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"Sustainable Development" in Pacific Micro-economies

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Summary — This paper argues that the central economic problem for a number of very small Pacific Island economies is the preservation and enhancement of their status as rentier societies, and the relatively high living standards (*vis-à-vis* other developing countries) which go with the status. The thrust of most development planning in the region, with its focus on "sustainable" expansion of productive activity, is misdirected in these small countries. It is not productive activity, but rent entitlements, which must be sustained and reproduced over time. Aid, philately, and migrant remittances are not merely supplements to local incomes; they are the foundations of the modern economy. Insofar as conventional "development projects" crowd out aid and remittance entitlements, their impact is immiserizing. Criticism is offered of a recent argument for returning to sustainable subsistence economies.

1. INTRODUCTION

Decolonization of the South Pacific in the last three decades has produced a swarm of small island economies with varying degrees of political sovereignty. Excluding Papua New Guinea with its three million people and Fiji with its 650,000, the region covered by the South Pacific Commission contains roughly 20 small "countries" with a combined population of 1.2 million people — an average of 60,000. The smallest sovereign independent states are Tuvalu with 8,400 people and Nauru with 7,300; below these in size come Niue (self-governing in free association to New Zealand) with about 3,000, and dependencies of Australia and New Zealand such as Norfolk Island (1,900) and Tokelau (1,700).[1]

Official discussion of development prospects in these small island economies has tended to be dominated by the view that self-reliance and sustainability are desirable policy goals, while "dependence" is both undesirable and incompatible with the first two. In this paper I argue that for several of the smallest economies of the region, "dependent development" is both sustainable, and preferable to a drive for self-reliance. The criteria widely used by governments and international agencies to appraise development performance appear misconceived in this setting. In addition, some recent Malthusian analyses of development prospects appear unduly pessimistic.[2]

The paper is based upon a recent study of five micro-economies: Cook Islands, Niue, Tokelau, Tuvalu, and Kiribati.[3] The main points of the argument can be summarized as follows.

(1) The colonial administrations long ago raised living standards in these micro-economies above the level which could be "sustained" on the basis of local subsistence-sector production.

(2) The key to rapid growth of consumption levels in these economies since 1945 has been the growth of migrant-labor remittances, government budgetary assistance, and other similar rent incomes, derived largely from the metropolitan economies. In Niue, Cook Islands, Tokelau and Tuvalu, commodity production for export has not functioned as a leading sector despite occasional local and shortlived booms in fruit or coconut products. In Kiribati, large-scale production of phosphates was a classic example of an export enclave until the deposits were exhausted in 1979. Current expansion in tuna fisheries also involves enclave structures, with Island governments collecting rents from foreign fishing vessels, but very little local participation.

(3) Capitalism as a system of production has no major role in these economies except where it is introduced as a deliberate act of social engineering by policymakers, with subsidies provided to ensure profitability. The dominant non-capitalist set of economic, social and cultural institutions constitute a "village mode of production" which retains the ability to reproduce itself on either a simple or an expanded scale, which has control over virtually all land resources, and

which accounts for most production of subsistence goods, export staples (except the large-scale industrial products phosphate and tuna) and cultural services (the "Pacific way of life"). One important partial exception is tourism in the Cook Islands, where both state-run and privately-owned commercial operations coexist with family and village enterprises, providing wage employment outside both village and government sectors.

(4) Alongside the village sector, and closely integrated with it, is a large government sector built up during the colonial era to supply modern services (health, education, transport, communications, public utilities) and supported in the post-colonial era very largely by subventions from the former colonial powers.

(5) Given that these economies are driven by rents rather than by income from productive export-oriented activities, the focus of analysis must be not on production constraints but on questions of incentives, rent-seeking behavior by households, and the political economy of aid bargaining. So-called "Dutch disease"[4] comes to the fore as an important part of the explanation for the weakness of commodity production and the "failure" of many conventionally conceived development plans in the region.

(6) The future sustainability of above-subsistence living standards, and the prospects for future increases in those living standards, hinge upon the durability of existing and future sources of rent income. Despite frequent claims and threats to the contrary, both budgetary support for local governments, and remittances from overseas migrants to island-resident households, appear to be reasonably secure for the foreseeable future — budgetary support because of the role of "aid" in the western alliance's strategic exclusion of the Soviet Union from the South Pacific; and remittances because in the South Pacific setting, migration involves not the dismembering of kin groups but their internationalization (or transnationalization). There are good reasons to anticipate that living standards in the very small island economies will remain broadly indexed to unskilled wage rates in the New Zealand, Australian and US economies.

(7) Under these circumstances, the "development" problem for planners and policymakers is not so much the promotion of modern, capitalist, tradable-goods-producing sectors within the island economies, as the question of how rent incomes should (a) be made more secure and predictable, and (b) be allocated among members of the island society, to determine the "mix" of economic activities. Since considerations of economic efficiency do not apply in the usual way, this "mix" will be that which aid donors and local authorities regard as socially desirable. It may appear ironic that the problems of administering affluence should thus come to the fore in economies which remain at relatively low absolute income levels. This is, however, the natural consequence of the fact that scarcity of natural resources has ceased to act as a binding constraint on levels of consumption in these small, very open economic systems. The relationship of most of these Pacific micro-economies to the metropolitan economies of the region is akin to that of a suburb, inhabited mainly by pensioners and bureaucrats, within one of those economies. Any attempts to treat the island micro-economies as autonomous units, separate from the regional economy into which they are inextricably linked, is likely to prove misdirected.

2. SOME BASIC DATA

In this section we shall summarize the findings of a recent study of trade, government budgets, and population movements in some of the very small South Pacific economies.[5] The purpose is to illustrate some of the points made in the preceding section, and to highlight long-run trends in these economies.

