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Special Funding for Cyclone Rehab

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With the latest estimates of cost of damages, we have a grimmer picture emerging almost on a daily basis. In addition, there are shortages developing in the supplies of normal, daily consumption needs and building materials, indicating the possibility of rise in domestic price level. Further, we have the news that additional purchasing power is being injected by way of distribution of welfare payments.

In a speech at the listing of Vision Investments on the South Pacific Stock Exchange, Reserve Bank of Fiji (RBF) Governor expressed fears of likely rise in price level in the next six months. One of the twin objectives of RBF is containing price level. Though there is no definite inflation target, the objective is not more than 3.5 percent to 4 percent.

IMF Report

As recorded by latest (January 2016) IMF Article IV Mission Staff Report, inflation during last three years has been low: 2.9 percent in 2013; 0.5 percent in 2014; and 2.8 percent in 2015, thanks to low world commodity prices including that of oil.   The Governor was optimistic that any immediate domestic price level increase would be alleviated to a greater extent if the agriculture sector recovers with improved supply position of root crops and vegetables in the second half of the year.

The Governor also focused on the second objective: foreign reserves, which are at a "very comfortable level". The IMF Report says reserves have been US$990 million or 5.3 months of imports in 2013; US$1010 million or 5.2 months of imports in 2014; and US$1.062 million or 4.8 months of imports in 2015.

However, the emerging shortages have to be met with greater volume of imports than before. The exports earnings are likely to decrease due to adverse impact of cyclone on exports of sugar and other agricultural products. Although rise in aid and remittances would certainly add to the reserves, the pressures on domestic price level are obvious. Rising consumption impact would be higher on non-tradables and given the shortages, it would be translated into rise in real exchange rate, hurting exports including tourism earnings. In that event, the RBF Governor indicated the need for “addressing the sustained pressures on foreign reserves”. The appropriate measures would include “assessing special funding from IMF”.

IMF assistance

Fortunately, over past four decades, the purpose of the IMF's lending has changed dramatically. We are aware of “harsh conditionlaities” resulting in belt tightening measures, prescribed for borrowing countries, facing crises in balance of payments, which arise usually from years of fiscal deficits and poor policies. Those crises are a result of self inflicted wounds caused by inadvisable expansionary policies.

The IMF has become “kinder and gentler” to countries facing problems not of their making but due to external shocks beyond control. These shocks include terms of trade shocks, natural disasters, post-conflict situations, broad economic transition, poverty reduction and economic development, sovereign debt restructuring, and confidence-driven banking and currency crises.

For countries in crisis, facing any adverse reserve position due to natural disasters, like Fiji, IMF assistance would be only “a small portion of the resources needed to finance their balance of payments.” But the purpose is to signal to the rest of the world that “the country's economic policies are on the right track, which reassures investors and the official community, helping countries find additional financing from other sources”.

The reason is IMF is not a development bank.

Investment needs

The advice would be to approach multilaterals including World Bank or Asian Development Bank for capital needs.

The Vanuatu case of Post Pam Reconstruction is relevant here. Like Fiji, Vanuatu’s economic policies and fiscal and monetary policies have been prudent.

Following the 2015 March cyclone, IMF approved a disbursement of Special Drawing Rights (SDR) 8.5 million (about US$11.9 million) under the Rapid Credit Facility (RCF) and a purchase in the equivalent of 8.5 million (about US$11.9 million) under the Rapid Financing Instrument (RFI).

The RCF provides rapid financial support in a single, up-front payout for low-income countries facing urgent financing needs, whereas RFI enables the country to purchase SDR, as and when required.

The RCF and RFI are intended to help the member country cope with its immediate foreign reserve needs and to “catalyze critical donor support for the recovery.” The RCF loan carries a zero interest rate with a grace period of 5½ years, and a final maturity of 10 years.

Once the immediate foreign reserve needs are met by IMF assistance, which also endorses credit worthiness of the country, and after assessing the full cost of damages inflicted on the infrastructure and public and private properties, Fiji can approach ADB for loan and grant assistance for re-construction and technical advice on design and advice on cyclone proof dwellings.

Fiji may need investment funds.

It is obvious the aid and remittances received would only meet the immediate and basic needs and they finance only consumption components.

Any loan assistance from ADB can also have a component for on-lending to Fiji Development Bank to provide loans to those needing assistance in construction of houses.

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