Public Expenditure Review

April 2023

Fiji

Towards Fiscal Sustainability & Improved Spending Quality

Copyright Statement:

Acknowledgment:

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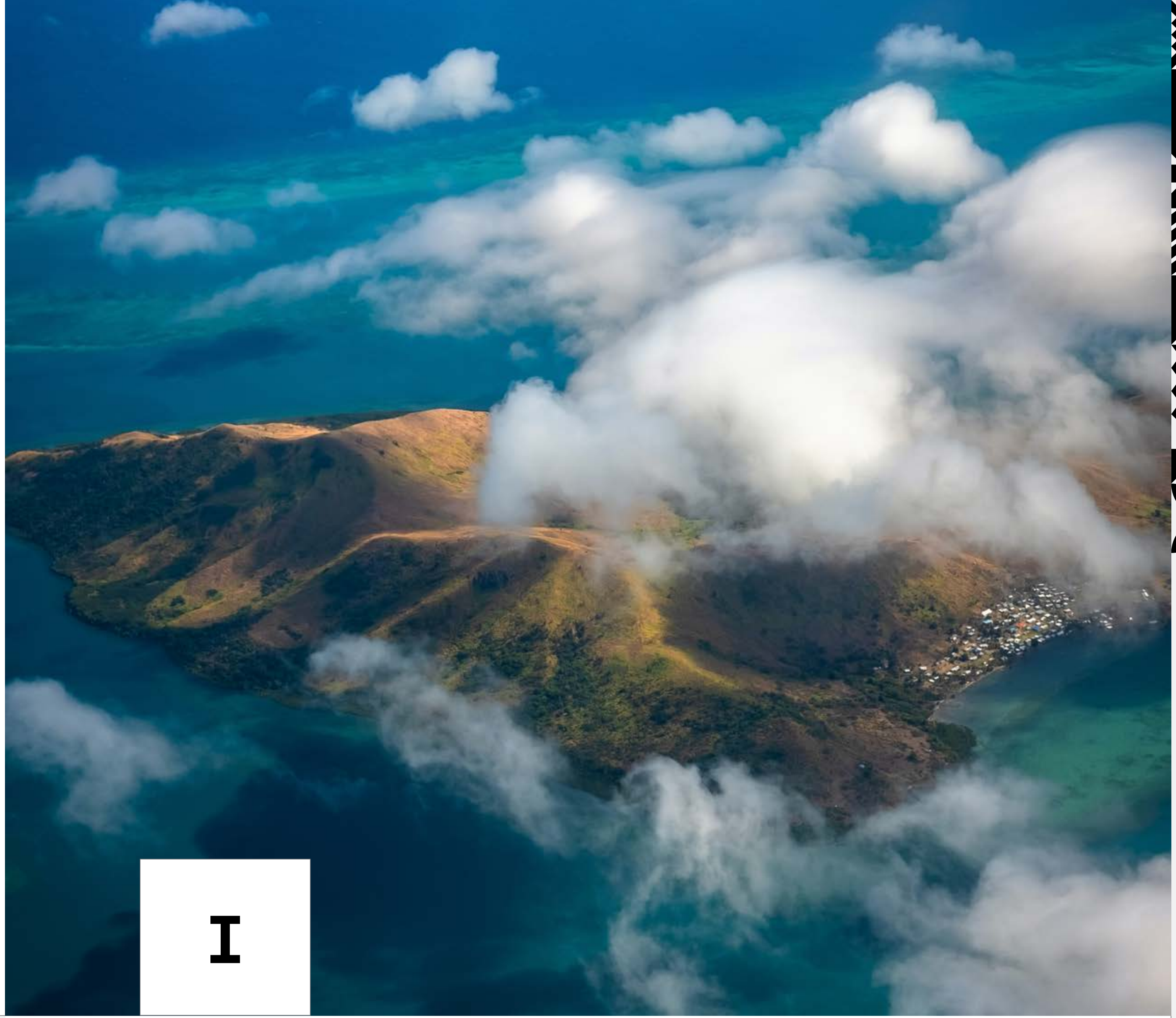
ABSTRACT

THE COVID-19 PANDEMIC, coinciding with multiple tropical cyclones, caused an economic crisis of unprecedented scale in Fiji. As a result of this and the Government of Fiji (GoF) response, the fiscal deficit and public debt skyrocketed, greatly exacerbating trends that had emerged before the onset of COVID-19. The rising debt sustainability risks significantly increase the urgency and scale of fiscal consolidation. In this context, this Public Expenditure Review (PER), requested by the GoF through its Ministry of Finance, Strategic Planning, National Development & Statistics, assesses the Government's consolidation plans and alternative fiscal consolidation pathways, their impact on debt sustainability, and required reforms to achieve them. Based on the GoF's priorities and their importance for consolidation, growth, and resilience in Fiji, the PER focuses on consolidation options and complementary public management reforms in the areas of domestic resource mobilization, the civil service, capital investment and sugar industry support. It further summarizes the key findings of detailed technical Background Chapters on these subjects, proposing a strategic fiscal consolidation program that rebalances the authorities' fiscal consolidation plans. Recommended substantial revenue reforms support domestic resource mobilization to finance well-targeted spending programs that support growth and investments in public service delivery and climate and disaster resilience.



I

In the years prior to the pandemic, an expansionary fiscal policy stance supported growth, but increasing public debt levels prompted the GoF to initiate a fiscal consolidation program in 2019. Following years of low fiscal deficits that contributed to falling debt levels, the GoF substantially increased spending in 2014, including for investment in infrastructure and human capital. While this supported higher growth, revenue collections lagged, leading to accumulated deficits and reversing previous achievements in lowering public debt levels. This prompted the authorities to announce tighter spending controls as part of a medium-term fiscal consolidation program starting in FY19, which was quickly derailed by the onset of the COVID-19 pandemic in FY20.

The COVID-19 pandemic—coinciding with multiple Tropical Cyclones—caused an economic crisis of unprecedented scale in Fiji. International border closures halted tourism, which had generated 40 percent of output and 30 percent of jobs, with ripple effects on all segments of the economy. Concurrently, Fiji was hit by multiple tropical cyclones, illustrating the country's high exposure to climate and disaster risks. The combined impact resulted in a 17.0 percent contraction in GDP in 2020 and a further 5.1 percent fall in 2021 – four times worse than the average for the Pacific Island Countries over the two years.

As a result of the economic crisis and the GoF response, the fiscal deficit and public

debt skyrocketed, exacerbating trends that had emerged before COVID-19. Extensive tax policy relief measures—in combination with the collapse in economic activity due to the shutdown of the tourism sector—undermined revenue collections, which could not offset nominal spending cuts. As a result, fiscal deficits increased substantially, driving up public debt from a pre-crisis level of below 50 percent of GDP to over 90 percent by the end of FY22 (July 2022).

This situation, combined with emerging global economic risks, threatens Fiji's macro-fiscal stability, an essential foundation for sustainable economic and social development. Recent global price shocks, monetary tightening in developed economies, and disaster and climate risks further threaten macro-fiscal stability in Fiji. Regarding the latter, Fiji's Climate Vulnerability Assessment (CVA)[1] concluded that climate change would amplify the current dangers to highly vulnerable sectors such as transport, water, fisheries, and the environment. It estimated that annual losses in these sectors could range from around 5 - 20 percent of GDP, requiring an investment of F$9.3 billion (close to 100 percent of GDP) over 10 years, plus additional maintenance and operation costs and social expenditures, to substantially reduce the country's vulnerability. Together, this calls for ambitious fiscal consolidation over the medium term to contain risks before they have the chance to materialize and free up fiscal space for critical investments to foster growth and resilience.

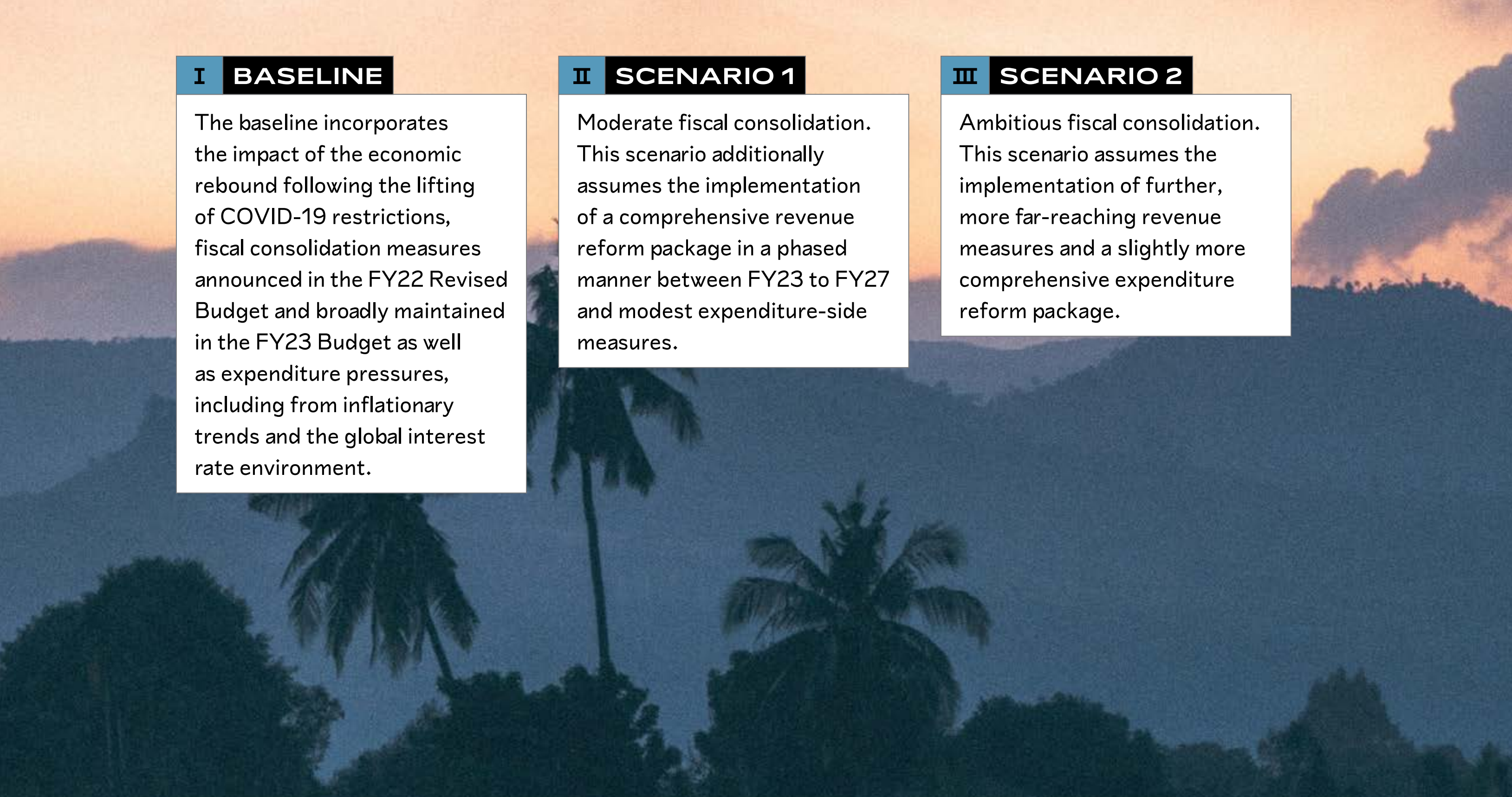
In response, the authorities have outlined fiscal consolidation plans to reduce public debt levels substantially. The FY22 Budget set out a fiscal consolidation path based on substantial, rapid revenue increases and further nominal expenditure cuts. These provided the foundation for a long-term consolidation trajectory to drive down debt levels to close to 70 percent by FY30 and around 60 percent by FY36. However, a significant downward correction in revenue collection estimates as part of the FY22 Revised Budget pushed consolidation efforts further onto the expenditure side, requiring corresponding highly ambitious cuts in expenditures. Together, this would result in an undesirable consolidation path, with growth projections highly likely undermined by significantly reduced spending, including lower capital investment, which would threaten targeted reductions in debt levels. The FY23 Budget reverts to a more balanced consolidation path; however, revenue increases appear optimistic without supporting reforms and a (near) spending freeze in nominal terms until FY30 would risk undermining growth, service delivery, and investments in climate and disaster resilience.

In this context, the PER assesses different consolidation pathways to inform a strategic reform program supporting the authorities' consolidation targets. Using a baseline and two reform scenarios varying in ambition, the PER illustrates consolidation pathways and their impact on debt sustainability, and assesses these against the Government's fiscal targets outlined in the FY22 Budget.

>90%

of GDP – Fiji's public debt by end of FY22

1 Government of Fiji, 2017. Fiji Climate Vulnerability Assessment. World Bank: Washington, DC.



I BASELINE

The baseline incorporates the impact of the economic rebound following the lifting of COVID-19 restrictions, fiscal consolidation measures announced in the FY22 Revised Budget and broadly maintained in the FY23 Budget as well as expenditure pressures, including from inflationary trends and the global interest rate environment.

II SCENARIO 1

Moderate fiscal consolidation. This scenario additionally assumes the implementation of a comprehensive revenue reform package in a phased manner between FY23 to FY27 and modest expenditure-side measures.

III SCENARIO 2

Ambitious fiscal consolidation. This scenario assumes the implementation of further, more far-reaching revenue measures and a slightly more comprehensive expenditure reform package.

The background chapter on revenue identifies the significant potential for increasing domestic resource mobilization in Fiji. To realize this, reforms must go far beyond the measures introduced in the FY22 Revised Budget and the FY23 Budget. The analysis identified six reform areas to help Fiji return to its long-term revenue collection average. The first priority is to reform the value-added tax (VAT) regime by expanding the VAT rate introduced in the FY22 Revised Budget to other goods and services and reversing the zero-rating of VAT on essential items. The latter should be combined with increased social assistance transfers to compensate low-income households. Secondly, the personal and corporate income tax (PIT and CIT) regimes should be strengthened. This should comprise simplifying PIT ratesand broadening the base, updating the CIT regime, and reducing tax incentives. Thirdly, expanding the excise tax regime—particularly by introducing or increasing excises on alcoholic beverages, fuel, and sugar products—would have positive revenue and social and environmental impact. Reversing departure tax reductions introduced as part of the pandemic relief package should be implemented as tourism rebounds. Lastly, a renewed focus on improving revenue administration performance should supplement tax policy reforms.

