AID & DEVELOPMENT IN THE SOUTH PACIFIC

Peter Bauer • Savenaca Siwatibau • Wolfgang Kasper

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WITH COMMENTARIES BY

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Foreword

In November 1989, the Mont Pelerin Society held a Pacific Regional Meeting in Christchurch. One session of that meeting was devoted to the issue of development in the South Pacific. This volume is an edited reproduction of the papers presented at that session by the three main speakers and two commentators.

Above and beyond all its other attributes, this book is remarkably informative. Seasoned observers of the South Pacific as well as those in need of an introductory briefing will find it a useful reference. It will also be useful to those interested in the more general aspects of developing nations, in particular the aspect of foreign aid.

The key to the book's success as a source of information is the different perspective adopted by each author. Savenaca Siwatibau looks at the South Pacific from the inside, as an active practitioner of national and regional policy. He provides the reader with a capsule of information on the strengths and weaknesses of each South Pacific nation and then explores features that they share. This is a very detailed and practical approach. Wolfgang Kasper takes the view of an outsider. Rather than concentrating on the details of individual cases, he stands back from the often confusing array of specific features and looks at the more fundamental forces at work in determining the fate of the region. Peter Bauer takes a similar approach, but limits his analysis to the issue of aid at an international level. However, Professors Kasper and Bauer both pepper their works with an outstanding range of illustrative examples.

The impressive display of information is unlikely to leave the reader with much confidence in the South Pacific. Professor Bauer's analysis of aid leads firmly to the conclusion that 'intergovernmental subsidies, known as foreign aid ... should be terminated', but he sees no prospect that they will be or that aid procedures and practices will be substantially reformed. Professor Kasper agrees that aid as it stands is damaging mostly because it encourages the further development of statism which, in turn, works to discourage growth and development. Mr Siwatibau's detailed list of factors affecting development is also rich with examples of negative influences, ranging from ecosystem overload to inappropriate national financial management.

However, not all is doom and gloom. Mr Siwatibau's list of developmental factors provides the reader with some arenas of potential growth, such as tourism, fisheries, agriculture and mining. But Mr Siwatibau is always careful to add that success will depend on other factors such as the correction of national financial management, reductions in the role of governments, not only domestic ones but, through aid monies, foreign ones as well. His belief that success can be achieved is supported by examples: Kiribati's efforts to reduce government dependence on aid, the attempts by the Fiji government to privatise the Fiji Sugar Corporation, and the participation of nations in the South Pacific Regional Trade and Economic Co-operation Agreement (SPARTECA).

Professor Kasper is also optimistic in his assessment of the potential for successfully developing the region through a program of liberalisation and self-help. He even sees some place for foreign aid, given that there are no prospects for abolishing it and given the application of a series of caveats that he labels the 'Ten Commandments of Foreign Aid'. He is also an advocate of an economic and currency union in the South Pacific, which he sees as a mechanism for avoiding many of the costs faced by small-scale governments.

While Mr Siwatibau and Professor Kasper temper their enthusiasm for their proposals by remaining aware of the practicalities of reform, the two commentators — Colin Simkin and Peter Jennings — both remind the reader of the limitations inherent in development prospects. Professor Simkin is critical of Professor Kasper's proposal for a Pacific union and suggests that 'outsiders ... can hope to have only an educative influence'. Mr Jennings suggests that aid to the South Pacific will continue because both Australia and New Zealand wish to avoid the prospect of having 'slums' develop in their own backyards: hardly an optimistic outlook.

The book is therefore a pessimistic document. Given that it is also informative, it is hard to conclude that the pessimism is unwarranted. All contributors advance compelling arguments for change, most notably for change away from aid dependence and excessive levels of political control and bureaucracy. But equally compelling is their demonstration that the prospects for change are remote. Indeed, there is some expectation that conditions will further deteriorate. For instance, the divergence between growing expectations of higher living standards and the ability of national economies to produce those living standards could cause conflict to grow. The 1987 coups in Fiji, the Kanak uprising in New Caledonia and the secessionist/ land-rights conflict in Bougainville may foreshadow a more violent future for the South Pacific. It is hard, therefore, in the light of a potentially catastrophic future of violent poverty for the region, to give up all efforts to achieve change.

The contributors to the volume do offer some encouragement. Professor Kasper's comments on transport and communication are an example. Making transport in the South Pacific more competitive is something that Australian and New Zealand governments can achieve through their involvements in Qantas (and thus in Air Pacific) and the Forum Line. Furthermore, the opening up of their own ports to competition would assist in two ways: by reducing the total costs of handling transported goods, and through a demonstration effect. Professor Kasper's support for non-government organisations as appropriate vehicles for the delivery of aid funds is also worthy of close examination.

Perhaps most encouraging are the examples of success that Mr Siwatibau cites. Tuvalu is attempting to reduce its dependence on aid through the setting aside of a trust fund similar to that established by Kiribati. Organisations like the IMF, the World Bank, the Asian Development Bank and the EEC are granting aid only on condition that certain policies are introduced. Vanuatu has successfully established itself as a financial centre and Nauru, the Cook Islands and Tonga are attempting to follow suit. Mr Siwatibau suggests that 'the need to deregulate the business environment is gaining recognition' and he cites the example of a nation that has successfully followed IMF guidelines to achieve financial stability after a period of disastrous macroeconomic imbalance.

As Professor Simkin suggests, the role of the outsider is largely one of an educator. To this end he commends the Centre for Independent Studies for advancing the cause of economic liberalism through the publication of its Pacific Papers series. This latest addition to that series makes a valuable contribution to the educational role of the CIS.

Jeff Bennett
Australian Defence Force Academy

Foreign Aid: Mend It or End It?

Peter Bauer was born in Hungary in 1915, and migrated to Britain in 1934. He has held senior academic posts at Cambridge University and the London School of Economics, where he was Professor of Economics from 1960 to 1983. In 1975 he was elected Fellow of the British Academy, and in 1982 he was elevated to the peerage.

His books include: *The Rubber Industry* (1948); *West African Trade* (1954, 1963); *Economic Analysis and Policy in Underdeveloped Countries* (1958); *Dissent on Development* (1972, 1976); *Equality, the Third World and Economic Delusion* (1981, 1982); and *Reality and Rhetoric: Studies in the Economics of Development* (1984). He is the author of the CIS Occasional Papers *Economic Control or Economic Development?* (1990) (which is based on the 1989 John Bonython Lecture), *Population Growth: Curse or Blessing?* (1990) and *The Third World Debt Crisis: Can't Pay or Won't Pay?* (1990).

Foreign Aid: Mend It or End It?

Peter Bauer

I. INTRODUCTION

'Foreign Aid is the central component of world development.'[1] This is what Professor Hollis B. Chenery said in 1981, when he was Vice-President of the World Bank in charge of economic research.

He could not have been right in saying this. Large-scale development takes place in many parts of the world without foreign aid, and it did so long before this policy was invented some 40 years ago.

Although evidently not a central component of development, foreign aid has been since World War II the centrepiece of academic and public discussion on the economic prospects of Asia, Africa and Latin America and on the relation between the West and these regions. Whatever its impact on development, foreign aid has had far-reaching results. For instance, it has brought into existence the Third World (also called the South), as concept and collectivity. Foreign aid is the source of the North-South conflict, not its solution. The primary significance of aid lies in this important political result. It has also promoted the politicisation of life in the recipient countries. These results have been damaging both to the West and to the peoples of the less-developed world. The amount of money spent by the West in no way measures these effects.

II. THE THIRD WORLD AS A WESTERN INVENTION

Discussion of foreign aid[2] envisages the world as being one-third rich (the West) and two-thirds poor (the Third World or South). In this picture, extreme poverty is the common and distinguishing character-

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1. *The New York Times*, 1 March 1981.

2. In accordance with standard practice, foreign aid in this essay refers to official economic aid, i.e. gifts from donor governments to recipients governments, both directly and also indirectly through international organisations. It includes the grant element in subsidised loans. It excludes

istic of the Third World. But statistics in World Bank publications show a continuous range in the per capita incomes of countries. The absence of a distinct break in the series undermines the concept of a Third World demarcated from the West on the basis of per capita incomes. The choice of line of division between rich and poor countries is quite arbitrary. One could equally well say that the world is two-thirds rich and one-third poor.

The picture is misleading also in that many groups or societies in Third World countries, especially in the Far East, the Middle East, South-East Asia and Latin America, are richer than large groups in Western countries. Nor is the Third World stagnant. Both before and after World War II, many Third World countries grew rapidly, including South Korea, Taiwan, Thailand, Malaysia, Singapore, Jordan, Guatemala, Venezuela, Colombia, Brazil, Kenya and the Ivory Coast.

It is not sensible to lump together and average the incomes of the very different societies of the Third World or the South, which comprise at least two-thirds of mankind. What is there in common between say Thailand and Mozambique, Nepal and Argentina, India and Chad, Tuvalu and Brazil, Vanuatu and Nigeria? Their societies live in widely different physical and social environments, and display radically different attitudes and modes of conduct. The Third World includes millions of aborigines and pygmies, and also peoples with ancient and sophisticated cultures, and others employing highly advanced methods of business and technology. It is both misleading and condescending to treat the richly varied humanity of the majority of mankind as if it were much of a muchness, or an undifferentiated, uniform, stagnant mass, a mass, furthermore, which could not emerge from this state without external donations.

Nor is brotherhood a common characteristic of the Third World, as is evident from the persistent hostility and even armed conflict between many Third World countries, including India and Pakistan, Iraq and Iran, Morocco and Algeria, Ethiopia and Somalia, Guatemala and Belize, not to mention the numerous civil wars. It is not surprising that attempts to organise economic cooperation within the Third World have failed, except for collective bargaining with the West over aid and related matters. In fact, this collective bargaining is often organised and financed by the West.

The common characteristic of the Third World is the receipt of foreign aid and not poverty, stagnation, exploitation, brotherhood or

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military aid, private investment and the activities of charities. 'The West' includes Japan, Australia and New Zealand: i.e. it refers to the OECD countries.

skin colour. The concept of the Third World and the policy of official aid are inseparable. The Third World is merely a name for the collection of countries whose governments, with occasional and odd exceptions, demand and receive official aid from the West. This is the only bond joining together its diverse and often antagonistic and warring constituents, which have come to be lumped together since the late 1940s as the underdeveloped world, the less-developed world, the non-aligned world, the developing world, the Third World, and more recently the South.

The Third World is, moreover, a progeny of the West. Aid was introduced and has always been organised by the West. It began with President Truman's Point Four Program of 1949. He urged bold measures to help the less-developed countries where, he said, over half of mankind was living in sickness and wretchedness.

In creating the Third World, the West has created an entity hostile to itself. Some individual Third World countries have been neutral or even friendly to the West, but the organised and articulate Third World is at best critical and more often hostile.

Foreign aid also encouraged the notion of the West (or North) as a single economic decision-making entity, a homogeneous aggregate with identical interests capable of imposing its will on the Third World. In fact, Western governments do not cooperate in setting market prices. And foreign suppliers compete for business in the Third World markets. Obvious examples include suppliers of manufactured products such as cars, trucks and chemical products, and construction and engineering consultants. Manufacturers and commodity traders compete vigorously in the purchase of exports from the Third World.

Foreign aid consists of inter-governmental wealth transfers. To describe these transfers as development aid disarms criticism, obscures issues and prejudges results. It has helped bring about an axiomatic support for this policy.

Who could be against aid to the less fortunate? Aid must be good, more aid better. When aid advocates talk of a disappointing record, they do not mean that aid has been ineffective or damaging. They mean that there should be more of it. If aid were consistently referred to by its appropriate name — that is government-to-government gifts — it would lose much of its emotional appeal. I shall use the terms gifts, transfers and aid interchangeably, and occasionally refer to aid recipient countries; but it should be remembered that the recipients of official aid are always governments.

Axiomatic support for aid helps to explain many anomalies.

Western aid has gone to governments explicitly hostile to the West, such as those of Ethiopia, Vietnam and Cuba, which have pursued policies plainly damaging to the West and to other recipients of Western aid; to governments at war with each other; to governments whose policies created refugees and to governments of countries who have taken them in (at high costs and with resultant tensions);[3] to governments that severely restrict the inflow of capital, the shortage of which is said to be the ground for aid; and, more generally still, to governments pursuing policies which plainly retard economic advance and damage the interests of their poorest subjects.

III. AID AND DEVELOPMENT

Although the case for aid is largely taken for granted, various arguments and rationalisations are advanced. In this essay I examine the three most often heard and influential of these arguments: promotion of development; relief of poverty; and furtherance of the political and economic interests of the donors.[4]

Since its inception in the early post-war years, the central argument for foreign aid has been that without it Third World countries cannot progress at a tolerable rate, or at all. In fact, external donations

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3. Two recent examples are the flow of refugees from Vietnam to other South-East Asian countries, e.g. the Philippines, Malaysia and Indonesia, and from Ethiopia to the Sudan. The governments of all these countries have simultaneously received Western aid throughout the relevant period.

4. In the text I examine the three most persistent and widely-canvassed arguments for aid. Besides these, numerous secondary and ad hoc arguments and rationalisations emerge from time to time, such as the restitution for past wrongs, global redistribution and compensation. These arguments shift with the vagaries of politics and with the audiences addressed. The arguments hinge on the assumption that aid promotes development or relieves poverty. They therefore fall away when these assumptions are shown to be untenable, as they are in the text of this essay. Moreover, they are insubstantial in their own right, so to speak. I have reviewed them at length in Chapter 5 of my *Equality, The Third World and Economic Delusion* (1982), entitled 'Foreign Aid and Its Hydra-Headed Rationalisation'. A fairly new, but now very influential, argument is that aid is necessary to alleviate the burden of Third World debt. Even more recently, aid is being advocated also to enable Third World governments to fight the drug traffic, protect the environment and preserve endangered species. Even the African elephant has been pressed into the service of foreign aid.

   I should like here to consider briefly one persistent and recurrent theme of the literature of foreign aid and cognate subjects. This theme is that there have never been necessary for the development of any society anywhere. Economic achievement depends on personal, cultural, social and political factors, that is, people's own faculties, motivations and mores, their institutions and the policies of their rulers. In short, economic achievement depends on the conduct of people and their governments.

It diminishes the people of the Third World to suggest that, although they crave for material progress, unlike the West they cannot achieve it without external subsidies. Much of the Third World progressed rapidly long before foreign aid — witness South-East Asia, West Africa and Latin America. Large parts of these regions were transformed in the 100 years or so before aid. There are, of course, Third World societies which have not progressed much over the last 100 years. This lack of progress reflects factors that cannot be overcome by aid, and are indeed likely to be reinforced by it.

The Minor Role of Increase in Capital

The argument that aid is necessary for development rests on the belief that the volume and the cost of capital are critical for economic advance. If this were so, how is it that large numbers of very poor people could have become prosperous within a few years without external donations, as they have done the world over, as for instance originally very poor immigrant communities in North America and South-East Asia? To have capital is a result of economic achievement,

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is a long-term tendency for the terms of trade of Third World Countries to deteriorate, and that therefore aid from the West is required as a form of redress. In so far as aid does not promote development or help the poor, the argument is irrelevant. It also begs the question why governments have not set aside resources to provide against adversity at times when terms of trade have been more favourable. Moreover, the allegation of persistent deterioration of the terms of trade of Third World countries is altogether unfounded. It is doubtful whether there is any sense in averaging the terms of trade of such a highly diverse aggregate as the Third World. It can always be suggested, by choosing particular years, commodities and countries, that the terms of trade of Third World countries have deteriorated. In so far as averaging or aggregating Third World terms of trade is at all sensible, it is worth noting that by historical standards the commodity terms of trade of this collectivity have been distinctly favourable since World War II. Changes in the more relevant indicators have been even more favourable: these indicators allow for changes in the real cost of exports, the improvement in the range and quality of imports and the huge expansion in the volume of trade. The aggregate real purchasing power of the Third World over imports has expanded very greatly in recent decades.

not its precondition.

Much recent research by leading scholars, including Simon Kuznets, has confirmed that increase in capital played a minor role in the economic advance of the West in recent centuries. Moreover, these findings refer to capital formation. They apply even more to the significance of the volume of investible funds because much spending, conventionally termed investment, does not result in productive capital formation. Furthermore, the findings refer to capital formation in societies in which social and political conditions were helpful to economic achievement.

The Role of Private Investment

Whatever contribution capital can make to development can be secured without aid. To begin with, direct investment from abroad is likely to flow into areas in which capital can be employed productively. Externally financed plantation, mining, trading and other commercial enterprises have been established in many parts of the less-developed world in apparently unpropitious conditions in the absence of a hostile social and political climate. The inflow of this type of capital has been accompanied by an inflow of technical and administrative skills, and it encouraged new ideas and methods of production. As part of their operations these enterprises, notably banking and trading companies, have also financed small-scale local farmers and traders. Foreign direct investment played a large part in the economic progress and transformation of much of South-East Asia, Africa and Latin America in the 19th and 20th centuries.

Direct investment apart, enterprises and governments in the Third World capable of using capital productively can readily borrow commercially abroad as well as at home. Both before World War II and since, the thousands of enterprises in the less-developed world that advanced from very modest beginnings to considerable size and prosperity readily found the necessary capital. Even in the very poor Third World countries, small-scale producers have had access to external funds. For instance, Western and Levantine trading firms have regularly lent substantial amounts of money to trustworthy African borrowers. Ability to borrow does not depend on the level of income, but on responsible conduct and the ability to use funds productively.

Third World governments have also been able to borrow readily, even too readily, from international banks. This also applies to borrowing for facilities that do not yield a directly appropriate return.

If such spending, often known as infrastructure spending, is productive, it increases national income and thus taxable capacity, so that governments can readily service the borrowed capital.

As both Third World governments and enterprises who can use funds productively and conduct their finances responsibly can secure external funds, it follows that the maximum contribution of aid to development cannot exceed the avoided cost of borrowing, that is, interest and amortisation charges as percentage of the national income. The most that aid can do for development is to reduce the cost of a resource which is not a major independent factor in the development process. For large Third World countries these benefits must be modest, even minimal, and far too small to affect any macroeconomic aggregate. For instance, for India in the early 1980s this benefit would have been of the order of between one quarter and one half per cent of recorded GNP.

Aid and the Growth of Government

It may be thought that even such modest contribution to development is worthwhile: the recipient countries must derive some benefit from the inflow of resources while the donors can afford to give away a small proportion of their incomes. This prima facie plausible reasoning overlooks the adverse repercussions of official wealth transfers. These repercussions arise because, unlike manna from heaven, aid does not descend indiscriminately on the population at large, but goes directly to the government.

It is because aid accrues to the government that the latter increases its resources, patronage and power compared with those of the rest of society. The resulting politicisation of life enhances the hold of the governments over their subjects and increases the stakes, both gains and losses, in the struggle for power. This result in turn encourages or even forces people to divert attention, energy and resources from productive economic activities to concern with the outcomes of political and administrative processes and decisions. This sequence provokes tension which often erupts in armed conflict, especially in countries comprising different ethnic and cultural groups. Such sequences must inhibit economic advance because the deployment of people's energies and resources necessarily affects the economic performance of a society. Foreign aid has not been the sole cause of the politicisation of life in the Third World, but it has contributed significantly to the process.

Foreign aid has also helped or enabled many recipient governments to pursue policies that plainly retard growth and exacerbate poverty or even misery. The long list of such policies includes: persecution of the most productive groups, especially ethnic minorities, and sometimes their expulsion; suppression of private trade, and at times destruction of the trading system; restriction on the inflow of foreign capital and enterprises; extensive confiscation of property including forced collectivisation; voluntary or enforced purchase of foreign enterprises which absorb scarce capital and deprive the country of valuable skills; price policies which discourage agricultural production; expensive forms of support of unviable activities and projects, including subsidised import substitution; and the imposition of economic controls which, among other adverse effects, restrict external contracts and domestic mobility and so retard the spread of new ideas and methods. Many aid recipients regularly pursue several of these policies; the Ethiopian government pursues all of them.

Such policies, singly but much more so when pursued together, impoverish people and even cripple the economy. Vietnam, Ethiopia, Tanzania and Uganda are conspicuous examples of the pursuit of such policies. These policies often directly provoke conflict, even armed conflict, the effects of which are exacerbated by the neglect of public security and of the protection of life and property, which in the Third World often goes hand-in-hand with ambitious, far-reaching policies.