Our figures cover five small economies. Two of them (Tuvalu and Kiribati, formerly Britain's Gilbert and Ellice Islands Colony) are independent nation states, having gained that status in 1978 and 1979 respectively. Two more (Cook Islands and Niue) are self-governing in free association with New Zealand, having ceased to be directly-ruled New Zealand dependent territories in 1965 and 1974. The fifth (Tokelau) remains a dependent territory of New Zealand, run by an Administrator based in Wellington, although in practice a substantial devolution of authority has taken place.

All five lack fiscal or monetary autonomy. They belong to the currency areas of Australia (Tuvalu and Kiribati), New Zealand (Cook Islands and Niue) or Western Samoa (Tokelau), and have no monetary authorities, although Tokelau (and in the past the Cook Islands) mints souvenir coins for sale to collectors around the world. (Thus Tokelauan dollars, although they can be offered as legal tender, are produced as an export item, not a medium of exchange. Gresham's Law keeps them out of general circulation.) Island governments, whether nominally sovereign or not, depend for much of their revenues upon budgetary support from former or actual colonial powers. Their ability to

run budget deficits is restricted by donor-imposed cash limits, while any attempt to run budget surpluses leads merely to reduced levels of aid, since donors expect to see their money fully spent during each current period, and tend to reduce subsequent assistance by the full amount of any *ex post* local-government saving — a novel version of the paradox of thrift.

Nominal exchange rates are fixed exogenously by the values of the dominant currencies in use; traded goods prices are hence determined by prevailing prices in New Zealand, Australia and Western Samoa, adjusted for (generally high) transport costs.

The indigenous inhabitants of the three former or actual New Zealand dependencies have New Zealand citizenship and enjoy unrestricted access to the New Zealand labor market. Wage and salary rates in these economies, and the opportunity cost of labor used by the village economy, are thus indexed to the New Zealand real wage (with adjustment as appropriate for travel costs, probability of unemployment, etc). Kiribati and Tuvalu citizens do not have free access at present to any metropolitan economy, but labor migration to the Nauru phosphate diggings, and to work for international shipping lines, does provide some external reference point for local wage rates.

Tables 1–3 summarize the trends of the last 40 years in trade, government finance, and population.[6] Table 1, showing deflated values for per capita imports and commodity exports, reveals the widening gulf between the two (which should *not* be read as an *ex ante* Chenery–Strout "gap") since World War II. All five economies exhibit a "takeoff" of private consumption (the dominant component of import demand) at different times during the past four decades: Niue and the Cook Islands in the second half of the 1940s; the Gilbert and Ellice Islands (now Kiribati and Tuvalu) in the mid-1950s, and Tokelau in the mid-1960s. Between the early 1950s and the early 1980s, per capita imports more than doubled in the Cook Islands, more than trebled in Tokelau, and more than quintupled in Niue. The slowest growth of per capita imports — 40% over the 30 years from 1950 to 1984 — was exhibited by Kiribati, the phosphate export economy. This reflects both the enclave character of Banaba phosphate production, and the differences between UK and New Zealand colonial policy — especially the stronger New Zealand commitment to extend the metropolitan welfare state to its dependencies.

The process of transition from the old, export- and subsistence-led colonial order to the new import-led "mirab"[7] order was virtually completed by the mid-1970s in all five, and per capita import levels have been stable or even slightly declining during the late 1970s and early 1980s.

Only in Kiribati could it be claimed that export expansion led import demand during this period — and there the link was dramatically broken in 1979 by exhaustion of the Banaba phosphate reserves. Since then Kiribati has shared the characteristics of other resource-poor small-island economies. In 1982/83 the ratio of imports to commodity exports was five for the Cook Islands and Kiribati, six for Niue, nine for Tokelau, and 116 for Tuvalu. (Including stamps as an export brings the Tuvalu ratio down to 2.6; philatelic sales are a mainstay of the Tuvalu balance of payments.)

Table 1. *Per capita commodity trade data for five micro-economies deflated to 1982 values annual averages, $**

Period	Cook Islands Imports	Cook Islands Exports	Niue Imports	Niue Exports	Tokelau Imports	Tokelau Exports	Kiribati† Imports	Kiribati† Exports	Tuvalu Imports	Tuvalu Exports
1920–29	372	361	160	145	46‡	91‡	110§	271§	—	—
1930–39	201	199	140	119	n.a.	n.a.	111‖	366‖	—	—
1940–49	289	207	217	172	n.a.	n.a.	n.a.	n.a.	—	—
1950–59	598	352	832	203	42	58	239	266	—	—
1960–69	778	480	560	100	85	30	316	370	—	—
1970–79	1,411	362	910	129	242	59	335	643	323¶	21¶
1980–83	1,558	296	1,328	189	310	40	305	56	400	18

*$NZ for Cook Islands and Niue, $Aust for Kiribati and Tuvalu, $WS for Tokelau.
†Includes Ellice Islands (Tuvalu) to 1975.
‡1926 only.
§1925–29.
‖1930–36.
¶1976–79.

Table 2 shows the financing of local government budgets since the 1920s, bringing out clearly the very long-standing external supplementation of government finance in the New Zealand dependencies. From well back in the colonial era, government services in those economies have been provided in excess of the ability of the local economy to pay for them from its tax revenue, so that the present pattern does no more than maintain a status quo established deliberately by the present aid donors in the days of "colonization by the welfare state."