In light of spending restraint implemented since 2019 and commitments in the FY22 Revised Budget and FY23 Budget, additional expenditure side measures must be well-targeted. In addition to recent nominal expenditure cuts, the planned phasing out of pandemic support and restraint in public spending are immediate priorities. These are committed in the FY22 Revised Budget, and its forward estimates up to FY24 were maintained in the FY23 Budget. The public wage bill is manageable in Fiji, but moderating its growth amid reinstating full pension contributions and inflationary pressures remains important for fiscal consolidation. The nominal cuts of capital spending during COVID-19 should be partially reversed to enable investments to support growth and resilience. This should be executed with precision to realise increases in value for money. An in-depth analysis of the sugar industry found substantial consolidation potential from the phasing out of subsidies and an excise tax on sugary products. Complementary Commitment to Equity (CEQ) analysis and an education sector PER (both forthcoming) highlight substantial scope to improve the targeting of social assistance and tertiary education support. This could generate moderate fiscal savings without undermining access and quality of public social spending. The background chapters on fiscal consolidation, the wage bill, infrastructure spending, and sugar sector subsidies provide detailed analysis of these and complementary reforms.

As a result of the analysis, the PER proposes a strategic fiscal consolidation program, substantiating and rebalancing the authorities' plans. Identified revenue reforms aim to support the authorities' targeted domestic resource mobilization increases. While revenue increases are projected to be more gradual in the short-term than projected by the authorities, continued revenue reforms over the medium term would enable somewhat higher, well-targeted spending in the long-run that would support higher growth and investments in service delivery and resilience improvements. Table 1 below provides an overview of the recommended reform measures under each of the three scenarios, which are discussed in this report and more extensively in the accompanying background papers of the PER.

TABLE 1 Five-Year Plan: Reform Measures by Scenario

	Baseline	Scenario 1: Moderate consolidation	Scenario 2: Ambitious consolidation
REVENUE		ADDITIONAL COMPARED TO BASELINE	ADDITIONAL COMPARED TO SCENARIO 1
Tax	1 Recovery effects from the COVID-19 pandemic 2 Tax reforms introduced in the FY22 Revised Budget • Value-added tax (VAT) increase on selected goods and services, partially offset by the zero-rating of essential items and elimination of the Environment & Climate Adaptation Levy (net positive impact on collections) • Cuts in the film tax rebate scheme • Reversal of recent fuel duty increase (negative impact on collections)	1 Simplification of personal income tax rate structure and lowering of threshold 2 Tax fringe benefits the same as ordinary income Introduction of dividend withholding tax 3 Elimination of reduced corporate income tax rates and export incentive 4 Removal of zero-rating of VAT on essential items, partially offset by an increase of Poverty Benefit Scheme 5 Extension of increased VAT rate to other goods and services 6 Increase in excise tax on alcohol 7 Increase in departure tax from F$100 to F$125	1 Reversal of the fuel duty reduction 2 Introduction of an excise on sugar(y) products 3 Further increase of departure tax to pre-crisis levels of F$200 4 Implementation of a revenue administration improvement program, partially offset by program costs
		EXPENDITURE	
Personnel	Nominal wage bill growth below GDP growth in FY23 and FY24 to reduce spending relative to GDP to 8.9 percent	Nominal wage bill growth measurably below GDP growth in FY24 to reduce spending relative to GDP to 8.5 percent	Extension of slower nominal wage bill growth until FY25 to reduce spending relative to GDP to 8.1 percent
Transfers & subsidies	Phasing out of pandemic support measures	1 Reduction in sugar sector subsidies, partially offset by redirected agriculture support spending 2 Reduction in generous Tertiary Education Loans Scheme (TELS) allocations, combined with better targeting 3 Increase in Poverty Benefit Scheme spending 4 Improved targeting of public social spending	1 Full phasing out of sugar sector subsidies, partially offset by agriculture support spending 2 Further reduction in TELS allocations, combined with better targeting 3 Improved targeting of public social spending
Other recurrent spending	Restraining supplies, consumables and other recurrent spending	Further modest cut to other recurrent spending	1 Further modest cut to other recurrent spending 2 Costs of the revenue administration improvement program
Capital	Gradual increase to 9 percent of GDP	1 No change in spending 2 Strengthening of public investment management	1 No change in spending 2 Strengthening of public investment management

Sources: Fiji FY22 Revised Budget and FY23 Budget; World Bank staff assumptions.

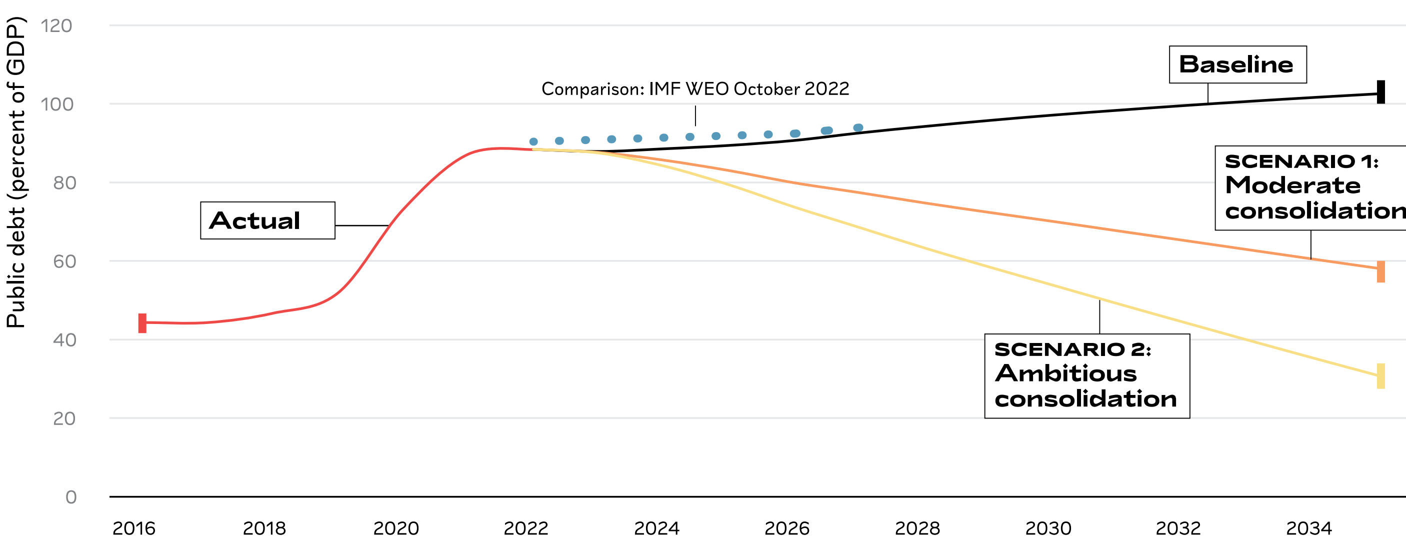
Based on the analysis, the PER recommends that, at a minimum, the Government pursues a moderate fiscal consolidation scenario, which entails significantly bolder reforms than those presented in the FY22 Revised Budget and FY23 Budget. All indications are that measures considered under the baseline will not be sufficient to put Fiji on a sustainable debt trajectory and would leave the country without any buffer for a future shock. This conclusion is in line with the IMF's macro-fiscal projections as per the October 2022 World Economic Outlook, which also foresees a gradual upward trend in public debt levels absent further reform. At a minimum, the GoF needs to implement additional reform measures in the extent of those presented under Scenario 1 to achieve a moderate level of fiscal consolidation that puts debt on a downward trajectory. With an estimated debt ratio of 65 percent of GDP by FY36, this would almost allow the authorities to meet their long-term debt target of 60 percent of GDP.

More extensive consolidation measures and complementary reforms will be required to bring debt to its pre-pandemic debt levels within a decade. An ambitious fiscal consolidation, as presented under Scenario 2, would also help to achieve the GoF's broader fiscal targets for revenue, expenditure and fiscal balances. While individual reform measures are estimated to have a negative impact on growth, concurrent reforms to improve public investment management and target poverty spending can help offset a significant share of negative growth impacts that result from fiscal consolidation.

"The COVID-19 pandemic, coinciding with multiple Tropical Cyclones, caused an economic crisis of unprecedented scale in Fiji"

The GoF should complement fiscal consolidation with public financial management and private sector development reforms. Priority should be given to (i) improving data collection and information systems; (ii) strengthening strategic fiscal planning and budgeting; (iii) continuing prudent borrowing and sound debt management practices; and (iv) closely monitoring and reducing fiscal risks from contingent liabilities. Lastly, while not assessed as part of this 'public sector lens' PER—except for references to infrastructure financing in the capital investment chapter and land reform in the sugar industry review—continuing reforms to address cross-cutting private sector development constraints in the areas of skills, finance, infrastructure, and the business environment is fundamental to build a sustainable basis for domestic resource mobilization and livelihoods for the citizens of Fiji. The recently released in-depth Country Private Sector Diagnostic (CPSD) titled Creating Markets in Fiji by the International Finance Corporation provides a comprehensive list of reform recommendations in this regard. The CPSD further identifies outsourcing services, health care, and agri-logistics as strategic sectors to drive growth and contribute to economic diversification, resilience, and inclusive job creation while strengthening Fiji's position as a sector hub/market leader in the Pacific region.

FIGURE 1 Fiscal Consolidation Pathways and Their Impact On Public Debt



Source: Fiji MoF, IMF WEO, World Bank staff estimates.

TABLE 2 Contributions to Fiscal Consolidation

Scenario			Baseline	Scenario 1	Scenario 2
Fiscal deficit in FY22 (percent of GDP)			-12.0	-12.0	-12.0
Cumulative reform impact by FY27 (percent of GDP)		Tax revenue	0.5	4.2	6.1
		Primary expenditure	-3.6	-4.4	-5.3
		Total consolidation	**4.1**	**8.6**	**11.4**
Recovery and other changes (net consolidation, percent of GDP)			0.6	0.5	0.6
Fiscal deficit in FY27 (percent of GDP)			-7.3	-2.9	-0.1
Public debt	Percent of GDP	2023	87.9	87.6	87.5
		2032	99.6	65.2	44.3
	Change 2023-2032	Total	11.7	-22.5	-43.2
		p.a.	1.3	-2.5	-4.8
Growth	Average annual real growth rate 2023-2027		5.3	5.1	5.0

Sources: Fiji MoF Fiscal Outturn Report FY22, World Bank staff estimates.

Introduction

1

The Fiji Public Expenditure Review 2022 is motivated by the need to **ensure debt sustainability and rebuild fiscal buffers in the wake of COVID-19 and emerging global economic risks.** This report presents the findings of the PER undertaken by the World Bank at the request of the GoF and its Ministry of Finance, Strategic Planning, National Development & Statistics (MoF).[2] Based on the priorities identified by the MoF and their importance for fiscal consolidation, growth and resilience in Fiji, the team commissioned five background papers that were produced for this PER.[3] These technical papers comprise: (i) debt sustainability and fiscal consolidation pathways; (ii) domestic resource mobilization; (iii) the cost of the civil service; (iv) capital investment; and (v) sugar industry support, with sugar having historically been an essential commodity in Fiji and government subsidies continuing to be considerable.

The PER aims to support the GoF in identifying reforms that help achieve the required fiscal consolidation while supporting growth and fiscal space for investments in service delivery and resilience. Following an assessment of the Government's consolidation plans, it outlines a baseline and two reform scenarios, varying in ambition, to illustrate alternative consolidation pathways and their impact on debt sustainability. It further identifies reforms with significant potential for increasing domestic resource mobilization, achieving expenditure savings, and improving the allocation of public resources. In addition, the PER looks at reforms that could improve public spending quality and help offset the negative impacts of fiscal consolidation measures. The PER provides policymakers and other interested stakeholders with findings and recommendations that are further detailed in the accompanying background papers.

The PER is organized as follows:

SECTION

2

provides the context for the evolution of public finances over the past years.

SECTION

3

makes a call to action linking the growing risks to macro-fiscal stability in Fiji with illustrative fiscal consolidation pathways. The section further presents outcomes from the modeling of reform effects and their impact on debt sustainability and growth.

SECTION

4

presents reform options available to achieve fiscal consolidation targets and improve the quality of spending. It includes a snapshot of each recommended reform (or package of related reforms) and underlying analysis, which are elaborated in more detail in the background papers.

2 The ministry responsible for finance was renamed from Ministry of Economy (MoE) to Ministry of Finance, Strategic Planning, National Development & Statistics (MoF) in December 2022. References in this report and the background papers to publications issued prior to December 2022 use MoE.

3 The background papers were completed in June 2022. Background chapter A was subsequently updated to incorporate data from the preliminary fiscal outturn for FY22 and the FY23 Budget. The updates are reflected in this PER report.

Context & Recent Developments

P.9–15

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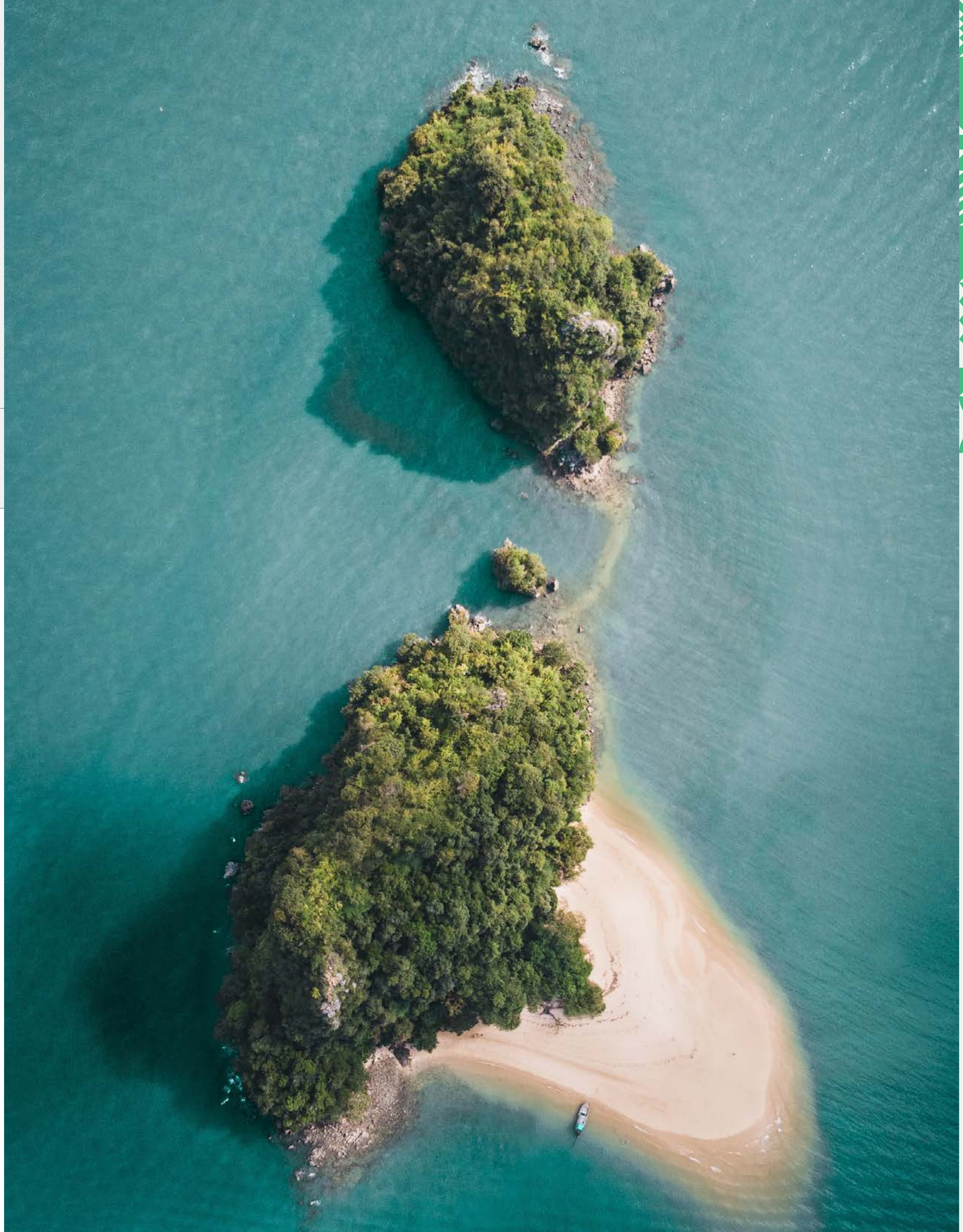


Fiji is a small island nation with a high level of human development and upper-middle-income status.** The country is in the South Pacific Ocean with a population of about 900,000 and an area of 18,000 square kilometers spread over 330 islands, of which about 110 are inhabited. Remoteness, natural hazards and climate change represent major obstacles to economic and social development. Fiji has achieved high human capital development and upper-middle-income status, with a GDP per capita of $6,143 in 2019, equivalent to 14,186 international dollars at purchasing power parity. Prior to COVID-19, tourism was the main driver of the economy and a major source of foreign exchange, contributing nearly 40 percent of GDP.

