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Pacific Economic Policy–To Invest or to Protect?

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Introduction

Academics and international development agencies have expressed growing concern regarding the lack of economic growth in the Pacific islands and the economic policies employed by these countries. Even where there has been growth, it has usually been dependent on a few industries such as minerals, tourism, tuna, and forestry. This growth has been highly susceptible to externally imposed disturbances, and, in many cases, this growth has provided limited additional beneficial impact to the local economy.

The concern over policies in support of growth is the subject of the publications of Duncan (1994), Siwatibau (1994), and the "2010" research project of the Australian National University (1994). The international agencies have also contrasted the low growth with the high levels of aid, and the World Bank refers to this apparent contradiction as the "Pacific Paradox" (1993a). The South Pacific Forum turned the region's attention to policies in support of sustainable economic management in 1994.

This paper[1] is not concerned with proving or disproving the region's experience of economic growth. Rather, a better understanding of the nature of economic policy is of greater importance for the future of the region. Much has been analyzed and written by both aid agencies and academics concerning economic, especially macroeconomic, policy, but this paper argues that the means to economic growth must be grounded in deeper analysis. Previous analyses of economic policy have been incomplete in overlooking the prior need to correct the institutional practices and factor market distortions that otherwise prevent the achievement of the stated goals of economic policy.

In preparing this paper I have relied on my own experiences of researching and advising on policy issues in the region, including participation in a current study of the investment climate for the Pacific tuna industry, as well as the growing expanse of relevant literature. Producing generalizations on the economies of such a diverse region is never easy, but there are, alternatively, some commonalities that should be aired.

Sound macroeconomic policy?

If the broad goals of macroeconomic policy are economic stabilization and the generation of savings in support of investment and employment then it is, broadly, possible to question Duncan's (1994) opening comment that the economic policies of the Pacific islands are diametrically opposed to what are now widely recognized as the requirements for sound economic development.

While this comment is not far off the mark for some policies and countries under certain governments, many other efforts must also be noted. Some smaller governments, noticeably Kiribati and Tuvalu, have been especially fiscally prudent since independence, consistently foregoing consumption to save for future generations. In addition, many countries in the region retain hard foreign currencies as their medium of currency exchange, and while this practice limits the options for macroeconomic management it helps maintain relatively stable monetary environments. Moreover, with a few noticeable exceptions, few countries have placed policy restrictions on the movement of foreign currencies, goods, or peoples.[2]

As Browne (1995:1) states with respect to the 1980s: "The authorities in the Pacific islands have traditionally followed a conservative philosophy with regard to the implementation of macroeconomic policies. Combined with plentiful external aid, this approach has helped to preserve a stable financial environment, a sound balance of payments position, and an open trading regime. Exchange rates have been subjected to remarkably little fluctuation, and external debt problems have been avoided." The World Bank (1993a:2) also noted that the Bank's Pacific member countries: "have been more successful in achieving macroeconomic stability than in achieving growth."

Aid could be considered a key factor influencing sound macroeconomic policy. It is, however, important to note how aid influences both the domestic fiscal and the international trade accounts. In both cases because aid is commonly tied to goods and services and is not provided as cash, "fungibility" is extremely limited, and the debits and credits of aid cancel each other out. Budget and trade deficits are not so much a reason for, as a result of, aid. This situation does not, however, mean that aid does not import other longer-term costs that are apparent in the case of additional recurrent costs and expanded government activity.

The case for the existence of sound macroeconomic policy, however, must not be overstated. The international indebtedness of the Cook Islands and Papua New Guinea, the recent policy inconsistency of the Papua New Guinea government, the increased fiscal deficits of American Samoa, the Marshall Islands, and the Federated States of Micronesia, all prevent any such general argument. The case supporting a stable Pacific economic environment may also be faltering because, according to Browne (1995), some deterioration in macroeconomic performance has occurred in recent years.

