally, it encompasses the processes and procedures used to collect and monitor Federal Government revenues (PEFA, 2023).

Grade A is awarded when entities collecting the majority of revenues use multiple channels to provide payers with easy access to comprehensive and up-to-date information on key revenue obligations and rights, including, at a minimum, redress processes and procedures. Grade B is given when entities collecting most revenues provide payers with access to comprehensive and up-to-date information on the main revenue obligations and rights, including redress processes and procedures. Grade C is assigned when entities collecting the majority of revenues provide payers with access to information on key revenue obligations and rights, including redress processes and procedures. Grade D is given when performance falls below the standards required for a Grade C score (PEFA, 2023).

The sixth pillar focuses on accounting and reporting, with an emphasis on the integrity of financial data, in-year budget reports, and annual financial reports. Financial data integrity involves assessing treasury bank accounts, suspense accounts, and advance accounts. Regular monitoring of these accounts helps strengthen the reliability of financial data, contributing to

strong internal controls. One of the most effective methods for ensuring data reliability is reconciliation, which involves identifying and resolving any discrepancies between the government's records and its bank account data, including the amount and nature of the mismatches (PEFA, 2023).

To assess the reliability of data integrity, Grade A is awarded when bank reconciliations for all active Federal Government bank accounts are conducted at least weekly, at both aggregate and detailed levels, typically within one week of the end of each week. Grade B is given when bank reconciliations occur at least monthly, usually within four weeks of the end of each month. Grade C is assigned when bank reconciliations take place at least quarterly, typically within eight weeks of the end of each quarter. Grade D is given when performance falls below the requirements for a Grade C score (PEFA, 2023).

The final pillar focuses on external scrutiny and audit, which includes both external audits and legislative review of audit reports. It assesses the scope and standards of external audits, the submission of audit reports to the legislature, follow-up on audit findings, and the independence of the Supreme Audit Institution. These elements are essential for ensuring accurate budget outcomes by providing assurance that the information is reliable and free from material errors that could impact the interpretation of the reports (PEFA, 2023).

To evaluate external scrutiny and audit of the budget, a scorecard ranging from Grade A to D is used. Grade A is awarded when financial reports, including revenue, expenditure, assets, and liabilities of all Federal Government entities, have been audited according to International Standards of Supreme Audit Institutions (ISSAI), an organization that was established by International Organization of Supreme Audit Institutions (INTOSAI) to guide public sector auditors in performing high-quality audits or equivalent national auditing standards for the last three completed fiscal years. These audits must identify any significant issues, as well as systemic and control risks (PEFA, 2023).

Grade B is assigned when financial reports from Federal Government entities, covering most of the total expenditure and revenue, have been audited using ISSAIs or national auditing standards during the last three completed fiscal years. These audits must identify any significant issues, as well as systemic and control risks. Grade C is given when financial reports from Federal Government entities representing the majority of total expenditures and revenues have been audited using ISSAIs or national auditing standards over the last three completed

fiscal years (INTOSAI, 2024), and the audits highlight any significant issues. Grade D is awarded when performance falls below the requirements for a Grade C score (PEFA, 2023).

PEFA Assessments

Tuvalu has gone under multiple evaluations of its public financial management systems through the PEFA framework, beginning in 2007. These reviews were completed in 2011, 2015, 2022 and a streamlined Agile assessment in 2024. However, Tuvalu has made progress in many areas such as budget preparation and reporting, the core weaknesses of institutional capacity still remained in execution, oversight, and long-term planning.



Figure 6.3 PEFA Assessments (2007- 2024). Source: Author Analysis (2024).

The 2007 PEFA assessment of Tuvalu revealed several critical shortcomings in the country’s public financial management systems. Although the full report was not publicly released, subsequent evaluations and peer reviews have outlined key issues identified during the assessment. These included significant variances between budgeted and actual expenditures, weak oversight of public enterprises that contributed to fiscal risks and inefficiencies, inadequate financial reporting and internal controls that undermined transparency and accountability, and outdated procurement regulations that negatively impacted the efficiency and effectiveness of public spending (Government of Tuvalu, 2011).

In 2011, the Asian Development Bank, through its technical assistance program, prepared a public financial management performance report and conducted a PEFA assessment of Tuvalu. The results revealed a predominance of low scores, with many indicators graded at C or D levels (ADB, 2011). Notably, under the ‘budget credibility’ indicator, actual expenditure composition exceeded the originally approved budget by more than 15% in at least one of the past three years. Additionally, there was no reliable ‘data available’ on the stock and monitoring of expenditure payment arrears over the previous two years (Tuvalu Auditor

General, 2021). The assessment also found no evidence that Tuvalu consistently met its ‘debt servicing obligations’, suggesting weaknesses in data management within the Planning and Budget Department of the Ministry of Finance (MoF) (UN, 2020; Zaman, Francisco, & Choueiri, 2018). These findings highlight serious deficiencies in Tuvalu’s financial documentation and record-keeping practices (ADB, 2011).

The comprehensiveness and transparency of Tuvalu’s budgetary process were found to be lacking, particularly in how the fiscal deficit was disclosed and managed in 2011 (see Figure 6.4). According to the ADB’s PEFA report, while the Medium-Term Fiscal Framework (MTFF) acknowledged the presence of a fiscal deficit, the budget documentation failed to outline specific strategies for addressing it. Furthermore, nine critical areas were not adequately addressed or detailed in the budget documents, indicating significant gaps in fiscal planning and public financial disclosure as demonstrated in Figure 6.4 below.

STATEMENT OF INCOME AND EXPENDITURE

For the Year Ended 31/12/2011

The accompanying notes form part of these financial statements.

	Notes	<u>2011</u> <u>Actual</u>	<u>2011</u> <u>Budget</u>	<u>2010</u> <u>Actual</u>
<u>RECURRENT INCOME</u>				
Taxation	9	6,444,401	5,861,200	5,707,408
Interest, Dividends and Rent	10	1,520,430	3,016,629	1,880,821
Fisheries Licenses		5,683,624	5,360,000	7,151,855
.TV		1,876,980	2,850,000	2,025,950
External Assistance and Grants	11	8,086,961	11,816,000	5,686,649
Other Income	12	2,693,297	2,843,810	2,495,526
TOTAL RECURRENT INCOME		26,305,692	31,747,639	24,948,209
<u>RECURRENT EXPENDITURE</u>				
Wages, Salaries, and Allowances		10,985,474	11,241,803	10,819,215
Contributions to Tuvalu National Provident Fund		955,988	985,796	906,795
Travel		1,379,164	1,116,129	1,467,260
Fuel, Electricity and Communications		2,240,792	1,771,787	2,342,599
Maintenance		1,372,896	1,201,387	1,653,825
Loan Repayments & Bank Fees		497,611	518,000	1,199,162
Grants and Subsidies (incl. Scholarships Support)	13	5,989,489	8,589,157	8,699,796
Tuvalu Medical Treatment Scheme		2,132,755	1,804,600	2,203,277
Other Expenses	14	3,654,497	5,324,334	3,725,225
Special Development Expenditures		681,280	766,179	1,105,679
TOTAL RECURRENT EXPENDITURE		29,889,946	33,319,173	34,122,833
RECURRENT SURPLUS / (DEFICIT)		(3,584,253)	(1,571,534)	(9,174,624)
<u>OTHER REVENUE AND EXPENDITURE</u>				
Unrealised Gain (Loss) on Trust Fund Investment	4	912,549		3,584,832
Unrealised Gain (Loss) on Investment in Corporations	5	(562,502)		1,444,414
Unrealised Gain (Loss) on Currency Movement (Offshore Loans)	7	47,236		1,008,296
Doubtful Debts Expense	6	355		(145,241)
TOTAL OTHER REVENUE AND EXPENDITURE		397,638		5,892,301
TOTAL SURPLUS / (DEFECIT)		(3,186,616)		(3,282,323)

Figure 6.4 Statement of Income and Expenditure. Source: Government of Tuvalu (2023).

The absence of a centralized digital archiving system further hampers coordination between ministries and delays information retrieval for audits, reporting and policy planning. Additionally, frequent staff turnover and insufficient training contribute to inconsistent record-keeping practices, weakening the reliability of financial documentation and reducing transparency in public administration (see Figure 6.5).

Budget Documentation	Yes/No
• Macroeconomic assumptions, including at least estimates of aggregate growth standard	No
• Fiscal deficit, defined according to GFS or another international recognized standard	No
• Deficit financing, describing anticipated composition	No

<ul style="list-style-type: none"> • Debt stock, including details at least for the beginning of the current year 	No
<ul style="list-style-type: none"> • Financial assets, including details at least for the beginning of the current year 	No
<ul style="list-style-type: none"> • Prior year’s budget outturn, presented in the same format as the budget proposal 	No
<ul style="list-style-type: none"> • Current year’s budget (either the revised budget or the estimated outturn), presented in the same format as the budget proposal 	No
<ul style="list-style-type: none"> • Summarize budget data for both revenue and expenditure according to the main heads of the classifications used, including data for the current and previous year 	No
<ul style="list-style-type: none"> • Explanation of budget implications of new policy initiatives, with estimates of the budgetary impact of all major revenue policy changes and/or some major changes 	No

Figure 6.5 Budget Transparency and Documentation. Source: ADB (2019).

The absence of critical components in Tuvalu’s budget documentation demonstrates a systematic issue in the country’s PFM capacity. According to PFM experts, the limited human resources and institutional capacity through understaffing and lack of specialized technical expertise in standardize budget documentation align with international norms such as ‘Government Finance Statistics (GFS) framework’ were the problems (IMF, 2014).

Based on Tuvalu’s budget ‘documentation practices’, there is a critical lack of transparency and completeness in publicly available financial information. Key components typically expected in comprehensive budget documents such as macroeconomic assumptions, fiscal deficit definitions, deficit financing strategies, and detailed data on debt stock and financial assets are notably absent. Furthermore, essential comparative data, such as prior year’s budget outturn and current year’s revised estimates, are not presented in a format aligned with the proposed budget.

The lack of summarized budget data by main classification heads and the absence of clear explanations on the fiscal implications of new policy initiatives further highlight the documentation gaps. These shortcomings significantly weaken public understanding of fiscal policy and hinder informed scrutiny and accountability in Tuvalu’s public financial management.

The analysis of Tuvalu’s public financial management practices reveals a severe lack of transparency and accountability, as evidenced by the complete absence of public access across five key areas of fiscal reporting such revenue, expense, asset, liability and equity reporting. Publication of ministerial reports and assessments is irregular. For instance, publication has been sporadic. In 2014, the Office of the Auditor General (OAG) indicated that there is always a delay on disseminating crucial financial information. For instance, OAG had publicly made audit reports from 2016 to 2021 without 2022 to 2024 reports published.

The documentation practices also challenge accessibility. Citizens do not have access to in-year budget execution reports, which prevents them from tracking how government funds are spent throughout the fiscal year. This omission undermines accountability and limits public oversight of budget implementation. Similarly, the year-end financial statements are not made publicly available, leaving a critical gap in assessing the government’s financial performance compared to its approved budget. This restricts informed public discourse and weakens trust in government reporting. The absence of publicly available external audit reports is especially concerning, as these documents provide independent assessments of financial operations. Without them, there is no assurance that identified risks or inefficiencies are being addressed.

Public Access	Yes/No
• In-year budget execution reports: the reports are routinely made available to the public through appropriate means within one month of their completion	No
• Year-end financial statements: the statements are made available to the public through appropriate means within six months of completed audit	No
• External audit reports: all reports on Federal Government consolidated operations are made available to the public through appropriate means within six months of completed audit	No
• Contract awards: award of all contracts with value above approx. USD \$100,000 equivalent are published at least quarterly through appropriate means	No
• Resources available to primary service units: information is publicized through appropriate means at least annually, or available upon request, for primary service units with national coverage in at least two sectors (such as elementary schools or primary health clinics)	No

Figure 6.6 Public Access to Information (2011-2024). Source: ADB (2019).

Additionally, contract award information especially for high-value contracts above USD\$100,000 is not published. This lack of disclosure raises serious concerns about

procurement transparency and the potential for corruption. Lastly, there is no public reporting on resources allocated to essential service units like schools or health clinics. This prevents citizens from evaluating whether basic services are being adequately and fairly funded.

In 2011, public access to financial information was highly restricted. Important documents such as in-year budget execution reports, year-end financial statements, and external audit reports were not made available to the public (ADB, 2011). Furthermore, oversight of fiscal risks from state-owned enterprises was inadequate due to the limited capacity of the Public Enterprise Reform and Monitoring Unit (PERMU), which was understaffed and unable to effectively monitor SOE spending and performance. Therefore, Tuvalu's failure to provide public access to essential fiscal documents reflects deep-rooted weaknesses in transparency and civic engagement. Addressing these issues is vital to improving public trust and the effectiveness of public financial management.

According to the ADB (2011), Tuvalu's PEFA framework demonstrates some strengths in 'policy-based budgeting,' including a well-organized budget calendar that is widely understood within the government. Policy-based budgeting is a budget approach that aligns government spending with its strategic goals, priorities, and public policies. The involvement of the Cabinet in overseeing the budget formulation process, with the Ministry of Finance setting budget ceilings and drafting the budget, has been positive. Additionally, the use of the Medium-Term Fiscal Framework alongside the annual budget offers a forward-looking view and helps identify emerging issues related to the growth and decline of the Tuvalu Trust Funds. While these are commendable efforts, the MTFE and budget allocations have not accounted for setting appropriate 'expenditure ceilings,' which remains a gap in the budgeting process.