Fiji is highly vulnerable to extreme weather events, which are increasing in frequency and intensity due to climate change. Fiji's geographical location and large coastal area —where the population and major assets are located—make it vulnerable to climate change and disasters caused by natural hazards. Estimated damages and losses of recent cyclones and floods ranged from 20 percent (TC Winston in 2016) to 3.3 percent (TC Harold in 2020) of annual GDP. Due to climate change, extreme weather events, including tropical cyclones (TCs), floods and heavy rainfall, are likely to become more intense and frequent.[4] Sea level rise and storm surges will further affect many sectors, people's livelihoods, and the food and water supply, among others. Fiji's CVA (2017) found that by 2050, an additional 3.8 percent of the population is likely to fall into poverty due to implications of climate change, and investments in these vulnerable sectors and social protection programs would help reduce these impacts.

In the years prior to the pandemic, an expansionary fiscal policy stance supported growth but increasing public debt levels prompted the GoF to initiate a fiscal consolidation program in 2019. During FY08–FY13, prudent fiscal management resulted in average annual fiscal deficits of 0.7 percent of gross domestic product (GDP). This caused public debt levels to gradually decline from a peak of 53.4 percent of GDP in FY10 to 47.4 percent in FY13. Subsequently, the GoF substantially increased spending, averaging 30.6 percent of GDP over FY14–FY19 – five percentage points of GDP higher than the average in the previous period. The higher spending, including the substantial investment in infrastructure and human capital, supported an almost doubling of the average annual real growth rate from 1.6 percent to 3.5 percent (3.1 percent in per capita terms). However, revenue collections did not keep up with higher spending, driving up deficits to 3.4 percent of GDP over FY14–FY19. Initially, public debt levels continued to decline on the back of higher real growth, bottoming out at 43.5 percent of GDP in FY17, before going back up to 48.9 percent of GDP by FY19. With it, interest payments were projected to increase to over 3 percent of GDP over the medium-term, prompting authorities to announce tighter control of spending as part of a medium-term fiscal consolidation program, quickly derailed by the onset of the COVID-19 pandemic in FY20.

Coinciding with multiple Tropical Cyclones, the COVID-19 pandemic caused an economic crisis of unprecedented scale in Fiji, one of the worst economic contractions in the world. COVID-19 had limited direct health impacts on Fiji in the first year of the pandemic, but the country was severely affected by a second wave in April to September 2021. A rapid vaccine roll-out, combined with natural immunity, stabilized new infections and hospitalizations. The economic impact throughout the pandemic devastated Fiji's economy, as international travel restrictions halted tourism, which had generated 40 percent of output and 30 percent of jobs. This tourism downturn had a ripple effect on all segments of the economy, with a negative impact on related industries, such as retail trade and transport, and spillover effects on consumption, finance and investment. Furthermore, Fiji was hit by successive tropical cyclones Category 3 (January 2021), Category 4 (April 2020) and Category 5 (December 2020) during the pandemic. The combined impact of COVID-19 and the natural disasters resulted in a 17.0 percent GDP contraction in 2020 and a further 5.1 percent fall in 2021– four times worse than the average for the Pacific Island Countries and the fourth-worst in the world (after Lebanon, Afghanistan, and Palau), over the two years.

The economic downturn, combined with extensive tax policy relief measures, undermined Fiji's historically strong revenue performance. Fiji has a relatively diversified revenue base and had an impressive average tax-to-GDP ratio of 24 percent between FY15-FY19, which is high compared to many

40%

of GDP pre-COVID-19 comes from the tourism in Fiji

Facts about Fiji

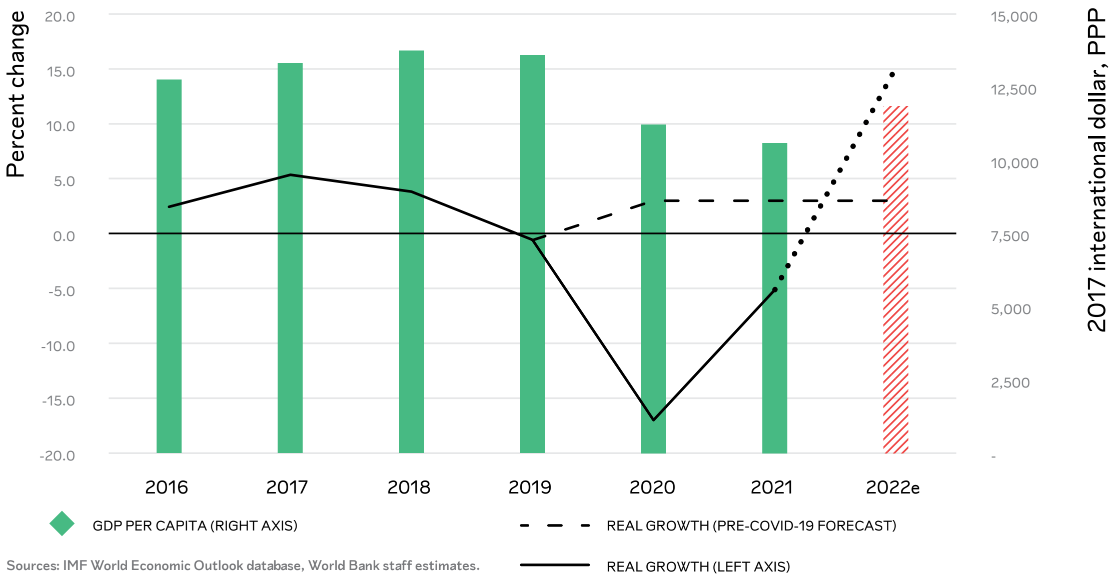
POPULATION
900,000

SQUARE KM
18,000

ISLANDS
330

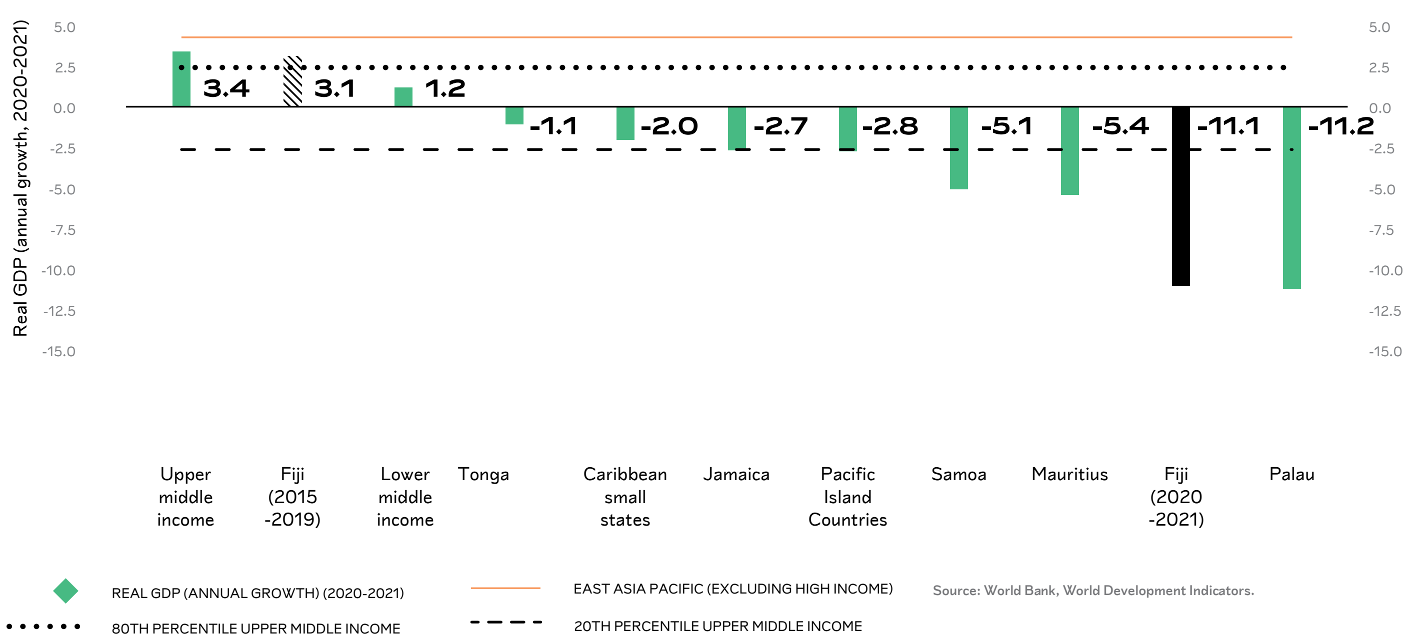
4 IPCC 2021. Sixth Assessment Report of the Working Group 1, Summary for Policy Makers; The World Bank Group and Asian Development Bank 2020 - Climate Risk Profile: The Pacific Region; World Bank. 2017. Climate change and disaster management. Pacific Possible: Background Paper 6.

FIGURE 2 Combined COVID-19 and Disaster Shocks Led to a Sharp Output Contraction In Fiji...



Sources: IMF World Economic Outlook database, World Bank staff estimates.

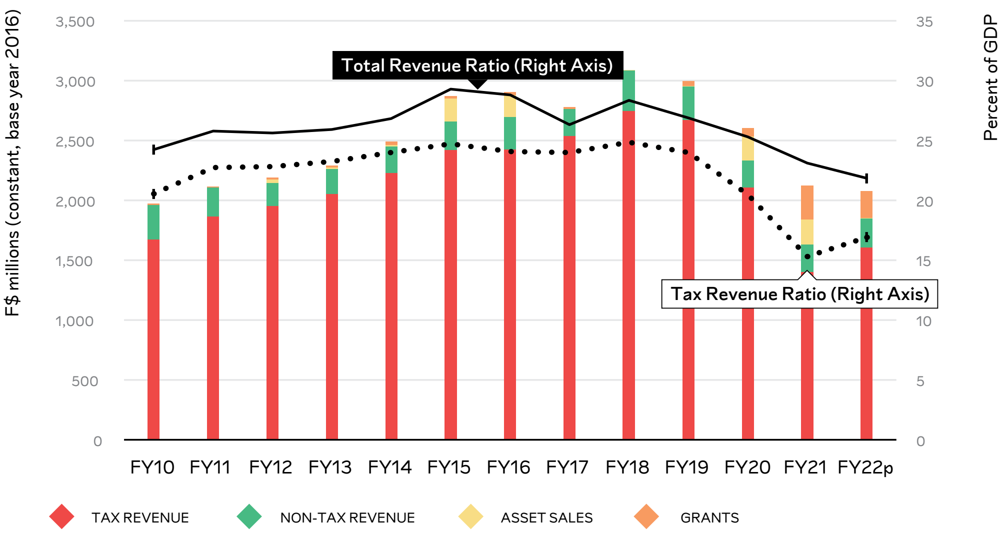
FIGURE 3 ...Which Was Four Times Worse than the Average for the Pacific Island Countries over 2020-2021



Source: World Bank, World Development Indicators.

of its peers and within the top quintile of upper-middle-income countries. A number of policy changes weakened revenue performance in the years prior to COVID-19, including a cut in the VAT rate from 15 to 9 percent in 2016, a doubling of the personal income tax-free threshold in 2017, and increasing the use of generous tax incentive schemes to promote development. The subsequent economic crisis sharply accelerated the decline in revenue performance, causing a one-third drop in tax collections to 15.3 percent of GDP in FY21. This was driven by the downturn triggered by international border closures and domestic lockdowns, as well as extensive tax relief measures introduced in the FY20 COVID-19 Response Budget and FY21 Budget. The tax relief measures were extensive and included a widening of VAT exemptions (especially on medical supplies), an increase in the export income deduction, accelerated depreciation on construction investment, and a wide range of cuts to minor taxes that cumulatively added up. While tax collections partially recovered in FY22, their share in total revenue remained relatively weaker compared to pre-COVID-19 times due to the relief measures.

FIGURE 4 Fiji's Strong Revenue Performance Has Been Undermined by COVID-19 Impacts…



Sources: Fiji MoF, IMF, World Bank staff estimates.