But even where macroeconomic policy has been sound (or at least stable and conservative such as in Kiribati and Tuvalu), this situation has not commonly led to value added investment, trade, and growth. There must therefore be more at issue than the matter of sound macroeconomic policy alone. The policy equation should be further dissected. An environment that is supportive of economic growth does not, of course, solely consist of setting appropriate macroeconomic policies. Equally important, it also includes relevant microeconomic policies, including factor market policies, as well as the implementation of these policies.

A vested microeconomy?

In addition to some relatively sound macroeconomic policy, the region has also enjoyed a profusion of projects, programs, and other facilities implemented by aid donors and regional organizations that have been aimed at strengthening infrastructure, transportation, communications, trade, skills, health, education, development finance, and more: all in support of economic growth. But, despite all this assistance, economies commonly have not grown significantly, and in some instances they have stagnated.[3] As Duncan (1994) comments, there has been little "pay-off to aid," which is partly the result of microeconomic policy.

If the primary goal of microeconomic policy is the removal of domestic distortions in support of investment, employment, and improved welfare then, unlike macroeconomic policy, the region has been slow to endorse the "best" microeconomic practice. The operations of the domestic economy have been distorted by expansive government and the continued subsidization of public utilities and public enterprises by many island governments, continued subsidization of key services and staple commodities such as inter-island transportation and copra, uneconomic utility pricing, and the occasional tariff setting in favor of revenue generation. These distortions may have temporarily enhanced government employment and public sector and community welfare, but jobs and welfare have been achieved only at the cost of a climate that deters long-term private investment.

Hidden subsidies in the form of soft finance and underemployed government labor, low public sector labor productivity, and, in some cases, a lack of loan supervision and collection, hidden inter-public enterprise and inter-government credit, and a higher tolerance for tax arrears are further examples of a lack of financial discipline and poorly directed resources.

This level of government intervention has consistently favored the established interests of the traditional and government sectors at the expense of the emerging interests of the private business sector. Although the subject has been talked about for ten years or more, there remains a common requirement for both public and private enterprise reform that incorporates greater enterprise accountability whether in the form of private profit or public output.

Some of the required areas of reform could be undertaken by island governments with minimal additional external assistance from the respective professions. Moving toward a full cost user fees policy will help improve resource allocation. Adopting strategic output budgeting will, for the first time, enable policies and development strategies to be translated into policy-accountable budgetary practice, as the government of New Zealand has proved. The same budgetary system will make performance based staffing possible, which will greatly aid reforms of the public sector, public enterprises, and the labor market. Other areas of essential reform that would primarily support the private sector have, however, been strongly resisted.

Forgotten factor markets

In the case of the Pacific islands, the public sector microeconomic reforms that have been mooted thus far do not go far enough. Achieving economic growth is not just a matter of marshaling the standard macro- and microeconomic policy environment. Economic growth also relies on supplying domestic factors (land, labor, capital) at a price and in a condition that will allow domestic economic gain. This factor market component of microeconomic policy may have been commented on, but it has been greatly under-emphasized thus far in the recent debate on economic policy. As previously mentioned, the aid industry has funded and Pacific governments have implemented many infrastructure, transport, communications, education, health, development finance, and other supply-side support programs. The economic impact of these programs has fallen far short of intended results because the supplies of Pacific islands' land, labor, and capital remain protected and in some cases expensive and therefore uncompetitive.

Investment and trade are not only economic transactions; they are also important social and political transactions. As Hooper and James (1994) note, the connections between the government, the traditional, and the private sectors "also have clear social and cultural dimensions." Moreover, the domestic factors of production, (including complementary information, innovation, and entrepreneurship) and indigenous businesses are also subject to social and political valuation and influence.

While it could be argued that social and political influence over trade and investment is apparent throughout the world, it can also be argued that, in the Pacific, these non-economic demands can be much greater. My own studies of the environment and culture of small business management in Micronesia (1994, 1995) led me to conclude that, although in Micronesia as elsewhere, business culture needs to fit and adapt to a changing business and social environment; in the case of Micronesia the social influences of the greater community on business policy are much more pervasive. The continuing demands of the community influence the availability and pricing of domestic factors, commodities, commercial services, and business in general. In the Pacific this situation amounts to greater "reserve prices"[4] being placed on what are the essential requirements of the modern economy.

