Current economic trends in the South Pacific

This edition of the Pacific Economic Bulletin has drawn on writers from the region to present an appraisal and outlook of their national economy. The editors are grateful for their cooperation. The views expressed are their own and not necessarily those of the institutions with which they are affiliated.

Fiji

Recent growth rates for Fiji have been less than impressive when compared with the levels of four or five years ago, buoyed as they were by extensive growth in the manufacturing sector following the introduction of tax free factories. The Fiji economy grew by just 1.7 per cent in 1993, down from 3.1 per cent in 1992. Although the general downward trend was widespread across sectors, the brunt of the slowdown fell on the non-sugar agricultural sector following the devastation caused by cyclone Kina in early January. Greatly reduced construction activity also contributed. The decline resulted from the completion of several large projects in 1992, including the Parliament building and earthworks at Denarau Island.

The general economic slowdown in 1993 masked progress in a number of areas. The official industrial production index expanded by 5.8 per cent against a 1.1 per cent increase the previous year. The expansion was in both domestic and export industries. Nearly 3.7 million tonnes of sugarcane were crushed in 1993 compared with 3.2 million tonnes in 1992. Sugar production increased by 3.8 per cent to 442,156 tonnes in 1993 while export earnings from sugar in the calendar year were US$231 million compared with US$221 million in 1992. Garment exports, which since 1989 have superseded gold as Fiji’s third largest foreign exchange earner after tourism and sugar, bounced back from a 1992 drop in earnings to record a US$12 million increase for a total of US$129 million.

Tourism

Tourism has been Fiji’s major foreign exchange earner since 1989. Earnings from tourism were estimated at US$364 million in 1993, up from US$328 million in 1992. Recession in source markets in 1991 saw visitor numbers fall away. Since then however, the general upward trend has continued, with tourist arrivals for 1993 at a record 287,462, an increase of 3.2 per cent over 1992. The average length of stay was 8.5 days compared with 8.7 days a year ago. The major source markets for Fiji’s tourism industry in 1993 were Australia (27 per cent), the United States (15 per cent), New Zealand (14 per cent), Japan (13 per cent) and Europe (10 per cent). The declining share of Australian tourists has been a matter of concern for the industry. The decline is due to competing...
destinations in Asia and the deregulation of the airline industry in Australia. More Australians are taking domestic vacations as a result of the reduction in domestic fares. Recent data indicates that future strength lies in the North American, Japanese and European markets; however, the Fiji tourist industry is also working hard to retain its share in the traditional Australian and New Zealand markets.

Hotel industry sources are optimistic about the future of tourism following economic recovery in the industrialised countries. The 295,000 tourist arrivals initially projected for 1994 could easily be exceeded with Air Pacific flying to Los Angeles from July and a third weekly flight to Japan also commencing soon. Increased arrivals are also expected from Europe. Data for the first four months of 1994 indicate arrivals running at more than 11 per cent above the corresponding 1993 period.

The move away from portraying Fiji as a purely sun, sea and sand destination towards ecotourism will have an impact on the industry and appropriate facilities will need to be developed if Fiji is to capitalise on this new opportunity. The industry is also set to benefit from ‘Visit the South Pacific Year’ in 1995 and ‘Visit Fiji Year’ in 1997. The increase in visitors to the region as a result of the Olympic Games in Sydney in the year 2000 presents a further opportunity for the industry.

Inflation, wages and productivity
There has been a progressive decline in the inflation rate over 1993 and the first four months of 1994, largely due to the influence of low inflationary pressures in trading partner countries: much of Fiji’s inflation is imported. In addition, the impact of the introduction of a value added tax in July 1992 fell out of the calculation in the latter half of the year. The year-on-year increase in the consumer price index at the end of 1993 was 3.0 per cent, significantly below the 6.3 per cent recorded over 1992. The downward trend has continued in 1994: the year-on-year index rose by 2.0 per cent in April.

Fiji’s labour force in 1993 was 268,000. Of this, paid or formal sector employment was 95,254. The increase in employment in the formal sector was 2 per cent, a similar growth rate to that recorded for 1992. Paid employment has generally increased from the 1989 level as a result of the creation of tax free factories in Fiji. In 1993, employment in these factories increased by 9 per cent to 13,327, mainly as a result of new entries to the garment industry under the scheme. The growth in paid employment has been achieved mainly through the private sector and reflects government policy favouring an export-oriented economy through private sector investment.

The government has continued to emphasise the linking of wages to productivity. A number of employees, both in the private sector and local government, settled on rates ranging from 5 to 7 per cent in 1993. Some industries in the private sector have quoted higher rates due to increases in productivity and their ability to pay to retain skilled workers. Following the military coups in 1987, the rate of emigration affected several occupational groups, in particular professional and managerial workers. These skills were replaced on a temporary basis by hiring expatriates, while training programs and skills development were undertaken to ensure responsiveness of the labour force to the demands of the market. Despite these programs and a fall in the rate of emigration, industry sources still cite skills shortages in the garment and building and construction industries.

Balance of payments
The balance of payments position weakened considerably in 1993. After a surplus of nearly US$80 million in 1992,
the position reversed to a deficit of US$66 million in 1993. Both the current and capital accounts ended the year in deficit, reversing the surpluses of the previous year.

The merchandise trade deficit widened, with a 24 per cent increase in imports more than offsetting a 4 per cent expansion in exports. The increase in imports was due mainly to the importation of an aircraft, although there was also increased demand for consumer merchandise, particularly food and manufactured goods, and a higher value of machinery imports. Export proceeds from sugar, garments, gold and fish all increased. Although there was an increased surplus on the services account arising from higher tourism receipts, this was not sufficient to offset the trade deficit.

As a result of the overall balance of payments deficit, the level of external reserves declined in 1993, reversing the large increase of the previous year. Gross external reserves of the Reserve Bank were US$415 million at the end of 1993 compared with US$498 million at the end of 1992. The level of reserves at the end of 1993 was equivalent to 5.4 months of retained imports of goods (cif) and debt service payments.

Although detailed official figures are not yet available, the balance of payments recorded an overall deficit in the January–April 1994 period, with the seasonal absence of sugar receipts. The level of reserves declined further from December 1993 to US$337 million, equivalent to 3.8 months of retained imports (cif) and debt service payments.

**Monetary policy**

Monetary policy continues to focus on liquidity management and the close monitoring of private sector credit growth, and its impact on Fiji’s foreign reserves and inflation rate. Money broadly defined (M3) rose by 6.5 per cent in 1993 compared with 14.1 per cent a year ago, due mainly to a slowdown in the growth rate and a decline in deposit rates. Private sector credit growth is currently averaging 14 per cent on an annual basis. The impact of the rising trend in credit on reserves over the first four months of 1994 is difficult to assess given that there is also a seasonal downturn due to the absence of sugar production at this time of year.