FIGURE 5 …Including From Tax Policy Relief Measures Introduced in FY20 and FY21

1

Reduction in **import duty** and **import excise duty** on selected goods

2

Local excise duty on **alcohol** reduced by **50%**

2

Capital gains tax exemption increased from F$16,000 to **F$30,000** and various other income tax relief measures

4

Elimination of stamp duties

5

Reduction of airport departure tax from F$200 to **F$100**

6

Removal of **service turnover tax** on prescribed services

7

Environment and Climate Adaptation Levy rate reduced from 10% to **5%**, and threshold increased (subsequently eliminated)

8

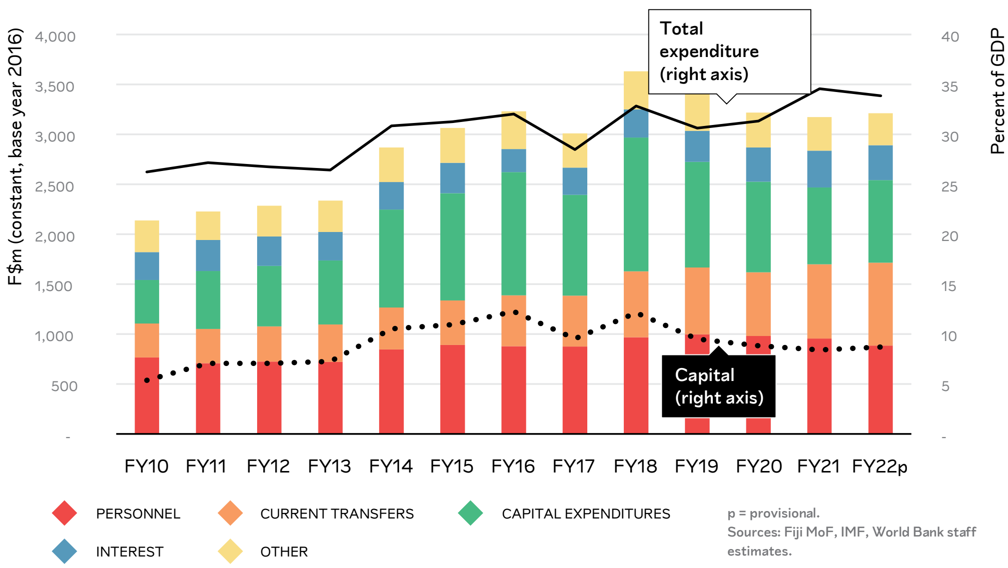
Other minor tax policy measures

Source: Fiji MoF, Revised-MoE Budget FY20 & Budget FY21.

The authorities showed spending restraint during the pandemic, but the sharp output contraction drove up public spending relative to GDP. In response to the expansionary fiscal policy stance since 2014 that led to increasing public debt levels, the Government had begun to implement an expenditure-based fiscal consolidation just prior to the economic crisis, reducing spending in real terms in FY19 following a peak in FY18. This continued with further spending cuts in FY20 and FY21, but the steep fall in output drove up public spending relative to GDP. Capital spending was particularly affected by cuts, falling from an annual average of 11.1 percent of GDP over FY14-FY18 to an average of 8.8 percent of GDP since fiscal consolidation started in FY19, bottoming out at 8.4 percent of GDP in FY21 before slightly increasing to 8.7 percent of GDP on the back of a real increase in total spending in FY22 (provisional).[5] Spending on capital outlays is considered on the low side in view of public investment needs to improve public social and economic services and strengthen resilience to climate and disaster risks, greater scrutiny is required of other large spending areas, such as social assistance schemes, tertiary education support and sugar industry subsidies, to enable a slight rebalancing (without undermining access and quality of desirable programs). While the phasing out of pandemic support measures reduces public expenditures in FY23, spending pressures are mounting as government activity reverts to pre-pandemic levels and inflationary pressures grow.

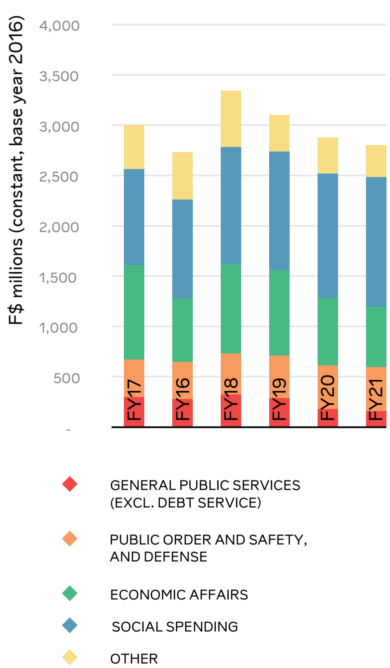
5 The Government's budget and accounting classifies substantial spending as capital that would generally be considered recurrent. This includes COVID-19 related social assistance schemes and subsidies, tertiary education scholarships and loans, and sugar industry support schemes, among others. To aid comparisons with the government budget and financial reports, only spending on social assistance schemes has been reclassified under current transfers while investments in human capital and agricultural production have been retained under capital spending. This overstates spending on physical capital outlays and should be addressed as part of reform of the budget classification, Chart of Accounts, and a related upgrade or replacement of the FMIS (see reform measure D.1 below and Background Chapter A for a more detailed discussion of the issue).

FIGURE 6 Following a Period of Gradually Increasing Spending, Consolidation Started in FY19...



p = provisional.
Sources: Fiji MoF, IMF, World Bank staff estimates.

FIGURE 7 ...and Needs to Continue Through Savings and Quality Improvements Across Large Spending Programs



Note: Detailed data for FY22 is not yet available.
Sources: Fiji MoF, IMF, World Bank staff estimates.

"The authorities showed spending restraint during the pandemic, but the sharp output contraction drove up public spending relative to GDP"

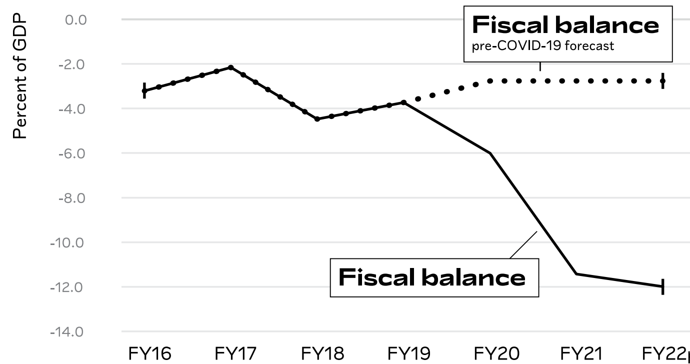
As a result of the economic crisis and GoF response, the fiscal deficit and public debt skyrocketed, sharply exacerbating the trends that had emerged before COVID-19. The fiscal deficit widened from 3.7 percent of GDP in FY19 to 11.4 percent in FY21. The deficit is estimated to have further increased to 12.0 percent of GDP in FY22, as lagging revenue impacts coincided with continued expenditure pressures to support economic recovery. The effect on public debt has been severe, with debt ratios almost doubling from a pre-crisis level of below 50 percent of GDP to over 90 percent by the end of FY22. Cumulative debt-creating flows in 2020 and 2021 have mainly been the primary deficit, negative real GDP growth, and, to a lesser extent, real interest rate effects. For a country as exposed to external shocks as Fiji, the pre-COVID-19 debt level was already considered on the high side. Levels of around 90 percent leave the country with limited buffers to address future shocks and highlight the scale and urgency of the fiscal consolidation required.

While Fiji substantially strengthened its public financial management system and practices in the past years, weaknesses remain that pose risks to implementing fiscal consolidation. A Public Expenditure and Financial Accountability (PEFA) assessment in 2019 found that Fiji's public financial management system is on track to be strong in terms of budget execution control. Performance in debt management and monitoring contingent liabilities and other fiscal risks was also considered robust, and the authorities have since addressed most remaining weaknesses in these areas. However, overly optimistic revenue forecasts, even in years not affected by shocks, have been an overriding issue in Fiji that undermines budget implementation. Weaknesses in strategic fiscal planning and budgeting and underlying data availability and quality gaps are contributing factors. The latter is caused in parts by outdated information systems and the absence of a functional/program classification system and key performance indicators, which impede evidence-based policy-making more broadly. Together, these issues risk undermining the design and implementation of a medium- to long-term fiscal consolidation program.•

Estimated fiscal deficit in FY22

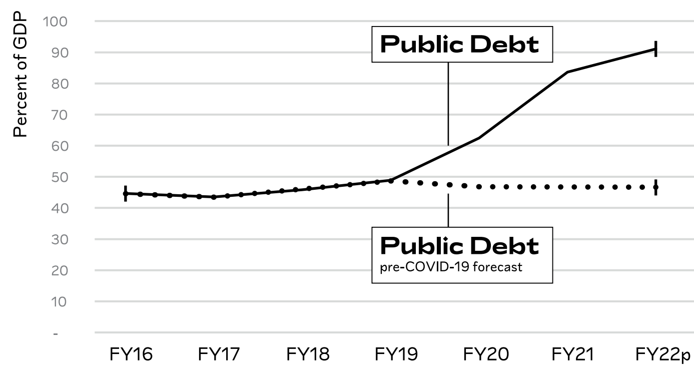
12%

FIGURE 8 Revenue Shortfalls and Limited Room to Cut Spending Amid Pandemic Needs Drove Down the Fiscal Balance...



Sources: Fiji MoF, IMF, World Bank staff estimates.

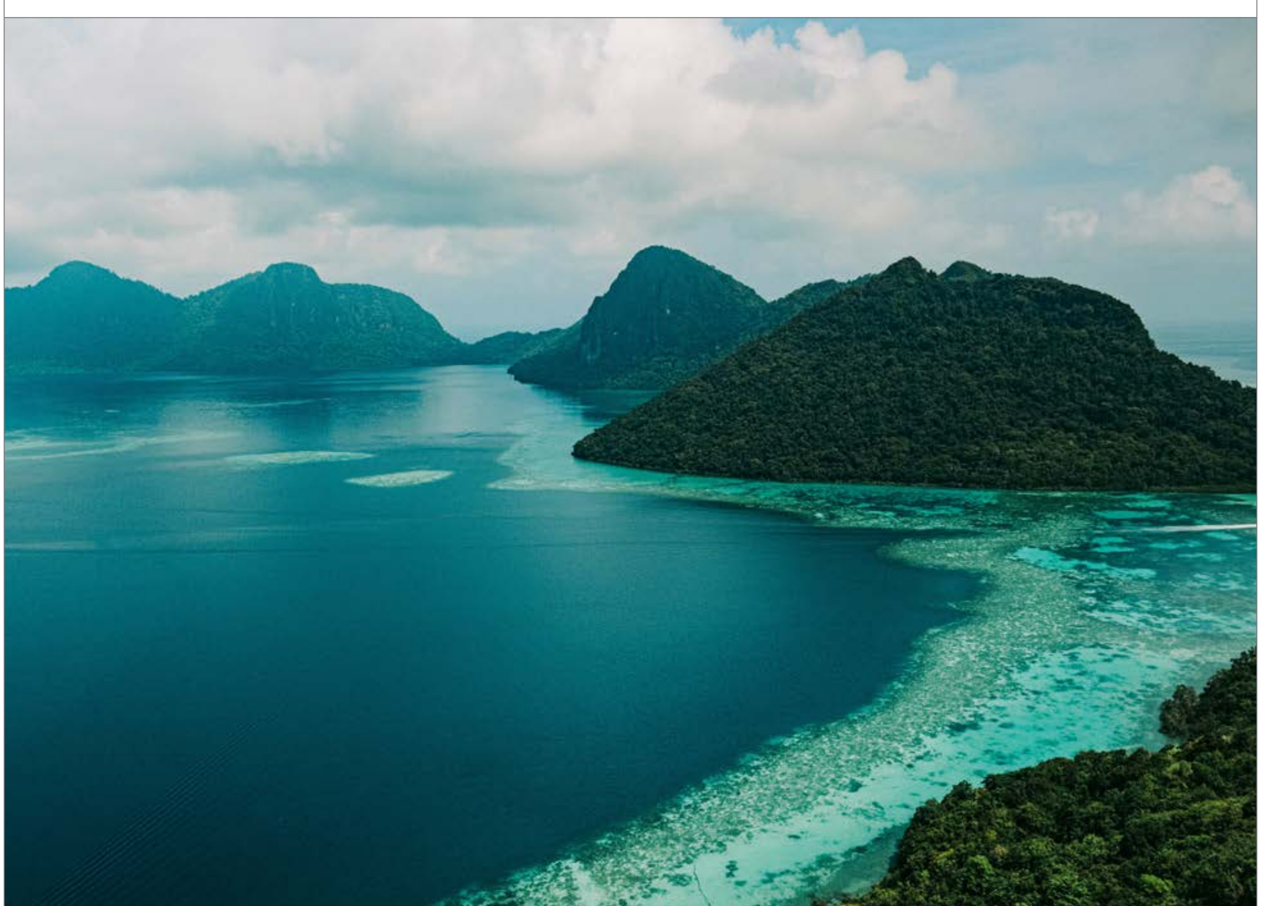
FIGURE 9 ...and Public Debt, Which Almost Doubled Relative to GDP by the End of FY22 to over 90 Percent



Sources: Fiji MoF, IMF, World Bank staff estimates.

Key Challenges & Fiscal Consolidation Pathways

Ch.3



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Risks to Macro-fiscal Stability

Government Building Suva

Investment needs for climate and disaster resilience over 10 years are estimated at

F$9.3 bn

The spike in debt and deficit levels that are the legacy of the economic crisis amplifies the risks to Fiji's macro-fiscal stability. The combined effects of the economic crisis triggered by COVID-19 and natural disasters in 2020 and 2021 have left Fiji with historically high fiscal deficit and debt levels, estimated at 12.0 percent and 91.1 percent respectively at the end of FY22. Left unchecked, these trends could eventually spark a macro-fiscal crisis.

Moreover, these risks are exacerbated by continued volatility in the global economy, the chronic risk of natural disasters, and the growing impacts of climate change.

Global price shocks: A combination of factors including the war in Ukraine and disrupted global supply chains (including from China's extended zero-COVID-19 strategy, with further risks emanating from the subsequent rapid removal of restrictions) have substantially driven up prices for energy and food, with follow-on effects on other consumer goods and input factors. This has increased the risk to the global economic outlook and Fiji is not immune. As a net importer of goods (including substantial quantities of fuel, machinery and food), a small domestic market and its tourism service export dependence, Fiji is particularly exposed to these external factors.

Global monetary tightening: Central banks in developed countries initiated significant and rapid monetary tightening in the first half of 2022 in response to a surge in inflation. Central banks in the United States, Australia, New Zealand, the United Kingdom and the Euro zone, among others, have all raised interest rates earlier and more aggressive than previously expected, with further (large) hikes implemented in the second half of 2022 and (smaller ones) expected in 2023. This has resulted in capital outflows from developing countries like Fiji and some increases in debt servicing costs. Higher debt servicing costs from the global interest rate hikes are a particular risk in light of the steep upward shift in debt levels due to the pandemic.