Let us examine the primary economic requirements in turn. First, land is commonly committed to the requirements of a partially subsistence economy with many complex, personal, traditional, and customary applications.[5] The complex nature of land tenure in the region has been extensively documented. However, what is less well analyzed is that, with some notable exceptions such as Fiji and Rarotonga in the Cook Islands, the lack of a market for either freehold and/or leasehold land in the islands greatly restricts the development of a domestic property market. The lack of a domestic property market, in turn, greatly curtails security for commercial credit. As a direct consequence, Pacific domestic commercial capital markets are commonly small, with excess capital exported and lost to the region's economies. While the export of excess capital from small, vulnerable economies must be expected, this excess could be reduced if a domestic capital market were to develop.

In effect, the reserve price for the second economic requirement, **commercial** capital, may therefore be considered to be high relative to other economies where land can be employed for collateral purposes. Some may argue that as a result of the level of aid, the region does not have a capital constraint. However, this capital is usually tied to particular use, it little circulates and multiplies internally, and it obviates the need to create a domestic capital market[6].

Third, labor is subject to the continuing requirements and support of subsistence, limiting availability and raising the price of labor to the non-subsistence economy. In some countries the expectations of remuneration are also reinforced by welfare payments, especially in the French and US-linked territories and countries. In the same, and other, countries wage expectations are greatly increased by a large and disproportionately remunerated government sector. While in still another group of countries the labor forces may also consider the opportunities for higher paid employment overseas. The reserve price for Pacific labor can therefore be high relative to what the economy, or at least certain sectors of the economy, can afford. Noticeable exceptions are the labor forces of the resource-poor atoll economies where migrants have long accepted relatively low paid unskilled, or lesser skilled, employment on other islands.[7] While the restrictions on labor availability and pricing may not be as extensive as land and capital, the phenomena may nevertheless be strong with respect to particular sectors or segments of the labor market. This is most especially the case with respect to a preference for employment in the public sector and, for unskilled labor, with respect to an aversion for employment in the private sector in some countries.

Last, in a number of countries indigenous business has been protected from foreign competition, more by practice than by tariff barriers, thereby driving up the reserve price of domestic commerce. For instance, in some Pacific island countries, foreign investment proposals are vetted for their potential competition with domestic business interests. The "price" of foreign investment may also be further distorted by political interests, e.g., by redirecting foreign investment in order to benefit a particular electorate.

Domestic factor markets and commerce are either undeveloped in the case of land and commercial capital or underdeveloped in the case of commerce. The domestic labor market may also be hampered by strong price preferences. The Pacific region's land, unskilled labor, capital, and commerce are also relatively expensive in comparison with the same factors from other regions. While undeveloped land and capital markets have constrained both macroeconomic and microeconomic objectives insofar as private savings, private investment, and privatization are concerned, this situation may be of little concern to the public sector that has benefited from stability, increased employment, and apparent "savings" in the form of high levels of aid.

Although a proportion of indigenous Pacific businesses succeed, these businesses remain predominantly small, isolated, and restricted by industry despite the protections from foreign investments (Pollard and Qalo 1994). Indigenous business success could be more widespread, but it is constrained by the lack of essential and competitively priced land, labor, and domestic commercial capital. Alternative aid supplied business skills, development finance, and industrial estates are inferior substitutes to their domestic counterparts in support of growth. These aid supplied alternatives have probably helped to greatly lessen and to postpone the pressure to develop domestic factor markets.

Although relatively high domestic reserve prices have deterred private sector investment, they have not depressed public sector investment.[8] In deterring private investment the absorption of new information, technology, and innovation, which can lead to further growth and investment, is also discouraged. Where investment has taken place it has tended to be short term. Foreign rather than domestic factors have often been preferred because of relative availability and prices. Pacific economies therefore stand to gain very little even when investment is attempted. The trade status of the region--where many countries continue primarily to be importers of commodities and exporters of capital and labor--is therefore likely to continue.

