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The future of Papua New Guinea-Australia relations



a paper¹ based on an address to the Institute on 25 October 2011 by

Ms Jenny Hayward-Jones

Programme Director – The Myer Foundation Melanesia Programme at the Lowy Institute
Lowy Institute for International Policy²

The buck stops with Australia when it comes to ensuring the stability of Papua New Guinea. Jenny Hayward-Jones assesses Australia's relationship with Papua New Guinea, examining past failures in the relationship and the impact of recent events and global dynamics on it. She makes suggestions as to where the relationship might head, capitalising on the new opportunities that now present.

Key words: Papua New Guinea; Australia; bilateral relations.

The Australia-Papua New Guinea relationship is vital strategically and economically for both nations. I shall discuss the relationship's historical context, its importance, the impact of recent events on it, and the way in which global changes are altering the dynamics of our engagement with Papua New Guinea (PNG). I will address past failures in the relationship and provide some suggestions for where the relationship can go from here.

Papua New Guinea Today

PNG is the largest and most economically significant state in Australia's sphere of influence, the Pacific Islands. Despite its rich natural and human resources wealth however, PNG continues to face very significant challenges to its human development and political stability and remains of significant concern to Australia. Some social indicators have improved since independence, while others have worsened. Overall, PNG continues to lag behind other Pacific islands, the Asia-Pacific region and the world in progress on human development. Incredibly, the World Bank's most recent report on the millennium development goals ranked PNG as the only country besides Somalia to register as "far" off-track on all the quantifiable goals (Delfin and Quijada 2011).

Since independence, PNG's economic performance has been unstable³ and, while recent growth has been impressive, it has not yet been converted into better national living standards. Around 40 per cent of the population live below the international poverty line (US\$1.25 a day), while the population grows at close to 2 per cent a year. Urbanisation is occurring rapidly, and a large youth bulge is generating considerable concern, given high rates of crime and insufficient employment opportunities in urban areas.

About 87.5 per cent of the population lives and works outside the formal economy in rural subsistence agriculture. Here, the national government has very little relevance to the everyday lives of its citizens. Highly mountainous terrain makes infrastructure incredibly difficult and expensive to build, and government service delivery is poor. Poverty and malnutrition are rife. More than 70 per cent of rural people lack formal education, and only 27 per cent are fully literate⁴. Political authority and allegiance are exercised mostly at the clan level.

Violent clashes between clans erupt frequently; with retributive rape, witchcraft and killings commonplace. There is tension between landowners and mining projects, and, with strained relationships between provincial and state authorities, there is ever-present potential for these to escalate into rebellion or secessionism tendencies.

Australia's Interests in Papua New Guinea

For Australia, PNG's simmering instability has been a significant concern for over a decade. Canberra is acutely conscious of the potential for PNG to become a failing state and political rhetoric and policy-making since the September 11 terrorist attacks⁵ and the Bali bombings have reflected concern that the so-called Melanesian "arc of instability" would become a hotbed of transnational crime, people-smuggling, money-laundering and terrorism.

A vital point of distinction between our relationship with PNG and our other important military or aid commitments is that this one is far from a shared responsibility. In the context of our most vital alliance, the buck stops with Australia when it comes to ensuring the favourable alignment and stability of PNG and the Pacific Islands region. The United States looks to Australia to take responsibility in the Pacific.

In PNG, Australia has traditionally been the dominant source of aid, investment, exports, imports, and defence.