The policies just recited are often said to be mistaken in the sense that they would not have been adopted if policy-makers had recognised their likely consequences. This view is at best a serious oversimplification. Most of the policies are pursued because they accord with the purposes and interests of the ruling group. These purposes may include the promotion of governmental power, the satisfaction of politically effective pressure groups, and the provision of financial rewards to politicians, civil servants and their allies. The pursuit of many of these policies is therefore not irrational in the accepted meaning of the term, although if carried too far they may prove counterproductive and undermine the position of those in power. To describe them as irrational or misguided is to imply that the policy-makers are engaged in the single-minded pursuit of increasing general economic and social welfare.

A number of governments pursuing such policies, most obviously in Africa and Asia, could not have survived without Western aid, which has even increased substantially in the face of such destructive policies. This situation throws into relief a conspicuous anomaly. Recorded per capita income is a major factor in the allocation of much

Western aid. This applies for instance to British aid and to the large amounts of aid distributed by the International Development Association, an affiliate of the World Bank. On this criterion, governments pursuing destructive policies can qualify for more aid. Paradoxically, aid allocated on the basis of per capita incomes rewards policies of impoverishment. This is evidently so for aid given direct to governments. It applies also to project aid. Such aid will be accepted only if the project fits in with the overall objectives of the government. And generally it enables the recipient government to spend more in pursuit of its general policies.

Aid and the Balance of Payments

Another factor affecting the allocation of aid has been actual or anticipated balance of payments difficulties. The application of this criterion has encouraged policies adverse to development. Confidence that balance of payments difficulties will attract further aid encourages financial profligacy, notably inflationary policies. These policies are often accompanied by exchange and other controls. Inflation, payments difficulties and controls engender tension and insecurity, even a crisis atmosphere, thereby inhibiting domestic saving and productive investment and encouraging a flight of capital.

Some other untoward effects of aid may rate brief mention. Official transfers have often biased development policy towards unsuitable external models. Subsidised import substitution, construction of petrochemical complexes and state-owned airlines are familiar examples. Adoption of external prototypes in development policy has often gone hand-in-hand with attempts at more comprehensive modernisation. Such efforts have included attempts to transform people's mores, values and institutions, attempts that in turn have invited backlash and conflict. It is ironic that governments that engage in ambitious programmes and projects of these kinds have simultaneously neglected the basic functions of government, including the most basic of all, namely, the protection of lives and property.

Finally, there is a further adverse result, the exposition of which is slightly technical. The inflow of aid funds drives up the real rate of exchange, and adversely affects foreign trade competitiveness. This effect can be offset to the extent that the subsidised transfers enhance the overall productivity of resources. For various reasons, such enhancement is unlikely in practice. In any case, it can occur only after a time lag of years. Meanwhile the higher real exchange rate makes for continued dependence on external assistance. This particular effect of aid follows from the well-established proposition of international trade theory that an inflow of capital appreciates the real exchange rate.

Aid's Asymmetrical Effects on Development

Aid involves a double asymmetry in its effects on development. First, any favourable effect is on a resource that is not critical for development. The adverse effects, on the other hand, operate on critical determinants, primarily political and cultural determinants. Second, an amount of aid that is too small to benefit development appreciably can nevertheless bring about adverse effects. It is the relationship of aid to GNP that is relevant to the favourable effects, namely, the reduction of the cost of investible funds. And because aid goes to governments, it is the relationship of aid to government receipts and to foreign exchange earnings (themselves readily subject to government control) that is relevant to the adverse repercussions.

Aid is necessarily much larger relative to tax receipts and foreign exchange earnings than it is to the national income of the recipients. Indeed, the differences in these ratios are striking. I calculated them for the year 1980 for India and Tanzania, the leading aid recipients in Asia and Africa. For India, aid was 1.6 per cent of recorded GNP, 16.8 per cent of tax receipts and 31.2 per cent of export earnings. For Tanzania, the corresponding figures were 18.1 per cent, 106.8 per cent and 152.8 per cent. Thus, for both countries aid as a percentage of tax receipts and foreign exchange earnings was a large multiple of its percentage of GNP. The multiple becomes larger still when it is remembered that while statistics of tax receipts and foreign exchange earnings are reasonably reliable, the statistics much understate the GNP of Asian and African countries.

Thus, an amount of aid which, at best, could bring about an insignificant increase in income per head, could greatly increase the resources directly available to the government. And it is the latter increase that brings about the adverse repercussions.

Some Irrelevant Evidence in Favour of Aid

The progress of the recipient countries is often instanced to demonstrate the effectiveness of aid. This evidence is in fact irrelevant. However substantial the progress of an aid recipient country, the contribution of aid can never exceed the avoided cost of borrowing the investible funds as percentage of GNP. And the cost and volume of these funds are not critical for development. Moreover, the adverse repercussions still operate.

The establishment and success of individual projects financed by aid are also often instanced as evidence of its value. This again is irrelevant. When such projects promise to be productive they can be financed by government or private enterprise without aid, so that its contribution is again limited to the avoided cost of borrowing. The idea is unwarranted that such activities and projects could not have taken place without aid. Third World governments financed infrastructure projects long before foreign aid. Similarly, there were privately-financed plantations, mining, manufacturing and transport enterprises in many parts of Asia, Africa and Latin America long before there was aid. And projects financed without aid are more likely to be productive because they are usually more closely geared to market conditions and to the surrounding social scene.

The success of the Marshall Plan in the early post-war years is frequently evoked in support of aid to the Third World. This analogy is altogether misleading. After the war the economies of Western Europe had to be revived, not developed. As was clear from pre-war experience, the personal, social and political factors congenial to economic achievement were present in Western Europe. Moreover, recent research suggests that Marshall aid played at most a minor part in the recovery of the economy of the Federal Republic of Germany. This finding accords with expectations. In any event, Marshall aid to Europe was terminated within four years of its inception, and Germany then became an exporter of capital and soon thereafter a major source of foreign aid. This experience contrasts with suggestions that official aid to the Third World will have to continue for generations, and at least into the 21st century.

IV. AID AND POVERTY

Relief of poverty is the second major proclaimed purpose of foreign aid. This is the objective that most appeals to genuinely compassionate people in the West. But aid does not go to the pitiable figures of aid advocacy. It goes to the governments, that is, to the rulers. These rulers are often directly responsible for the misery of their subjects. But even when this is not so, it is still the case that aid goes to the rulers whose policies, including the pattern of public spending, are determined by their own personal and political interests, among which the position of the poorest has low priority.

Over most of the Third World there is no machinery for relief of poverty by the state. Even if a recipient government wanted to use aid to help the very poorest, this could be difficult, even impossible. What is more important, such help may not accord with the political or personal interests or ideological priorities to Third World rulers, or indeed with local mores. In fact, it often conflicts with these priorities and mores. This situation is evident in multiracial, multi-tribal or multicultural countries. An Arab-dominated Sudanese government will not help the poorest blacks in Southern Sudan, hundreds of miles away, and with whom it is in persistent armed conflict. The rulers of Ethiopia will not help the people of Tigray whose distress is caused or exacerbated by the military action of the government. In Sri Lanka, a Sinhalese-dominated government is unlikely to help the Tamil poor. Such examples can be readily multiplied.

In the context of aid for development, I have already recited a long list of policies that affect development adversely. These policies also exacerbate poverty. I have noted also that the allocation of Western aid rewards impoverishment. Indeed, the more damaging the policies, the more acute becomes the need, and the more effective become appeals, for aid. The experience of Ethiopia and the Sudan in the early 1980s makes this clear. The destructive policies of these governments have been largely responsible for the mass misery that in turn has been so effective in eliciting large sums of both official aid and private charity.

In many aid recipient countries it is the poorest who are worst hit by policies such as enforced population transfers, suppression of trade, forced collectivisation and also by the civil wars and other forms of breakdown of public security. These policies and conditions have forced large numbers of people to rely for their existence on precarious subsistence production, the hazards of which have become particularly plain in Africa.

There are also many less extreme instances of wasteful policies. The poorest do not benefit from brand new capitals, such as Brasilia, Islamabad, Abuja, Lilongwe or Dodoma. And they do not benefit from the international state airlines throughout the Third World, including countries such as Burundi and Laos, where the vast majority of people do not use airlines and local people cannot fly them. Many of these projects and enterprises have to be subsidised by local taxpayers.

Spending on show projects and the presence of rich people in Third World countries in which there are many extremely poor people make clear that the rulers, while demanding external donations in the name of relief of poverty and international redistribution, are not much interested in helping their poor. They are interested in redistribution if it advances their own personal and political purposes, as for instance expropriation of the wealth of their political opponents or of politically unpopular groups.

While external donations can do little or nothing for development of relief of poverty, they can relieve immediate shortages, especially of imports. This enables governments to pursue even extremely damaging policies for years on end because this result of the donations conceals from the population, at least temporarily, some of the worst effects of these policies. In such conditions continued Western aid also tends to suggest endorsement of these policies, which confers spurious respectability on those who pursue them. It has been widely and rightly recognised that Western aid has kept afloat African rulers pursuing destructive policies, thus enabling these rulers to persist with these policies.

The obvious question arises whether donor governments could use aid to help the poorest either by influencing the policies of recipient governments or by channelling funds directly to the poorest.

The attempts by Western donors to influence the policies of the recipients have been half-hearted and ineffective. For instance, the governments of Ethiopia and the Sudan have successfully resisted the rather unenthusiastic attempts of Western donors to induce these governments to modify their harshest policies. In 1984 the government of Ethiopia stated emphatically that Western aid and voluntary charity must conform to their own policies. Third World governments have insisted both that the distribution of aid must conform with their own policies, and as far as possible must be distributed under their own auspices.

V. AID AND WESTERN INTERESTS

The third major argument envisages aid as serving the political and economic interests of the West.

According to one variant of the argument, without aid the Third World will drift into the Soviet camp, or in other ways go against Western interests. This argument is insubstantial. About one-third of all Western aid is channelled through official international agencies. In the allocation of funds, these organisations are not permitted to take into account the political interests of donors. Moreover, the Soviet Union is represented in the United Nations and can thus affect the direction of substantial multilateral transfers under United Nations programs, though its own financial contribution is negligible. Indeed, practically all Soviet non-military aid is channelled to client states, notably Cuba, North Korea, Vietnam, South Yemen, Ethiopia and Afghanistan. These countries have simultaneously received aid from the West.

The political interests of the West are also ignored largely in direct transfers between donor and recipient governments. Aid administrators are rarely qualified to know how to promote Western political interests and are often not inclined to do so. More generally, if official transfers were to serve Western political interests, they would need to be geared both to the political or military significance of the recipient countries and to the conduct of the recipient governments.

Many aid recipient countries, most obviously in Africa and the South Pacific, but also in Asia and Latin America, are of no political or military significance. And many aid recipient governments are openly hostile to the donors whom they abuse, embarrass and thwart as best they can. At times they do so to assert their independence from the donors. Some aid recipients are also hostile to the market system and sympathetic to the Eastern Bloc of controlled economies. Whatever the reason, many aid recipients have since the earliest days of aid opposed and denigrated the donors, even when their own political survival depended on subsidies from these donors. The West feeds the mouths that abuse it. Many Third World rulers have derived their aid from the West, but their ideology and political stance from the East. Examples range from Nkrumah in the 1960s to Nyerere and Mengistu in the 1980s.

According to another variant of the political argument, the poverty and stagnation in the Third World countries, endemic without aid, would bring to the fore populist, nationalist or communist governments hostile to the West, especially to the United States. This argument assumes that foreign aid is necessary or helpful for development and relief of poverty, and also that support for anti-Western politicians depends on low levels of income and low rates of growth. Neither of these assumptions is sound, as should be obvious from modest reflection and observation.

The advocates of the argument that aid promotes Western prosperity, or is even necessary for it, claim that this policy increases purchasing power in the Third World, advances growth there and thereby promotes exports and employment in the West. This argument is a major theme of the Brandt Report. The argument is, moreover, invalid even if aid increased incomes substantially. Exports bought with the proceeds of foreign aid are given away. It is sophistry to argue that people who give away part of their wealth are better off or will be better off. An enterprise does not prosper if its owners give away money to people who later may buy its products with the money they have been given.

Of course, special groups in the donor countries often benefit from aid. For instance, the supply of ships, financed by British aid, to India, Poland and Vietnam in the 1970s benefited labour, management and shareholders in British shipyards. But the government funds involved could have been used for other forms of so-called employment creation. The ships could also have been sold to the highest bidder or given away to British owners.

Similarly, aid to the Third World will not alleviate unemployment, recession and de-industrialisation in the West. If these real or alleged ills could be alleviated by government spending, this could be achieved more effectively by more spending at home. Domestic spending is much more effective in maintaining or increasing employment than giving money to distant governments. Moreover, any assets created by domestic spending remain at home.

Often, spending on aid can aggravate domestic unemployment, for instance by diminishing the volume of productive investible funds, an outcome that reduces employment, opportunities and incomes where these depend on domestic spending.

In sum, the idea that aid helps the economies of the donors simply ignores the cost of the resources given away.

VI. REFORMING FOREIGN AID

I have argued that the intergovernmental subsidies known as foreign aid are more likely to inhibit than to promote Third World development and relief of poverty. It should be terminated. But this is impractical, partly because of the momentum of existing commitments, and partly because of the influential and articulate interest groups involved. There are certain reforms that, if implemented, could bring the operation of these transfers closer to the proclaimed objectives of aid.

The first and most important single reform would be to change radically the criteria of allocation. The subsidies should go to those governments whose policies are most likely to promote the economic progress and general welfare of their peoples through humane leadership, effective administration and the extension of personal freedoms. Such a reform would remove the most conspicuous anomalies of official aid, and enable it to make whatever contribution it can to improve the condition and prospects of the poorest.

Second, official aid should be bilateral, not multilateral: that is to say, it should go direct from donor government to recipient governments rather than through the international organisations. This would permit at least a vestige of control by the elected representatives of the taxpayers who are the real donors. In multilateral aid there is not even a semblance of control by the donors.

Third, to serve its proclaimed purposes aid ought to be untied, that is, separated from the purchases of exports from particular donors. Subsidies to Third World governments could then be distinguished from subsidies to exporters of bankers in the donor countries.

Fourth, aid ought take the form of grants rather than subsidised loans. Such loans confuse donations with investment and set up tensions between donors and recipients. Moreover, when tied aid and subsidised loans are linked, as they often are in practice, it becomes quite impossible to ascertain who gets how much and from whom, that is, whether and to what extent the taxpayers of the donor countries subsidise the aid recipient governments rather than exporters and bankers in their own countries.

Such proposals for reform may be worth reciting but they will not be implemented. That is so because not only is the policy of foreign aid supported by powerful interests, but the existing methods, arrangements and practices also benefit powerful and vocal special interest groups. These include the national and international aid organisations and bureaucracies, notably the World Bank, the International Monetary Fund, the United Nations and its offshoots, as well as its regional commissions in Asia, Africa, and Latin America; churches and other aid lobbies; and the commercial beneficiaries of aid transfers.

There is, therefore, no realistic prospect in the foreseeable future of substantial reform of the procedures and practices of official aid, including the methods of allocation.

Some Aspects of Development in the South Pacific: An Insider's View

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Some Aspects of Development in the South Pacific: An Insider's View

Savenaca Siwatibau

I. AN OVERVIEW OF THE SOUTH PACIFIC COUNTRIES

The island countries of the South Pacific display a wide diversity of physical and economic characteristics (see Tables pp. 40-44 below). At one extreme, **Papua New Guinea** (PNG) is a large rugged country with a population of about 3.6 million and a land area of 462 840 square kilometres. It is endowed with rich mineral deposits, and its enclave mineral sector dominates its economy. The external sector, GDP, and the government's fiscal position are highly sensitive to developments in the mineral sector. PNG is also well-endowed with good soil, forests and abundant living resources within her Exclusive Economic Zone (EEZ). At the other extreme are the small atoll countries such as **Tuvalu**. This country has a population of only 8500 and an area of only 26 square kilometres. Its soil is poor and its population relies heavily on marine products for its livelihood.

Vanuatu, the **Solomon Islands** and **Fiji** are, like PNG, made up of larger, rugged mainly volcanic islands that are relatively rich in natural resources. They have fertile land, timber and minerals. Gold is an important industry in Fiji. Deposits of gold with a potential for commercial development have been located in the Solomon Islands and in Vanuatu. Similarly, the potential of the sea has yet to be fully developed.

These countries actively promote manufacturing by fiscal means. Concessions granted to manufacturing industry are generally related to the level of employment, foreign exchange generation or conservation and the extent of local equity participation. Manufacturing is highly protected in these and other Pacific island countries.

These countries have the potential to achieve economic viability and independence. But this will depend on a number of preconditions being fulfilled, including sound macroeconomic management and enlightened commercial policies that help release the initiative and energies of the private sector.

Micronesia and **Polynesia** (situated in the North, North-West and East Pacific) are made up of groups of smaller islands. A few of these islands have rich soils, but most of them are small, isolated atolls with poor soil. Forestry is important only in Samoa. While marine resources are relatively plentiful in these countries, the likelihood of finding mineral deposits is reportedly remote.

Tonga, Western Samoa and the **Federated States of Micronesia (FSM)** have the potential, given appropriate adjustment policies, to achieve economic independence over time. They too are heavily dependent upon external trade and finance; their exports exceed their imports by wide margins. They are heavily dependent upon aid and, in the cases of Tonga and Western Samoa, remittances. In Tonga, remittances are currently running at more than 300 per cent of exports and 50 per cent of imports. The corresponding figures for official aid are 200 per cent and 33 per cent. Similar ratios of remittances and official aid to exports and imports apply to Western Samoa. The FSM, under the Compact of Free Association with the USA, has assured inflows of funds over the medium term, and have good prospects for increased trade with Japan particularly through exports of high quality tropical fruits and vegetables and, possibly, processed agricultural products. These countries have good soil but other natural resources are relatively limited. The prospects for finding minerals in these countries are also limited, but it has yet to be determined whether minerals exist under the sea bed, as in other island countries. Prospects for agricultural diversification, and for further development of their subsistence sectors, are good. Prospects for the tourist trade are also promising. Manufacturing is accorded priority in these countries; Tonga already has a well-managed industrial estate with a number of successful private ventures that compete effectively in the export markets.

The **Cook Islands, Kiribati, Tuvalu, Niue**, and the **Marshall Islands** have broadly common characteristics. Aid inflows are particularly important to these countries. The Marshall Islands, like the FSM, receives substantial grants under the Compact with the United States. It also receives a substantial injection of funds through the lease of the Kwajalein base to the US government and from the earnings of local people who work there for wages comparable to those paid in the US. The country's economic dependence upon the US is very high.

These countries are made up of atoll islands and cover a relatively small area. Population growth rates are high in the Marshalls and Kiribati but are relatively low in Niue, the Cook Islands and Tuvalu, partly because, in the case of Niue and the Cook Islands, of unrestricted migration to New Zealand. These countries are resource-poor; land is scarce and of low quality. Minerals are absent, but the discovery of mineral deposits under the sea bed within their EEZs cannot be ruled out. Imports exceed exports by wide margins, and by more than five times in the case of Kiribati, the Marshall Islands and the Cook Islands. Their high levels of consumption are sustained through remittances in the cases of the Cook Islands, Niue and Tuvalu and through aid in all cases. The level of dependence upon external aid is very high. Prospects for launching viable projects and programs are relatively limited and the current level of consumption and welfare is sustainable only through continuing aid.

The level of economic activity in the money sectors of these countries is determined by: the external prices of copra and other minor crops; the inflow of remittances and aid; rent on the use of fishing rights within the EEZs; overseas investments by financial institutions; and, in the cases of Tuvalu and the Cook Islands, earnings from the sale of commemorative stamps.

II. COMMON CHARACTERISTICS OF THE SOUTH PACIFIC COUNTRIES

The economic adjustments necessary for self-reliance will not be easy for most island countries. The process requires difficult political choices which in the short term may necessitate a decline in living standards.

Most of the countries of the South Pacific achieved independence over the last 25 years. They have taken their places in various international forums. They communicate as a group or individually with other nations, large and small, on an apparently equal footing. But in a rapidly changing domestic and global environment they are having to observe that:

- popular aspirations rise at an ever faster rate. People want more and more for less and less;
- what may be economically sound is politically difficult to put in place;

- external shocks impact with great speed upon their fragile economies and the necessary adjustments that such shocks demand are politically and socially painful to put in place. It is tempting to bypass such adjustments and other adjustments required to ensure long-term growth and development by relying on the goodwill and generosity of benevolent and economically stronger neighbours;

- political independence is one thing, economic independence quite another.

