# Economics Division Working Papers

## South Pacific

# Recent economic developments in smaller South Pacific countries: Cook Islands, Kiribati, Tuvalu and New Caledonia

Ila Temu

96/4





Research School of Pacific and Asian Studies ANU

**Enquiries**
The Editor, Working Papers
Economics Division
Research School of Pacific and Asian Studies
The Australian National University
Canberra 0200
Australia

Tel (61-6) 249 4700
Fax (61-6) 257 2886

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**Ila Temu** is Director of the Islands/Australia Program at the National Centre for Development Studies, Research School of Pacific and Asian Studies, The Australian National University, Canberra.

This paper is based on work done for ESCAP in the preparation of the 1996 Economic and Social Survey of Asia and the Pacific.

# Abstract

The verdict is out. The small island economies of the South Pacific are not doing as well as similar economies elsewhere. Dependence on foreign aid has provided a false sense of security. Tough policy choices have been avoided as governments continue to take the easy options. Those options are now fading and the tough choices have to be made. Cook Islands is just now making these difficult choices, cutting the public service and salaries by more than 50 per cent as of July 1996. It remains to be seen whether the other small Pacific islands countries follow this lead.

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# Recent economic developments in smaller South Pacific countries: Cook Islands, Kiribati, Tuvalu and New Caledonia

Economic management among the Pacific island economies is fast proving to be quite a difficult task, despite their small size. Endowed with limited natural resources, development in many of these small island economies has been driven largely by external resources such as foreign aid and remittances. These finance not only development projects but also relatively large public sectors. With declining aid levels and limited opportunities for emigration, this dependence is increasingly threatened and its continuation is highly uncertain.

The development of limited available natural resources also introduces environmental risks which could jeopardise the future of these fragile atoll and island environments. The need for sustainable development is crucial. Fast increasing populations and the growth of urban centres also pose threats to the environment. Vulnerability to natural disasters such as cyclones introduces an added risk.

The economic reality faced by these economies is harsh. Small domestic markets, dispersion and isolation mean that the cost of government service delivery is high and that private business enterprises face high costs which, in turn, affect profitability. These high costs result from high wage rates, and high service and transport costs.

## Cook Islands

### Macroeconomic performance and policies

Official national accounts data for Cook Islands are available only up to 1990. The Asian Development Bank has produced a set of national accounts data to 1994 based on gross turnover statistics (Asian Development Bank 1995). These estimates are used in assessing recent economic growth in the Cook Islands.

The open nature of the Cook Islands economy is reflected in the degree of variability in growth occurring over time. In 1984 a real growth rate of 12.7 per cent was achieved while in 1987 it had declined to 0.5 per cent. Over the next two years it picked up to about 7 per cent but dropped sharply again in 1990 to 1.9 per cent. In 1991 and 1992, another substantial increase occurred with growth rates of 8 per cent and 11 per cent, respectively. Estimated growth rates for 1993 and 1994 are 8 per cent and 7.4 per cent, respectively (Table 1).

Table 1 **Cook Islands: gross domestic product by major industries, 1992–94 (at current market prices, NZ$'000)**

| | Gross domestic product (NZ$'000)[e] | | |
|---|---|---|---|
| | 1992 | 1993 | 1994 |
| Agriculture | 22,971 | 24,807 | 26,643 |
| Manufacturing | 5,261 | 5,681 | 6,102 |
| Trade | 28,877 | 31,185 | 33,493 |
| Transport/communication | 14,539 | 15,701 | 16,863 |
| Finance | 12,145 | 13,116 | 14,086 |
| Public administration | 30,461 | 32,895 | 35,329 |
| Total | 126,871 | 137,009 | 147,148 |
| Annual growth | .. | 8.0 | 7.4 |

[e] estimates
**Source:** Asian Development Bank, 1995. *Key Indicators of Developing Asian and Pacific Countries*, Vol XXVI, Oxford University Press, New York.

Growth performance in Cook Islands has been driven by improved conditions and performance from individual sectors, including public expenditure on capital goods. Growth in the mid-1980s was driven by public expenditure on electricity and water while in the late 1980s, growth occurred largely through improved conditions in agriculture and fisheries. In the early 1990s, increased activities in construction, tourism, finance and business, and transport and communication contributed to economic growth. The main factors contributing to this were exceptional increases in tourist numbers and increased government spending in construction on the Sheraton Hotel and the National Cultural Centre. In 1993, the tourism and finance and business sectors held up well to counter the subsequent decline in construction activities.

Gross turnover statistics for March 1994 indicate substantial improvements in agriculture and fishing, while tourism and finance and business have continued to perform well. The Asian Development Bank estimate for growth in 1994 is 7.4 per cent. Increases in visitor arrivals in 1992–93 were expected to continue in 1994. For the first five months of 1994, total visitor arrivals were 25 per cent higher compared to the same period in 1993.

While the improved performance of these sectors could have made possible growth of about 7.4 per cent, election hysteria and some confusion over the total national debt set in motion a significant level of capital flight which would have adversely affected these opportunities through restrictions on domestic credit and lending. A total public debt figure of NZ$245.7 million was quoted in the media at the time of the elections. The more correct figure, according to Asian Development Bank estimates, is NZ$139.6 million, which represents principal only. Some 60 per cent of this debt is due to borrowings undertaken by the government for the Sheraton Hotel. This single event is likely to have a significant negative impact on overall economic growth for 1994. An expenditure freeze imposed in 1994 will contribute to this negative impact.

With concerns over fast-increasing public debt, commercial banks in the Cook Islands had little choice but to curtail domestic lending. Westpac's overdraft facility appeared to have reached its limit and there was concern that the government was borrowing beyond its ability to repay, raising fears about economic management and the ability of the government to reverse this trend. There was also a great deal of uncertainty about the stability of the local currency, leading to capital flight.

