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Aid Has Failed the Pacific

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EXECUTIVE SUMMARY

Per capita income has grown at less than 1% a year in the Pacific during the past 30 years. In some islands it has declined. Population has grown at more than 3% a year. The discrepancy between population and income growth lies at the core of the Pacific's problems. The little income growth that has taken place has gone to small urban elites, so that village standards of living are deteriorating. Economic decline has inevitably led to crime and violence. Australia is not keeping abreast of the Pacific's problems, allowing aid to add to the region's difficulties. Nauru and the Solomon Islands are disintegrating and Papua New Guinea's problems are acute.

Inappropriate economic policies have failed to deal with the hard tasks of development and with the negative effects of aid and mineral income flows. That is why Pacific governments are failing their people.

The Pacific was seen as an earthly paradise by early European explorers and latter day anthropologists. Benign climates, ample food and leisure made for unusually high self-sufficiency standards. The Pacific is rich in agricultural land, timber, fish and minerals and attractive to tourists. All Pacific economies, even the smallest, can achieve high modern standards of living if they adopt policies that fit their size.

Since 1970 the Pacific has received US$50 billion—A$100 billion (in 1998 dollars)—in aid. Australia has been the largest donor. But because aid flows are not earned income, they create economic 'rents' that distort economies. Aid flows are fungible. They can be spent on projects and programmes of the recipient's choosing—on consumption rather than investment. Because they bias an economy against the private sector, they undercut employment and growth and lead to corruption. Super-profits from rich mineral deposits similarly create economic rents that also have negative economic effects, leading to public waste. Together aid and minerals have made development difficult worldwide, notably in Africa. Australia had to apply hard-headed economics to its own mineral booms and to reform its protectionist, public ownership and regulation policies. Understanding that aid can have negative effects is essential to assisting the Pacific to growth and development.

Re-colonisation in any form is not a solution. Pacific problems can only be tackled in the Pacific. The first step toward reversing stagnation and falling incomes is the recognition that excess of population over income growth means serious trouble. No amount of muddling through will fix this fundamental disequilibrium. Pacific societies have to adopt policies that establish secure, free economic environments that deal with economic rents and make growth possible.

The Australian stance most likely to be effective would be to suspend all aid and thus to provide the catalyst for change. Withdrawing US aid turned Taiwan and South Korea into economic 'tigers', but it would be a harsh step for the Pacific.

A softer alternative, still taking into account the potentially damaging effect of aid, would be to insist on the principle of mutual obligation in Australian aid to the Pacific. At present, Pacific states regard aid as part of their government revenues. They spend aid on consumption. That is why roads, electric power, telecommunications, schools and health centres are deteriorating. Responsibility to Australian taxpayers demands that this practice must end. Australian aid funds must be removed from Pacific island budgets where they encourage waste and corruption. Aid should only be spent on mutually agreed development projects and programmes designed and monitored by teams nominated by the sovereign recipients and donors. Funds should only be disbursed on the evidence of met targets and audited expenditures. Without such changes, Australian aid will continue to damage the Pacific.

Experience shows that Australia cannot rely on the IMF, the World Bank and the Asian Development Bank for the conditionality that was supposed to make aid effective. These organisations have their own internal agendas that have failed to stimulate growth and have led the Pacific into debt. Loans have also been spent on consumption and are hence unsustainable. For greater aid efficiency and effectiveness, Australia should move funds from multilateral to bilateral aid.

Migration to Australia is already taking place from the Pacific. Increasing awareness of migration possibilities to Australia could assist the Pacific. But migration must be under the same conditions as for other immigrants to avoid the creation of welfare dependent ghettoes of Pacific immigrants in Australian cities. Emigration to Australia would increase remittances, savings and skills, and some migrants would return and start businesses.

The Department of Foreign Affairs and AusAID, with inputs from the Treasury and the Department of Defence, should take responsibility for strategic knowledge and programming of Australia's relationship with the Pacific to help the Pacific to reverse current trends and move forward. AusAID needs to be empowered to put mutual obligation into practice. The time for a well-informed public debate on aid to the Pacific to support policy change is long overdue.

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1. INTRODUCTION

At independence, Pacific peoples hoped for high standards of living in education, health and longevity as well as material comforts. But increased living standards have only been realised by the misapplication and misappropriation of aid and resource funds by political and bureaucratic elites and their business cronies. Redistribution has taken place, but from the majority of Pacific islanders to these elites. The living standards of Pacific peoples have stagnated and even fallen. In Papua New Guinea, Solomon Islands and Vanuatu, bare nutrition, no schools or health services, are leading to the spread of malaria, tuberculosis and HIV/AIDS. Women have always been, and are, the workers of the Pacific, yet they bear the brunt of emerging deprivation and insecurity in villages and towns. Many men are unemployed in urban areas and most are underemployed in villages. Deep dissatisfaction has inevitably followed, erupting in a culture of arms and violence.

The Economist recently asked whether the Solomon Islands qualifies as the Pacific's first failed state, conscious that instability is also endemic in Bougainville and the Papua New Guinea Southern Highlands and looms elsewhere.[1] Australia's security is threatened by the passage of drugs, arms and ultimately, terror and the flight of large numbers of economic refugees. Across the Torres Strait, Papua New Guinea's population is expected to rise to some 10 million by 2025. Unless there is a sharp change of direction in Papua New Guinea, the prospect not merely of a failed state, but of a rogue state (like those of Amin, Mobutu, Bokassa and Mugabe in Africa), cannot be lightly dismissed.

Aid policies have to counter the negative effects of aid rents if compassion and economics are not to be in conflict.

Economic theory showed, albeit counter-intuitively, that protection hurts employment, and enabled Australia to adopt reforms that have made us economically strong. Economic theory, again counter-intuitively, shows that the economic rents associated with aid impede the growth of developing countries. Aid policies have to counter the negative effects of aid rents if compassion and economics are not to be in conflict.

The Pacific is not unique. The combination of high mineral rents with large aid flows damaged a number of developing countries in Latin America. Aid and mineral rents have created havoc in some 30 sub-Saharan states. Lessons must be learned from those countries, like Chile in Latin America (after many vicissitudes) and Botswana and Mauritius in sub-Saharan Africa, which have adopted policies that have led to positive growth and development. Botswana has shown that traditional tribal societies can grow strongly. Mauritius, with a similar ethnic heritage to that of Fiji, has prospered. Thirty years ago, Botswana and Mauritius had lower per capita incomes than Papua New Guinea and Fiji; today they have, respectively, more than twice the per capita income of the two Pacific countries.

Table 1. Comparison of economies of African and Pacific countries

	Population	*Per capita income $ US current*		*Gross national income per capita $ purchasing power parity*
		1972	2000	2000
Botswana	2,000,000	240	3,300	7,170
Papua New Guinea	5,000,000	290	700	2,180
Mauritius	1,000,000	300	3,750	9,940
Fiji	800,000	500	1,820	4,480

Source: World Bank, *World Development Indicators*, 2002, Washington, D.C. Current dollar data give an exaggerated illusion of growth for all four countries. Growth charts on p. 7 are in constant dollars.

The large flows of aid to the Pacific, together with mineral, timber and fishing rents, have not resulted in rapid growth, but have led to stagnation and decline by permitting counterproductive policies to persist.

2. PACIFIC OVERVIEW

Despite their distinct Polynesian, Melanesian and Micronesian origins, different colonial experiences, varying sizes and resource endowments, the island states of the South Pacific have many common characteristics. The colonial era left 19 national entities, ranging in size from a population of 5.2 million in Papua New Guinea to 1,000 in Tokelau. They do not include American Samoa because it has opted to be part of the United States. American Samoa's 69,000 people in 2000 had a per capita income of US$8,000 (purchasing power parity), much higher than that of long independent Pacific states.

Population and income growth

Pacific data are weak. The attempt to build up a database for the Pacific was unfortunately abandoned in 1994.[2] The longest and most consistent data series are those compiled by the World Bank's Development Data Group in Washington from national statistical offices in the Pacific. Tables 2 and 3 and charts 3 to 6 are based on these data sets although they contain inexplicable variations and revisions, reflecting the weakness of their sources. IMF data, based on the generally more reliable central bank data for Papua New Guinea and Fiji (charts 1-2) show the same trends. The Asian Development Bank and the *CIA Factbook* give an array of varying figures, but also show the same trends. The fundamental reason for inconsistent and inaccurate data is that Pacific states do not value data objectively, but regard data as political weapons in internal debates and in their annual requests for aid. Political adjustments to data are frequent.

Within the overall similarities of Pacific societies and economies, there are, of course, wide differences, just as there are differences in small countries. Each Swiss Canton regards itself as having unique geographic, cultural and economic characteristics, including different languages and dialects, albeit within the broad Swiss federation of 7 million people—that is, roughly the same population size as the Pacific's 7.7 million people.

Despite data difficulties, the gap between population and income growth for the Pacific as a whole and for most Pacific states has been evident for years (Table 2). The Jackson Committee's review of Australian aid drew attention to it in 1984.[3] Ten studies, headed *Pacific 2010* by the National Centre for Development Studies in the early 1990s, followed by seminars throughout the Pacific, pointed to the high economic and social costs of population exceeding economic growth.[4] Pacific governments and aid agencies did not respond by re-examining their policies.

All Pacific states are economically viable if they choose policies appropriate to their size and level of development.

The lack of growth in most of the Pacific states is not warranted by their geographic situation, natural endowments, or cultural diversities. All Pacific states are economically viable. They would all be able to reach high living standards, like those of Australia and other industrial countries, without aid, if they chose economic and political policies appropriate to their size and level of development.

Papua New Guinea and Fiji are large enough to govern themselves independently if they adopt government structures appropriate to their populations of 5 million and nearly 1 million people respectively, if they engage modestly in international affairs and if they opt for pro-growth policies.

In the medium sized Pacific states, government would have to be tailored to the needs of populations of 100,000 to 500,000 (the size of a small to medium city in industrial countries) to enjoy economic and hence true independence. That such small entities were not joined in a federation at independence is a persistent and high cost legacy of colonialism. The colonial powers as late as the 1960s and 1970s (and to date in French Polynesia and New Caledonia) encouraged the Pacific states to differentiate themselves by allegiance to their metropolitan colonial powers rather than to cooperate as Pacific neighbours to achieve high living standards. Their present scale of individual political and bureaucratic structures and inappropriately elevated international representation provide high incomes for elites while rural populations bear the cost. Entrenched elites oppose any political and economic rationalisation that would reduce the considerable benefits they monopolise at the expense of the rest of the population. Modern communications make a federation with small government technically practicable. But inappropriately swollen governments persist because they are funded by aid.

Limitations of government and international representation and federation are even more essential for very small states, with populations of less than 50,000 people. The smaller islands are not even the size of a suburb in industrial countries. Their path to real independence means giving up illusions of power and concentrating on good living standards. They should follow the example of Norfolk Island that, without aid, has a per capita income nearly twice that of Australia.[5]

Inappropriately swollen governments persist because they are funded by aid.

