

PALAU

1. Economic Statistics

Population: 19,129 (2001)

Land Area: 497 square kilometers

Exclusive Economic Zone: 629,000 square kilometers

Political Status: independent republic in free association with the United States since 1994

GNP: US\$133.6 million (1999)

Major Industries: agriculture, tourism, subsistence fishing

Merchandise Exports (FOB): US\$11 million (1998)

Major Exports: handicrafts; agricultural goods; taros and coconuts

Merchandise Imports (CIF): US\$79 million (1998)

Major Imports: mineral fuels; manufactured goods; machinery; food

Currency: United States Dollar

2. Economic Profile and Performance

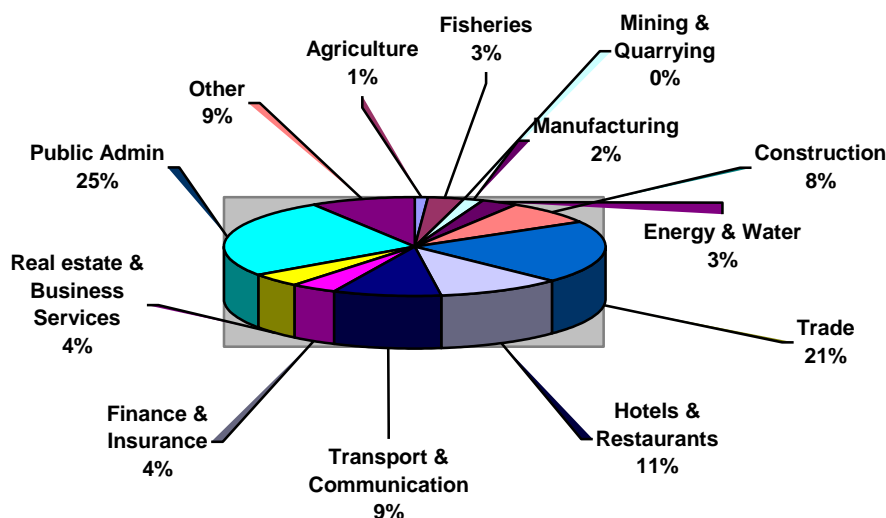
Palau is a small developing economy, generating a total GDP of US\$133.6 million in 1999. Despite the fact that it is a remote country, it enjoys a relatively high standard of living which, in the main, is a result of support funds drawn down annually from the Under the Compact, the United States government agreed to pay Palau US\$447 million over the first 15 years (1994–2009) of the 50-year Compact. There is also provision for major infrastructure projects, including the construction of a road around Babeldoab and the continuation of some United States federal programmes. Palau also receives preferential trade access to the United States under the Compact.

The Republic of Palau has started down a new path of economic and social development. Palau's economic future is based around the opening up of opportunities afforded by its unique natural resources and culture, its modern and open economy. The areas of growth in Palau have been in construction, transport and communications, real estate and business services. The key areas of development that have been prioritized are roading, improving its international gateways, electrification, communications and general infrastructure. The potential remains for significant growth in agriculture and fisheries in the next few years given Palau's natural abundance in fisheries and its proximity to the Asian market.

The Compact obliges the United States to defend Palau. It also commits the United States to continue to provide, at no cost to Palau, many services including air safety, weather prediction, health services and assistance in the event of a natural disaster. Tourism, the main source of income in Palau, has recovered from a decline in 1998 and the first six months of 1999, effected by the Asian economic downturn. Palau's tourism is focused on high-income, small-volume tourism, in order to achieve a balance between maintaining its pristine environment and tourism infrastructure development.

Small-scale agriculture is experiencing an increase in demand, and fishing is also important to Palau. Japan is a major importer of Palau's tuna and Mackerel, and Chinese and Taiwanese long-line fishing fleets also fish in Palau's Exclusive Economic Zone (EEZ).

GDP Contributions 2001 (at current prices)



Source: Palau Statistical Abstract 2002

3. Agriculture and Fisheries Sectors

There is limited agricultural production beyond the subsistence farming of taro, cassava and sweet potato. With a small area of land to cultivate and a small domestic market, large-scale commercial agriculture is not viable. Palau has only limited forest reserves and there are no plantations of introduced species. Apart from high-quality manganese in the seabed of Palau's EEZ, yet to be quantified, there are no other known mineral resources.

