



Kiribati

The economy of Kiribati has performed poorly in recent years with GDP growth having declined in most years since 1988. Although GDP growth was positive in 1995, the main stimulus to the economy came from a sharp expansion in government current expenditure, leading to the emergence of a fiscal deficit. This was a factor behind the rise in the rate of inflation and the decline in the balance-of-payments current account surplus. For the longer term, the achievement of sustainable growth will require significant revisions in the nature and extent of the Government's involvement in the economy and a stronger role for the private sector in the development process than is currently the case. An apparent weakening of the Government's commitment to fostering the private sector is not conducive to the achievement of its development objectives.

Recent Trends and Prospects

In contrast to the experience over the previous six years, when GDP growth declined on average by about 2 percent per annum, growth recovered in 1995 to an estimated 2.6 percent. There was some improvement in agricultural and fisheries output but most of the growth came from government services and trading activities following a large rise in civil service salaries. Manufacturing and construction activities were weak following the completion of some major projects in the previous year, and the performance of state enterprises continued to be disappointing.

In its budget for 1995, the new Government, elected in late 1994, adopted a fairly

expansionary approach to fiscal policy, in contrast to the conservative stance of previous administrations. Current expenditure was budgeted to increase by 56 percent, to over 87 percent of GDP. Wage and salary outlays were to be raised by 46 percent and other expenditure (including that on maintenance, health, and education) by nearly 60 percent. An increase in current revenue to 76 percent of GDP from 64 percent in 1994 was largely accounted for by drawing on interest earnings of the Revenue Equalisation Reserve Fund (RERF). The current fiscal balance thus moved from a surplus of 3.3 percent of GDP in 1994 to a deficit of 10.7 percent in 1995. Development expenditure, though less than planned because of a shortfall in external grants, lifted total expenditure to 128 percent of GDP compared with 104 percent in 1994. The overall balance including grants registered a deficit, estimated at 15 percent of GDP compared with 6.5 percent in 1994.

Inflation in Kiribati was somewhat higher in 1995 at 6.5 percent on average compared with 5.1 percent in 1994. Price changes are strongly influenced by the rate of inflation in Australia, a main source of imports, although prices were also influenced by increases in domestic money incomes in 1995.

The external position was less favorable in 1995 than in the previous year. Export receipts - mainly from copra and marine products - rose marginally but still were equivalent to only about 16 percent of imports, which increased by over 21 percent. The trade deficit thus widened to 75 percent of GDP from 67 percent in 1994 (Figure 2.26). Net services receipts, principally RERF interest,

fishing license fees, remittances from workers abroad, and official transfers, though slightly lower than in the previous year, were sufficient to yield a current account surplus equal to 13.7 percent of GDP. This was much lower than the 1994 level of nearly 35 percent. Net capital outflows led to an overall balance of about 3.7 percent of GDP in 1995. RERF balances – the main component of external assets – were equivalent to about six-and-a-half years of imports at the end of 1995 compared with over seven-and-a-half years in 1994.

The outlook for the Kiribati economy in the immediate future depends very much on the fiscal stance adopted by the Government. A further expansion in government expenditure of the order that occurred in 1995 is not in prospect and thus, in the absence of improved performance in the productive sectors, economic growth is likely to fall below

that of 1995. However, the maintenance of expenditure and the fiscal deficit at 1995 levels is likely to require RERF drawdowns above what are necessary to meet the Government's objective of maintaining the real per capita value of the RERF intact over the long term. The balance-of-payments surplus could also be expected to contract further as the demand for imports is maintained.

Policy and Development Issues

The immediate task is to secure a return to a more conservative fiscal stance so that the real value of the RERF is not impaired. Some improvements in revenue, such as indirect taxation, could be made but the prospect also is for a decline in fishing fees, a major source of revenue. The burden of adjustment would thus need to fall primarily on current expenditure (development expenditure usually being kept close to what can be financed from external grants). Short-term expenditure-restricting measures, such as the freezing of staff levels, are possible, but a more constructive and enduring approach would be to hasten reforms in the structure and size of the public sector and improve management efficiency. The system of output budgeting introduced in 1995 is an encouraging innovation; however, a substantial increase in trained staff and rigorous application to all resources – physical and human – are required if the system's potential benefits as a management tool are to be ensured.

Public sector reform should also include a reappraisal of government regulatory activities, many of which do more to impede economic development in Kiribati than to promote it, especially by inhibiting private sector growth. The more restrained attitude to privatization that has emerged over the past year needs to be reconsidered; the privatization of the manifold commercial activities now undertaken by government agencies and enterprises in Kiribati offers considerable scope for efficiency gains to the economy as a whole and could significantly reduce government expenditure or release resources for more beneficial public purposes.

