

## BACKGROUND

The population of the Republic of the Fiji Islands was estimated to be 794,000 in 1999. Almost 54 percent live in rural areas; around 47 percent of the urban population live in the greater Suva area. Fifty percent of the population are indigenous Fiji Islanders and 45 percent are Indo-Fijians. The country's Human Development Index is the second highest amongst PDMCs, reflecting a high literacy rate, high longevity, low infant mortality, and relatively high GDP per capita. The workforce in 1996 totaled 281,000. There are serious skill shortages, however, due to the high level of emigration of skilled persons: around 2 percent of the labor force per year since 1987.

Until 1987, Fiji had a democratic system of government based on the Westminster parliamentary system. Following a military coup in May 1987, Fiji was declared a republic. In 1990, a new constitution was agreed to by the Great Council of Chiefs that guaranteed indigenous Fijians 37 of 70 seats in the House of Representatives, with 27 seats for Indo-Fijians, five for "general electors" and one to represent the island of Rotuma. The British monarch was removed as Head of State and replaced by an appointed President, who has to be a native Fijian. In 1997, a new constitution reduced the number of seats reserved for Fijians from 37 to 23, the number for Indo-Fijians from 27 to 19, and the number for other ethnic groups from five to three. The remaining seats were to be open seats. The President was still to be a native Fijian, but there were no

restrictions on other positions, such as that of prime minister. A period of political instability began in May 2000, when armed rebels took over Parliament in an effort to depose the elected Government, which was led by an Indo-Fijian. An interim Government was appointed, pending new elections.

Eighty three percent of the land is held under "native title", that is, in the collective ownership of indigenous Fijian communities. Around 28 percent of this area is leased, mostly for agricultural purposes. The Government holds title to 9 percent of the land, of which three quarters is leased out. The remaining 8 percent is freehold. Over 90 percent of the sugar crop is produced by Indo-Fijians, usually on land leased from indigenous Fijians. Agricultural leases on communal land began expiring in 1997, with the majority expiring in 2000 and 2001. Rents have been fixed at below market rates, with a substantial share appropriated by the Native Land Trust Board. Landowners are reluctant to renew leases, so that farmers have stopped investing and banks are unwilling to lend until the issue is resolved.

## THE MACROECONOMIC ENVIRONMENT

Fiji has the second largest and the most developed economy of all the PDMCs. The economy is based on tourism, agriculture (predominantly sugar), and fishing, and is therefore vulnerable to external shocks. Services account for over 50 percent of GDP. Agriculture (sugarcane, livestock, forestry, and subsistence) and fishing account for 17 percent of GDP. Sugar is by far the most important crop, generating 36 percent of agricultural GDP in 1999. Sugar processing accounted for 16 percent of manufacturing GDP in 1999.

Between 1994 and 1999, the economy grew at the average annual rate of 3.2 percent. Real growth fell by 0.9 percent in 1997, grew by 1.4 percent in 1998, and increased by a provisional 8.0 percent in 1999 (Table 2.1). The growth fluctuations reflect the disruptions in sugar harvests caused by cyclones, labor disturbances, and the impact of recessions in Australia and New Zealand on tourism. The initial outlook for 2000 was a growth rate of 3–4 percent. Political instability after May caused a revision in the growth projection to –13 percent. The inflation

rate was quite low during the 1990s due to low inflation in trading partners and weak domestic demand, although a 20-percent devaluation of the Fijian dollar (F\$) in 1998 put temporary upward pressure on prices.

Gross domestic investment rose from 12.0 percent of GDP in 1994 to 15.4 percent of GDP in 1998, but still remained low by regional and international standards. Private sector investment in particular was depressed, especially in the agriculture sector. Investor confidence was hit hard by the events of May 2000. To increase investment, the Government operates a number of tax-free factory zones, as well as offering tax holidays for major hotel developments.

The country's modest rate of growth can be attributed to political and economic uncertainties (particularly regarding property rights), emigration of skilled workers, distortion of relative prices through excessive regulation, and a large and inefficient public sector. About 53 percent of the Consumer Price Index (CPI) is subject to price controls, which, along with tax and tariff preferences and Government industrial promotion schemes, have distorted market signals and discouraged both domestic and foreign investment. Although the Government has encouraged the development of the timber industry and investment in manufacturing and tourism, foreign investors have been discouraged from acquiring controlling interests in domestically owned enterprises. Investment and customs regulations also remain cumbersome.

The public sector is estimated to account for around two thirds of output generated in the formal sector. Civil servants account for one quarter of paid employment, and public wage increases have been high relative to output and productivity growth (although wages were cut by 12.5 percent in 2000). The public enterprise sector is also large, with assets estimated at F\$1,715 million in 1998. Of the 30 public enterprises identified in 1997, only three have been privatized to date. These enterprises have earned low rates of return, and confront a number of major problems. The latter include multiple and often conflicting objectives, lack of commercial focus, lack of accountability on performance, Government intervention in decision making, and continued reliance on Government financial support. Most State-owned enterprises are protected

from competition and continue to contribute to crowding out the private sector.

The Government ran budget deficits throughout the 1990s (Table 2.1). While the so-called headline balance moved into surplus in 1998, this reflected substantial asset sales. The real position was that the underlying balance was in deficit of 4.0 percent of GDP, compared with a 1997 underlying deficit of 2.5 percent. The increased deficit resulted from the costs of restructuring the National Bank of Fiji (NBF) and growing interest payments on public debt. The wage bill remained high, and generous tax incentives (such as tax holidays of from eight to 20 years) resulted in low effective tax rates. The underlying fiscal balance improved in 1999, but was expected to deteriorate in 2000 as Government revenue fell short of original estimates.

Monetary policy was progressively eased in the late 1990s in order to stimulate demand. This was an ineffective mechanism, since investment plans were affected predominantly by excessive regulation and the uncertainty regarding agricultural leaseholds and property rights. Despite monetary easing, broad money growth was slow and turned negative in 1997, as private sector credit contracted sharply (Table 2.1). NBF restructuring occurred that year, with NBF liabilities being transferred to the Government. The Government continued to intervene in financial markets by putting controls on interest rates for mortgages to low-income families, which are restricted to 6 percent, even though the cost of funds to the Housing Authority is considerably higher.

The external current account balance improved from a deficit of 3.5 percent of GDP in 1994 to surpluses in 1996, 1997 and 1999 (Table 2.1). This largely reflected higher tourism earnings. The capital account moved into deficit in 1996 and 1997, registered a surplus in 1998, and then recorded a deficit in 1999. The overall balance was in surplus for four of the six years 1994–1999, and import cover of foreign reserves rose from 2.9 to 4.8 months. In mid-2000, monetary policy and capital controls were tightened in order to protect foreign reserves from the effects of political instability. The policy stance and controls were eased in September, as the reserves position became more secure. Although all current account payments are free, limited capital account controls remain. These involve significant compliance costs for business, but are retained as a policy tool.

The Fiji dollar (F\$) is pegged to a weighted basket of currencies including the Australian, New Zealand, and United States dollars, the Japanese yen, and the Euro. Following the coups in May and September 1987, the Fiji dollar was twice devalued. The nominal exchange rate appreciated by close to 10 percent in the period 1990–1995, then was devalued by 20 percent in January 1998. This nominal devaluation was effective in improving the country's international competitiveness: the real effective exchange rate depreciated substantially in 1998, and slightly in 1999 (Table 2.1).

## THE STRUCTURE OF THE FINANCIAL SECTOR AND INSTITUTIONS

The financial system in the Fiji Islands consists of the Reserve Bank of Fiji (RBF); seven commercial banks (two locally incorporated institutions and five branches of foreign banks); and a number of nonbank financial institutions (NBFIs). The latter category includes a superannuation fund (Fiji National Provident Fund [FNPF]), the Fiji Development Bank (FDB), a merchant bank, one credit corporation, two housing finance companies, 39 credit unions, 14 insurance companies and brokers, one investment corporation, and one unit trust. There are also evolving money and securities markets and a stock exchange. Informal financial enterprises also operate.

Banking has a long history in Fiji. The ANZ Bank (a branch of the Australia and New Zealand Banking Group of Australia, [ANZ]), started operating as the Union Bank in 1880, which merged with ANZ in 1955 and became an Australian bank in 1977. In 1990, it acquired the business of the Bank of New Zealand in Fiji. Westpac (a branch of the Westpac Banking Corporation), started its operations in Fiji in 1901 as the Bank of New South Wales. The Government-owned National Bank of Fiji (NBF) started operations in 1974, when the Savings Bank of Fiji was converted into a commercial bank. NBF was reported to be insolvent in 1995 and was restructured in 1996/97. An Asset Management Bank was set up in 1997 to try to recover some of NBF's debts. In 1998, the Government sold 51 percent of its share of NBF to Colonial National Bank (CNB), which is part of the Colonial financial conglomerate; and announced its intention to sell a further 20 percent of the shares of NBF to the public.

**Table 2.1**  
**Macroeconomic Indicators for Fiji Islands, 1994–1999**

|  | 1994                    | 1995    | 1996    | 1997    | 1998    | 1999    |
|--|-------------------------|---------|---------|---------|---------|---------|
| <b>Output and inflation</b>                |                         |         |         |         |         |         |
|  | (in percent)            |         |         |         |         |         |
| Real GDP growth (factor cost)              | 5.1                     | 2.5     | 3.1     | -0.9    | 1.4     | 8.0     |
| Sugar Production                           | 21.0                    | -15.8   | -0.3    | -20.5   | -22.0   | -33.0   |
| Change in CPI (end period)                 | 1.2                     | 2.2     | 2.4     | 2.9     | 8.1     | 0.2     |
| Change in CPI (period average)             | 0.6                     | 2.2     | 3.1     | 3.4     | 5.7     | 2.0     |
| Gross Domestic Saving/GDP                  | 12.7                    | 13.0    | 15.5    | 15.9    | 15.7    | —       |
| Gross Domestic Investment/GDP              | 12.0                    | 12.5    | 10.0    | 10.1    | 15.4    | 11.0    |
| Foreign Saving/GDP                         | 3.5                     | 0.9     | -2.9    | -0.2    | 1.6     | -1.0    |
| <b>Money and Credit</b>                    |                         |         |         |         |         |         |
|  | (annual percent change) |         |         |         |         |         |
| Net foreign assets                         | -13.8                   | 21.9    | 13.4    | -4.1    | 57.7    | 12.2    |
| Total domestic credit                      | 4.0                     | 1.0     | 4.1     | -10.1   | -5.4    | 1.3     |
| Private sector credit                      | 8.7                     | 2.9     | 4.7     | -13.0   | -4.9    | 3.4     |
| Broad money                                | 0.1                     | 4.3     | 0.9     | -8.7    | -0.3    | 14.2    |
| <b>Central Government</b>                  |                         |         |         |         |         |         |
|  | (percent of GDP)        |         |         |         |         |         |
| Total Revenue and Grants                   | 26.2                    | 25.8    | 25.1    | 26.5    | 35.0    | 27.8    |
| o/w Grants                                 | 0.2                     | 0.2     | 0.2     | 0.2     | 0.1     | 0.04    |
| o/w Privatization                          | 0.0                     | 0.0     | 0.0     | 0.0     | 8.6     | 0.6     |
| Total Expenditure                          | 30.2                    | 29.1    | 32.3    | 35.7    | 38.2    | 33.9    |
| Current expenditure                        | 24.4                    | 24.7    | 23.9    | 25.4    | 31.6    | 27.7    |
| o/w Wages and Salaries                     | 11.1                    | 11.7    | 11.0    | 11.7    | 11.7    | 11.3    |
| o/w Subsidies                              | 4.0                     | 3.9     | 3.9     | 3.8     | 4.3     | 4.9     |
| Capital Expenditure                        | 3.2                     | 2.8     | 6.9     | 8.5     | 4.4     | 4.6     |
| o/w NBF Restructuring                      | 0.0                     | 0.0     | 2.7     | 4.0     | 0.0     | 0.0     |
| Overall balance <sup>a</sup>               | -1.5                    | -0.6    | -5.0    | -6.6    | 4.6     | -0.7    |
| <b>Balance of Payments (F\$ million)</b>   |                         |         |         |         |         |         |
| Exports, f.o.b.                            | 727.0                   | 740.8   | 913.6   | 803.8   | 839.5   | 1,051.6 |
| Imports, f.o.b.                            | 1,053.7                 | 1,070.8 | 1,179.5 | 1,182.2 | 1,221.0 | 1,286.0 |
| Private remittances                        | -34.8                   | -37.2   | -42.7   | -16.5   | -13.9   | -21.1   |
| Official transfers                         | 105.0                   | 163.5   | 155.4   | 121.5   | 195.0   | 114.4   |
| Current Account                            |                         |         |         |         |         |         |
| (including official transfers)             | -92.3                   | -26.2   | 87.6    | 49.0    | -11.9   | 54.7    |
| (In percent of GDP)                        | -3.5                    | -0.9    | 3.0     | 1.6     | -0.4    | 1.5     |
| Capital Account                            |                         |         |         |         |         |         |
| (excluding reserves)                       | 40.6                    | 101.2   | -4.8    | -28.5   | 101.5   | -56.5   |
| Errors and Omissions                       | 35.1                    | 34.0    | 14.6    | -60.8   | -22.7   | 60.4    |
| Overall Balance                            | -16.6                   | 109.0   | 97.4    | -40.3   | 66.9    | 58.6    |
| Gross Official Reserves                    | 384.7                   | 498.4   | 590.6   | 557.9   | 764.7   | 827.0   |
| (in months of imports of goods & services) | 2.9                     | 3.7     | 4.0     | 3.8     | 4.8     | 4.8     |
| External debt (F\$ million)                |                         |         |         |         |         |         |
| (eop) <sup>b</sup>                         | 399                     | 385     | 354     | 352     | 447     | 514     |
| (In percent of GDP)                        | 15.0                    | 13.8    | 11.9    | 11.6    | 13.7    | 14.3    |
| Real Effective Exchange Rate <sup>c</sup>  | 115.1                   | 114.8   | 114.2   | 115.6   | 99.0    | 97.6    |
| F\$ per US\$ (end period)                  | 1.41                    | 1.43    | 1.38    | 1.55    | 1.99    | 1.97    |

— Not available.

a. Including restructuring costs and privatization receipts.

b. As at June 1999.

c. Period average.