National development plans, strategies, and policies may have been thoroughly analyzed as Siwatibau (1994) suggests. However, the reason these plans are not adequately implemented is not solely because a commitment to declared goals is lacking as Siwatibau suggests but also because these plans are based on flawed assumptions. Such plans commonly assume a ready availability of transferable land, labor, capital, and services. Development plans assume any labor constraints would be overcome by education and training, and capital constraints would be overcome by development finance. As they stand, the plans typically do not reflect the true priorities and policies of both the leaders and the people who place high reserve prices on domestic factors and services. The plans' focus on sectors such as fisheries, tourism, education, health, and so on is also a politically neutral approach that overlooks the prior need to mobilize domestic factors and services if domestic economic growth is truly desired.

It should present no surprise that Pacific economies have grown little, given the high domestic reserve prices, the economic policies that favor the public and traditional sectors, and the economies based on foreign rents rather than resource investments. Non-commercial kinship obligations, values, and vested interests may also deter economic growth, but some kin and commercial interests are alternately intent on pursuing business and investment.

The lack of attention to factor pricing and mobility begs the question why this issue is overlooked. The reason may not amount to a gap in information but rather a preference for current tenure and distribution. Aid and foreign investment may also mask this preference. By implication therefore the same reserve pricing may imply a desire to avoid, or not to commit to, economic growth and the implications of growth, as embodied in national development plans.

Contrary institutional practices

Duncan (1994) correctly advises that stable economic policy is vital to investor confidence. Much of the work of the World Bank's Foreign Investment Advisory Service would also support this opinion. However, any apparent policy inconsistency may be indicative of not only a lack of political commitment to explicit policy but also a commitment to other preferred policies. As above, non-economic and vested economic demands may have a greater influence over trade, investment, and factor markets, and this influence may be manifested in institutional practice.

Even where declared policies should have supported investment and growth, the institutional environment has often prevented the realization of the benefits from policy implementation. As an example, possibly all Pacific island countries declare support for long-term foreign investment and have a number of policy instruments in the form of laws, taxes, and investment missions to attract it. But sound, sustained investment has commonly been deterred by institutional practice.

These other "institutional" deterrents include the lack of internal coordination within government, some lack of equitable law enforcement, approval processes that favor discretionary as opposed to open universal treatment, a preference in some countries for government rather than private investment, a concentration of decision making on hierarchy or consensus rather than delegation, and a preference for political over executive endorsement. The issuing of essential work permits and business licenses can also be subject to exacting regulations and interpretations.

Domestic investment is additionally curtailed in many close communities where, for example, relatives or other close associates as officers of a land registration entity, a business licensing bureau, and/or a national development bank, for example, may have difficulty in objectively appraising local registrations, licensing, and loan applications from known, influential domestic investors.

Not only are prospective investors generally deterred by contrary practices and protective pricing policies but also shorter-term exploitative undertakings are invited. The current investment environment alternately attracts short-term and exploitative logging, drift netting, mobile processing, and plant and equipment sales disguised as investment.

In such circumstances sound private investment is also unlikely to materialize even if sound economic policy were a condition for international aid. If the goal is economic growth then institutional reforms are not merely essential complements to economic reform (World Bank 1991:10), they are essential prerequisites.

Protection?

Institutional practices and the availability and pricing of land, labor, and capital may reveal some of the real development preferences of governments and peoples. In the Pacific these preferences lie more in protecting and maintaining the status quo than in risking domestic investment and change. The existing beneficiaries of the current factor and commercial regimes are also unlikely to support any change in this situation. If the region wants more economic growth, however, then to what extent should governments and peoples lessen this protection? Current development theory favors market deregulation, competition, and free trade. However, I suggest that reducing protection is more a matter of degree and measure and not one of extreme.