Open market operations continue to provide the major tool of monetary policy. Reserve Bank notes/bonds were used in the day-to-day management of liquidity of the banking system and resulted in a reasonable rate of return on short-term investments to institutional investors.

The level of Reserve Bank notes/bonds outstanding at the end of 1993 was US$111 million compared with US$165 million at the end of 1992. The latest figures for May 1994 show that with the relatively low level of liquidity in the banking system, the level of Reserve Bank notes/bonds outstanding was US$75 million.

Further relaxations in exchange control were effected in January 1994, mainly in the area of investment-related policies, as a more permanent solution to the problem of excess liquidity. The exchange rate of the Fiji dollar is linked to a weighted basket of currencies of Fiji’s major trading partners. Over the year to April 1994, the Fiji dollar appreciated in nominal terms against the deutschemark, pound sterling, Australian dollar and US dollar. Depreciations were recorded against the Japanese yen and the New Zealand dollar. These movements in the rates mainly reflected changes in the cross rates of the major currencies.

The real effective exchange rate index in the March 1994 quarter appreciated by
0.6 per cent over the December quarter, but showed an overall depreciation of 0.2 per cent over the year. This depreciation reflects a significant fall in the differential between Fiji’s inflation rate and those of its major trading partners.

1994 Budget

The revised Budget for 1994 was presented to Parliament by the Minister of Finance on 6 April 1994. It emphasises government’s commitment to an export-led, low cost and high growth economy. The key elements of the government’s economic policies as outlined in the revised 1994 Budget are

• deregulation of the economy to bring domestic prices more closely in line with world prices
• restraint in the growth of government expenditure to ensure availability of resources for growth in the private sector
• reform of the system of direct and indirect taxation to minimise market distortions and improve incentives for risk taking and effort
• a wage policy that recognises the paramount importance of maintaining international competitiveness
• the mobilisation of all sectors of the community in support of economic expansion
• the reorientation of specific sector policies in accordance with the above general policies.

The net deficit for 1994 is projected at about US$69 million or 2.9 per cent of GDP and is expected to be financed mainly from domestic sources. The net deficit of 3.7 per cent recorded in 1993 was largely the result of an increase in outlays due to increases in wages and salaries and allocations for rehabilitation and relief operations following cyclone Kina. In addition, revenue collections—in particular from customs and excise—were about 10 per cent lower than in 1992, partly due to tariff reductions associated with trade liberalisation.

Outlook

The outlook for 1994 is for growth above 3 per cent. Indications are that sugar production is likely to be around 475,000 tonnes (an increase of over 7 per cent). The outlook for tourism is optimistic and there is also expected to be renewed activity in the building and construction sector, together with an expansion in gold mining and manufacturing.

An important consideration for the future is the impact of GATT on the sugar industry. Efficiency will be an issue that will need to be addressed in terms of cane quality and the pricing structure. With the government looking towards diversification of the agricultural sector, the private sector will need to identify appropriate projects.

For 1994 therefore, growth prospects are upbeat, inflation has moderated, employment is expected to pick up, and the deficit is expected to fall. However, there are lessons to be learnt and Fiji must cushion itself against uncertainties and proceed slowly in areas where caution is warranted. The development path should be mapped out and the strategies proposed adhered to in order to secure long-term gains.

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Papua New Guinea

At a time when the financial resources available to the government are expanding strongly, providing opportunity, Papua New Guinea finds itself facing additional problems. Oil and mineral revenues in 1994 were budgeted at 250 million kina more than in 1992. This money might have been spent on such basic needs as rural
infrastructure and primary education and health services to equip people better to realise their economic opportunities. Instead, half of the additional oil and mineral revenues was distributed to consumers through tax and tariff reductions; and new and increased expenditures absorbing 80 per cent of the revenue increase were programmed. Accordingly the budget deficit continued to widen to unsustainable levels. A mini-Budget in March this year only partly closed the gap. Meanwhile the conflict on Bougainville is proving intractable—a situation affected to some extent by a different sort of conflict between the New Guinea Island provinces and the State over proposed reforms to the system of provincial government—lingering questions over the prime ministership debilitate executive government, and unemployment and underemployment continue to rise.

Political and constitutional reform

The Bill to repeal the organic law on provincial government and to enact the organic law on provincial authority and local government (OLPALG) has been withdrawn for further drafting.

Sub-national governments are to have their own revenue-raising powers, some of which appear to be less appropriate than others. One question is whether the organic law would entrench and even amplify inter-provincial differences in income and wealth. Transfers from the national government to the provinces are to be guaranteed on area and population bases, that is, independent of a province’s level of development. Taxing powers, on the other hand, would yield revenues related to level of development. In particular the goods and services tax, the developed property tax and road-users’ tax would favour the already better-off provinces. The National Economic and Fiscal Commission provided for under the OLPALG has no powers, other than to recommend to the national government additional transfers to the less well-off provinces. It is likely to suffer the same fate as the existing similarly constituted National Fiscal Commission, which didn’t function for very long.

The executive

The strong government that Paias Wingti promised the nation on being elected Prime Minister by one vote in mid-1992 is looking increasingly fragile. The legislature gave the executive arm of government wide-ranges powers in the Internal Security Act to curtail people’s freedoms. The Supreme Court has, however, already ruled some of them unconstitutional. Early in 1994 a major cabinet reshuffle took place, with Sir Julius moving from Finance to Foreign Affairs, John Kaputin took over Mines and Petroleum from Masket Iangalio who, completing the circle, slipped into the Finance chair. With some prompting from the central bank, Masket Iangalio lost little time in reversing some of his predecessor’s tax and expenditure measures, using the drop in the oil price as the trigger for a mini-Budget in March.

Business environment

A survey conducted by the Institute of National Affairs in November 1993 revealed private sector concerns about the policy environment, consultation with government and the economic and political outlook. Almost two in five firms are operating below 75 per cent capacity utilisation. Three out of four firms see no increase in capital expenditure in 1994; one in four will spend less; half of the private sector expects no growth over the next three years; one in four firms expects to contract or is uncertain. Shortage of skilled local labour, unreliable public utilities or services and poor infrastructure are constraining growth. The policy environment is essentially negative for the private sector: two in five firms see no
improvement in economic conditions three years hence; almost one in four expects them to be worse. Almost half the private sector is either uncertain about the political climate three years from now or thinks it will be less favourable than now. Twice as many firms think the political climate will be less favourable.

Of two-thirds of the private sector is unhappy with the forms and quality of consultation with the national government. One in three firms view such consultation as erratic or deteriorating. The private sector is even less happy about provincial government consultation, cold comfort for the national government. Of great concern is the fact that the private sector spends 3 per cent of sales revenue on combating law and order problems. For about half the private sector this is at least equal to capital expenditures; for one in 4 firms it is more. Four out of 5 firms spend at least as much on law and order as on employee training; 2 in 5 spend more.

