

Money Matters but Expectations Do Too

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After the announcement of 2012 National budget many things happened. The lowering of the corporate and personal taxes was much appreciated by people at large. The benefits of this new measure was felt widely by all the sections of the population. In fact for most middle income families there were significant gains. Wage earnings increased by around 10 to 13% for those in the higher income brackets. However, the increases were much lower for the lower income brackets.

The tax reduction measure for the 2012 National Budget was an extremely bold step taken by the government to put more money in the pockets of the people. It was basically an expansionary approach, based on the assumption that increased consumption would lead to increased output and thus lead to other balances in the economy. Such measures are not new. However, in this case it was definitely an extraordinary one given the proportion of the tax cut. It was by any measure a huge tax cut never seen before in Fiji's history. If a simple proportions calculation is done, assuming all other things as given, the revenues would be expected to decline by about \$120 million which could push the actual deficit to around 3.5%, more than 1.5% points higher than projected. Were this so, it would be a seriously bad situation to be in for any government in Fiji's economic condition.

There are many lingering issues that need to be raised. Foremost, the question is whether the tax reduction is sustainable without raising other taxes. One would have expected the tax reduction to be much lower or more gradual over time during which period the government would have been able to better handle the downside risks. The sudden reduction would be far more difficult to adjust.

It is likely that the resulting increase in consumption may not be realised to spin any output growth in the economy. If this really is the case, then the economy may fall trapped in a vicious cycle of imbalances and give rise to greater macroeconomic risks. But despite all these downside possibilities, there is a sense of happiness among the people

about this tax reduction that increases their disposable income.

Under normal economic circumstances, it would be expected that the increase in income would match with a corresponding increase in productivity. The question is whether this matching productivity shift is possible. Past trends show that it may not be possible. Thus the national economic pie may not grow to match the proportion by which the consumption would increase in the economy. Further to this it is least likely that government expenditures (particularly wasteful ones) would be taken care of by some internal mechanisms.

Combined with the current global slump (2011) and weak economic recovery, domestic indicators are reasons for worry. The domestic economic situation looks even grimmer after the unfortunate event of the recent floods (March 2012), which has caused significant damage to the economy and dampened the confidence of huge proportion of stakeholders. The resulting economic shock could be as big as 3% if decline in crop, tourism and other businesses are factored in together with the costs of damages.

With this, the risk of rising government deficit increases significantly; the projected deficit indicated in the budget may worsen substantially if tax collection from other sources such as departure taxes, stamp duties, the new levies, and fees and fines do not produce results as expected. The government may then have to consider some other forms of taxes that could take away what has been given under the 2012 budget. More so the government would need to borrow more to finance its expenditures, or worse still stifle expenditure in some areas of activity.

Additionally, it is expected that the government policies would remain expansionary in 2013 as elections approach.

Recent sentiments from businesses also seem negative despite promises of tax relief for flood affected businesses and reduced corporate taxes. It could be arising from a number of apprehensions that businesses hold about the business environment in the country. It may be that businesses clearly know that even if incomes increases after the tax reduction, the actual net gains may not really be that great after all. It generally seems that the negatives override the small positives that seem to exist. The closure of around 50 businesses in Nadi may be a reflection of the lack of confidence in the economy, although this is not any deliberate making of the government.

Apart from the lower taxes, the government is expecting other gains, which are expected to have lasting effect. Sugar output if increased by about 16% as expected, may be a boon for farmers. It was also projected that tourist arrivals would increase by about 7%, mostly due to increased

marketing by Tourism Fiji. This would be a much welcomed and anticipated development. Those associated with these sectors would enjoy higher incomes from higher levels of activities which would create positive spin-offs on the overall economy. But the problem is whether all these remain achievable after the devastating floods and depressed investor and business confidence. People in the affected areas are still in serious difficulty and working hard to cope.

Most other productive sectors have remained stagnant or have declined in the last 12 months. The general lacklustre economy is a worrying sign. Without higher economic growth one cannot expect much to happen even if the government's budget looks as good as it does for 2012.