Encouragement of the private sector, complementary government investments in education and infrastructure, and stable governments have served other economies well, such as in South East and East Asia. But these priorities have not necessarily been supported by unfettered factor markets and free market practices conducive to investment.[9] Protection was also a feature in the development of the developed economies, and they continue to protect their agricultural, fisheries, and other industries. In lessening its protective stance the Pacific should examine development theory as well as observe what the new world traders' practice as opposed to what they preach. All societies and economies place some protection or "reserve prices" on their domestic factors. Why shouldn't the Pacific?

The new world trade order that will continue to emerge under the new World Trade Organization may help the large, developed, well diversified, and highly regulated economy that attracts investment both to market and to produce and that also has complex and well developed systems of protection for the consumer, employee, and producer.

The renewed emphasis on free trade is also most incomplete and misleading in that it neglects the context of policies and practices controlling domestic business and industry. While the more developed economies may have comprehensive regimes in place that control monopolies, cartels, and other restrictive practices, the Pacific islands generally do not. This arena can be just as protective as international trade is supposed to be free. Today's economies do not need protective tariffs to protect domestic industry. Will the developed economies allow the islands free and fair trade and investment? The developed economies may be comparatively well positioned to take advantage of freer trade, but does this situation present a level playing field for Pacific producers? As UNCTAD (1985:25) has commented: "In a small country with no free trade, industrial growth may be inefficient, however, with free trade a small country may experience no growth at all and may in fact deindustrialize." Protection and investment are not alternatives; they are complementary facets of growth.

It is important to note that whereas Asia, North America, and Europe may have long protected their industries, sometimes beyond their comparative international economic viability, the Pacific islands are protecting factors of production. There is an immense difference between protecting established industries and protecting factors of production, between protecting established economic activity and creating an economy.

Rents or resources?

If the region's overall development policy and practice is viewed as one that effectively protects the region's economic factors and interests, an alternative interpretation is placed on the MIRAB (migration, remittances, aid, and bureaucracy) development equation or theory of Bertram and Watters (1985). Rather than view the MIRAB economy as an economy where rents[10] predominate and where alternate domestic resource development is redundant, the MIRAB economy should be viewed as simply one that results from factor protection, factor export, and domestic private sector restraint, reinforced by aid and short-term foreign investment.

If economic management is focused on strengthening foreign rental earnings through remittances, overseas investments, licenses, and aid, the need may be obviated to mobilize and to risk domestic factors in raising incomes from greater national resource development. As is to be expected, the MIRAB experience has so far led to minimal national economic growth. Some in the international aid community are therefore recommending a re-examination, if not a reduction, of the "A" and "B" elements of MIRAB in the post-cold war era. Other donors, however, continue to support these elements.

Some island governments may indeed wish to lessen their economic dependence on aid and other foreign-sourced rents. Even if rentals could be strengthened through, for example, internationally invested trust funds and increased fish license fees, the resultant incomes that may help reinforce island welfare and cultural identity do not help economic independence and island *raison d'être* through domestic investment and new domestic economic activity.

It should also be recognized that the "rentier economies" have not necessarily avoided the creation of greater individual inequalities. For example, in the absence of land reform, informal land transfers are increasingly taking place in the region leading to more unequal distribution of land. The Federated States of Micronesia's second national development plan (FSM 1993:248) refers to "large tracts of land being aggregated by individual private owners" with an increasing proportion of the population existing on small, inaccessible, leased plots or being landless. Such transfers are made with little protection of the rights and responsibilities of parties to the transfer thus adding to the complexity and uncertainty of the market. Land reform is needed to provide a new legal, administrative, and economic framework that is both accepted and enforced and that protects all parties to formal transfers.

What reform?

The Pacific island leaders are confronted by a great challenge, that is, how to secure the desired social, cultural, and political identity and status quo and yet maintain, if not increase, the social and economic well-being of growing populations when confronted by stagnant if not declining economies. If the Pacific desires domestic investment and even modified economic growth, there may be no recourse save to lessen factor protection, revise reserve prices, and correct existing institutional practices. Complete removal of existing institutional protection is not politically feasible, and there may, as above, be little case for such an extreme.