Table 2. Pacific economic indicators

	Land area Km²	Population '000s 2000	Density people/Km² 2000	Annual Growth % 1970-2000 Population	Real GNP per capita	GNP per capita $ purchasing power parity [8] 2000
Papua New Guinea	463,000	5,200	11	3.7	0.3[4]	2,180
Fiji	18,272	812	44	1.9	2.7[5]	4,480
Solomon Islands	28,530	447	16	3.9	-0.4[6]	1,710
French Polynesia	3,265	235	72	3.7	(NA)	23,340
New Caledonia	19,103	213	11	3.2	(NA)	21,820
Vanuatu	11880	197	17	4.6	-0.3[7]	2,960
Samoa	2,935	170	58	0.6	0.8[7]	5,050
Micronesia Fed. States	702	118	6	3.3[1]	(NA)	2,000
Tonga	699	100	143	0.5	2.6	1,660
Kiribati	690	91	132	2.8	-1.2	950
North Marianas	477	70	68	(NA)	(NA)	12,857
Marshall Islands	181	50	36	2.9[2]	(NA)	1,600
Cook Islands	240	21	88	0.0[2]	(NA)	5,000
Palau	458	20	23	(NA)	(NA)	9,000
Wallis & Futuna	274	20	14	(NA)	(NA)	2,000
Nauru	21	12	571	NA)	(NA)	5,000
Tuvalu	26	11	423	1.6[3]	-1.4[6]	1,100
Niue	259	2	8	(NA)	(NA)	3,800
Tokelau	10	1	100	(NA)	(NA)	1,500
Pacific average				3.4	0.6	

Notes: (NA) data not available or vary by more than 25 per cent among sources.
[1] 1980-2000; [2] 1981-2000; [3] 1983-2000; [4] 1973-2000; [5] 1968-2000; [6] 1967-2000;[7] 1979-2000
[8] Purchasing power parity for the Pacific is not derived directly but from econometric estimates based on 'like' countries; it is only applicable to urban, not to subsistence rural areas. The high purchasing parity per capita incomes for French Polynesia and New Caledonia reflect the high salaries of the French 'metros' employed in the public service.
Source: Compiled from World Bank data, except for Cook Islands, Wallis and Futuna, Nauru and Tokelau which are based on the *CIA Factbook*.

Economies of scale

All Pacific states except French Polynesia and New Caledonia (still territories of metropolitan France), the North Marianas, Cook Islands, Wallis and Futuna, Niue and Tokelau are United Nations (UN) members. They can outvote the United States, China and Russia in the United Nations Assembly and in all its committees and agencies except the Security Council. The Pacific states' main use of UN membership is to maneouvre and beg for aid. All but the very small Pacific states are also members of the IMF, the World Bank and the Asian Development Bank. International organisations have acted irresponsibly (in the interest of their own growth and employment) in encouraging Pacific states to inflate their individual state claims instead of fostering federation. Servicing international obligations individually leads to travel and stints in New York, but eats up money and scarce trained manpower. Kiribati, Samoa, Solomon Islands, Tuvalu and Vanuatu have taken the amazing step of having themselves declared 'least developed'—that is, failed economies—by the UN. This enables island politicians and bureaucrats to travel to UN meetings at the UN's expense.[6]

Is there poverty in the Pacific?

National, and hence international, social indicators are so subject to political manipulation that they are even less reliable than population and income data, fluctuating unrealistically from year to year and among sources.[7]

Although the UN, the World Bank and the Asian Development Bank have devoted hundreds of consultants' hours and thousands of pages to defining poverty in the Pacific, they have not produced a coherent series of social indicators. A careful qualitative approach that takes into account the low quality of the available data is required for a realistic assessment of Pacific living standards.

The work of women in traditional agriculture has thus far kept up with population growth so that 'absolute poverty' in the sense of the hunger that afflicts (as a result of rule by rogue governments) perhaps 35 million people, mainly in sub-Saharan Africa, is not yet present in the Pacific. The suggestion that an income of less than US$1 a day indicates 'poverty' in the Pacific insults the hard working women who provide food for villages.[8] But a high proportion of villagers lack access to education and health. A maternal death ratio of 370 per 100,000 live births in Papua New Guinea and 274 per 100,000 live births in the Federated Micronesian States are among the highest in the world. They indicate a total absence of health services. For the other states where women are at risk, reliable figures are not even available. Access to primary education, at 2 to 3 years of schooling for girls and not much more for boys, equally ranks among the worst in the world. In villages where transport is poor and deteriorating, and in areas succumbing to warlordism and crime, there is little cash income and thus few manufactured goods. The people are denied almost all the opportunities that the 21st century offers. Girls and women who do the bulk of the work are, in particular, most disadvantaged by the lack of education opportunities and the failure of governments to provide health services.

In urban areas high unemployment is making too many people dependent on too few earnings and sharply limiting the consumption of manufactured goods. Thus the Pacific is a much larger market for second-hand than for new clothes. Because the penetration of radio and television is very limited, Pacific islanders remain isolated from the world even in urban shanty towns.

Although there is not widespread hunger in the Pacific, standards of living are thus unconscionably and unnecessarily low and falling. Some disabled and elderly people and families headed by single mothers are already on the edge of hunger in the towns. If growth does not accelerate and population continues to increase, limits of traditional agriculture will be reached and hunger, as well as the other indicators of poverty, will emerge on a broad scale.

Standards of living are unconscionably and unnecessarily low and falling.

Longevity and health

In Papua New Guinea, the Solomon Islands and Vanuatu, life expectancy has risen from between 40 and 50 years in the 1970s to around 60 years in 2000 (Table 3). In Micronesian and Polynesian states, where colonial regimes introduced better malaria control, elementary health and education services in urban areas, expectation of life was around 60 years by 1970. Life expectancy also increased by perhaps 10 years during the last 30 years, mostly during the early years of independence before health and education services began to decline. But fertility rates and infant mortality are still high, and maternal mortality, where figures are available, is stratospheric. Health indicators for the Pacific are more akin to the failed states of sub-Saharan Africa than to developing East Asian countries that had lower per capita incomes in the 1970s than the Pacific states. Australian indicators show the long distance Pacific states have to travel if they are to provide their peoples with the benefits of high living standards.

The threat of rape is so great that many girls cannot go to school and women teachers are afraid to work in the countryside.

Education

Education enrolment suggesting full primary participation is unreliable for Papua New Guinea, Solomon Islands and Vanuatu, where rural schools have fallen down and teachers do not attend schools because they cannot find secure accommodation. The threat of rape is so great that many girls cannot go to school and women teachers are afraid to work in the countryside. Figures on years of schooling, only available for Papua New Guinea, indicate an average of 3.3 years for boys and 2.4 years for girls. With typical inconsistency, the World Bank reports that 64% of boys and 53% of girls complete primary education. But literacy rates are said to have fallen from 36% to 29% for men and from a higher 52% to 43% for women from 1990 to 2000. On the same page, the expected years of schooling are stated to be 9 for men and 8 for women.[9] The low quality of education is a serious problem. Elites send their children to boarding schools in Australia and New Zealand.

New problems are emerging. High sugar and fat urban diets and alcoholism associated with underemployment are leading to a rising incidence of diabetes, heart, kidney and liver disease. Youths seeking a life in urban areas often have to return to their villages. The lack of health services means that HIV/AIDS is spreading rapidly.

Table 3. Pacific social indicators

	Life expectancy		*Fertility rates births per woman*		*Infant mortality per 1,000 live births*	*Maternal mortality per 100,000 live births*
	1970	2000	1970	2000	2000	1996-2000
Papua New Guinea	47	59	6.1	4.4	56	370
Fiji	64	69	4.1	2.8	18	(NA)
Solomon Islands	40	(NA)	7.0	5.4	22	(NA)
French Polynesia	(NA)	73	5.6	2.6	10	(NA)
New Caledonia	61	73	4.3	2.6	7	(NA)
Vanuatu	40	(NA)	6.5	4.4	35	68
Samoa	61	69	6.7	4.3	21	30
Micronesia Fed.States	(NA)	68	5.0[1]	3.7	26	274
Tonga	(NA)	71	6.5	3.6	17	81
Kiribati	(NA)	62	4.3[2]	3.9	52	56
N. Marianas	(NA)	(NA)	(NA)	(NA)	(NA)	(NA)
Marshall Islands	(NA)	65	(NA)	(NA)	(NA)	(NA)
Cook Islands	(NA)	71	(NA)	3.3	20	20
Palau	(NA)	70	(NA)	(NA)	(NA)	(NA)
Wallis & Futuna	(NA)	(NA)	(NA)	(NA)	(NA)	(NA)
Nauru	(NA)	59	(NA)	4.6	25	(NA)
Tuvalu	(NA)	64	(NA)	2.8	38	(NA)
Niue	(NA)	(NA)	(NA)	(NA)	(NA)	(NA)
Tokelau	(NA)	(NA)	(NA)	(NA)	(NA)	(NA)
Australia	71	79	2.9	1.8	5	6

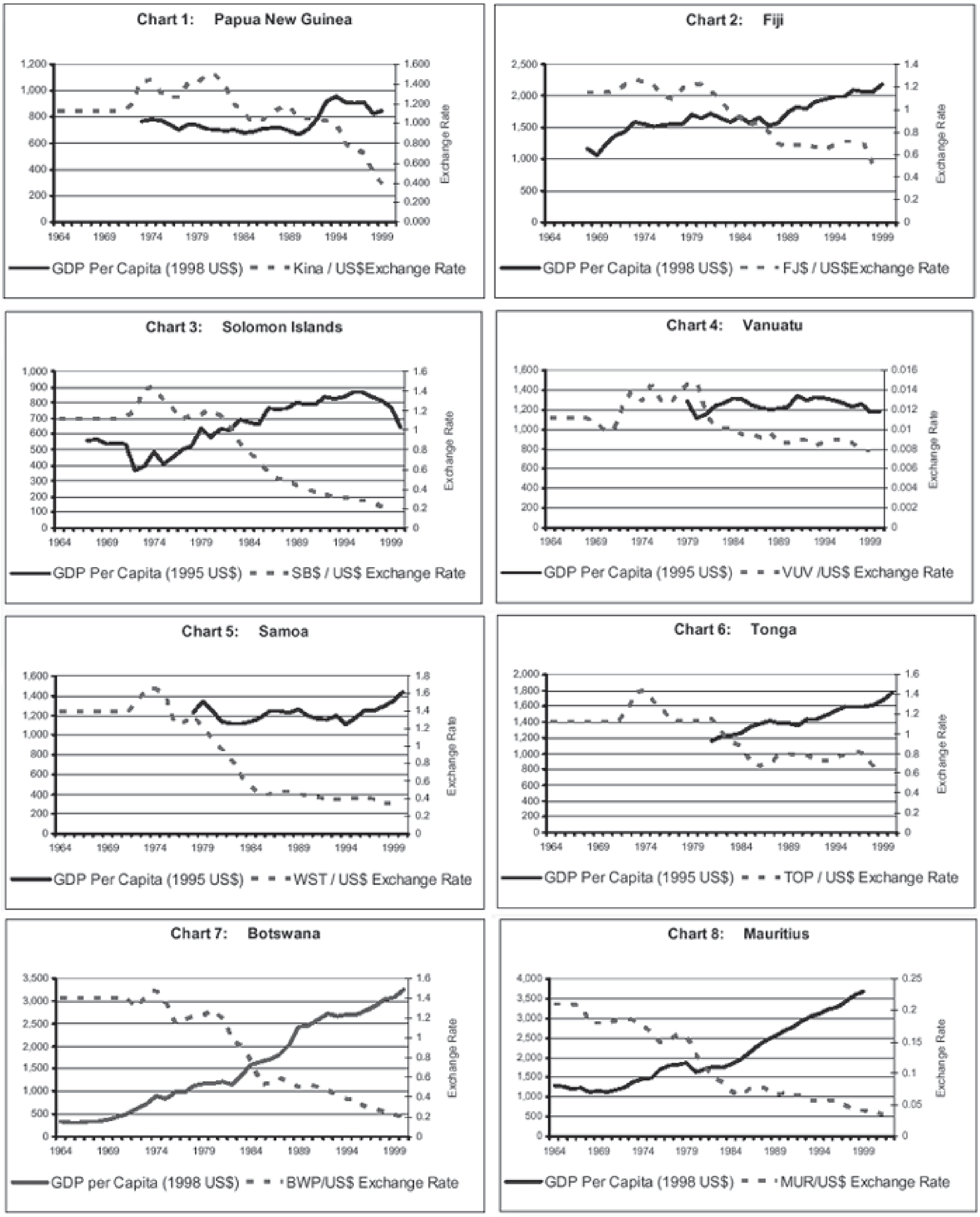
Notes: (NA) data not available or varies by more than 25 per cent among sources. Estimates for medium sized populations necessarily fluctuate from year to year and for very small populations would be meaningless.
[1] 1987; [2] 1973

Source: World Bank, Asian Development Bank and *CIA Factbook*.