Agriculture, livestock, forestry and fishing comprise a small share of the total national output and income. While there certainly is potential for growth, especially in agriculture to meet more domestic demand for food and fiber from domestic production, the likelihood of that happening soon is small. The reason for agriculture's limited role is Palau's small market, which cannot take advantage of economies of scale that make commercial agriculture financially successful.

As pointed out in the findings of a recent presidential task force on agricultural development, it costs less to import foods and fiber than to produce them in Palau. While exceptions do exist, this situation of imports meeting more of the demands for food and fiber is common to the small Pacific Island economies where small markets and small landmasses prevent the establishment of large commercial agricultural enterprises.

In rural Palau, most households earn a part of their livelihood from subsistence farming and fishing. Women grow staple crops such as taro, cassava and sweet potato. Men provide the protein for the household's diet by catching fish. Rice has recently become an important staple food. Bread made of imported wheat flour has gained popularity as a staple also mainly in urban Koror, where several commercial bakeries operate.

Among the most pressing problems agriculture faces, especially in small economies, is the availability of adequate labor willing to work on farms and capital to invest in both skills and facilities. As agriculture is always subject to uncertainties dictated by nature, and demand for food does not necessarily go up with rising income, its earning potential is both limited and unpredictable. That is one of the main reasons agriculture often receives subsidies in most economies, usually in Europe, Japan and the United States. Since an adequate supply of food and fiber is always a high priority, governments readily justify subsidies and other assistance programs to agriculture.

Beyond subsistence fishing and a small local market, including restaurants, Palau's main source of income from this sector is generated through the sale of licenses to foreign fishing vessels from Japan and Taiwan that are involved in catching tuna in its extensive EEZ.

Palau, with a total land area of 188 square miles, has an EEZ of 237,835 sq miles out of which 0.2% (560sq miles) constitute inshore waters with a diverse ecosystem hosting a wide range of species. Coastal waters are fished by the population on a subsistence basis while Coastal State Fishing Cooperatives, numbering 11 with a total membership of around 90, engage in commercial fishing as well. The cooperative network operates nearly 50 out-board motor boats.

Palau - Total catch of fish in coastal waters by species 1997/2001 (lbs)

Species	1997	1998	1999	2000	2001
Assorted reef fish	189,463	167,450	308,493	286,483	294,761
Parrot fish	37,031	25,009	27,861	12,098	57,516
Surgeon & unicorn	22,565	8,706	29,699	23,428	101,613
Emperors	12,366	36,990	17,591	9,204	20,586
Rabbit fish	9,071	6,836	17,571	10,433	25,613
Groupers	1,311	3,475	9,033	2,424	23,835
Others	39,337	85,392	67,658	58,769	69,594
Total (lbs)	311,141	333,858	477,906	402,839	593,473
Total (kg)	141,427	151,753	217,230	183,108	269,760

Source: 2001 Government of Palau, Statistical Yearbook

The recorded annual landings from coastal fisheries amounted to around 270,000kg in 2001 (Table 1). Regulatory provisions are strictly implemented to manage the coastal and reef resources while the management plan for fisheries is also under development by the Department of Fisheries, with a total staff of 34.

Only a small fraction of landings from coastal fisheries is traded, most being used for consumption by the household. There are three market outlets for fish, one in the capital Koror, the other two in the eastern and western locations of the country. Around 300-400kg of

fish are air freighted to Guam and Saipan weekly by three exporters operating from Koror. Airfreight charges to Guam is around \$ 1.95/kg to Guam. If the consignment exceeds 100kg the rate is half, i.e. 0.98cts/kg.

**Palau - Employed population (> 16 yrs) by industry and income
1999/2000**

Industry	Total	Total with Income	Median Income	Meat Income
Total employed	9,383	8,068	5,583	8,520
Agriculture	167	151	3,011	4,468
Forestry and fisheries	501	387	5,579	6,855
Construction	1,232	850	4,367	6,661
Manufacturing	65	63	5,150	6,108

Source: 2001 Statistical Yearbook

Fishing in the off-shore waters is carried out by a fleet of 3 locally based foreign long-line fishing vessels and 36 licensed foreign long liners. Licensing fee for foreign vessels ranges from US\$1,500(< 21mt), US\$ 2,500 (21-70mt) to over US\$3000 (>70mt). Several Japanese Fishing Associations too operate in the EEZ. High priced fish such as sashimi quality tuna caught by the fleet of locally-based foreign fishing companies are air freighted, mainly to Japan (Osaka) and Guam, from Koror (Table 4).