The pressing issue is not so much which sector to prioritize, or which investment to promote, but how to optimize the involvement of domestic labor, land, capital, and indigenous business and how to tailor macro- and microeconomic and institutional policy in support of domestic gain. The alternative facing the governments of the region is that without investment economic growth will continue to be restrained, without economic growth very few jobs will be created, without jobs people will continue to vote where they can in the form of migration or, eventually, in favor of new policies and a change of government. And there is evidence of an increasing interest in alternative economic policies. A government commitment to the necessary reforms will become a more and more pressing issue in the region, and these reforms are more likely to become socially and politically painful the longer they are postponed.

A more complete framework for investment and economic reform is required. If the region's peoples and governments want some economic growth then the size and nature of this task must not be underestimated. Economic growth will require investment that leads to economic gain, and investment requires economic reform. Commitment to reform must be deep, comprehensive, substantially accepted by the community, and long term. The commitment must be deep enough to embody land reform and enterprise reform; comprehensive in its coverage of policy, institutional practice, factor availability, and pricing reforms; and understood and agreed upon by small, close communities.

Land reform may require repeating the kind of effort undertaken by Fiji's Ratu Sukuna who held extensive meetings with the community in the 1930s to convince the people of the wisdom of establishing the Native Land Trust Board. While this institution may now be outdated, the effort involved provides lessons for today. Enterprise (private as well as public) reform can be based on the efforts of successful indigenous private entrepreneurs as well as foreign investment. Enterprise reform also means increased competition for government operations, domestic business, and all vested interests.

There are a number of initiatives that the governments of the region could undertake that would support the required reforms, and these initiatives place little demand on outside assistance. In the case of land, the following actions would greatly facilitate land transfer and the creation of capital markets: simplifying legislation, improving survey, registering titles, conducting independent audit and appeal, and maintaining up-to-date records in support of a market in **leased** urban land. In the case of public sector reform, as previously mentioned, the adoption of "strategic output budgeting" can effectively translate the prevailing policies and development strategies into budgetary practice. The concentration of government investments in education, especially in support of specific skills, needs to be continued. New tax regimes, strengthened public investment planning, and general policy analyses are also still needed in many countries.

Many of these reforms are possible and already proved. Fiji has adopted a number of macroeconomic and microeconomic reforms. Kiribati, as other countries, has shown that investments in education can pay off. I-Kiribati have been trained as lawyers, pilots, economists, statisticians, accountants, doctors, nurses, and other professionals as well as professional administrators. Output budgeting is being adopted by the governments of Kiribati and Tuvalu. The Marshall Islands, Niue, and Tuvalu are also working on public sector reform.

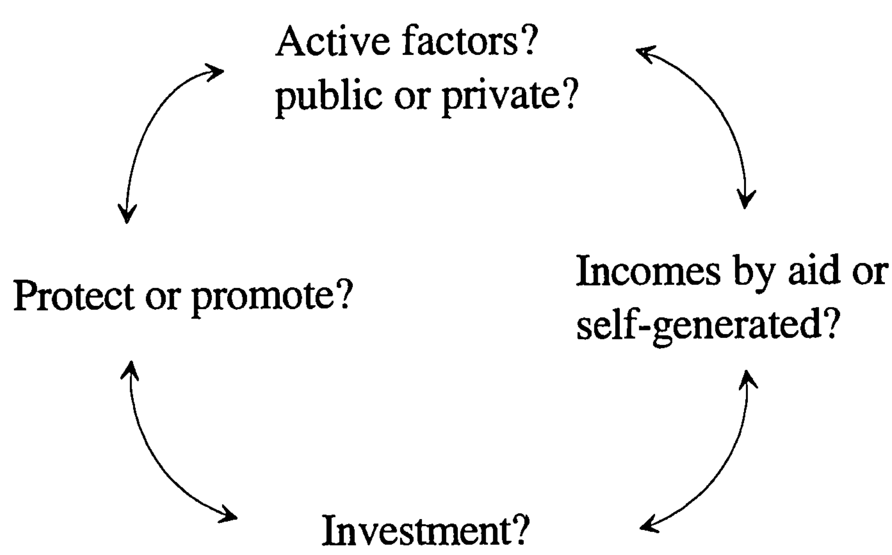
All these efforts are, however, incomplete, and if the experience of the so-called "transition" economies in central and eastern Europe provides any guidance then the factor and enterprise reforms under consideration are likely to be prolonged if not postponed. As Roland (1994) suggests with respect to Europe, where political constraints exist, the process of privatization will be slow and gradual. Beyond trade, fiscal, monetary, wage, price, and sector policies, the Pacific island governments need an investment policy that ties all other considerations of policy and practice together.