Sources: Ministry of Finance and Ministry of Planning 1999; RBF 1998, 1999.

The Bank of Baroda started operations in 1961, the Habib Bank in 1991, and the Bank of Hawaii in 1993.

NBFIs play an important role in the mobilization of savings and are important institutional investors. FDB started its operations in 1967 with the provisions of the Fiji Development Bank Act, and FNPF was founded in 1966; FDB is Government owned and FNPF is a statutory organization. The Housing Authority and the Unit Trust of Fiji (UTF) (also both Government owned) are also defined as NBFIs. Of the 10 insurance companies licensed under the Insurance Act of 1998, eight sell general insurance and two sell life insurance. Colonial Insurance is the largest insurance company. Credit unions operate under a new Credit Union Act 1999, which protects the interests and funds of individual members and provides prudential and reporting guidelines.

RBF performs the regular central banking functions, including the issuance of currency, the formulation and implementation of monetary policy, the management of foreign exchange reserves, and prudential supervision. RBF derives its powers for prudential regulation from the Reserve Bank of Fiji Act and the Banking Act 1995; these include powers to license and terminate operations of financial institutions. RBF supervises the banking and insurance industry, and those credit institutions authorized to accept deposits. Otherwise, supervision is done by the Ministry of Finance.

To carry out the interbank payments system, a different bank is nominated each week as the clearing bank. All checks are listed and lodged twice daily at the clearing bank; the balances are provided to RBF, which updates the central bank accounts at the end of each day. There are then two full days during which checks are subject to recourse. Checks are therefore not fully cleared until day 4. There has been some discussion about printing optical recognition characters on checks. There is no high value payment system, although the banks will provide special clearance at a bank for a fee.

The commercial banks are considering installing automation systems, but at the moment even their automatic teller machines (ATMs) do not link. There is no electronic linkage between the banks and RBF.

The Fiji Islands has the widest range of financial institutions of all PDMCs, although it is still quite shallow, in the sense that there are only a few institutions in each category. As in other PDMCs, the urban areas are provided with much better banking facilities than the rural areas, where there is less access to banking facilities or services. In 1997, there was one branch or agency for every 6,010 people. This represents a considerable decline since 1994, when there was one branch or agency for every 3,835 people, and is mainly accounted for by the reduction in the number of branch agencies of FNB from 124 in 1994 to 66 in 1997.

The assets of the seven commercial banks constituted 31 percent of the F\$6,421.9 million total assets of the financial sector as at October 1999 (Table 2.2). ANZ is the largest of the commercial banks, with 12.3 percent of the total assets of the financial system, followed by Westpac (7.4 percent) and CNB (3.7 percent).

FNPF is the largest asset holder, with almost 34 percent of the total assets of the financial system as at December 1999. Because of portfolio diversification restrictions related to trustee requirements and FNPF's investment limits abroad,<sup>3</sup> 62 percent of FNPF's investments were in Government securities (mostly Government bonds), most of which it holds to maturity. This has prevented an active bond market in Government securities from developing. In early 2000, however, RBF was moving toward relaxing capital and foreign exchange controls, though the events of May caused the temporary tightening of controls referred to above.

FDB is the principal development finance institution (DFI) in the Fiji Islands. There are also 52 active and 15 dormant credit unions registered with the Registrar of Credit Unions.

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<sup>3</sup> As of 1 January 2000, FNPF is permitted to invest F\$50 million annually in offshore investments; RBF approval is still required.

**Table 2.2**  
**Total Assets/Liabilities of the Financial Sector, 1994–1999**

|                                       | 1994  | 1995       | 1996       | 1997       | 1998       | 1999       |
|---------------------------------------|---|------------|------------|------------|------------|------------|
|                                       | (in percentage of Total Assets/Liabilities) |            |            |            |            |            |
| Reserve Bank of Fiji                  | 11.2  | 12.5       | 12.4       | 12.4       | 15.2       | 16.4       |
| <b>Commercial Banks</b>               | 37.1  | 35.1       | 31.8       | 32.9       | 30.2       | 30.8       |
| National Bank of Fiji/Colonial        |   |            |            |            |            |            |
| National Bank                         | 11.5  | 11.0       | 3.5        | 2.5        | 2.8        | 3.7        |
| ANZ BankGroup Ltd                     | 11.9  | 11.8       | 12.0       | 13.9       | 12.9       | 12.3       |
| Westpac Banking Corp.                 | 9.6   | 8.1        | 7.6        | 8.1        | 7.5        | 7.4        |
| Bank of Hawaii                        | 0.5   | 1.1        | 1.8        | 2.5        | 2.5        | 3.2        |
| Habib Bank Ltd                        | 0.3   | 0.3        | 0.3        | 0.2        | 0.5        | 0.6        |
| Bank of Baroda Ltd                    | 3.2   | 2.8        | 2.4        | 2.5        | 2.7        | 2.8        |
| NBF Asset Management Bank             | 0.0   | 0.0        | 4.2        | 3.1        | 1.4        | 0.8        |
| <b>Nonbank Financial Institutions</b> | 43.5  | 42.8       | 46.8       | 45.3       | 45.5       | 46.5       |
| Fiji Development Bank                 | 6.4   | 6.6        | 6.2        | 6.6        | 6.0        | 5.7        |
| Fiji National Provident Fund          | 31.5  | 31.3       | 30.4       | 34.6       | 35.1       | 33.9       |
| Others <sup>a</sup>                   | 5.6   | 4.9        | 10.2       | 4.0        | 4.4        | 3.4        |
| <b>Other Financial Institutions</b>   | <b>8.3</b>                                  | <b>9.6</b> | <b>9.1</b> | <b>9.5</b> | <b>9.0</b> | <b>9.8</b> |
| Insurance Companies                   | 7.0   | 7.1        | 6.7        | 6.8        | 6.3        | 6.7        |
| Credit Institutions <sup>b</sup>      | 1.3   | 2.5        | 2.5        | 2.7        | 2.7        | 3.1        |

a. Includes Housing Authority, Unit Trust of Fiji, National MBf Finance (Fiji) Limited.

b. Merchant Bank of Fiji, Credit Corporation (Fiji) Limited and Home Finance Company Limited.

Source: Reserve Bank of Fiji 1998, 1999.

## PERFORMANCE OF COMMERCIAL BANKS

Total lending by commercial banks in 1999 was F\$1,174.4 million. Table 2.3 shows the breakdown by lending category: the largest was private individuals, followed by wholesale and retail trade and manufacturing. The agriculture sector received just 3.5 percent of the total loan amount. At the end of 1999, ANZ and Westpac accounted for 63.6 percent of total deposits and 69.8 percent of total loans in the banking sector.

CNB is the major retail bank and is increasing its retail base at the expense of the other banks. At the end of 1999, it had some 15,000 resident shareholders and assets of F\$239 million. This is seen as a strong base on which to cross-market its other services. The bank has 19 branches and 66 postal agencies

**Table 2.3**  
**Bank Loans by Sector, 1999**

| Sector                                   | F\$ millions | Percent |
|--|--------------|---------|
| Agriculture                              | 41.5         | 3.5     |
| Manufacturing                            | 145.7        | 12.4    |
| Wholesale/Retail                         | 356.3        | 30.3    |
| Private Individuals                      | 366.5        | 31.2    |
| Building Construction and<br>Real Estate | 69.3         | 5.9     |
| Business Services                        | 54.6         | 4.6     |
| Others                                   | 140.5        | 12.0    |
| TOTAL                                    | 1,174.4      | 99.9    |

Source: RBF 1999.

throughout the Fiji Islands and is the best placed of all the financial institutions to service the rural areas.

Interest rate spreads, interest margins, and returns on equity of commercial banks in 1997 are shown in Table 2.4. In contrast to these numbers, the then Government-owned NBF earned negative returns on equity of -92 percent in 1994 and -67 percent in 1995. Restructuring improved the outcome to a -11 percent return on equity in 1997.

The profitability of the well-managed foreign commercial banks has been perceived as high. A 1999 Committee of Inquiry into Financial Services examined the profitability of foreign commercial banks in the Fiji Islands and made comparisons with the banks' global operations. The results are presented in Table 2.5. Even allowing that variations in accounting policies and reporting requirements made direct comparisons difficult, the Committee concluded that ANZ, Westpac, Bank of Hawaii, and Bank of Baroda were earning relatively high rates of return in the Fiji Islands, and that the high returns were due largely, if not exclusively, to a lack of competitiveness in the industry. The Committee accordingly recommended that Government pursue means of fostering competition.

The Government subsequently requested the Prices and Incomes Board to examine commercial banks' fees and charges.

**Table 2.4****Return on Equity, Interest Spreads, and Interest Margins for Commercial Banks, 1997**

| <b>Bank</b>    | <b>Return on Equity</b><br>percent | <b>Interest Spread</b><br>percent | <b>Interest Margin</b><br>percent |
|----------------|------------------------------------|-----------------------------------|-----------------------------------|
| ANZ            | 27.0                               | 5.6                               | 5.7                               |
| Bank of Baroda | 26.0                               | 4.7                               | 4.7                               |
| Bank of Hawaii | 45.3                               | 4.1                               | 3.7                               |
| Habib Bank     | 5.2                                | 5.9                               | 5.2                               |
| Westpac        | 27.7                               | 5.2                               | 5.1                               |

Source: Bank Annual Reports, 1998.

**Table 2.5****Comparisons of Return on Equity on Fiji Operations compared to Global Operations, 1993–1997**  
(percent)

| <b>Year</b> | <b>ANZ</b> |        | <b>Baroda</b> |        | <b>Habib</b> |        | <b>Hawaii</b> |        | <b>Westpac</b> |        |
|-------------|------------|--------|---------------|--------|--------------|--------|---------------|--------|----------------|--------|
|             | Fiji       | Global | Fiji          | Global | Fiji         | Global | Fiji          | Global | Fiji           | Global |
| 1993        | 18.8       | 5.1    | —             | —      | 11.9         | 3.1    | —             | 14.9   | —              | 0.6    |
| 1994        | 21.8       | 15.5   | —             | —      | 3.9          | 3.3    | -64.0         | 12.1   | —              | 9.6    |
| 1995        | 24.2       | 19.8   | —             | 4.2    | 23.3         | 5.7    | 9.0           | 11.9   | 13.0           | 12.7   |
| 1996        | 22.9       | 18.6   | 51.5          | 12.3   | -8.7         | -59.1  | -16.0         | 12.4   | 23.0           | 14.6   |
| 1997        | 27.0       | 15.8   | 26.0          | 14.9   | 5.2          | —      | 27.1          | 12.6   | 28.0           | 16.0   |

— Not available.

Source: Ministry of Finance 1999.

The Board inquiry generated a recommendation that a Banking Commission be established independently of the RBF, with the mandate to oversee all financial institutions, and specifically to monitor the level of bank fees, charges, and interest rates. Banks would be required to justify any increases that the Commission considered excessive. There was a related proposal for a Banking Ombudsman to be appointed to "resolve disputes between banks, insurance companies, credit unions and other finance sectors

and their consumers." The foreign commercial banks continued to argue that profitability in terms of foreign currency return to their shareholders was in fact much lower than the Fiji dollar return, and that increased regulation was not required and would exacerbate already severe relative price distortions. Nonetheless, situations of imperfect competition may call for design and implementation of appropriate regulations, bearing in mind that Government failure, as well as market failure, can be a problem.

## FINANCIAL DEEPENING AND INTERMEDIATION

The ratios for financial deepening show that a reversal occurred during the 1990s, which was due to NBF restructuring in 1996 and 1997, the sharp contraction of private sector credit growth in the 1997 recession, and low and declining deposit rates attributable to increasing liquidity. The ratio of narrow money to GDP grew from 19.2 percent of GDP in 1994 to 33.7 percent of GDP in 1999, while the ratio of broad money to GDP fell from 78.8 percent to 75.1 percent of GDP (Table 2.6). The latter decline was attributable to a drop in time deposits from F\$770.5 million in 1994 to F\$418.5 million in 1999. The ratio of broad money to GDP was high compared to other PDMCs, but was low compared with countries with more developed financial sectors. The deterioration in financial deepening was also evident in the ratio of quasi money to broad money, which demonstrates the willingness of savers to use the banking system to save their money. This ratio fell from 75.6 percent in 1994 to 55.1 percent in 1999.

Total domestic credit accounted for 62.8 percent of total banking sector assets in 1998, down from 73 percent in 1994. The statistic shows the considerable liquidity in the financial system that is available for bankable projects. However, sufficient effective demand for funds was not forthcoming: loans to the private sector fell from 60.2 percent of GDP in 1994 to 48.4 percent in 1999 (Table 2.6).

Interest rates on both time deposits and lending fell over the period 1994 to 1999. Rates on time deposits fell from a weighted average of 6.8 percent to one of 2.9 percent, or in real terms from a weighted average of 6.2 percent to one of 0.9

percent. The average lending rate fell from 11.3 percent to 8.5 percent over the same period, and in real terms from 10.7 percent to 6.5 percent over the period. The spread between average deposit and average lending rates widened from 4.6 percent in 1994 to 5.6 percent in 1999 (Table 2.7).

Except in 1998, both savings and lending rates remained positive in real terms. There were signs that interest rates on housing loans were beginning to fall, with interest rates for commercial bank housing loans falling to 8.3 percent in 1999 from 9.0 percent the previous year. With no secondary market for Government bonds, an inactive stock exchange, and an underdeveloped real estate market, the public has no option but to hold savings deposits. These factors have helped keep deposit rates low.