Given the problems of 1994, the Government of the Cook Islands took a number of new initiatives in 1995, including new legislation to restructure the public service and to ensure greater accountability. A new Public Service Bill has been drafted to streamline the public service through use of employment contracts which emphasise performance and productivity. A new *Audit Act* and the establishment of a Public Expenditure Review Committee with wide-ranging powers are the two measures taken for greater accountability. The Asian Development Bank has sponsored an institutional capacity-strengthening project to assist in areas of economic planning and budgeting.

Two further measures were undertaken to stabilise the economy: the conversion of currency back to the NZ dollar, and the introduction of greater tax incentives for large deposits. These measures are aimed at attracting back funds taken out of the country in 1994/95.

With the establishment of its own ministry in October 1994, outer island development seems to be a priority, with the development and integration of infrastructure a key focus. The Cook Islands Development Bank is currently negotiating a US$3 million loan for this and other private sector development needs.

Black pearl sales ranked second to tourism in 1994, bringing in NZ$5 million. This sub-sector has received a much-needed boost with the establishment of the Marine Resource Centre at Tongareva in August 1995. The Centre should assist pearl farmers as well as producers of other marine products. A total of 150 small pearl farms were established on Penrhyn Island with the first harvest expected in October 1995.

The long-line tuna fishery also attracted some investment in 1995. Two vessels are now in operation and are producing for the sashimi market. Two fish-packing houses have also been established. A new police fuel facility on Penrhyn will also allow better policing of the country's exclusive economic zone. The fishing sector's contribution to GDP should improve as a result.

There has been only moderate inflation in Cook Islands over the period from 1990 to 1994 (Appendix Table 1). The largest increases in prices occurred in 1993 by over 7 per cent. This increase was evenly distributed across all commodities except tobacco and alcohol, which had increases of up to 10 per cent. The increasing trend of consumer prices reflected the lagged effects of strong domestic demand and the depreciation of the NZ dollar. An appreciation of the NZ dollar since 1993 was the main factor in moderating inflation in 1994.

## International trade

Cook Islands trade balance in 1994 represented about -92 per cent of the estimated gross national product (Asian Development Bank 1995:37). This has increased from about -79 per cent in 1985. Limited opportunities for exports and increasing import demand have contributed to this trend. Except for the negative growth in exports in 1994, both imports and exports have recorded growth of about 13–14 per cent each year (Table 2).

Food and manufactured consumer goods dominate imports while manufactured exports is the main export category. Pearls represent the main export and although not explicitly stated, they are probably included as manufactured exports. No explanation could be found for the reduction of over 50 per cent observed for fruit exports in 1994, however, with pawpaw as the major commodity, this could reflect either a bad production year or quarantine problems.

The growth in imports over this period can be attributed to a combination of factors, including the depreciation of the NZ dollar prior to 1993, increased government borrowing to finance a number of major construction works and the increasing number of tourist arrivals over this period. Tourism in 1995 is likely to be affected by the cutback in *Polynesian Airlines'* services, especially in those routes that service the US market. An intensive marketing strategy has been mounted by the Tourism Authority to counter this.

## Private sector development

An important part of the initiatives proposed in 1995 is the privatisation and cooperatisation of a number of activities currently operated by government. The government trading post, Cook Islands Liquor Supplies, has been corporatised and a new management team has taken over operations. There are also plans to privatise

**Table 2 Cook Islands: total exports and imports, 1992–94 (NZ$'000)**

| | 1992 | 1993 | 1994 |
|---|---|---|---|
| Exports (major items only) | | | |
| Fruit (fresh/canned) | 1,622 | 1,720 | 916 |
| Manufactured | 3,855 | 4,740 | 4,693 |
| Copra | - | 2 | - |
| Clothing | 16 | 33 | 258 |
| Total | 6,300 | 7,155 | 6,962 |
| Imports (major items only) | | | |
| Food | 22,553 | 25,682 | 29,526 |
| Beverages/Tobacco | 6,495 | 7,380 | 8,489 |
| Fuel | 12,872 | 14,649 | 16,878 |
| Manufactured | 36,658 | 41,686 | 47,961 |
| Machinery | 19,638 | 22,390 | 25,738 |
| Total | 109,163 | 124,249 | 142,911 |

Source: Asian Development Bank, 1995. *Key Indicators of Developing Asian and Pacific Countries*, Vol XXVI, Oxford University Press, New York.

the Akitua Resort, the Rarotongan Hotel and the Banana Court. A Cabinet subcommittee has been set up to identify and screen other activities which can be privatised, with public utilities such as water, electricity and transport targeted.

For Cook Islands, as well as for many other island countries, the breakdown in GDP between public and private sectors is difficult because government still owns and operates a large number of activities which are private in nature. Public administration is a separate category in GDP calculations and could provide a minimum limit for the public sector share, giving an average figure of 24 per cent for 1992–94 (Table 1).

In terms of employment in Cook Islands, the category 'others' seems to dominate, accounting for 89 per cent of the total employment (Appendix Table 2). While the exact details of what this category includes have not been provided, it is probably safe to assume that a significant part of this category is public sector employment. Using Survey of Employment figures for 1990, of the total 4778 people employed in that year, some 56 per cent were employed in the public sector.

The current government also recognises the important role of the private sector in the development of the Cook Islands economy. There is currently a proposal to set up a Trade, Investment and Business Agency, a statutory body whose prime responsibility will be to promote and facilitate private sector development. It is also expected to undertake licensing and regulatory functions. In terms of foreign investment, current policy encourages joint venture operations where the government is expected to take up a majority 51 per cent share in any activity.

In 1994 the government identified a number of economic opportunities for private sector involvement. These include the development of agriculture to supply the domestic market and niche markets wherever possible, fishing and pearl farming, infrastructure development and tourism. The government is eager to support the private sector in taking advantage of these opportunities.