Papua New Guinea

Australia's nearest neighbour is a small economy in global terms, on the way to becoming medium sized with a population of 5.2 million projected to reach 10 million in 2025. Its mainland is the second largest island in the world (after Greenland). It is rugged (like much of Switzerland) and population density is low. Some 700 to 800 languages are spoken but Pidgin and English are *lingua francas*, making for a greater possibility of national cohesion than would two or three major language divisions.

Charts 1-8: GDP per capita growth rates and exchange rates



Note: The appreciation of the US dollar is a major factor in the 'decline' of these currencies. Botswana and Mauritius have followed market exchange rate signals since independence to ensure that their exports were not damaged by overvaluation of their currencies.
Source: International Monetary Fund, International Financial Statistics for Papua New Guinea and Fiji (http://ifs.apdi.net/imf/) and World Bank for Solomon Islands, Vanuatu, Samoa, Tonga, Botswana and Mauritius.

Rich mineral deposits added large annual inflows to aid so that, if appropriate policies had been adopted, Papua New Guinea could have become a rapidly developing country. Instead, Papua New Guinea's economic stagnation is evident (Chart 1). Per capita income only increased from A$1,200 in 1970 to A$1,340 in 1999 (in A$1998).[10] The value of the kina has fallen sharply. At best, social and economic infrastructure is deteriorating, and more commonly, collapsing. The Lae-Mt Hagen highway is in many places a goat track terrorised by robbers. No road links Port Moresby and Lae. Mining and timber are in decline. Agricultural exports are growing very slowly. The private sector is dominated by expatriate investors.

Formal employment is concentrated in some 65,000 public sector jobs, and at a generous count, some 70,000 formal private sector jobs, making total formal employment of 135,000 jobs. Every year 50,000 young people are added to the labour force. About 100,000 people (40% of the urban labour force) are openly unemployed in urban areas. At least one million men are seriously underemployed in rural areas. As population pressure on land increases, women are typically fully engaged in subsistence agriculture and some cash crops for protein and to pay for other food supplements, clothing and school fees, while men, and particularly young men, lounge about villages.

Fiji

Fiji, paradoxically, had the good fortune of only modest mineral and timber resources, so that it did not have to struggle against the negative impact of aid and mineral rents. But under the Lomé arrangement, Fiji sugar had privileged access to high price EEC-EU sugar markets. The consequent economic rents were garnered by indigenous Fijian landowners on whose land Fijian Indians grew sugar. The tribal chiefs appropriated, consumed and wasted the rent incomes. Their savings and investment have been negligible. Sugar's future has been crippled by the lack of long term leases. Many frugal sugar farmers educated their children and saved and invested in businesses that form the core of the urban private sector.

Discouraged by political discrimination, many Fijian Indians have emigrated.

Fiji's growth has been modest, increasing in the 1990s when a clothing export industry was able to develop because the Rabuka coup suspended the (Indian Fijian) trade unions' domination of the labour market. Tourism was also stimulated by the loosening of the labour market. Even very modest economic growth led to falling population growth. But urban unemployment is still estimated to be 20%. With a semi-feudal indigenous Fijian society pitting itself against Fijian Indians, lack of economic progress has made Fiji susceptible to military coups and uneasy political stand-offs that discourage investment. Discouraged by political discrimination, many Fijian Indians have emigrated.

Solomon Islands

Solomon Islands, with a population of nearly 500,000, after 30 years of independence has ceased to function as a state. Welfare and statist policies encouraged waste and corruption. Communal land ownership deterred agricultural development. The exploitation of the Solomon Islands' timber resources by a small elite led to large scale corruption. There were no jobs for the rapidly growing population so that society disintegrated into violence and chaos.

French Polynesia and New Caledonia

The French colonies are governed as territories of metropolitan France. Their high per capita incomes reflect salaries of the French public servants who enjoy rotations in the Pacific at the expense of French taxpayers. Discussion of Kanak independence has been put off for at least 10 years in New Caledonia and indefinitely in French Polynesia. Nickel rents supported the French colonial government in New Caledonia, but the mineral is running out. French Polynesia was maintained by nuclear testing. Tourism is becoming the main industry but it is limited mainly to French citizens by the overvaluation of the Pacific franc's tie to the French franc. Exports other than minerals are not viable.

Vanuatu

With nearly 200,000 people, Vanuatu has a heavy government burden complicated by the colonial history of the British-French Condominium (known in the Pacific as the Pandemonium for its grossly inefficient bilingual administration) which imposed dual legal, government and education structures, together with two foreign languages—French and English—on top of the local Bislama, (in itself a second language for the ne Vanuatu) on this small state. Much of the aid to Vanuatu is spent on these inappropriate remnants of colonialism, not least on ensuring that all official documents are translated into French and English. Vanuatu has created an off shore financial centre that is dependent on the employment of expatriates. By adding to unduly high wages in the public sector and the effect of aid in appreciating the exchange rate, other business, exports and hence employment are stalled. The gains from the financial centre accrue to the same groups as the rents from aid, leaving people in the countryside without education and other services and infrastructure.

Samoa and Tonga

Samoa and Tonga are similar traditional agricultural economies. Each has small and inefficient formal sectors producing for the domestic market, but each also has successful small, export-oriented agricultural and manufacturing production. Emigration to New Zealand, to Australia via New Zealand and via American Samoa to the United States sustains these islands. Official figures are thought to underestimate remittances to such an extent that in both states actual remittances are higher than aid plus exports.[11] Samoan and Tongan families use migration and remittances to find jobs. Tongans seek escape from the absurdities of their society's domination by Tongan royalty, the nobility and their cronies.[12] Growth would be even more positive if excessive government did not absorb far too high proportions of local revenue and aid. In Tonga the King and his barons have appropriated, and lost, millions of public money which they find indistinguishable from their personal finances. The most recent depredation reported was a Royal investment of US$26.5 million with the King's court jester, who lost it.[13]

Samoans and Tongans use migration and remittances to find jobs.

Nauru, Kiribati and Tuvalu

These three Pacific states have benefited, in different ways, from marine phosphate deposits.

Nauru, initially a German colony, in 1918 became a United Kingdom, New Zealand and Australian Trust Territory administered by Australia. These three countries' farmers benefited from cheap phosphate till World War II when the Japanese used the island as an aircraft carrier, shipping most of its 5,000 people to Truk in the Marianas, where all but 500 starved to death. In 1945 the Trust status was resumed. In 1963 Nauru obtained the world price for its phosphate. When Nauru became independent in 1968, each man, woman and child, was worth A$500,000 (A$3.5 million in 2003 dollars). Phosphate prices rose in the 1970s giving Nauru the second highest income in the world (after Saudi Arabia) so that millions of dollars poured into the island.[14] Australia paid Nauru A$100 million to compensate it for the under-pricing of phosphate in colonial times. Although it was known that the phosphate deposits (which were never inhabitable) would run out in the 2000s, Nauru abandoned its conservative commercial advisors, becoming the victim of the shadiest financial, legal and academic operators in the world. It ultimately provided a financial centre for drug and terrorist money laundering, with the sale of passports as a sideline. Elections are pending, but the island is still refusing to settle its debts and to opt for a conservative financial stance that would enable all Nauruans to live in comfort.

Kiribati's remittances from its phosphate workers on Ocean Island and Nauru have been key incomes. Kiribati has a phosphate based Trust Fund. It is currently intending to use it to develop state owned enterprises, even though these have proved to be a disaster throughout the Pacific. If this plan goes ahead, Kiribati will follow Nauru and will soon be making increasing demands for aid.

Tuvalu has benefited from the remittances of its phosphate workers. Tuvalu did not receive any revenues from phosphate, but has converted much of its aid into a long term Trust Fund to support its social services.

The Federated States of Micronesia, North Marianas, Marshall Islands and Palau

The former American colonies are best characterised as drowning in aid. The total population of the four groups is 260,000, but individually they range from 20,000 people in Palau to 118,000 for the Federated States of Micronesia. Beautiful, pristine islands have been turned into rubbish tips covered with discarded beer cans as productive traditional agricultural societies became welfare dependents. Many islanders emigrate to the United States to escape waste and corruption at home.

Cook Islands, Wallis and Futuna, Niue and Tokelau

The Cook Islands, Niue and Tokelau are substantially integrated into the New Zealand economy. Migration is so high that there are more emigrants in New Zealand than people on the islands, with substantial remittances flowing back to the islands in addition to large aid flows.[15]

Prospects for federation

The lack of cooperation in the Pacific dates back to the conflict policies of the colonial powers that cut up the Pacific into their 'possessions' in the 19th century. The islands are still slaves of their colonial past. They have ignored the benefits of joining together to share costs of government and international representation and of free trade in goods and services, capital and labour. The two regional organisations—The Pacific Community headquartered in French speaking Noumea and the Pacific Forum in English speaking Suva—are typical of form without content that plagues Pacific institutions. They are both ineffectual because the Pacific states are not interested in any measures that would rationalise administration and thus deprive them of jealously guarded political and public service jobs. The Community and the Forum waste the aid funds on which they depend.

3. PACIFIC TRADITIONS

The pressures that made for the 'Puritan ethic' of work, saving and investment in less favourable climates were absent.

The Pacific is so well endowed naturally that its traditional material lifestyles were envied by the first European explorers as akin to paradise. Idealised views of the 'noble savage', however, ignore claustrophobia and endemic violence, including cannibalism. Besides gardens and orchards, the region also had stands of tropical timber, ample marine resources and in some islands, minerals. Traditionally, men cut down trees and fenced gardens, hunted and protected their villages. The societies were polygamous, with several wives needed to work gardens. Leisure was ample, particularly for men. They enjoyed even greater leisure once modern tools were applied to the making of gardens, hunting was replaced by imported sources of protein and tribal fighting was contained by the colonial administrations. Pressures that made for the 'Puritan ethic' of work, saving and investment in less favourable climates were absent.

Development implies a change from traditional to modern societies. Such change has both costs and benefits. In the Pacific these costs are particularly marked by the loss of leisure. The costs of change are only worthwhile if they are compensated by higher personal security, personal freedom, better education, health and longevity, higher incomes to buy manufactured goods and a richer social and cultural life. The slower the transition and the smaller its rewards, the more are societies likely to cling to (idealised) traditional ways despite all their costs. Without evidently rising benefits, the costs of change erupt into violence and crime.

As the Pacific became a laboratory for anthropologists, the idealised views of Pacific societies came into prominence.[16] Overpopulation that from time to time pushed people off from island shores in search of new lands to settle, but more often to drown at sea, was ignored. So was the claustrophobia and violence to which it led in many small societies. The treatment of women as chattels in polygamous societies was airbrushed out of the poignant palm fringed vignettes of island life. For many missionaries, modern life was thought to bring nothing but unfortunate temptations. Imperceptibly, anthropologists, sociologists and geographers moved from describing Pacific societies to prescribing for them.[17] Roseate views of traditional life became dominant and were adopted as realistic and accurate by Pacific leaders. It was a short step to argue that traditional social institutions could be maintained without change and yet deliver the modern education, health, jobs and incomes that Pacific islanders, like people everywhere, want.

Cargo culture

No evident effort was needed to obtain the goods that missionaries and colonial administrations brought to the islands. Local inhabitants soon learned to enjoy new foods and other consumer goods, but a lack of connection between work, income and consumption led to various forms of 'cargo cult' in colonial times. These were strengthened by the air drops of food and blankets during World War II. Cargo cult expectations became a serious problem, notably in the Solomon Islands, but they were present throughout the Pacific.

Cargo cult expectations were readily translated into dependence on aid.