In contrast, Kiribati during the phosphate era often ran budgetary surpluses; in the 1980s however it has joined the others as an externally-financed government sector. Tuvalu from the outset in 1976 relied on external finance for more than half of expenditure.

impulse for local incomes over the long run (with the partial exception of Kiribati phosphates), rapidly-growing government sectors were characteristic of all five, and generated a substantial share of household incomes by the 1980s. During the last four decades, real government spending per capita has risen 5.7 times in the Cook Islands, nearly 20 times in Niue 13 times in Tokelau, and nearly three times in Kiribati. Clearly, government has been a "leading sector" in the growth of living standards in all these societies, and has accounted for the bulk of wage employment expansion in the Islands. (On a rough estimate, government employment is 40% of cash employment in the Cook Islands, 90% in Tokelau, 80% in Niue and 53% in Tuvalu, if the Philatelic Bureau is excluded from the government sector in Tuvalu. Data for Kiribati were not to hand.)

Table 2. *Per capita government finance data annual averages, deflated to 1982 dollars*

Period	Cook Islands Total Spending	Cook Islands Local Revenue	Niue Total Spending	Niue Local Revenue	Tokelau Total Spending	Tokelau Local Revenue	Kiribati* Total Spending	Kiribati* Local Revenue	Tuvalu Total Spending	Tuvalu Local Revenue
1920–29	99†	54†	46	47	19‡	31‡	38§	48§	—	—
1930–39	117	76	117	114	n.a.	n.a.	51‖	50‖	—	—
1940–49	190	98	137	81	n.a.	n.a.	142¶	94¶	—	—
1950–59	519	258	548	252	125	30	127	115	—	—
1960–69	859	399	1,261	576	271	41	233	207	—	—
1970–79	938	483	2,318	1,060	1,120	84	401	441	587**	244**
1980–83	1,070	676	2,694	924	1,683	282	387	145	826	353

*Including Ellice Islands (Tuvalu) to 1975.
†1927–29.
‡1926 only.
§1925–29.
‖1930–36.
¶1947–49.
**1976–79.

It needs to be emphasized that the bulk of government budgets are spent on wages and salaries for the provision of modern services to the population, so that the expenditure of external budgetary assitance generates two rounds of living-standards boosts in the islands — government services in the first round, and private consumption out of cash income in the second round. The rising level of imports shown in Table 1 is, thus, only half the story in terms of real standards of living in the island societies.

Comparing Table 2 with Table 1, it is immediately apparent that whereas the export sectors in our five economies provided little or no growth

Table 3 shows, insofar as is possible, the growth and geographical distribution of the population of each of the five islands communities during the past half-century. It will be noted that the three economies with unrestricted access for migrant workers into a major metropolitan economy — Cook Islands, Niue, and Tokelau — all exhibited a surge of movement to New Zealand during the 1960s and early 1970s, to a point where a new steady-state distribution of island-born population seems to have emerged by the mid-1980s, with net migration converging to the rate of natural increase in the Islands. This conclusion needs some qualification in the case of

Table 3. *Islands-born population by place of residence*

Year	Cook Islands In Cook Is.	Cook Islands In N.Z. %	Cook Islands Total	Niue In Niue	Niue In N.Z. %	Niue Total	Tokelau In Tokelau	Tokelau In N.Z. %	Tokelau Total	Year	Kiribati In Kiribati	Kiribati Overseas %	Kiribati Total	Tuvalu In Tuvalu	Tuvalu Overseas %	Tuvalu Total
1936	11,943	157	12,100	4,105	54	4,159	1,170	0	1,170	1931	n.a.	n.a.	n.a.	3,994	95	4,089
		1			*1*			*0*							*2*	
1945	13,574	393	13,967	4,253	222	4,475	1,388	0	1,388	1947	31,513	n.a.	n.a.	4,487	579	5,066
		3			*5*			*0*							*11*	
1951	14,757	999	15,756	4,553	330	4,883	1,571	10	1,581	1963	43,336	n.a.	n.a.	5,444	1,319	6,763
		6			*7*			*0.6*							*20*	
1956	17,054	1,992	19,046	4,707	753	5,460	1,619	7	1,626	1968	47,682	1,404	49,086	5,782	1,683	7,465
		10			*14*			*0.4*				*3*			*23*	
1961	18,378	3,374	21,752	4,868	1,414	6,282	1,860	23	1,883	1973	51,784	1,765	53,549	5,887	1,807	7,694
		16			*23*			*1*				*3*			*23*	
1966	19,251	5,838	25,089	5,194	2,014	7,208	1,900	248	2,148	1979	56,213	2,299	58,512	7,349	1,303	8,652
		23			*28*			*12*				*4*			*15*	
1971	21,317	7,389	28,706	4,990	2,912	7,902	1,655	950	2,605							
		26			*37*			*36*								
1976	18,112	12,156	30,268	3,843	4,379	8,222	1,575	1,212	2,787							
		40			*53*			*43*								
1981	17,695	13,848	31,543	3,278	5,091	8,369	1,572	1,281	2,853							
		44			*61*			*45*								

Italic figures = percentages

Niue, where depopulation of the "back villages" appears to be continuing and may have proceeded to the point where some of those communities cease to be viable entities.

The two societies with restricted migration outlets — Kiribati and Tuvalu — have distinctively lower overseas-resident shares of *de jure* population: 3–4% in Kiribati, and 15–20% in Tuvalu, in contrast to 44% for the Cook Islands, 45% for Tokelau, and 61% for Niue. The sharp reduction in overseas-resident population in Tuvalu between 1973 and 1979 was due to the repatriation of large numbers of Tuvaluans formerly employed in Tarawa by the government of the Gilbert and Ellice Islands Colony, whose employment terminated with the splitting-up of the Colony. Currently, overseas employment opportunities for Kiribati and Tuvalu are limited virtually to Nauru phosphate employment and international shipping lines.