On the broader economic front, investments have remained low and skill-migration continues at a rapid pace. The lack of growth and continuing skill migration would continue to fuel the downward spin and further damage confidence in the economy. The confidence among businesses may nosedive rapidly unless the government comes up with some constructive policies to rejuvenate the economy, particularly in the sugar belt where flood is a major worry.

The world economy is expected to grow at a slower pace during 2012 than was predicted earlier. While the Asian economies may continue to grow at a reasonable rate of 7-8%, the developed economies - US, Euro-zone, Australia and New Zealand - are expected to remain subdued for the next twelve months. What are particularly worrying are that the Australian economy is forecasted to grow only at around 2% and the US economy at 1.7%. In the face of this reality the managers of the economy need to be more creative and innovative where new ideas are absolutely necessary.

The government's current investment on road infrastructure is a good approach towards building confidence. But the current rate of construction and repair is not keeping pace with the rate of deterioration. While the government's current approach can be lauded as good gesture, much more needs to happen in the economy for long run sustainability of higher consumption. Improving the business environment in the country is a sure way of achieving this, which is only possible if political stability is established in the long run. The government's efforts at the moment seem genuine and a positive one.

Up-keeping the morale of the workers is another important issue. The economy-wide wage increase is a good sign but it has to go with proportionate increases in productivities. This is where the civil service needs government attention where merit and good working culture needs

to prevail. Appropriate systems are needed in place to monitor and improve work culture in the civil service. Honesty and ethical practices are extremely important. But much more is needed if worker output is to be increased. Increases in productivity cannot happen without new technologies. Technologies need new investments, ideas, skills and above all, investor confidence. This is where the manufacturing sector in Fiji has fallen silent.

Government needs to do more on investments by supporting domestic businesses by improving the business environment and simplifying procedures. The environment should not only be attractive to big or foreign investors but also to small domestic investors including those engaged in the rural economy. Such efforts include establishing long term security of land tenure for leaseholders and supporting market mechanisms and logistics. Streamlining customs rules and facilitating international trade in niche areas such as agriculture exports and low end manufactured goods would be most attractive and viable steps the government can take to improve business environment.

However, consolidating property rights and curbing crime are going to be major challenges for any government, including the one after the 2014 elections. Rural helplessness and lack of opportunity continue to exist. This helplessness largely determines the attitude of the people, who increasingly begin to believe that only the government can help. The government can do more for the rural sector to change the attitudes of the people by empowering them to be productive. The small-holder farmers need new ideas and extension support for high value crops with market facilitation. It is particularly important that new markets are facilitated, where the government needs to provide support for new ventures both in primary agriculture production and processing where more extension resources and expertise are needed. Promoting high value crops is a viable option for rural development and growth.

Lastly, political reforms need a fresh look. A definite march towards a democratic government is needed. I would expect the government to take measured steps towards more open media and facilitation of sensible public debate. An open discussion on the Constitution is a must for long-term stability. The apprehension among those who hold power about dirty, nasty politics is understandable but despotic measures to control dissent or disagreement is not good for the country. In fact it is far worse than the dirty, nasty politics we hope to banish.

It is indeed true that Fiji cannot afford to get mired in racially, or religiously divisive politics, but it is also true that without free and open media, we cannot achieve a prosperous and democratic society.

Reasonable discussions and debate can only be established through free media and freedom of speech, including academic freedom.

The academic fraternities currently feel stifled, particularly on important constitutional matters and discourse on the economy. The current curb on speech and censorship of the media (including self-censorship) should diminish as elections come closer. Remaking a new and a better Constitution is a huge challenge for the government but it is doable if good faith prevails. At the moment (2012), it seems the government is scared of public scrutiny.

Constitution-making needs contribution from all stakeholders, otherwise it would be deemed incomplete. Then even the most basic essence of establishing a tolerant society would be defeated. I think the whole process of involving the people would be of great value to the new Constitution if it is to form the basis for freedom and peace for all.

Thus, one needs to go beyond the mechanical government revenue and expenditure arithmetic to figure out the outcomes. Even if the government puts more money into the pockets of the people in the current period, and that too at the expense of the future generations, no real progress can be made unless the people feel confident about the future and become more productive economically. This indeed goes beyond government's accounting and budgetary processes.

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