RESERVE BANK OF FIJI ECONOMIC FOCUS

Investment and Economic Growth

Investment, in the economics literature, is largely defined as expenditure on the acquisition of new plant, machinery and equipment. Building of roads, houses, hospitals and bridges also constitute investment spending. Collectively these kinds of spending are known as capital expenditure or physical investment.

Investments such as putting money aside as a fixed deposit with banks or buying shares in a company constitute a financial investment. The latter form of investment differs from physical investment in the sense that physical investment generally improves a country's productive capacity or the ability to produce more goods and services into the future. Such investment leads to the enhancement of a nation's capital stock. While financial investment is important, as it provides an indicator of the overall wealth of the nation, economists when monitoring a country's growth prospects track the physical investment expenditure of households and business firms.

There are many desirable benefits of investment expenditure. As we increase a nation's stock of capital, the ability of an economy to produce more goods and services also improves. For instance, a farmer investing in a tractor is likely to be more efficient in planting his/her crops. This is likely to lead to a bigger harvest in the subsequent years. Similarly, a Government investing in a road from the farm to a nearby town would assist the farmer in transporting his crops to the local market. As such, investment generally leads to higher output in the economy.

Investment also leads to the creation of new jobs. Take for example the businessman who would like to invest in a new garment factory. He needs planners, designers, engineers and construction workers to allow his project to get off the ground. On completion, the businessman will need to employ people to become machinists, cutters, packers and supervisors. As such, investment helps to increase employment in the economy.

A rise in employment potentially means an increase in the number of taxpayers in the country. This in turn should lead to higher revenue for the Government through increased tax collections. Increased tax revenues then allows the Government to provide a greater level of service to its citizens by expanding some the current programs or by undertaking new projects like investing in new roads, schools and hospitals. The government can also retire some of debts at a faster rate if its revenue base increases.

Additionally, as more people secure jobs, the number of people who are able to afford the basic necessities of life like food, clothing, medicine and children's education increases. Thus, sustained investment growth can have a direct positive impact on improving people's living standards and consequently in reducing poverty levels.

There are several important determinants of investment. One such determining factor is the level of demand in the economy. When demand for goods and services are low, firms will most likely postpone investment plans until the economy improves. But if demand for their goods and services is high, they would be inclined to invest more in plants and machinery in order to be able to supply more. In addition, if businesses are doing well and making good profits, this provides an incentive for them to expand their investment in the economy.

Lower borrowing costs i.e. lower interest rates or price of credit, also influence firms and households to increase their investment plans. Other considerations such as sound macroeconomic conditions, favourable investment policies of the government, good law and order are also important for investment activity to thrive.

Government is expected to provide and maintain most of the public goods such as provision of water, roads, schools, hospitals etc. Consequently, Government's direct some of its expenditure towards capital works.

In addition, statutory corporations as well as the private sector, have invested considerably in Fiji. According to the Reserve Bank of Fiji, investment as a percent of GDP was around 16 percent in 2003. The Government, however, hopes to reach a target of 25 percent in the near future.

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