Cargo cults were fed by resentment in the colonial period. Expatriate families did not have to work hard to enjoy high standards of living while local people worked in gardens, on plantations and as domestic servants. Cargo cult expectations were readily translated into dependence on aid flows. In the Pacific there did not seem to be any conflict between dependence on aid and national independence. A culture of mendicancy, no less debilitating at the level of the political state than the cargo cult was for individuals, thus permeates the Pacific. Treating aid funds contributed by Australian (and other) taxpayers as components of national revenues to be spent largely on consumption, seems natural to Pacific governments. The notion that Australian taxpayers have the right to oversee how their taxes are spent is regarded as bizarre in the Pacific.

Communal land ownership and clan loyalty

Communal land ownership and clan loyalty provide security and ensure that in traditional societies noone goes hungry. Most of the Pacific has been stalled at the communal stage of development, though feudalism has emerged in the role of chiefs in Fiji and royalty and barons in Tonga.

Communal land ownership has held back indigenous entrepreneurship in the Pacific as it has everywhere in the world. The very considerable literature on land issues, starting with an Asian Development Bank sponsored survey of South Pacific agriculture in 1979, failed to ask whether economic growth and development on the basis of communal ownership was possible. There was no attention to how the transition from communal to individual property rights might be managed.[18] Land reform was stalled. Arguments for individual property rights did not emerge until the 1990s.[19]

Changing from communal to individual property rights undoubtedly has costs for some individuals. Some will benefit more than others. But experience worldwide shows that where the transition from communal to personal property rights takes place in an open society, the benefits to the lowest income households that emerge from the process are far greater than those of standing still. Taiwan and Thailand are examples of positive transitions to individual rural property rights that led to rapid growth.

Not one country in the world has developed on the basis of communal land ownership. Scandinavian aid agencies failed miserably when they tried to introduce co-operative farming as a transition to private property rights in Tanzania. Incomes fell steeply in the wake of their efforts.

The extraction of timber from communal lands in the Pacific led to exploitation by foreign firms and monumental corruption, with little return to the landowners or the nation, and without replanting to sustain yields. In the Solomon Islands, combined village and political corruption was a major factor in the collapse of civil society.[20]

Clan loyalty, admirable in traditional societies, is inappropriate for a high income modern society. It reduces the costs of unemployment and underemployment in stagnating Pacific societies by creating an informal welfare network, but at very high cost. Clan loyalty makes it impossible for individuals to save and invest. Women with jobs in Port Moresby have to buy food daily so that it is not eaten while they are at work. Farmers in the Nadi district of Fiji do their banking far south in Suva at great inconvenience to protect their savings from their clan. The indigenous retail store programme in Papua New Guinea failed because clan members expected not to have to pay. Samoans and Tongans escape to New Zealand and Australia to be able to save and invest.

Clan loyalty makes it impossible for individuals to save and invest.

The failure to explain the high costs of communal ownership in the Pacific has maintained political opposition to land surveys and the allocation of individual land rights. When the Morauta Government initiated land tenure reform, it was sabotaged by its own Government members who mounted protests in the streets. The initiative had to be withdrawn.

Pacific Islanders who want to cling to communal land ownership rather than command individual property rights have every right to make that choice. They have to accept, however, that their living standards will not rise, and that the present levels of male underemployment, alcoholism and crime, will increase. Young men will continue to drift in and out of urban areas, spreading HIV/AIDS. There is no reason, moreover, for Australian or any other taxpayers, to underwrite such choices with aid.

Corruption and crime

The violence that was endemic in Pacific societies was held at bay during the colonial era by the imposition of security, and probably more importantly, by rising living standards. The growth of crime and civil unrest that has followed high unemployment and underemployment since independence is well documented.[21] Apart from open warlordism in Bougainville, Solomon Islands and the New Guinea Highlands, the Pacific is awash with guns, coups occur and threaten, and urban crime, among the highest in the world, is spilling into villages. The comprehensive study by Alpers and Twyford concludes:

> In Fiji, the Solomon Islands, and Papua New Guinea, groups bent on rebellion, intimidation, and profit have treated state-owned armouries as gun supermarkets, taking weapons when needed.
>
> Direct impacts of armed conflict include death and injury, violation of human rights and international humanitarian law and forced displacement . . . Indirect impacts . . . include declining access to basic entitlements such as health and education, long term trauma and disruption, in particular to the prospects of an entire generation of young people, damage to social and economic infrastructure, and declining levels of investment, economic productivity and self sufficiency.[22]

Women and children are the main victims. Maxine Pitts found: 'Sexual and other aggressive attacks on women and children are frequent, vicious and violent in Papua New Guinea'[23] and violence against women is widespread in the Pacific.

Making bloated governments the main source of income and resource rents has made corruption rife throughout the Pacific. High levels of corruption among the political and bureaucratic elites and their business associates in the Pacific have been documented. They are constantly covered in the Pacific press although corruption is so common that even large scandals scarcely merit a day's attention. Expatriates play a major role in transferring the gains of corruption abroad. Pacific legal systems are not operating and corrupt practices are not prosecuted. Frank Senge Kolma, writing in *The National* [24] pointed to eight Papua New Guinea reports that 'unveiled a litany of corrupt practices, bribery, fraud, and mismanagement, flaunting of power and flouting of laws, rules and regulations. The Auditor-general's Office and Ombudsman

Commission have regularly been decrying corrupt practices in their annual reports. In many instances, important leaders of Government have been referred to answer charges before leadership tribunals and many have lost their offices as a result. However, none have gone to jail for their crimes. The common person sees the law chasing after him to rob him of his freedom while leaving the larger rascal free to rob him of everything else.'

When thieves who steal from the public purse are not pursued, small criminals are encouraged in their depredations. Papua New Guinea is by no means unique. Fiji's National Bank of Fiji scandal was followed by corruption probes into the Customs Department, the Companies Office, the Registrar General's Department, the Housing Authority, the Agriculture Department and the Public Works Department.[25] Corruption is endemic in Vanuatu. In Samoa, a notorious report of the Controller and Chief Auditor, Sua Rimoni Ah Chong, was repressed. The circumstances surrounding the murder of a Cabinet Minister have never been cleared up.[26]

4. COLONIAL LEGACIES

Nostalgia for the colonial era is emerging in the Pacific as well as among old Pacific hands in Australia and New Zealand. It is misplaced. Colonial administration was almost entirely carried out by expatriates. *Kiaps*, other local administrators and Christian Missions treated local populations as children. Roads, airfields, ports, water and electricity serviced urban areas where expatriates lived. Production and productivity were neglected except for expatriate plantations. Australian trading firms dominated wholesale and retail trade. Social infrastructure was minimal. Education was the biggest failing. In the Anglophone colonies, *pidgin* was regarded as a good enough language for islanders. Society was colonial. As late as 1963, when the Anglican (indigenous) Bishop of the Solomon Islands visited the capital, he had to stay in the official residence because the Honiara 'blackbirders' hotel (immortalised by Somerset Maugham) still only accepted white guests. In Port Moresby, the waiters (called 'boys') were thought so incapable of remembering the names of such exotic breakfast dishes as bacon and eggs that customers ordered each dish by numbers.

The prospects for independence were long denied (as they still are in the French colonies) so that when independence came to the Pacific as a result of global anti-colonisation agitation, Pacific populations were unprepared for it. Unpreparedness was a major cause of the difficulties the Pacific has encountered. Reaching backwards towards re-colonisation was unrealistic and untenable then, and is even more unrealistic now, as the Australian Government clearly recognises.[27]

'The common person sees the law chasing after him to rob him of his freedom while leaving the large rascal free to rob him of everything else.'

The welfare state in the Pacific

Welfare-statist policies and institutions that characterised post-World War II England, France, Australia and New Zealand were imposed on the Pacific in the last days of colonialism in the name of equity. Redistribution was put ahead of production, most clearly in Papua New Guinea's 1972 'Eight Aims',[28] which ignored that there was nothing to distribute until production and productivity increased. The other Pacific states followed the same policies. In Fiji, planning was regarded as so central to economic policy that the production of chickens and eggs was 'planned' for 20 years ahead. In New Zealand's colonial Western Samoa, public health services in urban areas entitled the high income urban population not only to free health for themselves and their families, but also for their pets. Cats and dogs were de-sexed at the public expense. The health service did not, of course, stretch to the indigenous countryside.

The social and physical infrastructure throughout the Pacific is still based on 1950s concepts. Town planning in Port Moresby mimicked Canberra's, one of the world's costliest urban communities, least adapted to real hydrocarbon costs. Universities copied Australian 'redbricks' with disproportionate social and humanities faculties in a region crying out for technical and professional qualifications.

In the 1960s and 1970s Australian welfare-statist advisors promoted policies for the Pacific that New Zealand and Australia had to transform to stop falling behind the rest of the world. The public ownership of utilities—electricity, telecommunications, ports and airlines—was an essential component of welfare-statist policies. It was not recognised that air and shipping services could be obtained more economically on contract than by national ownership, notably for small economies. Excessive wage and manning policies were universal. Public enterprises became sources of corruption as well as inefficiency. They meant high costs of inputs into private production, notably of exports, and high costs, directly and indirectly for consumers, limiting already small markets. Continuing losses of publicly owned enterprises—Air Nuigini, for example has not been in the black for even one year of its operations and Air Nauru lost $40 million a year—undermined budgets throughout the Pacific. When it finally became evident that publicly owned enterprises were crippling budgets in Papua New Guinea, the Morauta Government attempted privatisation. It was thwarted on all sides. The public enterprises it tried to corporatise or privatise were so run down that they were worthless. Because the public sector had crowded out the private sector, there were very few local private buyers. The public service employees in inefficient public enterprises were able to combine with politicians benefiting from the mismanagement of public enterprises to prevent privatisation.

Public enterprises became sources of corruption as well as inefficiency.

The colonial administrations copied zoning, trading and industrial regulations into the Pacific. This has crippled the evolution of an informal sector critical to development in rapidly growing countries. Personal services such as hairdressing, washing and dry cleaning have been limited by regulations designed to keep the streets clear in London, Canberra and Wellington. Police forces that seem incapable of containing assault and robbery are still bulldozing informal fruit and vegetable markets because stall holders are in the 'wrong place' (where the customers are) or are unwilling to pay the licence fees and the additional charges that police demand.

Trade policies

Inappropriate trade policies (following Australia and New Zealand of the 1960s) are a core problem in the Pacific. Critically, economic advisors failed to recognise the costs that appreciation of the exchange rate as a result of aid and resource rents created for non-mineral exports and for import substitution.[29] Mineral, timber and fishing rents could carry the appreciation of exchange rates, but high exchange rate policies exacerbated market appreciation, dragging down the export of agricultural products and hindering manufacturing for the domestic market. Many of the Pacific's expatriate advisors were unaware of the importance of labour intensive employment, not merely to put the underemployed and unemployed to work, but also to create skills on the job and to stimulate savings, entrepreneurship and indigenous investment. Skill creation is still regarded as something that governments should do.[30]

The Pacific economies are so small that they were of necessity fairly open at independence, but UN advisors supported protection for import substitutions. In spite of the natural protection afforded by distance, high wages and input costs meant that Pacific firms could not compete internationally in producing building materials, consumer goods such as furniture and canned fish and beef. High tariffs were therefore introduced and are still around 40% and anti-dumping is used to limit imports further.[31] Beer appears to be the principal domestic manufactured product that is competitive. Because protection fosters capital intensive choice of techniques, expatriates and expatriate firms from industrial countries dominate the modern economy in the Pacific.

The Pacific islands have adopted the creed of the IMF, the World Bank and the Asian Development Bank that foreign investment equals development. They seek it eagerly with tax holiday subsidies. But foreign investment only has positive returns for a country if it is invested in competitive production for the domestic market or for exports. Foreign investment in minerals has led to internationally competitive production and exports. But high tariffs have created 20 year old 'infants' that cost the balance of payments more than they save.[32]

Corruption and crime even deter foreign investment in minerals. Mineral exploration is down. Some foreign investment is still going into the exploitation of timber, but because of corruption, on shockingly bad terms.