### Social services

The role of government in the provision of social services is crucial for many island countries. In Cook Islands the attainment of a high standard of living has always been an important social goal. Available statistics show that in 1993, community and social services, as well as housing, represented about 6.4 per cent of the GDP. In terms of housing, the government encourages home ownership largely through subsidised housing loans. Sanitation, water supply and garbage disposal are provided free in the city.

In 1995 the government established a new health board to ensure that the high quality of health service in the Cook Islands is maintained. The policy of free medical care continues to be maintained. Private health services are available for a fee but any prescriptions can be obtained free at the public hospital. Social welfare benefits are available to children below 10 years of age and those who are over 60 years. Education is compulsory.

## Kiribati

### Macroeconomic performance and policies

The last official statistics on the National Accounts of Kiribati were published in 1988 and contained national account statistics only up to 1985. Subsequent statistics have been compiled by a number of different organisations such as the World Bank, Asian Development Bank and AusAID. The most current estimates are available from the latest AusAID study on the Kiribati economy (AusAID 1995).

The low growth performance of the Kiribati economy reflects the harsh environment in which such small, resource poor and isolated countries have to exist. Between 1982–91, growth in real GDP averaged only 1 per cent per annum. With population growing at rates higher than 2 per cent, a decline in real GDP per capita has been inevitable. AusAID (1995) estimates this decline to be as high as 25 per cent for the period 1982–93. The per capita GDP for 1993 is estimated to be A$617 per annum, among the lowest in the Pacific region.

For the three years for which GDP data is available, all sectors except transport/ communication and public administration show a decline in their contributions to GDP (Table 3). In agriculture and fisheries, declining commercial activity has been the major cause for the declining sectoral share. The dominance of government is reflected in the share of public administration which accounts for about 27 per cent of the GDP in 1993. The growth in government activities has continued to be an important influence on GDP. Official development assistance has made this possible for Kiribati. External grants are estimated to represent 55 per cent of GDP and 35 per cent of total budgeted expenditure in 1995 (AusAID 1995). A significant part of this assistance has been channelled through the development budget.

The low levels of output which have been characteristic of small countries like Kiribati have not resulted in adverse economic conditions for another reason. An assessment of GNP statistics reveal that the economy still enjoys significant inflows of income from abroad in the form of transfers from earnings of the Revenue Equalisation Reserve Fund and remittances from I-Kiribati who are employed on foreign vessels and on the phosphate mine in Nauru. The Fund started with an initial deposit of about A$0.5 million and was valued at over A$315 million in 1994 (AusAID 1995). This represents a significant investment by the government of Kiribati which should almost guarantee future income flows and higher levels of consumption, despite low levels of output in the economy.

Table 3 **Kiribati: gross domestic product by major industries** (at current prices, A$'000)

| | 1991 | 1992 | 1993 |
|---|---|---|---|
| Agriculture | 3,880 | 3,938 | 3,333 |
| Fishing | 6,607 | 6,320 | 6,373 |
| Construction | 1,802 | 1,449 | 1,755 |
| Trade and hotels | 6,579 | 5,900 | 6,000 |
| Transport/communication | 4,185 | 4,400 | 4,700 |
| Finance and insurance | 2,136 | 1,859 | 1,900 |
| Public administration | 11,931 | 12,510 | 12,700 |
| Total | 45,750 | 45,942 | 47,238 |
| Annual growth (per cent) | 6.3 | 0.4 | 2.8 |

**Source: AusAID, 1995. The Kiribati economy, International Development Issues draft report, Canberra (unpublished).**

The drawdown from the Revenue Equalisation Reserve Fund has increased from an estimated A$4.4 million in 1994 to a budgeted level of A$7.5 million in 1995. This represents a significant increase as the average drawdown for the past three years has been only about A$3 million. The prudent fiscal policy of the 1980s appears to have been abandoned in 1994 and 1995 as the government has opted for more expansionary budgets. Substantial improvements in fishing royalties have also provided support for expansion. Total budgeted government expenditure has increased from A$53.9 million in 1994 to A$73.9 million in 1995, an increase of about 37 per cent. Over 50 per cent of this increase is from the development budget. This new expansionary policy, with emphasis on the development expenditure, should translate into better growth opportunities over the medium term.

Given the value of the Revenue Equalisation Reserve Fund, this change in policy approach is appropriate—fiscal restraint may have been overdone given that important welfare services such as health and education could have been improved with these funds. Kiribati still has poor social indicators by regional standards, although much improvement has occurred in recent years. Life expectancy is about 53 years while infant mortality rates are about 82 per 1000. The gross primary school enrolment ratio is 84 per cent and the adult literacy rate is only about 10 per cent. The fast-increasing urban population in Tarawa is beginning to cause strain on urban services, especially water, garbage and sanitation and environmental effects are being compounded as maintenance lags behind the increasing demand for these services.

CPI data for Kiribati refer to the retail price index for Tarawa. The average change in the index has declined between 1993 and 1994, occurring across most major items including food and alcohol/tobacco, which together account for 64 per cent of the weighted index (Appendix Table 1). Transport, accounting for only 8 per cent of the weights, recorded the highest increase. On this basis, the rate of inflation in Kiribati is moderate.

### International trade

The vulnerability of Kiribati's economy is reflected in its trade statistics (Table 4). The enormous extent of annual variability in trade, both in terms of exports and imports, is reflective of this.

On the export side, the country has had only two major exports, fish and copra. This makes export revenues vulnerable, not only to price changes, but also to circumstances such as weather and natural disasters. The decline in value for copra between 1992 and 1993 resulted in a decline in the output of copra over this period. The same is true for fish—the volume of fish declined from 2,600 metric tonnes in 1989 to 286 metric tonnes in 1993. This decline in fish exports has been more than offset by increases in seaweed as well as the introduction of new marine exports such as aquarium fish since 1991, and *bêche-de-mer* since 1993. Re-exports are an important component of total exports from Kiribati.