The aid programs of the Asian Development Bank, Australia, the European Union, and Japan may continue to spend in the Pacific islands while the United Kingdom, the United States, the World Bank, and others now lessen their presence or withdraw. Some donors may press for a more accountable, if not acceptable, policy framework while others continue to fund unsound ventures. Whatever the aid industry's vogue, whatever its conditionality, or whatever trade or economic pact may be promoted from without (Duncan 1994), the export of island labor and capital to rim countries and a corresponding import of commodities to the islands are likely to continue unless, on balance, investment is favored over protection. Aid has so far had limited influence over general economic policy and even less over institutional practice and domestic factor markets. Aid has alternatively helped island governments to maintain a policy of factor and commercial protection and factor export and to postpone the creation of an economy in support of domestic investment.

The international aid community should match the Pacific's commitment with professional assistance where required, much as this same community has been trying to assist the "transition" economies of Europe. Such assistance should be viewed as support for the barest form of economic protection, that is, strengthening economic management. But, at the same time, capital aid must be reformed to take full account of the recipients' economic structure, which includes factor pricing and institutional practices. Aid agencies must desist from displacing domestic private economic initiative. The latter type of aid is especially galling in the case of "commercial" fishing vessels and cold stores that continue to be donated for government use.

A pattern emerges

The paper's analysis might be best summarized in the form of the following simple investment circle.



At present the above "investment circle" is at best static; it may be contracting as economies and societies decline. The challenge is growth. If the Pacific islands are to create and sustain new activity then new income, primarily profit generating activities are needed. If profits are to be generated then private investment is essential. Long-term, value-added investment will, however, materialize only if the macroeconomic and microeconomic, institutional, and factor environments are all supportive. The present policy regime prevents the investment circle from growing. If even qualified economic growth is desired then the economic reforms so far proposed by academic and aid agencies are insufficient. Reforms of domestic factor markets and institutional practices are essential prerequisites to other economic reforms.

Some macroeconomic management has been sound, but this management has best served government stability, government employment, and incomes. It is in the areas of microeconomic management that governments have been less inclined to abide by proven international practice. A pattern emerges where vested interests prevail. It is really a matter of who gains and who loses from maintaining or altering the current economic impasse. Current policy and practice may favor traditional and governmental interests on the domestic front, and short-term exploitative investment on the international front. However, the private sector is unlikely to be happy with excess government activity, uncertain government regulation, and uncertain public utilities, as well as trying to compete with government wage levels.

A common element in the division of interests is aid. High levels of aid have reinforced government activity and traditional interests. High levels of aid have lessened the need for alternate private activity, and the same aid has greatly lessened, if not removed, the need to release domestic factors of production. But how can an economy be created, let alone grow, without land, labor, and capital? Factor protection comes at a great price, which is the curtailment of a growing economy.