Minerals (gold, copper, silver, petroleum, nickel and phosphate), timber, agricultural products (coffee, cocoa, copra, palm oil, rubber, tea, vanilla and vegetables) and fish (or the sale of fishing rights) are the principal Pacific exports. Clothing from Fiji and some small manufacturing exports from Tonga and Samoa are the sole labour intensive manufactures, although unemployment and underemployment cry out for such industries.

Increasing the processing of their raw materials is a Pacific obsession. Petroleum refineries and other so called 'value adding' proposals abound. But processing tends to be highly capital and technology intensive. If it is not undertaken efficiently and on a large enough scale to be internationally competitive, it will erode the resource rents earned in the primary stages of mining, timber extraction and fishing, as many developing countries have found to their cost.

Pacific countries have Most Favoured Nation (MFN) access to world markets, so that membership of the World Trade Organization (WTO) only has formal significance. Because the GATT/WTO exempted developing countries from its reciprocity and tariff reduction obligations, it is of little use in persuading domestic interest groups of the value of free trade. Most of the Pacific countries are also individual members of APEC, essentially a political organisation that does not bring reciprocal trade benefits. Considerable scarce resources are spent on trade representation by Pacific countries. But trade requires business, not government, salesmen. World trade markets are not in Europe or America but on the internet. The Pacific countries are wasting their slim resources, with the encouragement of donors, on trade offices that have nothing to sell.

Trade requires business, not government, salesmen.

Pacific countries are the so called 'beneficiaries' of three preferential trade arrangements. Giving developing countries the General Scheme of Preferences (GSP) was an United Nations Conference on Trade and Development (UNCTAD) proposal. It was accepted by industrial countries embarrassed by their high tariffs and quantitative restrictions on labour intensive products of interest to developing countries.[33] Fiji clothing exports benefit from the United States GSP.

The EEC-EU, in addition to its GSP scheme, introduced the Lomé preferential tariffs (with aid components for primary product trade fluctuations) for its previous colonial dependencies in Africa, the Caribbean and the Pacific (ACP states). Privileged quota access at a high price to the EEC-EU's heavily protected sugar market was the principal benefit for the Pacific. Fiji's clothing also has privileged access, but the Lomé rules of origin have made it difficult to exploit. Access to the EEC-EU markets for fish was found to be exploitative and damaging to Pacific fisheries because of the complexity of the Lomé rules of origin and ownership of fishing vessels.[34]

Australia (with New Zealand) increased the scope of its Australian Scheme of Preferences with the South Pacific Regional Trade and Economic Co-operation Agreement (SPARTECA) that, with the exception of sugar, gives the Pacific duty free access to Australian markets. Its principal impact has been the encouragement of Australian investors in the Fiji clothing industry and the establishment of the motor vehicle electric harness plant by a Japanese investor in Samoa.

Preferential tariffs for developing countries always seemed dubious, with importers in industrial countries being the principal beneficiaries. They appeared to be attractive while industrial country tariffs were high, but they encouraged investment that became uncompetitive when tariffs fell. This is a current problem for the Fiji clothing industry. Recent research has reinforced previous doubts about the value of preferential schemes for developing countries by finding that preferences delayed developing countries' trade liberalisation reforms.[35]

Inappropriate industrial relations

Australian and New Zealand trade unions had the best of intentions when they gave their Pacific brothers their unique labour market regulation systems. But both countries have substantially reformed their own labour market regulations and in both countries there is a lively debate about further reforms. The 1960s 'industrial relations club' tripartite organisation of governments, employers and employees was even more inappropriate to developing economies than it has been for Australia and New Zealand, but in the Pacific it persists, crippling employment creation.

Wage and salary levels and working conditions within the Australasian industrial relations framework were not related to productivity levels of undeveloped economies. Basic wage determinations were introduced in colonial times. When Australian advisors became involved in remuneration determinations for indigenous public servants in Papua New Guinea in the 1970s,[36] basic wages were supplemented by wage loadings and working conditions based on colonial rates of pay that compensated expatriates for short terms of employment and absence from their home countries. Privileges such as housing and home leave were loaded on to Pacific administrative costs and continue to this day. Shift work and weekend rates, sick leave, holiday and long service leave were awarded and spread to the private sector. These on-costs not only raised the cost of production, but also introduced inflexibility. Pacific ports typically worked eight hour days and five day weeks whether ships were in port or not. The rents associated with mineral development enabled high remuneration to be negotiated in mines (with additional education, health and housing benefits), placing additional wage pressures on the private sector and strengthening arguments for high protection. As fringe benefit on-costs amount to 40% of earnings (much as in Australia), tinkering with basic wages in the 1990s had little impact on the relationship between productivity and earnings.

Inappropriate industrial relations are replicated throughout the Pacific.[37] Inexorable market based currency devaluations indicate the overvaluation of remuneration in relation to productivity, but they have not been able to affect the structures of high labour costs.

The inappropriateness of industrial relations is illustrated every day.

The inappropriateness of industrial relations is illustrated every day. When a Port Moresby (woman) entrepreneur developed a line of sportswear clothing that attracted the interest of a large Australian retailer, she regretfully had to decline the opportunity to become a supplier. She had started on a small scale, but if she employed more than 50 workers she would have become subject to Papua New Guinea wage and working conditions that competition against other clothing suppliers could not support. She closed down her factory. Other attempts to start up clothing exports in Port Moresby have also failed. In Fiji the labour intensive clothing sector struggled with similar difficulties until the Rabuka coup in 1989 so weakened the economy and the (Indian led) trade unions that women, desperate to buy food to feed their families, accepted substantially lower than officially mandated wages. Limited attempts to reform industrial relations in the Pacific have not been successful.

It would be interesting to see whether the two Papua New Guinea public and private sector trade unions would be prepared to support, or at least shut their eyes to, the introduction of measures that would enable labour intensive export industries in Port Moresby and Lae. In a similar situation in Singapore in 1965, with youth unemployment up to 17%, the Singapore trade unions agreed, with strong pressure from Lee Kwan Yew, to the introduction of 'pioneer' status for firms that would produce for export. 'Pioneer' status suspended all industrial arrangements (except occupational safety) for an initial period of five years. Most of the initial workers were young women. They were so unused to the discipline of eight hour shifts that the firms provided free coffee at the start of shifts to encourage timely and regular attendance. When the first five years had passed, Singapore had become one of the East Asian 'Tigers' with a labour shortage. The labour conditions associated with 'pioneer' were bypassed in a rapid escalation of skills and wages. A similar experiment in Papua New Guinea would require secure industrial estates and perhaps even secure housing for workers. Smaller Pacific islands only need small investments to soak up unemployment as the knitting factory in Tonga and electric harness motor vehicle plant in Samoa have shown.

Economists cannot predict which labour intensive industries would be suitable for the Pacific at this stage of development of world markets, but trade theory indicates that a country will always have a source of comparative advantage that it can exploit in trade with other countries. Given an appropriate policy environment, entrepreneurs, not bureaucrats, will find it.

Some progress in agricultural output could be expected in the Pacific with improvements in infrastructure and security, at least to supply local food demand. But the difficulties of transforming communal into individual land ownership are so great that urban employment solutions are likely to be more successful in the short to medium term than agricultural ones.

5. MACROECONOMIC POLICIES AND BUDGET DEFICITS

Most of the Pacific islands (with the encouragement of the IMF) have opted for a full structure of monetary as well as fiscal policy, including independent currencies managed by central banks. While Papua New Guinea and Fiji have the economies of scale to make independent monetary policy viable, it is doubtful whether central banks are economic for smaller economies. Some of the very small islands have opted for the use of United States, Australian or New Zealand dollars. This means that they have to maintain prudent fiscal policies—that is, tax collections that meet expenditures—to ensure price stability. Dollarisation (using a foreign currency) is not an option for economies that are fiscally imprudent and where unions are so strong that wages are inflexible, as Argentina demonstrated. The tying of the Pacific franc to a French franc at an overvalued rate is a major cause of economic stagnation in the French Pacific as it is in West Africa.

Given the present state of the Pacific economies, a common Pacific currency is some time away. Real reforms in all Pacific economies, followed by at least a decade of fiscal prudence and monetary stability with solid economic growth, would be necessary before any form of Pacific currency, or one joined to the Australian and/or New Zealand dollars, would be feasible.

The Pacific financial sectors are weak, reflecting government ownership and intervention in banking. Until individually owned land can be used as security, banking will not develop in rural areas. Government ownership of banks, unreasonable central bank practices and excessive government borrowing for budget support have crowded out the private financial sector. The World Bank's International Finance Corporation (IFC) has added to the 'crowding out' of private sector lending by public sector intervention. Its subsidised Kula Fund edges out medium to long term private financing opportunities.

The bulk of budgets is spent on consumption.

Budgets

The Jackson Committee in 1984 drew attention to the escalation of budget deficits in the Pacific.[38] The budget problems of Papua New Guinea were further documented by Ron Duncan and Ila Temu in 1995.[39] Satish Chand has brought the story up to-date showing that the current direction of policy is not sustainable.[40] Haroon Akram Lodhi has drawn attention to Fiji's escalating budgets.[41] Pacific budgets are characterised by persistent and escalating excesses of expenditure over revenue. None of these deficits have funded investment. The maintenance of infrastructure has been neglected. The bulk of budgets are spent on consumption, that is, excessive wages and wasteful practices of public enterprises, administrative wages and salaries, and purchases of goods and services (that include substantial corrupt payments). In spite of aid and resource revenues, Pacific governments habitually budget to spend more than they collect in total 'revenues'—including aid—by borrowing domestically and abroad from official and commercial sources. Actual expenditures exceed revenues and aid flows by even greater amounts than annual estimates presented to Parliaments.

The Morauta Government's attempts to reform the Papua New Guinea budget were undermined by members of his uneasy coalition. His moderate reforms were unacceptable to those whose depredations of the public purse they curtailed. Hence the vigorous political campaign against him that led to the return of 80 new, inexperienced members of Parliament. Fiji's budget deficit financing exploded after the Rabuka coup, and again after the May 2000 coup. Economic reform came into conflict with attempts to subsidise indigenous Fijians, so that little has been achieved. Escalating budget deficits were a critical component of the collapse of the Solomon Islands. The costs of budget waste are evident in Nauru's inexcusable squandering of billions of dollars.

Aid donors have contributed markedly to escalating budget deficits in the Pacific by permitting their taxpayers' funding of aid to be considered as 'revenue'. [42] The international financial organisations also allow concessional loans (that have to be repaid by Pacific taxpayers) to be considered revenues. Pacific budgets thus openly recognise that aid is fungible; that is, it can be spent by governments on their recurrent programmes rather than on development. Aid funds contribute from 20 per cent of budgets in Papua New Guinea to 80 per cent of budgets in small states. Budget estimates generally show lower aid revenues than development expenditures, with domestic revenue contributions to development expenditures. But actual recurrent expenditures expand in practice to reduce development expenditures to negligible shares of actual budgets, accounting for the lack of infrastructure maintenance and expansion. Removing aid flows from budgets is essential if Pacific governments are to reform their economies and hence balance their budgets.

Pacific governments deny that they have serious economic and social problems. They do not indicate any intention of reforming their economies.

Is reform being contemplated?

Pacific governments show no awareness of the discrepancy between population and national income growth and deny that they have serious economic and social problems. They do not indicate any intention of reforming their economies. Prime Minister Somare's recent summing up of Papua New Guinea's economic situation,[43] his Government's proposal for an export based recovery plan[44] and Joshua Kalinoe's presentation to an Australian Senate Inquiry, [45] all clearly indicate that no departure from past policies is being contemplated. The Senate Committee's questioning could not elicit any evidence of programming that would lead to Prime Minister Somare's export-led recovery. Such fundamental export bottlenecks as communal land ownership and inappropriate labour regulations were not mentioned. There was talk of, but no plan for, the rehabilitation and extension of roads and for the privatisation of public utilities. Corruption was claimed to be no higher than in other countries, with Port Moresby's crime like that of any large city such as Sydney. Thus Japanese tourists, instead of 'over-flying' Papua New Guinea, were to become the mainstay of a rapidly expanding tourist industry. Timber exports were to be increased without a plan for avoiding environmental damage or the corruption associated with past timber extraction. And notwithstanding the decline in mineral exploration, mineral investment was expected to recover to create new exports.

