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Financial crises and lessons for Fiji

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Global economic downturn since 2008 is now affecting island nations. Neither size nor location matters.

In the Pacific, we hear Tonga (population: 106,000; land area: 717 sq km; GDP: US$816 million) is in bad shape.

From the Caribbean, we hear that International Monetary Fund (IMF) will approve a multi-million dollar Stand By Agreement with its usual belt-tightening measures to a much larger and mineral resource rich but crisis-ridden Jamaica (population: 2.9 million; land area: 10,990 sq.km; GDP: US$ $13.8 billion).

Tongan economy

National Reserve Bank of Tonga (NRBT) Governor Mafi told the business community on January 30 that the economy is not doing well. She observed:

“We are part of a global economy so the development in the international market and economies will definitely affect us here in Tonga, and we are still suffering from the spill-over effects from those economic developments internationally from the impact from the global finance crisis."

Tonga’s exports, mainly agricultural products: squash, vanilla beans and fruits and vegetables and fish are decreasing. Tonga’s manufacturing capacity is insignificant compared to Fiji with no strong import substitution possibility.

There is also a decline in inward remittances from Tongans working overseas. Remittances in 2008 were US$123.2 million. They fell to US$63 million in November 2012. Tourism receipts were inadequate to offset decline in export earnings and remittances, as number of tourist arrivals during past nine years has been stagnant.

As domestic investors are hesitating to borrow in a contracting economy, banks have excess liquidity. Further, there is rise in non-performing loans as well.

Tonga's public debt is 45.1 percent of GDP, above the internationally prescribed threshold of 40 percent. External debt is 90 percent of total debt and China is the major lender. Repayments would begin soon. They would amount 18 percent of public expenditure in 2013. They will result in cuts in essential services.

The IMF has declared Tongan's economy is at a "high risk of external debt distress".

J**amaica**

On February 12, the visiting IMF Mission confirmed that Jamaica will be seeking another round of a multi-million dollar Stand By Agreement (SBA) for getting out of debt trap it created for itself for a decade. A 27-month SBA worth US $1.27 billion expired in May 2012. In fact, it lapsed after the previous government was unable to meet performance targets set by the IMF.

Jamaica is lucky with mineral resources,

The bauxite-alumina industry with foreign investment has shifted its dependency on sugar and bananas. It is leader in the export of minerals.

What went wrong were the fiscal excesses year after year, since 1962, resulting in the build-up of public debt. Today it is J$1.7 trillion or US$18 billion (130 percent of GDP). The *Chicago Tribune* called Jamaica, "The Greece of the Western Hemisphere."

More than 50 percent of its budget is now devoted to service its loans and only 20 percent is spent on health and education programmes.

All the credit rating agencies have described the outlook negative.

The statement by IMF Mission Chief sums up the situation:

"The Jamaican economy has experienced very low economic growth, declining productivity, and reduced international competitiveness. An important factor behind these problems has been Jamaica's unsustainable debt burden, which has undermined confidence and elevated risks to economic stability".

Before seeking the second round of IMF assistance, Jamaica tried to restructure its loans to stretch them out over more years, at lower interest rates, with no success.

Under the new IMF assistance, there are pre-conditions:

- eliminate discretionary tax waivers
- freeze wage levels to achieve a wage to GDP ratio of 9 percent by 2015/2016
- pass a Public Debt Management Act;

- implement a new debt exchange offer, asking bond holders to accept terms that will reduce debt to GDP ratios by 8.5 per cent.

Fiji's competent macroeconomic policies

Fiji's debt level is 51.5 percent of GDP, having been reduced from 54 percent from 2010. Even if the government guaranteed debt is included, the debt level is well below 70 percent of GDP.

Fiji was ravaged by three cyclones last year, the deadliest being Evan of December of 2012. Unforeseen and unbudgeted expenditures to meet these emergencies would be imposing a burden on public finances. Policy makers are aware that they have to be met with prudent measures.

Recognizing Fiji's competent fiscal management, on February 14, Moody's Investors Service upgraded the government's foreign and local currency long-term bond ratings to stable from negative. Better policies and improved outcomes are responsible for the favourable rating.