A number of physical and economic characteristics bearing upon the development prospects of the Pacific island countries are common.

- Production bases are very narrow, with heavy reliance upon a limited number of export items. Export markets are also narrowly concentrated.

- External and internal shocks, produced for example by export price variations and devastations by hurricanes, are frequent. They generate fluctuations in exports, GDP, consumption, revenue, the current account of the balance of payments and external reserves.

- Economic activities are subject to extensive regulation by the authorities.

- The ratios to GDP of imports and exports of goods and services are large.

- External sector positions are fragile. But for the substantial volume of aid receipts and remittances by overseas residents, most Pacific island countries would experience persistent and unsustainable current account deficits.

- Political and social instability appears to have increased in recent years. This trend may be a function of rapidly rising aspirations that cannot be matched by economic performance and of an apparently growing conflict between slowly evolving cultural and traditional norms on the one hand and, on the other, the necessity for rapid changes in a modern world where effort, efficiency and merit are essential for the satisfaction of aspirations.

- Capital moves in and out freely despite the exchange controls that most island countries, apart from Vanuatu, have in place.

- Island countries, particularly those located South of 10 degrees S and North of 10 degrees N, are exposed to frequent hurricanes. The devastations brought about by such hurricanes have, at times, been catastrophic.

- Domestic markets are relatively small. They are also highly fragmented, since settlements are separated either by rugged terrains or by large expanses of sea.

- External markets are remote. This, together with relatively low volumes of production, results in high unit costs for transportation and marketing.

- Population growth rates are relatively high for most islands, except the Cook Islands, Niue, Tonga and Western Samoa, where emigration has featured prominently in recent years.

- Skills are in short supply at all levels.

- A fragile physical environment is characteristic of small island states.

- Wage levels are relatively high, particularly when compared to low productivity. This situation reflects the lack of skills at all levels and the highly-regulated labour market in a number of countries.

- The role of the public sector in the economy is pervasive and dominant. The public sector, which tends to dominate the economy, is invariably the largest employer. It generally sets the pace for national wage and salary settlements. This role has not always been conducive to the growth of the private sector, particularly where the high level of public sector wages and salaries is supported directly or indirectly through aid receipts.

- The mobilisation of domestic resources for investments is not always supported by appropriate fiscal policies. Regulations in the financial sector appear to have adversely affected the growth of private sector savings and the efficient flow of resources into classes of investments that yield the best returns.

- Per capita aid to the region is high. The level of financial resource flows to the Pacific island countries has apparently not been among the constraints against development in the region. Supportive domestic policies, needed to ensure the maximum returns from such flows, are probably lacking.

- Difficult land tenurial problems remain to be satisfactorily addressed, particularly in parts of Melanesia.

- Annual economic growth rates have fluctuated widely and have on average been very low; they have been consistently lower than growth targets envisaged in development plans. Given the high population growth rates in most of the island countries, the standard of living has not improved or has declined in a large number of island countries over the last ten years.

III. FACTORS AFFECTING DEVELOPMENT

Ecosystems

Accelerated development in Pacific island countries is often accompanied by extensive exploitation of natural resources that harms their fragile ecosystems.

An integral component of sound economic growth in the long term is careful management of the environment on a sustainable basis. This requires an appreciation of the delicate balance that needs to be achieved in the management of the life-support systems such as air, soil and water, as well as such natural communities as rainforests, mangroves, coral reefs, and deep sea marine life. Concern has increased in recent years over the threats that development activities pose to the long-term viability of these natural communities. When the South Pacific Regional Environment Programme (SPREP) was being formulated in 1980/81, the 22 member nations identified at least 14 major environmental issues. The list has grown in recent years.

Damage to ecosystems arises from both domestic and external factors. Some environmental problems may be addressed by domestic policy; these include soil erosion, mining damage, extraction of sand and gravel, fresh water shortages and water pollution, deforestation, endangered species, land use, coastal erosion and land reclamation, mangrove eradication, overfishing in inshore waters, coral reef destruction, use of toxic chemicals, disposal of liquid and solid wastes, and rapid population growth on islands with limited carrying capacity. Those problems that must be addressed by external authorities include increased radioactivity (e.g. through nuclear weapons tests), toxic and nuclear waste dumping, driftnet fishing, and the impact of the greenhouse effect on the sea level.

It is likely that the persistent neglect of environmental issues could, over the long term, frustrate the economic development of many resource-poor Pacific island nations; the experience of the people of Banaba is illustrative. The current deforestation — whether for expanding human settlements, for agriculture or for timber extraction — may, without sound management, result not only in increased soil erosion but also in the loss of a whole range of species comprising the forest ecosystem. Environmental scientists tell us that Pacific Oceania has one of the highest rates of indigenous species in the world: they also claim that it has one of the highest species extinction rates in the world. The loss of many rare species of plants and animals means the loss to the region and to the world of important organisms that are potential sources of food and medicine in the future. The loss of forest ecosystems deprives the island landscape of a distinctive feature with important tourist industry potential. Sound management of the environment should therefore be an important component of development strategies in the island countries.

A sustainable development path for the island countries with stable physical and biological environments may not, in the long term, be achievable without the willing cooperation of countries outside the region. Driftnet fishing threatens the ocean resources upon which the Pacific island economics heavily depend. The greenhouse effect could mean, perhaps in the next century, the wholesale relocation of the populations of small nations such as Kiribati, Tuvalu, Tokelau and Marshall Islands. Radioactive pollution, though perhaps localised in its impact, could have secondary impacts that are perhaps still not extensively studied.

The issue of radioactive pollution is part of a larger concern over what appears to be growing militarisation in the region: a trend that reflects the strategic importance of the Pacific. If this trend continues the island countries will need to continually assess how changes in the global balance of power will impact upon their long-term development prospects and their stated objective of economic viability with less aid dependence.

Foreign Aid

Australia, New Zealand, Japan, the US, the UK, France and the EEC provide substantial aid to the Pacific countries. France supports New Caledonia and French Polynesia, while the US provides substantial aid to its former Trust Territories in Micronesia.

Table 3 (p. 42 below) shows the extent of aid to some of the countries in the region. Aid impacts significantly upon the balance of payments and the government budgets of these countries, particularly Western Samoa, Vanuatu, Tonga, PNG, Kiribati, Tuvalu, Niue and the Cook Islands.

Aid flowing into projects and programs that are carefully evaluated, are economically and financially viable and improve the productive capacity of a country have much to recommend it. Such aid supplements domestic savings. Aid flows, particularly to the public sector, have allowed relatively higher wages and salaries to be maintained, and contribute to upward pressures upon wages and salaries throughout the economy. But the multiplier effect of wages, recurrent expenditures and capital expenditures financed through aid works in both directions. A reduction in aid, even in real terms, is likely to have noticeable impacts upon the external sector, government revenue, GDP and employment. Current account deficits would probably increase, necessitating reduced consumption and (perhaps) investment. Government spending would inevitably have to be reduced as part of the adjustment program aimed at avoiding increased indebtedness (particularly external) and loss of external reserves.

The upward pressures upon wages and salaries that stem from substantial aid inflows may have introduced additional difficulties in a number of South Pacific countries. The aid- or remittance-induced increases in wages and salary levels appear to have had adverse effects upon agriculture. In Tonga, Samoa and the Cook Islands, for instance, agricultural wages are already high and it is increasingly difficult to secure agricultural labour: a situation compounded by rural emigration to the towns and overseas. This trend contributes to the relatively poor performance of agriculture in the region. Since subsistence and commercial agriculture will always be central to future economic development in the Pacific island countries, this trend needs to be addressed.

Large aid flows do have a negative secondary impact on the tradable goods sector, including agriculture. They enable countries to avoid, for long periods, currency adjustments that are necessary for long-term growth. The combination of wage levels and relatively strong currencies stemming from substantial aid flows have tended to erode the competitiveness of a number of island countries.

The real growth in aid implicit in a number of development plans is probably realisable in the short term. But it probably will not be sustained over the medium to long term. Budgetary grants from bilateral donors are expected to fall steadily. In PNG the annual reduction in budgetary aid is to be partly replaced by project allocation. In the Cook Islands a similar reduction has started. Kiribati recently decided not to accept annual budgetary grants. For Vanuatu this form of aid ended in 1988. The future of aid to the region will reflect donors' changing economic and security interests in the area. As this relationship is likely to be a changing one, a conservative assumption on future aid growth is a prudent course for island countries to take.

Kiribati's effort to reduce government's dependence upon budgetary aid support is of interest. In anticipation of the exhaustion of phosphate deposits at Ocean Island, the proceeds of taxes on the country's phosphate were set aside and invested overseas. Interest earnings were reinvested. A London merchant bank manages the Fund's portfolio, aiming to maximise income while avoiding exchange losses. The capital in the fund is preserved and part of the income is now utilised to help finance the budget deficit; neither capital nor income may legally be used to finance the country's current account deficit.

Tuvalu now has a similar trust fund, whose capital was provided by bilateral donors. The small countries could consider a similar arrangement to help reduce their dependence on aid. It could be implemented out of improved external reserve and fiscal positions, which require appropriate macroeconomic policies. Part of the annual income of the fund could be reinvested and the balance used to help finance budgets, which should restrain the growth of current expenditures and ensure that capital projects meet stringent criteria.

The International Monetary Fund (IMF) attaches conditions to its financial assistance. The World Bank and, more recently, the Asian Development Bank have begun to require changes in the macroeconomic policies of countries to which they lend. The EEC now requires discussions on policies and priorities with African, Caribbean, and Pacific (ACP) countries to which it provides aid. Some developing countries have found the exchange of views with multilateral organisations beneficial.

Bilateral donors have not, so far, imposed such conditions. Their sensitivity on the issue is perhaps understandable. Yet some such process, involving discussion of national priorities and policies, probably needs encouragement in the Pacific. Joint reviews of economic performance are beneficial. Donors could identify those aspects of approved programs that meet minimum standards for funding, thus minimising the possibility of priority distortions by donor and recipient and the pursuit of objectives that may be at variance with national ones.

Remittances

Remittances are particularly significant in five of the South Pacific countries. Private transfers as proportions of GDP hover around 28.7 per cent, 22.8 per cent and 8.6 per cent in Tonga, Western Samoa and Kiribati respectively. Figures for the Cook Islands and Niue are not available, but remittances are as important for them as they are for Tonga and Samoa. In these countries the impact of remittances upon GDP, employment, revenue, wages and salaries, the current account and foreign reserves is as important as that of aid receipts. By helping to induce high labour costs and enabling the maintenance of overvalued strong currencies, large remittances have had negative repercussions upon the tradable goods sector. If used mainly for increased consumption, remittances steadily increase an economy's structural dependence.

Remittances are likely to increase with the number of residents migrating to other countries. Where emigration to developed countries is unrestrained, as it is with Cook Islanders and Niueans migrating to New Zealand, remittances will probably continue to increase in real terms. Countries that do not enjoy similar arrangements should build more conservative assumptions about remittances into their long-term economic strategies. This is important, since the level of remittances is likely to be inversely related to the length of residency overseas.

Minerals

PNG has rich deposits of gold and copper, which have become its largest sources of foreign exchange and revenue. Fiji has a successful goldmine, and more gold deposits have been found. Deposits of copper ore were found in the 1970s but their commercial development awaits further improvements in the market prices for copper. There are good prospects for gold mining in Vanuatu and the Solomon Islands.

For some time, large international companies supported by governments have been active in geological mapping and exploration of parts of the seabed. The sophisticated technology and capital that are required mean that reliance will have to be placed upon large multinationals for ongoing exploration and commercial development. This is a field of shared interests and hence useful cooperation between private capital and governments.

Agriculture

Agriculture, which supports the bulk of the population in the region, is the sector upon which sound economic development and economic independence will continue to be based. The apparent neglect of subsistence agriculture will need to be rectified. International agricultural marketing problems abound, and government policies, both overseas and domestic, have not always been supportive.

In Tonga, vanilla, a high-value low-volume product, has become the largest export earner ahead of copra. Other non-traditional export crops that are being tried or are under consideration by Departments of Agriculture in the region include avocado pear, pawpaw, mango, spices (vanilla, pepper, cloves, chillies), pumpkins, medicinal plants, orchids, flowers and other tropical ornamentals. Maricultural possibilities include seaweeds, shell fish, crustaceans, eels, pearls, *bêche-de-mer*, and black and pink corals.

To develop these products, more resources will need to be channelled into technical and marketing research. South Pacific countries could develop and capitalise on significant niches in the market. But increased reliance must be placed on the private sector, with the public sector playing at most a supportive role.

Fishing

Fishing is as basic as agriculture in the region. There still exists unsatisfied local demand for fresh fish.

Offshore fishing in the expansive EEZs in the region has great potential. But technology, capital and knowhow will need to be imported. Already it has made possible tuna fishing and deep-sea fishing for high-value fish such as deep-sea schnapper. Some countries, such as the Cook Islands, Vanuatu and Kiribati, have offered to sell licenses to overseas fishing organisations: an additional source of income in the short term. Prospects for increased domestic private capital involvement in this important sector will improve over time.

Tourism

Tourism is already a major industry in Fiji, Vanuatu and the Cook Islands, and is growing in importance in Tonga, Western Samoa and the Solomons. The other countries in the region are also actively encouraging its growth.

Heavy investments in tourist infrastructure have been undertaken, and more are planned. These include the building and extension of airfields and airport facilities, electricity supply, roads, water supply, telecommunications, and sewerage systems. These involve large public sector outlays, which have been supported through bilateral and multilateral aid.

The tourist industry is a ready market for agricultural and aquacultural produce, artefacts and a wide range of domestic services. Although leakages out of the tourist industry are still substantial, increased domestic supply of food such as fruits, vegetables, fish and root crops should overcome this.

The contribution of tourism to employment, foreign exchange receipts and revenue is growing with the industry in the region. More and more local people are moving into management positions as a result of training undertaken by the industry. This general improvement in skill levels benefits other sectors of the economy when employees move into them from tourism.

Tourism will become more important to the economies of the region and represents a necessary diversification of their economic base. It will supplement but is not likely to replace agriculture and fishing as the most basic economic sector in the South Pacific.

Financial Centres

There are encouraging prospects for financial centres in some of the smaller countries of the region. Vanuatu established the framework for its centre in the early 1970s. The industry has grown steadily and has become an important contributor to the economy. Vanuatu receives an estimated $US1.5 million annually in direct revenue from licenses and registration fees; about 200 local people and 148 expatriates are employed in the industry. The total overseas assets of exempt banks and other financial institutions registered in Vanuatu hovers around $US2 billion, while the annual foreign exchange earnings generated by the industry are estimated at about $US3 million.

A number of smaller countries, including Nauru, the Cook Islands and Tonga, are trying to develop their own financial centres. The industry is very mobile; the required domestic investments tend to be limited to telex machines and other office equipment and the associated training. These countries and Vanuatu will probably need to work out a way of maximising the returns to themselves. For the smaller countries the prospects for growth in their offshore financial sectors are good.

The industry needs skills in banking, telecommunications, and secretarial work. It also calls heavily upon the services of lawyers and accountants and other skills that tend to be in demand throughout an economy. The growth of the industry could therefore support the strengthening of skilled and professional services.

Population, Emigration and Training

The natural rates of growth in population are still generally high, but some improvements have occurred in recent years. The actual population growth rates in Tonga, Samoa, the Cook Islands and Niue are low or negative because of continuing emigration. But while beneficial, emigration is not a solution to the problem. Attitudes could change in the destination countries. If negative changes take place, the actual rate of growth in population will move closer to the natural rate of growth. Those who leave the country tend to be enterprising types with technical or professional skills. They are also likely to be able-bodied members of the labour force. Their departure tends to impact negatively upon agricultural and other forms of production.

High natural growth rates result in high dependency ratios and a young population structure. This imposes a heavy burden upon the public sector, which has to invest heavily in social infrastructure such as schools, hospitals and housing.

Urban migration is already a problem in all the South Pacific countries. It has eroded the workforce in the rural areas while inflating demand for services and increasing visible unemployment in the towns. The rising urban population pre-empts an increasing proportion of public sector resources at the expense of the rural sector. High urban population growth rates and the associated high rates of urban unemployment are closely related to the rising urban crime rate.

All island countries in the region are wrestling with this problem, and are promoting rural development in an attempt to counter the urban drift. But government salaries and urban wages are kept high by labour market regulation and powerful unions. A steady movement towards a deregulated climate where exchange rates and wage levels are increasingly determined by market forces would help the adjustment process in this important area.

Academic achievement remains the main focus of the educational system in the region. Already graduates and diploma-holders in arts subjects are finding difficulty obtaining jobs. But demand for technical and commercial skills and tradesmen remains unsatisfied. A restructured educational system that responds flexibly to changing demands for various skills should be an important element in the requisite development strategies of the Pacific Island countries.

Private Investment

The South Pacific countries are promoting private sector investments. The level of domestic savings in the region falls far short of domestic investments: this suggests an important role for overseas investments in the future development of the region. Private investments are likely to be attracted by:

- political stability, a factor that has been somewhat uncertain in recent years;
- an expectation of steady growth in the economy;
- an expectation of internal and external financial stability based upon the past record and economic management;
- freedom to repatriate profits and capital;
- stable cost structures and rising labour productivity;
- a stable industrial relations climate;
- a deregulated business and financial environment;
- a land tenure system that provides security and ready access for the investor;

- expanding domestic and export markets;
- an efficient deregulated domestic capital market and easy access to overseas capital markets.

The need to deregulate the business environment is gaining recognition, and a number of countries have started cautiously along this path. Privatisation of public sector corporations is now frequently discussed, with the Asian Development Bank and the International Finance Corporation providing useful advice on this subject.

The Fiji government has been trying to privatise the Fiji Sugar Corporation through the sale of shares to the public. In 1988 the government's share in Air Pacific was reduced substantially through the issue of new shares to Qantas. A number of central government commercial activities have also been corporatised with the aim of ultimately privatising them.

The South Pacific countries participate in a number of international arrangements that enhance their attractiveness as hosts for investments. The South Pacific Regional Trade and Economic Cooperation Agreement (SPARTECA) allows selected exports duty-free access to Australia and New Zealand. Under the Lome Convention, agreed quotas of manufactured goods are granted access to the EEC markets. They also benefit from the Generalised System of Preference (GSP), under which the industrial countries grant free entry to imports from developing countries.

The South Pacific countries need to look for markets beyond Australia and New Zealand. In addition to the opportunities under SPARTECA they should capitalise on the opportunities available within the GSP and the Lome Convention. But these opportunities can only be fully grasped if their economies become increasingly competitive and when more joint ventures with overseas companies possessing marketing strength are established.

National Financial Policies

The economies of the South Pacific countries are very open. Capital flows in and out relatively freely. National income, revenue, and the current account fluctuate with goods and services receipts. The maintenance of stable and sustainable current account positions and comfortable levels of external reserves are preconditions of steady growth.

The Pacific island countries have fixed exchange-rate regimes.

Kiribati and Tuvalu use the Australian dollar, while Niue and the Cook Islands use the New Zealand dollar. The Tongan currency is still pegged to the Australian dollar. The Solomon Islands, PNG, Fiji, Vanuatu and Western Samoa each peg their separate currencies to baskets of currencies that are important to their external commercial relations. Fixed exchange-rate regimes are adopted by countries with small, open economies in order to ensure relative stability in the movements of their currencies. Their narrow foreign-exchange markets, concentration of exports and financial institutions imply that relatively small speculative transactions would result in wide fluctuations in their currencies if they were freely floating.

But fixed exchange rates, economic openness and high mobility of capital into and out of the country make active monetary policy relatively ineffective. Liberal credit policy aimed at promoting growth is unlikely to work. Aggregate demand and labour costs will increase, prices and the current account deficit will rise, net capital outflow will grow, reserves will fall and the external debt position is likely to deteriorate quickly. Gains in output are likely to be short-lived as adjustment policies become unavoidable in the interest of re-establishing national financial stability.