Fiscal imbalance

One year after the 1993 budget the anticipated surpluses had become a budgeted deficit of 243 million kina in 1994—likely to widen to 400 million kina—and a projected deficit of 220 million kina in 1995. Expanding deficits, planned and unplanned, will almost double public debt outstanding in the 3 years ending 1994, despite rising revenues from minerals and oil. Interest payments will consume 10.5 per cent of expenditure in 1994, rising to 12 per cent in 1997. It is not easy to discern the increased non-mining output, employment and revenue that will flow from the rapid rise in debt.

Compared to 1993, capital expenditure’s share of total expenditure is down 14 per cent in 1994; maintenance’s share of capital expenditure is down 20 per cent; and design’s share of capital expenditure is down 26 per cent.

The March mini-Budget

Adjustments to government policy were made by the new Minister for Finance and Planning, Masket Iangalio, in March 1994. The mini-Budget was prompted by the deterioration in the fiscal outlook, made worse by falling oil prices. Expenditure cuts of 54 million kina and new revenue measures of 81 million kina were introduced. Cuts were made in grants to local government, in appropriations to the village services scheme, in district urban development, higher education, housing, highways and provincial transport programs, and alternative financing (through aid) of the armed forces housing project was arranged.

Revenue adjustments were made through increases in personal income tax rates, an increased duty level on fuel imports and increases in standard rates of import duties.

Output

Mining, oil and gas has contributed to more than one-third of the increase in GDP since 1990. Sector exports in 1993 were twice those in 1988 prior to the closure of the Panguna mine in May 1989. The sector is now contracting and accordingly GDP in 1994 is projected to decline marginally. New developments in the pipeline are expected to reverse the decline, beginning with Lihir. Private non-mining sector development has been steadier and less spectacular than mining, with growth between 1990 and 1993 of 10 per cent.

Agricultural export volumes rose in 1993 over 1992 for palm oil, copra and coffee but fell for cocoa. Palm oil output has increased seven-fold since 1980 as new nucleus-estates have converted older copra and cocoa plantations on alienated land. Copra production seems to have responded to the price support, but the opposite changes in coffee and cocoa suggest that agronomic and climatic conditions are also important.
conditions have more than offset the effects of price support.

Log exports reached an all time high in 1993, providing a boon through higher-than-budgeted export taxes for the highly expansionary budget and a bane for policy which seeks to phase the industry out of log exports into processing. The policy conflict spread to the industry, including the landowners, with the issues being strongly contested in the media. Recent inventory measurements show that the sustainable extraction rate is only half what government has been planning on.

Employment

Members of the Employers’ Federation of Papua New Guinea expect employment to rise in the first half of 1994, reversing the decline since 1989. The expected rise, 5 per cent, would follow declines of 2.5 per cent, 0.5 per cent and 1 per cent in previous half-yearly periods respectively. Half-yearly changes in employment reflect seasonal demand for agricultural labour. Measuring annual changes, employers expect employment in June 1994 to be 2.5 per cent up on June of the previous year. These expectations may be optimistic. Employment in December 1993 was down 3 per cent on the previous December, twice the June annual decline. Moreover, similar expectations a year ago did not materialise. As well, the delay in Lihir, expected to commence construction in the June quarter this year, seems certain to keep actual employment below expectations.

The Bank of Papua New Guinea’s survey shows a 10 per cent decline in non-mining employment, compared with the 20 per cent estimate of the Employer’s Federation (including mining) between 1989 and 1993. In both surveys most of the decline occurred between 1989 and 1991. Between 1992 and 1993 both surveys registered a 3 per cent decline in employment. The contraction in employment in 1993 was broadly based, affecting all regions and all industries.

Prices and wages

Agricultural export prices in 1993 averaged 8 per cent higher than in 1992 for coffee, only marginally so for cocoa but lower for copra (by 5 per cent) and palm oil (3.5 per cent). World commodity prices are currently in an upswing (see Rutherford this issue). These price developments should relieve pressure on the budget deficit through lower price support payments. Log prices in 1993 averaged 240 per cent higher than in 1992. These prices peaked in the March quarter 1993 and have since halved.

Under arrangements just completed, there is a three year agreement under which public sector pay will be based on performance. This provides for annual increases up to 6.3 per cent in two components: a cost of living adjustment of 3 per cent and individual performance appraisal. The structure aims to improve productivity and impartiality, and competence in its implementation will be crucial to its success.

Enterprise agreements in the market sector, following the 1992 deregulation, show a similar trend towards adopting these two bases for pay adjustment — cost of living and performance. Concerns that wage settlements in the capital-intensive mining, oil and gas sector might have flowed through to other sectors lacking the same capacity to pay have so far been unfounded. Major projects are too isolated and remote and employ too few people to exert economy-wide labour market influences.

Consumer prices were raised 6 per cent by the 10 per cent devaluation in January 1990, the pass-through being completed in 18 months. Since then, inflation has resumed its increasing trend
at a rate of 4.5 per cent per annum. The December quarter 1993 saw a slight quickening in inflation; surprising in the light of declining world inflation, especially in Australia, the source of many of Papua New Guinea's consumer goods.

Trade, exchange rate and reserves
Exports increased by 700 million kina (or 40 per cent) in 1993. Oil contributed almost three-quarters of the increase with Kutubu's first full year of production. Oil production peaked in the June quarter of 1994. Log exports almost trebled and accounted for 37 per cent of the increase in exports, agriculture for 6 per cent. Gold and copper exports declined by 9 per cent and 18 per cent respectively of their 1992 values.

Compared with the corresponding period a year earlier, in the week ended 11 May 1994, the kina had weakened against the yen by 5 per cent, against the New Zealand dollar by 4 per cent and against the Australia dollar by 1.5 per cent. It strengthened against the deutschmark by 5.5 per cent and against the US dollar by 1.5 per cent.

The current account for 1993 recorded a surplus of 535 million kina or 12 per cent of estimated GDP. Net foreign assets of the banking system reached a low point in March 1993. International reserves covered 1.7 months of non-mining imports in December 1993, up from 1.4 months in September. The level of reserves remains low as the resources sector runs down its external debt and the government finances expanding deficits with domestic borrowings.

Money and interest rates
The Bank of Papua New Guinea changed its target variable for monetary policy in 1993 from private sector credit to total money supply. This change accompanied the foreign exchange liberalisation announced in the 1993 Budget. It assumes stability in the velocity of money and in the money multiplier.

