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Urban Bias and Development Banking in the Kingdom of Tonga

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Most development banks in the South Pacific were established as public enterprises in the 1970s with the principal aim of providing loan capital for investment (agricultural, industrial or commercial), and channelling available capital into areas of productive investment. Lending activities, rather than equity participation, constitute the bulk of the operations of all the Pacific banks, and these contribute to the high costs of administration. A substantial source of funding for the banks is aid, and without this intervention it is hard to see just how the private sector would have been able to develop, particularly at the village level.

The banks of the South Pacific, unlike those of larger LDCs, are multi-purpose institutions catering for a range of needs and problems, including education and training, the identification and initiation of new or improved local enterprises, the provision of assistance for social infrastructure and the sharing of risks with foreign and local entrepreneurs. In several cases their objectives include a direct or indirect regional component, such as to help control rural-urban migration and to promote rural development and the participation of the indigenous population in economic development.

South Pacific banks have a particularly strong official commitment to rural development, which reflects the significance of agriculture in national development and the predominantly rural population distribution.

Examination of LDC economies has revealed a persistent and widespread bias in favour of urban areas, the explanations for which are now well known although the principal thesis has been the subject of extensive critical review. Despite arguments over the structures and processes that have led to this scarcely novel phenomenon, and the simplicity of the basic rural-urban division, there has been no dispute over the general tendency for economic activity to be increasingly concentrated in urban areas. Neither has there been any argument, consequently, against the fact of a growing inequality in the distribution of development benefits between rural and urban areas. Examination of the financial structures of some Asian countries supports the particular hypothesis of financial urban bias, in the sense that there is a net transfer of funds from rural to urban areas, which is not justified by social returns and reflects the failure of rural credit markets. In several cases the concentration of commercial bank credit in urban areas contributes to this bias.

This paper examines the extent to which the thesis of financial bias is applicable to the case of credit delivery in Tonga and hence whether it contributes to more widespread urban bias and regional inequalities.

The Kingdom of Tonga

The population of Tonga, although scattered over thirty-six inhabited islands, has increasingly become concentrated in Tongatapu and the capital of Nuku´alofa.

In 1939 some 46 per cent of the population were in Tongatapu but by 1984 this proportion had reached almost 70 per cent, following migration from the Ha`apai and Vava´u regions (see Table 1). Agricultural exports constitute about 80 per cent of total export earnings and more than two-thirds of the population depend primarily on agriculture as a source of livelihood. In 1981-82 the estimated GDP per capita for Tongatapu was T$643, compared with T$411 for Vava´u, T$335 for Ha´apai and T$322 for both ´Eua and the Niuas.

Development finance historically has been heavily concentrated on Tongatapu which has received a disproportionate share of services. Reversal of the trend towards a concentration of economic development on Tongatapu has resulted in greater attention being given to spatial aspects of development policies. Since 1975 the Third and Fourth Five Year Development Plans have officially emphasized rural and regional development to achieve a more equitable distribution of goods, services and income between the people in different parts of the Kingdom, to slow the growth of the Nuku´alofa area and emphasize agricultural development.

The establishment of the Tonga Development Bank in 1977 as a multi-purpose development finance institution was expected to assist in the process of regional and rural development. Its purpose was to promote the expansion of the economy of Tonga for the economic and social advancement of the people of Tonga by giving financial and advisory assistance to enterprises operating or about to operate in Tonga.

In its first year of operation, Tongatapu received 73 per cent of loans by value; in subsequent years, this proportion never fell below 68 per cent and by 1985 was again 73 per cent of total loans by value (see Table 1).

Table 1 Population distribution and development finance by island group

	Tongatapu	Vava´u	Ha´apai	´Eua	Niuas
Population					
1956 - Number	31,264	12,487	9,918	1,925	1,254
- % Total	55	22	17	3	2
1984 - Number	66,311	15,059	8,554	4,007	2,517
- % Total	69	16	9	4	3
Development Bank loans 1985					
Agriculture					
- Number	1,378	492	273	317	28
- Value ($´000)	1,058	596	96	94	36
Industry & commerce					
- Number	221	34	33	11	4
- Value ($´000)	1,548	63	52	8	19
Total					
- Number	1,599	526	306	328	32
% Total number	57	19	11	12	1
- Value ($´000)	2,606	659	148	102	55
% Total value	73	19	4	3	2
SPF/RDF projects					
- Number	112	27	33	14	12
- % Total	57	13	17	7	6

Despite this pattern the Bank concluded in its last annual report: `in conjunction with Government´s strategy for a more balanced development among the various island groups of the Kingdom, TDB has been contributing towards this goal through the provision of financial assistance' in line with its own lending policy which was to lead 'to an increase in the incomes and living standards of people, particularly those at the village or grassroots level' (Tonga Development Bank, Annual Report, 1986).

The Managing Director claimed in 1984:

> TDB feels that, with its strong concentration in the grass roots, it can bring about a more balanced development of people. The villager is given an equal opportunity to the town dweller or salary earner - all he has to do is display a preparedness to help himself. Such promotion also means more employment of idle land and human resources, less drift of the unemployed to the towns and, hopefully, a more equitable distribution of wealth.