There is a large degree of excess liquidity in Fiji's banking system, as measured by the gap between broad money as a percentage of GDP (which measures the amount of liquidity available) and the ratio of domestic credit to GDP (which measures the number of bankable projects in the economy). This measurement reached 19.8 percent in 1999, one of the highest for PDMCs. Restrictions on foreign exchange have been partly responsible for the high degree of liquidity. Measures by RBF to preserve foreign exchange reserves have prevented FNPF from investing part of its portfolio abroad, and it is difficult for FNPF to find investments locally, so that a lot of the funds are invested in RBF notes, Government instruments, and commercial bank deposits. This can be quite destabilizing for the banking system, especially because there is uncertainty about when large deposits will be put into or taken out of the banking system. However, foreign exchange controls have been gradually relaxed, with the exception of the tightening of capital controls in May–September 2000 referred to above.

High levels of liquidity also reflect the scarcity of bankable projects. The land tenure system, and especially the problems with sugarcane farm leases, has made it more difficult for banks to lend using land or leases as collateral. In addition, the lack of bankable projects at a reasonable risk, the high default rate, and the difficulty in using the legal system for collecting on nonperforming loans add to the high level of liquidity.

**Table 2.6**  
**Financial Intermediation Statistics, 1994–1999**

|  | 1994                | 1995    | 1996    | 1997    | 1998   | 1999    |
|--|---------------------|---------|---------|---------|--------|---------|
|  | (F\$ million)       |         |         |         |        |         |
| Money Supply (M2)                            | 1,414.4             | 1,475.7 | 1,488.3 | 1,358.5 | 1353.8 | 1,546.1 |
| Narrow Money (M1)                            | 344.6               | 386.2   | 456.3   | 445.3   | 493.9  | 694.5   |
| Currency (outside banks)                     | 115.6               | 117.8   | 125.4   | 134.0   | 159.8  | 189.9   |
| Demand Deposits                              | 216.0               | 257.0   | 319.5   | 300.8   | 321.1  | 482.1   |
| Quasi Money                                  | 1,069.7             | 1,089.6 | 1,032.1 | 913.2   | 859.9  | 851.6   |
| Savings Deposits                             | 299.3               | 310.8   | 334.6   | 352.1   | 394.0  | 433.2   |
| Time Deposits                                | 770.5               | 778.8   | 697.4   | 561.1   | 465.9  | 418.5   |
|  | (in percent)        |         |         |         |        |         |
| Growth of Demand Deposits                    |                     | 19.0    | 24.3    | -5.9    | 6.7    | 50.2    |
| Growth of Time Deposits                      |                     | -1.1    | -10.4   | -19.5   | -17.0  | -10.2   |
|  | (in percent of GDP) |         |         |         |        |         |
| Currency                                     | 6.4                 | 6.4     | 6.6     | 7.1     | 8.4    | 9.2     |
| Demand Deposits                              | 12.0                | 14.0    | 16.9    | 16.0    | 16.8   | 23.4    |
| Time Deposits                                | 42.9                | 42.4    | 36.8    | 29.9    | 24.4   | 20.3    |
| Narrow Money                                 | 19.2                | 21.0    | 24.1    | 23.7    | 25.9   | 33.7    |
| Broad Money                                  | 78.8                | 80.3    | 78.5    | 72.3    | 71.0   | 75.1    |
|  | (in percent)        |         |         |         |        |         |
| Private Sector Credit<br>(% of GDP)          | 60.2                | 60.5    | 61.5    | 54.0    | 50.6   | 48.4    |
| Private Sector Credit<br>(% of total credit) | 86.0                | 87.7    | 88.2    | 85.4    | 85.8   | 87.5    |
| Currency (% of broad money)                  | 8.2                 | 8.0     | 8.4     | 9.9     | 11.8   | 12.3    |
| Narrow Money (% of<br>broad money)           | 24.4                | 26.2    | 30.7    | 32.8    | 36.5   | 44.9    |
| Quasi Money (% of<br>broad money)            | 75.6                | 73.8    | 69.3    | 67.2    | 63.5   | 55.1    |
| Demand Deposits<br>(% of narrow money)       | 62.7                | 66.6    | 70.0    | 67.5    | 65.0   | 69.4    |
| Total Domestic Credit/<br>Banking Assets     | 75.3                | 71.2    | 70.5    | 68.9    | 62.8   | 54.7    |
| Currency in circulation<br>per capita (F\$)  | 152.3               | 153.3   | 161.8   | 171.5   | 200.2  | 233.8   |

Source: RBF 1999.

**Table 2.7**  
**Nominal and Real Savings and Lending Rates**

|      | Weighted<br>Average<br>Time<br>Deposit<br>Rates | Average<br>Lending<br>Rates | Inflation<br>Rate | Real<br>Weighted<br>Average<br>Deposit<br>Rates | Real<br>Weighted<br>Average<br>Lending<br>Rates | Nominal<br>Interest<br>Spread |
|------|---|-----------------------------|-------------------|---|---|-------------------------------|
| 1994 | 6.70  | 11.29                       | 1.2               | 5.5   | 10.1  | 4.6                           |
| 1995 | 6.78  | 11.10                       | 2.2               | 4.6   | 8.9   | 4.3                           |
| 1996 | 5.77  | 11.57                       | 2.4               | 3.4   | 9.2   | 5.8                           |
| 1997 | 5.18  | 10.17                       | 2.9               | 2.3   | 7.3   | 5.0                           |
| 1998 | 4.01  | 9.11                        | 8.1               | -4.1  | 1.0   | 5.1                           |
| 1999 | 2.88  | 8.47                        | 0.2               | 2.7   | 8.3   | 5.6                           |

Source: RBF 1999.

## COMPETITION<sup>4</sup>

Although there are seven main trading banks in the Fiji Islands, the banking sector is highly concentrated. At the end of 1998, ANZ and Westpac accounted for around 69 percent of total deposits and 69 percent of total loans in the banking sector. Foreign banks naturally focus on profit in their own currencies and have little interest in localizing their operations.

There is little price competition, especially on the deposit side, because of the high level of liquidity in the financial system. However, there is price discounting in the form of exemption from fees; and there also seems to be diversity in pricing on deposit accounts. There is little evidence of price fixing or market sharing. Nonprice competition seems to be the main arena. Although it has been suggested that even nonprice competition declined in the late 1990s, with the quality of services worsening, the introduction of electronic banking in different forms and other types of product innovation suggest some degree of dynamic efficiency in the banking sector.

<sup>4</sup> This section draws heavily on Ministry of Finance 1999.

The nonbank sector does not appear to be capable of providing effective competition to banks in most deposit-related products. However, in certain loan products such as housing and vehicle loans, leasing, and agricultural loans, NBFIs do provide some competitive pressure. FDB, with its small share of the market, cannot compete with the large foreign banks.

The lack of a fully functioning money market—especially a secondary market, the small number of traded securities, the small capital market, and FNPF's large holdings of Government bonds—means that people have few alternatives to bank deposits for savings. The lack of such a market to soak up high liquidity also impedes competition.

Historically, however, there has been successful entry into and exit from the banking industry, which has been facilitated by RBF's licensing policy. Entry has occurred despite the relatively high fixed costs of setting up in a small market dominated by two banks and the length of time needed to build up business. The opening up of 12 foreign exchange dealerships has markedly increased competition in foreign exchange transactions. Growth in the economy would increase the demand for financial services and encourage the development of financial markets. This could encourage other banks to enter the market.

## **NONBANK FINANCIAL INSTITUTIONS (NBFIS)**

### **Fiji National Provident Fund**

The Fiji National Provident Fund (FNPF) is a statutory corporation. Its board is appointed by the Minister of Finance, and consists of the Permanent Secretary from the Ministry of Employment, two employer representatives, and two employee representatives.

FNPF receives approximately F\$14 million per month in contributions. Employers are required to pay an amount equal to 16 percent of their employees' salaries to FNPF, 8 percent of which they may deduct from their employees' salaries. All contributions are added to members', i.e., employees', balances. Members may take an interest-free loan against contributions to buy a house, which must be repaid only if the house is sold.

They may withdraw money for education and medical expenses, subject to certain prudential limits. They may also use funds as equity for starting a small business: for example, they may use their FNPf funds for up to 50 percent of required equity capital. Finally, members may withdraw up to F\$2,000 to invest in the Unit Trust of Fiji. At the time of writing, there was a proposal before the Government that would permit members to buy shares directly. On reaching retirement age (55), members can take a lump sum, a pension, or a combination of both. The entire balance is also payable: (i) on the death of a member (the funds are paid to the beneficiaries); (ii) if a member is declared medically unfit for work; or (iii) if a member permanently migrates (acquires a permanent residence visa from some other country).

FNPf investments are made under the Trustee Act. An Investment Policy Committee (a subcommittee of the board) establishes the investment policy. The policy permits investments in commercial bank deposits, Government securities, semi-Government securities, listed securities with a minimum capitalization of F\$2 million and a record of dividend payments for the previous five years, and unlisted securities. For the latter type of investment, FNPf must have the approval of the Attorney General, who must declare the security to be a "trustee" investment. This mechanism has been used to permit FNPf to invest in Amalgamated Telecom Holdings Ltd (ATHL) and Home Finance.<sup>5</sup> Offshore investments are limited to Australia, Canada, Japan, New Zealand, and United Kingdom, but may be expanded in the future.<sup>6</sup> FNPf also has substantial property investments, especially in Suva.

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<sup>5</sup> FNPf also invests in unlisted securities through the Kula Fund, a regional venture capital fund operated by Commonwealth Development Corporation, ADB, IFC, EIB, and regional governments. Although the original intention was to bring securities to listing, this is difficult, as company owners sometimes do not wish to list or may prefer to list on an overseas exchange rather than the Suva exchange.

<sup>6</sup> FNPf invests around F\$50 million abroad, or approximately 10 percent of its portfolio. When investing abroad, FNPf has to take into account the foreign exchange exposure and, as the range of countries in which it can invest is increased, plans to appoint a global asset manager.

In late 1998, FNPF bought 51 percent of ATHL from the Government. Although the sale was by tender, and a commercial bank made a bid, it has been suggested that FNPF paid a much higher price for the securities than was justified, thus distorting the market price. If a tranche of shares were offered to the general public, it would be difficult to make the offer at a significant discount to the price paid by FNPF, as this would reduce the value of FNPF's holdings. However, if the offer price were not attractive to other investors, then the issue would fail, with consequent adverse effects on market development. This outcome could sour the investment climate for many years. The banking sector contends that FNPF is able to engage in transactions like the ATHL share purchase because of its monopoly position, its freedom from taxation, and the relative lack of a full commercial focus in its operations.

FNPF's investment in domestic equities is limited at present to 15 percent of its total portfolio. With the investment in ATHL, the 15 percent has been slightly exceeded. As a result of this constraint and the limits on overseas investment, much of FNPF's portfolio is liquid instruments. The sheer size of these holdings creates distortions in financial markets. FNPF would like to invest in new projects, such as tourist developments, but cannot do so under the Trustee Act. A new act before Parliament may extend the permissible range of investments.

The general consensus among other financial institutions is that:

- (i) FNPF deposits in the banking system create instability, because they are very large and can be moved on little or no notice;
- (ii) FNPF is the largest buyer and holder of Government securities, and as it pays no tax, it distorts the entire interest rate structure;
- (iii) FNPF acts in effect as a lender of last resort to the Government; and
- (iv) the level of compulsory savings distorts the intermediation process.

Most financial institutions would like to see the investment arm of FNPF broken up into smaller units and private sector

entities given an opportunity either to manage a portion of the funds or to develop competing products.

### **Fiji Development Bank**

The Fiji Development Bank (FDB) is the principal DFI in the Fiji Islands. Total assets of FDB as at 30 June 1999 stood at F\$364 million, with a total gross loan portfolio of F\$353 million. Compared to other development banks in PDMCs, FDB is more mature in terms of size and infrastructure. It has 10 branches in the main provincial centers, each of which is run as a profit center. The branches are grouped into Western, Northern, and Suva regions. Within the Suva region, there is a further separation into agriculture, industrial, and commercial. A special loans scheme is also run out of Suva. Information systems provide detailed branch and portfolio breakdowns.

FDB's profitability has been declining since 1995, as table 2.8 shows. A major reason for this is the relatively high cost of funds, which leads to a very narrow interest spread of 1.96 percent. This compares with interest spreads of 8 or 9 percent for other development banks in the region. With such narrow interest margins, FDB has had to operate extremely efficiently, as indicated by operating costs of 1.6 percent of average assets. Nonetheless, the number of loan approvals fell from 2,866 in 1995 to 1,007 in 1999.

The high cost of funding in large part is due to the fact that the FDB has had to obtain most of its funding from the market through the issuing of long-term bonds and promissory notes, which are guaranteed by the Government. As at 30 June 1999, long-term bonds on issue stood at F\$248 million and promissory notes at F\$17 million. The bonds were offered by tender to financial institutions for terms of three, five and seven years. The FDB has an application before RBF to accept term deposits from the general public. If approval is given, FDB would then come under RBF's supervision regime.

Lending by FDB represents approximately 25 percent of the total lending of the financial sector. Around 25 percent of FDB's total lending portfolio is to the agriculture sector, making FDB the major lender to agriculture, accounting for 67 percent of total agricultural loans. FDB also has a major presence in

Table 2.8

## Performance of Fiji Development Bank

|                              | 1995    | 1996    | 1997    | 1998    | 1999    |
|------------------------------|---------|---------|---------|---------|---------|
| <b>Financial Performance</b> |         |         |         |         |         |
| Net Profits (F\$'000)        | 1,857   | 302     | 522     | 316     | 106     |
| Total Assets (F\$'000)       | 326,270 | 343,658 | 356,014 | 356,393 | 363,993 |
| Profit (Loss) / Average      |         |         |         |         |         |
| Equity                       | 2.75    | 0.42    | 0.72    | 0.43    | 0.14    |
| Interest Spread (%)          | 2.47    | 2.36    | 2.08    | 1.82    | 1.96    |
| Earnings Spread              | 3.14    | 3.06    | 2.70    | 2.46    | 2.61    |
| <b>Lending Performance</b>   |         |         |         |         |         |
| Approvals (Number)           | 2,866   | 1,817   | 1,428   | 1,365   | 1       |
| Loan Portfolio (Number)      | 10,944  | 8,910   | 7,829   | 7,226   | 7,271   |
| Gross Loan Portfolio (F\$ m) | 324.0   | 336.6   | 344.4   | 346.4   | 352.6   |
| Growth in Loan Portfolio (%) | 8.8     | 1.6     | 2.2     | 0.7     | 1.8     |
| Arrears/Loan Portfolio       | 12.5    | 9.3     | 10.1    | 10.0    | 7.69    |

Source: FDB 1999.

building and construction, hotels, and tourism-related industries (Table 2.9).