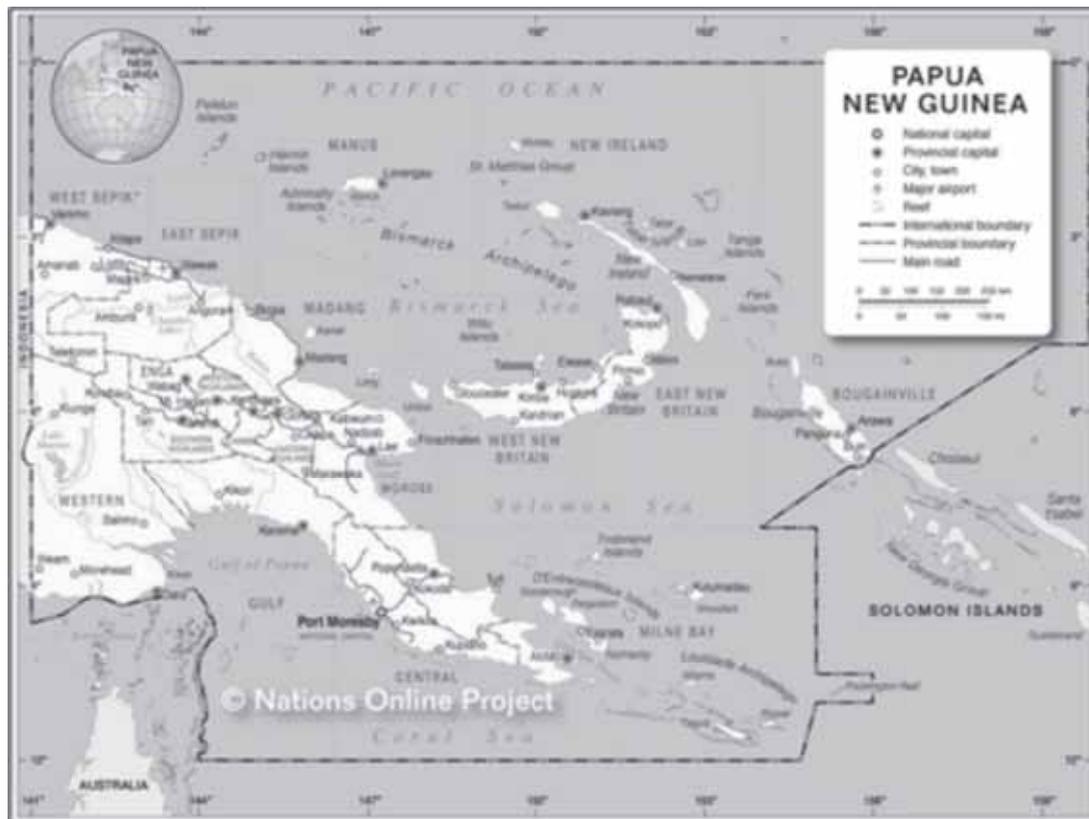
¹For publication, the presentation was edited, shortened and updated to include the constitutional crisis of December 2011.

²jhayward-jones@lowyinstitute.org

³World Bank, *GDP Growth (Annual, %)*. <http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG/countries/PG?display=graph>

⁴Rowan Callick. Growth stymied by big man rioting. 12 October 2011. <http://www.theaustralian.com.au/news/world/growth-stymied-by-big-man-rioting/story-e6frg6ux-1226164219130>

⁵The al-Qaeda raid on New York and Washington on 11 September 2001



Map: Papua New Guinea (Source: Nations Online Project – maps)

While other countries are increasingly active there, none have the deep history of cultural, political, military, and economic linkages that we and PNG share. Australia administered part, and then all, of PNG from 1906 until 1975, when it became formally independent. Informal dependence on Australia endured for many years after that, with Australia continuing to provide a large amount of budgetary support and administrative assistance. Australian companies were heavily invested in PNG's economic fortunes, with Australia PNG's dominant trade partner and primary source of investment.

Economic linkages remain strong with bilateral trade totalling almost \$6 billion in 2010. In the same year, the cumulative total of European, Japanese, and Chinese trade with PNG was less than \$2.5 billion. For Australia, PNG was our 15th biggest trading partner⁶. For PNG, Australia was by far its biggest⁷.

Australia also remains by far the largest source of development assistance to PNG, where we have our second largest international aid programme. Our 2011-12 aid budget in PNG is \$482.3 million – roughly 5 per cent of the PNG government budget, and four times China's aid.

While Australia's aid commitment in Indonesia is technically larger at \$558 million, Australia receives a far smaller amount of political leverage in return for the aid it gives there. In 2009, total net aid represented 5.3 per cent of PNG's gross national income, whereas for Indonesia it represented only 0.2 per cent. In the same year, Australia

supplied about 60 per cent of the aid that PNG received. In Indonesia, Australia's aid made up only 10 per cent of total gross aid receipts. PNG is where Australia has the greatest capacity to leverage interest, and where Australia has the greatest capacity to make a difference.