**Palau - Migratory fish* exports by locally-based foreign fishing companies
1996/2001 (mt)**

Year	1996	1997	1998	1999	2000	2001
Quantity	2,256	1,813	1,855	2,559	2,334	2,031

* tuna and other migratory species

Source: 2001 Statistical Yearbook

All exports are subjected to an export levy of US\$0.25/kg. In 2001, total fish exports by the fleet of locally-based foreign fishing companies amounted to over 2000mt. Foreign vessels do not land their catch locally.

Except for some root crops and fresh fish, the domestic market heavily depends on food imported duty free. Fish is relatively costly when compared to imported animal products such as poultry, which is marketed around US\$ 0.70/lb upward, whereas most varieties of fresh fish would cost US\$ 1.50- 2.50/lb. Imported canned fish is popular in Palau, especially among the urban population and among foreigners, numbering around 6500, employed in Palau.

Retail market price of canned fish in Koror

Product	Origin	Weight	Price (US\$)
Sardines in tomato sauce	Philippines	155 gm	0.50
Light meat tuna in oil	Thailand	7 oz	0.90
Light meat tuna in oil	Japan	7 oz	0.90
Solid white tuna	US	6 oz	1.89

Source: Price information collected during the study

The Department of Fisheries plans to embark on a project promoting value addition of fish through a Japanese assisted program. The project envisages to introduce a wide range of fishery products targeting the local market and the tourists, who are predominantly Japanese and Taiwanese. The products identified for such promotion includes smoked/ dried fish, kamaboko, sashimi tray pack, tuna jerky etc.

4. Food Sector

In general, Palau's small market makes it difficult to take advantage of economies of scale that make commercial agriculture successful, and the country is very dependent on the importation of foods to maintain food security. The Republic of Palau has no significant food

exports outside the fisheries sector. Palau is developing a commercial fishing industry, but commercial fishing still consists predominantly of foreign ships catching tuna in Palau's exclusive economic zone for sale and production elsewhere.

Food is mainly imported into Palau from the US, Japan and Korea. Although there is a large balance of trade deficit, subsistence agriculture and fisheries are critical in sustaining the domestic cash market and supporting the growing tourism sector. Agriculture in Palau consists mostly of root crops, vegetables and fruits, with some pork and poultry production, the latter mainly for eggs that satisfies most of the local market. Fisheries and agriculture combined represented on average 5% of the country's GDP for the period 1990-1998.

As with other US affiliated Pacific markets, Palau can sell manufactured goods in the United States duty free. The country has yet to take advantage of these favourable conditions with respect to the export of food products. Palau's processed food industry consists of one brewery, a number of bakeries, a few meat processing/packaging plants and an ice cream plant. The majority of food businesses are restaurants, hotels, snack bars, food vendors and fast food outlets and stalls. None of the establishments operate under HACCP or quality assurance systems.

4.1 National capabilities to meet importing country food safety requirements

Food standards do not exist in Palau and the food processing industry is not sufficiently diverse and knowledgeable to have the capacity to implement quality assurance and HACCP systems. There are also limited resources and technical capacity at the government level to facilitate the development of and enforce modern food safety and quality systems that would meet overseas market requirements. Having said this, the Ministry of Health is examining options for the development of comprehensive and Codex-based food standards for Palau.

The Bureau of Environmental Health and Sanitation of the Ministry of Health, under the provisions and guidelines on basic food safety in Chapter 34 of the Palau National Code, carry out food inspection. Public health food inspectors play a role in ensuring the safety of locally produced food in their routine inspection and assessment of food premises. This largely focuses on visual inspection of foods, together with hygiene and sanitation and premise requirements. Attention is also given to process controls such as temperature control during food preparation, storage and display.