Table 4 draws together some very rough balance-of-payments estimates to emphasize the emergence over the past three or four decades of an economic structure driven by overseas-derived rent incomes: budgetary support grants, labor remittances, philatelic sales, and tourism. Of these, only the last (and that only in the Cook Islands) has any major tendency to generate backward linkages, and hence "modern-sector" employment, in the island economies.

In reading Table 4, it may be helpful to keep in mind the identity which underlies the structure of the table:

$$M - X \equiv T - I$$

where M is commodity imports
X is commodity exports
T is invisible exports plus net current transfers from abroad
I is net investment overseas.

This makes it plain that any increase in T (net invisibles and transfers) must be matched by some combination of falling commodity exports, rising imports, and capital outflows. As our discussion above has indicated, most of the adjustment in our case-study economies occurred by means of rising imports, with exports fairly static and capital exports providing a balancing item.

3. MODELLING THE DEVELOPMENT OPTIONS

In this section we argue that the important policy choices open to planners in small island economies have to do with the structure of incentives, and hence with the shape of the future society, rather than with the issue of whether or not "development" is "sustainable." We shall take it for granted that rent income will continue to provide the motor for these economies, and shall defer to the final section of the paper the issue of what policymakers can do to ensure the persistence of those income flows.

Our model is a simple one, derived both from a long tradition in development economics,[8] and from the recent debate on "Dutch disease" in rent-led economies.[9] In Figure 1, the total economically-active community of an island economy is shown along the horizontal axis, in units of available labor time. The left-hand vertical axis shows real wage levels, measured in terms of some representative bundle of incentive goods.

Since the labor market is open, the prevailing wage rate is set exogenously at the "world wage", W^* (the expected earnings from the export of a unit of migrant labor to the main migration outlet for the society, adjusted for the costs of migrating including psychological costs). (In other words, the local wage must suffice to "hold" footloose labor, by at least matching the subjectively-perceived external opportunity wage.) For present purposes we assume that W^* is substantially above the "cultural subsistence" level of income, which we denote W_1; and that the usual small-country assumption can be made with regard to the world wage (i.e. W^* is invariant with respect to the volume of out-migration from the island economy). The latter assumption will clearly need to be relaxed when we turn to the specific cases of Kiribati and Tuvalu, but is appropriate for the fully-open economies of the Cook Islands, Niue and Tokelau.

In part A of Figure 1 the village sector's labor absorption is determined by the intersection of the curve L_s with the world wage W^*. L_s shows the aggregate labor absorption behavior of the village economy, and may be read from either origin. Read from O, it shows the supply curve of labor for non-village employment, assuming that there exists no pool of "free" labor outside the village mode of production. Read from O', L_s shows the village economy's "demand" for labor — that is, its readiness/ability to absorb or release labor at various levels of the real wage.

The shape of the L_s curve reflects several features of the village mode of production. The long flat segment at wage rate W_1 shows the level of "cultural subsistence" at which the village economy can and will support its members in case of economic involution, with the loss of alternative income-earning opportunities. The diagram as drawn gives only slight weight to

Table 4. *Some balance-of-payments estimates: Annual averages ($000 at 1982 prices)*

	Commodity exports	−	Commodity imports	+	Philatelic and tourism	+	Aid	+	Remittances	=	Residual balance
Cook Islands											
1970–74	8,638		20,524		—		12,694		3,371		+4,179
1975–79	5,413		32,345		6,000		12,798		3,923		−4,211
1980–83	5,199		27,346		8,530		10,295		4,000		+678
Niue											
1970–74	608		3,172		—		4,700		50?		+2,186
1975–79	483		4,302		150		6,106		100?		+2,537
1980–83	568		3,984		300		5,353		300		+2,537
Kiribati											
1970–74	31,213		15,739		n.a.		n.a.		n.a.		n.a.
1975–79	35,581		18,712		1,000?		4,000		1,000		+22,069
1980–83	3,446		14,879		1,000		11,000		2,000		+2,567
Tokelau											
1970–74	85		363*		nil		270†		8		‡
1975–79	104		410*		40		236†		30?		‡
1980–83	63		490*		100+		227†		100??		‡
Tuvalu											
1979–82	124		3,021		1,500		3,500+		600		+2,703

*Store goods only.
†Calculated as a residual.
‡See note †.