FDB operates an indigenous loan scheme for Fijians, Rotumans, and eligible general electors. Lending under this scheme currently stands at F\$77 million. At present, the Government is moving to alter the rules of this scheme so that it is available to all Fiji Islanders. The New Zealand Small Loans Scheme is also run through the FDB; the scheme was established in 1989 with the objective of providing soft loans for establishing income-generating projects. The portfolio for this scheme currently stands at F\$440,000.

FDB has been reducing its exposure to the agricultural sector and has been increasing its exposure to commercial lending. In addition, it has diversified its lending by moving into leasing products. This type of financing is quite different from normal development bank lending and requires a different way of operating. The leasing is apparently operated as a stand-alone unit, is run on strictly commercial lines, and is operating profitably. A further diversification of FDB's lending is its equity investment scheme, which provides for FDB to invest equity in

new and existing enterprises. Equity investments of this type now stand at F\$13.2 million. FDB intends to reduce its exposure in this area.

FDB has strengthened its corporate planning and information management areas, with the introduction during 1999 of a new loans system and the completion of a second corporate plan. The information systems provide management with detailed information on each area of operations. The main areas where information could be enhanced are product and customer profitability.

FDB operates under the Fiji Development Act. Should the FDB receive approval to receive retail deposits, the act will need amending to ensure that depositors' rights are protected. A key governance issue is the significant involvement by the Government in the appointment of the FDB board, which consists of eight members, only two of whom represent the public sector. In 2000, the entire Board was replaced on the grounds of nonperformance. Two members who refused to resign challenged the decision through the courts. New board members have close connections to the Government. The Government also has intervened in FDB's operations, seeking to direct lending to poorer rural areas. Overt Government intervention is not an encouraging sign for staff and senior management, and does not augur well for future profitability.

The Government recently introduced a microlending scheme that is being administered through the Ministry of Finance. This scheme is likely to cut across the various small loan schemes being offered through the FDB. In addition, the Government has indicated that there is a need for a specialist farmers' or agricultural bank to address the specific needs of the agriculture sector. FDB is therefore an institution under some considerable market and political pressure, with growing confusion as to its future role.

FDB is the best positioned of all the development banks in the region to achieve the objective of commercial banking, due to its relative size and the level of maturity of its information and systems infrastructure. However, there is still a large proportion of the population that cannot access normal credit services for a number of reasons, including lack of assets against which to secure a loan. One option for FDB is to operate more

Table 2.9

## Fiji Development Bank Lending by Sector

|                                    | Fiji Total |           | FDB Total |         | FDB share of Total |        |
|------------------------------------|------------|-----------|-----------|---------|--------------------|--------|
|                                    | No         | (F\$M)    | No        | (F\$M)  | No                 | (F\$M) |
| Total Loans and Advances           | 45,743     | 1,446,229 | 7,270     | 352,606 | 15.9               | 24.4   |
| Agriculture                        | 7,375      | 129,793   | 3,943     | 87,417  | 53.5               | 67.4   |
| Sugar cane                         | 6,068      | 75,947    | 2,971     | 57,809  | 49.0               | 76.1   |
| Fisheries                          | 229        | 5,952     | 198       | 3,361   | 86.5               | 56.5   |
| Livestock                          | 166        | 9,355     | 122       | 7,134   | 73.5               | 76.3   |
| Manufacturing                      | 903        | 157,000   | 209       | 28,353  | 23.1               | 18.1   |
| Woodwork/<br>Furniture             | 94         | 7,373     | 13        | 2,810   | 13.8               | 38.1   |
| Building and Construction          | 275        | 57,814    | 33        | 17,167  | 12.0               | 29.7   |
| Hotels/Tourism                     | 54         | 33,260    | 25        | 16,890  | 46.3               | 50.8   |
| Real Estate (Development)          | 560        | 136,106   | 376       | 107,657 | 67.1               | 79.1   |
| Financial Institutions             | 162        | 5,956     | 151       | 2,677   | 93.2               | 44.9   |
| Wholesale/Retail                   | 2,364      | 393,640   | 380       | 44,048  | 16.1               | 11.2   |
| Transport/Storage                  | 752        | 45,806    | 446       | 20,758  | 59.3               | 45.3   |
| Professional/<br>Business Services | 681        | 49,006    | 89        | 4,524   | 13.1               | 9.2    |
| Private Individuals                | 30,997     | 362,257   | 1,371     | 30,605  | 4.4                | 8.4    |
| Home loans                         | 6852       | 266,996   | 644       | 30,163  | 9.4                | 11.3   |

Source: FDB 1999.

and more in conjunction with other institutions that are closer to the ultimate end user. Funds from donors could be aimed at a specific target market and the FDB could manage the scheme. The small loans scheme is an example of this, but donors would need to recognize that there are costs involved for the institution and that these would need to be taken into account. Another option could be working with major processors of agricultural products to provide funds to selected growers who are seen to operate on a sound business basis. These options could be explored as part of the development of a strategic plan for FDB.

## LEGAL AND REGULATORY FRAMEWORK AND SUPERVISION

RBF's Financial Institutions Department is responsible for the supervision of licensed financial institutions and insurance companies. Licensed financial institutions as defined in the Banking Act 1995 are commercial banks and credit institutions. Supervision includes the off-site monitoring and on-site review of the activities of commercial banks, and risk assessments of financial institutions. Prudential requirements on capital adequacy were issued in 1996, and those on large credit exposures and associated lending in March 1998.<sup>7</sup> RBF is committed to conforming to the Basle Core Principles for Effective Banking Supervision (1997). A policy paper on disclosure guidelines on licensed financial institutions was issued in November 1998. The minimum disclosure requirements are designed to be consistent with standards issued by the Fiji Institute of Accountants and International Accounting Standard No. 30.

Internal management control and the following of prudent parent company regulations have ensured that foreign-owned commercial banks are sound, and there has been little difficulty for RBF in supervising these banks. However, the locally incorporated NBF had less management expertise and was more susceptible to political influence, with the result that it became encumbered with low-quality assets. Prudential supervision powers, which were not enhanced until the Banking Act 1995 was passed, could not solve these fundamental problems.

The question arises as to the degree of supervision that should be imposed on nonbank institutions that do not take deposits, such as FDB and FNPF. FDB has a informal reporting relationship, but should be subject to formal prudential supervision to ensure that there is an early warning of any serious deterioration in lending performance. It also needs to have a strong loan review process, as well as effective collection systems

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<sup>7</sup> The large credit exposures limit for commercial banks restricts lending to a single borrower or group of related borrowers to no more than 25 percent of their capital. For foreign incorporated financial institutions, the 25 percent limit is calculated on the latest audited global paid up capital and published reserves of the institution.

and an appropriate capital adequacy ratio (though the current 20 percent ratio seems adequate).

FNPF, with assets approaching F\$2 billion, has no reporting relationship with RBF. It is unclear if there is any formal reporting to any authority other than annually to Parliament. However, FNPF does have a relationship with RBF as to the timing of its offshore investment activities and exchange controls.

The Government passed a Consumer Credit Act aimed at regulating high-interest, unlicensed lending. However, the act has drawn heavy criticism from the banks, which make the reasonable claim that it imposes heavy compliance costs on them without effectively curbing unlicensed moneylending and the charging of exorbitant rates by nonbanks.

## DEVELOPMENT OF MONEY AND BOND MARKETS

Monetary policy is conducted through open-market operations, using central bank securities to influence the level of liquidity in the banking system and hence short-term interest rates. RBF uses 91-day Reserve Bank Notes, issued weekly, as the operational target for monetary policy; since 1997, monetary policy has been implemented through the price of funds (short-term interest rates) rather than the quantity of funds. RBF is planning to move to daily issues of RBF Notes.

For RBF, monetary policy aspects come before income considerations, although there could be an income issue if domestic interest rates were to rise. RBF earns income on foreign reserves at interest rates that have been above domestic interest rates. The Government issues Treasury bills; promissory notes are issued by the FDB, the Public Rental Board, the Housing Authority, the Fiji Sugar Corporation, and the Fiji Electricity Authority. There is no reference rate to which banks can link their interest rates.

The Statutory Reserve Deposit (SRD) is also used as an instrument of monetary policy. Remuneration of SRD holdings by banks is linked to the average yield on 91-day RBF notes for the previous month. From September 2000, the 91-day rate was reduced from 5 to 4 percent. No interest is paid on excess reserves. An Unimpaired Liquid Assets Ratio had been used since

1984, but this was removed in January 1999, as part of the ongoing liberalization of the financial system.

RBF also issues Government Treasury bonds through an auction process. RBF makes recommendations but the Government makes the final decision on the allocation. Bonds are generally issued on a monthly basis. However, because issues are driven by the Government's need for funds, sometimes no paper is issued. Also, because the Government needs permission from Parliament to issue bonds, the issuance sequence can be disrupted, particularly at the beginning of the financial year, if budget approval is delayed. The Government is planning to issue bonds every two weeks, which would mean smaller amounts each time.

There is very limited trading in the secondary market. It takes around four to six weeks to trade. The Government started to issue some callable bonds, but these were unhelpful in terms of developing a secondary market because they are not fungible with any other bonds in issue, and they are very difficult to price, thus working against the development of a benchmark yield curve. RBF is building a portfolio of Government securities, which will enable it to trade Government securities rather than RBF notes when undertaking open market operations. However, it is difficult to create a liquid secondary market when FNPF owns 80 percent of Government bonds and bills, when the banks have excess liquidity, and when nonbanks are buying bonds for their own portfolios and holding them to maturity. It is always possible to place bonds, since FNPF is always prepared to buy. Nobody will sell.

The tender, allocation, and issue process for bonds is manual. There is no automated application procedure. The bonds are issued in certificated, registered form, as required by the Finance Act, and are listed on the stock exchange. When they were first listed, it was hoped that this would result in a considerable improvement in liquidity. But when bonds are traded on the stock exchange, they become subject to a levy by the Capital Market Development Authority (CMDA), which makes it expensive to trade. The new securities act will require that small trades be executed on the stock exchange, but will permit large trades to be executed over the counter, that is, directly between banks.

A number of Government-owned corporations and statutory organizations issue bonds that are guaranteed by the Government. These are the Fiji Broadcasting Commission, FDB, the Fiji Electricity Authority, Fiji Pine, and the Housing Authority.

## **DEVELOPMENT OF DEBT AND CAPITAL MARKETS**

Companies are incorporated under the Companies Act 1995, which does not require that private companies be audited, however large they are. However, the Companies Act is being revised under the auspices of the Law Reform Commission. The systems employed by the Registrar of Companies and the timeliness of the returns is not known, but it was not possible for the Suva Stock Exchange (SSE) to easily identify public companies for the purpose of encouraging the companies to list. There are five large accounting firms, some of which have linkages with international accounting firms. There is a Fiji Institute of Accountants, which has developed some local standards.

### **Capital Market Development Authority**

The Capital Market Development Act 1996 established the CMDA, with the dual objectives "to develop an efficient and thriving capital market in Fiji and to develop and regulate the activities of the various market participants". The authority is fully funded by the Government and has a board made up of the general manager of the FNPF (the chairman), the governor of RBF (deputy chairman), the permanent secretary for finance, the administrator general (whose office is responsible for company registration), the chief executive of CMDA, four representatives of industry, a chartered accountant, a lawyer from a local law practice, and the company secretary of Fiji Holdings Limited (FHL).

The CMDA has issued a wide range of regulations and rules, as permitted and required by the act. However, the act and the regulations have been reviewed, and a significant level of proposed change has been approved by the board and is awaiting Government approval. There is also a new Managed Investments

Act and associated regulations. The major changes to the Capital Markets Development Act and Regulations are, first, a clarification of the relationship between the owners of the Suva Stock Exchange (SSE) and organizations with access to the facilities operated by the exchange (the original act stipulated that members and owners were synonymous, which is not in line with modern international practice).<sup>8</sup> Second, the CMDA has been given power to approve all public offers and companies that list their shares; and third, there are new regulations relating to prospectus requirements, takeovers, and mergers. The original act also placed specific educational requirements on licensed representatives. This has proved a problem for CNB, which would like to market its unit trusts through its bank branch network. It is understood that this problem is being resolved through negotiations between CNB and the CMDA.

### **Suva Stock Exchange**

The Suva Stock Exchange (SSE) was established in the 1970s, with FDB providing a matching facility for sellers and potential buyers of shares. However, at that time, there was no emphasis on listing. SSE Listing Rules were redrafted in autumn 1999. The focus of the rules is to enable the listing of domestic Fiji companies while maintaining a liquid and transparent market. The listing rules cannot yet be brought into effect, as they were drafted in conformity with the amendments being proposed to the Capital Markets Development Act. At present, there are nine companies listed on SSE. SSE and the CMDA have been talking extensively to companies about listing, although the companies are mostly family businesses to whom the disclosure requirements seem intrusive and rather threatening. Nonetheless, SSE is hopeful that more companies will list.

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<sup>8</sup> In 1996, ownership of the exchange was extended to include Colonial Fiji, Credit Corporation of Fiji, FDB, Fijian Holdings Limited, FNPF, National Bank of Fiji (51 percent of which was subsequently acquired by Colonial), and National Mb Finance. In the last quarter of 1999, Kontiki Securities also became an owner.

The Public Enterprise Act was passed in December 1996. This Act gives the Public Enterprises Minister the power to establish and reorganize enterprises, and provides for such enterprises to be declared "Government commercial companies" or "commercial statutory authorities". Such declaration subjects the entities to a range of performance, accountability, and reporting requirements. In 1998, the Public Sector Department was administering 30 public enterprises in various stages of corporatization and privatization. Proposals were made for regulating monopoly industries and privatization guidelines were established. However, subsequent political uncertainty has caused implementation to stall.

