



The Interim Minister for Finance, National Planning & Sugar Industry, Mahendra Chaudhry, this morning delivered the Revised 2007 Budget Address. The Budget revises the Original 2007 Budget previously announced by the SDL-led Government in November 2006 ("OB-2007").

In the following pages, the Kontiki Weekly summarises the main elements of the Budget, with particular emphasis on the capital/financial markets and investment environment.

The Budget was produced under a tight timeframe following the coup of December 2006. As a result, many of the announcements are general policy "signals" only with specific details to be worked out in the coming months. Furthermore, only limited information has been released to the public.

Strategy

The Budget adopts a 3-pronged approach:

1. **Stabilisation** (Short Term) - of Government finances and the economy.
Government has chosen not to increase the deficit to "spend its way out of trouble" but has instead focused on (i) limiting the deficit and (ii) shifting funding from operational to capital expenditure. In view of the reductions in Government revenue, this has necessitated large cuts in operational expenditure.
2. **Quick Recovery** (Medium Term) – By targeting productive areas of the economy through budget allocations, incentives and other areas. These include forestry, agro-business, marine products, audio-visual, ICT, mineral water, tourism and sugar.
3. **Sustainability** (Medium to Long Term) – Laying a platform for growth based on responsible financial management and export growth.

| Fiji Revised Budget Estimates (\$'000) | | | | | |
|---|----------------------|-----------------------|------------------|-----------------|-----------------|
| | 2007 Revised A | 2007 Original B | 2006E C | Change A - B | Change A - C |
| Estimated Revenue : | | | | | |
| Direct Taxes | 430,559 | 485,928 | 387,953 | -11% | 11% |
| Indirect Taxes | 879,788 | 953,375 | 776,716 | -8% | 13% |
| Others | 155,137 | 166,191 | 151,479 | -7% | 2% |
| Total Operating Receipts | 1,465,484 | 1,605,495 | 1,316,147 | -9% | 11% |
| Total Investing Receipts | 6,161 | 71 | 30,474 | 8626% | -80% |
| Total Estimated Revenue | 1,471,644 | 1,605,565 | 1,346,621 | -8% | 9% |
| Estimated Expenditure: | | | | | |
| Operating | 1,178,259 | 1,253,738 | 1,145,944 | -6% | 3% |
| Capital | 277,432 | 300,025 | 282,916 | -8% | -2% |
| Value Added Tax | 116,679 | 157,080 | 119,804 | -26% | -3% |
| Total Estimated Expenditure | 1,572,370 | 1,710,843 | 1,548,663 | -8% | 2% |
| Estimated Net Deficit | (100,726) | (105,277) | (202,042) | -4% | -50% |
| Debt Repayments | (270,320) | (270,644) | (192,409) | 0% | 40% |
| Gross Deficit | (371,045) | (375,921) | (394,451) | -1% | -6% |
| Net deficit as a Percentage of GDP | 2% | 2% | 4% | 0% | -50% |
| GDP | 5,079,139 | 5,153,697 | 5,031,579 | -1% | 1% |
| Real GDP Growth | -2.5% | 2% | 3% | -225% | -174% |
| Inflation - estimates | 3% | 4% | 3% | -25% | -3% |

**Immediate Measures**

- The **budget deficit** has been held at 2% of GDP through:
 - A 5% cut in civil service wages and salaries across the board;
 - A freeze on all new recruitments and creation of new posts; and
 - Reductions in allocations to non-priority departments/areas
- **Capital expenditure** has been largely held steady, just \$22.6m (8%) lower than in OB-2007 and \$5.5m (2%) lower than in B-2006.
- With total revenues for the year expected to be \$133.9m or 8% lower than in OB-2007, Budget cuts have focused on **operating expenditure**. Total operating expenditure is \$75.5m (6%) lower than in OB-2007.
- Government has signalled a need to reduce **interest rates** to encourage investment and reduce the cost of doing business. To achieve this, adequate liquidity and preservation of foreign exchange is targeted through the following:
 - RBF has assured that "...adequate liquidity will be injected ... when needed."
 - Government to explore borrowing from offshore over the next 2 years
 - Government to examine (i) raising the minimum requirement for foreign exchange that foreign investors bring in (ii) linking corporate taxes to the amount of profits retained in Fiji and (iii) ways to tighten the leakages of export earnings out of Fiji.
- There have been some adjustments to **tariffs** and **excise duties** for luxury and various food items (*refer Appendix 1*).
- As part of Government's social welfare agenda, **VAT** has been maintained at 12.5% while the rate of **welfare payments** has been maintained over OB-2007, with \$19m allocated for poverty alleviation and family assistance grants.