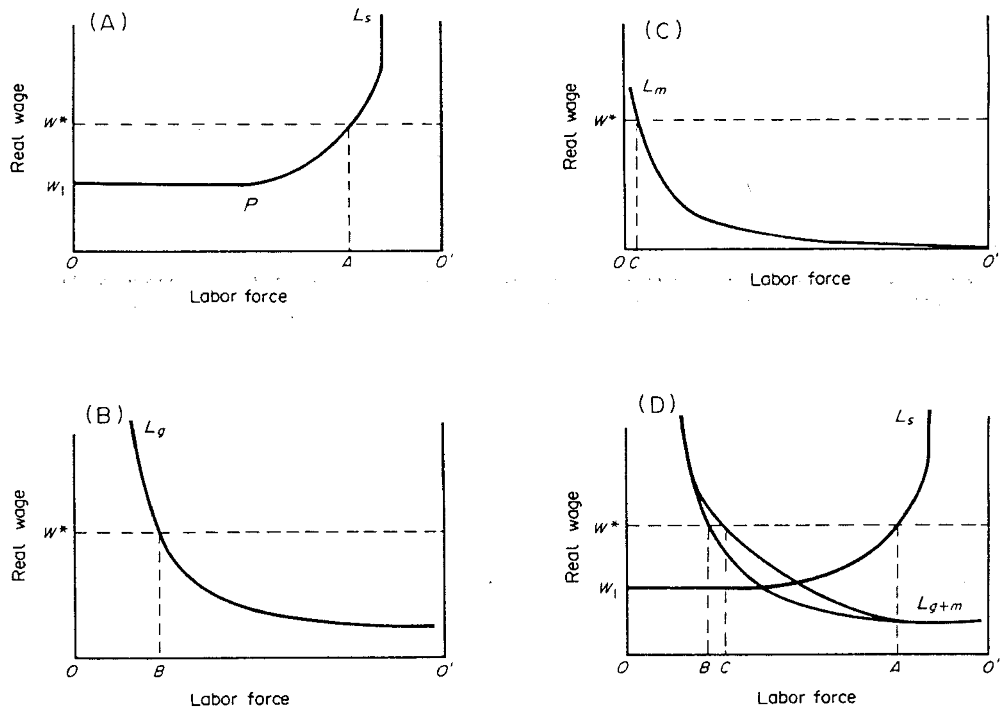

Figure 1.

diminishing returns in the village sector over the relevant range, reflecting our view that "subsistence affluence" remains attainable in all the economies covered by this paper. To the right of point P the curve turns upward, its convexity with respect to O' reflecting the diminishing marginal rate of substitution between imported goods and village products (including, of course, village "lifestyle" which is embodied in a package of village-produced goods and services). At some point the L_s curve turns vertical, since there is an irreducible minimum labor force which must be kept committed to the village mode of production (and hence must be withheld by households from recruitment into other sectors) if the village mode itself is to be reproduced. This upper section of L_s, obviously, would shift to the right if households ceased to value their neo-traditional culture and lifestyle and allowed preferences to swing towards imported goods and culture.

In Figure 1B, the size of the government sector is determined by the intersection of the curve L_g with the world wage W^*. L_g is drawn from origin O, and is a unit-elastic labor demand curve, reflecting the fact that island governments operate on budgets which are exogenously fixed in cash terms by aid donors, so that there is a one-for-one tradeoff between the government wage/salary rate and the number of employees.

Figure 1C introduces the demand for labor by a capitalist "modern sector" producing goods and/or services for profit. For a number of reasons, familiar from any commentary on economic prospects in the small island economies, we draw L_m to show a very small amount of modern-sector employment at the world wage W^*, and a significant increase in the size of the capitalist sector's labor demand only at very low real wage levels. The diagram as drawn would suggest that a major capitalist transformation of the economy would be profitable only at real wage levels equal to or less than the "cultural subsistence" level — which boils down to saying that capitalism would be a viable option only if the village economy were destroyed (e.g. by loss of its control over productive resources) or swamped by population growth to the point where it could no longer guarantee subsistence.

The position of L_m, however, besides being conjectural for wage rates below the existing rate W^*, is sensitive to government policies on the subsidization of tradable-goods production. As already noted, several modern-type ventures have been established and have survived for

some time under an umbrella of government promotion and subsidy, and it must therefore be recognized that aid donors could, if they were prepared to commit the necessary resources and exercise strong control over their use, pay subsidies sufficient to create and artificially sustain a large capitalist sector, probably at the expense of the village economy.

Figure 1D combines the foregoing points into a single diagram. L_s, L_g, and W^* are as before, while L_m is added on horizontally to L_g to give the total non-village local-economy demand curve L_{g+m}. The allocation of labor to which the economy then tends will be OB in government, BC in the capitalist modern sector, $O'A$ in the village mode, and AC employed overseas.

Although our diagram is a comparative-static construction and relies upon the existence of equilibrating mechanisms to deliver its results, it is nevertheless quite helpful in dealing with some dynamic issues. At a given world wage W^*, and with given government budgets and reproductive requirements for the village mode, the model predicts that any natural increase in total population will tend to be exported so long as outlets are open, but that migration will not result in actual depopulation of the island society (since local labor absorption $OB + BC + O'A$ remains the same). This appears to correspond reasonably with the current situation in the Cook Islands and Tokelau, where the surge of migration between 1965 and 1975 has given way to something resembling a steady state. In Niue, where a traditionally factionalized and divided society has shown signs of cultural disintegration in the last decade, the continuing depopulation (see Table 3) has followed from abandonment of the attempt to continue the reproduction of the village mode in several villages on the island. Indeed, events in Niue since 1970 could be said to have consisted of the departure of everyone except the civil service and their families (who of course continue to produce their own subsistence on village lands). (L_s in Niue, in other words, has been drifting rightwards.)

In Tuvalu and Kiribati, which do not face infinitely-elastic world demand curves for their labor, attempts to increase out-migration result in downward pressure on W^*, as does the closure of previously-open migration outlets which force the return of migrants. The most dramatic recent example of the latter process was the repatriation of Tuvaluan civil servants from Tarawa following the breakup of the Gilbert and Ellice Islands Colony in 1976, aggravated subsequently by the return of workers from the phosphate industries of Banaba after 1979, and Nauru in the 1980s. In order to absorb these people into the Tuvaluan government and village sectors, a considerable downward shift of the real wage has been evident, especially since 1980. Population growth in such societies, in the absence of widening migration opportunities, will tend to force them steadily into the low-wage category, and in Kiribati's case may even push the local economy back to cultural subsistence, unless an expanding government sector or a massive program of producer subsidies can be financed.[10]

Since there are no major activities generating large economic surpluses onshore in the Islands, and since any financial savings by the local population tend to be exported back to banks in New Zealand, Australia and Western Samoa, there are no grounds to expect the L_m curve to shift autonomously out to the right over time, as occurs in Lewis-type models of economic growth.[11] Absolute living standards in the Islands move closely with the world wage and the volume of rent income flowing in from abroad. Rising living standards thus reflect not an endogenous growth process, but an expansion of the rent-yielding niches which Island households have succeeded in colonizing elsewhere in the Pacific Basin — including, of course, their continuing claim upon the exchequers of the former or actual colonial powers.