External prices and exchange-rate changes influence domestic prices in small open economies more immediately than in bigger and less open economies. Exchange-rate devaluations quickly increase the prices of domestically-produced tradable goods. Higher living costs bring about rises in wages and salaries, which tend in a regulated labour market to adjust rapidly and maintain their levels in real terms. The prices of non-tradable goods will of course keep pace. A devaluation will therefore rapidly manifest itself in price increases throughout the economy. Unless wages and salaries are prevented from making this automatic adjustment, a devaluation designed to promote growth will not succeed but will certainly result in increased inflation. The Pacific island countries should ensure through fiscal, exchange-rate, monetary and incomes policies that the real effective exchange rates of their currencies move in directions that increase the competitiveness of their economies.

The link between budget deficits and the current account is particularly direct in small open economies. Budgetary excess results in increases in credit issued by the banking system and inflationary financing by the central bank. Under such conditions the private sector finds itself crowded out of the credit market to the detriment of private sector investments.

The Pacific islands are subject to sudden internal and external economic shocks. It is therefore important to maintain external reserves at relatively high levels, since adjustments to such shocks are economically and socially painful if owned or borrowed reserves cannot be readily accessed. Ready access to borrowed reserves is itself a function of a country's credit rating, which is in turn a function of sound national financial management. Private sector investment is likely to be encouraged if national financial stability looks assured.

The IMF already interacts with a number of Pacific island countries that will continue to seek its advice and financial assistance in their search for continuing external and internal financial stability. The IMF has not been popular with some developing countries to which it has provided conditional assistance. But the record of IMF activity in other countries should be of interest to the region.

Many countries allow political constraints to undermine financial discipline and to delay appropriate policy changes. In some cases, of course, external financial stability was disturbed through external shocks. But the realities of life being what they are, external imbalances need both adjustment and financing. The IMF plays the important role of imposing financial discipline while providing short-term balance of payments support. It does recognise that politicians may find it helpful to direct the blame to it when there is popular opposition to unpalatable policies whose imposition has become unavoidable.

It would be instructive to examine the background to the implementation of an IMF program by a country in the region. In the 1970s and early 1980s the country pursued expansionary fiscal policies to support the pace of development. Credit increased quickly. The rate of inflation rose, the current account deteriorated and external indebtedness increased. The world recession of the early 1980s, which was partly triggered by the second OPEC price rise, made things more difficult. The terms of trade deteriorated sharply as the prices of imports, particularly oil, rose while those of exports declined. The country's budget and current account deficits deteriorated sharply and inflation worsened. An IMF program was put in place in 1983, involving the usual stabilisation measures. The currency was devalued, the public sector deficit was cut back, and credit tightly contained.

Supported by favourable external developments after 1983, the program appears to have succeeded. Inflation rates have fallen, reserves have increased significantly and external arrears have now been extinguished. Now that financial stability has been achieved, the country is again able to focus primarily upon economic growth.

Regional Arrangements and International Organisations

Because of the countries' small size and populations, a regional approach is being pursued that aims to reduce costs through economies of scale. Some experiments, such as the Air Pacific regional airline, have not worked as expected. The University of the South Pacific, which is owned by some eleven governments, has done reasonably well in view of the inconvenience of having to deal with eleven different authorities.

The regional shipping line for a long time found it difficult to break even, and has been supported by government subsidies under aid for a number of years. There do exist opportunities for regionally supported projects and ventures. But the success of such ventures would probably be better assured through increased private sector involvement.

Donors such as the EEC, Australia and Japan are allocating a large part of their aid to regional projects in the South Pacific. Increasingly, the South Pacific Forum Secretariat has become the conduit and coordinating body for such aid. The member countries of the Forum regularly meet to evaluate their individual and collective needs and to formulate regional programs for donors to consider. This body also hosts discussions on important regional issues such as the marketing of agricultural produce, civil aviation, shipping, telecommunications, education and tourism. The regional heads of governments, including those of Australia and New Zealand, meet regularly within the Forum to exchange views and make decisions on political, economic and social issues that affect the South Pacific region. The benefits of the collective approach in a changing world where smallness has obvious disadvantages are increasingly appreciated in the region.

IV. CONCLUSION

The island countries have resources whose commercial development requires expertise, capital and technical knowhow from the developed economies around the Pacific Basin. Their EEZs cover millions of square miles. The resources in and under these zones have yet to be fully assessed. The mineral resources of Melanesia are substantial. The full potential of their forests will take years to develop. Tourism will be a growth industry. Agricultural development will be a continuing priority. The development of these sectors will reap mutual benefits to overseas and domestic investors.

Security and stability in the Pacific island countries will be as important to them as they are to Australia, New Zealand and the other powers around and outside the Basin. Without such security and stability in the region, the island countries cannot achieve their long-term goals and the bigger countries could find a rearrangement in their own strategic and economic interest in the Pacific.

The growing interest of the major powers in the Pacific region and its potential could in itself be destabilising. Already there is evidence of this. In the search for stability and security as well as for economic growth and development, the island countries will work increasingly as a group. Because of their size, this approach will assist in the achievement of their economic ambition and enable their collective voice to be heard in the various international forums and by bigger countries. Regional arrangements such as the Forum and the Forum Fisheries Agency are serving this objectives. But they will need to have their antennae finely tuned to rapidly changing global economic and geopolitical equations and be ready to respond promptly to maintain and promote the interests of the countries they serve.

Table 1:
Principal Physical and Demographic Features

	POP'N 1987	POP'N 2000 (est.)	POP'N GROWTH % p.a. 1982-87	MEDIAN AGE*	URBAN POP'N as % of total*	LAND AREA sq. km	EEZ AREA sq. km	GOVERNMENT
American Samoa	38 700	45 700	1.8	18.8	40	197	390 000	Administered through US Dept. of the Interior
Cook Islands	17 100	15 800	0.3	17.7	27	240	1 830 000	Elected assembly; House of Chiefs; NZ tutelage
Fed. States Micronesia	87 700	131 800	3.5	16.7	26	701	2 978 000	Territorial and local govt, US tutelage
Republic of Fiji	725 500	887 600	2.0	20.6	39	18 272	1 290 000	Constitution & Parl. suspended; military supported govt. ruling by decree; Council of Chiefs
French Polynesia	175 800	239 500	2.9	20.1	59	3 265	5 030 000	Internal autonomy, represented in French govt.
Kiribati	67 700	80 400	2.4	18.7	33	690	3 550 000	Elected parliament
Marshall Islands	37 800	58 300	3.8	14.8	60	180	2 131 000	Parliament and local councils
Nauru	8 800	11 300	1.0	18.8	100	21	320 000	Parliament of sorts
New Caledonia	153 500	188 600	1.2	21.7	21	19 103	1 740 000	3 regional entities under Terr. Congress and French govt.
Niue	2 500	2500	- 4.7	18.8	21	259	390 000	Legislative assembly & village councils, resident NZ rep.
Palau	14 000	15 300	0.7	20.0	68	494	629 000	2 chambers and 16 'state' govts
Solomon Islands	292 000	437 500	3.7	15.3	14	28 369	1 340 000	Legislative and provincial ass.
Tokelau	1 600	1700	1.3	20.2	n.a.	10	290 000	Island Councils under NZ admin.
Tonga	94 500	100 800	0.2	17.4	26	699	700 000	Kingdom, legislative ass. (part appointed, part elect)
Tuvalu	8 500	10 800	1.7	20.2	30	26	900 000	Parliament
Vanuatu	145 000	224 200	3.3	17.1	18	11 880	680 000	Parliament, council of chiefs
Wallis and Futuna	14 700	21 800	4.3	17.0	7	255	300 000	French administration, territorial assembly
Western Samoa	162 000	176 000	0.6	17.1	21	2 935	120 000	Largely titled heads of families
TOTAL ABOVE	2 056 700	2 578 500	–	–	–	87 596	24 608 000	
Papua New Guinea	3 463 300	4 568 500	2.1	18.5	13	462 840	3 120 000	House of assembly, national & 19 provincial governments
TOTAL WITH PNG	5 520 000	7 146 800	–	–	–	550 436	27 728 000	

* for latest available census year (between 1976 and 1986)

Source: South Pacific Commission Statistical Summary; ANU NCDS; Pacific Economic Bulletin passim

Table 2:
Key Economic Features

	GDP ($US m)	GDP per capita ($US)	RATE OF INFLATION (% p.a.) 1980-1988	SOURCES OF FOREIGN EXCHANGE
American Samoa	187.5 (1985)	5282	2.4	Fish, remittances from US, US aid
Cook Islands	34.1 (1986)	1985	6.5	Clothing & footwear, fresh fruits & veg., pearls, shells, copra
Federated States Micronesia	106.5 (1983)	1249	n.a.	US aid
Republic of Fiji	1044.7 (1987)	1440	4.9	Sugar, gold, fish, timber products
French Polynesia	2055.8 (1986)	11674	3.9	French military and aid, tourism, copra, vanilla
Kiribati	25.5 (1987)	376	3.9	Copra, fish, shark fin
Marshall Islands	46.3 (1984)	1302	2.0	US military and aid
Nauru	n.a.	n.a.	n.a.	Phosphate and investment income
New Caledonia	845.2 (1985)	5586	2.8	Nickel, French aid and military, tourism
Niue	3.8 (1984)	1367	6.9	Copra, coconut cream, taro
Palau	33.2 (1985)	2406	n.a.	US aid, fish, tourism
Solomon Islands	144.6 (1987)	495	10.8	Fish, logs, cocoa beans, copra
Tokelau	n.a.	n.a.	n.a.	Copra, remittances and aid from NZ
Tonga	58.8 (1985)	629	9.0	Vanilla beans, bananas, coconut oil, fish
Tuvalu	3.6 (1985)	442	3.0	Copra, fish, handicraft
Vanuatu	122.5 (1987)	845	5.9	Copra, cocoa, non-canned beef, logs, sawn timber
Wallis and Futuna	n.a.	n.a.	7.9	Remittances, aid
Western Samoa	101.9 (1987)	629	5.1	Coconut oil, taro, cocoa, coconut cream, copra
Papua New Guinea	3 038.6 (1987)	878	4.1	Gold, copper, coffee, timber

SOURCE: Statistical Bulletins of the various countries, SPC Statistical summary

Table 3:
Foreign Aid to the South Pacific

	YEAR	TOTAL ($USm)	PER CAPITA ($US)
American Samoa	1987	52	1408
Cook Islands	1988	11	631
Fed. States of Micronesia	1986	41	437
Fiji	1988	43	58
French Polynesia	1988	327	1715
Kiribati	1988	12	176
Marshall Islands	1986	17	450
Nauru	1987	53	6
New Caledonia	1988	261	1653
Niue	1988	5	1626
Palau	1987	24	1715
Solomon Islands	1988	35	117
Tokelau	1988	3	1446
Tonga	1988	13	128
Tuvalu	1988	13	1585
Vanuatu	1988	29	195
Wallis & Futuna	1987	20	1336
Western Samoa	1988	19	113
Papua New Guinea	1988	300	84

SOURCE: SPC Statistical Summary and Development Co-operation Report; Pacific Economic Bulletin, vol. 5, no. 1, June 1990.

Table 4:
Employment Patterns
proportions, % of the economically active population

	CENSUS YEAR	AGRIC. & FISHING	MANUFACT-URING	CONSTRUCT-ION	COMMERCE	TRANSPORT	SERVICES	OTHER
American Samoa	1980	2	24	8	11	9	46	0
Cook Islands	1981	21	7	6	12	10	29	15
Fed. States Micronesia	1980	2	1	12	11	6	60	8
Republic of Fiji	1986	44	8	5	11	5	15	12
French Polynesia	1983	16	6	15	18	7	35	3
Kiribati	1985	73	1	2	4	4	12	4
Marshall Islands	1980	4	3	10	15	8	59	1
Nauru	1977	0	0	7	4	1	6	82
New Caledonia	1983	22	9	6	23	6	29	5
Niue	1984	21	11	11	10	5	40	2
Palau	1986	13	1	7	14	3	43	19
Solomon Islands	1986	81	2	2	2	2	7	4
Tokelau	1986	38	11	21	3	0	21*	6
Tonga	1976	51	2	6	4	4	22	11
Tuvalu	1979	73	2	7	3	3	10	2
Vanuatu	1979	77	2	2	4	3	11	1
Wallis and Futuna	1983	82	0	11	2	0	4	1
Western Samoa	1981	59	2	6	4	3	20	6
Papua New Guinea	1980	82	1	1	1	1	4	10

* Including electricity, transport and finance

SOURCE: SPC Statistical Summary

Table 5:
Average Ratios to Gross Domestic Product (%)

	YEAR	IMPORTS	EXPORTS	TRADE DEFICIT	PRIVATE TRANSFERS	CURRENT A/C DEFICIT	OFFICIAL TRANSFERS	TOTAL GOVT REVENUE	TOTAL GOVT EXPENDITURE	OVERALL DEFICITS (excl. grants)	OVERALL DEFICITS (incl. grants)	EXTERNAL DEBT	EXTERNAL PAYMENTS ARREARS
Cook Islands	1985	58.8	15.6	43.0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Republic of Fiji	1984-88	27.7	15.2	12.5	0.5	2.8	1.6	24.8	29.1	4.3	3.8	33.7	n.a.
Kiribati	1982-84	75.0	20.1	54.9	8.6	43.7	67.8	47.1	83.4	36.3	1.2	7.0	n.a.
Solomon Islands	1983-85	45.0	51.0	5.6	-1.2	15.6	8.5	25.2	35.7	10.5	7.8	49.4	n.a.
Tonga	1982/83-86/87	55.2	8.1	46.1	26.7	15.0	18.5	26.2	47.3	21.1	2.0	38.3	n.a.
Vanuatu	1983-85	42.8	19.7	23.5	8.6	13.7	24.1	20.4	43.6	23.2	0.8	5.8	n.a.
Western Samoa	1983-85	53.3	18.5	34.8	22.8	11.8	14.2	31.8	48.6	17.3	4.3	79.6	1.9
Papua New Guinea	1981-84	42.1	34.8	7.3	-4.8	29.5	11.0	21.7	36.8	15.1	4.4	61.0	n.a.

SOURCE: IMF and national statistical publications

The Economics and Politics of South Pacific Development: An Outsider's View

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The Economics and Politics of South Pacific Development: An Outsider's View

Wolfgang Kasper

The outsider may be ignorant of many important details and nuances, but he is more likely to see the wood for the trees. Also, the outsider may speak with an impatience, bluntness and frankness which is part of the make-up of the dynamic, open cultures that have developed in the outside world, but which is not customary — and may, at first sight, appear intimidating — to those brought up in the 'Pacific way'. But if, ultimately, mankind's problems (and capabilities to solve them) are universal, there is scope for a contribution by the outsider. Yet, whatever the outsider suggests, he must be bound by the categorical imperative of international studies: not to recommend to others what he would find unacceptable in his own country.

I. INTRODUCTION

The vast South Pacific region — roughly the triangle between Christchurch, Panama and Manila — covers nearly a third of the globe. But it is home to only 2 million people in the islands (as many people as in Sydney's Western suburbs), plus 3.4 million in Papua New Guinea[1] (see S. Siwatibau, Table 1, p. 40 above). The entire region is populated by fewer inhabitants than Hong Kong. It is politically divided into about one-and-a-half dozen, mostly tiny, territories; only PNG covers a sizeable land area (nearly as much as Spain). The South Pacific embraces nations and territories with a great diversity of environments, people, races, political systems, and living

1. This excludes ethnic Polynesian and Micronesian minorities in New Zealand, Hawaii, and Guam, as well as Irian Jaya, which has a Melanesian population, but lies outside the Pacific region.

standards. However, if outsiders have any perceptions at all about the South Pacific, they submerge this diversity in an inaccurate amalgam of Rousseau and tourist brochures.

Does the vast but fairly empty South Pacific merit outside interest at all? And is one justified in imposing the notion of a somehow homogeneous region where such diversity exists? The reply to both questions seems 'yes'.

II. A THUMBNAIL SKETCH OF THE *CONDITION HUMAINE* IN THE SOUTH PACIFIC

Interest in the region seems in the first instance justified because it is so incredibly vast, covering nearly a third of the globe. The 200-mile Economic Exclusion Zone (EEZ) which the South Pacific people can claim is bigger than the territory of the USSR. This vast, thinly populated space may appear as a vacuum, but it is of considerable strategic importance, as it lies across major trade routes, especially those to Australia and New Zealand, and as it contains valuable marine resources. It is no coincidence that Pacific rim nations — Australia, New Zealand, the USA, Japan and the USSR, and in future possibly other Asian nations — take a growing interest in South Pacific affairs, contributing considerable aid, which in some cases exceeds the national product (see S. Siwatibau, Table 3, p. 42 above).

Despite this great diversity, the South Pacific countries share certain specific, common economic and political traits, which S. Siwatibau has described in his essay. Here we wish to highlight some of the key features:

- People live often in considerable **isolation** from the rest of the world and have to put up with high transport and communication costs. But they are reasonably well informed about the outside world, because they are literate and are likely to have family and friends in Sydney, Auckland, Los Angeles or Hawaii, which contain larger Pacific communities than most Pacific nations. After only about 100 years of contact with the outside world, air transport, short wave radio, satellites and video tape overwhelm the members of traditional communities with tantalising views of more dynamic, more colourful societies in the outside world. And officials from the South Pacific nations seem all the time to be attending countless regional and international meetings where they are confronted with the issues of the wider world (and with foreign officials who love to attend conferences in South Pacific resorts!).

- With a few exceptions, **natural resources** are confined to marine life and a benign climate (interrupted by the occasional, destructive cyclone).

- Because of the short history of contacts with the open world system, **anthropological** facts matter in the South Pacific. Most South Pacific people are Melanesians (the vast bulk of them), Micronesians and Polynesians, who share certain basic philosophies and community attitudes (for more detail and a summary of the literature, see Crocombe, 1987, and Brookfield & Ward, 1988). It is worth noting that the tradition of genuine private property is less clearly established than elsewhere: People could survive with few permanent possessions, and perishable commodities (tree fruit, pork) are best shared around freely when available. And small tribal communities are able to organise much activity under the central direction of their chiefs.

  But there are also important economic and cultural differences among Pacific communities that affect their development: Melanesians are born into a world of equals and have a long tradition of trade (they invented money independently of the rest of the world). In Melanesia, leadership and status flow, as in the United States, largely from economic effort, achievement and wealth. In contrast, Polynesians and Micronesians (as well as the [ethnically Melanesian] Fijians) inherit their social status within a rank hierarchy; members of the chiefly class are typically disdainful of economic effort, since material wealth flows from inherited status, as was the case with the European aristocracies before the French Revolution (Crocombe, 1987:17-21). The hereditary chiefs are used to claiming economic rents from ordinary people, as well as tribute from other tribes (and nowadays from development aid agencies).

  In addition to indigenous people, there are sizable groups of more recent immigrants, like the Indian majority in Fiji and the White and Asian majority in New Caledonia, as well as large mixed-blood populations, which, in some cases like Tahiti, account for nearly all the population. In PNG, there are about 75 000 Australians. Some economies are dominated by large expatriate communities.

- Most people claim a close, personal relationship to their **land**. They regard it as inalienable and, like traditional people everywhere, as their 'second skin', not as a production factor. It is true that land was sold readily to early settlers, but the full implications of these transactions were not understood at the time. Nowadays, land is often extremely scarce, because there are often no markets for land through which potential new land users could obtain the legal right to use the land.

- Most South Pacific nations had some **colonial experience**, but that experience was not traumatic, began late and ended only recently. Modern self-government is still the experience of only one generation of leaders. And considerable numbers of islanders continue to live in comparative affluence as subjects of France, New Zealand or the United States.

- Most **national governments** rule over small populations. And the rulers come straight from experiences of personal loyalty and social structures within traditional tribes or the churches. They rule often fewer people than in a sizable European village and (except in PNG) never more than in a middle-sized city. Yet the micro-states have almost invariably emulated the structures of national governments in much larger countries.

- South Pacific governments may appear to govern according to some form of Westminster democracy, but the substance of **politics** in the Pacific is very different. Most governments are run in reality as personal fiefs by traditional or newly formed elites whose positions were reinforced during the colonial era. They tend to govern in fairly paternalistic ways. This is in itself becoming a source of conflict with the young generation who begin to struggle free from traditional bonds, demand their allotted share in the economic cake, and are frequently materially more ambitious than their elders.