When SSE was restructured, it began trading with two brokerage members. These were Mercury Securities, owned by FNPF, and the exchange itself. Since then, the exchange has separated out the brokerage functions; the exchange broker now operates under the name of Fiji Stock Brokers. SSE is planning to sell the brokerage when a suitable buyer can be found. During 1998, FHL formed a stock brokerage company (FHL Securities), and in 1999 Kontiki Securities became a fourth brokerage. In addition, licensed dealers have access to the exchange to trade debt instruments.

It is difficult for brokerage staff to get training in the necessary skills. The only courses available are in Australia or New Zealand, and it is expensive to send people overseas. The financial sector has established the Pacific Islands Financial Markets Association to promote professional development.

SSE has trading sessions three times a week and plans to move to daily sessions when volumes increase sufficiently. Trading is by open outcry with members attending the trading sessions and shouting buy and sell orders. When the orders are equal and opposite they are "matched" by a caller and recorded as traded on the board. SSE would like to install an automated trading system in order to give the exchange a better image, to increase volumes, and to enable remote entry, which might encourage trading from other islands or other parts of the main island.

Settlement is by exchange of share certificates and checks at SSE premises on the due date for settlement. This system will be inadequate if and when volumes increase, and will need to

be replaced by a book entry transfer system allied to a central registration system to ensure market efficiency. Such a development should be made in conjunction with the installation of safe custody facilities, which will be needed if SSE becomes a regional facility.

SSE receives a grant from the Government, through the CMDA. In addition, the Government has supported the exchange by putting in place a regulatory body that is fully funded by the Government; giving investors a tax exemption for dividends paid on listed securities; and giving exemptions from stamp duty for transfers of listed securities. The income of the exchange, over and above the Government grant, comes from charges to members and listed companies for the use of its facilities.

SSE and the Government have made considerable progress in the last three years in developing a viable capital market for securities. SSE already has the ability to list companies that are incorporated outside the Fiji Islands, and the revised CMDA Act and Regulations will be supportive. In 1998, SSE was already considering whether it could form the nucleus of a regional market, though at that time it was concluded that it had insufficient resources and was insufficiently developed to undertake such an initiative. SSE still does not have the resources to undertake regional training, marketing, or systems development; and local resources are needed in the development of an automated trading system and in domestic promotion.

Further development of SSE will depend on growth in effective demand for equity. There is an unmet need for equity and debt financing (Admiralty Group Partnership 1998); but this need is in the area of relatively high-risk projects. Commercial banks often finance projects involving the South Pacific Project Facility (see below), though this is a small part of their overall business. The banks also lend to projects in which the Kula Fund provides an equity component, without themselves being prepared to provide equity finance.

## OTHER PROVIDERS OF CAPITAL

**FDB.** FDB has an equity investment fund but, as noted above, is seeking to cut back its equity investments, having underwritten an unsuccessful initial public offering of Fiji TV shares in 1997. Other providers of capital to the private sector include Colonial Fiji Life Limited, Colonial First State Investments, Fijian Holdings Limited (FHL), Unit Trust of Fiji (UTF), and FNPF.

**Colonial Fiji Life Limited.** This insurance company is required to invest 30 percent of its life assurance assets in Government bonds, and the balance is invested in mortgages, listed companies, and a number of unlisted securities (where a 40 percent stake with a minimum investment of F\$250,000, plus a seat on the board, can be taken).

**Colonial First State Investments.** This firm has launched three unit trusts, which are open-ended funds with heavy exit penalties for the first few years. The intention is that two of the funds (the growth fund and the balanced fund) will be invested in securities listed on the SSE. These funds are looking for blue chip investments and are not venture capital funds.

**FHL.** FHL is an investment company that was established in November 1994 to enhance Fijian participation in the market economy. The ownership of FHL is limited to various provincial and regional groups and indigenous individuals, with individual holdings limited to 100,000 shares. FHL shares are listed on the SSE on a restricted transfer board. FHL adopts a risk-averse investment policy aimed at a post-tax return of 11 percent. The investment portfolio includes extensive property holdings and shares in 15 companies, listed and unlisted. FHL has a window for "green field" projects that is capped at F\$2 million and is currently fully utilized. FHL is one of the owners of SSE and has established a brokerage house. It intends to develop its underwriting, distribution, and marketing skills.

As a supporter of indigenous Fijians, FHL gets preferential treatment in public offers. It has often been able to buy shares at a discount and is allocated fixed percentages of issues. It is

viewed as the natural partner for foreign investors seeking a local partner. Other capital market participants view this preferential treatment as a distorting factor in the market.

**UTF.** UTF was established 21 years ago under FDB and became independent in December 1997. UTF is aimed at individuals, although some institutions also hold shares. The minimum investment is F\$200 and the dividend is not taxed. The trust is an open-ended unit trust and is therefore concerned with liquidity. It invests in Government bonds (20 percent) and equities. The equity investments, by value, are predominantly in listed securities. UTF also invests in a few unlisted securities, but generally such stocks would have to be in an established company with a good profits record. UTF would look for at least a five-year history of profitable trading demonstrated by audited accounts and a good dividend record. It would also carefully assess the quality of the management. UTF does not have permission to invest offshore.

**FNPF.** As noted above, FNPF has a restrictive investment policy that allows for investment only in blue chip companies with a five-year profit and dividend record (although special provision was made to allow the purchase of 51 percent of ATHL). Three companies that have listed on the SSE have attempted to raise funds from the general public at the same time, by listing within 30 days of the initial public offering. These are Fiji TV, Rice Company of Fiji, and Atlantic and Pacific Packaging Company Limited, of which the latter two were successful.

Companies very often obtain financing from external trade partners in the form of either equity or debt. All incoming investments must be vetted by the Fiji Trade and Investment Board.

**The Kula Fund.** This regional venture capital fund, which is operated by Commonwealth Development Corporation (CDC) and funded by it and ADB, IFC, EIB and other aid agencies and regional governments, has made a number of investments in the Fiji Islands, but prefers not to reduce its relatively large minimum investment, because smaller projects take more effort to manage than large ones, and generally the sponsors lack the

financial systems and management discipline to build a successful business.

**Pacific Islands Investment Facility (PIIF).** The International Finance Corporation (IFC) has established the PIIF, which is administered through the South Pacific Project Facility (SPPF). This can provide development finance to organizations, as well as assistance in conducting market research, developing investment plans, and sourcing finance to organizations.

*The Kontiki Fund.* This organization is a private venture capital fund based in the Fiji Islands and run by expatriates with experience of fund management in developed markets. Its marketing material (which is restricted to professional investors) makes it very clear that this is a high-risk investment.

## MICROFINANCE

Reports from welfare organizations and recent surveys of low-income communities show that the number of families facing regular deprivation is on the rise and poverty is deepening in the Fiji Islands. This is partly because growth in jobs is being outstripped by the demand for paid employment and partly because there is not enough land to provide subsistence living. More people are working in the informal sector, as manifested in the increasing number of market vendors, road-side stall holders, and shoeshine boys. Other activities such as selling produce, sewing, cooking food for sale, and weaving mats and other handicrafts take place at home.

The poor have difficulty in accessing formal financial services, for both credit and savings, because of lack of collateral and inability to comply with other banking requirements. Most are unable to save money in banks, due to an inability to put up the minimum opening deposit. In addition, commercial banks cannot afford to provide services in outer islands and remote rural areas. A well-designed microfinance scheme is needed to respond to the financial needs of the poor.

There is a growing interest in and support for microfinance by policymakers, donors, and other stakeholders. More than 150 representatives of civil society organizations, the private sector,

financial institutions, Government agencies, and development partners have contributed to the drafting of a National Plan of Action for the development of microfinance in the Fiji Islands. The Plan outlined strategies to promote awareness and understanding of microfinance, create an enabling policy environment, identify ways to mobilize resources, and clearly delineate the roles and responsibilities of various stakeholders in the improvement of access to financially viable and sustainable financial services.

Microfinance institutions (MFIs) generally operate in the informal and semiformal financial sectors, with the exception of the New Zealand Small Loans Scheme operated by FDB. Other formal financial institutions do not provide microfinance, though they offer unsecured personal loans to people with regular sources of income.

### **Informal Sector**

There is a substantial flow of credit and savings transactions in the informal sector, but these are not recorded in official statistics, so their full extent and nature are unknown. The most common source of microcredit is friends and relatives, commonly referred to as *kerekere* or *dinau*. The extended family and the culture of sharing, giving, and reciprocity is well entrenched, especially in the rural areas; repayment usually is made in kind. Unregistered moneylenders are also important sources of quick credit.

What detail there is on the informal sector comes from a 1995 United Nations Economic and Social Commission for Asian and the Pacific sample survey that had a low response rate. This showed that there were various small-scale schemes, mostly created by village or organization-based groups ranging in size from three to 348 members and averaging 18. Most groups established their schemes to collect savings from members as a precaution against emergencies. These groups generally deposited the collected savings in commercial bank accounts, and some raised loans from the banks concerned. The other groups were established to provide future access to a source of credit or to finance collective work. Problems encountered in the operation of these schemes included misuse of funds, poor management, and low recovery of loans.

## Semiformal Sector

The semiformal sector includes moneylenders, credit unions, nongovernment organizations (NGOs), government organizations, and the United Nations Development Programme (UNDP). Pursuant to the Moneylenders Act of 1939, all moneylenders are required to register with the Registrar of Moneylenders, who issues an annual operating license upon payment of a F\$55 fee. At the end of 1999, there were 90 registered moneylenders. Section 22 of the Act stipulates that the interest rate on loans should not exceed 12 percent per year. However, anecdotal evidence is that some moneylenders charge as much as 20 percent every fortnight.

**Credit unions.** Credit unions have been operating since the Credit Union Act was passed in 1954. The Fiji Credit Union League (FCUL), the apex organization of credit unions, was established in 1956. FCUL is primarily responsible for promoting the credit union philosophy, organizing new credit unions, providing necessary services to affiliated credit unions to conduct sound business practices and to safeguard the funds of the members; guiding and directing credit unions to achieve self-sufficiency, and encouraging networking and cooperation between and among local credit unions and the national and international bodies concerned with the credit union movement. Credit unions have to be registered with the Registrar of Credit Unions. There are 52 active credit unions, with a membership of more than 10,000.

Credit unions extend loans to members either for provident or productive purposes. Provident loans are loans utilized to meet family and social obligations, while productive loans are utilized for activities that will generate income, such as buying farm implements or sewing machines. Loans usually range from F\$10 to F\$2,000, depending on the number of shares and level of deposits of the member. Interest of 1 percent per month is charged on a declining balance (pursuant to the Credit Union Act), and the loan must be repaid within a period of two years in weekly, fortnightly, monthly or semiannual installments, depending on agreed terms. Both the loan and members' shares are covered by insurance. In rural areas, credit unions are still the main

providers of savings and credit services. In urban areas, they provide cheap, quick credit to their members, who are mostly low-wage workers, while allowing them to save small amounts of money either through shares or deposits.

Credit unions reach the largest number of clients, although membership has declined because of ineffective and inadequate monitoring and supervision by the Registrar of Credit Unions, financial and manpower constraints in FCUL that prevented provision of training and support required by officials of newly formed credit unions, and mismanagement problems encountered by some individual credit unions that have eroded the credibility of the movement. The thrust of the movement now is one of consolidating credit unions instead of expanding or creating new ones. The FCUL is working on revision of the Credit Union Act to accommodate provisions that will minimize mismanagement of funds and help credit unions develop viable operations.

**NGOs.** There are many NGOs actively involved in the provision of services to disadvantaged groups, especially in the areas of education, training, and welfare-related activities. Most NGOs are urban-based and are serving the poor in urban and periurban centers, specifically in slums and squatter resettlement areas. Several NGOs are servicing rural people. However, only four NGOs have provided microfinance services to the poor: the Social & Economic Equity for the Disadvantaged (SEED) Foundation; Fiji Council of Social Services (FCOSS); Rotary Club of Ba; and Housing Assistance and Relief Trust (HART). Of these, SEED and FCOSS remain active. HART awaits additional funding before reengaging in microfinance provision.

*SEED Foundation.* The SEED Foundation was formed in 1998 and is the first local NGO specializing in the provision of microfinance and microenterprise development services for the disadvantaged. Its board is made up of a group of socially committed people from the private sector, representing a strong combination of skills, expertise in private business, financial management, and training. The members of the board are all based in Suva and have a strong commitment to make SEED into a financially viable institution. It has targeted disadvantaged women in the squatter settlements around Suva, adopting the

Grameen Bank approach with some modifications. As of January 1999, it had benefited a total of 99 women clients and disbursed a total of loans amounting to F\$12,785, with total cumulative savings of F\$4,366. The interest is calculated on the basis of a 20-percent flat rate over a 25-week period. SEED's funds came from fundraising activities initiated by SEED itself and from UNDP's Pacific Sustainable Microfinance and Livelihoods through Empowerment (SMILE) Program.

*FCOSS.* This is an apex organization of NGOs and is the recipient of a grant from the National Microfinance Unit (see below) to undertake a microfinance pilot project in low-income communities. Since the commencement of the project in December 1999, 165 low-income households have benefited from loan disbursements totaling F\$29,244. Total savings amounted to \$9,081.61. Like the SEED Foundation, the project replicates the Grameen Bank model through the formation of solidarity groups of five in communities of at least 30 people. The solidarity group serves to instill peer pressure to ensure high loan repayment. Loans range from F\$50–F\$250 and are payable weekly over eight months at a 25-percent interest rate. Group members save money through a group fund. Members are also encouraged to save individually. To qualify for a loan, an applicant has to undergo training and is taught the rules and regulations of the scheme, as well as the essential elements of business management. An applicant has to come up with a business plan for the proposed project. Projects funded include small-scale home-based businesses such as canteens, selling *kava* (Fiji's traditional drink), selling vegetables and root crops, and mat weaving. It is hard to determine the impact of the scheme in this early stage of implementation. It was reported that the repayment rate has not fallen below 90 percent.

