RESERVE BANK OF FIJI

INVESTMENT AND ECONOMIC GROWTH

Governments, organisations and individuals often make plans to achieve some particular goals in the future. Many do this by setting aside funds or spending on certain goods that will bring about future benefits. This process can be called investment. Investment can be defined as expenditure for the acquisition of new plant, machinery and equipment as well as for building roads, houses, hospitals and bridges. Collectively these types of spending are known as capital or physical investment.

Investments that involve putting money aside as fixed deposits with banks or buying shares in a company constitute a financial investment. This form of investment differs from physical investment which increases the country's productive capacity or the ability to produce more goods and services for the future. Such investment leads to the accumulation of a nation's capital stock and helps generate higher output in the economy. For instance, a farmer who purchases a tractor is likely to become more efficient in crop production thereby boosting overall output. Similarly, Government investment via construction of new roads between farming communities and towns would improve connectivity and accessibility for farmers to markets, implying greater opportunity for growth in the economy.

While financial investment is essential as it improves the overall wealth of the nation, physical investment would be more critical for small economies like Fiji which face large infrastructure gaps and where financial investment opportunities are limited.

Investment leads to the creation of new jobs. For example, a businessman investing in a new garment factory would need planners, designers, engineers and construction workers to get his project off the ground. On project completion, the businessman would need machinists, cutters, packers and supervisors. In this whole process, the businessman's investment is providing employment for many who contribute to raising the level of activity in the economy.

A rise in employment potentially means an increase in the number of taxpayers in the country. This in turn should generate higher revenue for the Government through increased direct and indirect tax collections. More tax revenues then allows the Government to provide a greater level of service to its citizens by expanding current programs or by undertaking new projects like investing in new roads, schools and hospitals. This additional spending by the Government provides further impetus for growth. Alternatively, the Government can also retire some of its debt at a faster rate if its revenue base increases.

Furthermore, as more people secure jobs, more will be able to afford the basic necessities of life such as food, clothing, shelter, medicine and education. Thus, sustained investment growth can have a direct positive impact on improving people's living standards and consequently reducing poverty levels.

There are several important factors that can influence or drive investment. One determinant is the level of demand in the economy. When demand for goods and services is low firms will likely postpone investment plans until the economy improves. However, if demand for goods and services rises, they would be inclined to invest more in plant and machinery to increase supply. In addition, existing businesses that are doing well and earning good profits, have an incentive to further expand their investment, thereby contribute more to growth.

Lower borrowing costs, that is, lower interest rates or price of credit, can also influence the investment plans of firms and households. The Reserve Bank of Fiji (RBF) when given the opportunity will use monetary policy to keep a low level of interest rates in the economy that is conducive to investment and growth. Since 2011, the RBF has maintained an accommodative monetary policy stance resulting in a downward trend in interest rates that currently remain at historical lows. We were able to do this because the two core objectives of monetary policy have remained within comfortable bounds.

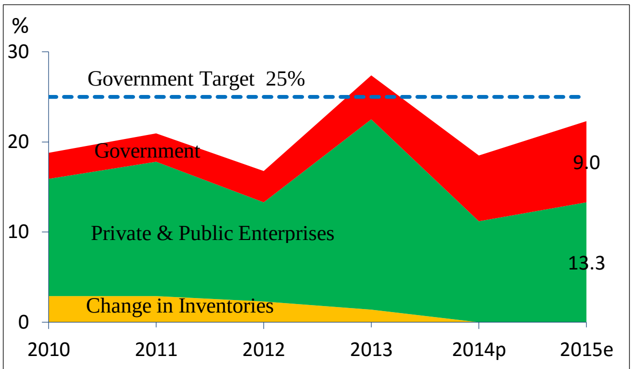
This boosted lending and investment levels over the years consistent with the higher average growth achieved over this period. Nevertheless, other considerations such as stable macroeconomic conditions (including low inflation and adequate foreign reserves), favourable investment policies of the Government and law and order are also important to support investment activity.

The Government invests considerably in the economy through the provision and maintenance of public goods such as roads, bridges, schools and hospitals. In the 2016-2017 National Budget, the Government allocated $1,454.1 million (14.7% of GDP) for capital expenditure. This huge investment will be used to improve the condition and delivery of the country's current public goods as well to replace those damaged by Tropical Cyclone Winston which is expected to assist in increasing Fiji's output.

Similarly, statutory corporations and the private sector also invest considerably in the economy.

For 2015, total investment in the economy is estimated to be around 22 percent of GDP. Of this, around 9 percent of GDP constitutes general Government investment while around 13 percent comprises investment by private and public enterprises.

Investment as percentage of GDP



Source: Fiji Bureau of Statistics & RBF

Such robust investment spending has supported Fiji's strong growth which averaged 4.7 percent over the last three years (2013 to 2015). Investment to GDP averaged 23 percent of GDP – close to its target – over this period. This clearly shows that higher investment spending is a key driver for growth. The Government maintains an investment target of around 25 percent of GDP that is essential for sustainable growth in the economy.

Notwithstanding its importance, measuring investment in the economy is not easy. The Fiji Bureau of Statistics carries out numerous surveys to determine the level of investment, which can be complex, costly and time consuming. In light of data limitations, the RBF relies on various partial indicators such as domestic cement sales, investment lending, investment imports and construction sector statistics that it solicits from various sources to produce more timely analysis on investment trends. In addition, the Bank conducts biannual Business Expectations Survey, to get feedback from businesses on their expectations for investment in the future.