The money supply increased by 174 million kina or 12 per cent in 1993. The bulk of the increase was due to an increase in net credit to government, and in movements in private sector credit and net foreign assets. Excluding mining and petroleum and advances under the price support schemes (totalling 104 million kina in 1993) total private sector lending decreased by 8.8 per cent, all in the second half. Borrowers' utilisation of credit limits declined over 1993 from 81 per cent to 70 per cent. Commercial banks' free reserves margin increased from 9 per cent to 17 per cent over 1993 and in the week ended 11 May 1994 to 25 per cent.

Foreign direct investment
In 1993, Australia was the largest foreign direct investor in Papua New Guinea, accounting for two-thirds of total foreign equity holdings. The United States held 12 per cent and the United Kingdom, 10 per cent. Japan and South Korea held 2–3 per cent each, Hong Kong, 1.6 per cent and Singapore, 0.8 per cent. Papua New Guinea experienced a net foreign divestment in 1992 and 1993 of some 3 per cent and 4 per cent respectively. These reductions occurred in the mining sector. Foreign equity holdings in the non-mining private sector increased by 10 per cent in nominal terms between 1989 and 1993, a real decline of 12 per cent. Dividends were paid out in 1992 and 1993 at the average rate of 14 per cent on the value of equity holdings. Whereas Asian investment is only a small proportion of the aggregate, it is increasing under Prime Minister Wingti's 'Look North' policy.

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Solomon Islands

The 1994 balance of payments performance of Solomon Islands has shown growth in the trade account which recorded a US$30 million surplus during the first four months of the year. Provisional data show exports grew 44 per cent over the same period last year, maintaining the upward trend started in mid-1992. This increase is predominantly led by the unsustainable extraction of forest resources. The heavy dependence on log exports is a major structural weakness of the economy and it is the first time since the 1960s that the export base has been so dependent on a single commodity, contrary to the overall objective of export diversification. Although fish exports are showing signs of recovery after two successive years of poor production, the other main exports—notably palm oil, copra and cocoa—are still depressed by low commodity prices. Imports meanwhile, were 5 per cent down on the same period last year, continuing the downward trend noted since the third quarter of 1993. However, with the increase in disposable incomes generated by the logging windfall and fiscal expansion, it is expected that imports will rise in the latter half of 1994. The tendency for consumption to march in line with the rise in current incomes has been witnessed in the past, even when the increase in incomes has proved to be temporary. External reserves rose 42 per cent to US$88 million by mid-May, reflecting the positive balance of payments performance during the period. In terms of reserve cover, this was equivalent to just over 2 months of imports of goods and non-factor services.

Exchange rate policy remains unchanged and continues to be governed by the need to protect competitiveness in the traded-goods sector. Against the trade-weighted basket, the Solomon Islands dollar depreciated 10 per cent during 1993, although against the Australian dollar (the main import currency), the movement was negligible. This positive situation is being reversed in 1994 with the Australian dollar strengthening on international foreign exchange markets.

Logging

Logging activities continued unabated at a rate estimated to be twice the sustainable level during the first four months of 1994, despite concern and numerous calls from various sections of the community to reduce harvesting to sustainable levels. Over 260,000 cubic metres of round logs were approved for shipment through the price monitoring mechanism between January and May 1994. Recent clashes between landowners and a major logging company in the Western Province once again highlight the need to pay particular attention to the concerns and interests of resource owners and to ensure maximum benefits from logging accrue to them.

The government recently announced its intention to introduce a ban on round log exports in 1997. However, there appears to be no mechanism in place to ensure that logging companies do not intensify their operations in the interim period. An immediate, but gradual reduction in the level of harvesting to sustainable levels would have been a more appropriate strategy. The need to strengthen monitoring, inspection and surveillance capacities of relevant government agencies and a review of the current tax structure on logging to ensure an economic rent from forest resources for government and resource owners are other important policy areas requiring urgent government action. The process of reform will be difficult for any government to take on, however, it must be done to ensure long-term sustainability of the forestry sector and an orderly development of the Solomon Islands economy.
**1994 Budget**

The 1994 Budget (passed at the end of 1993) signalled the new government's determination to address its fiscal imbalances. A national economic summit was convened to discuss a wide range of pressing economic issues, the results of which are being incorporated into the National Development Plan drawn up by the government. Consultation on a structural adjustment package with the International Monetary Fund is also at an advanced stage and should be concluded in the latter part of 1994. This program is envisaged to cover a wide spectrum of economic issues and will create a basis for economic recovery and growth. The three main pillars of the package are public sector reform, sustainable management of forest resources and encouragement of private sector-led growth.

Revenue collection grew 13 per cent in 1993—better than budgeted. This was largely attributed to increased tax revenues from log exports which doubled in 1993 to over US$60 million. Several taxation changes were also introduced in early 1994, including an 8 per cent goods tax, an expansion in the coverage of the sales tax, and a new 47 per cent tax imposed on high income earners of more than US$60,000 per annum. This temporary improvement in revenue performance was not, however, invested or used to reduce government debt but financed increased recurrent expenditures and hence the need for further domestic borrowing.

Efforts to curb and control expenditures appear to be having little success. This is reflected by the government resorting to heavy domestic borrowing from the financial system despite increased revenue collections. The government borrowed US$61 million domestically in 1993. In the first 4 months of 1994, this pattern continued, regardless of the stringent guidelines imposed by the 1994 Budget. As a result, the US$22 million earmarked for domestic borrowing for the whole of 1994 was already surpassed by mid-April. This trend must be reversed to prevent another explosion in government domestic borrowing which cannot be sustained without further deterioration in other sectors of the economy. The apparent lack of fiscal discipline and the unsustainable rate of government expansion, driven by the growth in recurrent expenditures, constitutes a major threat to economic recovery in Solomon Islands.

Monetary growth, reflecting developments in the external account and domestic credit, rose 10 per cent in the first half of 1994. The main increase was in demand deposits, highlighting the tendency for the private sector to hold more liquid financial assets—probably due to the uncertainties surrounding government demand for credit and the sustainability of the rise in incomes from logging. This is reinforced by the commercial banks' apparent reluctance to convert the rise in liquidity to private sector credit, but instead increasing their deposits with the Central Bank. By mid-May 1994, these have exceeded US$30 million following government instructions to cap the issue of new treasury bills and bonds. Domestic credit rose 15 per cent in the first 4 months of 1994 as a result of increased borrowing by government which rose 10 per cent to US$290 million, while credit to the private sector rose by 6 per cent to US$94 million. The growth in credit to the private sector (evident since 1993), after several years of decline and stagnation, is an encouraging development which is increasingly being threatened by the government's high demand for domestic credit. Interest rates have seen a welcome decline of 2–3 percentage points in 1993 in both lending and deposit rates. The commercial banks weighted average
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lending rate fell from 18.7 per cent in 1993 to 15.6 per cent in 1992, while the average deposit rate fell from 9.4 per cent to 7.6 per cent during the same period. The reduction in interest rates has been aimed at stimulating growth in private sector credit which has seen a turnaround in 1993. These rates have been maintained during the first 4 months of 1994.