- The people of the South Pacific are, as a rule, happily unfamiliar with genuine poverty. Nature — and foreign aid — have provided **'subsistence affluence'**. People enjoy reasonable standards of education, nutrition and health. Literacy rates are high (except in PNG). However, there are increasing exceptions. Local malnutrition is reported where young people emigrate and leave old people and children behind. Recorded per capita incomes vary widely (see S. Siwatibau, Table 2, p. 41 above). Recorded living standards are high in the French colonies of New Caledonia and French Polynesia (Tahiti) where, at least on paper, they exceed New Zealand's modest living standards, as well as in the US territory of American Samoa. Most independent countries in the Pacific enjoy middle-income status (if measured according to World Bank definitions). The exception (despite the appearance of national account statistics) is PNG, for which wider development indicators suggest living standards akin to those in low-income countries. The following comparisons may serve to underpin this point:

	PAPUA NEW GUINEA	LOW INCOME COUNTRIES (except China & India)	MIDDLE INCOME COUNTRIES
Adult literacy (%)	32	51	65
Primary school enrolment in 1985 (% of age group)	64	67	104
Secondary school enrolment (%)	14	22	49
Tertiary enrolment (%)	2	5	14
Life expectancy (at birth, in years)	52	52	63
Population/ nurse in 1981	930	1 400	7 130
Population/ physician in 1981	15 610	4 940	17 670
Daily calorie intake in 1985	2 145	2 100	2 719
Energy consumption/ population (kg of oil equiv.)	244	86	883
Share of labour in agriculture in 1980 (%)	76	71	43
Share of labour in industry in 1980 (%)	10	10	23

Source: IBRD, *World Development Report 1988 and World Tables*, 3rd ed., Vol. II

In some countries, there is still a sizable informal sector with local agriculture and fishing. In others, people depend on cargo from overseas.

- The indications suggest that **per capita incomes grow** only **slowly**, partly because of cuts in post-colonial aid, remoteness, diseconomies of small scale and resource shortages, and to a large extent because official policies are complacent. They are not very development oriented at best, and impede growth, often by blatant rent-seeking, at worst. In PNG, output growth since independence in 1975 has been around 2 per cent per annum, so that average per capita incomes have hardly grown. (The incomes of the small urban elite have of course risen substantially). The market incentives in all Pacific countries to raise living standards are weaker than elsewhere. Traditionally, survival and work effort have not been as closely linked in the minds of people as in harsher environments. And the modern economy often offers little incentives to strive for higher material attainment: The basic necessities come with little effort, but even modest luxuries incur high marginal costs because they are imported at high transport cost and under diseconomies of small scale. Governments reinforce this disincentive structure, e.g. by imposing high import duties. Where the incentive for people to move forward is weak, there is a danger of back sliding. 'Despite the present prosperity, there is a danger that "subsistence affluence" could become "subsistence poverty", at least in some of these island countries' (Committee to Review the Australian Overseas Aid Program, 1984:167).

- Like small places anywhere, the South Pacific countries are **heavily dependent** on exchange with the rest of the world. That is a normal aspect of the division of labour. But this means something very different in an isolated island from what it means in a European village. Moreover, dependency extends frequently to outright financial dependency. In many places, current living standards cannot possibly be maintained by local production and productivity without perpetual aid — a prospect that does not seem to bother many of the leaders. Although per capita aid transfers are the highest of any region on earth, the tradition of Pacific gift-exchanging and the Pacific brand of Christianity make high and lasting aid dependency quite acceptable. One happily accepts subsidies in exchange for friendship, loyalty and a little adulation, and one would be very angry if the remittances of 'aid tribute' stopped. In addition, there are of course remittances from compatriots who have found (often low-skilled) work in New Zealand, California or Australia.

- The outsider often has the impression of **boredom** and bewilderment, especially among the young. The youth problem is, in some places, aggravated by high population densities, deracination and a lack of economic opportunities. The supposed attractiveness of the 'Pacific way of life' is often revealed in high numbers of emigrants who voluntarily desert 'Paradise'.

- The image of the 'noble savage' and of a conflict free society à la Rousseau and Margaret Meade has probably always been more a romantic dream than a reality.[2] It certainly does not hold true now. While there has been no massive bloodshed, we now read regularly about **growing conflicts**, such as coup attempts in Fiji and Vanuatu against constitutional governments,[3] bloody riots and political arson in Tahiti and New Caledonia, arrow and dynamite attacks against mines in PNG,

2. Freeman, 1983. This is an excellent case study of how a fashion in the social sciences (liberation from all constraints in the tradition of Rousseau) was fraudulently and/or naively given empirical support by M. Meade. But Meade's evidence apparently had little to do with the facts.

3. During 1987, two military coups in Fiji — one of the more advanced economies in the South Pacific — overturned a democratically elected government with a Left-populist platform and, for the first time since independence, with a strong influence of the Indian majority. Positive discrimination along racial lines in favour of the indigenous Fijians has been introduced in some areas of social, political and economic life since then. The draft constitution of September 1989 enshrines the privileges of the Fijians and the hereditary chiefs, although the degree of positive discrimination still appears not strong enough for some of the military (*The Australian*, 26 Sept. 1989, p. 1). The political turmoil induced heavy losses of skilled people and capital and resulted in a massive recession (Kasper et al. 1988), showing painfully the limits of national sovereignty. There has been some economic recovery but the long-term dilemma of finding a growth-oriented political, civil and social order in the face of established group privileges will not go away, and the economic costs of positive discrimination will rise.

political assassinations in Palau, PNG and New Caledonia, urban youth problems in Port Moresby, Papeete and Suva, and growing internal regional conflicts in Fiji, Vanuatu and PNG.[4]

We have to conclude that the 'human condition' in large parts of the South Pacific is closer to that of Africa than to the rest of the Asia-Pacific region. It is becoming gradually clear that, behind the idyllic veneer depicted in tourist brochures, there is a 'heart of darkness' that has to be conquered in the interest of those who live in the South Pacific and those outsiders who share an interest in the stability of the region.

III. THE STRATEGIC FRAMEWORK

The South Pacific area is of considerable strategic concern to the populous and economically buoyant Pacific rim nations. The international strategic framework around the 'South Pacific population vacuum' will therefore have important consequences for the people of the South Pacific.

- Since World War II swept into the South Pacific, there has been only limited military presence, mainly by the United

4. The violent conflict over the Bougainville copper-gold mine is predominantly over rents, although separatist aspirations play a role. Taxation of the giant Panguna mine in the isolated North Solomon province contributed 45 per cent of PNG's export earnings and 17 per cent of PNG's internal revenue. The traditional land owners used to receive only 1 per cent of the mine's income (provincial government 5 per cent, national government 58 per cent, private shareholders 36 per cent). (*The Australian*, 25 May, 1989, p. 17; *The Economist*, 16 September 1989, p. 24). After bloody violence in mid-1989, which forced an indefinite closure of the mine, the local landowners were offered 20 per cent of the royalty, a 10 per cent stake in the mining company, plus other material concessions, at the expense of the central government's share. The attempted redistribution by political fiat has created great legal uncertainty, which may wreck PNG's fragile economy. With losses of exports and export taxes and possible future cuts in foreign investments due to the rebellion in Bougainville, imports and government spending will have to be cut back drastically; in turn a potential cause for civic unrest in a nation with an uneasy law and order record. This situation, meanwhile, does not prevent PNG parliamentarians from engaging in some deft anti-Australian and anti-capitalist rhetoric, blaming the rebellion and its consequences on foreign capital and clamouring for massive additional aid.

States, France and Australia; open conflicts elsewhere appear remote. Tensions over trade and politics are felt more acutely across the north Pacific, which has been more firmly under the umbrella of the **Pax Americana** and where most trade routes lie.[5]

- East-West rivalry stayed out of the South Pacific for most of the post-war period, but drew closer since the mid-1970s with the build up of the **Soviet** Pacific fleet and a sizable Soviet presence in Cam Ranh Bay, Vietnam. Since 1986, Mr Gorbachev has repeatedly signalled that the Soviet Union aims to be a Pacific power, but Soviet land forces in the Far East are being reduced by 20 per cent. Although 16 battleships are going to be retired from Soviet Pacific naval forces, the Soviet Pacific fleet has continued to upgrade its long range capabilities and its mobility. South Pacific countries are now within reach of new long-range submarines, new long-range MIG-31 fighter bombers with Cruise missiles, and newly installed SS-25 missiles.

- East-West rivalry also comes into efforts to keep the South Pacific a **nuclear-free zone**. The Soviet Union has signed an agreement which was promoted by Australia and New Zealand, as well as Pacific island states, whereas two of the three major Western players in the South Pacific — the US and France — have refused to sign. What precisely 'nuclear-free South Pacific' means is, however, subject to a wide band of interpretation by the signatories, so that the nuclear-free agreement has, in any event, more psychological than practical significance.

- Increasing numbers of overtures have been made by Soviet fishing interests to Australia and some Pacific nations. These may have been purely commercial. Several Soviet fishing contracts with island states have not been renewed, because they turned out to be unprofitable.

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5. It is symptomatic that a recent wide-ranging, detailed briefing about the Pacific to the US Senate by the new Commander-in-Chief, US Pacific Command, Admiral Huntington Hardisty, made no explicit reference to the South Pacific, apart from one passing reference to Micronesia (Statement of Admiral Huntington Hardisty before the Senate Armed Services Committee, 19 April 1989, mimeo).

- Possible future trade and pecking order conflicts between the US and Northeast Asian countries, as well as continuing US-Soviet detente, may echo into the South Pacific. So would a loss of US bases or a victory of the National People's Army in the Philippines. However, it is possible that East-West detente will undercut the most convincing motive for aid to the South Pacific (namely East-West rivalry). On the other hand, localised conflicts might in future attract increased military and economic aid.[6]

- The long-term future of **France** in the region is unclear, but France has signalled its intention to maintain a high profile presence. There is a certain rivalry for influence between France and Australia and New Zealand, some of which is interwoven with opposition to French nuclear testing and the promotion of a 'nuclear-free South Pacific'. The 'new class' Left in Australia and New Zealand appears to harbour ressentiments against France that, at times, even exceed those against the United States. The possibility cannot be ruled out that France will abandon some of her rather costly presence in parts of its Pacific territories, but will still want to maintain nuclear testing facilities. Some South Pacific French are dreaming of an active European Community role in the region, but that seems far-fetched.

- **Japan** (with $US93 million in 1988, the second biggest aid provider to the South Pacific after Australia) and other Northeast Asian nations have shown a cautious and growing interest in the South Pacific, but have often found that a real economic or political commitment is too unprofitable and requires much local knowledge. Interests from the major population centres in Northeast Asia are seeking marine resources, both by agreement with South Pacific governments and by illegal fishing. This has led to protests over driftnet fishing which the South Pacific Forum coordinated and to which Japan, so far, has responded with vague, half-hearted promises and offers of aid. The ruthless practices of Japanese

6. A rogue faction in Vanuatu politics tried to gain support from Libya. But this faltered promptly when the zesty drinking and womanising habits of the Melanesians, who were sent to Libya for weapons training, turned out to be at odds with Arab custom.

and Taiwanese fishermen and of tuna boats from California have caused justified concerns with conservation of viable fish populations. Yet it has become clear that the Pacific micro-states do not have the means to enforce their vast EEZs.

- **Australia**, together with **New Zealand**, has been the dominant provider of the hardware and software of modern development and the main point of contact for most people in the region with the outside world. Much of the 'hardware of development' has unfortunately come from these expensive sources. Cheaper Asian suppliers are now making some inroads despite poor transport connections. The 'software of development' in the South Pacific (concepts and ideas) also derives largely from Australia, where many of the Pacific leaders have studied or go for medical checkups. Unfortunately, the ideas they pick up are often fairly collectivist, though well-meaning, but often not terribly dynamic.

- Australia, the dominant middle power in the immediate region, is likely to keep a watching eye over the Southwest Pacific (Parliament of the Commonwealth of Australia, 1989; see also Thakur & Thayer, 1987, and Harries, 1989). Stability in the region is in Australia's own interest, because her most important trade routes (to East Asia and North America) cut across it. But the average Australian is much less interested in the South Pacific than in Asia, and Australians feel much less solidarity with the South Pacific than listeners of Radio Australia or visitors to academic and church insitutions in Australia (which form a Pacific lobby) are made to believe. Australia is building up naval and other capabilities to prepare against future instabilities and to be able to come to the support of threatened but friendly regimes. The Royal Navies of Australia and New Zealand are probably the only force that stands between criminal or totalitarian takeovers of small states of the sort that has been tried in mini-states in the Indian Ocean. This watching brief is carried out by Australia and an often doubting New Zealand in a division of labour with the US. But the US may step in if it disagrees with Australian political postures (e.g. in PNG or Fiji). Where precisely New Zealand with its idealistic, neutralist, isolationist bent will fit in over the medium term future is unclear, but probably doesn't matter.

We have to conclude that, for strategic and political reasons, there is heightened potential for change in the region. Internal troubles and dissensions would be readily exploited by rivalling outside interests. And outside antagonism could be easily attracted into the region. With instances such as Melanesian groups seeking support and training in Libya, secret arms shipments to Fiji, and efforts by Fiji to seek military support in Asia, peace and stability in the region now appear to have become more tenuous. The complacent, confident assumption of the past 45 years that the South Pacific is too remote for serious outside interference and will therefore always remain an area of pacific relations cannot be automatically extrapolated into the future.

IV. THE CHALLENGE OF CHANGE: PRAIS KONTROL NO MO[7]

The calm, ordered conditions of past decades may come to an end, at least for five interdependent reasons:

(i) Economic growth and economic opportunities in most South Pacific countries are insufficient to meet the rising material aspirations of growing numbers of young people. Economic pyramid climbers often face **artificial obstacles**.

(ii) The need for a more open, more dynamic economic gameplan is becoming particularly acute as post-colonial aid largesse is being reassessed in the light of superpower detente and some of the major donors are beginning to suffer from '**aid fatigue**'. The Pacific rim nations will not, and should not, be their South Pacific brothers' keepers forever.

(iii) The traditional, post-colonial gameplan has not offered sufficient incentives, challenges and opportunities for self-realisation to many of the citizens. Many of the most able and most ambitious leave to work elsewhere. If it is temporary, such **emigration** may be useful in transferring knowledge and skills, but large numbers of young, able-bodied South Pacific people have left their homes for good. Such an exodus leaves behind a sad, aging

7. Pidgin for 'economic liberalisation'.

society which is less viable, less innovative and less able to cope with new challenges.

(iv) The world **trade framework** is likely to change. Pacific rim nations may form trading alliances, which give small partners a chance, or a trade bloc, in which the powerful and their narrow trading self-interests dominate. The South Pacific micro-states will have no direct say in this, but should try to adjust to changing world trade conditions with a view to maximising their economic opportunities.

(v) **Military strategic and political changes** may introduce elements of instability. The 'splendid isolation' from world conflicts that the South Pacific has enjoyed since the end of the Great Pacific War in 1945 could come to an unexpected end. This might be brought about by antagonists within a South Pacific country or by a conflict amongst neighbours who seek new outside allies.

Possible challenges for change will confront fairly traditional governments and societies which are not very versatile and resourceful in coping with contingencies.

Paternalistic Collectivism

A common trait of government in the region — if one accepts the outsider's broad-brush abstraction from country detail — is its paternalistic collectivism. Pacific political leaders often come to treat government as their personal possession. They collect funds and often hand out financial support to personal followers. If an import monopoly is granted and a politician receives a kick-back, much of that money is likely to flow to personal followers: and many in the Pacific would not call this corruption! Only outsiders and the young call this bribery. Meanwhile, dilapidated roads and deteriorating health care standards are blamed on the irresponsibility of aid providers. As in Africa and other traditional, stagnant societies, this style of government has much to do with traditions of small, tribal societies that recognise the inherited authority of chiefs and accept the bonds of fraternal solidarity. In practice, the South Pacific experience is, of course, not all that different from pork-barrelling in the Western democracies. The difference is, however, that few people recognise this as a negative-sum game for the community as a whole; few people realise it is the cause of economic stagnation and a waste of aid resources.

Unlike Europe, where metaphysics and religion were separated from ethics after the Renaissance, and unlike East Asia, where Confucius pioneered ethical rules for social evolution 2500 years ago, the traditional, isolated and therefore fairly closed societies of the Pacific (and other less developed areas) lack deeply embedded social controls against rent-seeking and power politics. There are some sanctions in imported Christianity, but the basic philosophy of most people in the Pacific is not inimical to collectivism and tolerates the privileges of leadership.

The big challenge for South Pacific societies over the next generation will be to learn how to move between the valid, time-tested social model of the family or small community and the macro-model of the state and the national economy, at the level of what Hayek calls the 'extended order' (Hayek, 1988; 1979:153-76). Experience has taught us in the outside world that different modes of behaviour and different social conventions must be applied to the microcosm of our immediate surroundings and the macrocosm of modern society. European and East Asian societies have developed rules and restraints on natural instincts (e.g. by the rule of law, by property or honesty) that allow modern societies to increase 'in numbers and in wealth relative to other groups ... [enabling us] to sustain more from discoverable resources (and indeed in that very process discover more resources)' (Hayek, 1988:70). For example, private property offers the means and incentives for economic growth, although primitive instinct may induce us to seize (or socialise) whatever assets we come across. To cope with individual freedom and to learn sets of social behaviour conducive to modern productivity growth will not be easy in the South Pacific. But such rules are the foundation of economic progress.

It has become clear that the social rules of conduct which work so well within the family, the tribe or the small, intimate community, cannot be applied without great cost to societies with thousands, let alone millions, of members. In small groups, leaders are guided by knowledge and personal sympathy, which moderates their authority. However, the knowledge needed to coordinate, guide and monitor the actions of even a small nation can simply not be marshalled in one central location (like a cabinet or central plan office), and certainly not if society is continually developing and learning. Moreover, the personal knowledge, sympathies and solidarities with one's family members and friends, which temper the power of leaders of small communities, cannot be marshalled in relations between the leader and all members of a province or a nation. If a society the size of the average South Pacific micro-state is governed by the rules appropriate to small, familiar communities, then sympathies and solidarities are bestowed on immediate associates whom the leaders know directly. The other citizens get no such preferment and are disadvantaged, mainly because the effects of policy decisions on most members of larger societies are unknown and distant.

Mishaps and disorders occur under a paternalistic form of government. Collectivist leaders normally respond by more planning and better controls. But, as a consequence, the ordinary members of society only lose more of their freedom. The spontaneous forces of collaboration, imitation and evolution are lost. Centralised leadership, even if benevolent, destroys individual motivation to rival for economic gain and breeds indolence. When Pacific leaders promise free medicine or free transport, they are rarely aware of the destructive side effects on effort and capital formation. The result is a 'hand-out society' with few genuine entrepreneurs. Local people are then accused of not even supplying fish or fruit to hotels.

When larger societies evolve, as they have in the Pacific over the past 50 years, governments have, in many parts of the world, developed the rules that favour competition and spontaneous interaction amongst strangers. Minimum rules for good government require legality, accountability, public tendering, and control of governments by democratically elected assemblies. They also require small government because that ensures private property, which is the bedrock for a successful society of opportunity. These criteria facilitate the emergence of an extended order, which offers security and scope for decentralised experimentation by individuals, which in turn is an essential precondition for sustained economic development and cultural change. In an open, extended order, those who invent successful solutions for a problem or who import successful ideas from elsewhere will be imitated. This leads to a successful evolution which creates higher living standards and new cultural achievements and enables people to cope successfully with the inevitable adjustments to development.

So far, however, concepts like the European ideal of free, self-reliant, equal 'citizens of property' are still largely alien to most people in the South Pacific, as is the impatient aspiration for material betterment and democracy that we now observe in East Asia. The idea that living standards depend on work, saving, learning, adapting — in short, productivity — is less widely accepted than in the harsher environments of Europe or East Asia. After all, the concept of a 'cargo cult' is a Pacific contribution to the English language. Traditionally, people have displayed satisficing behaviour, trusted in their good luck, and solicited friendly support. This may be conducive to small group harmony, but not to sustained material progress and harmony within the larger national communities that have now been formed in South Pacific countries. Some leaders, e.g. in PNG, even consider the imported legal system or private property as alien elements in Melanesian culture and propose to discard these institutions. A wilful dismantling or breakdown of the law would make it impossible to maintain present living standards, let alone to ensure rising living standards for the rapidly growing population, because the law and its ethical foundations are essential preconditions for economic growth (Hayek, 1988:38-47;120-34).