| Sector | 2007 National Revised Budget Allocation (\$'000) | | | | | |
|---|--|------------------|------------------|------------|-----------|-------------|
| | 2007 | 2007 | 2006E | Change | Change | % of Total |
| | Revised | Original | | | | |
| A | B | C | A - B | A - C | | |
| Education | 320,678 | 333,989 | 298,886 | -4% | 7% | 20% |
| Infrastructure | 179,200 | 232,000 | 184,000 | -23% | -3% | 11% |
| Law & Order | 186,335 | 212,374 | 220,486 | -12% | -15% | 12% |
| Military | 80,740 | 85,956 | 76,487 | -6% | 6% | |
| Police | 69,947 | 77,558 | 68,802 | -10% | 2% | |
| Prisons Department | 13,544 | 14,333 | 13,231 | -6% | 2% | |
| Judiciary | 12,473 | 12,482 | 12,473 | 0% | 0% | |
| Legislature | 1,485 | 11,492 | 11,782 | -87% | -87% | |
| Other Law & Order Areas | 8,146 | 10,553 | 37,710 | -23% | -78% | |
| Health | 150,808 | 155,370 | 144,969 | -3% | 4% | 10% |
| Agriculture Fisheries Forests | 62,036 | 46,761 | 48,208 | 33% | 29% | 4% |
| Tourism | 13,987 | 17,269 | 19,116 | -19% | -27% | 1% |
| Women, Social Welfare & Housing | 29,282 | 34,944 | 26,518 | -16% | 10% | 2% |
| Fijian Affairs, Culture & Heritage, Provincial Development & Multi Ethnic Affairs | 54,656 | 85,753 | 44,618 | -36% | 22% | 3% |
| Commerce, Industry, Investment & Communications | 16,639 | 15,523 | 12,467 | 7% | 33% | 1% |
| Other Areas | 558,750 | 576,860 | 549,396 | -3% | 2% | 36% |
| TOTAL | 1,572,370 | 1,710,843 | 1,548,663 | -8% | 2% | 100% |



Measures for Recovery and Growth

General measures include the following:

- \$2.5m is allocated to implement selected recommendations of the **National Export Strategy**. Government has signalled that these will be progressively increased in future budgets.
- The current **export income deduction** of 50% will be maintained in 2007 and reviewed in 2008.
- **Industrial zones** around the country similar to the Valelevu and Vatuwaqa zones will be established to encourage small and medium-sized businesses.
- Government will explore the establishment of a **microfinance** bank to encourage small and medium businesses.
- The entire system of **concessions** will be reviewed with the intention of creating a level playing field and ensuring concessions are effective.

Measures for priority sectors include:

- **Tourism:**
 - Active dialogue with Australia and New Zealand through foreign missions to lower or remove existing negative travel advisories.
 - Fiji Visitors Bureau marketing grant reduced to \$10m (OB-2007: \$15m, B-2006: \$13m). This will be counterbalanced by the establishment of a marketing fund under the FVB whereby Government matches each dollar contributed by the industry.
 - FVB to be directed to increase its marketing efforts in Asia to diversify tourist sources. Likewise Air Pacific will be encouraged to expand its destinations accordingly.
 - Development of tourism-agriculture linkages through turn-key packages provided by Government to investors.
- **Forestry** – Government to explore returning ownership of mahogany plantations to landowners and encouraging downstream processing.
- **Agro-business:**
 - An assessment of how to better meet the demand for eat and vegetables required by the tourism sector from local production to be carried out.
 - Merger of Food Processors Ltd and the Agricultural Marketing Authority with privatization "...as soon as practically possible" to encourage local production and marketing.
 - Encouragement of strategic partnerships in green-house farming
- **Audio-visual** – The Fiji Audio-Visual Commission to be reorganized. No specifics provided.
- **ICT** – Kalabo Tax Free Zone to be designated an Information Technology Zone with operators granted a 10 year tax holiday with effect from 1 January 2007.
- **Sugar** – Reform to continue as a priority with a target of lifting production from 3 to 4 million tonnes in 3 years. The focus will be on upgrading mill facilities, improving the transport system, modernizing farming methods and diversifying into value added opportunities such as electricity cogeneration and ethanol production. Importantly, a cane quality based system will be introduced in the current crushing season. \$11.2m has been budgeted including \$9m EU grant for industry reform (B-2006: \$1.7m)

Investment Environment / Cost of Doing Business

In an effort to raise private sector investment and total investment to ~20% of GDP, the Budget announced various measures to create a more conducive investment environment:

- A revamp of the **investment approvals** process will involve:



- Reorganisation of the Companies Office
- Reform of the physical planning process within Government agencies and the property registration process
- Reform of the contract enforcement process and winding up procedures to improve credit collection.
- In **telecommunications**, Government will promulgate the Telecommunications Bill and establish a Telecommunications Authority. The Bill seeks to open up the telecom industry to competition and break up the existing telecom monopolies.
- An equitable framework for **land tenure** will be developed by Government and the NLTB to benefit both landowners and tenant farmers. In addition, Government will identify, develop and parcel arable land for leasing to potential farmers. \$1m has been allocated for this.
- **Government reform** will include:
 - Keeping the number of ministries at 16
 - Moving to a common services model to remove duplication e.g. corporate services
 - Establishing a task force for change management to drive productivity and efficiency
 - Privatisation of public enterprises
- Promotion of **good governance** will see the establishment of the Fiji Independent Commission against Corruption and a Special Unit of the Ministry of Finance to investigate allegations of abuse.
- **The banking system** will see RBF install an automated payment system between banks this year. In addition, Government has announced that it will examine the most effective way of regulating bank fees and charges and establish a Financial Ombudsman to address complaints from customers of financial institutions.

Implications for Capital Markets

Specific measures for the Capital Markets include:

- Allocations for the CMDA (\$810,400) and South Pacific Stock Exchange (\$250,000) have also been retained. The capital markets have again been mentioned as a key area for economic growth.
- Removal of the income tax exemption for Fijian Holdings Property Trust Fund (FHPT) - This tax exemption had originally been introduced to bring FHPT into line with other general (i.e. not property-focused) unit trusts, which are tax-exempt provided all profits are paid out to unit holders and not retained by the trust. The removal of tax exemption is part of Government's attempts to create a level playing field for all taxpayers.
- Removal of the tax-free dividend status for dividends paid by FHPT, Colonial First State Income Fund and the Colonial First State Income & Growth Fund – same reason as above.
- The above amendments do not apply to the Unit Trust of Fiji and the Fijian Holdings Unit Trust. These have apparently been left alone because they are seen as catering for "grassroots" investors with low minimum entry requirements.
- The sale of Government's FTV shares is budgeted to raise \$6m (no change from Original 2007 Budget).
- Government intends to quickly privatise the merged entity comprising Food Processors Ltd and the Agricultural Marketing Authority (see above).
- No other sales of shares or privatizations of Government entities are specifically mentioned or budgeted for. However the Budget clearly states an intention to divest shares in public enterprises, and we are aware that a list of candidates is being finalized for presentation to Cabinet.



