



Fiji

After achieving an average growth rate of 2.7 percent during 1990-1996, Fiji's economy continued to weaken during 1997 because of major changes in global currency and commodities markets. The devaluation of the currency in early 1998 and the continuation of economic reforms aimed at stimulating growth through private sector initiatives are expected to improve economic performance in the medium term.

RECENT TRENDS AND PROSPECTS

Fiji is one of the most developed of the Pacific island economies and has the standard of living of a lower-middle-income developing country. In the past decade economic growth has been low. After growing 3.1 percent in 1996, economic activity contracted by about 1 percent in 1997. A decline in sugar production caused by cyclones and industrial disputes and a decrease in investment because of the continued uncertainty about the renewal of leases for land used for sugarcane farming adversely affected the agriculture sector. The decline in gold prices had a negative impact on the mining industry. Activity in the building and construction sector was weak, and garment production faced increased competition from other Asian exporters. Tourism, however, continued to make a strong contribution to the economy, with substantial increases in visitor arrivals. Overall, investment remained low, reflecting the weaknesses in the economy and low investor confidence. Both private and public enterprise investment fell to around 4 percent of GDP. Government capital expenditure decreased to less than 3 percent, while operational expenditure remained at around 23 percent of GDP. Consumer prices rose by 2.9 percent in 1997. Weak domestic demand and excess capacity in the economy, a relatively stable exchange rate, and sub-

dued inflationary pressures in the economies of major trading partners contributed to the low inflation rate.

Fiscal performance deteriorated significantly. The budget deficit rose from 0.7 percent of GDP in 1995 to 5.7 percent in 1996 and to around 9.2 percent in 1997. In 1997, for the first time in more than a decade, government revenues did not cover operating expenditures. The government approved two supplementary budgets in 1997, including one for the Commodity Development Framework (CDF), which provides large-scale support to the agriculture sector. The increase in the budget deficit was partly caused by the decision to fund a restructuring program for the National Bank of Fiji, a government-owned commercial bank, which in 1995 had become essentially insolvent. Government debt increased from 41 percent of GDP in 1996 to 48 percent in 1997. About 90 percent of this debt was financed from domestic resources. The balance of payments switched from a surplus in 1996 to a deficit in 1997, largely because of a turnaround in the current account. Foreign reserves continued to remain at high levels, equivalent to almost five months of imports.

The exchange rate of the Fiji dollar is linked to a weighted basket of currencies of the country's main trading partners. Faced with a weak economy and a deteriorating medium-term outlook, the government devalued the currency by 20 percent in

January 1998 in an attempt to increase the competitiveness of Fiji's products and to protect incomes and jobs. In the months ahead inflation is expected to rise substantially to up to 9 percent, but to decrease to lower levels by 1999. Much will depend on the response of wage setters to the devaluation. A strong increase in exports is forecast, with economic activity growing by 2 to 3 percent in 1998 and beyond. The enactment of the new constitution in 1997 that gives more rights to native Indians and the subsequent readmission of Fiji to the Commonwealth is expected to lead to a recovery of domestic and foreign direct investment and to a decline in the rate of emigration.

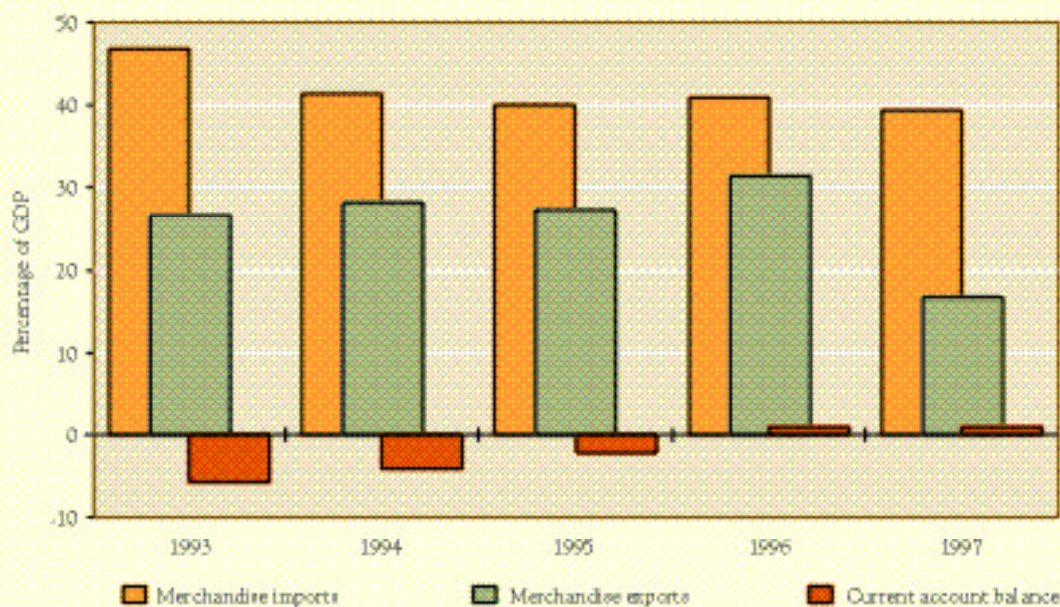
CRITICAL ISSUES IN SHORT-TERM ECONOMIC MANAGEMENT