*NMU.* The Ministry of Commerce, Business Development and Investment operates the National Microfinance Unit (NMU), which has six staff and F\$3 million to allocate to microfinance activities. A National Microfinance Taskforce with representatives from various sectors provides advisory support, and UNDP provides up to F\$450,000 in technical assistance. NMU is responsible not only for funding microfinance projects, but also for ensuring that the policy and regulatory environment is conducive to microfinance development. NMU seeks NGOs

in addition to FCOSS that can expand the outreach of microfinance and provides eligible NGOs with grants not exceeding F\$200,000. It also provides training to the NGO before it starts its microfinance activities.

*Small and Microenterprise Policy Framework.* An initiative that is related to the creation of NMU was the August 1999 adoption of a Small and Microenterprise (SME) Policy Framework, which aims at improving the policy environment for SMEs through the drafting of a SME Development Act. Among other things, this would provide a legal basis for the establishment of the National Center for Small and Micro Enterprise Development, which would serve as a focal point and coordinating mechanism for SME providers, and as a direct supplier of support services.

*WOSED.* In support of the Government's twin policies of increasing women's participation in the market economy and promoting rural development, the Department for Women and Culture embarked on a specialized program for women in 1993: the Women's Social and Economic Development (WOSED) Program. Patterned after the Grameen Bank, WOSED is the longest-running microfinance program in the Fiji Islands. As of January 2000, it covered five areas in the Central Division, six in the Western Division, three in the Eastern Division, and three outer islands. It has disbursed a total of 534 loans amounting to F\$162,000. Savings in the central fund amounted to F\$11,400, while individual savings amounted to F\$11,000. All loans are charged interest of 15 percent for six months, and loan funds are released to group members simultaneously. Individual borrowers are solely responsible for paying back the loans, and the solidarity groups are used as a means of facilitating loan collection. There is a plan to transform WOSED into an NGO.

*SMILE.* The UNDP Pacific SMILE Program based in Suva has initiated savings and loans schemes targeting low-wage factory workers and low-income households in Suva and suburban communities. The enterprise-based savings and loan scheme is carried out in partnership with private companies. It brings banking services to the workers at the factory, as many of the workers cannot afford the minimum savings deposit required by banks or find it too costly to travel to the nearest bank. As of February 2000, a total of 14 companies had joined the scheme,

servicing a total of 1,099 workers and with total savings amounting to F\$49,033. Savings deposits and loan repayments are made through salary deductions.

The community-based savings and loan scheme was launched in November 1998 at the Raiwaqa Public Rental Board Housing Estate. It was later expanded to two more housing estates, and now includes two church groups. All transactions are done at a community level, through a hired village collector. Most people welcome the scheme, as it enables them to save small amounts of money regularly without incurring any expense, since collection is done right at their homes. As of February 2000, the community-based scheme had served a total of 293 savers who had accumulated gross savings of F\$21,489.

Credit Unions, WOSED, and the FDB New Zealand Small Loans Scheme have wider geographical outreach than SEED and the more recently-established schemes of FCOSS and NMU (Table 2.10).

The savings and loan scheme of the UNDP SMILE Program has reached a total of 1,392 clients: 293 low-income households and 1,099 low-wage factory workers. Grameen Bank replicators all focus on poor and disadvantaged women (households) and ensure no leakage to nonpoor clients. WOSED has the highest membership, with more than 500 households, followed by FCOSS with 165 households and SEED with 99. Rotary Club of Ba and HART had 29 and 4, respectively. The FDB New Zealand Small Loans Scheme has benefited 222 women who can afford to meet the collateral, cash equity, and other requirements.

Under the law, only credit unions and development banks are authorized to extend loans, and only credit unions are authorized to accept savings. Government agencies are undertaking microfinance activities in pursuance of the poverty reduction or women-in-development strategies of the Government. NGOs are not supposed to engage in microfinance, pursuant to the Charitable Trust under which they are registered, but in fact are operating with de facto approval. NMU is encouraging NGOs to serve as microfinance institutions, pending the development of the necessary legal framework, which is needed to gain the trust of the people.

With most of the MFIs in the early stages of development, none has yet reached a level of operational sufficiency or financial

**Table 2.10**  
**Geographical Outreach of Microfinance Providers**

| Microfinance Provider                      | Name of Program  | Geographical Coverage  |
|--|--|--|
| Credit unions                              | Credit unions savings and loans                                | Key urban areas: Suva, Nadi, Lautoka, Sigatoka, Labasa   |
| SEED Foundation                            | SEED Foundation Microfinance Scheme                            | 5 squatter areas in greater Suva and 3 low income communities in the suburbs of Suva   |
| Fiji Council of Social Services            | Financial Assistance Program of the National Microfinance Unit | 3 pilot sites: Quia (urban settlement); Drekena (rural village); Wakanisila/Naibulivatu (periurban)                            |
| Rotary Club of Ba                          | Anandpur Microcredit Project                                   | Squatter settlement in Anandpur and nearby Bandrau in Ba   |
| Housing Assistance and Relief Trust (HART) | Microfinance Pilot Project (BULA)                              | HART Settlement in Valelevu  |
| National Microfinance Unit                 | Financial Assistance Program                                   | Same as FCOSS and Batiki outer island in Lomaiviti; will expand to 17 more low-income communities                              |
| Department for Women and Culture           | Women's Social and Economic Development (WOSED) Program        | Central (5 areas), Western (6 areas) & Eastern (3 areas including Rotuma and Levuka) Divisions and Cakaudrove, Bua and Macuata |
| UNDP/SMILE Program                         | Enterprise-based and Community-based Savings and Loan Scheme   | Greater Suva area (14 factories, 3 low-income communities; 2 religious groups)<br>Nationwide                                   |
| Fiji Development Bank                      | New Zealand Small Loans Scheme                                 |  |

Source: Interview with officials.

viability. Most are totally dependent on donor and Government grants or subsidies, and none has accessed loans from commercial banks. In terms of portfolio quality, SEED Foundation, WOSED, and the New Zealand Small Loans Scheme

suffer a high rate of loan arrears—20 percent or more, which compares with a guideline rate of 5 percent, and is attributed to the fact that the businesses have been terminated.

Given their low level of self-sufficiency, MFIs need to ensure that their interest rates cover operating costs, and to upgrade their human resource base through training. Staff incentive packages are needed and measures to improve repayment should be instituted (counseling, close monitoring, and peer pressure). Record keeping and management information systems also need improving, and there is a need to create standard reporting and accounting systems. Finally, a mechanism for better networking and sharing of experiences is needed, so that lessons and best practices can be learned. In the short to medium term, continued reliance must be placed on technical assistance and funds from Government and donor agencies.

## LAND OWNERSHIP STRUCTURE

Land ownership in the Fiji Islands falls into three categories: (i) Crown or State land, that is, land vested in the Government; (ii) freehold land, that is, land held free of any limitation as to duration, free of rental or other conditions, and usually vested in individual persons; and (iii) customary land held by *mataqali* or landowning units according to rules of custom.

### Crown or State land

State land makes up 7.5 percent of the total land area of the country. It is legally regulated by the Crown Lands Act and is divided into three subcategories: (i) Crown freehold is land that the Crown has acquired for public purposes (administration buildings, schools, roadways, airports, harbors); (ii) Crown land, Schedule A, is former customary land, the landowning unit of which has become extinct; and (iii) Crown land, Schedule B, is land for which no customary landowning unit has been found. The Minister of Lands may sell any of the three classes of Crown lands after consultation with the Cabinet. Each may also be leased or licensed by the Director of Lands. Crown land that has been leased or licensed may be mortgaged. Many Fijians argue

that Crown Land Schedules A and B should be classified as customary land and allocated to Fijians.

### **Freehold land**

Freehold land makes up about 10 percent of total land area and derives from customary land that was sold by Fijians to Europeans and others during the colonial regime. Since 1875, except for a short period, direct sales of customary land by Fijians except to the Crown have been prohibited. The only way in which freehold title can be acquired now is by a grant from the Crown. Any person may acquire freehold land. Freehold title is not restricted to citizens.

Titles to freehold land must be registered under the Land Transfer Act, and, except in the case of fraud, and subject to some minor modifications, the Government guarantees the validity of the title so registered. Freehold land may be leased, but if the lease exceeds 12 months, it must be registered under the Land Transfer Act. No prior approval by the Government or a Government agency is required for the leasing of freehold land.

Freehold land may be mortgaged, but the mortgage must be registered under the Land Transfer Act to be effective. No prior approval by the Government or a Government agency is required. A mortgage takes effect as a charge on the land, not as a transfer of title or possession. If there is default in payment of the loan, a mortgage may be enforced by entry into possession by the mortgagee of the mortgaged land and sequestration of the rentals, sale of the mortgaged land in the open market, or transfer of the mortgaged land by the Registrar of Titles to the mortgagee, technically termed foreclosure. Orders of the High Court are not required in order to exercise these remedies.

### **Customary land**

Customary land constitutes 82.5 percent of the land area and is held by landowning units called *mataqali*. For the sake largely of administrative simplicity, these were the only landowning units to be officially recognized by the colonial Government, although there was much evidence to indicate that landowning customs were more diverse than this: in some areas

it appears clear that individual ownership, or single-family ownership, was recognized, while in others tribal ownership was recognized (France 1969).

A systematic registration of customary lands and their *mataqali* began in the late 19th century and took many decades to complete. The results are recorded in the Native Land Register, which is kept by the Registrar of Lands. Customary lands are not registered under the Land Transfer Act, and the Government provides no guarantee of title to customary land registered in the Native Land Register.

Challenges to the Register may be made, and these number about five per year. Disputes about title to customary land are adjudicated by the Native Lands Commission, which consists of one or more persons appointed by the Minister of Fijian Affairs, and by the *Roko*, or Fijian administrative official, of the province in which the land is located. One or more persons are elected by the council of a province to act as assessors to assist the Commission in the province. Appeals against the decisions of the Native Lands Commission relating to land ownership may be taken to the Appeals Tribunal (see below).

Because *mataqali* did not originally have a uniform number of members or control landholdings of a uniform size, and because over the years there have been differences between the rates of births, deaths, and migration in different *mataqali*, there is today great variation in the amount of land available to members of different *mataqali*. Some *mataqali* are quite small and have more land than they need for their support, whereas others have many members and insufficient land for their requirements.

Since 1875, it has been illegal for *mataqali* to sell land, except to the Government, but until 1940, there was no legal restriction upon the power of *mataqali* to lease or license their land. At that time, the Native Land Trust Ordinance (now Act) 1940 was enacted by the colonial Government, with the support and encouragement of the eminent Fijian leader, Ratu Lala Sukuna, and the Great Council of Chiefs. Section 4 of this Ordinance (now Act) provides that the management and control of all customary lands is vested in a statutory body, the Native Land Trust Board (NLTB), for the benefit of the owners.

The NLTB is authorized to lease or license customary land without consultation with, or the consent of, the owners, and there no transaction in customary land may be made without the consent of the NLTB. In practice, NLTB usually does try to consult with custom owners before making a decision about the leasing or licensing of land; and it is required by law to satisfy itself that the *mataqali* will retain sufficient land for itself, before it arranges to lease or license customary land. The act and regulations do not specify the rent that the Board is to charge if it leases or licenses customary land, but the usual charge has been 6 percent of the capital unimproved value of the land. Leases of customary land must be registered under the Land Transfer Act. Most customary lands can be leased to anybody, but one third of bush lands are held as reserves for use by Fijians only. Both reserved and nonreserved customary land can be leased to members of the landowning unit, although this is not very common.

Rents collected by the NLTB for the leasing or licensing of land are kept by the Board for disbursement to the *mataqali* members, subject, first, to a deduction of 25 percent for administrative costs. Of the balance, 27 percent is paid to various chiefs, so that landowners actually receive 48 percent of the rents collected by the NLTB.

The NLTB consists of 12 members: the Governor-General as President, the Minister of Fijian Affairs as chairman, five Fijian members appointed by the Great Council of Chiefs, three Fijian members appointed by the Fijian Affairs Board from persons nominated by the provincial councils, and not more than two members of any race appointed by the Governor-General. There is no express provision for representation in NLTB of representatives of *mataqali* or the landowners.

The NLTB has come under increasing criticism in recent times, especially from Fijian landowners. Supporters of NLTB argue that it has granted many leases of customary land, which have ensured both economic growth of the country and also economic and social well-being of lessees; and that the uniform and relatively low level of rentals has kept production costs of agricultural crops, especially of sugar, stable. Arguments against NLTB are that

- (i) the rent charged is too low and does not give sufficient return to landowners;

- (ii) too large a proportion of rentals is deducted for administrative costs;
- (iii) too large a proportion of rentals is paid to chiefs, rather than to landowners;
- (iv) there is inadequate consultation with, and regard for the needs and wishes of, landowners, causing too much land to be leased out and resulting in inadequate land for the support and maintenance of landowners;
- (v) inefficient and slow administration causes delays in rent payments and delays in processing expired leases and granting new leases; and
- (vi) inefficient administration has caused leases and licenses to be granted to more than one person, causing unnecessary confusion and resentment, and expense and delay to resolve the dispute that arises.

Although it is not expressly stated in the Native Lands Act, customary land can be leased by NLTB to some or all of the members of the landowning unit, and leaseholds of customary land can may be mortgaged, but the consent of the NLTB is required. The mortgage, when registered under the Land Transfer Act, takes effect as a charge on the lease, not as a transfer. If the mortgagor defaults, the mortgagee can secure repayment of the loan by sale of the lease to some person, entry into possession of the mortgaged land, or transfer of the lease to the mortgagee. These remedies do not require the approval of the Supreme Court, but they do require the consent of the NLTB. There is a perception by lending institutions that the NLTB would not consent to the sale of leaseholds of customary land, or to the entry into possession of such lands. Although this may not accord with reality, it is a perception that makes lending institutions reluctant to accept leaseholds of customary lands as collateral security for loans.