To date, markets and individual or cooperative entrepreneurship are not great forces in the South Pacific world, partly because tradition, religion and foreign aid strengthen established hierarchical structures, and partly because the good life has so far not forced Pacific people into competition. Individualism is often distrusted in the Pacific and equated, especially by clergymen, with group destroying egotism. It appears, at least to the outsider, that only the social visions of paternalistic collectivism (of the right and left varieties) have a wide following. This is so because autocratic and caring colonial governments built on traditional tribal collectivism, as they wanted control and had little interest in the material advancement of the indigenous inhabitants. Colonial governments have been followed by equally paternalistic regimes. Few of them qualify as genuine, electoral democracies; instead they tend to preserve power within a small elite. But the results of this type of government are often iniquitous to the ordinary citizens: the exorbitant price of eggs in Port Moresby is due to the prohibition on holding chickens in backyards, the extortionate prices for staple foods in Vanuatu stem from the Prime Minister's grant of an import monopoly, and land regulations have created land shortages in many places.

Promoting Stability in the South Pacific

As we saw, the general surface calm and peace in the Pacific have given way to occasional flashes of violence, disruption, tension and conflict, as well as economic stagnation. The flashes are becoming more frequent and there has been a slow, subcutaneous drift towards a situation where overall harmony may, sooner or later, be no longer sustainable. It is possible, but not unavoidable, that the occasional flash will no longer simply relieve tension, but will trigger unpredictable chain reactions. The loudest warnings yet that such discontinuities may occur unexpectedly, were the events in Fiji in 1987 (Kasper et al., 1988) and the stirrings in Melanesia, including amongst New Caledonia's Kanaks and violent land-rights conflicts in Bougainville (PNG).

If the post-colonial gameplan becomes unsustainable, leaders and intellectuals should try to remove social obstacles to change before the problems become overwhelming. In such a situation, one should work towards reform and an evolution for the better while the going is still good, so as to avert uncontrollable and costly revolution later.

This applies first and foremost to leaders and the intellectuals within the region. But outsiders also have a role in shaping the region's future. In particular, Australians and New Zealanders have a self-interest in promoting growing prosperity and stability in the South Pacific. They, as well as the outsiders, ought to help turn social, economic, and political evolution for the better, in cooperation with the new generation in the South Pacific. A minimum constraint on outsiders should be that they acknowledge a responsibility not to support unsustainable, counterproductive trends by giving aid, even if it is easy for large, rich countries to inject substantial aid.

The key issue for the communities in the South Pacific is: Should they continue with tried, old ways, preserving the instinctively appealing, inherited social modes and procedures, even if this means economic stagnation, dependency and internal civic conflict? Should valued traditions, hierarchical structures, collective solidarity and sharing (so typical of the 'Pacific Way') be preserved, even if this means that increasing numbers of people slip from 'low-level affluence' into 'subsistence poverty' and aid dependency? Or should a new social and economic order with more individualism and equality before the law be encouraged to evolve, one that has been successful in the outside world?

It is increasingly evident that the existing social order is incompatible with the desired economic performance. There appear to be parallels with traditional, stationary European societies that had to come to grips with changing technologies and a dynamic economy 200 years ago. Europe was able to draw on a tradition of openness, change and the rivalry of diverse ideas (Baechler, 1975; Jones, 1981; Rosenberg & Birdzell, 1986). Achieving social evolution was easier in

Europe than for long-isolated, and often rigidly structured, South Pacific societies that have been catapulted into the modern world in less than 100 years. On the other hand, ideas are now transferred much more readily between different communities, and learning is easier for late developers.

Pacific communities will frequently not be compelled to make a black-and-white choice between traditional, collective, group-bound ways, and a purely individualist, competition oriented order. They may often be able to draw on traditional small group cohesion (extended family, the village) to modernise within voluntary associations, such as rural cooperatives (Kasper et al., 1988:90-2). However, it will be important that such cooperative associations are open and are not led by rent-seeking chiefs, and that people are given a chance to opt out, if they wish.

The Retarding Effects of Aid

Whatever mix of models Pacific communities choose for modernisation, clamouring for more aid from affluent, friendly countries is no solution. Aid only postpones the need for choice and deepens the dilemma. With the advent of development aid and national government, the spoils of interventionism have become bigger. And it seems generally accepted that high national office deserves its rewards. In PNG, for example, a sacked cabinet minister was reinstated while still under investigation for corruption. The dynamic, long-term costs of not adhering to the rules of an open society and of growing abuses of power have not yet been discovered in the young South Pacific countries. They have not yet had to make the bitter experiences that the outside world had to. Control mechanisms against rent-creation and rent-seeking (like the rule of law, genuine democracy, or a free and inquisitive press) are not firmly in place. This is of course not unique to the South Pacific. But what Buchanan observed as a general phenomenon certainly holds true in the South Pacific: 'Modern rent seekers are under no delusion about the "social good". They do not abide by the precepts of honesty, fairness, respect for the rule of law, etc. that are necessary for our civilisation to survive.' In the Pacific, too, it must be asked with Buchanan: 'Are we to accept their behaviour as a temporary aberration which cannot be changed by conscious effort, or are we to use the combined forces of scientific analysis and moral argument to defeat them?' (Buchanan, 1988-89:4).

Students of social evolution recognise that impasses and contradictions are now developing in the South Pacific, because the economic order is incompatible with economic aspirations. Openness, vertical mobility, and the scope for individual rivalry and self-realisation (which markets, civil rights and equality before the law offer) are increasingly needed to safeguard peaceful social evolution, cohesion, prosperity, stability, and a worthwhile challenge to the young.

The Success of the Market Order

Outside the Pacific, the competition of alternative socio-economic orders is now being overwhelmingly won by the individualist, liberal system. The sheer material success of the market economies has spawned privatisation, deregulation and reductions in central planning all around the world. Recently liberated entrepreneurs in many developing countries are now rapidly creating productive jobs where bureaucracies and central plans previously failed. The South Pacific could also benefit from relying much more on individual or cooperative initiative and the market place. This requires that government structures are pared back by selling publicly owned assets and cancelling many (normally imported) regulations on economic activity. Government should in any event be more along the lines of local government, and many national and international aspirations should be shunned. The affairs of the community should be managed within local council budgets. And, as is the case in the micro-states of Europe, aspirations to a national currency, a national balance of payments, national economic policies or a national defence force should be abandoned as inappropriate. The fixed cost of running a national currency and the small size of markets make it, for example, costly to run sufficiently deep foreign exchange markets and make it impossible to offer foreign traders the same currency amenities available in larger economies.

When the outsider raises such ideas, the answer is likely to be that this is against the 'Pacific Way'. The outsider will be told that those South Pacific people, who have been fully exposed to individualistic societies, as in Hawaii, Tahiti or Guam, have lost their identity. One hears pleas that the rat-race of the mass societies should not be imported into the South Pacific. And the belief is widespread that small, remote societies could not possibly compete in a modern, anonymous world. One also hears that individualism and rivalry have no place in small, intimate societies. The deeply religious people of the South Pacific also tend to invoke Christian reservations against the self-interested egotism of the market place. Instead, they advocate the fraternal community spirit of collective solutions. However, one soon realises that such objections invariably come from members of elites who have a personal, material stake in the status quo, including self-appointed Western experts who specialise exclusively in South Pacific affairs.

V. THE GAINS FROM LIBERALISATION

Promoting Economic Growth

Markets would stimulate entrepreneurial initiative and promote economic growth. What matters most for the sustained growth is the adaptation and use of knowledge. This knowledge is sometimes technical and readily described and transferred, but very frequently it is commercial, practical knowhow that needs to be acquired by trial and error and has to be adapted to the local scene and to changing times. If societies are managed by central bureaucracies, costly, ready-made imported packages of capital, technical knowhow and procedures tend to be acquired. This is even more so where tied aid subsidises the transfer of 'turnkey packages'. In contrast, private competitors are driven by the profit motive, which normally makes them cut costs by adapting imported solutions and by drawing on local assets. Entrepreneurs thus mobilise new local resources. More genuine rivalry of the market place would stimulate entrepreneurial energies into finding and developing the appropriate types of production for South Pacific locations. The solutions to production that are useful in bigger world markets may frequently not be appropriate to the South Pacific environment. Therefore, search and experimentation by many independent entrepreneurs, local or foreign, seems the best way to find solutions adequate to local conditions.

This is the reason for fast economic growth in those developing economies where the state has concentrated on making the supply of production factors elastic, by encouraging education and skill formation, saving and investing, the importation and adaptation of useful technologies, open international trade, and the attraction of direct foreign investments, but has desisted from direct involvement in production or from imposed detailed industry specific prescriptions (Kasper, 1989).

When contemplating the interrelationship between economic growth and competition, South Pacific leaders should look to public choice economics. For a long time, there was a tradition in economics and politics, stemming from notions of the virtuous Christian ruler, which assumed that knavish, self-seeking people would somehow turn into selfless knights who promote the common interest as soon as they acquired high public office. But public choice theory has demonstrated convincingly that there are markets for interventions in which politicians and bureaucrats make self-interested offers to supply regulations, and where licensed, self-interested producers demand regulation (Stigler, 1971; Buchanan et al. 1980; Brennan & Buchanan, 1985). It does pay for producers to be regulated, since that eases the intensity of market rivalry through price and quality competition and makes market niches secure against outsider competition (contestability). Interventions (including, in the extreme, by state ownership of assets) secure incomes that would not be possible under conditions of unfettered competition (rents). Firms then find it less urgent to compete by controlling costs and improving their products. And governments have normally found that regulation gives them prestige and influence, as well as material gain (for example for officials who serve on boards of companies).

Transport and Communications

Where the free market approach seems particularly necessary and promising is in the transport and communications sector. Competitive, inventive, and agile transport enterprises are crucial to overcoming, at minimum cost, the isolation of many South Pacific communities. Yet South Pacific governments have colluded with foreign aid givers and foreign government monopolies to create rigid, high-cost airline monopolies. These monopolies often fly inappropriate jets into oversized airports. Air Pacific, instead of having grown into a competitive trans-Pacific carrier thanks to its mid-Ocean base (as the private company Loftleidir of Iceland has done very successfully in the Atlantic), is now in danger of being 'loved to death' by the Australian state monopoly carrier, Qantas. In shipping, overmanned, loss-making, aid-supported ships (such as the mainly NZ-inspired, state-capitalist Forum Line) used for a long time to connect Pacific routes to high cost contact points with the world trade network, like Auckland and Sydney.[8] Some publicly-owned port authorities in the South Pacific are inefficient because their management owes more to

8. In 1989 the New Zealand government placed the Forum Line on a commercial footing by injecting funds (about two years' subsidy), by negotiating greatly reduced manning levels and off-times, and by privatisation. There are indications that this has made the newly-privatised company profitable, has improved services and lead to an expansion of the fleet.

the class struggle of the 19th century in far-away Britain than to the 20th century needs of the Pacific. South Pacific transport often suffers from Australian-New Zealand inspired union influence, and overbearing, cost-imposing administrative attitudes in public enterprise.

High transport and communications costs are a serious handicap to the small populations of the South Pacific (including the inhabitants of PNG, who are often isolated by steep terrain). Yet economics teaches us that people can prosper in small and remote countries. The precondition for this is that the transport costs to the big markets and from the big suppliers are borne by the remotely located producers. Living standards in competitive, isolated locations have to be somewhat low relative to the productivity that people attain, and this reduces the development potential in remote areas. But, by itself, this does not constitute a reason for income supporting aid.

To raise living standards, there is an urgent need to cut transport and communications costs in the Pacific. Private initiative could raise transport efficiency and versatility. Traffic monopolies have in the past been granted on the assumption that small scales of production would not merit competition. The costs of remoteness could be greatly cut by open skies and open port policies to attract new competitors and probably link South Pacific networks more closely to new, lower-cost contact points like Hong Kong, Singapore, Tokyo and Los Angeles. The privatisation of airports and port services would induce much creative cost cutting and would support a more flexible, diverse and versatile transport industry.

Depoliticising Resource Allocation

Another important advantage of a competitive approach is that markets depoliticise economic allocation. Where economic opportunity is regulated or the state is directly involved as a producer, decisions are made by administrative procedures in which political considerations matter. The long-term usefulness of a project to society (measured by the rate of return) counts often less than the short-term impact on the next election (measured by the expected return of votes). Administrative allocation induces the formation of groups and power-broking alliances (often around some criterion like regional origin or race), which offer political support in exchange for political favours. Organised client groups can deliver votes and tend to become better organised over time. Over time, younger leaders will try to compete for office by making more radical promises, so further distorting economic allocation. In such a system, economic growth gradually peters out. At the same time, rent-seeking stirs up passions and leads to political divisiveness, until, in the extreme, society becomes ungovernable (Rabushka, 1974; Sowell, 1983, 1990). Where, in contrast, allocation is left to the open market economy, possible conflicts are dispersed to the inter-personal level at which the conflicting interests of buyers and sellers are moderated by the 'invisible hand'. Traditional tension within countries like PNG or Fiji can best be reconciled if the flexible method of market allocation has a greater role and the state confines itself to a minimum role, providing a framework for market rivalry. Moreover, the invisible hand does not have to be greased. This aspect of the market order is an important consideration in several South Pacific countries, where allegations of corruption are heard.

Providing Opportunities for the Young

Another, important advantage of market competition has to do with more equitable challenges and opportunities for the young. In regulated, administered economic orders, the established, well-connected few tend to get ahead. They know what forms to fill out, what official to approach or bribe, who will pull what strings, what lawyers to hire, or how to get credit from the state development corporation. The less well-connected, including the uneducated young, have no access to these economic opportunities. They have few formal skills to join public administrations or regulated, high-class firms. And employers do not have to bother much with training unskilled youngsters. This is particularly the case where minimum-wage regulations keep unskilled young people from getting their foot on the first rung of the skill ladder, which gives access to learning-by-doing. The result is the alienated, frustrated, if not criminal and rebellious, youth that we increasingly observe in the Pacific.

Leaders concerned with the growing youth problem in the Pacific should be reminded that the unregulated market has, since time immemorial, drawn young people into working life, albeit initially by offering low rewards to reflect initially low productivity. With on-the-job learning and experience, their productivity will rise and so will the wage. This procedure may not appeal to the materially secure, 'new class' bureaucrats or the foreign observer. But disorderly, unlicensed job creation for the young is preferable to youth gangs of the type that endanger law and order in Port Moresby. [9]

9. In the context of the South Pacific youth problem, we should mention the experience of heavily-regulated Latin American countries where black

The demonstrated advantages of the market economy will make it, in the longer term, impossible for the South Pacific societies to avoid facing up to the challenge of market-oriented attitudes, whether through individual enterprises or through small cooperatives. This will entail some changes in traditional Pacific ways: more work, more systematic work, more saving, and a longer-term planning horizon.

The hierarchical Polynesian and Micronesian societies will probably have to overcome greater hurdles in adopting a materialist and competition-oriented social order than the Melanesian societies, whose inherited traditions are more akin to Western material attitudes. However, other societies with cultures that were originally averse to favouring individual competitive effort and enterprise have adapted successfully (e.g. the Japanese). The Polynesians, whose forefathers were risk loving, enterprising seafarers, whose voyages opened the vast South Pacific, and who developed a distinct material culture and civilisation in remote, resource-poor islands, should have the confidence that their cultural inheritance will facilitate the required social evolution. They may also take heart from the many Polynesians and Micronesians who have ventured into the outside world, and have adapted well to an extended, individualistic order. After all, South Pacific societies have been open and receptive to outsiders and outside ideas, in most instances without losing their self-assurance and identity.

VI. AID FOR STATIST POLICIES VS SELF-HELP

The Pacific tradition of collectivism has been reinforced by well-intentioned, corporatist influences from the outside. Many of the missionary teachings built on existing communal solidarity and existing hierarchies, and the predominant American, Australian and New Zealand influence in the newly-independent nations has been massive, state-reinforcing economic aid. This tendency has been further strengthened in recent years by a rapid build-up of Japanese aid. Much Japanese aid places big ticket projects in small Pacific locations with little concern for recurrent costs or sustained rates of return (or, rather, with the assumption of Japanese efficiency in making complex

markets and (strictly speaking illegal) economic activities in the informal sector have given young people and families the chance to produce and trade for their own benefit (de Soto, 1989). There is simply no need to license market stalls, taxis or exporters of produce. South Pacific governments could emulate East Asian governments which have set up small enterprise zones and market areas subject to minimal regulation.

lumps of capital work).

Most official development aid is typically channelled to government agencies and into big, easy-to-administer projects that are managed in bureaucratic administrative ways (note that we are concerned here only with economic aid designed to raise living standards, not with humanitarian aid to people living in extreme poverty or suffering the effects of natural catastrophes). Thanks to aid, South Pacific governments often can afford to aspire to emulating the style of fully blown national governments elsewhere.[10] They then set up elaborate government apparatuses in costly modern buildings, as if they had to care for many millions of citizens. They imitate five year plans full of prescriptive, irrelevant details, not least to impress aid-giving agencies, and set up aid-receiving agencies to interact with the mega-bureaucracies in Washington, Canberra or Paris.

Publicly-funded and administered education systems further reinforce the perception that living standards are unrelated to own effort, often through idealistic foreign school teachers and, at least in the case of social sciences in the two foreign-financed universities in the region (the universities of the South Pacific and of PNG), through teachings that often owe more to Bengali or New Zealand Marxism than to European liberalism!

Imported Trade Unionism

Another piece of anti-development ballast imported from Australia and New Zealand has been trade unionism in the small modern sectors. Australian-inspired unionism and price-indexed wage arbitration in PNG are responsible for exorbitant wage levels in the modern and public sectors. PNG manufacturing wages are four times those of Thailand; in the Solomon Islands they are twice as high. It is not surprising that no one invests in export-oriented manufacturing and that youth unemployment is around 25 per cent in PNG. Aid-supported governments in particular have been able to act as the pace-setters in wage increases that were unrelated to productivity or any other economic criteria (though a remarkable exception occurred in Fiji in 1987 when relatively highly-paid public sector employees had to take salary cuts after the politically-triggered economic reces-

10. This is sometimes pushed to ridiculous lengths. For example, in July 1989 the micro-state of Kiribati was to hold a Pacific ministerial meeting. There was of course insufficient accommodation for such an event. But the Australian government, at enormous cost to the taxpayer, provided a major Navy ship so as to allow Kiribati to play a grand international role!

sion). Exorbitant wage levels have been further reinforced by the privileges of expatriate aid workers. As a result of high public sector pay, ambitious and gifted young people typically seek government employment and have created aid-dependent administrative structures that undermine the potential for future economic growth.

The Aid Claim Mentality

Most of the best-educated people in the South Pacific are now card-carrying members of a class of professional aid-seekers, who increasingly regard foreign aid as a right (and threaten to make political mischief if they don't get it). The extent to which aid from the rich Pacific rim nations has come to be demanded by the privilegentsia as a right rather than a temporary gift is illustrated by the following press quote, chosen at random and representative of many similar instances:

> Palau has accused Washington of failing to provide its people with adequate health and social services. Palau's Vice-President [said] ... the US had failed to fulfil its duty ... and had left the archipelago economically weak. ... the US had not provided one dime for the electric power plant Palau relied upon, and had not helped to fix school buildings, roads, bridges and sewers. Palau needed a new hospital ... There was also no US funding for drug abuse programs for youth.

The report ends with the information that Palau received about $US33 million in US aid in 1988. This is about $US2700 per inhabitant and slightly more than the reported per capita income of Palau (*The Australian*, 17 May 1989).

A litany of similar demands can be found in publications by Pacific lobbies who, in reality, often display unacceptable, even insulting, post-colonial attitudes. Thus, a joint workshop of Australian academics and Pacific island professionals produced a long wish list of demands on the basis that much of the blame for what goes wrong is laid at Australia's doorstep (Brookfield & Ward, 1988:58). They expressed the strong belief that, because of the legacy of colonial rule and recent private investments, Australia has a moral obligation to offer large-scale aid. The fact that Australia was not a colonial power (except in PNG) and that private investors cannot bind Australian taxpayers to give more were conveniently overlooked, as was the fact that these nations are now in charge of their own fate and responsible for themselves. The guilt industry argues for open-ended, unconditional 'aid with dignity', preferably budget aid (which frequently is not even properly accounted for and dished out from sinking funds that are beyond the parliamentary control of recipient countries) or balance of payments support for whatever import bills are run up (e.g. for fish and beer, two major import items in many Pacific nations).