The 1998 Budget Address, delivered in November 1997, emphasized the government's efforts to adopt financial management policies that are consistent with promoting economic growth. This is to be achieved by consolidating revenue collection—

including improving tax compliance and reducing concessions and exemptions—and by controlling operating expenditures. Revenues are projected to grow in 1998, with half of the growth expected from the sale of government assets. Total expenditure is to rise only marginally, largely because of the completion of the restructuring program at the National Bank of Fiji in 1997. Capital expenditure is also forecast to increase only slightly, yet operating expenditures will rise to more than 26 percent of GDP. The government needs to adopt bolder reforms for reducing the budget deficit and debt levels, and to focus government expenditure on areas that encourage growth and development. Consistent fiscal policies would also help increase private sector investment levels.

In the near future the government will need to direct major efforts toward controlling inflationary pressures resulting from the devaluation. The government promised to exercise monetary policy with a view to containing inflation, and urged that productivity increases should be the only consideration in negotiating wage increases. The prices of

Figure 2.13 Exports, imports, and the Current Account Balance:
Fiji, 1993-1997



Source: Supplement to the 1998 Budget Address.

many consumer items are now rising. With one in four households below the poverty line, the price increases of basic food items are a particular concern.

The Asian crisis will affect Fiji indirectly by dampening growth prospects in its main export markets, and by strengthening competitiveness effects on the tourism and garment industries. Global trade liberalization policies are likely to have an adverse effect on exports under preferential trade arrangements, such as the South Pacific Regional Trade and Economic Cooperation Agreement and the Sugar Protocol under the Lomé Convention of the European Union. The implementation of structural adjustment policies and more effective utilization of resources is therefore crucial for achieving sustainable growth rates in the short to medium term.

POLICY AND DEVELOPMENT ISSUES

Land tenure issues relating to the expiration and renewal of sugar land leases are proving to be a major problem in Fiji. During the period 1997-2005, some 5,345 leases are due to expire. The National Land Trust Board has indicated that most of the landowners want the sugar land back from the lessees to grow sugar themselves, because they think that their returns will be higher than what they would obtain by leasing the land to others. The authorities are developing proposals for more flexible leases in the future that will help avoid the current bunching problem and that can provide more secure tenure. However, they do not appear to be working on policy measures to resolve the problem of a possible displacement of a large number of leaseholders during a short period.

Land tenure and the protection of property rights are also major issues for foreign investors, particularly those with large-scale investments as in the

tourist sector. Recent attacks on resorts, disputes with landowners, and perceptions that legal means to redress such problems will be ineffective are important disincentives for foreign investors.

Inconsistencies and uncertainties with respect to government policies discourage private sector investment. The CDF, the government's involvement in the construction of a major new hotel resort, and the escalation of tariff rates in the 1998 budget are important examples of government initiatives that are inconsistent with its stated aim of reducing its level of involvement in the economy. The CDF initiative was incorporated in a supplementary budget in 1997. While the original budget did not consider agricultural development as a central priority, the CDF was subsequently developed and given the status of an essential government activity. The program involves a range of functions, such as research, extension services, marketing, and quality control, which are considered to be government functions essential for supporting economic growth. However, the CDF also involves direct production and investment by government entities, which are inconsistent with the government's stated policy objectives and framework. In addition, critics have raised doubts about the government's ability to follow through on all these activities.

The medium-term economic outlook is not encouraging. The fiscal burden of the National Bank of Fiji's failure and lack of progress in curbing nonessential government expenditures will mean persistent budgetary pressures. Commitments of additional support for the National Bank of Fiji, the possibility of further government support for a major hotel development, and an infrastructure project for the sugar industry will keep pressure on the budget for several years. These pressures suggest that the government is unlikely to achieve its medium-term fiscal target of a balanced budget by 2000.