Inflation, which moderated to 9 per cent in 1993, is again under pressure: the annual movement to April 1994 shows a 11.8 per cent rise in prices, predominantly accounted for by local cost-driven factors. These included recent taxation changes, fiscal expansion, the rise in incomes related to the logging sector boom, and seasonal weather patterns which adversely affected the supply of local food items.

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Tonga

The Tongan economy has experienced a moderate but sustained rate of economic growth during the last 6 years, averaging 1.8 per cent. After allowance is made for the strong growth in transfers, both official aid and private remittances, real disposable income grew by 2.2 per cent. Given the stable population size, this translates into an acceptable economic performance, and a success by Pacific island standards. However, this success story has been dominated by two main factors: the exports of squash to Japan, and growth in transfer receipts of aid and remittances. Together these items account for two-thirds of current account receipts. While a high degree of economic specialisation may be expected for a very small, open economy such as Tonga, the reliance on a narrow range of income-generating activities puts development on a fragile basis. The major challenge facing the economy is to build on past success and develop new niche market activities.

Exports

Economic growth in 1993–94 is estimated to be 4.2 per cent, reflecting the significant growth in squash exports, construction and tourism. However, while squash production was a substantial contributing factor there is evidence to suggest that this was achieved by a decline in domestic agriculture as producers switched to more lucrative overseas markets. A squash export quota for the 1993 season was set at 13,000 tonnes compared with export volumes of 10,000 tonnes in the 1992 season. Shortage of local squash in Japan eventuated due to poor weather conditions, allowing the Tongan exporters to exceed their quotas substantially. Final export volumes surpassed 17,000 tonnes with prices also rising as the quality of the Tongan product was seen as the best ever. The 1994 season sees the export quota being lifted to 15,000 tonnes with a further 2,000 tonnes held in reserve for excess production. While in the early phases of development of the industry there was a need to ensure the quality of the exports, the continued imposition of a quota is of dubious value. Although controls may generate monopoly rents in the short run, it is far from clear that regulating the market is in the best interest of the Tongan economy (see Duncan, this issue, on commodity markets).

Manufacturing output has remained stagnant over the last five years, but the composition of production has changed significantly. In the late 1980s, the Small Industry Center saw significant growth in exports of manufactures, and the sector was seen as a potential development path for the economy. However, poor management together with deteriorating market conditions overseas resulted in
existing enterprises going out of business. Industrial output was maintained through production for the local market behind protective tariffs.

The tourist sector has been experiencing sustained growth since the end of 1992—albeit from a low base—and in 1993/94 grew by 10 per cent; making a small but important contribution to the economy. While Tonga does not present the same tourist potential as certain other Pacific island economies, potential does exist, particularly in the outer islands. As a future avenue for development, tourism affords potential but requires a firm commitment before gains will be realised. During 1993/94 the construction sector grew by 13 per cent with considerable investment in the financial sector contributing the record GDP growth.

Inflation

The annual rate of CPI change recorded 1 per cent for the year ending March 1994. The CPI fell significantly during 1993 reflecting the return of normal food supply conditions following the drought of 1992. The underlying rate of inflation has gradually declined after a period of high inflation following the impact of the fiscal expansionary period from 1989–91. Since 1992 the underlying rate of inflation has fallen from 4 per cent to the current rate of 3 per cent. However, at the present time the domestic component of inflation is approximately 4.7 per cent, significantly above the imported rate of 1.7 per cent. This indicates that Tonga is becoming less competitive and its export performance is threatened.

Government Budget

After a period of fiscal expansion in the late 1980s resulting in the fiscal deficit climbing to 7.5 per cent of GDP in 1991/92 following a 33 per cent civil servant pay rise, additional revenue measures and expenditure constraint has returned the situation to balance. In 1992/93 the government ran a small surplus. At the beginning of 1993/94 the situation deteriorated, with expenditures rising and revenues falling. This out-turn was reversed early in 1994, with buoyant levels of receipts following the record squash season and expenditure coming under control. For the 1993/94 period, the government is expected to run a small deficit funded through multilateral aid, but with an accumulation of resources with the domestic banking system. While the recent return to fiscal balance is welcome, it has been achieved through restricting the non-emolument component of expenditure with resulting loss in efficiency in the provision of government services.

The 1994/95 Budget has just been prepared and proposes a continuation of current policies with the estimates for both revenues and expenditures being cautious. While the document expounds a sensible orientation towards export markets, there is little discussion of how this desirable objective will be implemented. New revenue measures are included with additional taxes on imported beer, cigarettes and fuel, but at the time of writing the outcome of these measures is uncertain. While the rates of tax on fuel and cigarettes in Tonga are low by international standards, the impact of the extra tax on imported beer will be to raise the already high rates of effective protection afforded to domestic manufacturers. The expenditure estimates appear unrealistic with provisions for civil servant pensions being understated. This item has grown by 25 per cent since 1989/90 and is forecast to fall by 28 per cent in the coming year. However, after compensating for these various factors it is not unlikely that the fiscal position will deteriorate during the coming 1994/95 period, unless a substantial award is again given to civil servants following the current five-yearly negotiations. If a similar outcome to 1989/90 was to
eventuate, financial stability would be seriously jeopardised, eroding the gains and improved performance the Tongan economy has experienced in recent years.

The financial sector

After a period of sluggish performance the financial sector in Tonga has experienced rapid development since November 1993 with the opening of two new banks. The pace of business has stepped up with competition encouraging better services and greater lending to the private sector. After a three-year period when credit to the private sector stagnated, it is currently growing at 19 per cent per annum. This primarily reflects greater vigour of the existing banking sector, but also additional lending by the new banks. If it had not been for the reduction in demand for credit by the government, growth in overall domestic credit would have posed a severe strain on the financial system, threatening foreign reserve levels and inflation. An expansionary monetary period has thus been accommodated through prudent fiscal policies.

However, the future poses policy dilemmas. The new banks will need to find new customers, thus expanding the credit base. While the current civil service pay discussions are unlikely to result in a pay increase of the previous magnitude, any additional award would likely incur a demand for credit from the public sector. If the private sector demand is coupled with renewed public needs, the resulting credit expansion would be unsustainable. Credit restraint would almost certainly lead to a ‘crowding out’ of private demand, which at the present stage of financial development would be undesirable, and reinforces the need for coordination between monetary and fiscal objectives.