## **Legislation Regulating Land Tenure**

**Agricultural Landlord and Tenant Act (ALTA).** This act, which was enacted in 1966, was designed to provide stability in leases of agricultural land. "Agricultural land" is defined very broadly, to mean land used predominantly for the growing of crops; dairy farming; fruit farming; forestry; horticulture;

beekeeping; poultry keeping; or the breeding, rearing or keeping of livestock. Since most agricultural leases are leases of customary land, ALTA applies mainly to such land. Most leases are held by Indo-Fijians for sugar cane growing, so that the Act has important ethnic, social, and economic implications for the whole country.

The main effects of ALTA are the following:

- (i) agricultural land cultivated for more than three years without objection by the landowner is presumed to be under a 30-year lease unless the landowner can prove otherwise;
- (ii) all agricultural leases are for a period of 30 years;
- (iii) all agricultural leases are made subject to certain conditions and terms; and
- (iv) agricultural tribunals are established to adjudicate disputes arising under ALTA, and appeals from such tribunals can be made to a Central Agricultural Tribunal.

The original agricultural leases protected by ALTA have now started to expire. There has been much controversy about what should be done: many Fijian landowners have been demanding that leases be allowed to expire, so that they can use the land themselves and reduce the amount of land leased out; while most lessees are demanding that the protection provided by ALTA be continued. A review of ALTA has led to calls for an extension of existing leases by 30 years and an increase in rents to something within the 6–10 percent range. The issue remains unresolved (ADB 2000).

**Crop Liens Act.** The Crop Liens Act provides that crops of agricultural produce may be mortgaged, so that such mortgages can provide collateral security for a loan, whether the mortgagee is the owner or the lessee. The list of crops that can be mortgaged includes all agricultural crops currently grown in Fiji on a commercial basis. The list does not, however, include trees grown for commercial purposes, such as coconut palms or pine trees, nor does the Crop Liens Act provide for the mortgaging of livestock. At present, cattle (both beef and dairy), goats, sheep, and poultry are farmed commercially in some areas, but these cannot serve as collateral security for loans.

## Disputes

Disputes over land and security arise mainly with regard to (i) ownership of customary land; (ii) headship of *mataqali* and other Fijian social groupings; and (iii) enforcement of security over customary land. For many years the question as to which Fijians were the owners of which areas of customary land has been turned over to the Native Lands Commission for adjudication, as noted above. The Commission is required to inquire into the title to all lands claimed by *mataqali* or other divisions of people, who must mark out the boundaries of the land claimed by them. The Commission is also required to record any person who holds any customary title or office with regard to such land, or any easement or encumbrance to which the land is subject. At the end of the proceedings, the Commission announces its decision to the parties concerned.

The Native Lands Act provides that if a member of a landowning unit does not reside within the unit for two years or more, the Minister may, at the request of other members of the unit, declare that such person is no longer a member of the unit. The person is then divested of all interests in the land of that unit. Exceptions are provided in the case of Fijians absent on lawful, *bona fide* employment and women living away with their lawful husbands. In practice, it appears that rarely, if ever, has a request been made for the divesting of a member of a landowning unit, and this provision is virtually a dead letter.

The Native Lands Commission is also authorized, with the consent of the custom owners, to allot, at its discretion, a sufficient portion of their land to other Fijians who, having lost their right to their own tribal lands, have become dependent on the Fijian owners. There are limits upon this, however: the allotment can only be made with the consent of the Fijian owners, the land is only for the use and occupation of the dependents, the right of occupation expires if the dependent leaves, and no allotment can be made to a dependent who already owns land.

An appeal of a decision of the Native Lands Commission relating to the ownership of customary land may be taken to an Appeals Tribunal within 90 days of the announcement of the decision. The Chairman of the Appeals Tribunal must be a person having qualifications to be appointed a Judge of the High Court,

i.e., at least seven years' practice as a lawyer in the Fiji Islands or some other country approved by Parliament; or be otherwise suitable to be Chairman by virtue of his academic or other qualifications and experience. Two other members of the Appeals Tribunal must also be persons having such academic or other qualifications and experience as render them suitable for appointment.

Neither the Native Lands Commission nor the Appeals Tribunal is required by legislation to comply with principles of natural justice when conducting their proceedings, to hold their proceedings in public, to give reasons for their decisions, or—with one exception—to make public their decisions and reasons. Nor do these bodies, as a matter of practice, hold their proceedings in public, or publish their decisions or reasons. The one instance in which the Native Lands Commission must publicize its decisions is when it determines the headship of a division or subdivision of people: the law requires that such decisions must be read out publicly at the next meeting of the provincial council.

The Native Lands Commission is authorized by legislation to adjudicate disputes between Fijians as to the headship of any division or subdivision of Fijians having customary right to use customary lands, and to decide who is the proper head of such division or subdivision. Since the enactment of the Native Lands Trust Act in 1940, the headship of a division or subdivision of Fijians has involved not only social status but also financial return: as indicated above, chiefs receive significant shares of rentals for leases of customary lands. Not surprisingly, the number of disputes about chiefly titles, especially those titles to the larger areas of leased land, has greatly increased. In 1997, for example, of the 80 disputes dealt with by the Native Lands Commission, 50 percent related to chiefly titles. Since 1998, appeals of decisions of the Native Lands Commission with regard to chiefly titles have been heard by the Appeals Tribunal.

Leases and subleases of customary land may be mortgaged in accordance with the terms of the Property Law Act, but only with the consent of the NLTB, which has exclusive powers of management and control of customary lands. If a mortgagor defaults on repayment of the loan, the mortgagee may enter into possession and may collect any rents that are being paid for the

land, and he or she may sell the mortgaged land. If the land has been offered for sale at public action and failed to attract a sufficiently high bid, and if public notice has been given of the application for an order of foreclosure, a mortgagee may also obtain from the Registrar of Titles an order for foreclosure and have the land transferred to him or her. The exercise of these remedies requires the consent of the NLTB. There has been criticism about delays and inefficiencies on the part of the NLTB as to the exercise of these remedies.

## **KEY CONSTRAINTS ON FINANCIAL SECTOR DEVELOPMENT**

### **Inadequate Economic Environment of the Real Sector**

A very important constraint to the development of the financial sector is the economic environment in the real sector. If the financial sector is to grow, the real economy must also grow and be supported by appropriate policies. The first stage in an optimum order of economic liberalization is the establishment of balanced Government finances and deregulated real economies with predictable and consistent policies.

### **Public Sector Domination**

The public sector dominates the Fiji Islands economy. The civil service accounts for one quarter of formal employment and State-owned enterprises play a large role in the commercial sector. It is estimated that 60–70 percent of GDP comes directly or indirectly under Government control. Despite reforms, the public sector remains somewhat inefficient, and the privatization program has stalled.

### **Excessive Government Regulation**

Government regulation is still very prevalent. With the real sector so heavily regulated, it is difficult to proceed with more financial sector reforms. The approval system for businesses is still very cumbersome; this leads to considerable frustration for persons wishing to start a business. Foreign exchange controls

and regulations deter foreign investment: though the foreign investment bill has eased some problems, it is still excessively regulated. The Government imposes price controls on about 50 percent of prices, wholesale markups on many foodstuffs and household items are limited to 5 percent, and retail markups are limited to between 13 and 20 percent. Wage councils control wages. A large number of tax and tariff preferences and various industrial promotion schemes distort relative prices, as well as reducing Government revenues. All these controls lead to substantial rigidity in the economy, undermine efficient resource allocation, and prevent further liberalization in financial markets.

### **Land Tenure and Leasing Problems**

The low and falling investment rate caused by political and economic uncertainties, particularly regarding property rights, represents a huge constraint to economic growth and, therefore, financial sector development. Securing land lease renewals is the most important contemporary policy issue. ALTA only applies to new leases and does not allow for the extension of leases when they expire. Resolving the issue of leases for sugar and agricultural farming areas is crucial to economic growth. The ad hoc approach to this issue taken so far has not been good for business confidence, and failure to resolve it has also led to a significant emigration of Indo-Fijians, who stand to lose the most from the current uncertain situation.

The second most important land tenure issue is management and control of customary land by the Native Land Trust Board. The consent of this body is necessary for all transactions in customary land, including leases and mortgages of leasehold interests. The management of customary land is a very large undertaking, difficult for one body to operate very efficiently. There are continuing complaints of delays, misunderstandings, and mismanagement. Any challenge to the role of the NLTB at this time, however, is likely to be seen as an attack on Fijian values and interests, and therefore strongly resisted. No qualifications for membership of the Native Land Commission are prescribed by legislation, and members of both the commission and the Appeals Tribunal are appointed solely by the Minister of Fijian Affairs.

## Cultural and Communal Concerns

The strong communal culture in Fiji, which emphasizes sharing, makes it difficult to save money to start a business. Consumption is still generally more socially valued than accumulation. However, saving is not alien to Fijians, as evidenced by their accumulation of nonperishable goods such as mats and taro. People have the propensity to save money, even those with low incomes, provided there is proper motivation and a convenient mechanism to save small amounts on a regular basis.

The preference by the Government toward Fijians deters investment both by foreigners and nonnative Fiji Islanders. Fijians also place a high status on working in the public services, as opposed to working in agriculture. Running a business runs contrary to the communal culture that emphasizes sharing and obligation between family and clan members. With the traditional system of *kerekere*, some business people are finding it hard to reconcile the obligation to share with the need to protect and develop their business. On the other hand, some indigenous entrepreneurs have successfully drawn the line between business and family or traditional obligations.

Women, regardless of race, are disadvantaged as compared with men because of a relatively low literacy level, discrimination in paid work, and their perceived role as housewives who do not engage in business. Opportunities for Fijian women to enter business are also restricted by their exclusion from traditional rights of inheritance, an exclusion which means they have very limited control over family resources. In banking, women borrowers are at times required to have their husband guarantee a loan.

## Inadequate Human Resource Skills

Human resource skills are a large issue in the Fiji Islands. The low percentage of people with tertiary education (only 4 percent of the population) and the shortage of people with technical and professional skills represent a constraint to long-term growth of the economy and to the development of the financial sector. The large number of skilled workers who

emigrate (around 2 percent of the labor force per year since 1987) also creates a constraint to economic development, as they tend to be the most educated and best-trained people.

### **Government Intervention in the Financial Sector**

The considerable Government intervention in the financial sector has in particular constrained the development of FDB. Although RBF is relatively independent, its independence could be compromised by income problems if domestic interest rates were to rise above the level of international interest rates. It also must maintain its autonomy to run its supervision, monetary, and exchange rate policies, having to date ensured low inflation and a comfortable level of foreign exchange reserves. The NFPF and FDB are not supervised by RBF's financial institutions department. These institutions have not been adequately supervised in the past and are still not being adequately supervised.

### **Need for Standardized Accounting Practices**

Although there are five large accounting firms, some with linkages to international accounting firms, and a Fiji Institute of Accountants, (which has developed local standards), private companies do not have to be audited. Accounting practices and procedures need to be standardized, so that international accounting standards become the norm for the financial sector, public, and private sectors. This will help RBF with its on- and off-site supervision of commercial banks.

### **Slow Capital Market Development**

The development of a capital market is fundamentally dependent on the existence of companies that wish to raise finance through the market. The major problem for SSE is the lack of volume. Companies have not been very aggressive about listing on the stock exchange because of the many obstacles. One major obstacle is the legal costs incurred by the companies; another is the many licenses to apply for, which are transactions costs for the companies. It is important that the Government

understand the importance to the development of the capital market of a privatization process. A high profile privatization is a key component of such development.

## **Money and Bond Market Distortions**

Money and bond markets are significantly distorted by the size of FNPF and its monopoly. FNPF moves markets with its investments; consequently, there are no market-determined prices in the money or bond markets, and no secondary trading or yield curve. FNPF buys 90 percent of RBF notes and 80 percent of Government bonds and holds them to maturity; in these circumstances, it is difficult for buyers to find these instruments for sale. The lack of a market for Government bonds is not helped by the irregular timing of their issue and the need to obtain permission from Parliament to make the issue. In addition, high levels of liquidity have prevented capital and real estate markets from developing and from providing alternative investment instruments for Government bonds.

The problem is exacerbated by exchange controls on the capital account, which prevent FNPF from diversifying some of its portfolio abroad. Although RBF is moving toward fewer capital controls and more flexibility on exchange rates and monetary policy, RBF would have a problem in allowing FNPF to invest large amounts overseas, because it could cause RBF to lose too much of its foreign exchange reserves. Although foreign exchange controls are gradually being relaxed, the relaxation is taking place through the granting of specific exemptions and blanket approvals, rather than through repeal of areas of regulation. This is making the regulations more rather than less complicated.

While the reductions in the Statutory Reserve Deposit (SRD) and the removal of the Liquid Assets Ratio (LAR) could help to reduce the intermediation costs of the commercial banks, it actually does not help the excess liquidity situation for bankable projects. Reducing the SRD and removing the LAR gives the bank more liquidity and ensures that they hold Government bonds and RBF notes in the absence of any viable alternative investments.

## **Imperfect Competition**

The financial sector is characterized by imperfect competition as a result of the dominant position of the large foreign-owned banks and the high levels of liquidity in the system. The small size of the market also discourages the entry of other private banks: the length of time before profits can be made may well prevent other banks from entering such a small market.

The lack of a secondary market for central bank instruments or Government bonds, the small amount of trading on the stock exchange, and the underdeveloped real estate market, mean a lack of incentives for the public to hold savings, except for bank deposits. The lack of competition keeps savings and deposit rates low. Banks make high profits on their operation costs vis-à-vis their global operations; data suggests that they only fund very low-risk projects and have increased interest income more than interest expenses over the past few years. NBFIs and credit institutions do not provide competition for banks. FDB has had problems with bad loans and is still defining what its role should be, while FNPF has monopoly powers and absorbs over 80 percent of Government bonds and 90 percent of RBF notes, which it does not trade.

## **Inadequate Supervision**

Supervision of financial institutions needs strengthening. It would appear that at present, FDB is not appropriately supervised. FNPF is also outside RBF's area of supervision, although it is a major player in the financial system: the amount of pensions it pays and its portfolio diversification need supervising, particularly as FNPF may in the future be investing more abroad.