An expenditure ceiling refers to a fixed limit on the amount of money a government can spend during a given fiscal period within a year, which is a key tool for fiscal policy to ensure that spendings stays within a sustainable level and keeps to the government priorities. Understanding the ceiling is crucial for effective budget projections and controlling spending. These ceilings can be categorized into three common areas: aggregate ceilings, Ministerial/Departmental ceilings, and Medium-Term ceilings, which are typically part of the Medium-Term Expenditure Framework and usually set for a period of 3 to 5 years. By controlling deficits, expenditure ceilings contribute to macroeconomic stability by limiting inflationary pressures and reducing debt accumulation, which is particularly important for

small island nations like Tuvalu, where fiscal management is key to economic stability (Allen, Rayess, Doherty, & Goel, 2020; World Bank, 2013; World Bank, 1998).

Tuvalu's PEFA assessment was revisited, with the overall result being classified as 'poor.' This evaluation, conducted over three years from 2017 to 2021, received technical assistance of \$700,000 from the Asian Development Bank. The assessment's objective was in line with PEFA's mission to improve public financial management practices and strengthen public service delivery, focusing on enhancing fiscal resilience and discipline (Jimenez, Shresha, Subramaniam, & Ramos-Galacgac, 2021). The evaluation assessed 27 key indicators from Tuvalu's PEFA framework baseline, but the evaluators found the results to be 'inaccurate.' They highlighted that such inaccuracies could lead to misleading conclusions and undermine the effectiveness of future assessments and reforms.

According to ADB evaluators, several issues were identified advancing the reporting and recording of transactions that need to be addressed to improve public financial management technologies and systems in Tuvalu. One key concern was that the outcome indicators could not be effectively measured when compared to the 2011 PEFA report. Previous assessments lacked specific goals for improving targets, and there was no clear indication of progress. In terms of strengthening public accounting, the 'Mind Your Own Business' (MYOB) accounting software was partially evaluated, with the technical assistance report showing that it had been completed by 5 out of 7 public accountants. However, the evaluators noted that refresher training for MYOB is necessary in the future, yet such training has not planned.

In 2021, the impacts of COVID-19 and employee turnover were identified as significant challenges to improving PFM practices in Tuvalu. A key obstacle to advancing PFM reassessment this time, particularly in accounting and recording, was the Building Code Bill for the Tuvalu Government. The project, which began in 2019, had endorsement from the Minister of Public Utilities and Infrastructure (MPUI) and the Development Coordination Committee. However, progress was delayed in 2020 due to the pandemic, as border closures prevented consultants and technical assistance from traveling to Tuvalu. The Building Code Bill was finally completed in December 2024. The impact of the Building Code Bill is closely tied to public financial management reforms, as it enhances planning and control over public funds, ensures better tracking of contractors' compliance and audits, and establishes reporting requirements for construction materials and public investments in infrastructure. By improving the management of public investments, particularly in infrastructure, the bill helps prioritize

funding for sustainable and feasible projects that can better withstand the challenges posed by rising sea levels and climate change.

The measurement of procurement and compliance in Tuvalu's PFM framework has been criticized for being too general. According to Jimenez et al. (2021), their report revealed that the procurement and compliance evaluation in Tuvalu was 'partially evaluated.' They highlighted weaknesses in the 2011 procurement and compliance assessments, noting that PFM officers had not been properly trained, and the previous evaluations failed to mention the frequency of such training sessions. Furthermore, there was no use of pre- or post-test surveys to assess whether officers retained key training materials. The report also pointed out that there was no information regarding the qualifications, capacities, and scope of operations of PFM officers. Additionally, the facilitation of budget cycles and planning performance was not clearly defined, and there was no mention of how many procurement plans were developed on an ad hoc basis (Jimenez, Shresha, Subramaniam, & Ramos-Galacgac, 2021).

Recent changes also led to the implementation of the new TechnologyOne software for public accounting. TechnologyOne Financial Management Information System is designed to streamline and 'enhance the recording' (Chan, 2003) and analysis of complex accounting and financial reporting. The software provides comprehensive solutions for managing public financial operations efficiently and transparently. It captures real-time financial data, manages accounts payable and receivable, tracks asset management, supports budgeting and forecasting, oversees procurement, handles project financials, and facilitates the reporting and analysis of revenues and expenditures. However, the lack of sufficient training in advanced information systems and software created limitations in implementation.

Why does Tuvalu have Low PEFA Scores?

In the 1760s, the British Parliament presented the first national budget at the start of the fiscal year, laying the foundation for modern fiscal transparency and governance (Webber & Wildavsky, 1986). By the 1920s, many Western nations, including several cities in the United States, had implemented budget systems to address government inefficiencies and political corruption (Flesher & Flesher, 1979). During the 1960s, the concept of performance budgeting gained prominence, particularly among OECD countries and aid donors, who regarded it as essential for improving public sector accountability and the effectiveness of foreign aid distribution (OECD, 2007).

Since gaining independence in 1978, Tuvalu has introduced formal budgeting processes, yet persistent challenges remain. Public Expenditure and Financial Accountability assessments conducted in 2007, 2011, 2015, 2022, and the Agile PEFA in 2024 have consistently pointed out deficiencies in budget credibility, financial reporting, and public access to fiscal data (ADB, 2011; Jimenez, Shresha, Subramaniam, & Ramos-Galacgac, 2021). Although recent reforms such as the introduction of the Medium-Term Fiscal Framework and the implementation of the TechnologyOne Financial Management Information System (FMIS) represent steps forward, critical components like expenditure ceilings and comprehensive budget documentation are still underdeveloped, affecting fiscal discipline and public service delivery.

Under these reassessments of public financial management, the PEFA framework is now reinventing new tools and practices to the budget planning, allocation of resources, controlling and monitoring and evaluating of budget performances for effective budget management. ‘Budget credibility’ is one of the significant concepts that was reintegrated (Allen, Hemming, & Potter, 2013). Budget credibility emphasises the essential nature of realistic revenue projection and preparation, timely execution, spending as planned, avoidance of arrears, and above all is the importance of transparency and accountability (Allen, Rayess, Doherty, & Goel, 2020). The promotion of budget credibility is the core principle for quality good governance and fiscal transparency. Strong budget credibility will lead to effective budget formulation, execution and monitoring (Visser & Erasmus, 2002).

In modern approaches, the best way to measure budget credibility is to compare budget actuals against the budgeted incomes and expenditures. This is known as the ‘variance analysis’ (AFP, 2024). The variance analysis is the process of comparing actuals and budgeted revenues and expenditures. This is a key PFM tool used to identify where, why and how budget matrices or indicators differed from the plan and what they do about it.

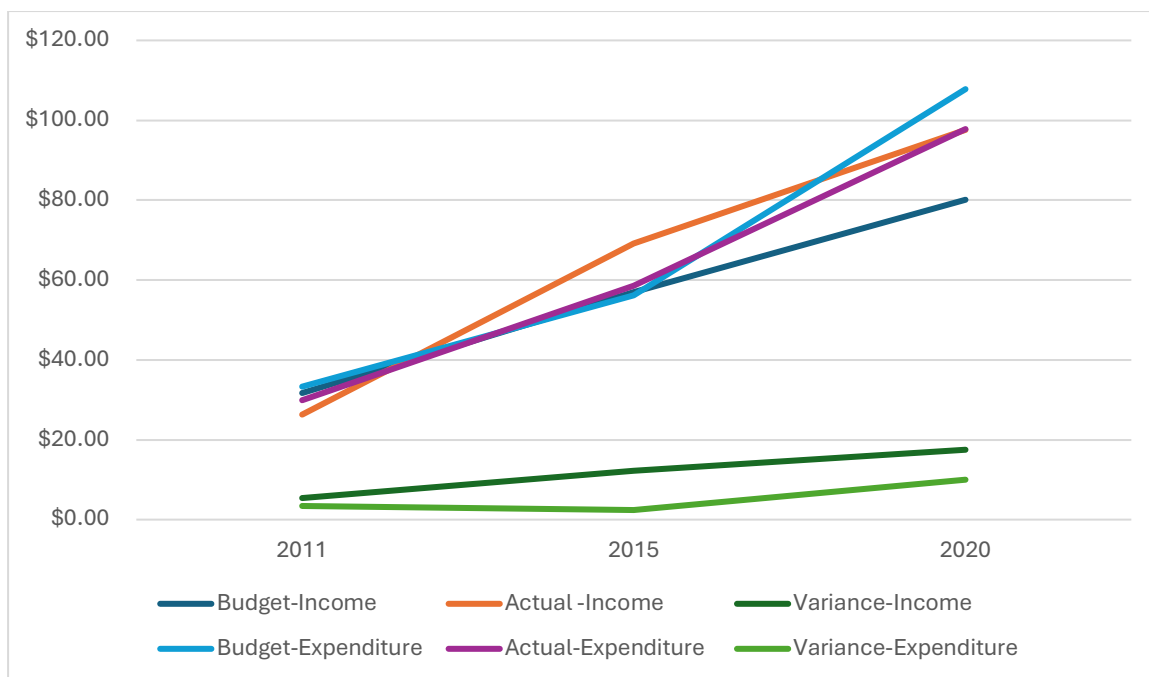


Figure 6.7 Snapshot of Variances Analysis 2011, 2015, and 2020 (in millions \$AUD).
Source: Data from Government of Tuvalu (2023).

Variance analysis is a strategic component of public financial management. It helps managers track departments and agencies spending according to plan. It supports early detection of under and overspending, which can help corrective action. These practices and analyses are ingredients for excellent review and audit of funds that ensure proper management, identify budget weaknesses, control costs, and prevent overspending – ultimately contributing to financial accountability and more accurate future planning, especially when forecasts are off (Visser & Erasmus, 2002).

Understanding favourable and unfavourable variances can tell the fiscal strength and weakness of the budget process and planning. As shown in Figure 6.7, if actual revenues exceed the budget planned amount, the variance is considered ‘favourable’ and if budget actuals fall short, it is ‘unfavourable.’ Conversely, if actual expenditures exceed what was budgeted, it results in an ‘unfavourable’ variance, while spending less than planned is ‘favourable.’ Understanding how to avoid unfavourable variances is essential to planning that may avoid future arrears and rising sovereign debt.

Figure 6.7 demonstrates favourable and unfavourable variance analysis. Between 2011 and 2020, Tuvalu's budget performance showed notable improvements in both income generation and expenditure control. In 2011, actual recurrent income fell short of the budget by \$5.4 million (i.e., unfavourable), while expenditure was AUD\$3.4 million (i.e., favourable) under

budget, reflecting an overall weak fiscal position. By 2015, revenue collection significantly improved, exceeding the budget by AUD\$12.3 million (favourable), though spending slightly overran by AUD\$2.4 million (unfavourable). In 2020, the strongest performance was recorded, with income exceeding the target by AUD\$17.5 million (favourable) and expenditure coming in \$10 million (favourable) below budget, indicating enhanced fiscal management and a healthy budget surplus (Tuvalu Auditor General, 2019; Government of Tuvalu, 2023).

Aspect	Cash Basis	Accrual Basis
Revenue	When cash is received	When revenue is earned
Expenses	When cash is paid	When expenses are incurred
Timing	Based on actual cash movement	Based on economic events

Figure 6.8 Cash Basis versus Accrual Basis Accounting System. Source: Author's Analysis (2024).

In 2020, the Auditor General reported that Tuvalu's government finances were prepared using a 'cash basis' accounting system, rather than the 'accrual basis' (see Figure 6.8) (Cavanagh, Flynn, & Moretti, 2016; IPASB, 2010). Cash basis accounting records transactions only when cash is received or paid, making it a simple and easy-to-use method suitable for systems with limited complexity. It also has fewer technical and IT requirements than accrual basis accounting. In contrast, accrual accounting records revenues and expenses when they are earned or incurred, regardless of actual cash movement. This provides a more accurate and comprehensive view of financial performance.

While the cash basis approach is straightforward, it fails to capture the full financial picture, such as outstanding bills or anticipated income. Although it ideal for a developing and small economy like Tuvalu because of it limited accounting infrastructure and low capacity, it has issues for cash management and accountability. The need to improve compliance and risk management assessments are significant steps toward building strong fiscal discipline mechanisms. Cash basis accounting also does not reflect the full financial position, as it excludes unpaid obligations and anticipated revenues (Smith, 2013). The simple goal of cash accounting is to simply track all economic activities through the use of journals and ledgers, where debits equalled the credits (i.e., 'double entry accounting') (Mattessich, 2000).

As we witnessed in Auditor General report (2020), the income and expenditure variances can be a problem for accurate forecasting. As a result, Tuvalu's financial statements may misrepresent the true fiscal position, which affects budget planning, revenue and expenditure

estimates, and leads to poor forecasting and unreliable financial models. According to Auditor General (2020), there are many unfavourable variances in many Government departments including the Finance and Economic Development, Home Affairs, Transport and Communications and so forth. According to Alistair M. Brown and Greg Tower (2002) such an approach is considered to be a ‘Western-broad model’ of cash and accrual reporting, which is different from a traditional Tuvaluan’s approach of accounting and reporting, ‘orally.’

Since ‘oral accounting’ is the common approach to accounting in Tuvalu, it has been difficult to build financial capacity for personnel due to the limited technical systems for budget execution. Oral accounting is not a new concept. It is an ancient approach that was also used in the ancient times when written systems of communication were not yet developed or widely accessible. In many ancient civilizations, such as Mesopotamia, Egypt, and Greece, oral traditions were integral part of managing finances, especially with tasks like trade, agriculture, and royal treasuries around 3000 BCE.

Before the advent of written language for Tuvalu in the late 1800s, Tuvaluans relied on oral traditions to keep track of important information on tracking ‘coconut harvests’ (Tetrapak, 2024), livestock and trade exchanges on oral accounting systems. In Niutao, the use of memory, verbal communication, and oral tracking of small financial transactions, debts and the distribution of goods were all based on oral accounting. The use of songs and chants were used to remember the records of the past. For instance, one song composed by the Niutao Island Community is known as the “Ko Muna a Taumia, Mono mo Tofikai” (Koch, 1983).