Appendix 1

| 2007 Fiscal and Import Excise Changes | |
|--|--|
| POLICY | Description |
| Lamps and lightning fittings | Increase fiscal duty from 3% to 15% |
| Cinematographic Film | Increase fiscal duty from 3% to 15% Impose import excise of 10% Further, the valuation rates have been increased to \$15,000 and \$20,000 for English and Hindi films respectively |
| Statuettes and ornamental articles of ceramic | Increase fiscal duty from 3% to 15% |
| Luxury Items | Increase fiscal duty from 3% to 15% |
| <ul style="list-style-type: none"> * Perfumes & toilet waters * Beauty-make-up preparations * Hair preparations * Pre-shave and after shave preparations * Leather goods of a kind normally carried in pockets & bags * Leather case, boxes & similar containers for camera lenses, binoculars etc * Glass jewellery and ornaments * Diamonds whether or not worked * Precious stones and semi-precious stones, other than diamonds whether or not worked * Synthetic or reconstructed precious or semi-precious stones including duct and powder * Silver indifferent forms * Metals claded with gold * Platinum, palladium, rodium etc * Various precious metal clads * articles of jewellery * Articles of goldsmith or silversmith wares * Imitation jewellery * Chain mesh-handbags, purses, wallets & similar articles * Fans * Refrigerators & freezers * Dish washing machines * Cloth washing machines Electro mechanical domestic appliance - vacuum * cleaners, floor polishes, kitchen waste disposers, food grinders & mixers and other appliance * Shavers - Hair clippers, Hair removing appliance * Hair dryers * Hair dressing apparatus * Hand drying apparatus * Smoothing irons | |



Appendix 1

| | |
|--|---|
| * Microwave ovens | |
| * Other cookers | |
| * Coffee/Tea Makers | |
| * Toasters | |
| * Microphones | |
| * Single loud speakers | |
| * Multiple loud speakers | |
| * Other Similar goods | |
| * Headphones and earphones | |
| * Amplifiers | |
| * Turntables, record players, cassette players etc | |
| * Tape recorders | |
| * Video recorders | |
| * Television cameras | |
| * Reception apparatus (radio) | |
| * Reception apparatus (televisions) | |
| * Cameras | |
| * Sunglasses | |
| * Binoculars | |
| * Watches | |
| Meat of Sheep, fresh, chilled or frozen | Increase fiscal duty from 3% to 15% |
| Meat of Goat, fresh, chilled or frozen | Decrease fiscal duty from 27% to 15% |
| Liquid milk | Decrease fiscal duty from 27% to 15% |
| Yogurt | Decrease fiscal duty from 27% to 15% |
| Cheese in Retail Pack | Decrease fiscal duty from 27% to 15% |
| Cheese in Bulk | Decrease fiscal duty from 27% to 3% |
| Breakfast food code 123 | Decrease fiscal duty from 15% to 3% |
| Potato chips | Specific duty of \$4.45 per kg will be decreased to \$3.00 per kg |
| Video monitors | Import excise of 10% |
| Reception apparatus for television | Import excise of 10% |
| Recorded tapes and discs | Import excise of 10% |

| Excise Changes | |
|-------------------|---|
| POLICY | Description |
| Carbonated Drinks | Removal of excise duty on carbonated drinks but 3% fiscal duty + VAT will be payable on raw materials |



KONTIKI
CAPITAL

Appendix 1

IMPORTANT NOTICE

Although the statements of fact in this communication have been obtained from and are based upon sources that the Firm believes to be reliable, we do not guarantee their accuracy, and any such information may be incomplete or condensed. All opinions and estimates included in this communication constitute the Firm's judgment as of the date of this communication and are subject to change without notice. This communication is for informational purposes only. This communication is made available in the Republic of Fiji through Kontiki Capital, a licensed investment advisor.

© Kontiki Capital Ltd., 2007. All rights reserved. Any unauthorized use, duplication or disclosure is prohibited by law and will result in prosecution.