Table 4 **Kiribati: total exports and imports, 1991–93 (A$'000)**

| | 1991 | 1992 | 1993 |
|---|---|---|---|
| Exports | | | |
| Copra | 1,625 | 4,350 | 1,754 |
| Fish and other marine products | 1,313 | 1,025 | 2,071 |
| Total | 3,698 | 6,513 | 4,475 |
| Annual growth (per cent) | -34 | 76 | -31 |
| Imports | | | |
| Food | 9,953 | 10,654 | 11,923 |
| Beverages and tobacco | 2,285 | 2,534 | 2,641 |
| Fuel | 3,631 | 3,951 | 3,032 |
| Manufactured | 6,495 | 6,839 | 9,306 |
| Machinery | 8,241 | 23,885 | 10,089 |
| Total | 33,226 | 50,530 | 40,874 |
| Annual growth (per cent) | -4 | 52 | -19 |

Source: AusAID, 1995. The Kiribati economy, International Development Issues draft report, Canberra (unpublished).

The major export markets for Kiribati are the European Union and the United States. Fiji was dominant in the late 1980s but its share has since declined to about 5 per cent. The Asian destinations, through Japan, are becoming important, accounting for 79 per cent of the total exports in 1992, but this had declined to 22 per cent in 1993. Fish and marine products are the main items of export for the Asian market.

Kiribati's low level of output has not restricted domestic consumption, as shown by the extent to which imports outweigh exports. This negative trade balance has been financed largely by transfers from abroad. Imports of machinery were responsible for the substantial increase in 1992. An increase of 44 per cent in External Development Grants could well have explained a significant part of this increase in imports.

While there has been an almost permanent negative trade balance for Kiribati, its current account has always had an equally permanent surplus (Table 5). Substantial inflows in net service receipts, especially from the Revenue Equalisation Reserve Fund have, more or less, countered the negative trade balance. In addition, Kiribati has been fortunate in receiving generous official transfers, giving it a much-needed foreign exchange cushion. While the capital account has sustained deficits for some time, the fact that these were small relative to the current account surpluses has meant that the overall balance has been positive for much of this time. While positive overall balances are shown for 1991 and 1992, these appear to have been temporary. A more realistic picture is reflected in the figures for 1993, with an overall balance of A$2 million. The increasing negative trade balance and net service payments, as well as declining foreign aid, has meant that past high levels of current account surpluses could not have been sustained for long. If this trend continues, it will not be long before deficits start creeping into the overall balance.

### Private sector development

The dominance of government in Kiribati's economy has meant that the private sector has had little or no opportunity to contribute to development. High public sector wage rates, supported largely through foreign aid, and low levels of productivity have made it impossible for private sector to compete with government. Other constraints affecting private sector development include limited access to and the availability of credit, lack of business support services, limited opportunities and market access constraints. With much of the skilled workforce already engaged by government, few are available for private sector jobs.

Current discussions on the need for private sector development, especially in new areas such as marine resources and tourism, on human resource development and public sector reform, should see a change in the involvement of the private sector.

Table 5 **Kiribati: balance of payments, 1991–93** (A$ million)

| | 1991 | 1992 | 1993 |
|---|---|---|---|
| Exports f.o.b | 3.7 | 6.5 | 4.5 |
| Imports f.o.b | 33.2 | 50.5 | 40.9 |
| Trade balance | -29.5 | -44.0 | -36.4 |
| Services (net) | 13.9 | 10.8 | 12.7 |
| Receipts | 37.8 | 37.3 | 40.7 |
| (of which RERF gross income) | 14.7 | 14.6 | 16.9 |
| Payments | 23.9 | 26.5 | 28.0 |
| Private Transfers (net) | 2.6 | 3.0 | 3.2 |
| Official Transfers | 23.7 | 33.3 | 21.6 |
| Current Balance | 10.7 | 3.1 | 1.1 |
| Capital Balance | -1.9 | 5.6 | 0.9 |
| Government | 0.8 | 1.1 | 4.6 |
| Non-bank financial institutions | -2.5 | -3.2 | -3.3 |
| Others | -0.2 | 0.7 | -0.4 |
| Government transfers overseas | .. | 7.0 | .. |
| Errors and omissions | 3.6 | 6.4 | .. |
| Overall balance | 12.4 | 15.1 | 2.0 |

**Source:** AusAID, 1995. The Kiribati economy, International Development Issues draft report, Canberra (unpublished).

This change should provide greater opportunities to the private sector to undertake activities which have, in the past, been performed by government. The current realisation that governments are somewhat ineffective in performing these tasks has made reforms all the more urgent if services are to be maintained and delivered effectively in service delivery. This is not to say that governments have no role to play. In fact, it is crucial that governments should continue but with roles that allow them to set up the conditions necessary for the private sector to operate effectively.

## Social services

Government expenditure in Kiribati has been expansionary in recent years. In 1991, expenditure on education and health represented 18 and 15 per cent of total expenditure, respectively. In 1995, based on budget estimates, these shares are 19 and 18 per cent, respectively (Table 6). These figures suggest a significant increase in expenditure on health while education has received a modest increase but has continued to attract a greater share of the budget. The expansionary nature of the 1995 Budget is also reflected in significant increases in budget allocation to health and education. Over this period, expenditure in both sectors have increased by over 50 per cent.

Table 6 **Kiribati: central government expenditure, 1991–95** (A$'000)

| | 1991 | 1992 | 1993 | 1994[e] | 1995 Budget |
|---|---|---|---|---|---|
| General services | 6,963 | 6,554 | 8,025 | 12,114 | 12,663 |
| Public order and safety | 1,906 | 1,936 | 2,098 | 2,489 | 3,046 |
| Education | 4,410 | 5,184 | 5,611 | 6,279 | 8,524 |
| Health | 3,729 | 4,252 | 4,245 | 5,419 | 7,900 |
| Economic services | 7,762 | 7,907 | 7,280 | 9,465 | 12,375 |
| Total | 24,770 | 25,833 | 27,959 | 35,766 | 44,500 |

[e] estimate

**Source:** AusAID, 1995. The Kiribati economy, International Development Issues draft report, Canberra (unpublished).

While it is probably too early to assess the impact of such increases in government expenditures in the social sectors, AusAID notes that ' impressive recent gains in child survival and life expectancy reflecting increased coverage of immunisation, control of vitamin A deficiency and improved access to curative care' (AusAID 1995:5). Heavy concentration of the population into South Tarawa is likely to create new health problems. High overall growth rates for the whole country will strain existing health and educational services such that greater increases in expenditure will be necessary to cater for this increased demand. If not, the quality and standard of service will have to be sacrificed to ensure that access is maintained.