*Koa katakata Taomia, I tana kakega
Koa galegale ai Mono, I tana kaufata
Kae fakamisi Tofikai, Tena paseuseu*

Translation:

*Taomia smiles because of his agricultural skills
Mono is astounded because of his resourceful and storage abilities
Tofikai is fulfilled because of his abilities to generate wealth*

In the Niutao community, the collaboration of ancestors such as Mono, Tofikai, and Taumia, who rescued the island from an overwhelming burden of sovereign debt, is recorded as a significant event in its history. According to the elders of Niutao, these leaders faced an unprecedented debt of over £4,000 in the 1910s. Through their leadership and collaborative efforts in collecting and selling copra, they quickly raised the necessary funds to build the first church on Niutao, Tineifale (Sogivalu, 1992). This approach was not new; the community had previously faced hardships and learned that effective collaboration among groups, kin, and

women's organizations, along with the division of labour, could serve as a powerful mechanism for planning, organizing, and executing major infrastructure projects.

Maega (2023) believes that the indigenous knowledge, practices and skills of Niutao people still existed, yet it kept sacred of the Niutao kinfolks who inherited from their ancestors like Taomia, Mono and Tofikai. These ancestors and their descendants are well known for ecological management of marine and land resources in Niutao. They have mastered the life cycles of coconuts, planting of taro and *pulaka* (i.e., *cyrtospermas merkussii*), or the season for lobsters and other marine life. Their abilities to pass on these techniques to their descendants today allows the people of Niutao to depend on their indigenous knowledge in 'bad business cycles' (e.g., economic recessions) and external shocks. Thus, their variance analysis had to focus on the time estimates for 'seasonal harvesting' (Ohannes, 1978).

Therefore, there is a big contrast between traditional practices and what was presented in variance analysis above. Tuvalu's financial statements may misrepresent the government's actual fiscal condition because of incomplete and inaccurate financial data, which negatively impacts budget planning, forecasting, and the accuracy of revenue and expenditure estimates in this case. This can lead to ineffective financial models and poor resource allocation. Furthermore, this issue can lead to overspending, which leads to fiscal deficits and increased public debt. This also can lead to the reduction of funding, stricter conditions, or suspension of supports from development partners, aid donors and investors.

Relying on oral accounting compromises the precision for accurate financial forecasting and often leads to misallocations of funds, a concern frequently raised by aid donors such as the World Bank and IMF (ADB, 2012; ADB, 2014). In contrast, proponents of global standard-based budgeting reporting, especially under the International Financial Reporting Standards (IFRS) argue that formalized, written financial frameworks significantly enhance the predictive power of financial statements, improving the accuracy of earnings and cash-flow forecasts.

However, local managers challenge this view, noting that modern economists and accounting professionals have often overestimated the efficacy of free market models and that in contexts like Tuvalu, formal systems including IFRS have yielded only limited resources. This tension captures an ongoing debate whether to preserve traditional, oral-based Tuvaluan financial practices, or to transition toward financialization through globally harmonized reporting standards like IFRS. This thesis ultimately argues for a proper mixture of both modern and

traditional approaches to ensure financial frameworks that enhance the predictive power of financial outlooks and cash-flow, which is critical for Tuvalu.

Figure 6.9 demonstrates the vast differences between aspects of Tuvaluan traditional management ways against global modern financial modelling (Allen & Tommasi, 2001; Visser & Erasmus, 2002). The traditional ways of management are also defined by Niuatui (1991) as the ‘Tuvalu Way’, grounded in traditional agricultural systems that were passed down through generations, presenting a strong contrast to modern financial models (Niuatui, 1991). Tuvalu’s traditional management approach is deeply rooted in natural cycles and seasonal rhythms, as highlighted by cognitive institutions in earlier chapters (Hau'ofa, 1994). It is predictable and relatively stable, functioning at a local or community level with minimal exposure to external influences, whether from foreign interactions or global economic shocks (Iulai, 2010; Colmer & Wood, 2012). Consequently, change occurs gradually over time, and volatility remains low, typically affected only by extreme weather events, such as those resulting from climate change, rather than sudden economic disruptions.

Aspect	Traditional Management Practices	Modern Financial Modelling
Predictability	High (seasonal, nature-based)	Low (driven by many uncertain variables)
Scale	Local or community-based	Global, interconnected
Influence of Human Behaviour	Minimal	High (speculation, market sentiment)
Complexity	Low to moderate	Very High
Volatility	Low (except in extreme weather)	High (affected by markets, politics, tech, and others)
Timeframe for Impact	Long-term, gradual changes	Immediate or short-term fluctuations

Figure 6.9 Agricultural System and Modern Financial Modelling. Source: Author’s Analysis (2024).

Tuvalu’s oral accounting (i.e., traditional) is rooted in the agricultural systems that were passed on by their ancestors, whereas the Western-broad models is based off the International Financial Reporting Standards (IFRS) (Boolaky, 2012). In the modern system, financial models highlight stability, complexity, and predictability. Local scholars in Tuvalu believes that traditional Tuvalu ways of management are deeply connected to natural cycles and seasonal patterns that ties with their agricultural systems of food production and security (Goldman,

1970; Iese, et al., 2021; Munro D., 1987). The significance of traditional management systems is directly linked to ‘land tenures’ and the division of labour (Brady, 1974; Kennedy, 1953).

This comparison underscores the great challenges modern financial modelling faces for planning and forecasting, especially when compared to the stability of traditional systems. In summary, while the ‘Tuvaluan Way’ is guided by ecological cycles and natural rhythms, modern financial systems are driven by ‘business cycles’ (Burns & Mitchell, 1946) fast-moving, unstable, and heavily influenced by global forces. Joseph A. Schumpeter developed a framework for understanding the business cycle, and he refers to the natural rise and fall of economic activity over time in a market economy. It consists of four main phases: expansion (i.e., economic growth), peak (high point of growth), contraction (recession), and trough (lowest point of the cycle) (Schumpeter, 1961).

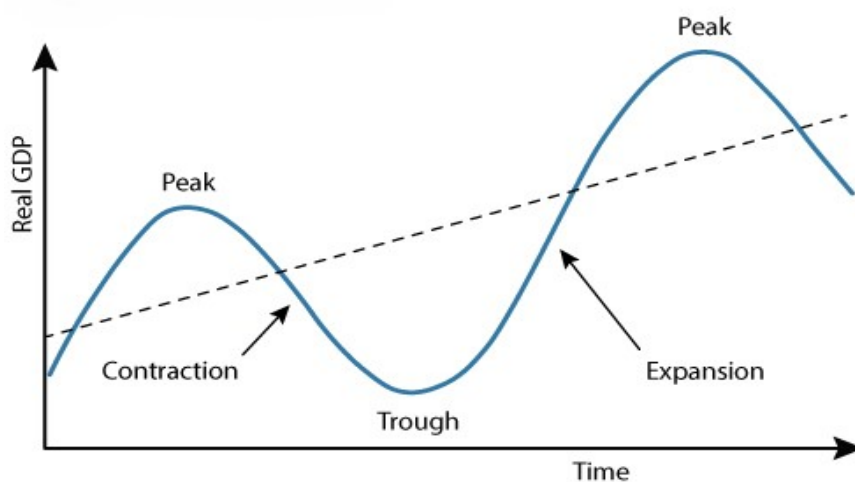


Figure 6.10 Stages of Business Cycle. Source: Wolla (2023).

The ‘expansion phase’ involves increased output, employment, investment, and consumer spending (Wolla, 2023). This is followed by the ‘peak’, where economic growth reaches its highest point, often pushing resources to full capacity. Then comes the ‘contraction phase’, or recession, marked by declining economic activity, rising unemployment, and lower consumer demand. Finally, the ‘trough’ represents the lowest point in the cycle, after which the economy begins to recover. Wolla (2023) emphasizes that these stages do not follow a fixed timeline, and their duration and intensity vary depending on external shocks, policy interventions, and global economic conditions.

In contrast, the traditional Tuvaluan way of life prior to European contact was not shaped by market fluctuations or capitalist production cycles but by seasonal and ecological rhythms. Economic life centred on subsistence farming, fishing, and communal sharing of resources. As

noted by Campbell (1989), Tuvaluan society operated through a ‘communal’ and ‘reciprocal system’, where food and labour were distributed based on kinship and customary obligations, not profit or wage incentives (Campbell, 1989). While there were cycles of abundance and scarcity driven by weather patterns, ocean currents, and crop cycles - these were addressed through ‘collective resilience’ and cultural practices such as food preservation and communal feasts (Ostrom,1990; Sogivalu,1985). There were no recessions in Tuvalu’s traditional or collective systems because these systems are not based on market dynamics, monetary exchange or capital accumulation. Tuvalu’s indigenous systems and economy operated on social obligations, shared resources, and mutual support, which focused on community survival and balance over profit and production.

The business cycle model is based on individualist, market-oriented economies, where economic performance is measured by production and monetary indicators like GDP and unemployment rates (Wolla, 2023). By contrast, the indigenous Tuvaluan economic model was rooted in ecological balance, cultural norms, and ‘community well-being’ (Campbell, 1989). As Hau'ofa (1993) observed, in Pacific Island contexts societies were not economically ‘small’ but rich in social networks, land knowledge, and traditional resource governance. Thus, while modern business cycles experience disruptive downturns and rapid growth, Tuvalu’s traditional system-maintained stability through adaptive ecological cycles and customary institutional structures, which prioritized survival, harmony, and interdependence over profit.

Mainstream Business Cycles versus Heterodox Ecological Cycles

Since the concept of a business cycle is a foreign flower, it is unfamiliar to the ears of Tuvaluan public managers. Business cycle curriculum can only be found in formal educational system in the form of college and mainstream economics. As pointed out in normative institutions and the role of modern education, not all young Tuvaluans have the money to attend college and learn how business cycles and business concepts impact the rising sovereign debt and economic development of Tuvalu. Learning these public financial management know-how and practices can be costly and not many Tuvaluans emphasise their value in living in remote and small isolation economy.

In analysing Tuvalu’s economic context, traditional economic theories must be reframed to suit its small size, cultural depth, and ‘ecological vulnerability’ (e.g., the cost of climate change through sea level rising, natural disasters and flooding) (UNDP, 2023). Neoclassical models in

public financial management typically attempt to assign market values to environmental assets using tools such as ‘cost–benefit analysis’ or contingent valuation. Yet these tools frequently fall short in capturing the cultural, spiritual, and communal significance of land and sea (e.g., main factors of production) in Tuvalu. Such methods, which reduce nature to dollars and cents, undermine the intrinsic ecological and social roles these resources play. Ecological economists rooted in thinkers like Daly and Georgescu-Roegen argue that neoclassical frameworks systemically ignore biophysical limits (e.g., limited resources, fail to internalize environmental costs, and distort our understanding of sustainability (Martinez-Alier, 2002).

Policy-makers in Tuvalu thus face a critical question: can the claimed benefits of these neoclassical valuation models outweigh the risks of ecological degradation, cultural disconnection, and increasing climate insecurity? In its place, alternative valuation methods grounded in indigenous knowledge, cultural stewardship, and long-term environmental resilience are essential. For example, the value of traditional coastal protection or customary fishing methods goes far beyond immediate economic returns they underpin ecological balance, community identity, and adaptive capacity in a climate-vulnerable nation (Olstrom, 2000; Olstrom, 1990).

Because neoclassical PFM equates progress with perpetual GDP growth, it inherently assumes unlimited substitutability of natural capital, a concept increasingly at odds with Tuvalu’s reality of finite land, fragile ecosystems, and resource constraints. Ecological economics challenges this view, advocating instead for a steady-state orientation that aligns growth with planetary limits and supports intergenerational equity.

Furthermore, neoclassical models’ base policy on the notion of individual rational utility maximizers, yet Tuvaluan society operates through collective decision-making, traditional marine tenure, and shared cultural values. A systems perspective, which recognizes the deep interdependence between social, ecological, and economic systems, is far more appropriate for guiding sustainable PFM in this context (Martinez-Alier, 2002).

Aspect	Neoclassical Approach	Ecological/Pacific-informed Approach
Valuation	Prices everything in monetary terms, ignoring non-market values	Embraces cultural, spiritual, ecological, and communal worth
Growth Model	Assumes sustainable, indefinite growth via substitution	Emphasizes biophysical limits, steady-state economics, intergenerational fairness

Decision-making Theory	Focuses on individual utility maximization	Centres on collective stewardship and resilience
PFM Implication	Could lead to ecological damage, cultural loss, and climate vulnerability	Supports adaptive capacity, knowledge preservation, and ecological integrity

Figure 6.11 Summary of Key Critiques Source: Author’s Analysis (2025).

In short, for Tuvalu, PFM must transcend neoclassical models to incorporate ecological economics and indigenous governance, ensuring both fiscal responsibility and cultural–environmental sustainability.

Conclusion

Ecological and collective approaches have the potential to significantly influence Public Expenditure and Financial Accountability (PEFA) assessments in Tuvalu, especially in the face of mounting climate-related financial risks. These approaches challenge the conventional neoclassical focus on market efficiency and instead emphasize environmental sustainability, social cohesion, and customary systems of governance - all of which are central to Tuvalu’s economic and cultural fabric (Daly & Farley, 2011; Hau‘ofa, 1993).

Tuvalu has undergone several Public Expenditure and Financial Accountability (PEFA) evaluations starting in 2007 and most recently through an Agile assessment in 2024 to gauge the strength of its public financial management systems under the guidance of institutions such as the IMF and World Bank. While these assessments have yielded procedural improvements in areas like budget formulation and reporting, Tuvalu’s fiscal stability remains precariously tethered to climate-induced shocks.

For instance, Cyclone Pam alone inflicted damages equivalent to over 30% of the country's GDP and displaced nearly half the population. The frequent and severe weather events that follow cyclones, coastal flooding, and water contamination, trigger unplanned expenditures spanning emergency response, infrastructure rehabilitation, and long-term adaptation (PFTAC, 2024; Niuatui, 1991). These costs strain domestic resources and deepen reliance on foreign aid, underscoring how environmental vulnerability directly threatens fiscal resilience.