This leverage, however, has dramatically decreased over the last 36 years. Whereas Australian aid constituted over 20 per cent of PNG's gross domestic product (GDP) in 1975, today it accounts for less than 5 per cent. Australia's aid to PNG is increasing every year, but rapid population growth,

economic output and terms of trade growth are rendering it increasingly insignificant as a fraction of the PNG government's budget and overall GDP. This trend is accelerating with an influx of international donor interest there.

Other Nations' Interests in Papua New Guinea

Traditionally focused on the Polynesian countries, New Zealand now plays a far larger role in Melanesia, with PNG and the Solomon Islands its largest international donor programmes. The European Union and Japan have active aid programmes in PNG, and Taiwan has spent tens of millions courting PNG officials. The United States opened a Pacific office in Port Moresby in October 2011, representing, on one level, increasing United States recognition of PNG's economic relevance, and on another, an overdue response to China's active engagement in PNG.

China's ambition to establish global economic and political reach has not left the Pacific Islands untouched. As an aid donor, China's regional strategy was framed until recently around securing diplomatic recognition at the expense of Taiwan. But since a diplomatic truce was established in 2008, China has been able to reorient its Pacific strategy. The primary beneficiary of this shift has been PNG. In 2009, PNG received more than half of China's development assistance to the entire Pacific. At US\$121.5 million, this represented a huge increase on China's development assistance to PNG which, prior to the truce in 2007 and 2008, was only around \$10 million (Hanson and Fifita (2011, 9).

⁶<http://www.dfat.gov.au/geo/fs/png.pdf>
⁷<http://dfat.gov.au/geo/fs/png.pdf>

With an abundance of natural resources, PNG's appeal to China is not hard to understand. PNG's exclusive economic zone is larger than China's, and its rich tuna stocks make investment in onshore processing a sound option for China, particularly given China's food security is falling in the face of rising demand at home. PNG's mineral resources and oil deposits further make it an attractive investment destination for China, a rapidly industrialising country whose global outreach strategy has been driven in part by a need to secure its growing energy needs abroad. PNG's commodity-based exports accounted for 73 per cent of all the Pacific's exports to China in 2010.

As China increases its foothold in the Pacific, many have questioned whether an overarching military strategy might not be driving it. So far, there is little substantial evidence to support such a fear. In limiting its engagement in Fiji, China has already demonstrated itself reluctant to upset the power balance in the Pacific. There are few incentives for Pacific Island countries to encourage an enduring Chinese military presence in their territories, given that these would be obvious targets in any Sino-American conflict.

The fact that China is yet to reveal military ambition in the Pacific, however, should not be taken as cause for complacency in Australia. Economic and strategic power go hand in hand and, as experience elsewhere has shown (Brautigam 2009), China's global aid strategy is driven primarily by a need to ensure sustained progress in its economic development at home. Establishing global trading links, diplomatic leverage and access to natural resources, is a fundamental part of this strategy. China's regional efforts are deeply strategic and should be taken extremely seriously.

Aid versus Trade with Papua New Guinea

In order to retain its own strategic primacy in PNG, Australia must question the on-going utility of its aid-based approach there. Where Australia's diplomatic standing in PNG has often been affected by the conditions it imposes on its aid programme, China's diplomatic standing in PNG is substantially enhanced by its disinterest in interfering in local government, by the comparatively low administrative burden its development activities create, and by the high level of investment and import demand that accompanies its aid.

Where Australia's official development-based approach does little to dispel unfavourable memories of dependency in the colonial period, China's multi-pronged, but primarily economic, approach is viewed favourably precisely because it comes from a country that has emerged from under-development itself and on its own terms. China is in PNG not because it thinks it can or should "save it", but rather because it sees economic potential that can be capitalised on for mutual benefit. After all, PNG may be a developing country with a massive internal poverty problem, but it will soon enter double digit growth rates and is encountering investment interest from all corners of the world. Official and non-official development assistance pales in comparison to the investment that PNG is currently receiving.