Natural disaster and climate risks: Fiji is highly prone to disasters caused by natural hazards, particularly cyclones and floods. These risks are expected to intensify as climate change impacts increase. Absent significant improvements in resilience, damages and losses could range from around 5 to 20 percent of annual GDP in the future (GoF, 2017). The CVA estimates that interventions in five main areas, namely housing and land use, infrastructure services (flood and coastal protection, transport, energy, water, health and education), agriculture and fisheries, ecosystem and environmental protection, and preparedness, social protection and health care can reduce the country's vulnerability, but they have significant financial implications. Investment needs are estimated at F$9.3 billion (close to 100 percent of GDP) over 10 years, plus additional maintenance and operation costs and social expenditures, highlighting the need to create fiscal space to finance higher public investment levels (in addition to mobilizing private sector finance).

The increased risks to macro-fiscal stability call for urgent short- and medium-term fiscal consolidation. While fiscal consolidation is always challenging and, if poorly implemented, can negatively affect economic and social development goals, the potential impacts of a loss of macro-fiscal stability would be far worse. The risk of such an outcome should not be taken lightly and prudence calls for robust preemptive measures to contain such risks long before they have any chance of materializing.

Fiscal Consolidation Pathways 3.2

In response to the increased macro-fiscal risks, the GoF has outlined fiscal consolidation plans in the FY22 Budget. The GoF published a medium-term fiscal framework (MTFF) for the first time in its FY22 Budget (July 2021). The framework sets out high-level fiscal targets for the next 15 years (2022–2036), aiming to increase revenue to 26 percent of GDP by FY23, reduce expenditure to 30 percent of GDP by FY24, achieve a primary balance surplus from FY24, and a corresponding fiscal deficit of below 5 percent of GDP from FY23 and 2 percent from FY26. Absent any external shocks, this targets a reduction in public debt to 81 percent of GDP by FY26 and about 61 percent by FY36, equivalent to an average annual decrease of roughly two percentage points of GDP. Overall, the medium- and long-term fiscal targets established in the MTFF provide a sound basis for fiscal planning and budgeting; however, the targeted rapid increase in revenue in FY23 appears highly optimistic without additional, far-reaching revenue reforms. Further, in light of Fiji's exposure to shocks discussed above, the targeted debt reduction constitutes only a 'minimum' required to provide some fiscal buffers against future shocks.

A supplementary budget passed in March 2022 adjusted the short-term outlook downwards by a measurable degree, with negative implications for the long-term fiscal targets. The FY22 Revised Budget substantially revised downwards revises revenue collection estimates compared to the FY22 Budget, requiring corresponding, highly ambitious cuts in expenditures. Despite these, the outcome would be a higher long-term deficit, with reductions in the debt-to-GDP ratio largely dependent on growth. Moreover, growth would highly likely be lower than the government estimates because of significantly reduced spending, including for capital. This trajectory does not appear to be fiscally sustainable nor desirable.

The FY23 Budget reverts to a more balanced consolidation path, but questions remain as to whether the targeted path is optimal as well as achievable absent more ambitious reform. While the updated MTFF targets (once again) revenue increases relative to GDP and in a slightly more gradual way than under the original MTFF, these still appear overly optimistic without supporting reforms. Further, following the initial substantial increases in FY23-FY24, the updated MTFF foresees a step-wise decrease in the revenue-to-GDP ratio back down to 23.1 percent of GDP by FY30, which is substantially below the targeted 26 percent under the original FY22 MTFF. On the expenditure side, cuts relative to GDP are more gradual in the short-term, while a targeted (almost) spending freeze in nominal terms until FY30 drives down expenditure relative to GDP to 23.6 percent by FY30. While MoF projects that this would bring down public debt to 67.8 percent of GDP by FY30, the significantly lower public spending—7 percentage points of GDP below the FY14-19 average and still 2 percentage points below the FY08-FY13 average—would risk undermining growth and leave minimal room for investments in service delivery and climate and disaster resilience, further reducing long-term growth prospects.[6]

In this context, the PER assesses a baseline and two reform pathways, with the aim of proposing a strategic fiscal consolidation program that substantiates and rebalances the authorities' plans. The baseline and two reform scenarios of the PER aim to give a sense of the consolidation required for different debt sustainability outcomes and reforms that could help achieve a sustainable debt path. The different consolidation pathways are summarized below and further detailed in Section 3.3. Section 4 summarizes the reforms required for each consolidation path.

6 Given the extent of targeted spending cuts, recurrent and capital expenditure would be affected, with the latter likely undermining investment-driven growth.

Baseline

The baseline assumes the implementation of credibly committed fiscal consolidation measures announced in the FY22 Revised Budget and considers expected recovery effects and expenditure pressures. Key revenue reforms include an increase in the VAT rate from 9 to 15 percent for selected goods and services, the VAT zero-rating of a list of essential goods, a cut to film tax incentives, and a reversal of the recently (FY20 COVID-19 Response Budget) introduced fuel duty increase. These measures were implemented as part of the FY22 Revised Budget and are assumed to remain in place. On the expenditure side, the baseline assumes the phasing out of substantial pandemic support from FY23 onwards, but adjusts spending slightly upwards for FY23–FY24, for which the budget foresees a continued nominal wage bill freeze at FY22 levels and nominal cuts to other current spending. The adjustment is based on a history of overly ambitious forward estimates and increasing inflationary pressures, including on wages and capital spending. As a result, the latter is assumed to gradually increase and stabilize at 9 percent of GDP, which is considered a minimum for funding investments needed to expand service delivery and strengthen resilience to climate change and disasters.[7]

Projections show that measures under the baseline are insufficient to arrest the upward trajectory of the debt to GDP ratio, which is not sustainable for Fiji. Under the baseline, debt would reach close to 100 percent of GDP by 2032, and would leave Fiji with no buffers in the event of any further shocks and with increasing debt servicing costs crowding out productive spending. This conclusion is in line with the IMF's latest macro-fiscal projections for Fiji (World Economic Outlook from October 2022), which also foresee a gradual upward trend in public debt levels absent more ambitious reform. Moreover, the baseline fails to achieve the fiscal objectives set out in the Government's original MTFF. Hence, measures under the baseline do not go far enough.

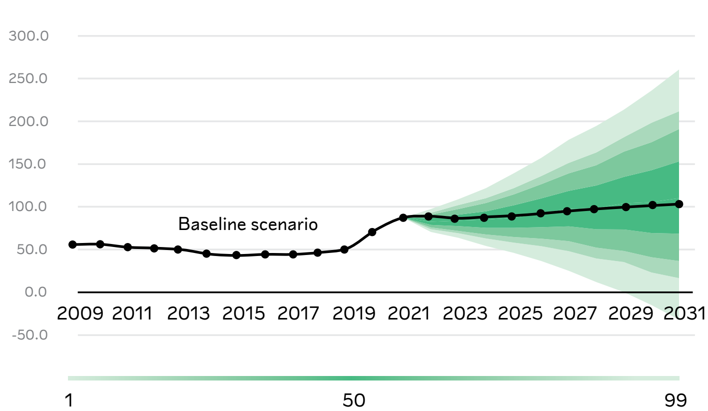
Fiji's high economic volatility increases the probability of undesirable debt trajectories, highlighting the risks associated with limiting reforms to the baseline measures. Due to frequent economic and disaster shocks, Fiji experienced higher volatility in economic growth than two-thirds of countries worldwide in the period from 1990 to 2020. The volatility has increased even further relative to other countries in the past two decades. This results in greater uncertainty surrounding the baseline projections, due to the comparatively higher variance in economic growth stemming from natural disasters. Factoring in economic volatility from natural disasters and other external shocks, the PER utilized stochastic modeling[8] on economic growth, revenues and primary expenditures to simulate 2,000 unique simulations under the baseline to provide a sense of probabilities around the projections. Of the 2,000 simulations conducted in the Fiscal Sustainability Tool, 65 percent of the time the debt-to-GDP ratio ends up above 80 percent in the baseline.[9]

7 Prior to the pandemic, the IMF recommended "sustaining capital expenditure at around 10 percent of GDP, including an increasing allocation of spending to support natural disaster resiliency" (IMF, 2020a). Given the increase in debt levels as a result of COVID-19 impacts, a slightly lower ratio of 9 percent of GDP should be considered in the short- to medium-term until fiscal space allows a gradual increase to the 10 percent target.

8 Stochastic modelling, as distinct from the traditional deterministic projections, is necessary to provide probability ranges around point estimates. In situations where there is historically little variance in growth, the deterministic projections (i.e., those in the baseline and scenarios 1 and 2) will have the majority of stochastic scenarios converge closely around the respective point estimates. However, when there is high volatility, the deterministic projections are only an average outcome, with much higher probability of achieving outcomes at a higher standard deviation away from the point estimates. Stochastic modelling allows us to put probabilities around certain outcomes occurring.

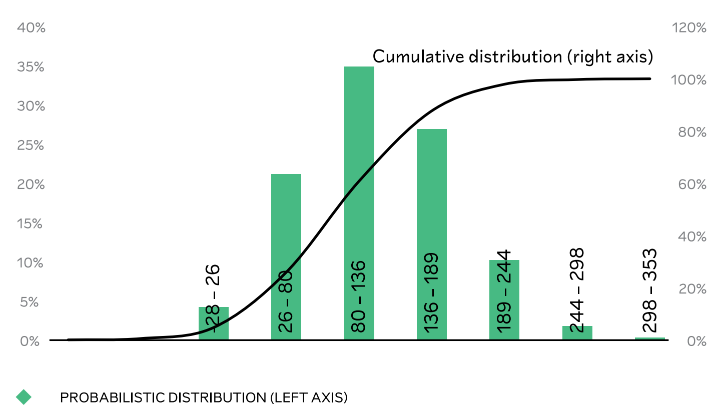
9 When running 2,000 simulations on the moderate reform scenario (Scenario 1), the number of times the debt-to-GDP ratio ends up above 80 percent was 35 percent and reduces further to 30 percent under the ambitious reform scenario (Scenario 2). Both scenarios are presented below. The stochastic modeling demonstrates the volatility around the point estimates produced in the baseline and two reform scenarios and the significant improvement in probabilities to stay below a debt-to-GDP ratio of 80 percent when moving to the ambitious reform path.

FIGURE 10 Stochastic Simulations Using Historic Economic Volatility Data Under the Baseline Show a High…



Sources: Fiji MoF, IMF, World Bank staff estimates

FIGURE 11 … Probability for Undesirable Debt Trajectories, Reinforcing the Importance of Decisive Reform Action



Sources: Fiji MoF, IMF, World Bank staff estimates

Scenario 1

Moderate fiscal consolidation

The moderate fiscal consolidation scenario additionally assumes the implementation of a comprehensive revenue reform package and modest expenditure side measures. This scenario comprises reforms to simplify the personal income tax rate structure and lower the tax free threshold, raise the fringe benefit tax, and introduce a dividend withholding tax. It would also eliminate reduced corporate income tax rates and export incentives, extend the increased VAT rate to other goods and services, raise the excise tax on alcohol to previous levels, and implement a modest increase in the departure tax. A removal of the zero-rating of VAT on essential items is combined with an increase in poverty benefit scheme spending to offset negative impacts on lower-income households.

Expenditure measures will support fiscal consolidation by focusing on the wage bill, tertiary spending and sugar subsidies. These revenue measures are supplemented by slightly lower nominal wage bill growth in FY24, a reduction in tertiary education scholarship and loan scheme spending, and a modest cut in other current spending. A gradual reduction in sugar sector subsidies is partially offset by redirected agriculture support spending to provide an enabling environment (including basic agricultural research and development). No cuts to baseline capital spending are made in order to limit negative long-term impacts on growth and maintain a minimum spending level to fund investments in public service delivery and climate and disaster resilience.

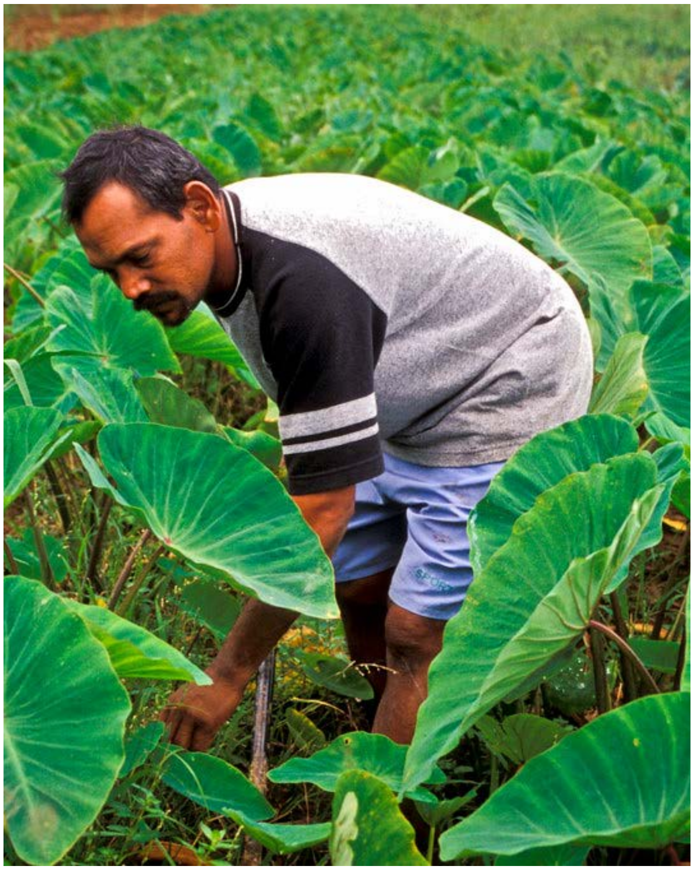
The moderate consolidation scenario puts Fiji on a pathway to reducing its debt to GDP ratio, which would fall to around 65 percent by 2032. This scenario would result in the government meeting the majority of the objectives set out in its MTFF and hence is the minimal viable scenario. However, this scenario would still leave the debt-to-GDP ratio well above its pre-crisis level of around 50 percent, which was considered high prior to the pandemic given Fiji's substantial exposure to shocks.

Scenario 2

Ambitious fiscal consolidation

The ambitious fiscal consolidation scenario assumes the implementation of further, more aggressive revenue measures, and a more comprehensive expenditure reform package. It considers the following selected additional revenue reforms over FY23 to FY27: (i) the reversal of the fuel duty reduction included in the baseline (and implemented as part of the FY22 Revised Budget); (ii) the introduction of an excise tax on sugar(y) products; (iii) a further rise in the departure tax to pre-crisis levels; and (iv) the implementation of a revenue administration improvement program, partially offset by its costs. Expenditure-side reforms include (i) an extension of the lower nominal wage bill growth until FY25; (ii) the full phase-out of sugar sector subsidies, partially offset by agriculture support spending; (iii) a further modest reduction in tertiary education support; and (iv) additional modest cuts to other current spending. Capital spending increases to 9 percent of GDP are maintained in this reform scenario, which is considered the minimum necessary to fund investments in public service delivery and resilience.