## **Outdated Corporate and Bankruptcy Laws**

Corporate and bankruptcy laws are outdated. In particular, the banking law on collateral is inadequate, and court procedures are very lengthy.

## **Constraints on Fiji Development Bank**

A number of constraints inhibit FDB's growth, including the land tenure system; increasing Government intervention in decision making; the high cost of funds, which puts them at a competitive disadvantage with commercial banks; the narrow skill base; lack of any formal prudential supervision; and the costs of maintaining a branch network in the outer islands.

## **Constraints on Microfinance**

In microfinance, the ability of MFIs to expand their outreach has been restricted by the high cost of service delivery to rural and outer island areas. There is also no appropriate legal and regulatory framework for microfinance, except for credit unions and thrift and savings cooperatives. Business training and advisory services are mainly available in major urban areas, and there is a lack of coordination on support activities for small and microenterprises between Government ministries, as well as with NGOs.

## **Education and Training Shortcomings**

The most quoted shortcomings in the education and training system include fragmented training policy; lack of awareness of existing training facilities; training mismatched with labor market needs; inadequate training facilities and a lack of training materials in the Fijian and Hindi languages; absence of curricula and training programs in new and emerging areas; and ineffective training programs for self-employment, including the informal sector.

## **RECOMMENDATIONS**

**To promote financial sector growth, improve the environment for real sector growth.**

The Government needs to create an enabling environment for private sector investment and trade and development.

Impediments to investment, such as outdated legislation and overstuffed bureaucracies, need to be removed. Decisions should also be made about foreign ownership and many other issues related to investment, so that a clear and consistent policy can be enunciated. The Government should maintain a macroeconomic environment conducive to the development of the financial sector by pursuing low inflation through prudent fiscal policy accompanied by the appropriate monetary policy. It should also implement reforms in the public sector to reduce its size and increase its efficiency. Price and wage controls should be liberalized, so that the real sector does not hold back the liberalization of the financial sector.

The Government also needs to focus on the sequencing, speed, and timing of the privatization program, and—where it can—to privatize public companies by bringing them to full disclosure and to listing on SSE.

### **Improve the operations of the Native Land Trust Board.**

The problems attending the renewal of rural land leases hangs over any decision to lend to this sector, and specifically over the future of the sugar industry. NLTB should continue to have exclusive powers of management and control of customary lands, at least for the short term, but subject to some significant modifications:

- (i) the practice of basing rentals on 6 percent of unimproved value should be altered to 6–10 percent of capital unimproved value;
- (ii) deductions from rentals for costs of administration should be reduced from 25 percent to 15 percent;
- (iii) deductions from rentals for chiefs should be reduced to 10 percent of the balance (after administration costs) for the chiefs of the *mataqali*; and
- (iv) a management review of staff and resources of NLTB should be undertaken to identify and remove causes of delays and inefficiencies in NLTB management.

The Native Land Trust Act, Cap 134, should be amended to provide expressly that

- (i) landowners be represented on the board;
- (ii) customary lands may be leased by NLTB to some or all of the members of a *mataqali* or landowning unit;
- (iii) leaseholds of customary lands may be mortgaged, with the required consent of NLTB;
- (iv) NLTB must promptly consent to leaseholds, mortgages, and enforcements of mortgages, unless it is satisfied that this is not in the interests of the landowners or the country; and
- (v) decisions by NLTB shall be subject to judicial review by the High Court.

Amendments should be made to the Native Land Act, Cap 133, to provide that

- (i) Native Land Commission members have qualifications of independence, impartiality, and experience in customary land matters;
- (ii) each party to a dispute about customary land may nominate an assessor to assist the Commission, together with the two assessors elected by the provincial council;
- (iii) the Native Land Commission and Appeals Tribunal must conduct fair proceedings, open to the public, at which each party is able to adduce evidence and cross-examine an opponent's evidence, and may make oral or written submissions; and
- (iv) the Native Land Commission and the Appeals Tribunal must publish their decisions and reasons.

### **Promote sound, efficient financial systems and strengthened supervisory systems.**

RBF's autonomy should be maintained, in order that it may perform its monetary and supervisory functions efficiently, and to ensure that the governor and members of the board of directors do not come under political influence. RBF must have the ability to take decisive action on problem supervisory cases, and must have the financial viability to conduct appropriate monetary

policy. The legislation must be strengthened so that firm, timely, and effective supervision of FDB, FNPF, and other NBFIs can take place under the purview of RBF's supervisory system.

Examination procedures, including on-site inspections and off-site surveillance, should be strengthened through short- and long-term training programs, to ensure that supervisors are capable of identifying weaknesses in financial institutions.

The judicial system should be strengthened so that matters relating to the financial sector are not unduly delayed but are promptly adjudicated, and so that the ability of the banks to enforce the contractual obligations of their customers is enhanced.

Clear international accounting and auditing standards should be adopted; these should be grounded within an updated commercial law that meets international standards.

The Government should continue to enhance and strengthen the process of regional cooperation and consultation in regulatory and supervisory matters, as initiated in the recent regional initiative by PDMCs to strengthen their financial sectors through the Pacific Islands Prudential Regulation and Supervision Initiative. In the same vein, a formal analysis is needed of the compatibility with international standards of the Fiji Islands' regulatory system and supervisory practices, in order to lay the foundation for the timely harmonization of financial sector regulation and supervision on a regional basis. The Government should also work closely with other PDMCs' supervisory bodies, with a view to eventually building a regional supervisory body for foreign banks. This would help to reduce manpower requirements and enable RBF to concentrate on supervising local banks and NBFIs, which need closer supervision.

### **Promote more effective competition for foreign commercial banks.**

To promote more effective competition for foreign commercial banks, the Government needs to encourage the development of NBFIs to compete with commercial banks' lending and other services; to develop efficient interbank and short-term money markets as alternative savings instruments; to allow FNPF to invest more money offshore, in order to mop

up excess liquidity in the financial system; to develop capital markets; and to provide institutional strengthening for MFIs.

To develop money and bond markets, the Government should ensure that regular issues of short-term instruments and Government bonds are available and should encourage the creation of secondary markets. This will provide more competition for commercial banks for both deposits and lending. By creating conditions that further the development of money markets, secondary markets, and interbank markets, RBF will also be able to mop up excess liquidity more easily.

Impediments in the real estate market should be removed, and public stock offerings to small savers should be made as the privatization program gathers momentum.

Commercial banks should be required to provide information on their fees, charges, and loan conditions throughout their branches and agencies, through the publication and distribution of literature. The Government should also encourage commercial banks to develop a more proactive approach to customer education. Introduction of mobile banks and substitute institutional arrangements in the field of payment mechanisms should be encouraged.

### **Reform the Fiji Development Bank and the Fiji National Provident Fund.**

A strategy for FDB's future should focus on greater independence from Government influence in its operation and in the appointment of the FDB board. The FDB legislation should be strengthened to provide for this greater independence. FDB should also develop stronger marketing and business planning skills, particularly in the area of providing assistance to FDB clients.

FDB should report to RBF covering

- (i) loan classification by sector and type;
- (ii) connected lending and concentration of loans to individuals and corporations;
- (iii) level of provisioning by types of loans;
- (iv) capital adequacy to reflect FDB's risk;
- (v) policies on interest accrual and suspension of interest of outstanding loans;

- (vi) policies on FDB officers, particularly those dealing with conflicts of interest as a result of lending to members on the board;
- (vii) policies on common minimum standards for disclosure; and
- (viii) relevant information on directors.

The FNPF Act should be amended to permit employers to opt out of the scheme, provided they provide approved alternative arrangements. Assistance will be needed to draft model recognition criteria for providers of collective investment vehicles and other alternatives. These criteria will also act as guidelines for private sector entities to design investment products that could be offered to private investors under the regulations.

### **Develop the capital market.**

To help develop a capital market, it is recommended that the Government consider participation in a new regional venture capital fund, should this opportunity arise. The nature of this fund is explained in the first volume of this study: *Volume One: The Regional Report*.

The Companies Act is being reviewed at the present time. Any amendments should ensure that public companies are required to file audited returns. In view of the small size of the private sector and the need to encourage its growth, the Companies Act should make turnover and/or importance to the economy an additional criterion for a company (or group of associated companies) to file audited accounts.<sup>9</sup> It is also recommended that the infrastructure of the registration process be improved and that staff be trained for these responsibilities.

It is recommended that the support to the CMDA and SSE in marketing to both companies and investors, currently being provided by ADB, should be continued. Encouraging companies to list is a long-term effort that will involve all participants in the

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<sup>9</sup> A problem with size criteria is that, to avoid meeting the criteria, proprietors often divide their activities into different companies. This can also happen in response to differential tax rates. Some antiavoidance provisions should therefore be incorporated into the act.

financial services industry. The major problem that companies see with listing is the need for disclosure and the need to produce audited accounts. Therefore, the upgrading of the functions of the Registrar of Companies would be a step in this direction. There is also a general need to educate companies about their public responsibilities.

The professionalism of staff working for brokers should be upgraded. A Pacific Islands Financial Markets Association has been formed that could be a focal point for a training program.

The Government should privatize one of its public enterprises through a public offer, as a high-profile contribution to the development of the capital market. The privatization should be supported by a significant publicity campaign to encourage the public to buy shares and to create public awareness of the stock exchange.

Technical assistance should be provided to SSE to investigate the options for implementing an automated trading system. The investigation should include a review of the feasibility, costs, benefits, and risks of SSE's using the same trading system as the Port Moresby Stock Exchange (POMSoX). Technical assistance should also be provided to determine the specification of the regional clearing and settlement facility "PacifiClear" in terms of

- (i) the legal changes necessary to implement a dematerialized system;
- (ii) the ownership of such a facility;
- (iii) the functionality required of such a facility, bearing in mind both current and future regional and national developments; and
- (iv) the potential cost of development and operation.

It is recommended that consideration be given to establishing a distributed, networked regional facility that uses Internet technology to link SSE and POMSoX to companies and investors in all PDMCs, with provision for other domestic

exchanges to be added to the network as they are developed.<sup>10</sup> Recognition by other Governments of the SSE and POMSoX regulatory structure would be necessary for development of a regional facility. Companies choosing to list on SSE would have to be freely transferable. Access to the system would be available to customers of licensed intermediaries in those PDMCs that have the necessary regulatory structure, and directly to investors in countries where there are no licensed intermediaries. This may involve some change in the CMDA Act and regulations and in SSE rules to recognize access by the regional facility. It would be desirable for SSE to have an automated trading system in order to form a node for a regional facility. A review of the relevant legislation would be needed to ensure that stock can be held in a nominee name with a third party custodian. Other issues to be addressed include currency exchange, investor awareness, and promotion to companies.

Agreement with RBF would be necessary to develop a regional stock exchange as recommended here, but exchange control regulations seem unlikely to cause significant problems.

### **Strengthen the environment for microfinance.**

The feasibility of microfinance in the Fiji Islands hinges on the following:

- (i) strong commitment of MFIs to outreach and sustainability through appropriate interest rate policies;
- (ii) long-term commitment of the Government and donor agencies to provide financial and technical assistance for capacity building, institutional strengthening, on-lending and related support services;
- (iii) establishing a conducive policy and legislative environment; and

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<sup>10</sup> The SSE already has the ability to list companies incorporated outside the Fiji Islands, and the revised CMDA Act and Regulations will support this policy. It is therefore possible today to permit regional companies to list on the SSE. However, the SSE does not now have the resources to undertake regional training or marketing or systems development.

- (iv) provision of support services, especially in microenterprise development and management and social mobilization.

Existing microfinance modalities, Grameen Bank replicators, and savings and loan associations/credit unions should continue to operate and should clearly emphasize savings mobilization before providing credit.

### **Strengthen and support the informal financial sector.**

The Government can strengthen the informal financial sector by

- (i) gathering relevant data on the informal financial system to determine the extent of its activity, problems, and needs;
- (ii) documenting best practices that are useful in developing more responsive microfinance schemes;
- (iii) formalizing microfinance schemes by registering them as credit unions;
- (iv) soliciting the support of various stakeholders, including church or religious groups, NGOs, private companies, Government agencies, provincial/city/town councils, and village chiefs.

Strengthening should be coordinated by the RBF; data should be analyzed and presented in a workshop to be attended by representatives of self-help groups and MFIs, relevant Government agencies, and NGOs, with an objective of drafting a plan of action to strengthen the informal sector.

### **Strengthen the policy and regulatory environment for microfinance.**

The environment for MFIs can be strengthened by

- (i) establishing a legal framework to enable NGOs to operate as MFIs (including developing a standard accounting and reporting system);

- (ii) facilitating the amendment of the Fiji Credit Union Act to enable credit unions to charge interest rates that will cover operations costs; and
- (iii) requesting the Small Business Advisory Unit to coordinate meetings with regulatory bodies to look at ways to lessen legal and regulatory restrictions on small and microenterprises.

Capacity building in MFIs should focus on

- (i) linking informal self-help groups with credit unions, with a view to ultimate registration as credit unions;
- (ii) training, particularly training in record keeping and financial management (the usual shortcomings of informal savings and loans clubs/associations); and
- (iii) connections with successful MFIs in other countries, to improve governance, policies and procedures, strategic planning, management, and social mobilization techniques.

MFIs should consider requesting FDB to consider wholesale lending to credit unions. They should also consider linking with NGOs that are actively involved in income-generating projects, to minimize the cost of training while providing technical advice and product marketing. The NMU, through linkage with international MFIs and donor agencies, could assist in mobilizing financial resources.

FCUL faces manpower and financial constraints that hinder fulfillment of its monitoring and supervisory role, especially with respect to credit unions in rural areas. These constraints should be eased through donor assistance.

Market research is needed on viable community-based enterprises, since the perennial problem of MFI clients is the lack of bankable projects. The formation of a Fiji Islands association of MFIs, and eventually a regional association of MFIs, could facilitate the pooling of funds and expertise in this and other areas such as training, policies, laws, documentation of best practices, and dissemination of information.