Despite a global recession, foreign direct investment into PNG quadrupled between 2007 and 2009, with annual

inflows increasing from \$96 million to \$396 million⁸. Since then, investment has soared far higher, with a \$16 billion ExxonMobil-led liquid natural gas (LNG) project in the PNG highlands underway and projected to bring an additional \$4 billion into government reserves every year from 2014 to 2042. In the short term, the LNG project alone is predicted by one analysis to double PNG's GDP and triple its export earnings.

By 2007, Malaysia was second only to Australia as a source of foreign investment in PNG, with US\$3 billion primarily devoted to logging. Since then, Malaysia's investments have increased in size and scope, with Malaysian interests active in plantations, malls, shipping, merchandising, insurance, aviation, banking, business and information technology, manufacturing and automotives. South Korea, too, has well-established interests in cement and cassava ethanol production in PNG; and Thai and Filipino companies have staked tens of millions in onshore fisheries processing. A co-venture between Frabelle, Thai Union, and Century Canning is set to open in Lae this year – the factory will be the largest in the country, producing 350 tonnes of canned tuna a day and creating 6000 local jobs in the process.

There is strong interest in PNG to expand its relationship with Indonesia. The security threat that PNG perceived across the border in Indonesia was once a key incentive for maintaining close alignment with Australia, but today PNG's military security is significantly enhanced, and its reliance on Australia reduced, by improving bilateral relations and trade with a democratic and stable Indonesia.

India, too, has strong interest in developing agricultural links with PNG, given the growth opportunities there, and the climatic problems and growing food needs that India faces at home. Bilateral trade is currently only \$120 million, but it is set to increase to \$500 million within the next few years.

Papua New Guinea's International Outlook

Australia has traditionally conceived of PNG as a Pacific state, and PNG's dependence on Australia, a Pacific power, has historically reinforced this. Today, as PNG's economy grows exponentially, the geographic and economic divergences between it and the other Pacific Islands become ever more apparent. Compared to the second largest Pacific Island state, the Solomon Islands, PNG's territory is 16 times larger, its population is 12 times larger, and its economy 13.5 times larger. PNG's economic growth rate is set to move into double digit figures within the next few years. The Solomons' economy is currently growing at around 5 per cent, but when the national logging industry collapses in 2015, growth is predicted to collapse with it. PNG, however, has strong growth potential and economic opportunities significantly enhanced by proximity to Australia and Indonesia, two of the largest and strongest economies in the region.

PNG has emerged from the 2008 global financial crisis as a key investment frontier for the booming economies of

⁸<http://www.gfmag.com/gdp-data-country-reports/201-papua-new-guinea-gdp-country-report.html#axzz1YvZY9z2H>

Asia, and is beginning to perceive a future with much greater ties to Asia. PNG is already a member of the Asia-Pacific Economic Cooperation forum, and has long been seeking full membership of the Association of South-East Asian Nations⁹. With increasing Indonesian support, this bid may eventually meet with success. While PNG continues to play an active role in key regional organisations such as the Pacific Islands Forum and the Melanesian Spearhead Group, its role in regional politics is increasingly confident, assertive and independent (MacLellan 2011). With its national priorities often divergent from those of its much smaller Pacific Island neighbours, it is more than willing to advance its own interests at the expense of collective regional bargaining in local and global negotiations.

Lessons for Australia

The shifts in foreign policy, trade, investment, and aid, signal a significant shift in the capacity of PNG to prosecute its own aims on a rapidly changing global stage. The time is more than ripe for Australia to re-examine its own relationship with PNG. Australian thinking towards PNG is dominated by an aid-security nexus that positions PNG as a foreign dependency, potential security and immigration threat, and aid burden that Australia must stabilise from the top down.

Our relationship has often been marred by political leaders citing the potential for instability to cause PNG's poor to flood across Australia's borders. Even as emerging economies throughout the region pour investment into PNG, Australia continues to negatively conceive of its booming neighbour in terms of proximity, poverty and instability. Where others seek to capitalise on opportunity in PNG, Canberra has often sought to contain it.