## Tuvalu

### Macroeconomic performance and policies

The last report on the National Accounts of Tuvalu (1988–90) was published in May 1992. The Statistics Office in Tuvalu is currently preparing an update which is scheduled for release in 1996. More current estimates of national accounts data are available from the Asia Development Bank (1994).

As in the other island countries, public administration dominates the economic structure, accounting for 28 per cent of GDP over this period 1989–93. Agriculture, including fisheries, is the second most dominant, accounting for 22 per cent of GDP.

GDP in Tuvalu has expanded at rates much higher over this period than those in the 1980s (Table 7). In terms of sectoral contributions, growth has occurred fairly evenly among all sectors, although the service sectors like trade and finance and public administration appear to have been booming in the Tuvalu economy. Increasing recurrent government expenditure, financed largely by increasing drawdowns from the Tuvalu Trust Fund, is probably a major factor in this trend. Total recurrent revenue financed out of Fund drawdowns increased from 8 per cent in 1989 to 54 per cent in 1992 and then declined to 29 per cent in 1993. With budget deficits in 1989 and 1990, it is somewhat surprising that there were budget surpluses over the period 1991–93. Under-expenditures in the development budget contributed to these surpluses, although somewhat dampened by over-expenditures in the recurrent budget, suggesting that increased recurrent expenditures were being financed from large drawdowns from the Tuvalu Trust Fund and transfers from the development budget.

With the use of the Australian dollar and heavy dependence on imports external factors, including exchange rate movements, have been responsible for much of the price variability in the Tuvalu economy. Australia, New Zealand and Fiji have been the major sources of imports, so one would expect some degree of imported inflation. From 1983 to 1993, inflation was moderate, averaging 4.4 per cent per annum and, fluctuating quite heavily, reached a peak of 11 per cent in 1991. Price increases in food, alcohol and tobacco were the main cause of this increase. Inflation has since subsided to 2 per cent in 1993 (Asian Development Bank 1994). The depreciation of the Australian dollar over the recent past is likely to exert upward pressure on domestic prices again.

Estimates of national income statistics for the period 1988–91 are indicative of the savings and investment situation in Tuvalu, suggesting negative gross domestic savings and high levels of gross domestic investment (Asian Development Bank 1994). This implies a large resource gap, estimated at about 50 per cent of GDP in 1991, to be financed from external financial resources. For Tuvalu, these resources include remittances by workers abroad, Tuvalu Trust Fund earnings and drawdowns, and

Table 7 **Tuvalu: gross domestic product by major industries** (at constant prices A$'000)

| | 1989 | 1990 | 1991[e] | 1992[e] | 1993[e] |
|---|---|---|---|---|---|
| Agriculture | 2,144 | 2,186 | 2,405 | 2,597 | 2,805 |
| Manufacturing/mining | 508 | 529 | 607 | 649 | 684 |
| Construction | 1,280 | 1,324 | 1,457 | 1,603 | 1,731 |
| Trade | 818 | 1,329 | 1,489 | 1,639 | 1,784 |
| Transport/communication | 646 | 362 | 417 | 458 | 504 |
| Finance | 876 | 982 | 1,081 | 1,167 | 1,260 |
| Public administration | 2,438 | 2,649 | 2,967 | 3,234 | 3,557 |
| Total | 8,909 | 9,581 | 10,669 | 11,614 | 12,623 |
| Annual growth (per cent) | 1.9 | 7.5 | 11.3 | 8.8 | 8.6 |

[e] estimate.

**Source:** Asian Development Bank, 1994. *Tuvalu: economic situation, policies and prospects*, South Pacific Regional Office, Manila.

foreign aid. In 1991, foreign aid represented 71 per cent of total external flows into Tuvalu and has been the main source of finance for the development budget. The main development projects financed over this period include airport extensions, a fisheries centre and a wharf.

In July 1995, the government of Tuvalu put out its National Development Strategy 1995–98 (Tuvalu 1995). Recognising the constraints within which development is to occur, this strategy 'outlines measures to improve the governance of life in Tuvalu, to provide a climate for better economic performance, to improve the provision of essential services, and to help distribute resources equitably among all Tuvaluans' (Tuvalu 1995:iii). The five priority programs identified are public sector reform, restructuring of the economy towards export-oriented business investment, improving economic infrastructure, education for life and upgrading human settlement.

In terms of macroeconomic policy, fiscal stability and increased government savings have been identified in the National Development Strategy as important macroeconomic objectives. Fiscal stability is to be achieved through the maintenance of the real value of the Tuvalu Trust Fund while the target for government savings is an increase from its current average of 9–10 per cent to 13–15 per cent of GDP. Recognising the unstable nature of revenues, the government plans to establish a Revenue Stabilisation Fund to stabilise revenue flows to the government budget. There are plans to increase the prices of government goods and services in line with the trend rate of inflation and also to adopt 'revenue neutral' taxation changes.

While the government of Tuvalu does not conduct any active monetary policy, the National Development Strategy recognises the importance of containing inflation and promoting international competitiveness. In this regard, the government must play a proactive role in containing and stabilising domestic costs. Interest rates and wages controls are the two options available to achieve this.

