Savenaca Narube: The Fiji economy – facing the global crisis

Summary of an address by Mr Savenaca Narube, Governor of the Reserve Bank of Fiji, to the Fiji Australia Business Council, Suva, 2 December 2008.

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Global crisis

- Looking at a snapshot of domestic economic conditions, the economy declined heavily in 2007 but is recovering this year, albeit at a low growth rate. The trade deficit is widening and exerting pressure on foreign reserves. Moreover, inflation rose to a 20-year high but is expected to moderate in 2009. Investment has fallen. Unemployment is rising and poverty is worsening. Now Fiji faces the global financial crisis.
- The IMF has revised world growth successively, down to 3.7 percent this year and is expecting a global recession, with growth forecast at 2.2 percent in 2009. Of our trading partners, New Zealand, Japan and the Euro-zone are in recession, while growth in the US and Australia has slowed considerably.
- The crisis has resulted in sharp swings in the Fiji dollar vis-à-vis the currencies of our trading partners. However, the Nominal Effective Exchange Rate remains stable.
- The financial crisis will affect us through the recession in our major markets and also in the changes to the exchange rate.

Exposure to trade in goods and services

- Fiji's commodity exports will be affected insofar as external demand falls. Hence, demand-driven exports, such as tourism, water and garments are likely to slow down. Supply-driven exports, while unaffected from the global crisis, are bound by on-going structural constraints. Overall, there is likely to be a slowdown in the growth of total exports.
- Tourism is anticipated to be under threat from the fallout of the global financial crisis. Visitor arrivals from the US, Europe and Japan are already falling, while New Zealand tourist arrivals are flat. The Australian market remains resilient and is a key source of growth. Exchange rate movements, particularly with the Australian and New Zealand currencies, will further dampen demand.
- Personal remittances are likely to decline further.
- Overall, imports are expected to rise. The weakening of the Fiji dollar, coupled with higher duty, is likely to raise the price of cement and cars out of Japan, dampening demand. On the other hand, the strengthening of the Fiji dollar against the Aussie and Kiwi dollars will lower food prices received from Australia and New Zealand. However, demand may be inelastic.
- The trade balance may worsen.

Growth outlook

- After contracting in 2007 (-6.6%), our economy is showing some recovery in 2008 (1.2%). Forecasts for 2009 and 2010 are 2.4 percent and 1.9 percent, respectively.

- The major drivers of growth are tourism, agriculture, manufacturing, mining and water, while the major drag, particularly for 2010 and 2011, is the reduction in Government expenditure, following the fiscal stimulus expected for 2009.
- These growth rates are too low, compared to our Pacific neighbours and similar small island developing countries.

Key challenges and policy mix

- Our key challenges are:
  - Safeguarding Fiji's external position
  - Raising exports
  - Raising investment
  - Raising and sustaining growth
- Budgetary measures
  - Pro-growth (fiscal deficit is 3% of GDP for 2009, support for priority sectors – tourism, agriculture, ICT)
  - Balance of Payments (BOP) support – bio-fuel, import substitution (increase in tariffs), enticing Fiji diaspora
  - Investment – infrastructure development, tax incentives
- Monetary measures
  - BOP – credit ceiling, exchange controls
  - Investment – low interest rates, special approvals for priority sector lending
- Government has indicated an expansionary stance for 2009. While a good increase is noted for capital expenditure, operating expenditure is too high, as a percentage of GDP. Nevertheless, the deficit is sustainable.
- On money and credit conditions, commercial banks' lending rate continues to decline and was around 8 percent in October. Our lending rate is the lowest in the region. Lending for investment purposes is rising.
- Monetary policy objectives – year-end inflation are still expected at 7.5 percent but will moderate next year. Foreign reserves remain under pressure.

Summary

- Current weak domestic economic fundamentals will be exacerbated by the global financial crisis. The key challenges must be met with coordinated monetary and fiscal policies.
- The current policy mix is appropriate. There is a need to raise growth in the medium term and the only way to do this sustainably is to raise exports of goods and services.