Under these circumstances, the structure of the island economy modeled in Figure 1D will be determined by the interplay of four elements:

(1) The level of the world wage, W^* — i.e. the extent to which, and terms on which, the local society has access to overseas employment opportunities.

(2) The size of income from abroad (export earnings, "aid" flows, remittances, philatelic revenues, dividends from foreign securities, etc.).

(3) The composition of the flow of income from abroad — in particular, its breakdown between incomes accruing directly to the village economy (export sales, remittances) and those accruing in the first instance to government ("aid", philatelic revenues, dividends on overseas reserves).

(4) The extent to which the cultural and economic vitality of the village mode of production is sustained or augmented (i.e. the position of L_s).

All of these are to some extent policy variables, both for policymakers within the Islands, and for policymakers in the main aid-donor countries. The central problem is to specify an agreed "target society" towards which policy should aim, and then to adjust the settings in Figure 1 as appropriate. Some possible scenarios are as follows.

(a) *Modernization model*

Suppose that it is desired to create a capitalist economy, with the government and the village reduced to subsidiary roles if any. The required policy package would then be one which raised L_m while moving L_g to the left and L_s to the right. One way of doing this would be to target aid flows into profit subsidies for modern-type enterprises (excluding village households unless these transform themselves into the planners' vision of modern enterprise), while cutting back on direct budgetary support for the local government sector. Where key resources remain in the hands of village households, some form of expropriation might be required to free these resources up for the new capitalist ventures. Considerable social disruption would be an inevitable accompaniment of such a program of capitalist transformation, and the suggested reduction of the government sector might prove impossible if the breakdown of traditional mechanisms of social control made necessary an increase in government spending on law and order.

Under Pacific Island micro-economy conditions, such an exercise would be unlikely to trigger off a self-sustaining capitalist growth process; and the long-run outcome would probably be a fully-monetized but severely demoralized and de-cultured society lacking even the residual capacity to assure its own subsistence by involution.[12] The attractions of out-migration to other, still-vital, culture centers would then increase, and it would become increasingly difficult to hold the indigenous labor force in its homeland. At the same time the objections to bringing in cheap (e.g. indentured) labor from elsewhere in the region would tend to fall.

Despite the high risks, high cost, and low probability of long-run "sustainability," this model of development continues to exercise a considerable hold over the imagination of development planners in the Pacific area, especially those associated with major international aid organizations. The analysis in the present paper suggests, however, that an externally-imposed "capitalist road" will prove a burdensome and expensive *cul-de-sac* for donors as well as islanders, and should not be pursued. Dualist development models are a poor guide for policy in the region.

(b) *Informal-sector promotion*

Alternatively, planners might opt for the Pacific equivalent of an "informal-sector-promoting" development process, with various types of subsidies channelled directly into the village economy with the aim of shifting L_s to the left and attracting labor back into a vital, expanded village sector. The key policy instrument would have to be income supplements to people active in the village economy. Examples of such supplements would be producer price supports, input subsidies for staples produced in the village sector, and increased allocations of funds to village (as distinct from central government) authorities to finance village projects (whether investment, such as reef passages or water reticulation, or recurrent, such as traditional education).

(It may be worth recalling at this point that nominal exchange rate changes are not available as a policy option in these economies, because of their inclusion in wider currency areas. The object of policies such as those outlined in the preceding paragraph is to alter the real exchange rate in favor of the village economy, without altering the nominal rate.)

If a reduction in the existing government sector were felt to be desirable or acceptable, then part of the existing government budget could be reallocated to subsidizing the village sector, thereby shifting both L_g and L_s to the left at the same time.

The case for such a strategic reorientation by planners seems fairly strong in micro-economies of the type considered here, and particularly in the New Zealand-linked economies, where the government sector has expanded to the point of rapidly diminishing marginal returns. The social and political advantages of a strong, prosperous village sector are obvious enough in an era when local self-government is being promoted, and when the maintenance and enhancement of neo-traditional Polynesian culture is viewed as a long-run policy goal. To these elements we should add the economic argument, familiar from other economies affected by "Dutch disease," for artificially sustaining local productive activities, even when these appear uncompetitive in the immediate term, in order to provide insurance for the long run. The capacity of these societies to involute back to cultural subsistence under pressure of a breakdown in their cash incomes depends upon the maintenance of the institutions and practices of the village mode of production.

A further element in the argument for subsidizing the village has to do with nutrition and health. The effects of a switch from local staples to imported foodstuffs such as rice, canned meat and sugar are well documented, and there seem to be strong public-health grounds for

providing incentives favoring dietary preferences for the local foodstuffs.

The costs of such a policy, obviously, will be affected by the level of W^* and the openness of migration outlets in the long run. In the New Zealand-linked societies which have already adjusted to a steady-state position consistent with unrestricted migration, the L_s curve is probably very steep over the relevant range, and a village-promoting policy thus has a firm basis on which to build even in the open-economy context. In Tuvalu and Kiribati, where W^* is only slightly above W_1 and where the world demand curve for their labor slopes down, a policy which subsidized village activity might, if it coincided with the opening-up of more migration outlets,[13] serve more to mitigate the migration squeeze on the village economy than to produce an actual expansion of its size. Opening up the labor market for these societies would have the effect of pushing their living standards up; subsidizing the village sector would ensure that the society which emerged following the living-standards adjustment continued to be organized predominantly in the village mode.