The number of projects financed has been more equitably distributed with Tongatapu having 57 per cent of all projects in 1985, a distribution much more like that of the population as a whole (see Table 1). Just over half (51 per cent) of all loans went into agriculture and fisheries though this represented only 43 per cent of the value of all loans. By contrast industry and commerce represented 46 per cent of all loans by value. These proportions were roughly similar to those of previous years, hence both the sectoral and regional distribution of loans have remained largely unchanged despite the commerce sector officially being given lower priority, with finance only being made available after requirements in the agricultural and industrial sectors have been met. Thus, over a nine-year period, disproportionately more credit has gone to Tongatapu and, although no data are available, a significant proportion of this is likely to have suppported urban industry and commerce, especially tourism. This has occurred despite the decentralization of bank administration to each region, reaching Vava'u in 1979, Ha'apai in 1981, 'Eua in 1982 and the Niuas in 1985.

Small project fund and rural development fund (SPF/RDF)

The Rural Development Unit in the Central Planning Department established the SPF/RDF program in June 1979. The SPF provides grant assistance to projects that do not directly generate income, but which meet rural community needs and contribute to social and economic development, such as water supply schemes, rural road improvements and village halls.

The RDF assists potential commercial projects which would contribute to economic development, such as vanilla curing sheds, passionfruit development, copra driers, fishing boats and engines. In itself the whole SPF/RDF program was an innovative one, that followed visits from the the Central Planning Department to every village in Tonga in 1979 and a series of subsequent village and regional development workshops, supported by an unusually highly motivated group of development planners. Projects funded were considered according to a points scheme based on particular criteria where self-reliance, income generation, employment promotion and location away from Tongatapu were all given high priority. Nonetheless, of 198 projects funded over a four-year period, some 112 (57 per cent) were on Tongatapu (see Table 1), and a third of these projects were in Nuku'alofa. Some 42 per cent of all SPF/RDF projects were in manufacturing and commerce and 48 per cent were in the service sector, mainly water supplies and vocational training projects.

Although the program was able to support projects on most inhabited islands, and thus reduce the possibility of contributing to inequality within regions (a situation which may not necessarily be true of bank loans), an internal review of the program was concerned at its possible contribution to increasing the gap between rich and poor, so much so that it recommended means testing of applicants. The internal review team stressed that, of all the instruments available to government, this program was one of the best suited to achieving the government's objective of improving income distribution and to favouring outlying regions and rural areas. However, the actual evidence suggests not only that the program achieved much the same kind of distribution pattern as the Tonga Development Bank but also that a very small proportion of all projects were directly productive; hence improved regional income, despite improved accessibility, would rarely follow directly from the projects.

Though neither the Bank nor the SPF/RDF program have contributed to any significant redistribution of resources within the Kingdom - indeed, they have essentially emphasized existing distributions - the two partial attempts to challenge the existing distribution have almost certainly prevented an even more biased distribution of resources.

Bank support has contributed to the success of the Small Industries Centre (with the export of machinery and manufactured goods reaching 5 per cent of total exports by value in 1984-85), the development of tourism (a sector increasingly emphasized in national development), and infrastructure provision. The SPF/RDF program has made an inevitably smaller but similar contribution, also supporting some small industrial and tourist developments. Thus despite two credit programs both oriented in different ways to rural and regional development, just as elsewhere in the South Pacific, the basic urban distribution of credit has remained unchanged. The cumulative concentration of credit in Tongatapu and Nuku'alofa has emphasized what is almost certainly a growing urban concentration of financial resources following the policies and practices of most other institutions and ministries in the Kingdom.

The pervasive nature of urban bias

The reasons for the problems of decentralization and redistribution are straightforward. Access to credit is hampered by a rural population spread over many inhabited islands with poor communication facilities, the limited understanding of credit facilities in more remote areas, the restricted availability of trained and experienced manpower, and some tendency of project staff to support familiar, local ventures. In remote areas, access to markets constrains some of the range of possible productive ventures, as in Tonga where the Niuas were too remote for most agricultural projects. Partly to minimize these kinds of disadvantages, the availability of cash, physical assets or other forms of assignable security are not regarded as prerequisites for access to credit, and hence Pacific banks have devised the concept of labour or sweat equity and have also funded very small projects where the costs of administering the loan are greater than the loan, and, in the case of Tonga, have established a special fund to break away from institutional constraints. Ultimately redistribution has not been achieved.

Though it can be argued that the Tonga Development Bank and the development banks in the South Pacific region generally have made a dynamic contribution to development and have an impressive record of lending to village communities, trade store enterprises, commercial activities, small-scale farmers and mini-borrowers, it is apparent that, on balance, this effort has not been towards strengthening rural or regional development but has tended to accentuate urban bias. This has occurred even when policies have been directed to rural areas though, without banks, credit provision in rural areas would vary from limited to non-existent and urban bias would be greater.

In Tonga, after nine years, the Development Bank has had minimal success in decentralizing its effective assistance. There has been little government impact on the outer islands and it is doubtful if such measures will induce people not to migrate, or migrants returning from overseas to return to their home islands. Development schemes seem likely to widen the gap between Tongatapu and other regions, even though they propose improvements in the outer islands. Thus whilst in theory development strategies in Tonga and in other parts of the South Pacific are oriented towards outer-island development, in practice there has been little effective change in the actual strategy of development. Rather, there is ambivalence, a lack of finance, a lack of will and a limited number of options for development in the outer islands to draw resources away from the capital city. To some extent this kind of financial bias is not only unavoidable but economically efficient, given the usually higher rates of return on urban credit and investment. However, in the Pacific not only are development banks almost the only source of rural credit but the demand for agricultural credit is likely to increase, as the volume of purchased inputs increases under the twin stimuli of population growth and government pressure to increase agricultural production, whilst urban unemployment shows every sign of worsening. The necessity to continue to challenge the pervasive urban bias that has accentuated regional economic disparities thus remains of vital concern in Tonga as it does elsewhere in the South Pacific region.