Australia's concern about instability in PNG would be legitimate if attempts to help PNG tackle it had been genuine, consistent and successful. They have not. PNG flitters on and off the political radar of our national government as expediency requires. Successive governments have consistently prioritised good governance in PNG, while overlooking the central importance that this paradigm accords to promoting private sector growth.

While Australia's largest mining investments have delivered significant services and employment opportunities at a community level, successive PNG governments have failed to spread the gains of investment at a national level. Rather than being re-invested in job creation, infrastructure, and services, the revenues have been used as an excuse to delay efficiency reforms, and have all too often disappeared into political pockets.

Australian aid dollars have been employed to counteract this poor governance and have been concentrated in attempts to strengthen law and order and the public sector. After more than a decade of this approach, even senior Australian officials admit there is little of substance to show for Australia's efforts¹⁰. The time is ripe for a shift in approach. This reality has been laid bare in successive aid reviews, is increasingly recognised by high-level Australian government officials, and was made abundantly clear by

PNG's new prime minister, Peter O'Neill, at the Australia-PNG Ministerial Forum in October 2011. O'Neill was remarkably frank about the failures of his own country to convert substantial revenues into economic development. He was blunt in acknowledging the pervasive grip of corruption in PNG, and was earnest in explaining his government's determination to combat it.

O'Neill's acknowledgements here were reflective of a surprising humility that has long been absent in the relationship. Such politeness should not be interpreted by the Australian government as an invitation to dictate the terms of future engagement. O'Neill may be determined to get the relationship off on the right foot, but he is equally determined not to repeat the mistakes of the past. O'Neill has made clear that Australia has also had its failings as a development partner in PNG, and has made even clearer his expectation that the relationship will only proceed on equal terms.

O'Neill urged officials to move quickly to commence negotiations on a proposed economic cooperation treaty (ECT), to replace the Partnership for Development that currently serves as the keystone of the bilateral relationship. It is vital that this ECT delivers on promises and expectations and does not consist purely of a motherhood statement on Australia's behalf. In order to capitalise on the significant opportunities for both Australia and PNG to grow through economic cooperation, the treaty must seek to enhance current levels of trade and substantially facilitate and incentivise Australian investment in PNG.

In terms of development assistance, O'Neill expects that, in future, AusAID¹¹ will act in concert with PNG's government, rather than independently of it. Where in the past AusAID's activities have been driven by Australian assumptions of what is good for PNG, in the future O'Neill expects them to align closely with his own government's four-pronged focus on health, education, infrastructure, and law and order.

For more than a decade, AusAID policy and aid dispensations have been overwhelmingly focused on strengthening PNG's law and order and public sector. Various governments in Canberra have tried to improve PNG's governance by attaching reform conditions to aid. The Rudd government diplomatically repackaged the policy as a "partnership" for development. Commitments on improving governance were to be jointly agreed and progress against them was to be jointly assessed. Good performance was to be rewarded with more aid, poor performance with less.

While the theory here is compelling, there is little empirical evidence as yet to suggest that such an approach works in practice. The return on Australia's aid spending remains extraordinarily low, despite more than a decade of aid conditionality designed to counter this. Australia's recent Independent Review for Aid Effectiveness recommended that the Australian government limit the expansion of its aid programme in PNG, given ongoing instability and poor governance that continues to powerfully undermine aid effectiveness.

⁹<http://www.rnzi.com/pages/news.php?op=read&id=45707>

¹⁰<http://www.lowyinstitute.org/Publication.asp?pid=1715>

¹¹AusAID is Australia's overseas aid agency.

Systemic constraints mean that Australia's aid is achieving neither its established purpose of improving governance, nor its more straightforward purpose of improving development indicators. This is something Prime Minister O'Neill has recognised and is something Australia must address. Australia has agreed to align aid with PNG's priorities and narrow the focus of the aid programme to spending on health (including HIV), education, transport infrastructure, and law and justice.

Australia's Options in Papua New Guinea

The Australian government now has two options. The first is to persist with established practice. In this option, we would continue to make development assistance the major focus of our relationship with PNG. We would continue to try to leverage better governance through aid, even as increasing GDP, foreign direct investment and international aid flows minimised the political leverage to be had from that aid. We could continue to use deplorable social indicators and the coming resource boom as a pretext to improve governance in PNG, even after historical experience has shown the limitations of this approach.