The only path for Fiji to return to pre-crisis debt levels is through the ambitious fiscal consolidation pathway. As shown below, this ambitious consolidation scenario is the only one that puts Fiji on a pathway to getting the debt to GDP ratio back to pre-crisis levels within a decade. It is also the only scenario that would achieve all the objectives set out in the Government's MTFF.



Summary of Reform Scenarios Modeling Approach & Results

3.3

Methodology

This sub-section summarizes the reform modeling approach. The reform scenarios are informed by the background chapters prepared by sector teams, and the modeling includes several central models to ensure internal consistency and second-round effects are captured. The growth impacts from the different consolidation pathways have been considered using the Fiscal Multiplier tool. To model the impacts of improved poverty targeting on growth outcomes, the PER utilized the Commitment to Equity (CEQ) framework and fiscal multipliers model to adopt a distributional estimate of spending that reflects the positive growth impact from that reform. To model the improvements in public investment spending, the PER utilizes the Long-Term Growth Model. These are explained further in Appendix 3 of Background Paper A. Subsequently, the Fiscal Sustainability Analysis (FSA) Tool was applied to quantify implications for debt sustainability. Using stochastic modeling within the FSA tool, the impact of disaster and other shocks was assessed.

Modelling the second-round growth impacts from fiscal consolidation

The consolidation measures will hurt economic growth and the PER results include those impacts for each scenario. Using a fiscal multiplier framework to assess the impact of different reforms on economic growth under the scenarios, results suggest that reforms under Scenario 1 result in a 1.9 percent lower GDP in FY25 and 1.1 percent lower GDP in FY27.[10] The reduction in GDP results primarily from tax measures, particularly increases in VAT rates. The second reform scenario further lowers activity, with GDP lower by 2.4 percent in FY25 and 1.3 percent in FY27. The additional weakness in activity in Scenario 2 is from the increases in excise taxes and further small cuts to current expenditure.

Modeling the growth impacts of improving the targeting of social assistance

Fiscal incidence analysis found that a significant share of spending on social assistance programs is allocated to wealthier households and better targeting could increase growth. The CEQ analysis showed that in the case of the poverty benefit scheme, for example, around one-third of the scheme goes to households in the upper half of the income distribution. These households have lower propensities to consume than those in the lower half of the distribution. Moving a share of this spending from high-income households to low-income households through better targeting could create a temporary positive impact on GDP. In an ideal case of reaching only low income households, the growth impact from increased poverty scheme spending would almost double from about 0.3 percent at the current targeting level to close to 0.6 percent. This provides a clear motivation for the authorities to continue reforms, such as the recent approval of an overarching social assistance policy and highlights the importance of implementing the planned social registry to inform better targeting.

Modeling the impacts from improving public investment management (PIM)

Using the World Bank's LTGM, estimates were made to illustrate how changes in public investment spending efficiency could increase growth. These show that improving PIM efficiency by closing half the distance between Fiji (with an upper-middle income median efficiency) and the average high-income median efficiency would raise the growth rate of per-capita growth in Fiji by around 0.05 percentage points per year. A more ambitious reform program that closes the full distance between Fiji and the high-income median efficiency would raise the long-term per-capita growth rate in Fiji by around 0.11 percentage points per year. While these contributions may appear small, affecting only new investment and therefore the total public capital stock only slowly, such growth impacts are long-lasting, adding up over time and making a case for decidedly reforming PIM in Fiji.

10 This factors in moderate improvements in targeting of social assistance and public investment management discussed below.

FIGURE 12 Improved Targeting of Social Assistance Programs can Result in a Temporary Boost to GDP from Additional Household Consumption…

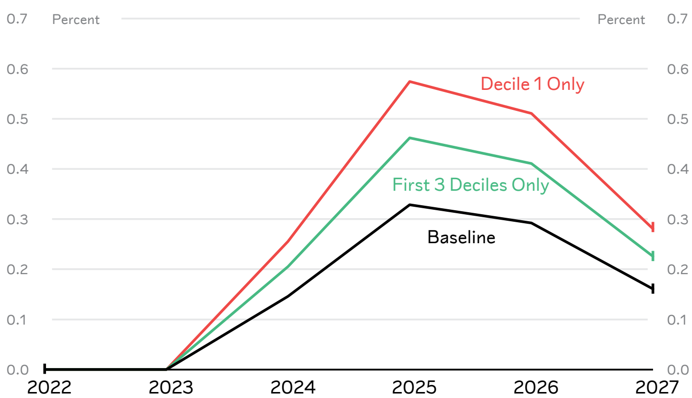


FIGURE 13 …While Better Public Investment Management Can Help Offset a Share of Negative Impacts on GDP from Fiscal Consolidation Reforms

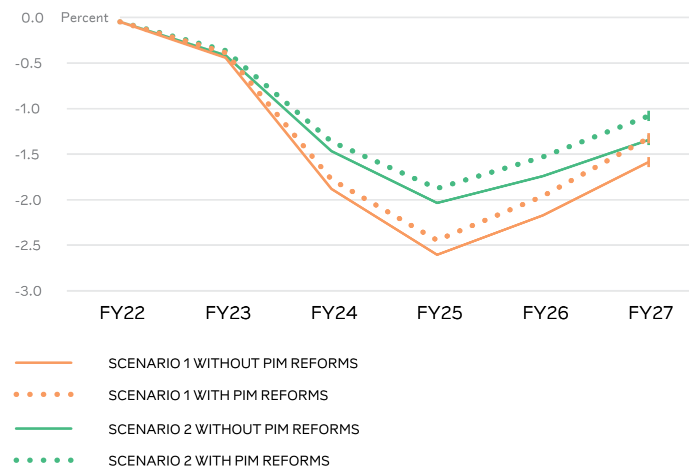


FIGURE 14 Impacts on GDP from Reforms under Scenario 2 Compared to Baseline

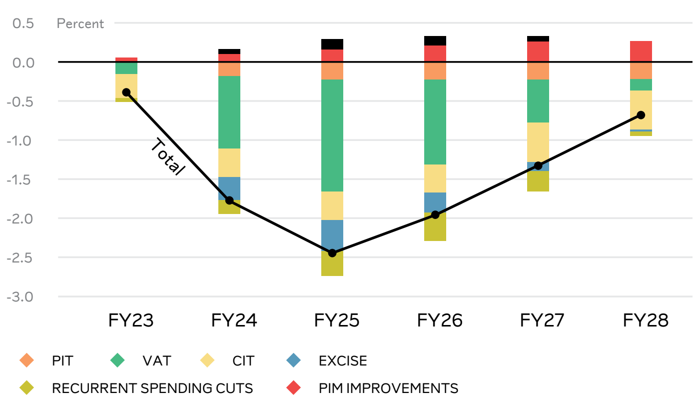
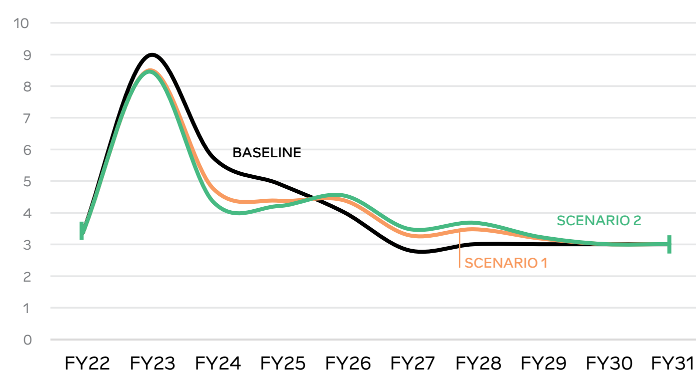


FIGURE 15 Real GDP Growth under Different Consolidation Pathways

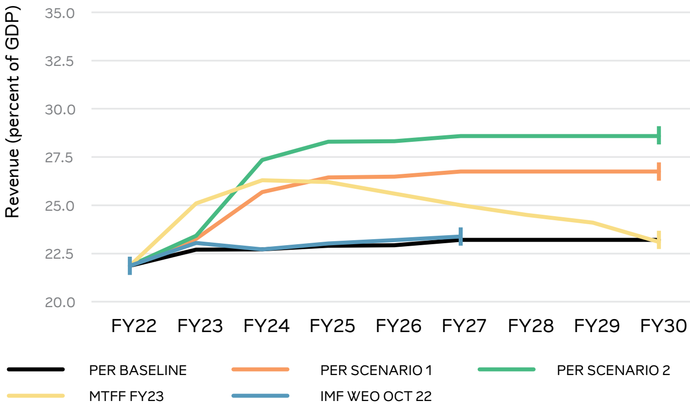


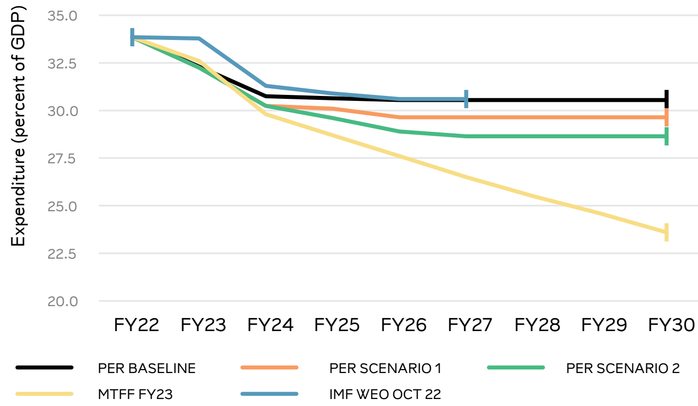
Source: World Bank staff estimates

Results

The results show that the Government needs to implement substantive revenue and selected, well-targeted expenditure reforms to chart a downward trajectory for public debt. This needs to be achieved in addition to what is already credibly committed under the baseline scenario. In both Scenarios 1 and 2, interest as a share of GDP returns to pre-COVID-19 levels (at varying speeds), which is essential to avoid the crowding out of more productive spending. To achieve their overarching debt targets, the authorities need to implement reforms at least as ambitious as those set out in Scenario 1. However, Scenario 1 is close to a zero primary balance scenario where growth would be the only debt reduction driver, which appears to be a risky strategy. As illustrated in the table below, the other fiscal targets are only consistently achievable with more ambitious reforms, in line with those included under Scenario 2. Only Scenario 2 reaches pre-pandemic debt levels within a decade, which are still considered high for a country exposed to frequent shocks. The ambitious consolidation path illustrated under Scenario 2 is particularly worth considering by the authorities, as the high disaster risk and exposure to climate change impacts as well as the uncertain global outlook warrant the rapid rebuilding of fiscal buffers and the freeing up of fiscal space for growth-and resilience-enhancing investments.

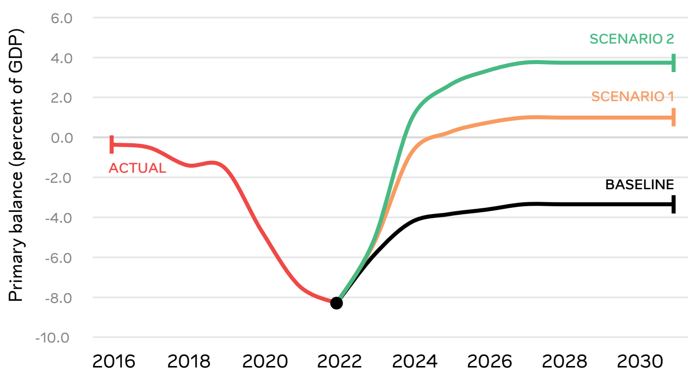
FIGURE 16 Revenue and Expenditure Trajectories under the Different Consolidation Pathways

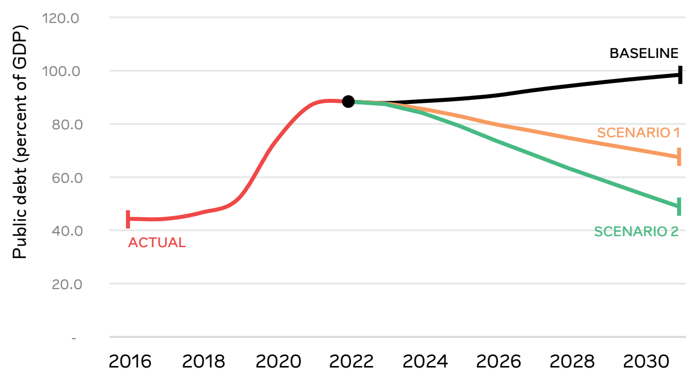




Sources: Fiji FY23 Budget, IMF World Economic Outlook October 2022, World Bank staff estimates.

FIGURE 17 Primary Balance and Public Debt Trajectories under the Different Consolidation Pathways





Sources: Fiji MoF FMIS, IMF World Economic Outlook October 2022, World Bank staff estimates.

TABLE 3 Contributions to Fiscal Consolidation

Scenario			Baseline	Scenario 1	Scenario 2
Fiscal deficit in FY22 (percent of GDP)			-12.0	-12.0	-12.0
Cumulative reform impact by FY27 (percent of GDP)		Tax revenue	0.5	4.2	6.1
		Primary expenditure	-3.6	-4.4	-5.3
		Total consolidation	**4.1**	**8.6**	**11.4**
Recovery and other changes (net consolidation, percent of GDP)*			0.6	0.5	0.6
Fiscal deficit in FY27 (percent of GDP)			-7.3	-2.9	-0.1
Public debt	Percent of GDP	2023	87.9	87.6	87.5
		2032	99.6	65.2	44.3
	Change 2023-2032	Total	11.7	-22.5	-43.2
		p.a.	1.3	-2.5	-4.8
Growth	Average annual real growth rate 2023-2027		5.3	5.1	5.0

* This comprises non-directly reform related changes to tax revenue from the economic recovery, stabilization of non-tax revenue collections at its long-term pre-COVID-19 average (2.6 percent of GDP over FY10-FY19), a partial normalization of grant receipts following a COVID-19-related spike, and changes to interest payments as an expected result from reform implementation and corresponding changes to fiscal outturns.

Sources: MoF Fiscal Outturn Report FY22, World Bank staff estimates.