Structural and institutional weaknesses further exacerbate Tuvalu’s fiscal fragility. PEFA assessments consistently highlight budget variances, weak internal controls, delayed financial reporting, and limited transparency in procurement and audits (Tkachenko, 2022; PFTAC,

2021). The country's reliance on cash-basis accounting and oral record-keeping complicates precise forecasting and accountability. Although the introduction of the TechnologyOne Financial Management Information System has improved digital tracking of expenditures, assets, and procurement since 2022, capacity constraints and sparse training have limited its transformative potential. Technical systems remain underutilized, and manual alternatives persist, often leading to late or inaccurate reports, undermining confidence in fiscal planning and oversight.

To navigate these complex challenges, Tuvalu must adopt a public financial management model that transcends both Western neoclassical frameworks, which equate value with market metrics and emphasize GDP growth and purely traditional systems that rely on oral traditions. Neoclassical approaches overlook ecological boundaries and cultural values, while oral systems lack the formal transparency demanded in a modern fiscal system (Stasavage, 2015; Stilwell, 2006).

A hybrid model offers a promising path forward by marrying international reporting standards and formal accountability mechanisms with ecological stewardship and indigenous knowledge. Such integration would value cost-effective coastal protection, sustainable fishing practices, and communal resource management not only for their economic returns but for their roles in preserving ecological balance, reinforcing community identity, and building long-term resilience in the face of escalating climate threats (Thomas, 2013; Tuvalu, 2012).

Moreover, Tuvalu's traditional collective practices such as shared labour and communal land use provide non-market contributions that are often overlooked in fiscal forecasting. Recognizing these inputs improves budget transparency and resource efficiency (Campbell & Crocombe, 1989). The next chapter will explore ideas of how we can rethink public financial management in the cases of small developing countries like Tuvalu in the Pacific Region. The impacts of cognitive institutions have tremendous implications that need to be addressed in order to reduce financial risks for Tuvalu.

CHAPTER 7. RETHINKING PUBLIC FINANCIAL MANAGEMENT IN TUVALU

It matters enormously whether your country has good health service, competent bureaucrats and sound finances. Good government is the difference between living and dying.

- Micklethwait and Wooldridge (2020)

Introduction

The concept of value in exchange is undeniably vital for the growth and development of small economies such as Tuvalu. However, the central tension between Old Institutional Economics (OIE) rooted in traditional systems (cognitive institutions) and New Institutional Economics (NIE) or regulative institutions, as emphasized by Geoffrey Hodgson (1998, 2004, 2012), does not merely concern *what ought to be*, but rather *how it ought to be*. This echoes the philosophical dilemma captured in one of Shakespeare's most iconic soliloquies from *Hamlet* (Act III, Scene I): 'To be, or not to be, that is the question.' Likewise, the most pressing question for public financial management practitioners today is *how* to strengthen the effectiveness of PFM systems in small, peripheral economies while mitigating financial risks within an increasingly interconnected global economy.

The persistent ineffectiveness of Public financial management systems, structures, and processes in Tuvalu has been widely documented. Foundational scholars such as Larmour (1998, 2005, 2012), Niuatui (1991), Munro (1982, 1985, 1990, 1996), Taafaki (1996), and Macdonald (1982, 1998) have long highlighted the structural limitations and contextual misalignments in Pacific governance.

More recently, emerging Tuvaluan and regional voices - including Boland and Dollery (2005), Falefou (2017), Iese et al. (2021), and Simeti and Illingworth (2023) have further critically examined the continued ineffectiveness of externally imposed PFM frameworks. These studies collectively argue that without genuine 'localization and contextual adaptation,' imported models remain ineffective in achieving long-term sustainability and accountability. This critique is further reinforced by broader regional scholarship (Baker, 1983; Balesh, 2013; Bargh, 2001; Becker et al., 2012; Bennett, 2015; Brady, 1974; Chambers, 1984; Colmer & Wood, 2012; Davies, Suhas, & Naidu, 2010; Duncan, 2011; Firth, 2004), which underscores the urgent need for culturally embedded and locally led PFM reform initiatives.

This chapter explores *kaitasi*, a longstanding cultural practice in Tuvalu that offers a heterodox framework capable of bridging the gap between formal (regulative) and informal (cognitive) institutions. *Kaitasi* embodies foundational principles of participatory governance and communal accountability, alongside economic practices such as shared labour and collective land use (Kitara, 2020; Nia, 2021; Niutao Island, 2016; Niuatui, 1991). Rooted in the values of shared ownership and collective responsibility, *kaitasi* presents a culturally embedded institutional model through which the state, citizens, island councils, and local communities engage collaboratively to address hardship and enhance resilience. This practice reflects a cognitive institutional dimension grounded in cultural legitimacy and localized financial decision-making, aligning with Simon’s (1997) concept of ‘bounded rationality.’ The core logic of *kaitasi* is captured by the “3Cs” model: collective, collaborative, and cooperative, which encapsulates its potential to mitigate financial constraints and foster fiscal stability within small island contexts.

Definition of Kaitasi

Building on the culturally embedded principles of *kaitasi*, its relevance has expanded beyond traditional village life into contemporary policy debates surrounding Tuvalu’s economic stagnation, fiscal mismanagement, rising sea levels, and challenges to fiscal discipline. As a dynamic and flexible institution, *kaitasi* demonstrates both evolutionary adaptability and heterodox strength, enabling it to coexist with and inform modern economic frameworks. Its integrative nature makes it a compelling tool for addressing systemic issues in public financial management. At the macroeconomic level, *kaitasi* promotes balance between renewable and non-renewable resource use, while fostering integration between indigenous political-economic knowledge and formal PFM systems. This synthesis underpins Tuvalu’s collective pursuit of sustainable development, offering a model where traditional values enhance modern governance for national resilience and global relevance.

The term *kaitasi* is derived from two Tuvaluan words: *kai*, meaning ‘to eat,’ and *tasi*, meaning ‘together.’ Literally translated as “eating together,” *kaitasi* symbolizes unity, solidarity, and mutual care within families, communities, and institutions. Rooted in traditional Tuvaluan values, this concept emphasizes the importance of shared access to resources as a foundation for social and economic sustainability. As explained by Kokea Logo, an elder from Niutao Island, sustainability in the Tuvaluan context means ensuring that everyone has a share - whether resources are abundant or scarce so that no one is excluded (Logo, 2024). This

philosophy reinforces the interconnectedness of key factors of production: land, labour, capital, and innovation - within a communal framework (Kitara, 2020; Niuatui, 1991).

Implication of Kaitasi

In the Tuvaluan context, *kaitasi* - the practice of shared ownership, collective responsibility, and equitable resource use strengthens both economic and social resilience. This principle echoes across the Pacific, particularly on Niutao Island, where kinship-based collaboration has historically ensured food security, land stewardship, and shared labour during times of hardship. In the traditional *kaitasi* system of Niutao, community bonds, interdependence, and shared accountability forms the backbone of recovery and survival. In this context, the strength of the community lies in its ability to come together in solidarity, rebuild from within, and ensure no one is left behind (Falefou, 2017).

As a heterodox and evolutionary concept, *kaitasi* offers a robust institutional architecture that is well-suited for both traditional customs and modern economic governance. It can interpret through Scott's three pillars: regulative, normative, and cultural-cognitive institutions, where *kaitasi* ensures the system stability and adaptive legitimacy in our uncharted financial waters:

- *Regulative*: formal rules and procedures guide budget design, fiscal decentralization, accounting standards, and audits;
- *Normative*: shared values and communal ethics reinforce appropriate stewardship of both renewable and non-renewable resources;
- *Cognitive*: ingrained beliefs and collective identity foster the 'logic of appropriateness' in public financial decisions.

Complementing this, both Douglass North and Geoffrey Hodgson emphasizes institutions as systems of rules and shared beliefs that structure social interaction, reduce transaction costs, and shape expectations. Within this perspective, *kaitasi* aligns formal fiscal systems with informal norms, embedding decentralisation in social reality and the right hybrid economic approach. This synergy between Scott's pillars and North's and Hodgson's rule-based institutional view enhances the capacity of *kaitasi* to guide policymaking from budget formulation through execution, while sustaining legitimacy, lowering enforcement costs, and reinforcing fiscal discipline throughout the public financial management cycle.

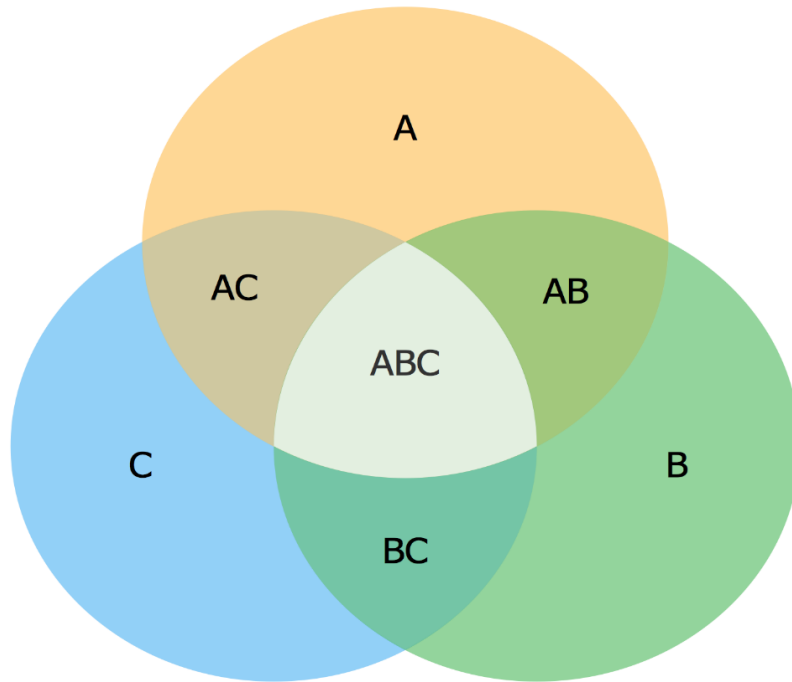


Figure 7.1 Three-Circle Venn Kaitasi model. Source: Author's Analysis of North-Hodgson's institutional lens (2024).

- *Circle A*: Regulative (formal rules) – represents legal frameworks, budgeting procedures, and audit mechanism capturing North-Hodgson's rule-based institutions.
- *Circle B*: Normative (community norms & ethics) – represents shared norms and ethical standards aligns with North-Hodgson's shared norms and values.
- *Circle C*: Cognitive (cultural beliefs & identity) – reflects ingrained cultural identity, collective wisdom, and the logic of appropriateness, echoing Tuvalu's cultural practices

The Venn diagram above demonstrates how where the *Kaitasi* model can improve PFM. At the point where $A \cap B$ (Regulative + Normative) or AB on Figure 7.1: formal decentralization rules are upheld and legitimated by community ethics - enhancing compliance with policy frameworks.

At the point where $B \cap C$ (Normative + Cognitive) or BC: shared beliefs reinforce communal ethics, embedding fiscal responsibility within local cultural identity.

At the point where $A \cap C$ (Regulative + Cognitive) or AC: legal rules are internalized through cultural norms - ensuring self-enforcement and reducing bureaucratic friction.

At the point where $A \cap B \cap C$ (Core of the Model) or ABC: the central overlap represents *kaitasi* at its most potent: a governance system that is legally grounded, ethically supported,

and culturally deep-rooted. This is where fiscal discipline, public financial management, and sustainable development converge.

Kaitasi is a deeply embedded traditional institution in Tuvalu, historically integral to communal life and increasingly relevant in contemporary policy discourse addressing economic stagnation, environmental vulnerability, resource mismanagement, and fiscal discipline. Its resilience lies in its inherently dynamic and adaptive nature, enabling it to evolve alongside modern governance frameworks. When aligned with contemporary Public Financial Management systems such as those evaluated through the Public Expenditure and Financial Accountability (PEFA) framework, *kaitasi* offers a culturally grounded mechanism to address systemic weaknesses in fiscal structures and processes. By leveraging its principles of shared responsibility, equitable resource distribution, and communal accountability, *kaitasi* can complement formal PFM reforms, thereby enhancing institutional effectiveness, transparency, and long-term sustainability.

Kaitasi and Fiscal Discipline

The fiscal role of *kaitasi* holds significant potential in addressing sovereign debt challenges, particularly in small island economies like Tuvalu. As a traditional mechanism rooted in shared ownership and collective responsibility, *kaitasi* functions not only as a cultural norm but also as a form of endogenous fiscal stimulus. It offers cost-effective, community-driven alternatives to conventional bailouts and debt relief, mobilizing collective assets and labour to reduce financial burdens.

At the 2022 United Nations Ocean Conference in Lisbon, *kaitasi* was formally introduced by Tuvalu as a principle of governance and sustainability. Dr. Tapugao Falefou, representing Tuvalu, emphasized that *kaitasi* reflects the nation's commitment to 'joint stewardship' - both within local communities and among the global community, over shared oceanic resources. While traditionally interpreted as 'eating together,' *kaitasi* carries broader policy significance, acting as a foundational institution capable of supporting economic resilience strategies.

In practical terms, *kaitasi* has served as a vital mechanism for mobilizing community-based resources to support essential infrastructure development, including the construction of Christian cathedrals, while simultaneously mitigating fiscal pressures associated with debt servicing. As Bertram & Watters (1984; 2007) observes, island economies often draw upon

historical experiences and institutional memory to design adaptive mechanisms that sustain or restore economic stability during periods of distress (Bertram & Watters, 1984; Bertram G. , 2007).

Within this context, *kaitasi* functions as a culturally embedded economic safety net, structured to shield communities from financial crises, macroeconomic contractions, and exogenous shocks such as natural disasters and global pandemics (Kennedy, 1953). Its integration into modern fiscal policy discourses underscores the relevance of embedding traditional institutional logics within modern sovereign debt management strategies, particularly in small, vulnerable economies where formal safety nets may be limited or externally dependent.