The aid-claim mentality displayed in the South Pacific shows all the traits of welfare-dependency in Western countries. As is the case with the rent-seeking in our welfare systems, aid distribution can never end poverty, because these very policies undermine the will for self-reliance and productive effort. Open-ended development aid policies create their own tightly-knit pressure groups of beneficiaries, in particular an aid-dispensing bureaucracy and the privileged spokesmen in the recipient countries. No leader of a Pacific nation has, of course, much incentive to remove the need for support. And donor countries find it relatively easy to keep providing aid to the small communities in the South Pacific. Saving a few million dollars is not worth the political and administrative cost of winding down aid budgets.

If aid reliance were scaled down in favour of individual achievement, people other than the 'administrative rich' would prosper, like the energetic entrepreneurial 'doers', often young people born without privilege and with no connection to the ruling elites. These people would, in the first instance, not set up large, conspicuous operations, but would probably try small business experiments. This has happened in Fiji. Since the coups, a very severe, politically-induced recession and a cut in aid and government regulation have created a number of new entrepreneurs who started garment manufacturing. They are mainly of Indian, i.e. non-privileged, origin and have, in the midst of great adversity, been quite successful in creating jobs in export businesses (Kasper et al., 1988:93-7). This development has been denigrated as providing 'substandard jobs', yet these jobs pay workers about the national average per capita income. Foreign observers may deplore this, especially visiting trade union officials, who are not altogether uninterested in eliminating low-cost competition! But these new jobs are capable of producing output that is competitive in Sydney and Los Angeles. It seems doubtful whether these enterprises would have been possible if aid to Fiji had not been cut and the local currency had not been devalued as a consequence.

Foreign aid also makes it less necessary to control production and distribution costs in the Pacific. For example, aid has led to bizarre import-substitution policies in some small South Pacific countries; these have driven up overall cost levels and now curtail export opportunities. Border protection has often been made almost a condition for granting foreign aid. Thus, Australia prides itself for having given costly and massive support to promote national self-sufficiency in (high-cost) rice, beef and dairy products in Fiji, which is tied to Fiji import protection. But the aid-provided model farms exploit the average consumer by charging high prices (a regressive effect on income distribution) and stifle local private agricultural enterprise.[11] Other aspects of the same aid/high cost syndrome have been, as already mentioned, centralised wage-setting and high minimum wages (in the small formal sectors), which are totally unsuited to developing country conditions and have impeded job creation.

Massive aid inflows (as well as remittances from relatives who work in Auckland, Sydney, Noumea or San Francisco) have the further, insidious economic effect of pushing up the exchange rate in those small nations that run their own currencies. This makes for an 'aid variant of the Dutch disease', in which strong currency receipts make it harder for local producers to be competitive in world markets, because their local wage is too high in US dollar terms. It is therefore quite possible that massive aid to some of the small South Pacific countries and territories has, on balance, destroyed jobs, not only because it has removed the incentive to work and compete, but also because it has led to an overvalued exchange rate. South Pacific nations might be advised to follow the example of those East Asian countries that have weaned themselves so successfully from development aid.[12]

If the rich nations with an interest in the South Pacific want to promote stability and economic self-reliance they should first and foremost help to facilitate trade, and not rely on aid. The offer of free market access to Australia's and New Zealand's protected markets (on

11. Since the massive economic collapse in the wake of the 1987 military coups, Fiji has been reassessing some of its import-protection policies. Some export-processing zones and selective export promotion have been instituted to neutralise Fiji's self-imposed cost-level disadvantages of regulation. This deregulation has produced welcome economic results (Kasper et al., 1988).

12. It appears that the new government of the Solomon Islands has begun to take a critical look at aid projects and the role of expatriates. It is, however, not clear how far this review is driven by critical economic analysis and in how far it reflects a nationalist-collectivist attempt to extract more of the rents for local powerbrokers.

certain, limiting conditions) under SPARTECA has probably had a helpful effect in turning potential producers in Pacific countries towards exports.[13] In a number of cases, this has helped to kick off new ventures in export trade. But SPARTECA has also led to public protests of (long-feather-bedded) garment unions in Australia and New Zealand.

If Australia and New Zealand, or the partners in a future Pacific trade arrangement, are really serious about helping their South Pacific neighbours, they will open their markets completely and remove all limiting conditions from SPARTECA for all products of South Pacific provenance. If the South Pacific nations were equally serious about growth by trade, they would stop experimenting with administrative gimmicks like special export zones and make those zones nationwide, as Mauritius did with good effect. Those South Pacific countries who opt for a free-trade strategy could convincingly plead for duty-free access for their products to big markets around the Pacific. Since theirs are small and poor economies, they have a very good chance of readily gaining concessions.

The Ten Commandments of Foreign Aid

As it is unlikely that the first-best solution — gradual elimination of all economic aid — will be acceptable, at least the following 'ten commandments' of foreign aid ought to be adhered to:

1. Whatever official economic aid is given in future should be channelled into general, functional uses. This means that aid should help to make the supply of production factors plentiful and elastic by assisting in education and technical training, by helping with the improvement of the infrastructure, by facilitating the transfer of knowledge and technologies, and by making temporary loans of skilled overseas experts.

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13. SPARTECA is a multilateral agreement between Pacific island nations, Australia and New Zealand that gives Pacific exports preferential access and assists the island nations in gaining market shares. Since January 1987, many products from these nations have been allowed to enter Australia and New Zealand duty-free. But there are exceptions, e.g. exemptions to shore up Australia's protectionist policies on garments, textiles, footwear and sugar. In addition, there are tight and inconvenient rules of origin that limit processing in the Pacific nations (Kasper et al., 1988:120-2).

2. Aid should never be channelled to specific, privileged industries, and certainly not into state-owned ventures.

3. Given the politicisation of allocation by elites and the poor resources of administration and accounting in the South Pacific States, aid should never be provided in the form of unconditional budget or balance-of-payments aid.

4. Aid should discriminate as little as possible between specific activities and locations. Neutral assessors should estimate the long-run social rate of return, and auditors should monitor these assessments after the event and be able to recommend remedial action.

5. Economic aid should be put where it promises a high return and should not be allocated on a 'needs' basis, because that wastes aid and misdirects scarce local resources.

6. The donors should give aid on the firm condition that trade protection is reduced, as well as regulation and state ownership. Aid could thus serve as a countervailing force to a built-in tendency to rent-seeking.

7. Aid should not be offered where there are blatant abuses of civil and economic freedoms, because that undermines the ultimate usefulness of aid to the recipient citizens.

8. Aid should not contribute to inefficiencies or inequities that are unacceptable in the aid-giving countries. If, for example, the land tenure system inhibits rational use of scarce land, aid should not compensate for the resulting, self-imposed losses. This must not be considered as interference in internal affairs, but should, on the contrary, be accepted with the understanding that aid recipients always have the sovereign right to reject conditional aid.

9. As much aid as possible should bypass the sticky fingers of aid bureaucracies to be distributed and administered privately. Voluntary, private agencies are capable of combining financial provision with practical advice and support, even if aid officials find administering such aid dispensation

cumbersome and messy.[14] This would correct the bias towards big ventures, which is often inappropriate in the small Pacific communities.

10. All aid programs should be offered on a strictly temporary basis with clear sunset clauses.

VII. COPING WITH SMALL SCALE: EVOLUTION OF A PACIFIC UNION

An excellent way for some or all of the many micro-states of the Pacific to overcome some of the handicaps of small scale would be to form an economic and currency union, as 13 small Caribbean nations are now doing.[15] Pacific nations could become (politically and culturally different) 'cantons' within a Pacific Economic and Currency Union. This would allow individual Pacific communities to devolve many tasks of 'national' policy and would save its citizens great expense, since there are high fixed costs in running a national government. Such a union might evolve gradually and possibly from a core of pioneers, just as European integration was inspired by the Benelux idea. No grand design needs to be adopted. A gradual, evolutionary trial-and-error approach seems more appropriate. The Pacific Union could grow organically, with some small states making a start and others joining when they realise its value. A Pacific Union now seems technically feasible thanks to modern communications (satellites, fax

14. Much might also be gained by imitating the US experiment with semi-privatised aid in the Caribbean where boards of trustees that are made up of local businessmen are appointed to serve on US-financed investment trusts, whose charter it is to help small- and medium-sized local enterprises. The trustees are given a direct financial interest in the success of the ventures that they select for support, so that they tend to combine US aid money with their own management skills and entrepreneurial expertise to ensure success. Such direct incentives do not exist in bureaucracy-run projects.

15. Thirteen English-speaking Caribbean countries decided in July 1989 to fully integrate their economies within four years (*The Australian*, 10 July 1987, p.7). This initiative appears to differ greatly from the many attempts by groups of developing countries to form customs unions which have created inward looking, protectionist policies and have all failed (Vaitsos, 1978). A genuine economic union means central management and does not imply the erection of an external tariff wall.

machines etc.).

The evolutionary growth of a Pacific Union could start with the formation of a currency union. At present, the costs of administering small currencies far exceed the gains from seigniorage. The small Pacific currencies do not allow sufficiently deep, properly functioning spot and futures markets for foreign exchange or proper financial markets: important aspects of an efficient monetary system. It may even be advantageous for a Pacific Union to abandon all aspiration to an independent exchange rate policy and to tie the common Pacific currency to a major currency in the outside world (e.g. the US dollar, the yen, the Australian or New Zealand dollar, or even to gold). The Pacific Union might even abandon a separate currency altogether. This would remove all balance-of-payments concerns, reduce the risk of inflationary accidents, and enhance the attractiveness of the South Pacific to foreign investors. It would of course also stop governments printing money to finance budget expenses.

A Pacific Union could not aspire to maintain external protective trade barriers (Drake & Hall, 1987). But it could adopt trade policies that facilitate internal and external exchange. A Union-wide trade policy could also protect the various local governments from illusions of national economic independence, i.e. protect them from the temptations and costs of import substitution. A Pacific Union would be big enough to run transport policies, support inter-island transport services and offer Union-wide information services to attract tourists and investors. Passport controls could be abolished or at least greatly simplified. In the newly-emerging Pacific trade initiatives, a Pacific Union could act as a more equal partner. The major Pacific rim nations could assist by giving the Union generous free-trade concessions.

Trade or central bank policies would no longer absorb the resources of the micro-states, and the governments of the various 'cantons' could concentrate on the tasks of local government, such as ensuring law and order, providing local infrastructure, supporting education, safeguarding the environment, or attracting job-creating capital from overseas. Given the severe limits of administrative and financial resources in the Pacific, fewer administrative tasks mean better government.

Economic cooperation in a Pacific Union could be strengthened if aid for the member countries were given to the Union and it was left largely to the representatives of the member countries to distribute it. It would seem possible to form a consortium of aid donors (possibly under International Bank for Reconstruction and Development [IBRD] auspices) that offers not only resources but also advice and expertise. The Union might also subcontract the administration and implementation of aid projects to private investment trusts. There seems a good chance that discussions on the best possible use of aid at the Union level would shift the emphasis away from local rent-seeking and political favouritism. The procedure would also make it likely that aid is properly accounted for.

In all likelihood, there will be little immediate support amongst the elites in the Pacific for a Pacific Union. After all, nationhood is a new and cherished experience, and nationalism gives rent-seeking a certain respectability. Nevertheless, economic and political problems are likely to grow, and a new, post-colonial generation may want to try a new and rational approach. They may see that closer cooperation in an organically growing Union offers them a chance to tackle established interest groups. And foreign countries may prefer a prospering and integrated South Pacific, much as the United States viewed Europe in the 1950s.

VIII. CONCLUSION: ETHICAL AND CULTURAL CONSEQUENCES OF OPENNESS AND COMPETITION

Pacific nations need not resist evolution by competition for fear of cultural homogenisation of their small societies, or that they might lose their own distinctive, and rightly cherished, cultural values. Adapting to a growth- and performance-oriented economic lifestyle does not mean that treasured and valuable social traditions have to be abandoned. Experience demonstrates that one can absorb Western technology, management and economic modes of behaviour without giving up one's Chinese, Malay, Korean, Japanese, or Indian identity. The industrially flourishing Asians are now enriching the global industrial civilisation by making their own, culturally based contributions, and people in Europe and America are eager to emulate them. Indeed, growing material welfare allows inherited cultures to flourish and stimulates their further growth, whereas materially-weak civilisations are culturally on the defensive and may eventually lose much of their identities. After all, a culture is a living organism that evolves and thrives by absorbing new concepts. It does this much better when the material civilisation flourishes.

It would be desirable for the world at large if the culturally-rich and varied South Pacific nations managed to integrate their cultural heritage with the economic and technical world civilisation. Much would be lost to mankind if, because of a refusal to evolve and adapt, the South Pacific contribution were to languish on the defensive as a folkloric curiosity or a subsidised museum piece. But with economic vigour, old and new influences can integrate and cultures can grow. We could then, maybe, look forward to the first Fijian-made world hit movie, to a Kanaky-inspired management style for retirement villages around the world, to a flourishing trans-Pacific airline with South Pacific cabin service, or the first worldwide consumer product that is inspired by PNG Highlanders!

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Commentary

Colin Simkin

I find myself so much in agreement with these three valuable papers that I can offer little more than supportive comment and some qualification to statements that seem to me to be in need of qualification.

Lord Bauer, with a typical application of sound common sense to acute observation, strips away much of the humbug that has become accepted opinion in regard to foreign aid, and exposes the damage that it has done to both recipients and donors. Mr Siwatibau has had practical experience of aid administration in the Pacific island countries, and draws on it to give us an informed report of their problems and prospects. Professor Kasper gives a thorough analysis of those countries, which are extraordinarily dependent on foreign aid, and convincingly argues that they must seek a different path to economic growth.

What we have first to grasp is Professor Bauer's point that foreign aid is a transfer from donor governments to recipient governments, either directly or through multilateral agencies such as the World Bank, the IMF or the EEC. It excludes private investments, donations from charitable organisations, or remittances from expatriates. During the 19th century, entrepreneurs and governments in developing countries were able to get private foreign capital for sound, and even unsound, projects; it was in this way that Australia, New Zealand, South Africa, Canada, Latin America, Southeast Asia, and even India and Sri Lanka developed, as well as Fiji and Papua New Guinea. In our time, developing countries would find much less difficulty in obtaining loans from the world's vastly greater capital markets. For sound projects, that is, but it is only sound projects that can use capital transfers to promote economic development. It follows, as Professor Bauer says, that the maximum contribution that foreign aid can make to a recipient country's economic development is limited to the cost of

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servicing the debt that would correspond to the aid transfer: a maximum contribution that must always be much less than this transfer.

But the actual contribution will be even smaller, and may well be negative. For the transfer does not go directly to productive uses but to governments, i.e. politicians and bureaucrats. It is notorious that a good deal of aid is corruptly used to enhance the wealth of politicians and bureaucrats rather than the general welfare of their subjects. Much of it has also gone to finance show projects of an uneconomic nature: e.g. new national capitals, such as Islamabad or Brasilia; pretentious administrative buildings, such as can be seen in Kuala Lumpur or Canberra; a national air or shipping line, such as Air Pacific and the Forum Line; etc. etc. Too often the remainder goes to inefficiently-run nationalised industries, or is filtered through elaborate bureaucracies to private enterprises that are handicapped by administrative controls and that obtain funds and licenses more by lobbying than by merit. It is not surprising, therefore, that demands for aid continue to grow after more than four decades of aid-giving. Only Japan, South Korea, Taiwan, Hong Kong and Singapore have used aid effectively enough to dispense with it.

These countries, although not perfect examples of market economies, have vigorously promoted private enterprise to gain its well-known benefits — and with spectacular success. But most others (Thailand is an exception) have used it to pursue, or to maintain, socialist or semi-socialist policies based on some kind of central planning. Foreign aid to them has, accordingly, impeded economic development more than it has helped it. I have always found it paradoxical that the US-dominated World Bank, even during the Eisenhauer Administration which was particularly hostile to domestic macroeconomic planning, made its aid to developing countries conditional upon the drafting of five-year economic plans. And that at a time when few of them had either satisfactory statistics or personnel capable of preparing macro-plans. About all that could be said for such plans is that they were good enough to secure aid. And so, from its very inception, foreign aid was increasingly channelled to countries where it did the least good because of the associated crippling of free enterprise. One such country was India which, particularly in the 1960s, was arrogantly holding up to other countries its own misguided planning system as the model for Asia.

Yet more went wrong than economic results. Professor Bauer stresses the hostility that recipient countries have developed, individually and collectively, towards donor countries: the so-called East-

West, or North-South, divide. Such hostility, of course, is a common result of aid, and is not confined to the Third World. During the 1939-46 War, I served alongside American forces, and became friendly with a Midwest Republican who, as you might expect, was a strong isolationist. He deplored his country's entry into the European war and, during one of our arguments, made a striking prophecy. 'We are bound to win that war', he said, 'and after it we'll be asked to give huge sums to put Europe on its feet again. We'll be mugs enough to do that — and we'll become the most hated nation on earth.' I saw what he meant when I mixed with people in Oxford and the LSE in 1948 and 1949. Not that unreasonable and ungenerous anti-Americanism was confined to Britain; we have had plenty of it here.

It is not surprising that Third World hostility focuses on the widening gap between income levels in the least developed countries and those in the more advanced countries. But it is wrong to ascribe this to lack of aid. All that aid can do is to help the growth of productive capital, and even in advanced countries productive capital and natural resources are less important for general economic growth than 'the conduct of people and their governments', as Professor Bauer puts it. To grasp this point, we need only compare Australia with Japan, New Zealand with Singapore, Sri Lanka with Switzerland, or Pakistan with Thailand. There is, moreover, much blatant hypocrisy in appeals for foreign aid to relieve evident and deplorable poverty in Third World countries by governments that provide no aid for their own poor and foster more glaring inequalities of income within their borders than are tolerated in any Western country.

I would qualify Professor Bauer's analysis in only one respect. The economic consequences that he exposes are not necessarily confined to intergovernmental transfers. After the first oil shock of 1974 the World Bank, the IMF and the US encouraged private financial institutions to recycle petro-dollars by generously lending to governments of Third World countries that were net importers of oil. This recycling was accompanied by massive increases in the money supplies of both lending and borrowing countries. The result has been that many Third World governments incurred huge burdens of external debt, burdening major financial institutions in Western countries with what is called a crisis of sovereign debt. I conclude that private lending to developing countries gave even worse results than the intergovernmental transfers which they largely replaced, and that such lending can be very dangerous in the absence of appropriate limitations upon money supplies.

Professor Bauer's political realism makes him pessimistic of even minor reforms to foreign aid, in spite of its glaringly counter-productive effects. Professor Kasper is more optimistic, although foreign aid exceeds GDP in five of the 19 countries in his survey of the Pacific Islands, and is at least one-third of GDP in another five of them. Six of them, too, depend heavily upon remittances from nationals working in Australia or New Zealand. But twelve of them are very small, with populations below 100 000, and the smallest, Tokelau, has less than 2000. Not unnaturally Professor Kasper pays most attention to PNG, which has over 3 million people, and to Fiji, which has three-quarters of a million. (He is familiar with Fiji's problems as a result of leading a team of Australian economists to investigate its problems after a military coup had suspended democratic government because of considerable racial tension between Fijians and Indians.)

All of the Pacific island countries, except Tonga, were under colonial rule, and when most of them became independent states they adopted the forms of democratic government. But, Professor Kasper emphasises, these forms are largely a facade for deeply rooted tribal systems that are characterised by the traditional authority of chiefs and by what he calls 'paternalistic collectivism'. This had been reinforced by colonial protection of traditional customs and rights, especially land rights. Contact with the West gave markets to native cultivators for copra, bananas, oranges, and fish. In Fiji, indentured Indian labour cultivated sugar plantations, and European enterprises extracted timber and gold from Fiji and PNG and timber also from Vanuatu. Resulting imports, and modern schooling, created tastes for Western goods, and these were greatly developed after independence by foreign aid, which in many cases came to exceed export receipts, and by the familiarity with higher living standards that resulted from large numbers of islanders migrating to Australia or New Zealand for work, either temporarily or permanently.