Interest rate objectives have been to maintain real interest rates and positive differentials with overseas. Measuring inflation using the underlying rate, the real interest rate objective has been met. Given essential capital mobility in the balance of payments, maintaining interest differentials with those overseas becomes the more critical variable. During the last two years, the average differential with Tonga’s trading partners has moved from a negative to a balanced position. The current firming of interest rates overseas as the world moves out of recession and attempts to maintain non-inflationary growth suggests a similar rise may be necessary in Tonga, especially if the domestic credit market continues to overheat. Pressure for a change in monetary policy has been averted as deposit interest rates have firm in the domestic market as banks compete for funds. However, as the situation stabilises and competitors establish a market share, forces will materialise for a change in monetary stance.

Balance of payments

On the external side Tonga has maintained balance in the current account of the balance of payments and the foreign reserves have risen to healthy levels in recent years: sufficient to cover more than six years of imports. However, the balance of payments structure remains fragile with a limited number of foreign exchange earners. The exchange rate is pegged to a basket of currencies, which has remained unaltered since the pa‘anga ceased to be linked at par to the Australian dollar in February 1991. The rapid rate of inflation that followed the fiscal expansionary period in the late 1980s resulted in a substantial appreciation of the real exchange rate. The real exchange rate has stabilised since the beginning of 1991, with minor appreciation subsequently as domestic inflation has exceeded that of Tonga’s trading partners. Real appreciation has coincided with a growing economy and the evidence suggests largely with full employment of resources. Under such circumstances policy should
be oriented towards limiting domestic inflationary pressure and microeconomic reform rather than any nominal depreciation, which would simply be eroded through inflation.

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Vanuatu

After two robust years of growth in 1989 and 1990 when the economy grew in real terms by 4.5 per cent and 5.2 per cent, respectively, growth slowed down considerably in 1991 to around 2 per cent. This downward trend persisted in 1992, aided by the fears and apprehension normally associated with any change of government. In Vanuatu’s case, the result was a decline in the real production of goods and services by 2 per cent. However, this recession was short-lived as the new economic push under the banner of free enterprise produced immediate positive results, evidenced by the 4.2 per cent real growth in 1993. Last year’s growth was largely driven by the services sector although the net contribution of the agricultural sector was positive, with the increase in squash pumpkin, and coffee and cocoa exports. The economy seems to be in a position to repeat last year’s performance, again with the services sector being the locomotive.

Inflation

Despite the strong economic growth last year, domestic inflation was maintained at an impressive 1.7 per cent: the lowest rate in the last decade. Only in 1982 did the economy record a lower rate, 1.4 per cent. This very low inflation rate was the result of many factors, the major ones being the continued low inflation in Australia and New Zealand (which account for the bulk of Vanuatu’s imports), the steady levels of the vatu and Australian dollar and the New Zealand dollar exchange rates, and the increasing competition between the three major wholesalers and supermarkets in Port Vila to accommodate their new and ongoing capacity expansions. Inflation was still in check in the first quarter of this year; however the vatu began to weaken against both currencies in April and May but particularly against the Australian dollar which, if it persists, will have an adverse impact on domestic inflation.

Balance of payments

After a bad year in 1992 when both the overall balance as well as the current account experienced net outflows of 452 million vatu and 2,744 million vatu, respectively, the new economic push by the government also had a positive impact on the external account. The nominal overall balance of payments returned to a positive level of 1,835 million vatu. By March this year, provisional data revealed that the nominal overall balance had declined by 993 million vatu. Part of this decline is attributable to the strengthening of the vatu against the US dollar: an appreciation of 3.8 per cent.

Post-Uruguay

The recently concluded GATT Agreement is giving some serious concern to the Vanuatu authorities as it appears the Agreement is biased against tree crops such as copra, cocoa, coffee, in that it reduces their marginal advantage or preference in international trade. The Vanuatu authorities are planning to establish a working committee to address this issue for long-term planning.

Money supply

Domestic credit advanced by the commercial banks reached 6,487.9 million vatu in March this year: an 8.5 per cent increase over December 1993. The level of
domestic credit throughout 1993 was higher than in 1992—a major factor behind the high real growth rate last year. Commercial banks’ claims on the government by the end of March stood at 864.8 million vatu, while lending to the private sector remained almost unchanged at 7,921.3 million vatu from the December 1993 level of 7,941.6 million vatu.

Reflecting the developments in domestic credit at the end of March, the broad money supply (M4) was almost unchanged at 24,226.7 million vatu compared with 24,371.4 million vatu in December 1993. Currency with the public increased by 2.1 per cent by end March as compared to end December last year, reflecting the buoyant state of the rural cash economy; while demand deposits of residents (excluding government) in vatu increased in March by 2.5 per cent, mirroring the robust state of the urban economy. Total vatu liquidity increased by 4.8 per cent by the end of March to 9,156.1 million vatu, the highest since the country’s independence in 1980 and a positive indication of the state of the overall economy. Only demand deposits of residents denominated in foreign currencies registered a sharp decline of 19.4 per cent during the first quarter of 1994, reflecting the lacklustre state of the offshore and exempt banking centre.

Agriculture

Copra and cocoa, which together account for 30–40 per cent of all agricultural production, experienced a decline in production compared to the March quarter of 1993. This seems to be the consequence of false rumours in the islands about a lack of copra funds held by the Vanuatu Commodities Marketing Board, while excess rainfall late last year and early this year damaged a lot of cocoa flowerings, particularly on Malekula which accounts for two-thirds of the country’s cocoa production. Despite improved copra prices between December 1993 and March 1994, the value of copra exports was 15.9 per cent lower than the March 1993 quarter. Other commodities seemed to have done better which is reflected by their levels of exports. Cocoa export volume increased by 61 per cent whilst export receipts jumped by 252 per cent, reflecting the further strengthening of its world market price. Kava exports by the Vanuatu Commodities Marketing Board increased by 56 per cent compared to the first quarter of last year. Coffee and timber seemed to remain unaffected. More farmers have entered the squash pumpkin sector and are preparing land after the establishment of a Squash Advisory Committee by the Minister of Agriculture in January this year.

Despite this mixed start, the authorities are quite optimistic about a good year for the agricultural sector. The Vanuatu Commodities Marketing Board is sending senior representatives to the islands to talk to farmers to correct false rumours and encourage farmers to increase production of their produce, while concurrently launching a weekly radio program which encourages farmers to increase production and improve quality by introducing cheaper and simpler techniques of drying copra and cocoa with solar energy. Coupled with this is the bright outlook for prices of copra, cocoa, timber and squash pumpkins as well as the expected increase in production and exports of squash pumpkins and kava.

