

Political Conditions

Ethnic tensions and overall political instability mark Fiji's recent political history. In July 2003, the Supreme Court ruled that the Indian-dominated Fiji Labour Party (FLP), led by Mahendra Chaudhry, must be represented in the Cabinet. The decision comes amidst an ongoing power struggle between the FLP and the governing party, the Soqosoqo Duavata ni Lewenivanua (SDL) or Peoples Unity Party, led by Laisenia Qarase. It was hoped that the long-awaited Supreme Court ruling would ease political uncertainty in Fiji, however, Mr. Chaudry rejected Mr. Qarase's offer of 14 junior seats in an enlarged Cabinet and the post-2000 political impasse seems to be protracting.

Political stability is vital to future economic growth. Current uncertainty concerning land-leases and the future of Indian tenant farmers is at the forefront of racial tension that has hampered economic growth and deterred private investors. In 1997, thirty-year leases for farmers began to expire and Indian tenant farmers are being removed from Fijian-held property. The fate of Indian tenant farmers and the land-tenure issue is a high political priority for the government.

Economic Data

	1999	2000	2001	2002	2003f
GDP Growth	9.5	-3.2	4.3	4.4	5.1
CPI inflation (avg. per year)	2.0	1.1	4.3	0.9	4.0
Budget Balance (% of GDP)	-0.6	-3.4	-6.5	-7.0	-5.9
Current Account Bal. (% of GDP)	-4.5	-6.3	-3.6	-5.0	-3.7
Foreign Reserves (US\$ mn)	402.6	386.5	341.5	331.5	N/A

Sources: Economist Intelligence Unit, Asia Development Bank, Reserve Bank of Fiji.

Real GDP rose by an estimated 4.4% in 2002, largely driven by wholesale and retail trade (which benefited from strong consumer spending), as well as growth in the transport and construction sectors.

The economy was sluggish in the first quarter of 2003, the result mainly of a decline in tourist numbers and overall global economic weakness. Nevertheless, consumer spending has continued to be strong and, coupled with increased visitor numbers, the economy recovered in the second quarter. Barring a further increase in political instability, the medium looks favourable for the Fijian economy, with the Asian Development Bank (ADB) projecting health growth in 2003 and 2004.

The increase in headline inflation from 1.6% in December 2002 to 4.7% in September 2003 mainly reflected an increase in Value-Added Tax (VAT) - from 10% to 12.5% - in January 2003, which pushed up the price of food, household durables, alcohol and tobacco. The Reserve Bank of Fiji expects an average headline inflation rate of 4% for 2003, followed by a fall in 2004 as the impact of the rise in VAT passes.

Government endeavours to reduce debt

The government maintained an expansionary fiscal stance in 2002, with the budget deficit increasing to a substantial 7.0% of GDP, from 6.5% the year before. The recent VAT increase is designed to increase the government's revenue base and assist its effort to reduce the revenue shortfall. The government has planned to cut the deficit to 4% of GDP in 2003, however, the Reserve Bank of Fiji anticipates a budget deficit of 5.9% for 2003. Nevertheless, over the medium term the projected economic expansion should stimulate a further improvement in the government's fiscal balance.

The 2004 budget was presented in November 2003 and aims to reduce the deficit to 3.5% of GDP. In order to meet this target, the government emphasised the need for greater control of expenditure by improving adherence to planning processes. The 2004 budget is based on a 1% reduction in total expenditure and a 20% cut in capital spending. The spending split in 2004 is expected to be 82% on operating expenditure and 18% on capital expenditure, but the government reiterated its target of achieving a 70:30 spending mix by 2005. The government also emphasised the need for further structural reforms to make the economy more efficient and plans to be more assertive in implementing specific measures with the overall environment for reform assisted by the recent improvement in economic growth.

The sugar industry continues its decline

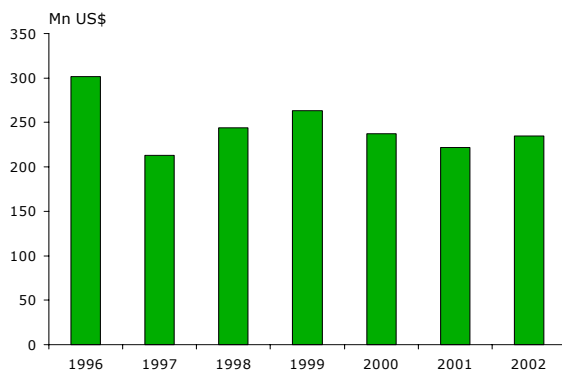
Apart from tourism, sugar is the biggest industry in Fiji, directly employing around one-quarter of the population. However, the industry is facing problems as Indians are barred from owning land and there is uncertainty over the renewal of leases. Additionally, high production costs (US\$28 per tonne, compared to US\$5-6 per tonne in Australia and Brazil), have undermined the sector's prospects.