### International trade

Available trade statistics are scanty and of little use in assessing growth trends (Table 8). This reflects the lack of real opportunities available for exports. Stamps appear to have dominated exports while copra has had a variable contribution. Fish, handicrafts and garments have also been exported at various times. In terms of imports, food and manufactured imports have been dominant. The negative trade balance for 1989 is 55 per cent of GDP. Again, such a large imbalance has been made possible by the large financial inflows referred to earlier.

As in the other island economies, the government is an important component of the Tuvalu economy. In 1990, 49 per cent of GDP was generated by general government activities while another 16 per cent was from public corporations (Tuvalu 1995), suggesting that government accounts for 65 per cent of GDP while the private sector accounts for the balance at 35 per cent. Available statistics for 1991 indicate that government, including public corporations, provided 72 per cent of total employment while the private sector provided only 28 per cent of jobs. The differences in the ratios between government and the private sector confirm that the private sector is relatively more productive than government. Initiatives under the National Development Strategy for public sector reform are therefore crucial if productivity and efficiency are to be increased in the public service for effective service delivery.

### Private sector development

While the government is likely to remain dominant in the economy over the long term, the National Development Strategy also recognises the important role of the private sector, especially in industrial development. Large scale export-oriented commercial ventures financed through foreign direct investment are targeted. A number of these activities have been identified in the Strategy, including commercial fishing (offshore tuna purse-seining and deep water snapper), tourism and small-scale manufacturing and other business activities.

With respect to commercial fisheries development, a joint venture arrangement between foreign and private domestic investors will be used to establish the first Tuvaluan-flagged purse-seine fishing company. Private domestic investors are also being encouraged to develop a small-scale deep water snapper fishery and a commercial artisanal fishery for the purpose of exporting.

Table 8 **Tuvalu: merchandise exports and imports, 1989–93** (A$'000)

| | 1989 | 1990 | 1991 | 1992 | 1993 |
|---|---|---|---|---|---|
| Exports | | | | | |
| Copra | 73 | 29 | .. | .. | .. |
| Stamps | 133 | 147 | 166 | .. | 216 |
| Fish | - | .. | .. | .. | .. |
| Garments | 100 | .. | .. | .. | .. |
| Total exports | 312 | 178 | 166 | .. | 216 |
| Imports | | | | | |
| Food | 1,514 | .. | .. | .. | .. |
| Fuel | 660 | .. | .. | .. | .. |
| Manufactured | 1,456 | .. | .. | .. | .. |
| Machinery | 632 | .. | .. | .. | .. |
| Total imports | 5,170 | .. | .. | .. | .. |

**Source:** Asian Development Bank, 1995. *Key Indicators of Developing Asian and Pacific Countries*, Vol XXVI, Oxford University Press, New York; Asian Development Bank, 1994. *Tuvalu: economic situation, policies and prospects*, South Pacific Regional Office, Manila.

The establishment of commercial tourism in Tuvalu is to be pursued using similar arrangements to those suggested for the development of commercial fisheries. Specific areas with potential for tourism will be identified so that all necessary infrastructure is put in place through the development budget. In recognising the importance of being competitive, the government is taking steps to address constraints relating to quality of infrastructure and services, training in hospitality, transport, marketing and investment capital. As a start, the Vaiaku Lagi Hotel is to be leased to a hotel management company with wide experience and good networks in the tourism industry.

In the area of manufacturing, cottage industries are to be encouraged with the government playing an active role in identifying overseas markets and providing the necessary technical support. While domestic and foreign investment are encouraged, Tuvaluans within the region who have access to investment funds are been particularly targeted. This is seen as an important means of establishing and extending marketing networks for Tuvaluan products.

Small business development is a key policy in the National Development Strategy, given the potential of directly improving income opportunities for a large number of people. Various technical assistance and training programs will be used in teaching business skills. A commercial centre and marketing facilities is to be set up in Funafuti, replacing temporary stalls currently in use for vending by small business operators.

The National Development Strategy recognises the importance of improving the economic infrastructure in Tuvalu, including transport, communication, energy and land services. Increased investment in transport infrastructure and the commercialisation of these services through joint venture arrangements between the state and domestic and foreign investors is an integral part of the strategy. With regard to communications, the Tuvalu Telecommunications Corporation will be required to operate along commercial lines except in areas of community service which are likely to be subsidised by government. This will require institutional strengthening and improved management. The government is in the process of approving a National Energy Policy where emphasis is again placed on efficiency and commercialisation.

Land management is recognised in the National Development Strategy as a major source of confusion and uncertainty. Land disputes are now a common occurrence in Tuvalu. Improved land management will involve legislative and institutional changes to strengthen the capacity of the judiciary and the Lands Division. Other areas to be addressed include issues relating to land rentals, land management plans and access to land by foreigners.

**Social services**

Social services have always been an important function of government. The quality of these services, however, is highly dependent on resource availability. The National Development Strategy gives an undertaking to ensure that there is improvement in the quality of social services. Programs such as public sector reform and local government review are a means of achieving these improvements. In addition, capacity building through skills development and better management, especially in health and education, is also seen to be a necessary component of this new approach. The private sector, in the form of community institutions, is also being encouraged to play a more active role in the provision of social services.

The equitable distribution of the benefits of development is fundamental to the National Development Strategy. Government recognises the important role and effectiveness of traditional systems of wealth distribution in Tuvaluan communities. These are to be enhanced as much as possible while other instruments of re-distribution available to government. The Strategy also recognises the importance of decentralisation and targeted social development to groups such as women and youth.

# New Caledonia

## Macroeconomic development and policies

National accounts statistics from New Caledonia are somewhat dated and availability has been restricted by the fact that much of it has been published only in French. The Tableaux De l'Economie Cale'donienne (1994) report is the first time these statistics have been published in English. The most current and detailed GDP data is available only up to 1990, while total GDP figures are available up to 1992 (Table 9).