TABLE 4 The Assessment of Scenario Outcomes Against Government Fiscal Targets Indicates the Need for an Ambitious Fiscal Consolidation

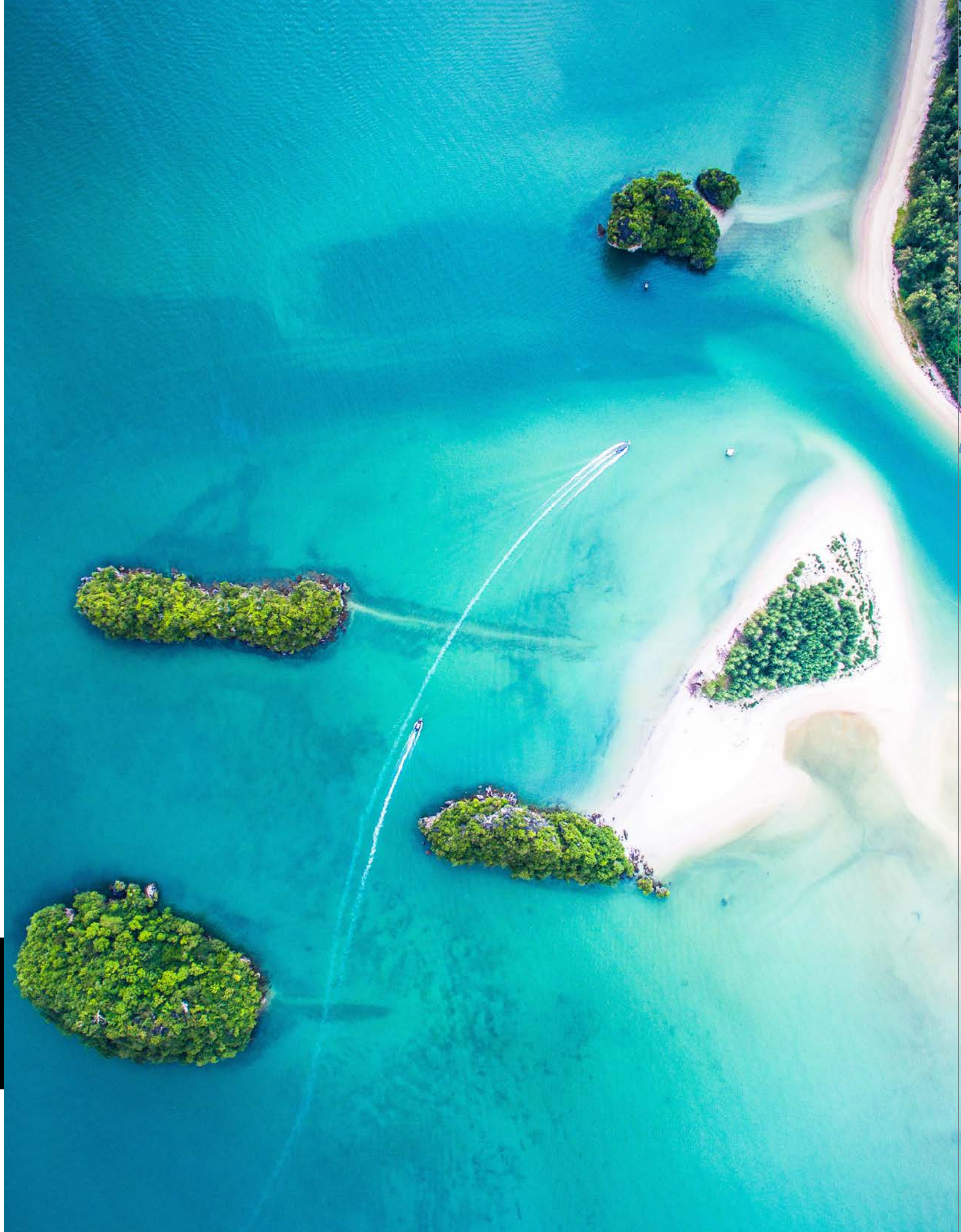
Government fiscal target (FY22 Budget Supplement)	Baseline	Scenario 1	Scenario 2
REVENUE-TO-GDP RATIO: To be maintained at 26 percent by FY23	**Not achieved** (22.7 percent in FY23 and 23.2 percent in FY27)	**Achieved** but later (23.3 percent in FY23 and above 26 percent from FY25)	**Achieved** but later (23.4 percent in FY23 and above 26 percent from FY24)
EXPENDITURE-TO-GDP RATIO: To be reduced to 30 percent by FY24	**Not achieved** (30.7 percent in FY24 and 30.5 percent in FY27)	**Achieved** but later (30.2 percent in FY24 and below 30 percent from FY26)	**Achieved** but later (30.2 percent in FY24 and below 30 percent from FY25)
PRIMARY BALANCE: Return to and maintain surplus from FY24 or earlier	**Not achieved** (ongoing deficits)	**Achieved** but later (-0.8 percent in FY24 and surplus from FY25)	**Achieved** (0.9 percent in FY24)
FISCAL DEFICIT			
Below 5 percent from FY23	**Not achieved** (9.6 percent in FY23)	**Achieved** but later (-9.0 percent in FY23 and below 5 percent from FY24)	**Achieved** but later (-8.8 percent in FY23 and below 3 percent from FY24)
Further reduction to 2 percent of GDP from FY27 or earlier	**Not achieved** (7.3 percent in FY27)	**Not achieved** (-2.9 percent in FY27)	**Achieved** (below 2 percent from FY25)
BORROWING: Restricted to high impact, high return and strategic capital expenditures	**Not achieved**	Achievable through prudent debt management and recommended public investment management reforms	
DEBT-GDP-RATIO			
80 percent by FY26	**Not achieved** (91 percent in 2026)	**Achieved** (80 percent)	**Achieved** (74 percent)
60 percent of GDP by FY36	**Not achieved** (103 percent in 2035)	**Achieved** (58 percent in 2035)	**Achieved** (31 percent in 2035)

Sources: Fiji MoF; World Bank staff estimates.

Reform Options

4

P.26–33



In-depth analysis by sectoral experts yielded recommendations of how fiscal consolidation can be achieved and the quality of public spending increased. Summaries of the main reform recommendations are presented on the following pages. The reforms are prioritized and sequenced across the scenarios described above, which can be adjusted to align with the priorities of the new Government that was formed after the December 2022 General Election.

The main reform recommendations comprise:

Five revenue reform packages, covering: (A.1) reforming the VAT regime by expanding the VAT rate rise to other goods and services and reversing the zero-rating of VAT on essential items (while compensating low income households for negative impacts); (A.2) updating the corporate income tax regime and reducing tax incentives; (A.3) expanding the customs and excise tax regimes; (A.4) simplifying personal income tax rates and broadening their base; and (A.5) reversing departure tax reductions as tourism rebounds. A supplementary reform to strengthen domestic resource mobilization should focus on improving revenue administration performance. Detailed analysis and reform discussions are presented in Background Chapter B.

Four expenditure reforms, covering: (B.1) controlling the public wage bill to prevent upward pressures from materializing and achieving a gradual reversal of spending back to FY16 levels; (B.2) prudently managing capital outlays, allowing for a slight increase to 9 percent of GDP, and making public investment more efficient and effective; (B.3) transitioning out of sugar sector support; and (B.4) phasing out pandemic support and restraining other current spending, broadly in line with the forward estimates of the FY22 Revised Budget and FY23 Budget. Detailed analysis and reform discussions of measures B.1 to B.3 are presented in Background Chapters C, D and E, respectively. Supplementary expenditure side measures the Government should implement are: (i) improving targeting of social protection schemes, and (ii) reforming the tertiary education scholarship and loan schemes. The two supplementary reforms are briefly discussed in Background Chapter A and in detail in the forthcoming CEQ report and education sector PER for Fiji.

Four complementary public financial management reform areas, comprising (C.1) continuing prudent borrowing and good debt management practices to reduce costs and risks of public debt; (C.2) closely monitoring and reducing fiscal risks stemming from contingent liabilities that have been increasing in recent years; (D.1) improving data collection and information systems to provide an evidence base for fiscal policy, reform design, and impact monitoring; and (D.2) strengthening strategic fiscal planning and budgeting to guide consolidation efforts over the medium-term in a transparent and accountable manner. These complementary reforms are discussed in more detail in Background Chapter A.

These reforms need to be complemented by business environment reform, fostering private sector development to support growth. This PER applies a public sector lens, with a fiscal consolidation focus supplemented by public financial management considerations. However, reforms to address cross-cutting private sector development constraints in the areas of skills, finance, infrastructure, and the business environment are equally critical to provide a sustainable basis for domestic resource mobilization and livelihoods for the citizens of Fiji. One important area for reform, alluded to in the sugar industry review in Background Chapter E, is land reform to enable the development of a diversified and competitive agricul-

Scenarios at a glance

Baseline

This comprises credibly committed reforms only and considers expenditure pressures stemming from inflationary trends and the global interest rate environment as well as investment needs (including for climate and disaster resilience). This provides the basis for fiscal consolidation, but is insufficient to achieve a downward trajectory in the debt-to-GDP ratio, which would increase to 101 percent by 2031.

Scenario 1: Moderate consolidation

This comprises substantial revenue reforms and targeted expenditure measures that would support moderate fiscal consolidation. Together, these would bring down debt relative to GDP to 76 percent by 2031.

Scenario 2: Ambitious consolidation

This comprises additional reforms supporting an ambitious fiscal consolidation, charting a steeper downward path of the debt-to-GDP ratio to 58 percent by 2031. This is the recommended scenario in light of Fiji's exposure to frequent shocks.

tural sector. Further, the enabling conditions for raising private sector finance for capital investments in service delivery and resilience is discussed in Background Chapter D. Complementary to the PER, an in-depth Country Private Sector Diagnostic (CPSD) titled *Creating Markets in Fiji* and published by the International Finance Corporation in May 2022, provides insights into constraints to private sector growth and investment in Fiji and a comprehensive list of reform recommendations to address these. The diagnostic further identifies outsourcing services, health care, and agri-logistics as strategic sectors to drive growth and contribute to economic diversification, resilience, and inclusive job creation while strengthening Fiji's position as a sector hub/market leader in the Pacific region.

FIGURE 18 Overview of Reform Recommendations

Sustainable debt & financing of public goods and services for growth and resilience

A. Modern revenue policy and administration

- A.1 Reforming the VAT regime
- A.2 Updating the CIT regime and reducing tax incentives
- A.3 Expanding the customs and excise tax regimes
- A.4 Reforming PIT
- A.5 Increasing the departure tax

SUPPLEMENTARY MEASURE: Improving revenue administration

B. Efficient expenditure allocation and management

- B.1 Controlling the public wage bill
- B.2 Prudently managing capital outlays and improving public investment management
- B.3 Phasing out of sugar sector support
- B.4 Phasing out of pandemic support and restraining other current spending

SUPPLEMENTARY MEASURE:

- Improving targeting of social protection schemes and
- Reforming the tertiary education scholarship and loan schemes

C. Effective liabilities and fiscal risk management

- C.1 Continuing prudent borrowing and strong debt management
- C.2 Continuing monitoring and gradually reducing contingent liabilities

Building Blocks

D.2 Strategic fiscal planning and budgeting

D.1 Effective information systems and data collection

Foundations

Modern Revenue Policy & Administration

Revenue reforms considered across the baseline and two scenarios have the potential to contribute 6.1 percent of GDP to fiscal consolidation by FY27, subject to reform ambition. The major share of these is expected to come from the restoration of VAT rates back to pre-2016 levels of 15 percent, which is in line with regional peers. Even when implementing a cash transfer to offset the impacts on poor households, significant fiscal gains remain. Further revenue gains can be achieved by the introduction of a 10 percent withholding tax on dividends. The PER also recommends an introduction of excise taxes on sugary products and an increase to excise taxes for alcohol. These taxes provide social benefits to help Fiji deal with significant health challenges associated with overconsumption of these products, with similar measures introduced in other Pacific countries in recent years. Finally, (i) reforming the PIT regime by simplifying the rate structure and broadening the base and (ii) increasing the departure tax and instituting annual price increases going forward could further support the revenue-based fiscal consolidation effort of the Government. Supplementary, the implementing of a revenue administration improvement program could yield net increases in revenue collections. These reforms assessed in Background Chapter B are presented on the following pages.

TABLE 5 Overview of Revenue Reforms

Reform #	Main purpose	Cumulative impacts by FY27 (percent of GDP)		
		Baseline	Scenario 1	Scenario 2
A.1 Reforming the VAT regime	To restore pre-2016 VAT rates with direct transfers offsetting negative reform impact on low income households.	+0.30	+2.76*	+2.76
A.2 Updating the CIT Regime & Reducing Tax Incentives	Elimination of reduced CIT rates, discontinuation of Export Incentive and introduction of dividend withholding tax	+0.68	+1.15	+1.15
A.3 Expanding the Customs & Excise Tax Regimes	Reversal of fuel duty increase, increase in excise tax on alcohol and introduction of an excise tax on sugar(y) products	-0.5	-0.14	+0.72
A.4 Reforming PIT	Simplify PIT rates and broaden the tax base	0.00	+0.31	+0.31
A.5 Increasing the Departure Tax	Reverse reduction in departure tax and index it to inflation	0.00	+0.16	+0.64
SUPPLEMENTARY MEASURE				
Improving revenue administration	Implement a revenue administration improvement program	0.00	0.00	+0.50
Total net change in revenue in percent of GDP		+0.47	+4.24	+6.08

* The additional social assistance spending to compensate low-income households for negative effects from the reversal of zero-ratings on essential items is included in the supplementary expenditure measures under Building Block B. below.

Reforming the Value-Added Tax (VAT) Regime

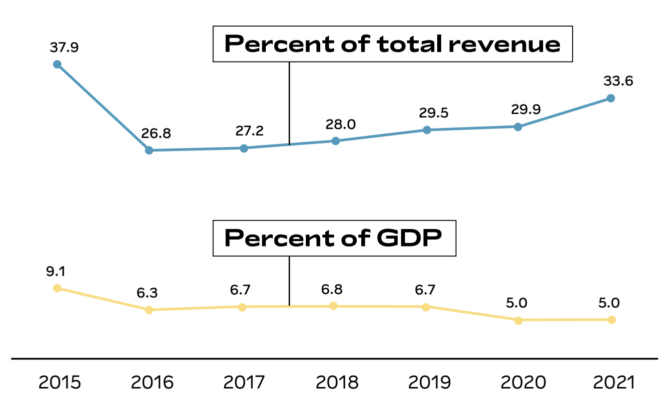
Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	VAT increase from 9 to 15 percent on selected goods & services, partially offset by zero-rating of essential items and ECAL elimination (implemented)	FY22	+0.30
1	Remove zero-rating of VAT on essential items*	FY24-FY25	+1.60
	Broadly apply increased VAT rate of 15% (phased as needed and with no or strictly limited exceptions)	FY24-FY25	+0.86
			Total: +2.46
2	No additional changes		
Total revenue impact in percent of GDP			+2.76

* The removal of zero-rating of VAT on essential items should be accompanied by an increase in direct transfers to offset negative impact on low income households. A spending program amounting to 0.6 percent of GDP is included for FY24-FY25 under Building Block B below.