The principle of shared ownership and collective responsibility, as expressed through *kaitasi*, reinforces ecological sustainability while contributing substantively to public financial management. Embedded within *kaitasi* are mechanisms for the financial accounting of sustainable resource use, including traditional knowledge systems governing fishing, taro cultivation, and coconut production each representing potential income-generating streams within community-based economies (Nunn, et al., 2023).

Beyond environmental stewardship, *kaitasi* promotes social cohesion, guarantees equitable access to resources, and supports the sustainable governance of ‘common-pool resources’ such as marine and coastal ecosystems (Ostrom, 2000). It also strengthens mutual support systems that are critical during economic stresses and business cycles. Importantly, *kaitasi* facilitates burden-sharing during periods of inflation or rising interest rates, encourages ‘inclusive financial practices’ through asset pooling, and minimizes conflict over land and fund allocations by embedding entitlement decisions within collaborative governance structures (Johannes, 2002). Collectively, these attributes position *kaitasi* as a culturally grounded model with direct relevance to fiscal resilience, resource equity, and the long-term sustainability of PFM systems in Tuvalu and comparable contexts.

In the context of asset pooling, the concept of *fagai* holds significant cultural and institutional importance in Tuvalu. Literally meaning ‘to feed,’ *fagai* extends beyond its basic definition to encompass the purpose of the meal, the number of participants involved, and the timing and nature of the social obligation attached to it. Each *fagai* is purpose-driven - whether intended for children, women, men, or the entire community and must be fulfilled promptly and without

delay. The obligation to contribute is not merely symbolic; it reflects a deeply rooted ethic of accountability and reciprocity.

Functionally, *fagai* serves a role comparable to that of a ‘potluck’ in many developed countries, yet with stronger institutional implications. It is a structured and expected form of collective contribution that supports communal functions and social cohesion. As illustrated in Figure 7.2, *fagai* can take various forms, enabling individuals and households to pool resources in support of a wide range of development projects from small-scale community initiatives to larger, more complex collective undertakings. Through this mechanism, *fagai* reinforces both economic resilience and participatory governance at the local level.

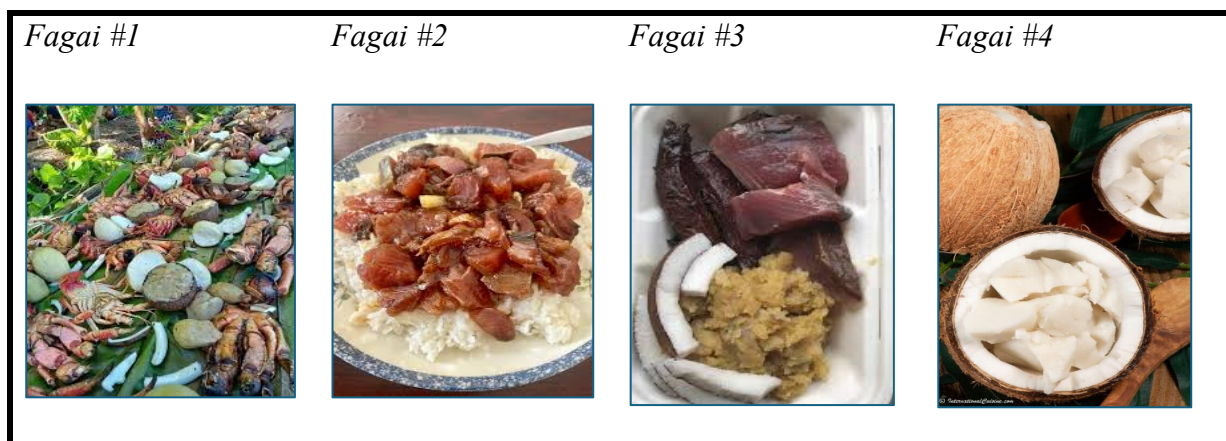


Figure 7.2 Types of Food Levy (*Fagai*) Source: Author’s Analysis (2024).

In pooling assets, the term ‘*fagai*’ is essential. *Fagai* simply means in Tuvalu is to feed. It further its implication what is to be fed and how many participants for instance. The *fagai* also comes with social obligation that require to be met and on-time without delay. By knowing what the *fagai* is for - whether is to feed the group of children, women, men or the whole community can have major implications. *Fagai* is a form of ‘potluck’ (resources sharing) in developed countries (Olstrom, 2000). Figure 7.2 demonstrates the various forms of *fagai* that people in Tuvalu could pool together in feeding the community in various development projects from small to large.

In Tuvaluan culture, *fagai* refers to traditional food contributions that function as a form of communal levy and social obligation, structured according to varying levels of effort, time, and resource input. The classification into four distinct tiers: *Fagai 1*, *Fagai 2*, *Fagai 3*, and *Fagai 4* illustrates a stratified system of contribution that accommodates differing household

capacities and willingness to participate. This tiered approach not only reflects cultural adaptability but also reinforces collective responsibility and inclusivity within the community, ensuring that all members can engage meaningfully in communal events and development efforts, regardless of their means – wealthy or poor.

Fagai #1: represents the most elaborate and labour-intensive contribution. It is typically offered during major community events such as weddings, funerals, or village-wide celebrations. This tier involves coordinated group efforts to harvest coconut crabs, prepare grated coconut, germinate coconuts, and make *fekei* - a staple delicacy made from *pulaka* (swamp taro) pounded and cooked in rich coconut cream. The complexity of *Fagai #1* reflects deep communal solidarity and high social commitment.

Fagai #2: is commonly seen during smaller community gatherings or family events. It includes prepared meals such as rice and fried fish, which require moderate preparation. While less demanding than *Fagai #1*, it still represents a meaningful contribution and maintains the spirit of reciprocity.

Fagai #3: blends elements of both simplicity and preparation. It includes raw fish, *fekei*, and coconut meat. This tier allows contributors to demonstrate effort and cultural knowledge while managing time and resources more efficiently than in *Fagai #1*.

Fagai #4: is the most basic form of food levy, often used in informal or time-constrained settings. It typically includes germinated coconut and green coconut (*niu*), requiring minimal preparation. Though simple, it still upholds the cultural principle that everyone should contribute something to the collective.

These four tiers of *fagai* illustrate the flexibility and inclusiveness inherent in Tuvaluan communal life, while also highlighting how traditional forms of communal financing and resource management have evolved in alignment with modern public financial management systems, structures, and processes in the Three-Circle Venn *Kaitasi* model (see Figure 7.1). By accommodating diverse household capacities at micro-level, the *fagai* model ensures continued participation and equity, preserving cultural cohesion and collective responsibility across island communities, even as governance frameworks become increasingly formalized.

These four levels of *fagai* reflect the adaptability and inclusive nature of Tuvaluan communal life and how communal financing and management adjusted to modern ways of PFM systems, structures and processes. They accommodate varying levels of household capacity while preserving shared responsibility and cultural cohesion within the island communities.

In Chapter 5 and Chapter 6, I have identified the features of cognitive institutions and their influences on public expenditure and financial accountability (PEFA). The imposing of PEFA assessments to evaluate the effectiveness of PFM in Tuvalu found that the influences of cognitive institutions (or old institutional economics) such as kinship, island communities and churches can complicate the reforms of fiscal disciplines by the ADB, World Bank and IMF.

Asset Pooling & Management (*Kai Filifili*)

Once a community has collectively pooled its assets, the principle of *kai filifili* emerges as a vital mechanism for the effective management of limited resources. As a fundamental expression of *kaitasi*, Tuvalu's traditional ethic of shared responsibility - *kai filifili* underscores the importance of 'pragmatism', prioritization, and strategic decision-making in the allocation and use of communal resources (James, 1907; Government of Tuvalu, 2020).

Shared responsibility can be operationalized not only through inclusive collaboration and transparent communication but also through the mechanisms of *answerability* and *enforcement* – which are core dimensions of accountability (Barcham, 2007; Iati, 2017). In this context, communal accountability plays a critical role in ensuring that commitments are honoured and that decisions reflect both collective input and compliance with agreed-upon international standards – good governance, PEFA, and modern budgetary process.

By embedding collective oversight within institutional processes whether is vertical or horizontal, *kai filifili* reinforces the coordination, equity, and resilience of governance structures - whether across central government departments, state-owned enterprises (SOEs), or donor-funded development initiatives. This culturally substantiated models – *Falekaupule* and *maneapa* systems offer valuable insights for enhancing the effectiveness and legitimacy of public financial management systems in Tuvalu.

Etymologically mentioned previously, *kai* means 'to eat,' and *filifili* translates as 'to choose' or 'to prioritize' by choosing which *Fagai* is appropriate for the occasion. This principle is brightly illustrated in Tuvaluan communal feasts, where, on special occasions, an orator may

deliberately break with established seating norms by inviting participants to cross the meeting space and select any seat to share in food prepared by others. This symbolic act represents a departure from protocol to allow for adaptive, needs-based choices, highlighting the importance of flexibility, context-awareness, and equitable access. In the broader governance context, *kai filifili* serves as a culturally grounded model of resource allocation that remind us of ‘adjustments and flexibility’ in communal decision-making.

In Tuvalu’s National Strategy for Sustainable Development 2021–2030, known as *Te Kete*, the principle of *kai filifili* is explicitly emphasized by the Honourable Seve Paeniu, then Minister of Finance, as a guiding framework for national planning. Drawing on Tuvaluan cultural values, Hon. Paeniu interprets *kai filifili* to mean ‘to be pragmatic and address the real challenges.’ This principle promotes a development approach substantiated in strategic prioritization and informed pragmatism.

More specifically, *kai filifili* advocates for a *context-sensitive approach* - one that actively involves all relevant stakeholders, including local residents, user groups, cultural leaders, aid donors, and environmental advocates. Rather than spreading scarce resources thinly across a broad array of initiatives, this approach calls for the careful selection of actions that directly address the most pressing and high-impact challenges facing the nation. By embedding *kai filifili* within *Te Kete*’s priorities, Tuvalu seeks to align national planning with both traditional (cognitive) and modern wisdom (regulative), and also practical necessity (normative), ensuring that development efforts are responsive, targeted, and sustainable.

By embedding *kai filifili* within *Te Kete*, the strategy aligns national development objectives with Tuvalu’s cultural values and practical constraints, ensuring that policy implementation remains both built and effective. Moreover, the broader principles of *kaitasi* offer culturally embedded solutions to persistent public financial management challenges, including fiscal mismanagement, financial accountability, and institutional credibility. This chapter explores how the integration of *kaitasi* through *coordination-coherence- complementary* (3Cs) model can enhance key PFM functions such as budget formulation, cash flow management, revenue mobilization, and debt governance, ultimately contributing to reduced sovereign risk and increased financial resilience over the long term.

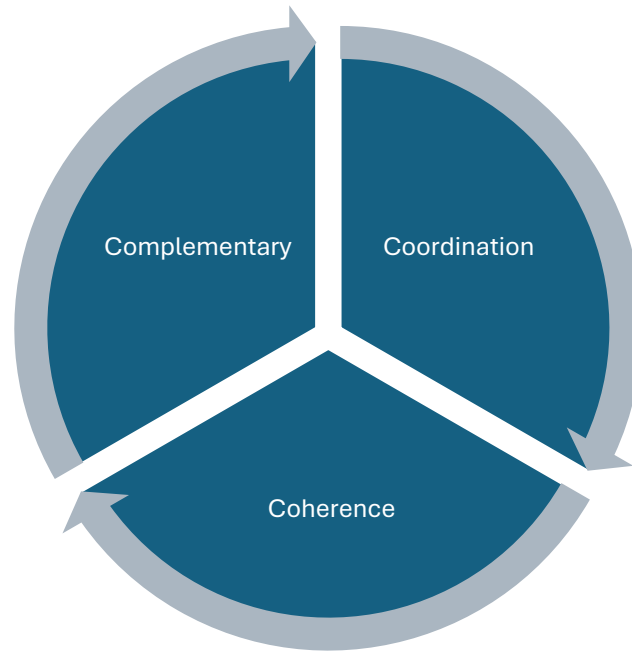


Figure 7.3 The 3Cs Model of Kaitasi. Source: Author Analysis (2024).

One way this 3Cs model can improve PFM is to improve the interactions between three main actors: the host country (aid recipient) (federal levels), the communities (local level), and aid donors or (investors). The *coordination*, *coherence*, and *complementary* functions of *kaitasi* can be operationalized through three key avenues: capacity building and coordinated governance; institutionalizing transparency; and aligning donor support with national objectives.

Coordination Approach: 1st C

A crucial step involves strengthening the capacities of public sector (regulative institutions) leaders such as senior Ministry of Finance officials and executives of state-owned enterprises (SOEs) to understand how their roles contribute directly to *Te Kete*, the national strategy for sustainable development, and to broader macroeconomic outcomes. This requires effective coordination through multi-processes and partners. For instance, the design and implementation of a Medium-Term Fiscal Framework (MTFF) and strategic budgeting are essential competencies. These enable government officials to map multi-year revenue and expenditure plans that align with *Te Kete* priorities and development goals while enhancing fiscal discipline and resource predictability.

The Medium-Term Fiscal Framework (MTFF) plays a pivotal role in translating strategic objectives into actionable, phased financial plans – (i.e., financial literacy discourses). By breaking down overarching development goals into specific multi-year revenue and expenditure targets, an MTFF enhances fiscal discipline, transparency, and decision-making efficiency (IMF, 2023). In the Tuvaluan context, integrating MTFF into national planning (i.e., financial literacy discourses) allows public sector leaders to align annual budgets with long-term national priorities such as strengthening ‘financial literacy’ through formal education. It also empowers both central and local government managers with the skills necessary to design sustainable, multi-year fiscal strategies that enhance the capacities of communities, educational institutions, and public enterprises alike.