It would not be realistic in this case to expect an expanded staples-exporting village mode to be economically self-supporting without continued subsidies; the idea that an escape from "aid dependence" can be engineered by economic growth in the village is a recurrent dream of aid planners, but is in no sense a necessary or expected outcome of the economic strategy discussed here.

(c) *State capitalism*

A third option for planners could be to favor the expansion of the state sector to effect a socialist or social-democratic transformation of local society. Such a process has in fact already occurred to a considerable extent in our five case studies, especially the New Zealand-linked ones, over recent decades. The main obstacle to its further progress is the difficulty of identifying credible, socially-rewarding activities for the civil service to undertake. It is, however, conceivable that the state might move into additional tradables production on its own account, on a non-profit basis, as a means of ensuring employment opportunities for growing populations. Such a state-employment-led model would be the probable outcome of a "more-of-the-same" orientation by present aid donors. Merely pouring more money into local government tends to increase the bureaucratization of Island society, and may threaten the viability of the village mode as (a) government employees intrude into the functions traditionally performed by village institutions, and (b) a growing proportion of local cash incomes accrue to village households from outside sources not subject to the redistributive mechanisms of neo-traditional village society (which implies increasing dispersion of incomes in the village, and possible breakdown of social solidarity). Such developments have recently caused a major reappraisal of New Zealand policies following the rapid expansion of the Tokelau Public Service between 1965 and 1980.[14]

(d) *Involution to subsistence*

Finally, planners might opt for a long-run target of self-sufficiency, as recommended by, for example, Tisdell and Fairbairn.[15] This would involve phasing out external budgetary support, cutting back the government sector to what could be supported from local tax revenues, and initiating a process of driving down the real wage towards the level W_1 in the hope that population growth would be damped and cultural subsistence assured. A major effort would be required also to shift local tastes away from imported goods and services, towards the traditional local substitutes produced within the village economy.

There are three major problems confronting such a strategy. In the first place, the political pressures arising from falling living standards would almost inevitably feed back to a recovery of aid flows, which would then have to be spent in some way (although hoarding or overseas investment might siphon off these inflows). In the second place, if migration outlets were open, the remittance economy could not be eliminated; the falling local real wage would simply drive all members of productive age groups abroad, leaving the village populated by the old and the young, living from remittances. A closed labor market would thus be a necessary condition if the strategy were aiming to produce a fully integrated self-sufficient village economy. In the third place, the required reversal of present trends in consumer tastes would not be easy to achieve on any sort of voluntary basis, while compulsion would be hard to justify in the absence of an actual (as distinct from merely foreshadowed) collapse of rent incomes from abroad.

Having assessed the four options outlined above, we would suggest that the second offers the greatest rewards for policymakers over the long run. This assessment assumes that real levels of aid flows will continue or increase, so that the achievements already wrought by the welfare

state in Pacific Island society will not need to be sacrificed. The parasitic over-expansion of government bureaucracies, however, will have to be confronted. The onus is on aid donors to design their programs in ways which channel increasing flows of recurrent income to village activities rather than to public service salaries. Familar techniques such as price supports and input subsidies seem appropriate; societies as marginal to world prices as the Pacific Islands can probably defend the replication, for social reasons, of the type of measures which characterize the EEC's Common Agricultural Policy, but which have acquired rather a bad name internationally as a result of that policy's impact on world markets.

4. UNDERPINNING RENTIER STATUS

An important implication of the analysis in this paper is that conventional notions of what constitutes economic development cannot be applied to the very small island economies of the Pacific. Ricardo's aversion to rentiers and Marx's preference for productive over unproductive labor, both inherited as strong prejudices of modern development economics, are inappropriate tools for analyzing these societies in isolation. In discussions of the Pacific *regional* economy, of which these small island societies form tiny satellite units, these ideas would come back into their own. The "modern," capitalist sector of the Cook Islands economy, for example, is located in New Zealand, not in the Islands — and a large proportion of the active labor force of Cook Islanders is employed in that sector. The links between the capitalist and the non-capitalist sectors are provided both by transfers to the Cook Islands Government through the New Zealand Government budget, and by remittance transfers among various component parts of the "transnational corporations of kin" which direct the allocation of each island family's labor around the regional economy.

The status quo, on which the future living standards and lifestyle of the island societies are to be constructed, provides a firm foundation provided only that the entitlement of island communities to rent incomes remains solid. This in turn requires that two conditions be met. The first is that labor access to the modern capitalist economies of the region continues (in the case of the New Zealand-linked territories) or is opened up (in, e.g., the cases of Tuvalu and Kiribati). The second is the continuing willingness of the major regional powers (Australia, New Zealand, the United Kingdom, the United States — and of course, in its territories, France) to subsidize consumption levels in the small Island countries. Both of these conditions hinge upon the long-run political commitment of the metropolitan governments to the welfare of island communities.

The biggest long-run risk is that donors' political commitment might weaken in the face of domestic pressures. Were this to happen, the Island countries might find themselves cut off from access to labor markets, prevented from transferring remittances, and/or deprived of direct budgetary support from metropolitan governments. Because of the extreme difficulty of the adjustment process that such changes would force upon the small island societies, there have been suggestions that Island governments should act now to capitalize (literally) the existing degree of goodwill towards their societies.

The entitlement to a sustained flow of annual budgetary supplements at present rests upon the annual budgeting exercises of the donor governments, with the significant exception of the Government of Kiribati's revenues from its Revenue Equalisation Reserve Fund, which currently stands at about US $120 million. This fund was built up from savings out of phosphate revenues in the 1970s before exhaustion of Banaban reserves. Dividends from the overseas stocks and bonds in which the money was invested provide a reasonably steady and reliable income, expenditure out of which can be budgeted several years in advance. Tuvalu, at the time of moving to self-government and then independence, asked the United Kingdom to provide a similar lump-sum investment fund with secure dividends, rather than insecure and uncertain year-to-year funding via budgetary grants in aid. The request was declined.