4.2 Issues and barriers to exports

Other than the fisheries sector, Palau has no established food exports. Palau will need to focus on agricultural policies that aim to diversify agricultural production and improve marketing and production efficiency in order to have opportunities to create food export markets. It has several technical cooperation programs that are addressing these areas. In general, development of export markets is constrained by numerous factors including:

- Low level of agricultural production due to small land holdings and population base
- Lack of skilled and high cost of labour
- Lack of storage and processing facilities for downstream production and value adding of agricultural crops
- The lack of integrated quality management and food standards in production and processing systems that could potentially facilitate and optimize comparative advantages
- Lack of post-harvesting food technology expertise and investment both within Government and industry to develop value added food processing.
- Other issues identified as barriers for exports include:
 - There is currently very little investment in the food industry and no real manufacturing industry of note.
 - The private and business sector forces have not reached a critical mass whereby they can effectively lobby Government for modernization of infrastructure and standards development.
 - The Chamber of Commerce is seeking improvements to infrastructure and the development of food standards, and is seeking to work more collaboratively with government to identify opportunities with respect to aid and technical co-operation programs.
 - The government needs to be responsive to the issues put forward by the private and business sectors and develop better collaborative working relationships.

4.3 Deficiencies in institutional and legislative frameworks

There are no domestic food safety or quality standards currently within Palau. Under the Palau National Code (PNC), food establishments are required to comply with requirements relating to food preparation, storage, equipment, personnel, waste disposal and pest and insect control. A Consumer Protection Act that could have strengthened the requirement for the preparation and sale of food was introduced into the National legislature recently but failed to gain support from the Government.

The lack of standards such as labeling, contaminant and microbiological criteria for foods and the lack of a food-testing laboratory make it difficult to objectively support food inspection and enforcement activities. In the absence of assurances against established food standards, the consumer is potentially vulnerable to foods of low quality and questionable safety. The incapacity to test imported ingredients and locally manufactured foods against standards also exposes the food industry to safety failures and potentially compromises markets.

The high dependency on the United States for food imports, has until recently, made food standards a low priority. However, as markets are progressively freed up, Palau is witnessing a greater amount of imports from other countries, particularly Asian markets. Such products often do not have English labels and their quality and safety is unknown.

The lack of comprehensive food safety and quality regulations and standards means that there is a lack of assurance against quality and safety of both imported food and that produced domestically. The Government of Palau recognizes the value in improving the safety and quality of food and the benefits this may bring in promoting confidence in the food supply. The presence of standards has benefits for the economy in being one of the platforms on which tourism can be promoted and the benchmark that the food industry must work to in its implementation of product quality and safety systems.

Seafood export standards and regulations are currently being developed for Palau.

4.4 Institutional framework

The Division of Environmental Health within the Ministry of Health is responsible for inspecting food establishments to ensure that they are safe and protect the health and safety of consumers. Every food establishment is required to have a health permit to sell food. The health permit is issued after completion of an inspection in which the requirements under the PNC have to be met. Food businesses are also given a risk ranking, based on the degree of non-compliance in certain areas. The lower the ranking, the more frequently a food premise is inspected.

Issues identified were the following:

- The Environmental Health Division has only four properly trained health inspectors within the food area and lacks the resources to extend inspection activities beyond that of basic food hygiene inspections.
- Palau does not have a national Codex committee, although the Ministry of Health is actively reviewing Codex food standards with a view to drafting similar standards for Palau.
- Staff within Health and Agriculture has received training in HACCP systems but have insufficient expertise to effectively audit and certify such systems.

Quarantine regulations are harmonized throughout the Federated States of Micronesia and are largely based on US requirements. There is insufficient technical capacity and resources to undertake independent risk analyses for plant and animal health related issues.

Palau is not a member of Codex and there is currently no competent authority. It is proposed that the Ministry of Health will take on the role for quality certification of exports. The seafood industry would like to access the EU market and there is a requirement for a competent authority to certify HACCP and quality assurance systems.

Palau has a hospital laboratory that can test foods for basic (standard plate counts) microbiological contamination. Low priority is given to testing of food samples and it is rarely undertaken. There is currently no capacity to perform comprehensive microbiological and/or chemical analysis of foods within Palau. An absence of routine testing of foods results in:

- An inability to objectively assess compliance against food standards.
- The food industry having a difficult task to develop added value products.
- A failure to facilitate the development of plant and product certification systems, which would help in export promotion.

There is currently no inspection or analysis at the border for imported processed and packaged foods and ingredients.

In enforcing the Food safety Regulations requirements, food inspectors utilize a risk-based approach that is dependent on the nature of the business and its compliance record in a number of food safety areas. For example, there is a requirement for food businesses to ensure that foods are stored, handled cooked and displayed at appropriate temperatures. However, it does not require monitoring of temperatures and records to be kept by businesses. Inspectors do not currently have the capacity to test temperatures of foods, nor can they objectively assess safety and suitability of foods for consumption against established microbiological and chemical standards. Trained officers using official protocols and checklists carry out quarantine inspection of animal and plant-based products at the border. The system is based on that developed by the SPC and is largely harmonized throughout Micronesia. Although there is a lack of technical capacity to assess the quarantine risk posed by animal and plant products, assistance is usually provided by SPC.