Our second option is to become both more realistic and more creative in our approach. We can come to terms with the limitations on intervention in PNG and look beyond the good governance paradigm for ways to effectively reduce poverty. As former PNG prime minister, Rabbie Namaliu, recently pointed out, Australia can make a real contribution to poverty reduction in PNG by helping its agricultural, marine and forestry sectors reach our import standards. This could make a real and sustained difference in rural incomes and welfare, by allowing the benefits of export growth to extend beyond the relatively small number of people employed by the mining sector.

Australia can improve service delivery in its aid programme by engaging to a far greater extent with PNG's numerous active civil society organisations. More co-ordination with them can make a large difference in achieving the aid programme's priorities in health and education. Australia can also help to address PNG's youth bulge problem, by rehabilitating the country's universities as promised, by increasing funding for vocational skills training in PNG, and by expanding and opening our seasonal worker scheme to young PNG adults, who lack access to employment opportunities, venture capital, and work experience.

While increasing the effectiveness of its development assistance to PNG, Australia can also put the diplomatic resources at its disposal to better use in the bilateral relationship. We can improve cultural linkages by increasing funding for popular national sporting exchanges. We can promote an exchange of ideas by making more funded places available in our national universities for Papua New Guineans to study alongside Australians. We can make bilateral visits between cabinet ministers occasions which are frequent and consistent, rather than sporadic and tokenistic. We can make open-ended dialogues the basis of our diplomatic relationship, and leave behind an expectation that warm and productive relationships can automatically result from aid cheques and intermittent photo opportunities.

To break with established practice will be difficult. PNG's government is about to receive billion-dollar windfalls from the Exxon-Mobil LNG project. It will be tempting to invest further in PNG's governance to ensure that these revenues are not wasted. For even as PNG faces a massive revenue boom, there is still a likelihood that PNG's resource blessings will be squandered as they have been in the past. While the minute, isolated and comparatively resource-poor Polynesian states are on track to meet most of the global millennium development goals by 2015, PNG is unlikely to meet any of them. But pressing need does not justify persisting with failed practice. At this point in time we should be questioning not only the capacity of Australia to improve PNG's governance, but also our right to try to do so. If we have learnt anything from the decade that ran from September 11 to the 2011 Arab Spring, it is that efforts to improve governments and governance are most effective when they come from within, rather than being imposed from without. Ultimately, it is the responsibility of PNG's citizens to make the national government answer to them. Corruption is an established and systemic practice that is permitted from the local level up. Aid on its own is unlikely to ever overhaul PNG's governance. Other solutions must be sought and encouraged.

Future Prospects for Papua New Guinea

Australia should take heart at the prospects for locally-driven change in PNG. The recently passed national budget contains the advent of free universal primary education. This is an important step towards nation-building and an informed citizenship that is being significantly aided by rapidly expanding internet and mobile telephony access across the country.

With greater national connectivity there are opportunities for Papua New Guineans to conceive of themselves as an interdependent people, rather than as a haphazard grouping of clans with conflicting and competing interests. There are signs of change in PNG. In August, we saw what appeared to be an entrenched political dynasty dumped in favour of new leadership. Sir Michael Somare had dominated PNG's leadership for a number of periods since independence, serving as prime minister a record four terms in that time.

Somare had been at the forefront of PNG's politics for over 42 years, and is widely viewed as the father of the nation. He is credited with ushering in a period of political stability over the last 10 years that was hitherto unprecedented. In his most recent two terms as prime minister, however, Somare presided over the systemic escalation of corruption in the highest levels of government, alongside a decade-long decline in the country's infrastructure, health and education services. National literacy and mortality indicators worsened, and Somare's conduct revealed him increasingly to be a man who preferred the prestige of office over the responsibilities of it.

