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Macroeconomic challenges before Fiji

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Last week, we discussed Fiji's 2015 growth rate forecasts of two international funding agencies and the Reserve Bank of Fiji (RBF).

Regardless of the differences in 2015 growth rate forecasts in percent (RBF: 4.5; ADB: 4.0; and World Bank: 2.5), it was clear that Fiji has had six years of continuous positive growth. That leads to the common concern: can Fiji sustain these growth rates over the medium term?

Growing investment

It is expected total investment as a percent of GDP would exceed the targeted rate of 25 percent of GDP in 2015. Private sector investment will be 13.5 percent of GDP in 2015. The rise in private investment over the last three years is reflected in the growth rates of investment lending: 28.1 percent in 2012 and 108.8 percent in 2013. Though the rise in investment was only 11.3 percent in 2014, there has been another spurt in lending in 2015: 48.9 percent for the first two months.

Private sector employment has gone up. Jobs advertised rose by 24.6 percent in 2012; 9.3 percent in 2013; 12.8 percent in 2014; and in 2015 up to February: 8.3 percent. Private consumption is increasing. Lending for consumption was up by 25.4 percent in 2012; and 89.6 percent in 2013. There was a slight decrease in 2014: the growth was 72.8 percent in 2014. It has picked up in 2015: already up by 56.4 percent up to February. Increasing trend in capital expenditure (in millions) by government is also seen: 2012: $533.8; 2013: $586.0; 2014:$841.6; and continuing in 2015: $1,321.

The impact of growth gets manifested in several directions. First, the annual fiscal deficit as percent of GDP is on the rise: 0.5 percent in 2013 to 2.0 percent in 2014. In 2015, it is expected to reach 2.5 percent. If the planned asset sales (with estimated receipts of $507 million) do not materialize to the fullest extent, fiscal deficit would be higher than anticipated.

Twin deficits

As it happens, fiscal deficit (government expenditure exceeding government revenues) and excess private sector spending (facilitated by lending) give rise to trade deficit. Trade deficits arise if imports exceed exports. Imports of investment goods (dominated by machinery and construction equipment as well as transport) rose in 2012 by 1.5 percent, in 2013 by 25.1

percent, in 2014 by 45.6 percent, while imports of consumption goods (rice and wheat flour and beverages and a host of manufactured goods) rose by 7.4 percent in 2012, 5.4 percent in 2013 and 30.5 percent in 2014. The trade deficits are offset by earnings from tourism and inward remittance inflows. Tourism earnings (in billion) were: $1.3 in 2013; $1.4 in 2014. Remittances (in million) were $339.1 in 2013; and $383.2 in 2014. They helped to reduce the size of current account deficit, defined as the net balance between total payments for imports of goods and services and total external receipts from exports of goods and services.

Rising current account deficits

Current account deficits as percentages of GDP send out a signal in regard to external stability of the currency. They are rising. In 2012, it was 1.8 percent of GDP: in 2013 it was 14.9 percent. It came down to 8.9 percent in 2014; but is expected to go up to a close 10 percent.

Not all current account deficits are worrisome. If there is steady growth in capital inflows, preferably, durable and non-volatile foreign direct investment (FDI) inflows in productive areas, unlike hot money, which are speculative in nature and pulled out any time, there is no worry. However, if FDI inflows are insufficient, it is the foreign reserve position which becomes critical. Fiji's reserves, which were high at US$ 915 million in 2012, have been declining to US$ 755 million in 2013 and US$ 750 million in 2014. Policy makers are aware that Fiji has to repay US $250 million, which was raised through issue of international bond in 2011. With the strengthening of the American currency, the debt obligations would mount in Fiji dollars.

In its March monetary policy statement, the RBF cautions that positive outcomes of past expansionist policies have "filtered into some pressure on Fiji's balance of payments position". Although inflation has remained low due to "soft global commodity prices (oil and food) and low trading partner inflation", one cannot be sure of the continuity in such a favourable climate in these days of uncertainties.

So, the macroeconomic challenges have to be met soon. The authorities have to change gears, to fiscal and monetary tightening.

As the saying attributed to Oliver Cromwell goes, "Have faith but keep the powder dry."