From the recipients' point of view the arguments for endowing these countries with a portfolio of reasonably secure income-yielding overseas investments, rather than annual recurrent grants, are strong and attractive, provided that the usual agency problem of management of the funds by politicians and officials can be overcome. If donors' willingness to underwrite living standards in the long run is genuine, then the overall financial cost of an immediate lump-sum endowment would be no greater than that of ongoing recurrent grants. The only difference would be that the Island communities, rather than the aid donors, would have control over the use of the derived incomes.

This would presumably be the sticking point from the donors' point of view. At present, the provision of year-by-year grants has benefits for donors at both the political and the cosmetic

levels. Politically, the system of annual grants confers real bargaining power and an important degree of political control over client states. Cosmetically, because grants in aid are classifiable as "development assistance" for purposes of the OECD statistics, donor countries are able to use these grants to inflate their apparent development contributions as shown in international statistics. It may therefore be anticipated that the most likely outlook is a continuation of the existing system, under which island societies live with some degree of uncertainty, but with insurance provided by the realities of geopolitics. In the eyes of the existing regional powers, the continued provision of budgetary grant aid to friendly governments remains an effective and cost-effective means of achieving the "strategic denial" of the region to Soviet influence; and since this goal seems likely to remain important to the present donors for some time yet, Island governments need only mount occasional well-publicized flirtations with the USSR in order to reproduce their rent entitlement from period to period.

As for the sustainability of the migration/remittance linkages between Island societies and the metropolitan economies, these seem likely to prove as durable as the transnational family enterprises which currently mediate them. On their present showing, those kin networks will be a feature of the South Pacific regional economy for at least the next generation, and probably beyond. That, however, is another story.[16]

NOTES

1. South Pacific Commission (1981), Table 2.

2. In particular, Tisdell and Fairbairn (1984).

3. Bertram and Watters (1984; 1985; 1986). The choice of countries was dictated by the terms of reference for the original 1984 work.

4. "Dutch disease" or "de-industrialization" is shorthand for the crowding-out of tradable-goods production by large rent flows. It was typical of oil-exporting economies, including the United Kingdom, during the decade of high oil prices after 1973 — see Barker and Brailovsky (1981), Shahid Alam (1982), Van Wijnbergen (1984), Pollard (1985). Similar symptoms have been identified in aid-dependent economies — see Hagen (1972) — and in Australia during that country's mineral export boom — see Gregory (1976), Corden and Neary (1982). The transmission mechanism for the crowding-out process is usually a real exchange rate which is "overvalued" from the point of view of non-rent-earning tradable-goods sectors; those sectors are consequently uncompetitive and will decline unless subsidized.

5. Bertram and Watters (1984).

6. The data used in these tables is from a database compiled during the preparation of Bertram and Watters (1984). The figures are drawn from a wide range of sources, particularly colonial administration reports for the colonial period, and official statistical publications of the post-colonial governments where available. Further information, and copies of the database, are available on request. In order to deflate current values to 1982 dollars, we have used the New Zealand consumer price index for the Cook Islands, Niue and Tokelau, and the Australian retail price index for Kiribati and Tuvalu.

7. This unattractive acronym is used as shorthand for "Migration-Remittances-Aid-Bureaucracy". For a discussion see Bertram and Watters (1985; 1986).

8. Ranis and Fei (1961).

9. See note 4 above.

10. Figure 1 is drawn for the case of a fully-open small labor market — i.e. a horizontal "world demand curve" for local labor, with labor considered a tradable commodity. In a completely closed labor market, where labor is internationally non-tradable, the wage in our model will settle at the intersection of L_s and L_{g+m}, with no external influence except those which may operate on L_g due to the need to recruit specialized (possibly imported) skills. In imperfectly-open labor markets, the world demand curve will slope down from left to right, and the local wage will be set where this demand curve intersects *either* L_s *or* L_{g+m} from above. Only the simple open-economy case is presented here; this model fits the present circumstances of the Cook Islands, Niue, and Tokelau, and the historical cases of Western Samoa and Tonga until New Zealand imposed immigration restrictions in 1975–76. The fully-closed model (where a Lewis-type surplus-labor model applies) corresponds to the larger islands in Melanesia and Micronesia — the Solomons, Vanuatu, and Papua New Guinea — which fall outside the scope of the present paper. Partially-open systems, where the world demand curve is downward-sloped and prone to shift back and forth over time, include Western Samoa, Tonga, Tuvalu, and Kiribati. Space precludes a full discussion of the Kiribati-Tuvalu situation here; some data on the role of migrant labor in Tuvalu are in Bertram (1980).

However, while Kiribati and Tuvalu *as countries* exhibit only partial integration into wider labor markets, both island groups exhibit integrated *internal*

labor markets, so that any outer island in either group can be modeled using Figure 1, but taking W^* as the wage in the dominant island of the group (Funafuti in Tuvalu; Tarawa in Kiribati). See Bertram and Watters (1985), p. 504.

11. Lewis (1954); Ranis and Fei (1961).

12. The impact of monetization and imported lifestyles on Nauru, some of the US Pacific territories, and the French-controlled Society Islands, indicates the real risk of such disintegration of the neo-traditional order.

13. Jackson *et al.* (1984), p. 181 recommended a quota-restricted migration scheme from Kiribati and Tuvalu to Australia. The proposal is still under consideration in Canberra.

14. Hooper (1982).

15. Tisdell and Fairbairn (1984).

16. Marcus (1982); Bertram and Watters (1985).

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