Pacific governments cannot alone be blamed for policies that turn them into paupers. At the side of each sit highly remunerated expatriate advisors putting a spin on embarrassingly incompetent and inadequate programming for more of the same.

Only the Pacific peoples can take charge of their own futures. Even if it means less polished presentations, they have to start writing their own policy and administrative papers rather than leaving them to expatriate advisors. After 25 years of independence many trained professionals are available. They are not being given the opportunities to work in their own countries. Many are working abroad. Given the difficult, counterintuitive concepts of the economic theory of aid and mineral rents, an open discussion in academia, politics, bureaucracies and media, similar to the debate that has transformed Australia from a protectionist to an open trading country, is essential in the Pacific.

The Pacific Way to Reform

The Speaker of the Papua New Guinea Parliament (former Prime Minister) Bill Skate in a double page colour advertisement in the *The National* daily newspaper in April unveiled plans for a giant 'Luna Park' fun park costing 7.4 million Kina (A$3.3 million) on Port Moresby's Ela Beach foreshore. The fun park will include an outdoor cinema, picnic pavilion, water slide, auditorium, children's playground and mini golf to entertain the 'raskols'.

Mr Skate, who is a Member of Parliament for the Port Moresby area, will back the project with public funds intended for his electorate, presumably on an ongoing basis, for the park is expected to cost 500,000 Kina ($A221,765) a year to maintain.

A letter to the *Post Courier* (22.4.03) sums up the local reaction:

> It truly angers me and is frustrating to think that there are people dying due to lack of medicines while we think of throwing money into lavish projects.
>
> Many other public services have grounded to a halt, policemen have been rendered incapable of doing their jobs because of a lack of money as well.
>
> A friend of mine in the National Capital District has been robbed three times on her way home from work. I wonder if she wants a fun park and the youths who robbed her want one too? Does the NCD need a fun park or better hospital care facilities or law and order?
>
> It makes me wonder if there is any truth in the unspoken statement that: 'An underdeveloped dependent PNG is better for its politicians and investors than a developed and self-sustaining PNG' because I can't see how a fun park will benefit PNG in any way. So what is the logic? I don't get it?
>
> God grant our leaders the common sense to see that basic services around the country could use the K7.4 million. Rethink the fun park. Clear vision is what our nation needs.
>
> Don't let this happen in PNG when basic services still don't function adequately after almost 28 years of independence.

There is no dearth of firms willing to construct Mr Skate's publicly funded projects. In this case it is a PNG-Australian consortium, CCS Anvil and Arup.

6. AID TO THE PACIFIC

Australia was an early participant in the Western flow of aid to developing countries. Sub-Saharan Africa has received the highest aid during the last 30 years, but its growth has been the slowest, with living standards falling in many African countries and more than 350 million people living in absolute poverty.[46] Aid appears to be inversely related to growth. Recent research shows that worldwide aid has not even been effective in countries that have adopted pro-growth policies.[47]

Table 4. Total and per capita aid flows by region

	Total aid flows 1970-1999 US 1998 million dollars	*Average annual aid flows per capita 1995-1999 US 1998 dollars*
Sub-Saharan Africa	416,600	22
India	85,000	2
Other South Asia	137,800	9
China	41,200	2
Pacific	49,300	220
Other East Asia	152,600	8
Caribbean	45,100	34
Latin America	111,700	10
Middle East and North Africa	282,600	15

Source: The Development Assistance Committee, *Development Co-operation Reports*, 1971 -2000, OECD Paris.

The Pacific has received almost US$50 billion of aid in 1998 dollars (A$100 billion) since 1970, representing the highest developing country aid inflows per capita in the world by a large margin. Papua New Guinea and Fiji, because of their relatively large populations receive relatively modest aid amounts per capita, although these aid flows are still much higher than equivalently sized countries in the Caribbean and Africa.

Table 5. Total and per capita aid flows to the Pacific since 1970

	Total flows since 1970 US 1998 million dollars	*Average annual aid flow per capita since 1970, US dollars*
Papua New Guinea	15,592	104
Fiji	1,576	65
Solomon Islands	1,477	110
French Polynesia	8,533	1,210
New Caledonia	8,708	1,363
Vanuatu	1,285	217
Samoa	1086	213
Tonga	698	233
Kiribati	593	217
North Marianas	-2	0
Marshall Islands	362	232
Cook Islands	407	646
Palau	532	933
Wallis & Futuna	274	457
Micronesia Fed. States	630	178
Nauru	18	51
Tuvalu	214	647
Niue	182	3,558
Tokelau	91	3,026
Pacific Islands (trust Tr.)	5,193	
Oceania Unallocated	1,449	
Total	49,258	220

Source: The Development Assistance Committee, *Development Co-operation Reports*, 1971-2000, OECD Paris. Aid flows include official development assistance (including the concessional elements of loans) from OECD countries, multilateral organisations and Arab countries.

Papua New Guinea is the largest aid recipient, with the Francophone territories next and the former Micronesian Trust Territories also receiving significant volumes in total and particularly per capita. Aid to Tokelau is six times its per capita US$500 income; and Niue's aid is three times its per capita US$1,300 income, illustrating extremes of 'boomerang' aid.

The Pacific, 30 years after independence, has little capacity for aid implementation by local contractors.

The aid that flows to the Pacific is termed 'boomerang' aid because much of it returns to donor countries in remuneration for consultants and implementing companies. Formal 'tying'—that is, insisting that aid is sourced in the donor or recipient country—is not the cause of this problem. Pacific firms receive preferences in bidding for bilateral and multilateral contracts. AusAID has worked to nurture Pacific firms. But the Pacific, 30 years after independence, has little capacity for aid implementation by local contractors.

Bilateral donors

France, Australia and the United States are the current principal aid contributors, with Japan emerging as a significant donor, particularly where it has fishing interests (Table 6). The bulk of French aid takes the form of payments to the French public servants who run New Caledonia and French Polynesia, so that the main benefits to local inhabitants are in supplying fruit and vegetables and domestic services. Expatriate staff live well, but there is little evidence of local development.

Bilateral aid agencies have annual meetings with Pacific states to discuss requests for aid ('shopping lists'), and review the progress of current aid projects and programmes. The recipient states play off donors against each other to increase aid volumes, playing on the bilateral donors' postcolonial unwillingness to impose efficiency and effectiveness conditions on recipients lest they be accused of 'neo-colonialism'.

Table 6. Aid to the Pacific by donor, 1999-2000

	Annual average $US million
Countries	
France	747
Australia	232
United States	161
Japan	151
New Zealand	74
European Union	45
Germany	5
Development Banks	
ADB (Development Fund)	26
World Bank - (IDA)	8
UN agencies	
UNTA	13
UNDP	4
UNICEF	3

Note: Aid data do not include defence expenditures or the (competing) aid flows from China and Taiwan.
Source: The Development Assistance Committee, *Development Co-operation Report*, 2000, OECD Paris.

Australian aid

AusAID has so many problems in delivering aid to the Pacific that it is difficult to recognise that it is one of the best of the industrial countries' bilateral aid agencies and far superior in efficiency and effectiveness to the multilateral agencies.

AusAID is crippled by two considerations. It is not permitted to express views about the Pacific (and other recipient) economies to establish whether a given economic environment makes it possible for aid to succeed. It is also not permitted to negotiate so as to compel recipient countries to acknowledge that Australia has a right to insist that its taxpayers' funds are spent efficiently on projects and programmes that will be effective.

Australia has a right to insist that its taxpayers' funds are spent efficiently.

AusAID's best projects and programmes have thus been in countries like Thailand and Indonesia that were sharply focused on growth in the 1970s and 1980s. In its Pacific projects in education, health, water supply, other infrastructure development and police support it has both hands tied behind its back. Because recipients have not been obliged to play by rules of mutual obligation, aid to the Pacific largely remains budget support. For example, AusAID pays for 85% of road maintenance in Papua New Guinea.

UN agencies

The United Nations Development Programme (UNDP) manages small but widely distributed multilateral flows, albeit with frequent visits from the staff of other UN agencies. UN programmes in the Pacific are not driven by Pacific needs, but by UN agendas. In the past most of the UN support in the Pacific has been for welfare and statist economic policies, notably for public investment and protection for import substitution. Until the 1980s South Asian socialists and East European central planners were heavily represented among UN advisors in the Pacific. Socialist outlooks have become more muted, but UN agencies still cast doubt on the strong relationship between economic freedom and economic growth.[48] UN advice found a warm welcome in the postcolonial Pacific and was also strongly supported by leading NGOs in Australia. In a democracy everyone of course has a right to their views, but the majority of Australian taxpayers in supporting reform at home has voted against the welfare and statist views that the UN promotes in the Pacific.

Pacific bureaucracies are constantly being visited by UN staff and their contractors. Conferences, seminars and thousands of pages of reports flourish.[49] They are short on analysis and lack reliable data series. Armies of staff and contractors are occupied in taking up the time of Pacific public servants who are thus deflected from attending to their responsibilities.

The IMF, the World Bank and the Asian Development Bank

The Pacific has also received some IMF credits and substantial loans from the World Bank and the Asian Development Bank. These provide a platform for co-financing and other loans from bilateral governments, export credits and commercial borrowing. At the end of 2002, Papua New Guinea was the only Pacific country with an IMF credit of (US$102 million). Papua New Guinea has received US$1.3 billion from the World Bank (in 1998 US dollars) and a sum of US$800 million from the Asian Development Bank.[50] The lack of development of infrastructure and social services casts doubt on the effectiveness of more than 25 years of development banks' lending to the Pacific. In 1992 the World Bank itself concluded that 'the Bank was generally unable to make an effective contribution to the development of the Pacific member countries during most of the 1980s'.[51]

The IMF, the World Bank and the Asian Development Bank are still committed to the view, shown to be erroneous by Peter Bauer 50 years ago, that developing countries cannot progress without aid to fill their 'savings gap' and their 'foreign exchange gap'. They have therefore played an important role in the Pacific in fostering aid dependency. The World Bank initiated a Consultative Group in 1988 to discuss and coordinate donor activities for Papua New Guinea. For other Pacific countries mendicancy is more informal. The aim of such consultations is to maintain aid flows.

The IMF, the World Bank and the Asian Development Bank have played an important role in fostering aid dependency.

The IMF and World Bank economic reports prepared for these and other purposes comment on the Pacific's lack of growth, but avoid analysing reasons that would be unpopular with the aid recipients.[52] The IMF and the World Bank took on the responsibility for conditionality (ensuring that recipient governments follow prudent project, programme and economic policies so that aid could work) to avoid 'colonial' interventions by bilateral donors and to supply economic analysis to other multilateral organisations to avoid duplication of effort. The Asian Development Bank has been happy with this arrangement. The IMF and the World Bank have disagreed from time to time in their policy advice, but this has not mattered because they did not intend their advice to be taken seriously. From time to time, when economic management became egregiously dysfunctional, the IMF and the World Bank have withheld their lending for a time but they have never terminated it. Without effective conditionality the international financial organisations' loans have readily found their place in Pacific budgets.

The content of the international financial organisations' lending programmes to the Pacific is not impressive. When the IMF, in December 2002, became concerned with the number of 'ghosts' (people with two jobs, dead people and others), thought to be at least 10% of Papua New Guinea's public service payroll, it engaged an Australian contractor to install a payroll system that 'is one of the most sophisticated in the world' at a cost A$13-20 million. The contractor argued that this would save the PNG government A$45 million a year by finding and dismissing the 'ghosts'.[53] Hopefully, this contract is funded by a technical assistance grant, for no payroll system can find and dismiss 'ghosts'. Only political will can do so.