Services and tourism

The services sector, led by the tourism sector, maintained its buoyancy in the first quarter of this year. Around 8,000 visitors are said to have arrived in Vanuatu in the March quarter and hotel occupancy rates should remain high in the vicinity of 60 per cent. The Radisson Royal Palms resort has just concluded a deal for its purchase by the Meridian hotel chain and Hotel Le
Lagoon is also up for sale as part of the Pan Pacific Hotel restructuring; these two hotels account for 50 per cent of Port Vila’s hotel rooms. The Finance Centre remains strong, buoyed largely by the banking sector. The retail and wholesale and transport (buses, taxis) sectors are down due to the loss of purchasing power of the striking and suspended public servants and teachers. Despite this adverse development, there is now greater competition between three firms (Better Price, Hebrida and Center Point and Bon Marche) in the wholesale and supermarket sector in terms of pricing and physical expansion into the Port Vila suburbs.

Air Vanuatu (Operations) Limited announced in March this year a net profit of US$1.2 million for its 1993 financial year which ended in December. This impressive result was achieved despite the stagnant state of the industry worldwide and mirrors the central role of the national airline in the country’s tourism industry.

**Fiscal reform**

In its effort to come up with a sustainable tax system, the Vanuatu government, appointed a tax consultant early in 1994 through the Australian Technical Assistance Bureau to research and recommend a more sustainable government tax system. The government is maintaining an indirect tax system which is heavily biased towards import duties and which is restrictive in terms of further base expansion and annual sustainable increases in revenue collection.

**Industrial unrest**

Labour developments are still in disarray following industrial action by the Public Servants Association (and the Teachers’ Union who went on a ‘sympathy strike’ on 22 February this year). The striking public servants were suspended and subsequently terminated by the Public Service Commission in March. One hundred and seventy-nine teachers are still on suspension. The efficiency and output of the public sector has been adversely affected by the industrial action. The government has recruited new staff to the public service and the Ministry of Education has recruited temporary teachers to ensure that classes are not discontinued. The government has promised that public servants who re-apply for their posts will be accorded due consideration.

**Housing scheme**

Another interesting development during the March quarter of this year was the launching of the Housing Scheme by the Vanuatu National Provident Fund for its members. Many members have acquired loans to buy government houses which are currently on sale. Although the housing scheme has not yet affected the domestic property market, it is certain that it will put upward pressure on property prices while the house rental market will come under opposite pressure. Most importantly, the government will accrue revenue while ridding itself of old houses and properties whose annual maintenance costs were a drain on the government’s annual budget.

**Franklyn Kere**  
**General Manager**  
**Vanuatu Commodities Marketing Board**

**Western Samoa**

After experiencing negative growth rates in the two previous years, following the devastation of cyclones in 1990 and 1991, the Western Samoan economy registered strong recovery in 1993, when real GDP grew by 7 per cent. However, the slowdown in economic activity during the last quarter of 1993 has continued into the first two quarters of 1994. Economic growth prospects for 1994 are poor as the rapid decline in agricultural production is expected to more than nullify the
improvements in the industrial and service sectors. The weakening of the external sector over the previous two years is also expected to continue into 1994. Net foreign reserves which dropped by WS$20.71 million during 1993 are estimated to have fallen by WS$4 million during the first quarter and a further WS$10 million fall is projected by the end of 1994. Public sector finances which have been under strain from the heavy demands of the cyclone rehabilitation program during 1990–93 are expected to be further weakened by the need to shore up a number of public enterprises and the expected drop in tax revenues as tax reforms are being fine-tuned during 1994. In the light of the above trends, the government in its 1994/95 Budget Statement has announced a number of policy measures to support its strategy of strengthening the production and export base in the medium term through private sector initiatives.

**Agriculture**

Agricultural production which grew by 7.4 per cent in 1993 has been dragged down rapidly as taro leaf blight devastation has reduced taro production from the second largest agricultural product to negligible levels during the first half of 1994. It is estimated that taro supplies at the Apia market during April 1994 were less than half a per cent of the quantities available during the same month in 1993. Taro exports during the first quarter of 1994 amounted only to WS$6,000 compared to WS$2.6 million during the same quarter in 1993. In the absence of an effective pesticide to control the taro leaf blight, taro production is not expected to have any significant recovery during 1994. Improvements in coconut and banana production are expected during 1994. Coconut production, which makes up 40 per cent of agricultural production, is recovering from cyclone damage. Coconut supplies at the Apia market during April 1994 were estimated to be 34 per cent higher than in April 1993. Given that the industrial demand for coconuts has remained stable during the first quarter of 1994 compared to the same period last year, it is evident that the high domestic household demand for coconuts has sustained the price per nut of 12 sene—a price which prevailed during 1993 through to the first quarter of 1994. Production of bananas has rapidly increased as the taro planters diversify their crops and the government through the Agriculture Store expands its commercial scale banana production for exports. Banana supplies at the Apia market during April 1994 were estimated to be nine times the level of April 1993. Banana production for exports during 1994 is expected to be WS$1 million.

**Industry**

Industrial production is estimated to have increased in 1993, led by the growth in the output of electricity, construction materials and the Yazaki production of car parts. These growth points more than offset the drop in production of beer, cigarettes, timber, coconut cream, soft drinks, soap, corned beef and paint. A major expansion of the production capacity of the Yazaki plant is expected to have a positive impact on the performance of the industrial sector, but only in the last quarter of 1994 at the earliest. A modest recovery in coconut cream production is expected to be more than nullified by the expected decreases in the production of the other manufacturing activities. Based on export data for the first quarter of 1994, the declining trend in the production of beer and cigarettes has continued into 1994.

**Services**

The service industry, led by tourism, appears to be the main growth area during 1994. Continued growth in this sector will be dependent on the minimisation of disruptions from the major restructuring of the national airline during the second half of 1994.
Inflation

The annual average inflation rate fell from 8.5 per cent in 1992 to 1.7 per cent in 1993. This favourable performance is attributed to the improvement in domestic production, a sharp fall in inflation in the main overseas trading partners, and the tight monetary conditions. The introduction of the 10 per cent value added goods and services tax in January 1994 and the decline in agricultural production expected for 1994 is expected to cause an upturn in the 1994 inflation rate. The consumer price index has increased on an average per month basis to 15.1 per cent up to March 1994. A reduction in import duties and in the value added tax on a wide range of basic food items and services was passed by Parliament in March 1994 and made effective from 1 April 1994. These changes are expected to slow the inflation rate for the rest of 1994. The annual average inflation rate for 1994 should be in the range of 10 to 12 per cent range.

The external sector continued to weaken during 1993 with an estimated overall balance of payments deficit of WS$20.7 million registered by end December 1993. Imports declined by 3 per cent and exports increased by 15 per cent. The 1993 merchandise trade gap of WS$247 million was financed by WS$31 million from the services account, WS$80 million in net private transfers, WS$115 million from capital inflows and a drawdown on foreign reserves of WS$20.7 million. Whilst the merchandise trade gap improved from WS$257 million in 1993, the earnings from the services account and the net private transfers worsened from their 1993 levels of WS$41 million and WS$107 million, respectively.