The two years prior to 1989 were years of high GDP growth for New Caledonia, with a peak of 38 per cent nominal growth in 1988. Growth in this period was driven by metallurgy—its share of GDP increased from 6 per cent in 1987 to 24 per cent in 1988. It has since dropped to 18 and 9 per cent in 1989 and 1990, respectively. This explains the slowdown in GDP growth observed for 1989, down to about 13 per cent, and the decline in 1990 by -1.2 per cent. This trend has been influenced largely by demand factors relating to nickel consumption, which in turn is influenced by activity in the industrial world. Looking at the sectoral components, the impact of the reduction in mining/metallurgy in 1990 was somewhat cushioned by improvements in the service sector. The service sector in New Caledonia includes transport and communications, finance and insurance, rental and hire services, hotels and restaurants and other commercial services such as law and accountancy. The total GDP figures for 1991 and 1992 indicate some moderate nominal growth at 9 and 3 per cent, respectively (Table 9).

Table 9 **New Caledonia: gross domestic product by major industries, 1989–92 (at current market prices, Fcfp million)**

| | 1989 | 1990 | 1991 | 1992 |
|---|---|---|---|---|
| Agriculture | 4,511 | 5,032 | .. | .. |
| Mining/metallurgy | 59,920 | 25,977 | .. | .. |
| Construction | 11,581 | 14,151 | .. | .. |
| Transport/telecom | 11,443 | 13,957 | .. | .. |
| Services | 36,546 | 46,699 | .. | .. |
| Commerce | 55,599 | 57,566 | .. | .. |
| Public administration | 54,522 | 62,076 | .. | .. |
| Total GDP | 253,475 | 250,427 | 272,200 | 281,400 |
| GDP growth (per cent) | n.a. | -1.2 | 9.0 | 3.0 |

**Source:** Tableaux De l'Economie Cale'donienne, 1994. *New Caledonia: facts and figures*, The Institute of Territorial Economic Statistics, Noumea.

Agriculture is not a dominant sector in New Caledonia, accounting for only 2 per cent of total GDP. Commercial farming, especially of livestock, is an important component of agricultural activity, occupying as much as 97 per cent of the total land area under agriculture. The importance of the public sector in New Caledonia is reflected in the high share of public administration in total GDP—about 25 per cent in 1990, representing mostly salary and wage payments. This trend is expected to continue.

Inflation statistics for New Caledonia is stated as average annual percentage change (Appendix Table 1). With 1986 as the new base year, there has only been moderate inflation in New Caledonia with the highest occuring in 1991. Inflation in 1991 was evenly spread among all components with foodstuff prices posting the highest increase (4.4 percentage points), thereby influencing the overall trend. The decline in 1994 was mainly due to the marginal increase in foodstuff prices compared to the increase in 1993. Moderate levels of price increases are expected to continue in 1995.

**International trade**

International trade in New Caledonia is dominated by imports. Exports are limited largely to nickel ore and ferro-nickels which together accounted for 77 per cent of the total exports in 1993. This makes export revenues vulnerable to changes in world demand for metal. The volume of nickel ore and ferro-nickels has been increasing over this period while total revenue has generally declined. The revenue impact has been more dominant, giving rise to the declining trend in export revenue over the period 1991–93. For 1994, better demand prospects for steel in the world market pushed steel prices up to US$2.88 per pound above the average price of US$2.39 per pound for 1993. Despite this improvement, with the break-even price above US$3 per pound this increase is assessed to be insufficient as the break even prices is above US$3 per pound. Another major concern is that substantial nickel stocks are held by the industry, reaching a peak in November 1994.

Foodstuffs, manufactured goods and re-exports represented only 11 per cent of total export value in 1993 (Table 9). Over two thirds of food exports are marine products such as tuna and other fish products. Commercial fishing in New Caledonia has been undertaken through near-shore fishing, offshore coastal fishing and deep sea fishing. The latter is picking up importance as people see opportunities for income generation from the vast deep water resources. To assist this development, a Sea Trades School was set up in 1991 to provide training for merchant navy certificates and other maritime training needs. New Caledonia has also been participating in the South Pacific Commission's Deep Sea Fishing Program.

The export to import ratio in 1993 was about 44 per cent and is typical of the situation three years prior to this. The total value of imports has remained somewhat stable at about Fcfp88,000 million (Table 10). Food and machinery and equipment have dominated imports over this period. A decline of about 1 per cent in total value of imports in 1994 is due to drops in purchases of transport equipment and metal and metal products. The most significant increase was in foodstuff imports, increasing in value by about 8 per cent. France continues to dominate imports, accounting for 44 per cent of the total imports in 1994. The European Union and Australia account for 15 and 12 per cent of imports, respectively. On the export side, Japan buys 59 per cent while Australia buys 41 per cent of the nickel ore. Japan is also dominant in the trade of ferro-nickels from New Caledonia, purchasing 24 per cent of the total exports while France, Germany and South Korea purchase 19, 13 and 13 per cent, respectively. In this regard, the appreciation of the Japanese Yen in 1994 will have had a beneficial impact on New Caledonia's export revenues.

### Social services

Health services in New Caledonia are among the best in the Pacific, both in terms of infrastructure as well as services. Since 1990, health services have been decentralised so that each of the three provinces has its own health and social welfare department.