The World Bank introduced a *Pacific Regional Strategy* in 2000 to overcome past failures.[54] In March 2003, eight ongoing projects in Papua New Guinea amounted to US$206 million. They covered technical assistance for gas development and two other mining sector 'strengthening' grants, forestry and road maintenance.[55] In Fiji, the main projects have covered highway, power, telecommunications, housing and sugar development; in Samoa roads, highways, power and telecommunications were targeted; the Tonga Development Bank received support and in Vanuatu the focus is on education, housing and agricultural research and extension. These projects are an improvement on the millions spent on 'public sector capacity building' in the 1990s that had no evident effect on public sector efficiency (though it filled consultants' pockets). But it is not clear, whether, being embedded in recurrent expenditures, they can be implemented efficiently and have high enough returns to service the loans.

The Asian Development Bank concentrates its funding in Papua New Guinea on budget support for Higher Education (US$16.5 million), Health Sector Investment (US$9.127million), Smallholder Support Service Pilot (US$7.6 million), Fisheries Development (US$6.5 million), Financial Management (US$25.8 million), Employment Oriented Skills (US$18.796 million), and Microfinance US$9.477 million). Road Maintenance and Upgrading (US$63 million) and Rehabilitation of Marine Navigation Aids (US$19.8 million) represent budget support rather than development. Out of a total US$203.351million in ongoing loans in September 2001, only two water supply projects (totalling $US26.739 million) could be classed as development projects. Taxpayers—mostly low income—will have to service and repay the Asian Development Bank's lending that goes to budget support. By 1999 only 18 out of the 36 projects in Papua New Guinea funded by the Asian Development Bank since Papua New Guinea joined it in 1971 had been evaluated. Only six were rated 'generally successful', 11 were rated 'partly successful' and one was rated 'unsuccessful' by the Bank's generous evaluation standards.[56]

The Meltzer Commission of the US Congress in 2002 concluded, devastatingly, 'that neither the World Bank nor the regional banks are pursuing the set of activities that could best help the world move rapidly toward (a world without poverty) or even the lesser, but more fully achievable goal of raising living standards and the quality of life, particularly for people in the poorest nations in the world'.[57] The Meltzer Commission strongly recommended a sharp downsizing of the IMF, the World Bank and the regional development banks to reduce the damage they were doing to developing countries.

The Meltzer Commission strongly recommended a sharp downsizing of the IMF, the World Bank and the regional development banks.

Table 7. Development bank flows to the Pacific

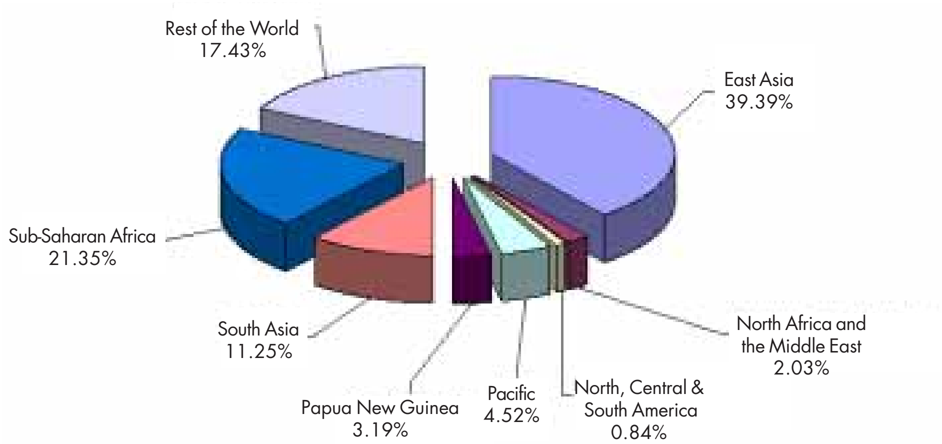
	World Bank 1945-2002 US million1998 dollars	*Asian Development Bank end 2001 US current million dollars*
Papua New Guinea	1,327	849.3
Fiji	277	161.1
Solomon Islands	59	79.3
Vanuatu	23	51.3
Samoa	87	113.9
Tonga	12	42.9
Kiribati		15.1
Marshall Islands		71.1
Cook Islands		26.7
Micronesia Fed. Sta.		56.1
Total	1,785	

Source: Compiled from World Bank, Asian Development Bank and IMF country data.

6.1 NGOs in the Pacific

Australian NGOs do not have much interest in the Pacific. Whales appear to engage more of their attention than the people of the Pacific. Partly this reflects the relatively high traditional living standards in the region, but also a lack of knowledge and interest in Australia about the Pacific. In part, of course, NGO venturers are more attracted by distant countries.

Chart 9. Australian NGO activity by region



Source: AusAID,www.ausaid.gov.au/publications/pdf/ngostatreport 02/report_charts-1.pdf

Multinational NGOs support policies that are a major cause of the Pacific's difficulties.

While the humanitarian role of NGOs is unquestionably important in the many disaster (although mainly man-made) situations that afflict developing countries, the role of NGOs in development is more open to debate. The multinational NGOs of which the main Australian NGOs are subsidiaries strongly support the welfare and statist policies that have been abandoned by Australia and that are a major cause of the Pacific's difficulties. The NGOs, of course, have every right to their views and to propagating them, though not at taxpayers' expense, particularly if they run counter to Australian national policy.

It is extremely doubtful whether typical NGO projects such as 'micro-finance' or 'empowering women' can be effective in regulatory environments that are hostile to the development of informal business activities. Yet they are subsidised by tax contributions to NGOs.[58]

The role of volunteers, for example as teachers, health workers or accountants should also be open to debate. Volunteers are often seen as taking jobs from local people. Young, inexperienced volunteers are often viewed dubiously as being aid that developing countries give to parents in wealthy countries to help immature young people to grow up, rather than aid that they receive. Perhaps Australian NGO workers should be required to gain experience in social work at home before they undertake development tasks abroad.

6.2 Debt in the Pacific

Debt/GNP and similar ratios can be misleading because the incidence of debt and debt repayment capacity depends on whether funds borrowed have been invested productively. Such rapidly growing countries as South Korea easily managed much higher debt levels than the Pacific because they invested the public and private sums they borrowed productively.

In the Pacific, only Papua New Guinea and Samoa have high debt/GNP ratios and even they have relatively modest debt service/export ratios. But even these low ratios become a burden because the funds borrowed have largely been spent on recurrent expenditures rather than being invested productively.

Discussion of debt forgiveness has thus begun, although Australia has no debt to forgive because it gives all its aid as grants.[59] The Australian Treasury has wisely believed that developing countries would not use loans more prudently than grants.

Aid forgiveness has a very sorry track record. By the early 2000s, debt forgiveness had a 25 year history. Its main effect was to enable countries to borrow more so that they were more in debt at the end of 2000 than they had been 20 years previously. A secondary effect of aid forgiveness has been to shift aid from countries that manage their economies reasonably well to those that are imprudent. During 1996-2000 the low income developing countries that had their debt forgiven had 30% of this group's population but received 70% of its aid flows.[60]

Table 8. Pacific debt, 2000

	Papua New Guinea	Fiji	Solomon Islands	Vanuatu	Samoa	Tonga
Debt outstanding US$m	2,515	120	152	67	147	58
Public and publicly guaranteed $USm	1,502	101	121	67	147	58
Private $USm	1,104	19	32	0	0	0
Debt service US$m	280	38	9	2	6	4
Public and publicly guaranteed: $USm	169	29	4	2	6	4
Private $USm	111	9	5	0	0	0
Debt/GNP %	71.3	13	55	31	84	38
Debt service/exports %	13.5	4	7	1	11	12

Source: World Bank, *Global Development Finance 2002*, Washington D.C.

7. CONCLUSION

As an open country, Australia is fortunate in being a neighbour to the region that has managed growth and poverty alleviation successfully. Yesterday's developing countries in East Asia have become trading partners. The Pacific, in marked contrast, has failed to develop. Large volumes of aid (in relation to the Pacific population) have contributed to failure. The relationship between aid and growth is inverse in the Pacific as elsewhere.

The relationship between aid and growth is inverse in the Pacific as elsewhere.

The failure of the Pacific economies to grow and develop has prevented the transition from traditional self-sufficient agriculture to modern well being. Living standards are low and stagnating. Parliaments and government bureaucracies appropriate disproportionately high shares of national income at the expense of the rest of the population. Corruption is inevitable when politics become the principal path to wealth. Poor education and health facilities result in the spread of HIV/AIDS. Years of fighting on Bougainville, political coups in Fiji, insurrection in the Solomon Islands and the chronic lawlessness in the Southern Highlands of Papua New Guinea point to a Pacific 'arc of instability'. The local populations, and particularly women, suffer the consequences.

Corruption, theft and assault have brought the private sector, and hence job creation, to a halt in Papua New Guinea and made life a misery in the towns. Crime is now spreading to the villages. Women are the most unfortunate victims. The situation in the Solomons Islands is worse. Other stagnating economies are heading in the same direction.

Welfare and statist policies dating back to colonial times bear the principal responsibility for economic failure in the Pacific. Their institutional manifestations (in the bureaucracy and trade unions) mean that they are constantly reinforced in public debates so that reforms toward a greater market orientation (such as the Morauta Government tried to introduce in Papua New Guinea) are sabotaged and ultimately defeated. Unless the Pacific states move strongly and rapidly toward market-oriented economic reforms, poverty will increase, standards of living will continue to stagnate and instability will worsen.

Mineral endowments and high aid flows have inadvertently contributed to the lack of growth in the Pacific by creating negative economic effects. These have to be countered by national and donor policies if they are not to swamp the economic environment. Mineral, timber and other resource rents have added to the distortions created by aid. Fungibility has deflected aid flows from productive investment to consumption and facilitated the corrupt accumulation of private fortunes by small elites. Aid flows have not been invested in development projects but dissipated in bloated public sectors.

Change can only come in the Pacific from Pacific initiatives. Any attempts at re-colonisation, or the introduction of more expatriates to the region, would only put off reform into the distant future. The Pacific states have significant numbers of well trained professionals, many of whom are either not able to work effectively in a corrupt environment or have emigrated because Pacific governments are not creating conditions for growth and development.

Australia can only help the Pacific by reforming its aid policies. It cannot rely on the international financial organisations. The IMF, the World Bank and the Asian Development Bank have failed to introduce conditionality that could make aid successful. On the contrary, they have added concessional loans to the aid spent on consumption and thus created unsustainable debt. Australia should work with the United States, following the recommendations of the US Congress' Meltzer Commission, to bring the international financial organisations under control by reducing their size and hence the damage they do to developing countries by creating indebtedness. A shift from multilateral to bilateral channels over which Australia has parliamentary oversight would increase the effectiveness of Australian aid.

A radical change in Australian aid policy toward the Pacific will require an understanding of the economic theory that explains why aid has been counterproductive.

Aid has to be linked to conditionality under the principle of mutual obligation.

Unfortunately, although disintegration in the Pacific is becoming a threat to Australia's security, and although continuing aid is likely to make it worse, radical policy changes will be difficult. Cutting aid has worked in the past (in Taiwan, South Korea, India and Chile); it would be the best solution, but it would be likely to be regarded as too harsh. A partial solution would link aid to conditionality under the principle of mutual obligation. This would require removing aid from Pacific budgets, with mutual agreement on its use, mutual monitoring, and disbursement only subject to audited accounts. But it would be pointless to continue even with strictly monitored and controlled aid if Pacific policies do not change. AusAID has to be empowered to have a strategic as well as operational capacity if it is to assess Pacific policies and take on the aid effectiveness tasks the international financial organisations have failed to carry out. AusAID, the Department of Foreign Affairs and Trade, the Department of Defence, and the Treasury have to start talking to each other in a meaningful way if Canberra is to catch up with what is happening in the Pacific.