Further restrictions on growth in the sector have resulted from the cane payment system - a system based on quantity rather than quality - and financial problems of the state-run Fiji Sugar Corporation, which has lost around FJ\$40

mn in each of the past two years. The future of the sector is placed in further doubt as the preferential treatment in sugar exports Fiji receives from the EU is endangered by Australia's challenge at the WTO against EU sugar subsidies. Approximately half of Fiji's exports of sugar go to the EU.

In its budget for 2003, the government has allocated funds to help revive the industry by restructuring the Fiji Sugar Corporation, creating four stand-alone companies answerable to their respective stakeholders. Restructuring will involve upgrading the mills and improving the transport and handling systems.

Sugar Export Earnings



Source: Reserve Bank of Fiji

Investment remains at low levels

After peaking at almost 30 per cent of GDP in the late 1970s and early 1980s, investment fell to an all time low of 10 per cent in 2000. Investor confidence has been low in recent years and private sector projects have been held back due to political and land tenure uncertainty.

In addressing these concerns, the Fijian government is committed to making the investment environment more attractive. The government is working toward maintaining macroeconomic stability, and implementing structural reforms to promote competition.

Government is keen to the diversify economy

The government is attempting to diversify the economy, in order to reduce the reliance on the agriculture sector (especially sugar crops), which is vulnerable to harsh weather conditions. Encouragingly, growth in 2002 was relatively broad-based. The implementation of tax-free export zones in order to promote the manufacturing industry is an example of the government's diversification agenda.

Fiji has a comparative advantage in providing skilled labour to private investors. Fiji is the

South Pacific Islands communications and transport hub. The hosting of the South Pacific Games in June 2003 further enhanced its status as a regional centre. Fiji has world standard air and road links and a well-educated population with English as the official language.

Tourism is vital to the Fijian Economy

The tourism sector is the key to the diversification of the economy. Apart from being the country's chief source of foreign exchange, the tourism sector contributes around 20% of GDP. The industry has recovered well from the steep decline in visitor numbers that followed the political instability of mid-2000.

In 2003, the war in Iraq and the SARS virus adversely impacted visitor arrivals early in the year. However, the industry has rebounded strongly and in August 2003, visitor arrivals were up 5% on the corresponding period in 2002, according to the Reserve Bank of Fiji. The strength of the recovery in tourist arrivals is such that, based on current trends, visitor arrivals in 2003 are likely to surge to a record level. Furthermore, it is anticipated that visitor arrivals will increase 2004.

The Fijian government realizes the importance of the tourism sector and the 2003 budget provides marketing grants totalling FJ\$13 mn to the Fiji Visitors Bureau, as well as funds for infrastructure projects.

Balance of Payments

Fiji's Direction of Trade - 2001

Exports		Imports	
US	28.6%	Australia	43.8%
Australia	19.6%	NZ	14.7%
UK	10.6%	Singapore	8.4%
Japan	5.1%	Japan	3.8%

Source - Department of Foreign Affairs and Trade, Australia

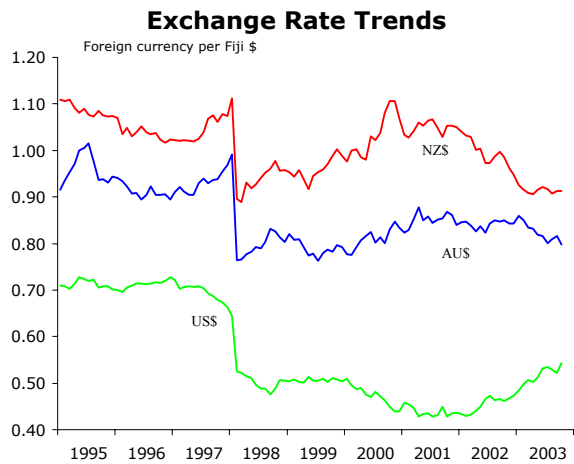
In 2002, there was a 3.6% increase in overall exports, reflecting the continuing recovery in gold exports. Increased imports of minerals, machinery and transport equipment and fuels, led to a 9.8% rise in overall imports. As a result, the visible trade deficit widened and coupled with increased investment income outflows, the current account deficit increased to 5% of GDP, from the 3.6% of GDP recorded in 2001.

At end-May 2003, overall exports have increased by 8% on the year-earlier level. This rise was largely the result of higher earnings from clothing exports, as well as higher

international prices for sugar. Imports at end-May were up 17%, reflecting increased demand for consumption goods and machinery and transport equipment.

Exchange Rate

Between end-2002 and end-September 2003, the FJ\$ has depreciated against the A\$ by 6.5%, while appreciating against the US\$ by around 12%. In 1997/98, the Asian financial crisis led to the depreciation of many currencies in the Asia-Pacific, placing competitive pressure on the Fijian currency. The FJ\$ was subsequently devalued by 20% in January 1998. At end-September 2003, the FJ\$ was valued roughly at the same level as it was in January 1998 after the devaluation.



Source: Datastream



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