The Supreme Court of PNG ruled in December that Peter O'Neill's election as prime minister was unconstitutional and restored Somare as prime minister. The governor-general, Michael Opie, recognised Somare as prime minister and swore in a new cabinet, but O'Neill

rejected the court's ruling and refused to vacate the government benches, instigating a constitutional crisis. The political impasse has been resolved in part by the governor-general switching his support to O'Neill and the public service declaring its allegiance to O'Neill, but Somare continues to claim he is the rightful prime minister.

A positive outcome of the crisis was that an increasing number of young Papua New Guineans became engaged in active debate on the future of the country through social media. It is now clear that there is a constituency of educated young people who want reform in their country.

With the end of the Somare era and with new international forces in play, Australia's government faces the challenge of consolidating the bilateral relationship with PNG while increasingly coming to terms with a new generation of leaders, whose values and expectations of the relationship differ from those of their predecessors. Peter O'Neill is almost 30 years younger than his predecessor. His worldview is not shaped by the pre-independence politics in which Somare's political perspective was formed. As prime minister, O'Neill comes with a character that is far more technocratic than that of his predecessor. If O'Neill follows through on key promises, his leadership could be deemed a decisive break with the Somare era, in both form and substance.

Where Somare allowed government services and infrastructure to flounder, O'Neill has passed legislation to make education free up to Grade 10 and has pledged to: rebuild key highways, the army and the police; enlarge central airstrips in the capital and in Lae; and create a centralised medical supplies base. Where Somare's government and Somare himself became increasingly tainted with graft, O'Neill announced upon election the establishment of an independent commission against corruption and the sale of the government's controversial AU\$52 million private jet. Where Somare's government included only one female representative, O'Neill has passed the first part of legislation that will ensure future parliaments will include at least 22, with a dedicated seat for women in each province. In a country with abysmal health, education, infrastructure, corruption, and gender representation, these are laudable initiatives. But with poor existing mechanisms for service delivery and with national elections due by June 2012, O'Neill will be hard-pressed to implement many of these reforms.

The Australian government appears to have recognised the opportunities that a reformist leader in PNG presents and support of the relationship's new turn is bipartisan and strong. Australia will continue to provide economic advisers and technical assistance to PNG as it moves to establish its sovereign wealth fund, and we will also provide administrative and policing support for PNG's 2012 elections. Australia and PNG also have mutually agreed to revive the policing element of the Enhanced Cooperation Programme of the Howard era.

Julia Gillard has congratulated O'Neill on the steps he is taking to promote gender-inclusive government and has announced her own government's intention to put AU\$1 million towards training PNG's female leaders in

democratic politics. Another promising initiative is the establishment of a public-private committee for senior trade officials and business leaders, which will serve to give momentum and vital industry input into the economic partnership negotiations.

While the Australian government and Prime Minister O'Neill both appear to have seized the initiative, our leaders have set out to accomplish much in an extremely short time. With the low re-election rate that characterises PNG's democracy, there is a strong chance that Canberra will have to acquaint itself with yet another leader following the elections. O'Neill's successors will surely share the confidence and expectations that come from leading a country that is growing, diversifying, and courting an increasing number of global economic and political powers along the way.

Conclusion

With global change occurring in a way that is both incredibly pervasive and extraordinarily fast, developed countries like Australia need to come to grips with an entirely new 'normal' that is neither static nor particularly well understood. They cannot afford to persist with the authoritative stance they assumed in their relationships with developing countries in the past. Dependence is increasingly becoming interdependence, and the dynamics of our bilateral relationships are shifting faster than we know. We can no longer afford to persist with established paradigms that were never productive and are no longer relevant. We have to find new terms of engagement that are based on mutual respect and mutual benefit.

The Author: Jenny Hayward-Jones is director of the Myer Foundation Melanesia Programme at the Lowy Institute. Earlier, she was an officer in the Department of Foreign Affairs and Trade for 13 years, serving in the Australian missions in Port Vila and in Ankara, where she was deputy head of mission from 2004 to 2007. She was a policy adviser in the Regional Assistance Mission to Solomon Islands in 2003-04; and was a member of the election monitoring delegation in the Solomon Islands in 2001. She holds a BA (Hons) in political science (Macquarie) and a MA (Monash) – her MA thesis focused on governance and political change in Vanuatu.

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