Minchao Jin & Zibei Chen (2020) examine how ‘formal financial education’ (e.g., school or workplace programs) and kinship - ‘family financial socialization’ (guidance from parents or guardians) each contribute to individuals’ financial knowledge and capabilities (Jin & Chen, 2020). Their analysis, based on data from the 2015 National Financial Capability Study, reveals that both channels positively impact financial literacy but in different ways:

- *Formal education*: tends to enhance technical understanding of concepts like budgeting, investing, and financial instruments.
- *Family socialization (informal education)*: exerts a stronger influence on everyday financial behaviours and practical money management.

Importantly, Jin & Chen find that while each approach is beneficial independently, their combined effect can be ‘less than additive,’ suggesting that family (informal) and formal teachings may overlap or even conflict when used together. They conclude that designing effective financial literacy programs requires a ‘coherent integration’ of both educational approaches - educational curricula reinforced by consistent kinship - family/social messaging to develop both knowledge and behaviour effectively.

In terms of regulative institutions, which encompass legitimacy through formal and informal laws, procedures, and enforcement mechanisms (i.e., inflows of foreign aid) (Scott, 1995), Tuvalu stands to gain significantly by coordinating shared governance (e.g., local, federal and investors) within its fiscal architecture (see Figure 7.4). Scholars such as Larmour (2005) and Allen, Hemming, and Potter (2013) advocate that ‘decentralized fiscal responsibility’ enhances both the effectiveness and legitimacy of public financial management in small

island states. In other words, delegation of fiscal responsibilities from the Federal to local government (i.e., *Falekaupule*) and other stakeholders can also encourage accountability.

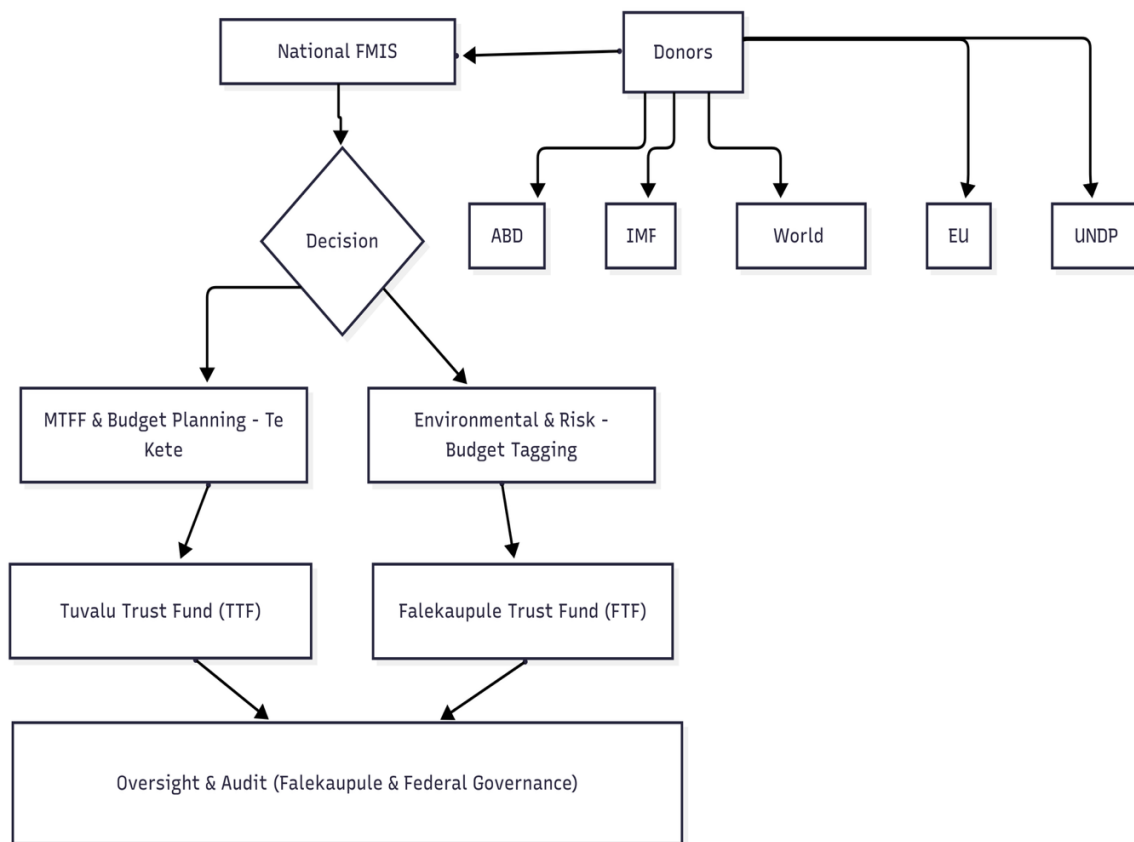


Figure 7.4 Fiscal Architecture of Shared Responsibility. Source: Author Analysis (2024).

Traditional bodies like the *Falekaupule* (cognitive institutions) and the legally recognized island councils of elders already possess regulatory authority within their communities. Endowing these institutions (regulative, normative, cognitive) including the Donors and Federal’s financial management information system (FMIS) to co-manage budget oversight – through budget tagging, procurement, and expenditure reporting (e.g., TechOne financial software) at the local level would institutionalize transparency and reinforce accountability through community-led structures (i.e., *Kaupule*) (as shown above Figure 7.4). Thus, coordinating a ‘participatory model’ in fiscal processes and promote compliance with local ownership and traditional enforcement mechanisms, thereby reducing financial risk and enhancing fiscal resilience across government departments, state-owned enterprises (SOEs), and donor-funded programs.

The effectiveness of coordination can also be found also through the channelling of climate changes funds. In Tuvalu, where climate change and global economic volatility pose constant

threats, shared fiscal planning and decision-making are vital for national resilience. At the national level, the establishment of the Tuvalu Trust Fund (TTF) and the Tuvalu Survival Fund (TSF) provides essential budget support and rapid-response financing for climate-related crises.

Simultaneously, at the local (island) level, the Falekaupule Trust Fund (FTF) empowers traditional councils to manage emergency and development resources directly. These community-driven mechanisms - grounded in *kaitasi*-style collective or shared ownership ensure that both national and local governments can mobilize funds quickly and transparently in response to shocks such as cyclones or economic downturns. Accordingly, shared stewardship is not merely a cultural value but a strategic institutional asset (i.e., *kai filifili* approach) that enhances the robustness of Tuvalu's public financial management framework.

A key priority in Tuvalu's sustainable development strategy, *Te Kete*, is building public-sector capacity, especially among senior Ministry of Finance officials and SOE leaders to coordinate and implement fiscal tools like a Medium-Term Fiscal Framework (MTFF) and strategic budgeting. The MTFF translates long-term strategic goals into disciplined multi-year revenue and expenditure plans, improving transparency and alignment with priorities such as enhanced financial literacy.

Research by Jin & Chen (2020) shows that combining formal education and informal family financial teaching boosts financial competence, highlighting the need for integrated literacy programs. Governance-wise, decentralizing fiscal responsibility, empowering both formal institutions (e.g. island councils, *Falekaupule*) and Island communities, supported by donors and financial systems - strengthens legitimacy, accountability, and resilience. This shared responsibility model extends to managing climate finance: national funds like the Tuvalu Trust Fund (TTF) and Survival Fund, alongside local Falekaupule Trust Funds (FTF), enable transparent, rapid, and community-driven responses to climate and economic shocks, turning shared stewardship into a strategic advantage.

Coherence Approach: 2nd C

The principles of *kaitasi* (shared ownership) and *kai filifili* (selective engagement) are integral to crafting effective policy solutions that align with Tuvalu's evolving institutional challenges and global dynamics. Embedding traditional Pacific values such as *ava* (respect), *alofa* (loving-kindness), and *tautua* (service) in budget policy design helps bridge modern public financial

management with local cognitive institutions (Besnier, 2009; Chambers K. S., 1984). This cultural coherence underpins more ethical and community-grounded fiscal decision-making, ensuring that budget allocations and service delivery genuinely benefit all citizens

By embedding these shared values across the regulative, normative, and cognitive levels of governance, Tuvalu can strengthen collective responsibility among local and national governments and aid donors. This culturally informed fusion promotes greater institutional legitimacy, social trust, and participation. Ultimately, grounding PFM in traditional ethical values fosters more effective governance structures and processes, reinforcing resilience and sustainability in Tuvalu's financial systems.

Within normative institutions, which govern societal values and behavioural norms - the cultural principles of *kaitasi* (shared ownership) and *kai filifili* (strategic choice) offer a powerful mechanism to professionalize fiscal conduct by aligning formal regulations with ingrained communal values (Government of Tuvalu, 2020). This synchronization is particularly potent in settings like Tuvalu, where oral traditions, spiritual beliefs, and culturally bounded rationalities inform decision-making. Channelling these through formal fiscal practices enhances shared ownership and legitimacy of public financial management.

For instance, incorporating public finance and financial literacy instruction into national and local education using culturally resonant methods such as traditional storytelling in local dialects or faith-based metaphors, can deepen communal understanding and trust in inclusive budgeting and financial processes. Additionally, involving respected community leaders (elders, church figures, youth representatives) in civic education initiatives strengthens the cognitive legitimacy of PFM reforms, anchoring technical reforms within community support networks.

By embedding social values like respect (*ava*), charity (*alofa*), and service (*tautua*) into fiscal operations, the cultural logic of *kaitasi* fosters greater transparency, accountability, and moral grounding in both budgeting and service delivery. This culturally rooted approach not only reinforces shared responsibility but also empowers participatory governance structures such as the constitutionally recognized *Falekaupule* to co-manage financial oversight, procurement, and expenditure reporting at the local *maneapa* system. Through this integration, normative reinforcement cultivates resilient, community-led mechanisms that elevate the credibility or legal frameworks and fairness of PFM in Tuvalu's multi-level governance system.

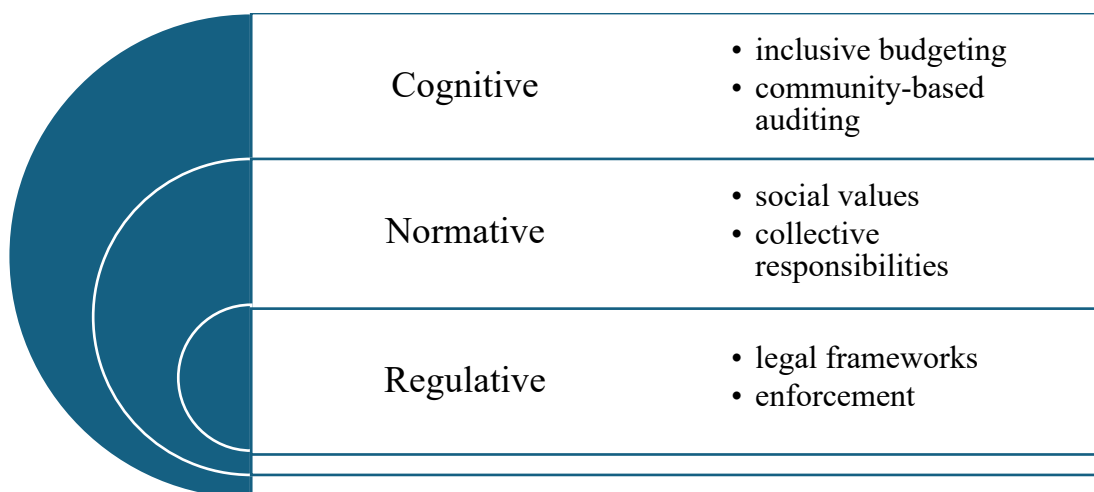


Figure 7.5 Shared Inclusive Budgetary Process. Source: Author’s Analysis (2024).

By combining these three institutional dimensions within proper coordination efforts through local, federal and donors - Tuvalu can significantly reduce the impacts of external shocks and financial crisis. Traditional practices of the *kaitasi* and interaction of the *Falekaupule* and the Federal governments provide a culturally grounded mechanism for inclusive budgeting, community-based auditing, and participatory oversight can improve these gaps. Beside reinforcing voluntary compliance and accountability through Island communities but also encourages coherence responsibilities among all stakeholders in PFM systems, structures and processes.

Complementary Approach: 3rd C

Local leaders possess contextual knowledge about infrastructure, education, health and environment priorities that may not be visible to national planners. This alignment prevents misallocation of funds and ensures they are directed to areas of highest impact. For instance, in the 2017-2020 National Development Coordination Policy and PEFA assessments (PEFA, 2024), Tuvalu emphasized aligning ‘*Te Kete*’ with local development needs through better coordinated budgetary process and planning frameworks. However, the incompatible of modern PFM governance and practices with traditional has been negatively reduced the effectiveness of PFM reforms.

However, with shared ownership (*Kaitasi*) approach and strategic choice (*kai filifili*), complementing traditional knowledge in Niutao Island community such as the Ao can further argues that modern PFM can build on common ecological knowledge and sustainable

approaches that some of the Niutao’s kins and their ancestors have embraced and kept for centuries. Kap Tafiti, Manager at the Polynesian Cultural Center (PCC) in the Samoan village repeatedly argues that the coconut is the main ‘tree of life’ for many Polynesian countries including Tuvalu (Tafiti, 2022). Below is the life cycle of the coconut tree.