Table 10 **New Caledonia: total exports and imports** (Fcfp million)

| | 1991 | 1992 | 1993 | 1994[a] |
|---|---|---|---|---|
| Exports (major items only) | | | | |
| Nickel ore | 9,734 | 8,734 | 7,867 | 7,285 |
| Ferro-nickels | 26,261 | 20,757 | 21,844 | 23,545 |
| Mattes | 5,352 | 4,456 | 4,775 | 4,946 |
| Other[b] | 4,570 | 5,487 | 4,261 | 3,642 |
| Total | 45,917 | 39,447 | 38,747 | 39,418 |
| Imports (major items only) | | | | |
| Foodstuffs | 15,132 | 15,162 | 15,285 | .. |
| Minerals | 8,617 | 7,175 | 8,616 | .. |
| Chemicals | 5,996 | 6,198 | 6,531 | .. |
| Metal | 6,177 | 5,813 | 6,464 | .. |
| Machinery | 18,631 | 18,085 | 14,901 | .. |
| Vehicles | 12,901 | 15,046 | 15,189 | .. |
| Total | 88,798 | 89,160 | 87,951 | 87,178 |

[a] data for 1994 obtained from 'New Caledonia in Brief', a brochure produced by Tableaux De l'Economie Cale'donienne.
[b] includes foodstuffs, manufactured foods and re-exports.
**Source:** Tableaux De l'Economie Cale'donienne, 1994. *New Caledonia: facts and figures*, The Institute of Territorial Economic Statistics, Noumea.

Together, they manage a total of 27 medical districts and have their own medical and para-medical staff with specialist services provided from Noumea when needed. Each of the provinces operate their health and social services as autonomous establishments with some oversight from the Territorial Health and Social Welfare department, whose responsibilities are now limited to planning, training and coordination functions. There is also a well-developed private health service in New Caledonia, offering a wide range of health services, including specialist services.

The observation with regard to the quality of health services is probably true also for education in New Caledonia. There are a total of 280 primary schools and 76 secondary schools. A total of 54 boarding houses are available for students from isolated areas. A total of 3728 teachers were employed in 1993. As in health, the Education Authority was also transferred to the provinces in 1990. In 1993, the provinces provided about 29 per cent of the funding while the rest came from the French Government. About 65 per cent of these funds represents salaries and wages, representing the extent of subsidy available for education in New Caledonia. Of the total student population, about 58 per cent are in primary, 40 per cent in secondary and 2 per cent in tertiary institutions. Tertiary education is currently offered only in Noumea. The expansion of the French University of the Pacific in 1993 has doubled its intake of students. About half of the students attending school are on some form of scholarship, funded mostly by the provinces.

## Conclusion

There is no doubt that tough times are ahead for these island economies. The economic challenge is one of making full use of the limited resources available, including foreign aid and remittances, while at the same time ensuring that development occurs in a sustainable manner. It is important that these countries begin establishing a firmer foundation for future development—dependence on foreign aid and remittances do not provide this foundation.

Tourism and marine resources offer the greatest potential. The high capital cost of investment in these resources means that foreign investment is necessary. The attraction of investment, however, should not be done by providing public subsidies which could well outweigh the benefits of developing these resources. Duncan and Temu (1996) argue that Pacific island countries should pursue policies which maximise the resource rent on marine resources, arguing that controlled access based on a system of auctions is likely to maximise these resource rents. Current policies of domestication are not likely to achieve this objective because of the need to provide subsidies at high public cost which in turn reduce the full benefit of resource rents.

Enormous opportunities exist for the development of tourism in these islands. This industry, however, relies heavily on the availability of certain infrastructure and services. Hotels, transport and other support services are crucial in the development of this sector. The establishment of tourism infrastructure and the provision of services could well impose a financial burden on these countries. Because of this, it is important that the industry is developed by promoting the natural advantages of the islands, rather than trying to compete with existing tourist destinations. This may mean promoting eco-tourism and other low cost arrangements where such opportunities exist.

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# Appendix tables

## Appendix Table 1 Consumer price index, 1990–94

| | 1990 | 1991 | 1992 | 1993 | 1994 |
|---|---|---|---|---|---|
| Cook Islands[a] | 27.4 | 29.0 | 30.0 | 32.2 | 33.1 |
| Kiribati[b] | 3.8 | 5.7 | 4.0 | 6.1 | 5.1 |
| Tuvalu[c] | 134.4 | 143.0 | | | |
| New Caledonia[b] | 1.4 | 4.4 | 2.5 | 2.9 | 2.0 |
| French Polynesia[b] | 1.4 | 0.7 | 1.7 | 2.1 | .. |

[a] prices relate only to Raratonga; base year is 1985
[b] average annual per cent change; base year is 1986
[c] base year is 1985

**Source:** AusAID, 1995. The Kiribati economy, International Development Issues draft report, Australian Government Publishing Service, Canberra (unpublished); AIDAB, 1993. *Tuvalu: economic situation and development prospects*, International Development Issues 29, Australian Government Publishing Service, Canberra; Asian Development Bank, 1995. *Key Indicators of Developing Asian and Pacific Countries*, Vol XXVI, Oxford University Press, New York; Tableaux De l'Economie Cale'donienne, 1994. *New Caledonia: facts and figures*, The Institute of Territorial Economic Statistics, Noumea.

## Appendix Table 2 Total employment by sector

| | Cook Islands 1993 | Kiribati 1990 | Tuvalu 1990 | New Caledonia 1989 |
|---|---|---|---|---|
| Agriculture | 400 | 2,580 | | 8,737 |
| Manufacturing | | 620 | | 4,588 |
| Mining | 300 | | | |
| Civil service | | 2,123 | 627 | |
| Government enterprises | | 3,484 | 89 | |
| Cooperative services | | | 117 | |
| Commercial services | | | | 14,883 |
| Non-commercial services | | | | 22,343 |
| Others | 5,600 | 2,163 | 45 | |
| Total | 6,300 | 10,970 | 878 | 54,230 |

**Source:** AIDAB, 1992. *The Kiribati Economy: development Options and prospects for growth*, International Development Issues 26, Australian Government Publishing Service, Canberra; AIDAB, 1993. *Tuvalu: economic situation and development prospects*, International Development Issues 29, Australian Government Publishing Service, Canberra; Asian Development Bank, 1995. *Key Indicators of Developing Asian and Pacific Countries*, Vol. XXVI, Oxford University Press, New York; Tableaux De l'Economie Cale'donienne, 1994. *New Caledonia: facts and figures*, The Institute of Territorial Economic Statistics, Noumea.

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