During the first quarter of 1994, average monthly exports were WS$600,000, as compared to the 1993 monthly average of WS$1.4 million—reflecting mainly the sharp taro export earnings decline. The average monthly imports for the first quarter of 1994 also fell to WS$16 million compared to the 1993 monthly average of WS$22 million. The decline was mainly in imports of capital goods. Private transfers for the first quarter of 1994 have edged upwards from a monthly average of WS$5.5 million in the 1993 first quarter to WS$6.5 million. Although there are expected improvements from tourist earnings and private transfers, their combined positive impact is expected to be nullified by the sharp deterioration of export earnings for 1994. Net foreign reserves have declined from WS$121 million as of end December 1993 to WS$106 million (or 5.1 months of imports) at end March 1994. Net foreign assets are estimated to decline by a further WS$10 million by the end of December 1994.

Government Budget

The budget deficit of WS$29.4 million incurred in the 1992/93 fiscal year is expected to improve slightly, with a deficit of WS$27.7 million planned for 1993/94. The implementation of revenue reforms in January 1994 was further refined in April 1994. The 1994/95 Budget introduced in June 1994 estimates total annual expenditures at WS$275 million compared to WS$251 million in 1993/94. The 1994/95 expenditures are to be funded from ordinary revenues (WS$195 million), WS$18 million of external projects loans, and WS$62 million capital grant aid.

A budget surplus of receipts over expenditures of WS$400,000 has been estimated for 1994/95. The increase of ordinary revenues from WS$183 million in 1993 to WS$195 million mainly reflects increased collections from the value added tax in its first full year. Net collections to government during 1994/95 are estimated at WS$27 million. The drop in income tax collections from WS$34 million in 1993/94 to WS$28 million reflects the full annual
impact of the reduction of the income tax rates introduced in January 1994. While the 1994/95 current and domestically funded development expenditures have maintained their 1993/94 levels, the distribution of development expenditures shows a strong bias towards grants or capital subscriptions to the statutory corporations and public enterprises. These total WS$21 million out of the total of WS$68 million of domestically funded development expenditures.

The outcome of the 1994/95 Budget will depend on the extent to which the government continues to provide financial assistance to statutory corporations and public enterprises, the pressure of salary and wage adjustments, the timing of the revision of departmental fees and charges, and the flow-through effect on the current budget of the maintenance of expenditures of the recently completed major infrastructural projects. Although the 1994/95 budget estimates do not envisage resorting to domestic borrowing, it is anticipated that any advances to statutory corporations and public enterprises will necessitate domestic borrowing later during the year. The extent of domestic borrowing and the use by the government of the statutory corporations in the financing of public sector projects may crowd out private sector investment. This crowding out risk is expected to increase in the latter half of the 1994 calendar year if the government increases its advances to support the financial restructuring of its national airline and uses the National Provident Fund to finance a major industrial complex to be leased to the government.

Money supply
Money supply (M2) declined by 1 per cent during 1993 resulting from a decline in foreign assets, partially offset by an increase in net domestic assets. The increase in net domestic assets in turn came from an increase in bank credit to the private sector and the public institutions and the decline in the government’s net deposits with the monetary system. For the first quarter of 1994, money supply (M2) is estimated to have declined further from WS$119 million as at end December 1993 to WS$115 at the end of March 1994, resulting mainly from the drop in net foreign assets. For 1994, monetary conditions are expected to be relatively tight as the government attempts to contain the deterioration of the external sector.

Exchange rate
The Western Samoan tala continues to be pegged to a basket of currencies of its major trading partners. On an annual average basis the real effective exchange rate index declined by 3.7 per cent in the 12 months ending December 1993. Increasing pressures on the external sector, projected worsening of the inflation rate compared to those prevailing in its major trading partners, and the 1994/95 Budget announcement that demand management measures will be used to rectify the situation, are all likely to support a decline in the real effective exchange rate index for 1994.

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Western Samoa

Kiribati
According to the current National Development Plan (1992–1995), the major economic policies of the Kiribati government are to diversify and expand the production base, privatise public enterprises, develop the outer islands for a more equal distribution of benefits and achieve greater financial and economic stability. In compliance with these major
objectives, the following economic development has taken place.

The annual population growth rate at the 1990 population census (the latest census) was 2.24 per cent compared with 2.1 per cent at the 1985 population census: the rate of population growth is still on the increase. Consequently, the public sector—the dominant employer of the formal sector labour force—has not been able to meet the growing demand for jobs. It has been estimated that between 1985 and 1990 about one school leaver out of ten obtained a permanent job. Given the pressure on Kiribati finances, unemployment is expected to worsen unless effective measures are taken to address the problem.

To minimise the problem, the government proposed a public service review, the first phase of which was undertaken last year. The main objective of the review was to identify public enterprises which can be privatised, thus reducing the size of the public sector and possibly reducing government expenditure on unproductive enterprises.

This review is facilitating the government’s policy of privatising public undertakings and promoting the private sector in order to create employment. Because of a shortage of local entrepreneurship and capital resources, joint ventures with foreign investors for investment in certain areas (particularly in the outer islands) are accorded high priority. Efforts are also being made to provide institutional support such as credit and marketing facilities for local investors and entrepreneurs and those in the outer islands. The Development Bank of Kiribati has played an important role in this program in providing credit to interested investors in the outer islands.

Between 1980 and 1992, recurrent revenue was growing faster than expenditures. It is expected that in the current period, the position should remain the same. Increased revenue has resulted in less dependence on external finance and reduced drawdown from the Revenue Equalisation Reserve Fund. On the development side, local funds have been insufficient to cover development expenditures and shortfalls have been covered by foreign aid and loans. In 1993, the government financed 3.4 per cent of the total development budget. The remainder was externally financed.

Despite the substantial resources available to Kiribati, there is an urgent need to increase the government’s capacity to utilise aid, particularly in the outer islands.

Air transport to and from Kiribati has improved following the re-opening of the Kanton Airport and the upgrading of Bonriki airport is expected to be completed in 1994. This will improve the development of tourism in Kiribati.

The government has also encouraged marketing of seaweed and bêche-de-mer to supplement the incomes of people in the outer islands. Remittances from Kiribati seamen who work on overseas ships are another important source of income for these people. In 1993, the government of Kiribati supported the agreement between South Pacific Marine Services (a major employer of Kiribati seamen) and the Kiribati Island Overseas Seamen’s Union on the reduction of Kiribati seamen’s wages and salaries with a view to encouraging overseas shipping companies to employ more seamen from Kiribati. From 1 January 1994 the South Pacific Marine Services partner companies agreed to a 9.6 per cent increase in the wages and salaries of seamen.

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