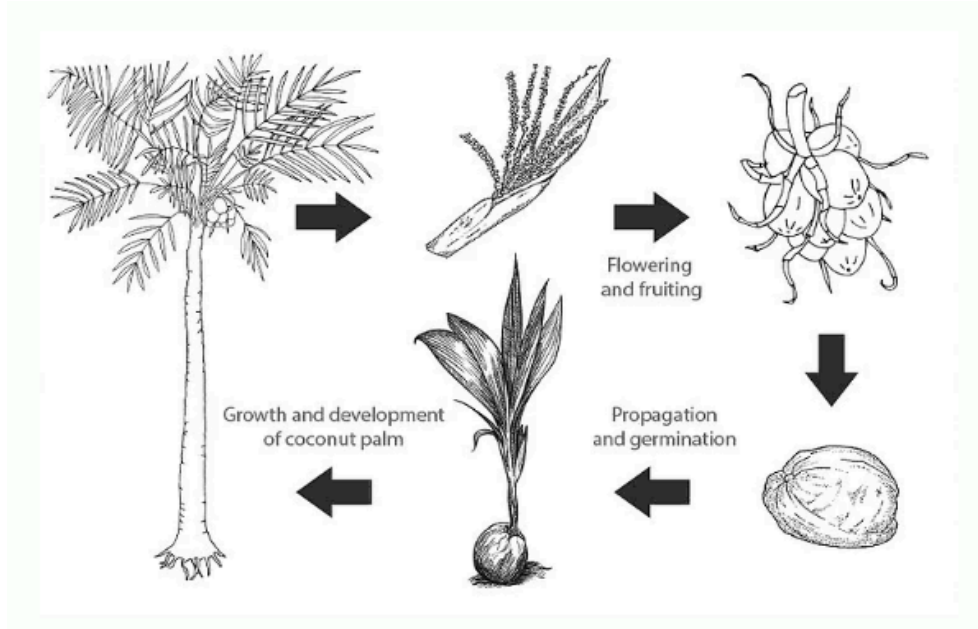


Figure 7.6 Coconut Tree Life Cycle. Source: Tastenirvana (2024) and Nakala Nia (2021).

These are the six key phases of the coconut tree life cycle - each one parallels important pillars and processes of public financial management. The cycle begins with the ‘seed’ and concludes with ‘fruiting and harvesting’, with precise timing essential to ensure every stage reaches its fullest potential: seed (germination), sprouting, growth (vegetative development), maturity, flowering, and fruiting & harvesting:

Phase 1. Seed Stage: a mature coconut falls to the ground and acts as a seed – rotting or sprouting in suitable conditions.

Phase 2. Germination & Sprouting: the seed germinates within the husk, forming a shoot and root system. A small sprout emerges within a few months.

Phase 3. Seedling Growth: the young palm develops its first true leaves and taproot, establishing itself in the ground.

Phase 4. Juvenile to Mature Tree: over 5-10 years, the palm grows in height and truck girth. Tall varieties typically flower between 6 and 10 years, while dwarf cultivars may flower as early as 3 to 5 years.

Phase 5. Flowering & Fruit Development: tiny flowers emerge in clusters (inflorescences), then set fruits that mature over approximately 9 months.

Phase 6. Fruiting & Harvesting: once mature, coconuts are typically harvested about 7 to 8 months after flowering. A mature tree can produce a coconut every 23 days – roughly 15 harvests annually, equating to around 150 coconuts per tree per year (Wattanaporn, 2024; Nia, 2021).

Below is a structured exposition delineating the six phases of the coconut life cycle alongside their public financial management counterparts - spanning budget planning, execution, reporting, and accountability.

The ‘germination phase’ of the coconut seed - the foundational stage where roots and shoots begin to develop reflects the ‘budget preparation and strategic planning’ process in PFM. At this stage, core fiscal frameworks are established, fiscal forecasts are laid out, and high-level policy priorities are articulated. These foundational activities correspond directly to the role of the coconut seed absorbing nutrients to build strength and viability.

Following germination, the ‘sprouting and early vegetative growth’ of the coconut tree align with ‘policy-based budgeting and fiscal framework alignment.’ As the tree allocates its energy toward structural growth, so too must governments link budget allocations to strategic policy goals. Resources are channelled to critical sectors within a medium-term framework, ensuring balanced and purposeful development.

During the ‘vegetative growth stage’, the coconut palm invests heavily in biomass - akin to the PFM’s budget execution and control phase. Here, funds are disbursed, procurement procedures are enacted, and internal controls including COSO-style risk mitigations ensure efficient utilization of public resources. This mirrors the importance of internal controls and systems to prevent misuse and promote operational discipline (PEFA, 2024).

As the tree begins ‘flowering’, it signals that yields are imminent. In PFM terms, this stage equates to ‘accounting and reporting’, when financial activities are systematically recorded and consolidated, and periodic financial statements are published. Accurate reporting enables managers and citizens alike to monitor progress toward fiscal objectives (PEFA Secretariat, 2016).

When the coconut tree reaches the ‘fruiting and harvesting stage’, it generates tangible benefits - coconut meat, water, copra. This corresponds to ‘external audit and scrutiny’ in PFM, where independent auditors evaluate performance, verify compliance, and ensure accountability to stakeholders. This phase ensures that harvested benefits are lawfully and effectively realized (PEFA, 2024).

Coconut Phase	PFM Element	Description
Seed/Germination	Budget Planning & Preparation	Building the foundation
Sprouting Growth	Fiscal Strategy & Policy-based Budgeting	Defining realistic budgets aligned with goals
Vegetative Growth	Budget Execution & Control	Deploying funds with strong management
Flowering	Accounting & Reporting	Recording and benchmarking progress
Fruiting/Harvesting	External Audit & Oversight	Verifying results, ensuring accountability
Replanting	Reinvestment & Feedback Loop	Using outcomes to refine future cycles

Figure 7.7 Comparison Coconut Phase and PFM Element. Source: Author’s Analysis (2024).

The final phase – ‘replanting or seed collection’ - symbolizes the ‘reinforcement and feedback cycle’ in PFM. Audit findings, budget evaluations, and performance reviews inform future fiscal reforms and budget cycles. This feedback loop is vital for institutional learning and sustainable financial stewardship.

Through this botanical analogy or ecological approach, it becomes evident that effective PFM requires deliberate attention at each stage from inception, through execution and review, to feedback and renewal mirroring the careful progression needed for a coconut palm to thrive and sustain future generations.

Conclusion

Using Kaitasi common model for coordination, coherence, and complementary can reinventing ways for PFM systems, structures and processes to be effective. A cooperative approach to strengthening public financial management in Tuvalu integrates formal fiscal systems with indigenous cultural and social practices, ensuring governance aligns with communal values and lived experiences. By grounding PFM in culturally resonant traditions such as kaitasi (collective responsibility) and *Falekaupule*-led consensus, the management of public resources gains both legitimacy and adaptability. These traditional mechanisms foster shared ownership,

embedding transparency and collective stewardship within the financial system, and reinforcing effective, culturally congruent resource governance to reduce current risks.

Decentralized enforcement through community-based tools like community scorecards and the *maneapa* system - further embeds accountability within local structures. Community scorecards empower citizens to assess budget allocations, service delivery, procurement processes, and financial performance, facilitating transparent dialogues and community-driven improvements. The *maneapa*, as a central communal gathering, functions as an open forum for monitoring public projects, enabling horizontal accountability by allowing community members including elders, family heads, women, and youth to directly question and inspect financial activities. These systems circumvent geographical and bureaucratic constraints, ensuring inclusive oversight and reinforcing social accountability.

The normative institutional dimension emphasizes embedding core cultural values such as inclusive dialogue (*fakapotopoto*), fair distribution (*vaetasi*), and collective obligation (*kaitasi*) into the fiscal cycle. Involving traditional leaders and community representatives in budget planning ensures alignment with social ethics and local development priorities. This participatory and values-driven process enhances public trust, improves compliance with fiscal obligations, and mitigates risks from elite capture or corruption. Through shared ownership and equitable distribution, Tuvalu's PFM becomes not only more efficient, but also socially cohesive, resilient, and reflective of its cultural identity.

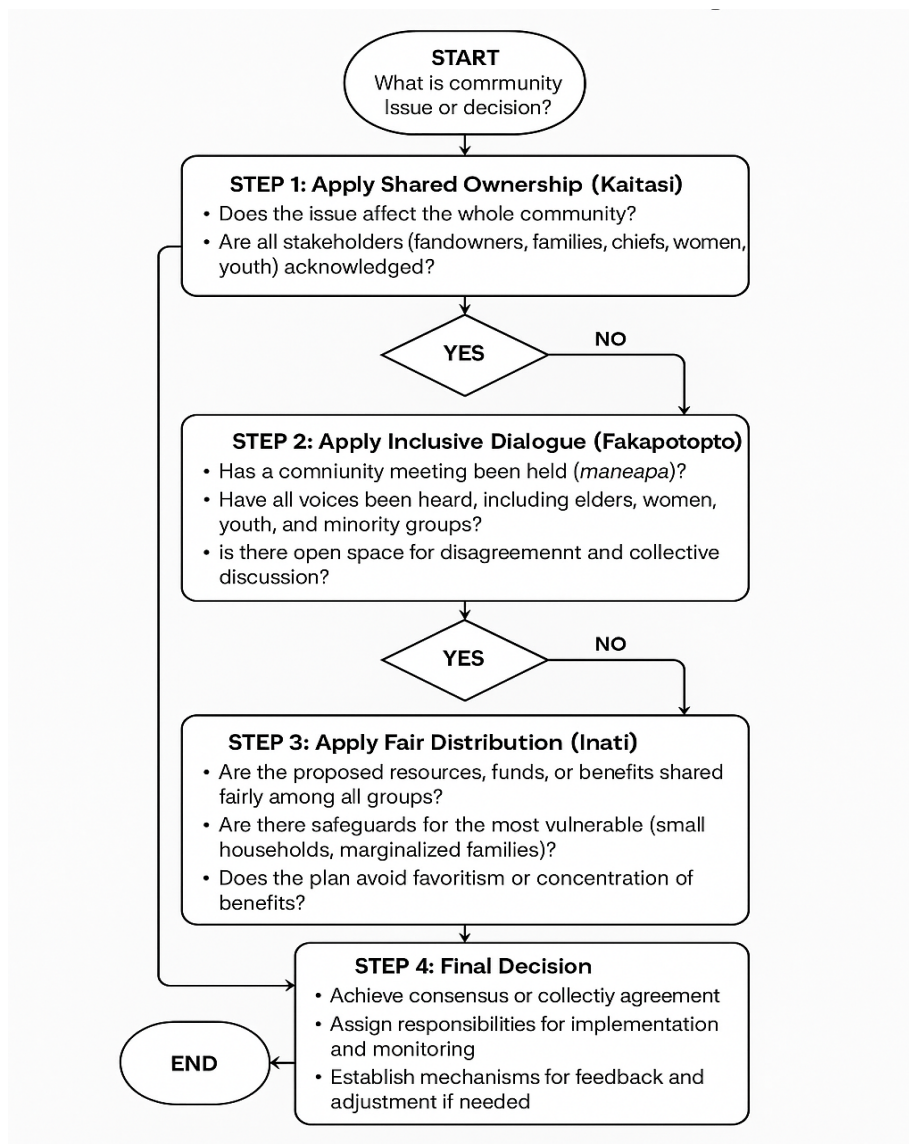


Figure 7.8 Decision-Making Tree. Source: Author’s Analysis (2024).

Strengthening Tuvalu’s public financial management demands a holistic, cooperative strategy that integrates shared ownership (*kaitasi*) across regulative, normative, and cognitive institutional dimensions. Involving traditional governance bodies such as the *Falekaupule* and the *maneapa* system, it can enhance transparency and accountability while mitigating fiscal mismanagement and mismanagement of limited resources in Tuvalu. Embedding communal values including *kaitasi*, *fakapotopoto* (inclusive dialogue), and *vaetasi* (fair distribution), bolsters normative legitimacy and nurtures voluntary compliance. Concurrently, communicating financial matters through culturally familiar narratives, using local language and oral traditions, strengthens public understanding and trust in governance.

Furthermore, melding traditional (old institutional economics) and contemporary (new institutional economics) approaches establishes coordination, coherence and complimentary (3Cs) mechanisms for joint fiscal planning and community-led auditing. Instruments such as community scorecards, village-based review forums, and the maneapa meeting system promote ‘horizontal accountability’ by empowering elders, chiefs, women, youth, and other stakeholders to participate in budget decisions, scrutinize expenditures, and ensure projects reflect local priorities. This culturally informed, participatory approach enhances fiscal efficiency, resilience to external shocks, and institutional legitimacy, ultimately strengthening inclusive, adaptive, and sustainable PFM in Tuvalu.

CHAPTER 8. CONCLUSION

Ko tou Malosi, ko tou Maumea. (Your Strength is your Wealth) - Tuvaluan proverb (1978)

Summary of this Study

Scott's institutional framework, emphasising regulative, normative, and cognitive pillars of institutional organisation and change, has provided the framework for this thesis to consider how to strengthen Public Financial Management in Tuvalu and reduce systemic financial risks. This thesis has shown that while regulative institutions aim to uphold good governance, they face major challenges due to limited transparency, weak accountability, unsustainable economic models under the MIRAB framework, and the emergence of Dutch disease effects. Normative institutions, which reflect moral values and professional standards, are constrained by short and culturally incompatible budgetary cycles, insufficient integration of local governance, misalignment between regional policy frameworks like the Pacific Plan and local realities, and gaps between traditional and modern education systems. Furthermore, cognitive institutions which are rooted in Tuvalu's historical memory, behavioural patterns, and cultural logic, reveals how local manifestations of loss aversion, simplicity bias, and weak financial literacy hinder reform adoption. The limited effectiveness of oversight bodies such as PASAI and local SAIs further complicates fiscal accountability. Understanding the interplay of these pillars is crucial for designing institutional reforms that are legally sound, culturally relevant, and socially accepted.

Scott's Three Institutional Pillars: A Foundation for Effective PFM

Richard Scott's institutional theory asserts that enduring social systems are structured around three interrelated pillars: regulative, normative, and cognitive institutions. Each pillar influences behaviour through distinct mechanisms: legal obligation (regulative), moral duty (normative), and internalised beliefs (cognitive). In the context of Tuvalu, these institutional pillars have not only shaped public financial reforms but hold transformative potential. When these pillars are effectively integrated and interact harmoniously, they can significantly strengthen public financial management and enhance institutional resilience.