The result has been a great discrepancy between aspirations for consumption and domestic means of satisfying them. So far the gap has been met mostly by transfers of aid or remittances, and by emigration, rather than by developing island resources. Professor Kasper shows that there are more obstacles in the way of development than lack of natural resources and distance from overseas markets. Chief among them, he says, is the persistence of paternalistic tribalism, reinforced by all the adverse consequences of foreign aid which Professor Bauer has exposed. In Fiji, paternalistic tribalism has had the unfortunate effect of fostering damaging racial tensions as Indians have very limited access to natural resources and dominate the country's more modern economic activities. The biggest field of employment for well-educated Polynesians or Melanesians is government service, in which they become adept in preparing aid applications and in drawing up, or administering, five-year economic plans.

These plans involve regulations and licensing, which reinforce the effects of paternalistic tribalism in hampering private enterprise and the development of a market system, and so all the attendant benefits which Adam Smith stressed for the division of labour. They have also been accompanied, in some island countries, by nationalisation of expatriate enterprises or by the creation of government enterprises or monopolies. It is not surprising, therefore, that real GDP, in most island countries, has lagged well behind population growth and that they are so dependent on foreign aid and remittances for maintaining unsatisfactory standards of living.

The obvious way out of these difficulties is to replace paternal tribalism and restrictive planning by a system of open markets and free enterprise. But in Melanesia and Polynesia, there are serious obstacles to such a transition. The main one is the attitudes of the peoples concerned. Much effective power is held by those who would feel most threatened by the decay of paternalistic tribalism. Its inherent collectivism has been supplemented in various ways by Western influences on trade unionism, labour legislation and education. Professor Kasper points to the influence of foreign school teachers in indoctrinating primary and secondary school pupils, and to the Bengali Marxism that is dominant in the social science faculties of the Universities of the South Pacific and PNG. In Fiji, the election victory of a coalition that defeated the Alliance Party in 1987 could be interpreted as a popular revolt against paternal tribalism. But the leaders of the coalition, mostly Indian, were far from demanding free enterprise. What they wanted was more nationalisation, unrealistic social welfare services, and redistribution of incomes.

As Professor Bauer said, economic progress depends basically upon the economic attitudes and qualities of people and their rulers. Throughout Melanesia and Polynesia there is, for the reasons Professor Kasper gives, little in attitudes or qualities that are favourable to transition towards open markets and private entrepreneurship. That is illustrated by the difficulty in finding examples of Melanesian or Polynesian entrepreneurship. Fiji's Indians provide nearly all of that country's businessmen, but have not voiced any demand for a free enterprise economy. Although popular discontent has grown, and in all probability will grow, with the economic stagnation of the island countries, it is difficult to see how this can lead to improvement in their economic conditions until there is influential leadership in persuading people to get rid of traditional and socialistic shackles on enterprise.

Professor Kasper, like Professor Bauer, would prefer to see foreign aid cease, despairs of that, and outlines ways of lessening its bad effects. The main one is that aid should become conditional on moves being made to reduce 'protection, regulation and state ownership'. Yet much of the aid comes from Australia, which is far from having realised Professor Kasper's conditions, and they would hardly be acceptable to the recipient governments until there is better understanding in their countries of the vices of regulation and the virtues of free markets. The same qualification applies to his further suggestion of a Pacific Union that would have a common currency tied to an external currency, and adopting policies that facilitate internal and external trade. And it seems to be half-hearted; Professor Kasper admits that it would have 'little immediate support' in view of strong feelings of nationalism and political independence.

Outsiders, therefore, can hope to have only an educative influence. In my view, organisations like the Centre for Independent Studies, besides continuing efforts to persuade their own politicians and people of the advantages of economic liberalism, should also try to persuade them of the need for drastic reform of foreign aid. And they could well extend such efforts to persuading similarly governments and peoples in the Pacific island countries. The CIS, indeed has made a good start in that direction with its 1988 publication *Fiji: Opportunity from Adversity?* (by W. Kasper, R. Blandy and J. Bennett), which inaugurated its *Pacific Papers* series.

In his paper, Mr Siwatibau mentions the effect of aid and remittances in raising wages and salaries, particularly in the public sector. The consequences include adverse effects on agricultural growth (particularly marked in Tonga, Samoa and the Cook Islands), excessive urban drift, and much unemployment. He also notes that foreign aid has maintained overvalued exchange rates.

Of considerable interest is his report that there is an expectation of foreign aid being reduced by donor countries, and some moves to reduce dependence by a few of the smaller island countries. Kiribati has decided to forgo annual budgetary grants, and has used its last receipts from Ocean Island phosphate to acquire a portfolio of foreign assets that meets part of its budget deficit. Both Tuvalu and the Cook Islands have started a similar reduction, and Vanuatu ended its budgetary aid in 1988.

Also of interest are his remarks about education. Arts graduates find it difficult to obtain employment, but there are unsatisfied demands for commercial and artisan skills. He stresses the importance of restructuring education to meet changing demands for skilled workers.

Large excesses of imports over exports, prospective reductions of foreign aid, and the general need for economic growth all point to the need to stimulate private investment. Mr Siwatibau recognises that this requires deregulation of the business and financial sectors, as well as political stability and good industrial relations. There are only a few signs of these conditions being provided, although the Fiji government has sold part of its holding in Air Pacific to Qantas, and is trying to sell the Fiji Sugar Corporation to the public. That is a pity, not only because of their present difficulties, but also because of the potential for economic development offered by huge fishing grounds, large forested areas, important mineral deposits (in PNG, New Caledonia and Fiji) and undoubted attractions for tourists. All this, as Mr Siwatibau, emphasises, could be attractive to the rapidly advancing economies of the Pacific rim.

How much has to be done is indicated by the imperfect statistics for employment. In PNG, much the largest of these island countries, less than 2 per cent of the active population is employed in each of manufacturing, construction, commerce or transport. In Fiji, perhaps the most diversified country, manufacturing accounts for only 8 per cent, construction for 5 per cent and commerce for 11 per cent. More than half of the island countries have very little or no manufacturing, and more than one-third very little commercial activity. Transport is only a little better.

My own feeling is that the main factor holding up economic development in most Pacific island countries is their people. I cannot regard such excuses as limited duration of exposure to the world economy or geographical isolation as in any way decisively important. Japan, Korea and Taiwan have not had a longer exposure to the world economy and both South Africa and New Zealand are at least equally distant from world markets. Nor do I think that educational backwardness is a reasonable excuse. Most island countries have long had better provision of elementary public education than rapidly-growing Thailand or Malaysia, and higher education in Australia and New Zealand has long been open to those islanders who could afford it or obtain scholarships. I am confirmed in this opinion by what I have seen in visits to more than a few island countries and, in particular, by a judgment of the head of a development bank. When I asked him what, in his opinion, was holding up economic development in his own island country, he replied, 'I am afraid it is our men'.

This, of course, is not to suggest any kind of racial inferiority in regard to abilities; I have had too many good students from Pacific island countries to entertain such an idea. What it does suggest rather is the need for radical change in outlooks and institutions, and I would hope that such changes will no longer be delayed, as they have been, by inappropriate policies of foreign aid and domestic economic regulation.

Commentary

Peter Jennings

IN his essay, Lord Bauer outlines what he says are the three arguments most often heard in defence of aid: promotion of development; relief of poverty; and furtherance of the political and economic interests of the donors. Australian and New Zealand aid programs to the South Pacific have, for the most part, been justified by reference to the first two arguments but motivated to a greater extent than is usually acknowledged by the third.

The three essays presented here provide ample theoretical argument and empirical evidence to demonstrate that aid cannot always be seen to promote development and relieve poverty. Even the Australian and New Zealand agencies charged with the disbursement of aid recognise that their programs fall short of achieving these goals and, in fact, may contribute to worsening conditions on some islands.

The March 1989 report of the Australian Parliamentary Joint Committee on Foreign Affairs, Defence and Trade, entitled *Australian's Relations with the South Pacific*, noted:

> Despite large and increasing flows of aid into the region, economic prospects are generally discouraging and the growth performances of these countries has been disappointing. Aid dependence is increasing rather than decreasing, and the goal of self-sufficiency seems for many of the smaller countries further away than ever ... research has shown that large aid flows, while having beneficial effects, can also hinder economic development indirectly. Aid may discourage exports and import competing industries [and] lead to an increase in the public sector at the expense of the private sector, particularly agriculture ... There is also an 'absorptive capacity' problem with the constraints on

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> economic development reducing these countries' ability to absorb high per capita levels of aid. (Parliament of the Commonwealth of Australia, 1989:55,59)

The Report argues that, of the island members of the South Pacific Forum organisation, only Papua New Guinea and Fiji have the capability to reach 'independent and self-sustaining economic growth'. The Solomon Islands, Western Samoa, Vanuatu and Tonga will need continuing long-term support to be able to develop preconditions for independent economic growth. Finally, Kiribati, the Cook Islands, Tuvalu, Nauru and Niue have almost no prospect of being able to function independently of aid programs.

In many cases aid forms an important part of the island government's revenue for recurrent budget expenses. The Australian report argues that, especially in the case of those islands that have little or no hope of self-sustained development, 'Economic development should no longer be the chief determinant of aid ... but rather ... aid should focus on easing the adjustments that must be made where growth prospects are absent' (Parliament of the Commonwealth of Australia, 1989:60-1).[1]

In New Zealand, the May 1990 Report of the South Pacific Policy Review Group entitled *Towards a Pacific Island Community* reached similar conclusions. The Report pointed out, for example, that oversized island bureaucracies and high levels of island government expenditure were being largely financed by overseas aid. It concluded that 'unless the size and cost of the public sector in the region is restrained, it will hold back growth of employment in other sectors'. In spite of what is clearly a negative consequence of aid, the New Zealand Report argues that Wellington's Official Development Assistance (ODA) 'underpins our relations with the Pacific ... Our mana [standing] as a people of the Pacific is maintained through our ODA because it gives substance to our relationships' (South Pacific Policy Review Group, 1990:110-11).

The conclusions of the reports demonstrate that the aid policies of the two principal metropolitan powers on the South Pacific are not designed — to refer again to Lord Bauer's criteria — solely with a view to promoting development and relieving poverty. If these goals had been the criteria, then both Australian and New Zealand policy has

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1. In Nauru's case it is assumed that the island will not be able to maintain continued economic viability following the depletion of phosphate reserves.

been less than successful.

At its very worst, aid has been a major contributor to the growth of large island bureaucracies, to the rapid urbanisation of island capitals, and hence to the decline in the numbers of people pursuing a more traditional lifestyle on the land. Aid tends also to be unevenly distributed, and thus it has contributed to the development of major wealth disparities between those islanders living a subsistence lifestyle and those who could be described as the urban, educated, government-employed, cash-earning elite.

The consequences of these developments can best be examined in the light of a single example. Here I would like to discuss Niue, which, since 1970, has been self-governing in free association with New Zealand. Niue has a population of about 2500, and some 20 elected politicians. Over 10 000 Niueans live in New Zealand and make an important contribution to the island's economy by sending back remittances to their families.

Niue currently receives aid from Wellington to the value of $NZ10 million annually. New Zealand is threatening to cut this amount unless Niue is able to effect cuts in the size of its public service. Some two-thirds of New Zealand's aid goes in direct budgetary support of the island's bureaucracy, which employs more than half the workforce. Fifty years ago, less than 3 per cent of the island's population was in paid employment, and the island was self-sufficient in food. In the late 1980s Niue imported food, and exports accounted for less than 20 per cent of imports.

Some Niueans claim that aid stifles most attempts to develop private enterprise operations on the island because the government offers most services free. Visiting the island in April 1989, Russell Marshall, then New Zealand's Foreign Minister, was reportedly approached by farmers, tourist operators and others from the private sector who 'accused the Rex government of victimising them as political rivals for complaining that public servants get preferential development loans'. These claims have been accompanied with allegations that government administration of aid projects has been wasteful and produced little in the way of tangible returns (Magnall, 1989).

Although it is one of the smaller islands, Niue's problems are similar to those found on many island states. Foreign aid has done little to create the basis for self-sustained economic development. Rather, it has helped to create cumbersome political and bureaucratic structures that are slow to meet the demands of people who aspire to more materially comfortable lives. One of the most worrying developments in the region is the widening of wealth disparities within island communities and the creation of an elite that, according to a prominent islander critic of aid, 'have a great deal more in common with each other than with members of the other classes in their own communities' (Hau'ofa, 1987:3).

Despite these criticisms, there is little prospect of Australia or New Zealand drastically restructuring or reducing their aid programs. Neither of the two main reasons for this receives much attention in the essays presented here. The first is that, realising that most of the smaller island states will never develop independently sustainable economic growth, Australia and New Zealand have more or less accepted that constant budgetary support is necessary simply to keep the island governments going. As the New Zealand economist Ray Watters has put it (1987:41), the metropolitan powers are paying 'to prevent slums developing in [their] own backyard'.

The second reason for continuing aid payments relates to the strategic conceptions of the metropolitan powers. Australia and New Zealand have followed a policy in the South Pacific designed to minimise any influence exerted on the islands by foreign powers potentially hostile to Western alliance interests. The phrase coined to describe this policy is 'strategic denial'. One frequently cited example of the policy in operation relates to Tonga in 1976. In April that year Tonga established diplomatic relations with the Soviet Union. Tonga informed Australia that the Soviets had offered an aid package in return for being allowed to build an international airport and receive landing rights. The Australian and New Zealand response was to raise the issue at the 1976 meeting of the ANZUS Council and to increase the volume of their own aid to the region. Tonga refused the Soviet offer.

A similar development took place in 1985 when both Tuvalu and Kiribati were approached by the Soviet Union to establish fishing agreements. Kiribati accepted the arrangement — to the general concern of the metropolitan powers — but Tuvalu refused, and shortly thereafter New Zealand increased its aid to that country by some 73 per cent (to $NZ600 000 in 1986).

Through much of the 1970s and 1980s 'strategic denial' by means of aid successfully contributed to keeping the South Pacific remote from the influence of those countries considered hostile to Western alliance interests. However, this point should not be overemphasised. The islands to a very large degree were conservative and pro-Western in their outlook. The profound influence of Christianity led the islanders to be suspicious of communist ideology. For its part the

Soviet Union placed a very low priority on seeking to influence events in the region.

In addition to these factors, the islands were very well aware of the economic value of stressing their strategic importance to Australia and New Zealand. The following quotation from an August 1985 letter from Fiji's Prime Minister Ratu Mara to Australia's Prime Minister Bob Hawke is revealing in its very bluntness:

> We have all expressed concern about the ongoing fisheries negotiations between Kiribati and the Soviet Union. Other countries in the region including Fiji have received similar overtures from the Soviet Union. These developments, in my view, make it all the more urgent that Australia and other long standing friends in the Pacific come forward with further positive, visible and affirmative action in providing supportive economic measures. I believe that no island country would feel compelled to enter into new alignments if such support were readily available from within our region. (Quoted in Hau'ofa, 1987:8)

Epeli Hau'ofa has referred to this as an 'arm-twisting game'. But it differs from the usual outcome of arm-twisting in as much as both parties feel satisfied with what they got out of the deal.

In the 1990s both parties might also discover the limits of their ability to twist arms. Many island states have embarked on policies to extend their diplomatic contacts beyond the metropolitan powers that had colonial interests in the South Pacific. In mid-1990 the Soviet Union opened in Port Moresby its first resident embassy in the islands. Both the People's Republic of China and Taiwan have been competitively pursuing diplomatic accreditation in the region, and offering significant aid packages as incentives. In general, the region is opening itself to access from the outside world and there appears to be little that Australia and New Zealand could do, if they were so inclined, to slow this process.

For their part, the islands are finding that there are limits to the barter value of strategic pawns. The Soviet Union, for example, allowed fishing agreements to lapse with both Kiribati and Vanuatu. One must assume that the catch, both of fish and of intelligence information, was not good enough.

For all that it may have become a more difficult policy to implement, Australia and New Zealand will continue to use aid as a mechanism for encouraging the islands to support 'strategic denial'. However, the policy will have to accommodate the interests of a new, younger and somewhat more assertive generation of island leaders intent on expanding the diplomatic horizon of the South Pacific. With this expansion will come new sources of aid. Japan in particular has taken a much higher profile in the region, and has its own political and strategic interests to promote.

The final topic I wish to address concerns the developing conflict in the islands between rising expectations of higher living standards (often generated by aid) and the cultural and political conditions that make it difficult for those expectations to be met. Mr Siwatibau and Professor Kasper both refer to this problem. As Mr Siwatibau says (pp. 24-5 above):

> Political and social instability appears to have increased in recent years. This trend may be a function of rapidly rising aspirations that cannot be matched by economic performance and of an apparently growing conflict between slowly evolving cultural and traditional norms on the one hand and, on the other, the necessity for rapid changes in a modern world where effort, efficiency and merit are essential for the satisfaction of aspirations.

A central task for the South Pacific countries in the 1990s will be to adapt their political systems so as to make an acceptable compromise between customary forms of social organisation and the more pluralist ideas that ensure that aspirations are satisfied by 'effort, efficiency and merit'.

Professor Kasper has faith in the possibility of creating this blend of tradition and openness — and the idea of PNG Highlander-inspired consumer products is a beguiling one. However, one should not underestimate the potential difficulties. Epeli Hau'ofa has expressed the concern that 'custom' can be used by governments as a means of undermining potential opposition (1987:12):

> Increasingly the privileged and the poor observe different traditions, each adhering to those that serve their interests best. The difference is that the poor merely live by their preferred traditions while the privileged often try to force certain other traditions on the poor in order to maintain social stability, that is, in order to secure the privileges that they have gained, not so much from their involvement in traditional activities, as from their privileged access to resources in the regional economy. In such a situation, traditions are used by the ruling classes to enforce the new order.

Arguably, one could interpret the new Fijian constitution in this light. More generally, there are political forces in many of the island states that seem intent on resisting the development of more pluralist societies. One cannot but be concerned at this trend. Island societies do indeed need to preserve customary practices. But if these are used as a means of slowing or denying political and social reform, then prospects for regional instability will grow in the 1990s.

The range of problems outlined by Mr Siwatibau and Professor Kasper suggests that there is the potential for growing violence and political fragmentation in the region. For this reason, I am deeply sceptical about the prospects for greater regional cooperation proposed in these two essays. Indeed, I think that a key problem may be to preserve the gains already made by the South Pacific Forum. As things stand, there is some danger that the ethnic divisions in the Forum may harden into political blocs. The Bougainville crisis reminds us also that problems of secessionism threaten the sovereign integrity of several states.

In sum, one could be forgiven for taking a somewhat pessimistic view of the prospects for the South Pacific in the 1990s. The islands will continue to be dependent on foreign aid for the foreseeable future, much of which will not be used to promote sustainable economic development. The islands too face a challenging period of adjusting their political systems to better meet the demands of their populations. One can, however, forecast with some confidence that Australia, New Zealand and the other metropolitan powers will continue to support the islands in pursuit of the policy remnants of 'strategic denial'.

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AID & DEVELOPMENT IN THE SOUTH PACIFIC

Peter Bauer
Savenaca Siwatibau
Wolfgang Kasper

The political economy of the South Pacific is dominated by foreign aid. This promotes domestic statism, which in turn retards the economic growth and development of the many countries in the region. As popular expectations of higher living standards are frustrated, the political tension and violence that some of the larger countries have experienced in recent years may intensify.

The authors in this collection see little prospect for any rapid reversal of the present aid-subsidised stagnation, but propose modest reforms that could help the region move away from aid dependence and bureaucratic control. They also identify some economic trends that indicate possible directions of future sustained development.

- **Peter Bauer**, a leading authority on development and aid, argues that if foreign aid cannot be terminated it should at least be given only to those countries that adopt enlightened economic policies.

- **Savenaca Siwatibau**, Head of the ESCAP Operations Centre for the Pacific, stresses the significance of Fiji's attempts to privatise some state-owned enterprises, Vanuatu's success as a financial centre and the establishment of trust funds by Kiribati and Tuvalu.

- **Wolfgang Kasper**, Professor of Economics at the Australian Defence Force Academy, advocates an economic and currency union of the South Pacific and shows how Australia and New Zealand can help make the region's transport and communications more competitive.

These and other proposals and developments are discussed by commentators **Colin Simkin**, Emeritus Professor of Economics at the University of Sydney, and **Peter Jennings**, formerly a Teaching Fellow in Politics at the Australian Defence Force Academy.

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