5. Trade Policies and WTO Membership

Palau has also signed a Compact Agreement with the United States. The Compact of Free Association (the Compact) is a 50-year political, strategic and economic treaty between the Republic of Palau and the United States. Under the Compact, Palau conducts its own domestic and foreign affairs as any sovereign nation would, while the United States retains control of defense and security matters as well as exclusive strategic access to Palau's waterways. For this exclusive access, the United States is to pay the government of Palau a specified sum of money in the first 15 years of the Compact.

Palau being a net food importer relies on imports for food security and at the same time a large portion of the population rely on subsistence agriculture and fishing. Imported foods are subject to 3% tariffs plus 3% Gross and Revenue Tax. This liberal tax scheme makes it difficult for local industries to be set up especially if all the raw materials and capital are to be exported.

Market access is not a major issue especially the access arrangement with the Japanese market and the US markets. Palau has not ratified the PICTA and PACER due to obligations under the Compact Agreement which is to be reviewed in the near future.

In terms of WTO membership the benefits that Palau would gain would be in the following areas:

- Improved access for garment exports to international markets;
- Improved legislation relating to food standards, intellectual property protection, transparent service sectors (given tourism is a major source of foreign exchange); and
- Improved access to technical support and capacity building.

The challenges to Palau would be the limited resources available to look after trade policies requirements under the WTO. The agriculture sector is very small and there would not be much impact at all if it becomes a member.

6. Recommendations

- (i) Promote diversification on agricultural products – there is certainly a lot of potential to develop the agricultural sector and attracting foreign investment through joint venture arrangements would enhance the production of vegetables and fruits. There is certainly potential for such to be exported to the nearby markets of Guam and Saipan.
- (ii) Commercial farming in giant clams – the market opportunities for giant clams would boost Palau's export earnings. Again attracting foreign investment through joint venture arrangements would facilitate such developments.
- (iii) Establishment of a modern domestic fish processing/ marketing network with increased focus on production of value added seafood for domestic market as well as speciality products for the tourist market. This would also help import substitution and increase earnings through exports.
- (iv) Explore possibility of using by-catch from foreign fleets for domestic marketing / processing operations as well as encourage land-based export-processing of tuna.
- (v) Further development of sustainable utilization of coastal and reef fishery resources including exploratory marketing in non-traditional markets in Asia.
- (vi) Strengthening of the seafood inspection system including quality assurance of exports through capacity building and implementation of appropriate HACCP-based process control measures in association with industry as well as speedy identification of a Competent Authority to ensure equivalence compliance for EU .
- (vii) Needs for training and capacity building - Trade policies and awareness raising – for Palau government officials and private sector to be aware of the international trade policies particularly the regional and multilateral arrangements, it is important to undertake awareness programs, consultations and training to assist the government in developing policies in the future.
- (viii) Control of imported foods - The implementation of a system for the inspection and testing of imported foods and ingredients would be beneficial for Palau in preventing mislabeled, low quality and potentially unsafe foods from entering and/or being dumped onto the domestic market and therefore better protecting the consumer. It would also give assurances to future food processors, which would have to rely heavily on imported ingredients for their food manufacturing. In order to implement a system that is compatible with WTO/ SPS and TBT requirements, domestic food standards must first be established and a greater capacity developed for their enforcement.

- (ix) Quality management systems training - There is a need within Palau to build upon current agricultural diversification programs and to look at establishing good agricultural practice systems for selected agricultural commodities of importance to the economy.
- (x) The Government in partnership with the food industry needs to take a proactive approach to facilitate the development of quality assurance and HACCP systems for food processing. Such systems will have benefits for production and will better assure the quality and supply of products. Assistance and training is required to better understand the requirements of these systems and to advise and train the industry in their establishment and implementation.
- (xi) Food safety training - Knowledge of and training in basic food hygiene is good across food businesses in Palau as the Ministry of Health has established ongoing programs for food businesses. The Government and industry should build on this and encompass training in the development and evaluation of process control and HACCP food safety systems. Further training is required within the health sector so that they can transfer this knowledge to the food sector.