Access to the Australian labour market to Pacific islanders, on the same terms as for other immigrants, is already developing directly and via New Zealand. To suggest that special exemptions should be made for unskilled (perhaps temporary workers) is the height of paternalism. People in the Pacific are just as able to acquire qualifications as those in other countries from which Australia receives immigrants. Such suggestions, moreover, ignore the high costs of such immigrant welfare ghettoes as have been created in Europe. They would not attract the migrants that Australia wants and would be of no service to the Pacific. Welfare recipients' remittances are not high and they do not return home with savings to start a business.

Low returns on Australian aid can be shrugged off. We can afford some $400 million annually to the Pacific to maintain political goodwill with developing countries. But our aid is damaging the Pacific. The time for a debate on aid reform is long overdue.

The Economic Theory of Aid

In economic terms, aid is a 'windfall', of unearned income, an 'economic rent'. Peter Bauer saw fungibility—that is the substitutability of capital—as the most counterproductive aspect of aid.[1] Fungibility enables governments to spend aid monies on their own objectives rather than on projects or programmes agreed with donors. Aid thus makes possible swollen political and bureaucratic establishments. Entrepreneurs are deflected from making money through business activities to earning public service and parliamentary salaries. Consumption takes the place of investment. Budgets are drained to enable large personal accounts to be accumulated by political leaders, bureaucrats, their crony contractors and expatriate helpers.

Bauer elaborated the insights of neo-classical economics and anticipated developments in the theory of rents and institutional economics to explain that even when aid projects and programmes have positive outcomes, aid has a negative impact overall.

Economic theory indicates that natural resource rents attract resources disproportionately to mining, timber and fishing rights. Resource rents lead to exchange rate appreciation, appropriately for mineral exports, but exchange rates become overvalued for import substitution and non-mineral exports. Investment becomes unprofitable in agriculture and manufacturing. Labour-intensive export industries fail to develop. Aid has similar effects. Because aid flows to governments, it attracts investment and employment to publicly owned enterprises.

Government ownership undermines the evolution of the institutions essential to growth and development. Clan loyalties characteristic of less developed societies do not lead to new 'internal' institutions, such as civil and business morality. Modern 'internal' institutions such as respect for the rights of the individual are essential to savings, entrepreneurship, investment and rising output and productivity. 'External' institutions such as police, legal systems and economic rules for the conduct of an economy have become clearly recognised as essential components of growth and development.

The expectation of aid, as of mineral incomes, discourages the build up of foreign reserves and encourages fiscal and monetary irresponsibility, with inadequate taxation, budget deficits and borrowing, leading to inflation and capital flight and so further undermining private investment. The large bureaucracies that implement aid are a dead weight on society, but support the parliamentary elites with whom they share the spoils. Waste and corruption at the top combine with low employment creation, leading to crime on the streets, so that business can not operate.

Import substitution and other regulations are used to offset appreciated exchange rates, increasing the regulatory role of government and further biasing the economy away from markets to the advantage of elites. Price controls and other regulations follow. They are maintained by aid long after their high costs, damage to employment creation and contribution to fiscal and balance of payments crises become evident. Regulations become the principal sources of patronage, intensifying the struggle for power, particularly in multi-ethnic communities.

Bauer already saw in the 1960s that aid organisations would not only retard development, but that, once entrenched, they would be very difficult to reform. If redistribution takes place when production and productivity are low, when there are only aid and resource rents to distribute, consumption levels for those benefiting from the rents become high, but the rest of society does not benefit. The Pacific economies illustrate the validity of Bauer's predictions and their elaboration in economic theory. The failure of aid (and resource incomes) to lead to growth thus does not arise from ill will, but from the failure to understand the economics of aid and resource rents and to devise appropriate policies to counter their negative effects.

[1] P. T. Bauer, 1966, Foreign Aid: An Instrument for Progress in B. Ward and P. T. Bauer, *Two Views on Aid to Developing Countries,* Institute of Economic Affairs, Occasional Paper 9, London.

Endnotes

1 *The Economist*, 15-21 February 2003, p.29.

2 The National Centre for Development Studies initiated a Pacific data bank in the 1970s so that economic and social indicators were regularly reported in the Centre's *Pacific Economic Bulletin* and available to governments and researchers. Since the responsibility for producing this data was moved to the Pacific Community in Noumea the data collection has collapsed. The attempt to give the Pacific ownership of this resource illustrates the pressures on AusAID to put politics ahead of performance. It was doomed to failure because the Secretariat of the Community does not have the depth of statistical and economic expertise to carry out the specialised work involved and thus could not assist national statistical offices of the Pacific to produce data of high quality. The return of the data work to the National Centre for Development Studies is urgently needed. The University of the South Pacific is putting together employment data for the Pacific and would be a suitable collaborator in the region.

3 Commonwealth of Australia, 1984, *Report of the Committee to Review the Australian Aid Programme,* AGPS, Canberra (Jackson Committee), Chapters 10 and 11.

4 J. Connell and J.P. Lea, 1993, *Planning the Future Melanesian Cities in 2010;* K.G. Gannicott and B. Avalos, 1994, *Women's Education and Economic Development in Melanesia,* J.B. Hardaker and E.M. Fleming, 1994, *Strategies for Melanesian Agriculture for 2010: Tough Choices*; J. Connell and J.P. Lea, *Urbanisation in Polynesia* , E.M. Fleming and J.B. Hardaker, *Strategies for Polynesian Agricultural Development;* M. W. Ward, *Women and Employment in Solomon Islands;* B. Thislethwaite and D. Davis, *A Sustainable Future for Melanesia? Natural Resources, Population and Development;* R.V. Cole, *Opportunities for Non-formal Education in Melanesia.* P.A. McGavin, *Labour Resource Utilisation in Melanesia* and R.V. Cole, *Pacific 2010: Challenging the Future,* Asia Pacific Press, National Centre for Development Studies, Australian National University, Canberra.

5 M. L. Treadgold, 1988, *Bounteous Bestowal: The Economic History of Norfolk Island*, Pacific Research Monograph, National Centre for Development Studies, Australian National University, Canberra.

6 'Least developed' status is conferred at a developing country's request if it meets an 'economic vulnerability index' that in effect signifies that it is an economically failed state. Of the 'least developed' states, 34 are in Africa, 8 are in Asia and 5 are in the Pacific. Members of the UN Committee for Development Planning that determined 'least developed status' used to wonder why countries would embarrass themselves by declaring they were failed economies. The principal reasons given to the Committee were that this enabled politicians and bureaucrats to travel to UN meetings at the UN's rather than a country's expense.

7 The manipulation of data is not confined to national statistical offices. UN Development Programme, 2002 and passim series, *The Human Development Report, 2002,* New York, presents a highly tendentious, politically motivated Human Development Index. I. Castles,1998, 'The Mismeasurement of Nations: A review essay on the United Nations Development Programme, Human Development Report 1998', *Population and Development Review,* 24(4), pp. 831-845, began a severe critique of the Index which is till ongoing but which has only been very partially taken into account by the Report's sponsors and authors. The Index and its components are, nevertheless, widely used for aid propaganda purposes. World Bank data on social expenditures, income distribution, unemployment and such items as 'access to improved water source', 'prevalence of undernourishment' and 'prevalence of smoking' are so subjective and vary so much definitionally from country to country, that they are highly misleading. In the Pacific they are only available for Papua New Guinea.

8 Asian Development Bank, 2003, *Millennium Development Goals in the Pacific: Relevance and Progress,* Manila, recognizes that '"poverty" is perceived to have connotations of hunger and destitution that do not properly reflect the nature of poverty in most of the communities' in the Pacific (p.7). This report, nevertheless quotes poverty levels of 65% in rural Marshall Islands (p.34), a range from 15 to 48% in Samoa (p.37) and 39% in Kiribati (p.20). AusAID's submission to the Senate Foreign Affairs, Defence and Trade References Committee on Australia's Relationship with Papua New Guinea and other Pacific Islands, 3 July 2002, p.4, claims 'that almost two million or over a third of PNG's population is living in poverty'. This is clearly a propaganda rather than an analytical evaluation.

9 World Bank, 2002, *World Development Indicators, 2002*, Washington, D.C., Table 2.13 p. 95 and Table 2.14. p. 99.

10 United Nations, 2001, *Papua New Guinea; Common Country Assesment,* Port Moresby, claims, without any supporting evidence, that Papua New Guinea grew by 3.3 per cent in real terms during 1985-2001, p.14. This is a typical collaboration between UN aid agencies and national statistical offices to persuade Papua New Guineans that their living standards are rising.

11 R.P.C. Brown and A. Walker, 1995, *Migrants and Their Remittances: Results of a Household Survey of Tongans and Western Samoans in Sydney*, Pacific Studies Monograph No.17, The University of New South Wales, Sydney, p.8.

12 D. A. Ahlburg, 1991,*Remittances and Their Impact: A Study of Tonga and Western Samoa*, Pacific Policy Paper 7, National Centre for Development Studies, Australian National University, Canberra.

13 *The Australian*, Breaking News, 11 March 2003.

14 N. Viviani, 1970, *Phosphate and Political Progress*, Australian National University Press, Canberra.

15 G. Bertram and R.F. Watters, 1985, 'The MIRAB economy in the South Pacific microstates', *Pacific Viewpoint* 26(3), pp. 497-520, dubbed these the 'Migration, Remittances and Aid' economies noting that remittances supported a large urban bureaucracy on the islands.

16 D. Scarr, 1990, *The History of the Pacific Islands: Kingdoms of the Reefs*, Macmillan, Melbourne.

17 R. Crocombe, 1989, *The South Pacific: An Introduction*, University of the South Pacific, Suva, is a prominent proponent of the idealised view of Pacific traditional societies. John Lodewijks on March 21, 2003, at the National Centre for Development Studies (Australian National University) – Macquarie University Pacific Update, strongly argued that Pacific islanders did not want to move from their traditional to modern societies.

18 G. Ward and A. Proctor, 1980, *South Pacific Agriculture: Choices and Constraints: South Pacific Agricultural Survey 1979;* L.T. Jones and P.A. McGavin, 2001, *Land Mobilisation in Papua New Guinea,* Asia Pacific Press, Australian National University, Canberra, discussed the failure of communal ownership to make land available for economic use, but so obfuscated the issues of communal ownership that they still failed to indicate how Papua New Guinea could move to private property rights.

19 S. Chand and R. Duncan, 1995, 'Resolving property issues as a pre-condition for growth: access to land in the Pacific islands', in P. Larmour (ed.) *The Governance of Common Property in the Pacific Region*, Pacific Policy Paper No. 19, National Centre for Development Studies, Australian National University, Canberra.

20 T.T. Kabutaulake, 2000, 'Rumble in the jungle: land, culture and (un)sustainable logging in Solomon Islands', in A. Hooper, (ed.), *Culture and Sustainable Development in the Pacific,* Asia Pacific Press, Canberra.

21 M. Pitts, 2002, *Crime, Corruption & Capacity in Papua New Guinea,* Asia Pacific Press, Canberra, is an excellent overview of violence in Papua New Guinea. All the Pacific islands are covered by P. Alpers and C. Twyford, 2003, *Small Arms in the Pacific,* Occasional Paper 8, Small Arms Survey, 21 March 2003, Geneva.

22 Alpers and Twyford, *Small Arms in the Pacific,* Summary, pp. xvi - xvii.

23 M. Pitts, *Crime, Corruption and Capacity*, p.9.

24 14 March 2003.

25 A. Sepheri and A. H. Akram-Lodhi, 2000, 'Fiji's economy: The challenge of the future', in A.H. Akram-Lodhi, (ed.), *Confronting Fiji Futures,* Asia Pacific Press, Canberra, pp.83-84.

26 E. Huffer and A. So'o, (eds.), 2000, *Governance in Samoa: Pulega I Samoa,* Asia Pacific Press, Australian National University, Canberra and Institute of Pacific Studies, University of the South Pacific, Suva, has many references to corruption in Samoa.

27 A. Downer, 'Neighbours cannot be recolonised', *The Australian*, 8 January 2003.

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