Regulative Institutions

The regulative pillar involves formal policies, laws, and enforcement structures; individuals comply because they *have to* under established authority. Tuvalu's economic aspirations have long been constrained by two critical factors: the inefficacy of its regulative institutions and the structural limitations of the MIRAB model, an economic framework built on migration (MI), remittances (R), aid (A), and bureaucracy (B). While this model provided foundational stability following independence in 1978, it has failed to promote 'economic diversification', fiscal discipline, or sustainable development. Regulative institutions (i.e., Westminster model, Parliament, Executive Branch of the Government, Ombudsman, etc.) are responsible for enforcing laws, managing public finances, and ensuring accountability, but have struggled with weak enforcement capacities, outdated legislation, and a lack of independence. Agencies such as the Office of the Auditor General and the Public Accounts Committee often lack the resources, political backing, and institutional authority to detect and correct financial mismanagement effectively.

At the heart of this failure is a broader issue of capacity and systemic inertia. Many regulatory frameworks, such as the Public Finance Act, remain outdated and disconnected from Tuvalu's evolving development needs. Implementation of these frameworks is undermined by a shortage of skilled personnel, poor data systems, and limited use of digital financial tools. Moreover, central government institutions continue to dominate the financial decision-making process, marginalizing island communities and stifling participatory governance. This 'top-down approach' often results in misaligned budget allocations and low public trust in financial processes (ADB, 2007).

The MIRAB model has likewise reached its limits. Although migration (MI) and remittances (R) have historically been vital economic lifelines, they are now subject to global volatility and can no longer be relied upon for consistent income. External aid (A), another pillar of MIRAB, has fostered dependency and discouraged the development of domestic revenue sources. Meanwhile, an oversized bureaucracy (B) has expanded under this model without corresponding improvements in productivity or innovation. Public sector employment, particularly in state-owned-enterprises (SOEs) consumes a large share of the national budget, reducing fiscal space for capital investment or private sector support. Furthermore, the model does little to incentivize investment in potentially productive sectors such as tourism, fisheries, and renewable energy.

To reduce financial risks and transition toward a more resilient economic model, Tuvalu must prioritize financial transparency and diversify its revenue streams. Strengthening the oversight role of public institutions is essential. This includes regular publication of fiscal reports, enforcing audit findings, and enhancing the independence of watchdog agencies (ADB, 2024). Public participation mechanisms such as community budget consultations through the *maneapa* system can also foster transparency and civic trust. Adopting a Medium-Term Fiscal Framework (MTFF) will allow for more strategic planning, aligning multi-year budgeting with *Te Kete*, Tuvalu's national development strategy. This will improve fiscal predictability and reduce the reliance on ad hoc donor support.

Revenue diversification is equally crucial. Tuvalu has opportunities to expand returns from the Tuvalu Trust Fund and leverage its .tv internet domain, which is a unique and underutilized asset. In addition, enhanced maritime fees for access to Tuvalu's exclusive economic zone (EEZ), along with investments in green energy and digital services, could serve as alternative sources of income. Engaging traditional governance institutions such as the *Kaupule* and *Falekaupule* can help legitimize new financial policies and increase compliance at the grassroots level. These measures, taken together, would not only reduce Tuvalu's financial vulnerability but also lay the groundwork for a more self-reliant and transparent economic future.

Normative Institutions

Normative institutions, as outlined by Geoffrey Hodgson (2000; 2004; 2012), encompass shared values (code of conducts), professional ethics, and institutional routines, and play a critical role in shaping public financial behaviour. The normative pillar operates through shared conventions, ethical standards, and social expectations, guiding behaviour through what people *ought to do*.

However, several limitations currently hinder their effectiveness in Tuvalu. Budgetary processes, for instance, often follow rigid routines and short timeframes that do not allow for adequate community consultation or critique of national priorities. These rushed budgetary rounds are not only inconsistent with Tuvaluan cultural practices of collective deliberation but also fail to integrate local government perspectives effectively. The exclusion of island councils from meaningful participation in national budgeting weakens both the legitimacy and accuracy of resource allocation decisions.

Moreover, the development of professionalism within public institutions is undermined by a misalignment between regional frameworks such as the ‘Pacific Plan’ and Tuvalu’s internal economic needs. Policies developed at the macro level often fail to reflect micro-level realities, especially in small, culturally rooted societies like Tuvalu. Additionally, there is a disconnect between traditional and modern education systems. While traditional knowledge systems emphasize ecological sustainability and long-term stewardship, modern curricula often prioritize short-term economic gains and technical knowledge, leading to fragmented approaches to development and budgeting.

Another critical component of normative institutions is the adherence to a strong code of conduct, which includes ethical leadership and anti-corruption safeguards. Unfortunately, PEFA assessments have revealed persistent weaknesses in Tuvalu’s procurement processes, particularly related to conflicts of interest and the limited enforcement of the Public Procurement Act 2013. Without clear ethical standards and accountability mechanisms, public trust erodes and financial risks multiply, especially in high-value sectors like infrastructure and aid-funded projects.

To address these challenges, Tuvalu must strengthen its normative institutions by aligning budgetary structures with cultural practices and timelines, enhancing professional development with a localized focus on ethical governance, and enforcing procurement laws with greater transparency. Emphasizing ethical leadership and incorporating traditional ecological wisdom into education and policy planning can also foster a more coherent and responsible financial culture. By reforming these institutional norms, Tuvalu can significantly reduce financial vulnerabilities and build a more resilient and culturally grounded public finance system.

Cognitive Institutions

The cognitive pillar embeds cultural values, beliefs, and mental models so that individuals comply because they *want to*, drawing from deep-seated identity and meaning (Hecker, 2012; Job & Ceccarelli, 2012). Scott argues that sustainable institutional change emerges only when all three pillars reinforce each other. An effective PFM system in Tuvalu, therefore, must leverage each dimension to promote resilience, legitimacy, and adaptive capacity.

Cognitive institutions in Tuvalu, which encompass deeply embedded cultural norms, institutional memory, and behavioural tendencies, have significantly shaped the trajectory of public financial reforms. The influence of institutional memory including Tuvalu's colonial

past, communal land tenure, and historical practices of resource sharing has led to a collective experience where modern budgeting processes are often viewed through the lens of customary values and shared obligation. These longstanding practices create both continuity and resistance to change. Furthermore, behavioural biases such as loss aversion, simplicity bias, and familiar tendencies influence how citizens and officials perceive financial reforms. For example, many individuals may prefer traditional, familiar approaches to resource distribution rather than adopting unfamiliar financial management systems, even if they are more efficient. These biases can result in reluctance to adopt transparency measures or shift from informal to formal accountability frameworks.

Another key aspect of Tuvalu's cognitive institutions is the role of communal and financial accountability, where social cohesion and mutual responsibility often override individual financial scrutiny. While this can reinforce trust and cooperation, it also contributes to limited critical engagement with public financial decisions. Compounding this issue is the weak presence of oversight institutions - notably the underperformance of PASAI (Pacific Association of Supreme Audit Institutions) at the regional level and the limited capacity of Supreme Audit Institutions (SAIs) within Tuvalu's local and federal systems. These weaknesses leave financial reforms vulnerable to minimal enforcement and low public awareness.

To improve PFM and reduce financial risks, reforms must acknowledge and align with these cognitive realities. This includes increasing 'financial literacy' using culturally relevant language, traditional storytelling, and community dialogues in the *maneapa* setting. Strengthening SAIs and ensuring that audit findings are clearly communicated to the public in accessible formats is also essential. Moreover, addressing behavioural biases through nudges such as default savings schemes, simplified budgeting tools, or visual spending trackers can help change financial behaviour gradually. Embedding public finance reforms within trusted communal frameworks and leveraging the credibility of elders and religious leaders can further legitimize these changes. In doing so, Tuvalu can create a culturally grounded financial system that builds on cognitive strengths while reducing fiscal vulnerability and enhancing long-term sustainability.

The Application of Institutional Pillars and PFM in Tuvalu

Reinforcing the Regulative Pillar: Legal Authority and Accountability

The Falekaupule Act 1997 already grants legal status to traditional local councils (*Falekaupule*) and outlines their governance roles including budget oversight and annual reporting (Government of Tuvalu, 2023). Strengthening this pillar involves embedding *Falekaupule*'s oversight functions that tied to procurement, budget approval, and auditing into national financial legislation. This would create enforceable mechanisms, impose penalties for budget mismanagement as pointed out in Chapter 7, and formalize local participation. As a result, Tuvalu would establish a more transparent and enforceable fiscal architecture, minimizing the opportunity for irregular expenditures or corruption.

Leveraging the Normative Pillar: Embedding Communal Values

Tuvaluan values such as *kaitasi* (shared responsibility), *vaetasi* (equitable distribution), and *fakapotopoto* (inclusive dialogue) are powerful normative forces that should be used for strategic choice (*kai filifili*). By integrating these values into professional codes, training, and community engagement protocols, PFM can foster voluntary compliance and ethical accountability. Public officials and citizens would feel a sense of moral duty, 'ought to', toward responsible stewardship of shared resources. This shift from coercion to civic integrity reduces enforcement costs and enhances internal peer oversight, ultimately fostering a more collaborative and responsible financial culture.

Strengthening the Cognitive Pillar: Cultural Resonance and Internalization

To resonate deeply with citizens, fiscal policies should be communicated through cultural channels - *maneapa* discussions, church forums, local storytelling, and indigenous language briefings. When budgets and performance information are framed within Tuvaluan cultural narratives, communities internalize fiscal principles as part of their identity, they want to support responsible governance. This cultural alignment enhances transparency, builds trust, and ensures that PFM practices remain relevant and anchored in local context, thus reinforcing compliance and reducing misalignment between policy and practice.

Integrated Risk Mitigation: Pillars in Synergy

When the regulative, normative, and cognitive pillars work together, they generate a multi-layered defence against financial risks. For instance, regulative institutions can measure clear rules, and legal mechanisms prevent mismanagement through enforceable standards. Normative values can establish ethical expectations and communal duty encourage proactive

stewardship and peer accountability. Cognitive institutions resonance can cultural affinity ensures internalization of fiscal norms and authentic public engagement.

This combined approach enhances institutional legitimacy, public trust, and financial resilience, enabling Tuvalu’s PFM system to better navigate risks such as misallocation, corruption, budgetary dependency, and vulnerability to external shocks. By embedding traditional knowledge within modern structures, Tuvalu can build a PFM system that is not only robust and legally sound, but also socially cohesive, culturally legitimate, and sustainable over generations.

	Regulative	Normative	Cognitive
Legitimacy	Legal systems	Moral and ethical systems	Cultural systems
Central Rudiments	Policies and rules	Work roles, habits and norms	Values, beliefs and assumptions
System Change Drivers	Legal obligation	Moral obligation	Change values are internalized
System Change	Fear and coercion	Duty and responsibility	Social identity and personal desire
Sustainers	Government, agencies, international bodies	Professional bodies, education systems	Cultural groups, indigenous knowledge systems
Behavioural Reasoning	Have to	Ought to	Want to

Figure 8.1 Regulative, Normative and Cognitive Elements of Institutions Source: Palthe’s Evaluation of Institutions Elements (2014).

Conclusion

Scott’s three-pillar model offers a comprehensive roadmap for reinforcing PFM in Tuvalu. By embedding Falekaupule authority and financial rules (regulative), integrating shared cultural values (normative), and communicating policy within local worldviews (cognitive), the PFM system becomes multifaceted and resilient. This holistic strategy closes governance gaps, strengthens stakeholder buy-in, and supports adaptive processes, ultimately empowering Tuvalu to manage its finances responsibly, transparently, and sustainably in an ever-changing global context. Such an approach has the potential to overcome dissatisfaction and disconnection rooted in the history of colonisation and past experiences during the Gilbert and Ellice Island Colony (GEIC).

The integration of regulative, normative, and cognitive institutional pillars offers a comprehensive and culturally grounded approach to improving public financial management and reducing financial risks in Tuvalu. When these three pillars operate in synergy, they establish a system that is not only legally enforceable but also morally compelling and culturally resonant.

By reinforcing the ‘regulative pillar,’ Tuvalu can formalize the role of traditional governance bodies such as the *Falekaupule* within national legislation, thereby enhancing local oversight and embedding accountability into law. Clear rules, audit requirements, and enforceable sanctions reduce fiscal opacity and mismanagement. However, regulations alone are insufficient without the moral reinforcement of the ‘normative pillar’. Embedding communal values like *kaitasi* (shared responsibility) and *vaetasi* (equity) into public service ethics, professional standards, and leadership practices encourages a culture of stewardship and duty. This normative influence ensures that public servants and citizens feel a moral obligation an ‘ought to’ in supporting financial integrity.

Simultaneously, the ‘cognitive pillar’ strengthens these reforms by ensuring that financial systems align with how people naturally understand and relate to governance. When budget transparency and fiscal education are delivered through traditional forums such as *maneapa* meetings, church gatherings, and indigenous storytelling, they become internalized. Citizens begin to ‘want to’ engage in PFM, not because of legal pressure or moral duty alone, but because it aligns with their identity and values.

The synergy between these three pillars forms a multi-layered strategy of resilience. Legal frameworks provide a ‘have to,’ ethical norms a ‘should,’ and cultural values a ‘want to’ approach to compliance. Together, they increase legitimacy, trust, and citizen ownership of financial reforms. This integrated framework not only mitigates risks like corruption, resource misallocation, and external dependency but also lays the foundation for a PFM system that is robust, inclusive, and sustainable for future generations.

Tuvalu’s pathway forward lies in embedding traditional knowledge into modern governance - bridging legal authority with moral responsibility and cultural meaning. When institutional pillars reinforce each other, they do not merely support good governance; they create a deeply rooted, community-owned model of financial accountability that can adapt and endure across time.

-THE END -

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