On a regional level the governments and the aid industry are yet to confront the full gamut of reforms needed to support investment. However, at the level of each individual country a new pattern may be emerging. The atoll resource-poor and isolated country of Tuvalu, which has generally received less aid, or has been unable to use all aid on offer, is undertaking land, public sector, and other reforms to stimulate economic growth. At the same time the Federated States of Micronesia and the Marshall Islands, having largely spent their relatively huge independence gifts from the United States are now confronting fiscal crises. ADB funded economic reform programs in these countries may be a route to more fundamental reform. However, whether through crisis or aid neglect, the fundamental issue is that if factors are to move from traditional and governmental control to private sector use then a new power sharing will have to be accommodated. The past experiences and current undertakings of Tuvalu, the Federated States of Micronesia, and the Marshall Islands provide sobering thought for the peoples and leaders in the other island countries. But another important question remains: will donors support the required changes?

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Footnotes

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[1] I am indebted to many colleagues who have commented on and helped to improve this paper. I would particularly like to thank Chris Browne, Ray Clarke, Ron Crocombe, Julie Delforce, Jim Di Giambattista, John Howe, Michael Moriarity, Andrew Needs, and Garrey Wiseman. Any remaining errors are mine.

[2] The same countries, however, have placed other obstacles to trade and investment.

[3] As Browne (1995) comments, GDP per capita has barely risen in the IMF member Pacific island countries over the past decade, and GDP per capita has declined in Kiribati, the Marshall Islands, the Federated States of Micronesia, and Western Samoa. GNP per capita might be considered to be a better indicator of economic activity and well-being in the case of Pacific island economies where foreign rental incomes are important. However, based on the few countries for which reliable data are available, net factor income from abroad would appear to add little to economic well-being. According to the World Bank (1994) in the case of Fiji, Papua New Guinea, and Solomon Islands, net factor income from abroad was negative every year from 1972 to 1992. The additional contribution of net factor income to GNP in 1992 (latest available data) was also negligible in the case of Tonga (2% of GDP), Vanuatu (5%), and Western Samoa (2%).

[4] The "reserve price" is defined as the minimum price or level of combined material and non-material remuneration, at which a particular factor (land, labor, capital) will expect to be remunerated, or will be offered for formal employment, given the combined consideration of all perceived alternative employment opportunities and other social uses.

[5] As Crocombe (1994) notes: "The customary tenures in the Pacific at the time of contact with industrialized societies were designed for self-sufficient communities, producing most of their own needs, and of limited mobility. Such a situation is now rare anywhere in the Pacific."

[6] We could not advocate disenfranchisement from traditional lands given the scarcity of land, the historic and spiritual importance of land, and the history of land ownership in Hawaii and elsewhere. However, some market for **leased** land that defends the interests of both lessor and lessee would aid land transfer and capital development. Not all land need be initially included in any proposed reform; for example, governments may wish customary title to be

maintained in the case of rural land where subsistence remains an important economic alternative.

Examples are the employment of I-Kiribati and Tuvaluan labor in the Nauru phosphate industry and, further afield, in New Zealand through the aid funded worker contract scheme, the employment of labor from Wallis and Futuna in the New Caledonia nickel industry, and Micronesians in the tourism industries of Guam and the Commonwealth of the Northern Mariana Islands.

[8] Data on Gross Domestic Capital Formation (GDCF) are commonly not available for Pacific island economies. Where these data have been compiled, they are also rarely broken down into public and private sector investment. Such a breakdown is, however, available for Kiribati where between the years 1979 and 1988 private sector GDCF varied from A$400,000 to A$865,000 with no discernible trend, and general government and public enterprise GDCF combined varied from a low of A$4,362,000 to A$11,827,000.

[9] The World Bank (1993b) records the "protections" offered by the governments of East Asia in the development of their economies through, for example, tariff protection, industry subsidies, cheap labor, tax incentives, a heavy investment in primary and secondary education, and reward schemes for leading exporters.

[10] Here, the MIRAB use of the term rent is employed in its more traditional usage as the periodic payment for the hire or use of durable items such as land, capital equipment, and machinery and not as economic rent. Economic rent seeking behavior may, however, be encouraged in an economy where rents predominate and rental incomes are preferred.