Background & analysis

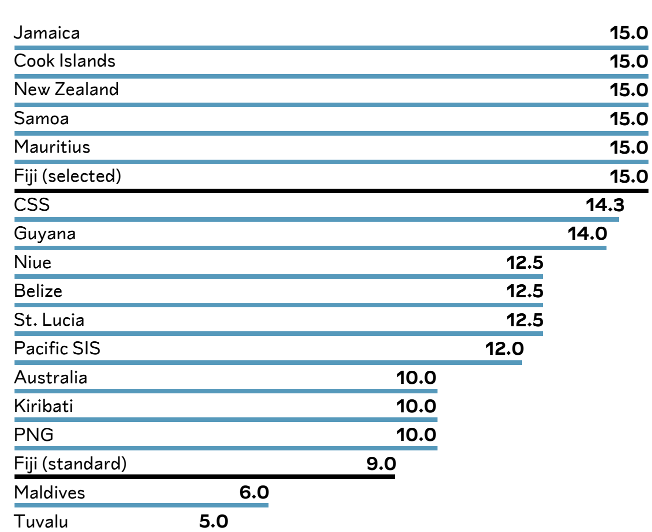
VAT has historically been Fiji's largest revenue source, but reforms in 2016 followed by COVID-19 have led to a decline in revenue performance. A VAT first came into effect in 1992 at a standard rate of 10 percent, which was gradually raised to 15 percent in 2012. VAT was the largest revenue source in 2015, accounting for 37.9 percent of total revenues and 9.1 percent of GDP. However, reforms in 2016 reduced the standard VAT rate from 15 to 9 percent, resulting in a sharp drop in VAT revenues to 6.3 percent of GDP. COVID-19 brought additional exemptions and a sharp economic downturn, further reducing VAT revenues to 5.0 percent of GDP by 2021. Fiji's standard VAT rate is amongst the lowest in the region and third-lowest among benchmark countries, and multiple rates and a growing list of zero-rated items complicate the system and erode its revenue potential. From April 2022, a higher 15 percent rate has been applied on selected goods and services. However, zero rating has also been extended to an additional 21 items.

FIGURE 19 VAT Rate Changes and COVID-19 had Substantial Impact on Fiji's Largest Revenue Source



Sources: Fiji MoF, World Bank staff estimates.

FIGURE 20 Overall, Fiji's VAT Standard Rate is Low Relative to Benchmarks (Percent)



Sources: FRCS, RBF and WB staff calculations

Reform recommendations

Reversing the negative trend in VAT collections is a high priority for fiscal consolidation, given their significance for domestic resource mobilization. The FY22 Revised Budget made a start, but further reforms are needed. The technical analysis recommends the broad application of an increased, single rate of VAT. Returning to the pre-2016 rate of 15 percent, already partially introduced through the FY22 Revised Budget, appears to be suitable. This could be implemented in a phased manner (as appropriate) and should have no or strictly limited exceptions, in line with international best practice. The VAT rate change should be complemented with reforms to the registration threshold, voluntary registration, and non-resident suppliers. Further, as fiscal incidence analysis shows that using the VAT regime to provide relief to poorer households through zero-rating of essential items is costly, the PER recommends replacing this with an increase in direct transfers to poor households, for which targeting needs to improve (see discussion on social protection schemes below).

Revenue A.2

Updating the CIT Regime & Reducing Tax Incentives

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	Cuts in the film tax rebate scheme (implemented)	FY22	+0.68
1	Eliminate reduced CIT rates and apply standard rate of 20 percent (implemented in FY23 budget)	FY23	+0.05
	Discontinue Export Incentive	FY24	+0.13
	Introduce dividend withholding tax at a rate of 10 percent	FY24	+0.29
			Total: +0.47
2	No additional changes		
Total revenue impact in percent of GDP			+1.15

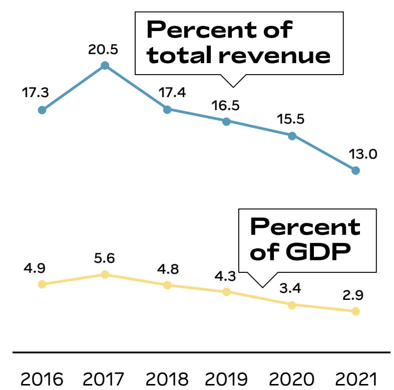
Background & analysis

Corporate Income Taxes (CIT) have historically been the third-largest revenue source after VAT and customs duties, although growing exemptions and COVID-19 have reduced its revenue performance. A Company Tax, levied at a standard rate of 20 percent, is the main CIT, followed by a 15 percent withholding tax and a host of other minor taxes. CIT revenues accounted for 20.5 percent of total government revenues in 2017, equivalent to 5.6 percent of GDP. However, the removal of a 9 percent non-resident dividend withholding tax in 2017 and a growing list of exemptions and incentives (especially for the film industry) began to impact revenue performance, a trend accelerated by COVID-19. CIT revenues fell to 13.0 percent of revenues and 2.9 percent of GDP by 2021.

Fiji's standard Company Tax Rate (CTR) is very competitive, while multiple rates and a growing list of exemptions and incentives complicate the system and erode its revenue potential. Fiji's standard CTR of 20 percent is the fifth-lowest among benchmark countries and regions. Before the FY23 Budget, reduced rates of 17 percent were applied to some companies and just 10 percent to listed companies. Moreover, there are at least 40 different tax exemptions and incentives, which greatly complicates the tax system, creates economic distortions and may have eroded up to 50 percent of all CIT revenues.

FIGURE 21

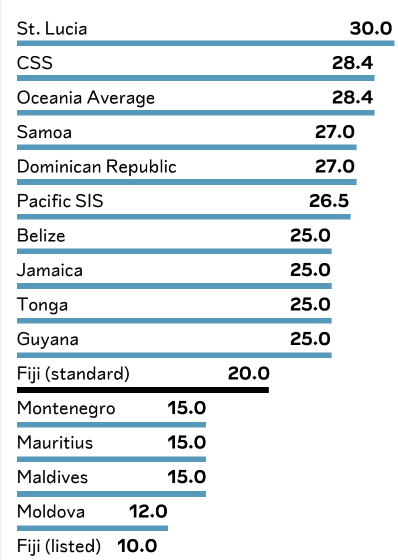
Growing Exemptions And Incentives, Plus COVID-19, Have Reduced CIT Revenues



Sources: FRCS, RBF and WB staff calculations.

FIGURE 22

Fiji's Company Tax Rate is Competitive Relative to Benchmark Countries and Regions



Sources: IMF, OECD, and WB staff calculations.

Reform recommendations

Reversing the negative trend in CIT collections is a high priority for fiscal consolidation, given their significance for domestic resource mobilization. A start has been made with the changes introduced as part of the FY22 Revised Budget and the elimination of the reduced company rates for selected companies and the broad application of the 20 percent standard company tax rate recommended by the technical analysis and introduced in the FY23 Budget. These should be maintained. Additional priorities include reviewing and rationalizing the long and growing list of CIT tax exemptions and incentives and reintroducing a withholding tax on non-resident dividends at a rate of 10 percent.

Expanding The Customs & Excise Tax Regimes

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	Reversal of fuel duty increase introduced in FY20 (implemented)	FY22	-0.51
1	Increase excise tax on alcohol	FY24	+0.37
2	Reverse fuel duty reduction implemented in FY22	FY24	+0.51
	Introduce an excise tax on sugar(y) products	FY24	+0.35
			Total: +0.86
Total revenue impact in percent of GDP			+1.15

Background & analysis

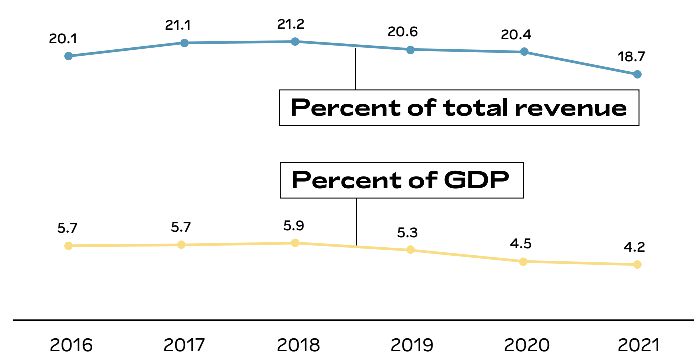
Customs revenues have historically been the second-largest revenue source after VAT in Fiji. Fiji levies both trade tariffs (fiscal duties), most frequently at around 5 percent, and specific dollar excise taxes on goods such as tobacco and alcohol. Customs revenues accounted for 21.2 percent of total government revenues in 2018, equivalent to 5.9 percent of GDP. The granting of exceptions to selected goods in 2018 (especially imported transport vehicles) and substantial COVID-19 relief measures, including zero-rating of medical supplies and reductions in import tariffs, significantly reduced revenue performance. Customs revenues fell to 18.7 percent of revenues and 4.2 percent of GDP by 2021. In addition, the Government recently cut the fuel duty in response to soaring global oil and energy prices.

Fiji's excise regime is narrow, undermining its revenue potential. Fiji's excise revenues equated to just 1.8 percent of GDP in 2019, which is the lowest of all comparable benchmarks. Unlike most countries in the region, Fiji has not been levying an excise tax on fuel products and motor vehicles, though the FY23 Budget increased import duties on cars and introduced a levy on luxury vehicles. In addition, the Government ceased indexing the specific excise amounts by 3 percent a year after businesses argued that the excise rates had reached their optimum levels, and implemented a 50 percent reduction in the alcohol excise tax as part of its COVID-19 relief measures.

1.8%

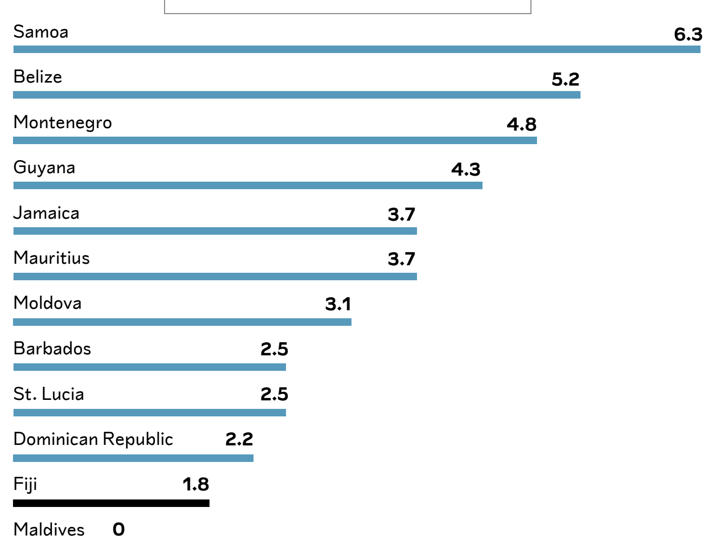
Fiji's excise revenues in 2019

FIGURE 23 Growing Exemptions and Incentives, plus COVID-19, Slowly Eroded Customs and Excise Revenues



Sources: FRCS, RBF and WB staff calculations.

FIGURE 24 Fiji Collects Less Excise Taxes as a Share of GDP than Peers



Sources: IMF, OECD, and WB staff calculations.

Reform recommendations

Reversing the negative trend in duty collections is a high priority for fiscal consolidation, given their significance for domestic resource mobilization. This should be driven by increases in excises combined with a review of the current customs exemptions, for which the technical analysis recommends a rationalization. Moreover, the Government should increase the excise tax on alcohol and introduce excises on fuel and sugar products. The Government should also resume the practice of indexing specific excise rates annually to preserve the value of the revenues in real terms. To mitigate concerns from the business community, rates could be automatically indexed to inflation rather than at the previous fixed level of 3 percent per year.

Revenue A.4

Reforming Personal Income Tax

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	None		
1	Simplify PIT structure and lower threshold to F$20,000	FY24	+0.16
	Raise Fringe Benefit Tax to 35 percent	FY24	+0.15
			Total: +0.31
2	No additional changes		
Total revenue impact in percent of GDP			+0.31

Background & analysis

PIT in Fiji consists primarily of a Pay As You Earn (PAYE) tax and a Social Responsibility Tax (SRT) applicable to high-income earners, resulting in combined marginal PIT rates from 18 percent to 44 percent. Fiji also has a host of other minor PIT taxes, of which the largest one is a Fringe Benefits Tax (FBT) at a flat rate of 20 percent. PIT has historically been the sixth largest revenue source in Fiji, yielding slightly over 2.0 percent of GDP before the almost doubling of the PAYE tax-free threshold to FD30,000 in 2017 reduced performance even prior to COVID-19. As a result, the PIT-to-GDP ratio declined by 0.5 percentage points to 1.7 percent by 2019. Overall, Fiji's PIT system is effective and progressive, with relatively few exemptions, the taxation of residents' worldwide income and nonresidents' income sourced in Fiji, and relatively comprehensive coverage of income sources. CEQ analysis confirms that the system succeeds in it its objective of being progressive. **However, the rate applicable to the first taxable income bracket (18 percent) is higher than benchmark countries, resulting in a relatively steep upward-sloping effective tax rate, instead of ensuring a gradually increasing effective tax burden on middle-income earners.** Further, the top marginal tax is relatively high and the rate structure appears unnecessarily complex. The tax free threshold of F$30,000 (about USD 14,000) is nearly three times Fiji's per capita GDP and is relatively high compared to most benchmark countries, resulting in a relatively low population coverage of the PIT regime. Finally, the flat FBT rate of 20 percent is very low compared to the top marginal tax rate of 44 percent, which may incentivize employers and employees to convert compensation into fringe benefits to take advantage of its preferential tax treatment.

Reform recommendations

Going forward, there are significant opportunities to increase PIT revenues as well as reduce complexity by introducing a single unified PIT rate structure, simplifying the rate schedule to perhaps 4-6 brackets, increasing the FBT tax to 35 percent to reduce incentives for tax avoidance, and optimizing the bottom and top thresholds. The latter could comprise (i) reducing the top marginal tax rate (44 percent), perhaps to 40 percent, in the long-term to increase the competitiveness of Fiji's top rate relative to benchmark countries, and (ii) reducing the income tax exemption threshold from its current level of FD 30,000, perhaps back to its previous level of FD 16,000 roughly in line with the benchmark average, while simultaneously reducing the rate applied to the first income bracket (18 percent) towards the benchmark average of 10 percent to create a more gradually upward sloping effective tax curve and broaden the applicable population base. Subject to further detailed analysis of revenue implications and distributional impacts of alternative rate levels, income bands and exemption thresholds, revenue gains of 0.16 percentage points are estimated from reducing the number of income bands from nine to four and lowering the tax-free threshold, and of around 0.15 percentage points from increasing the fringe benefits tax from 20 to 35 percent.

Revenue A.5

Increasing the Departure Tax

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	None		
1	Raise departure tax from F$100 to F$125	FY24	+0.16
2	Raise departure tax by a further F$75 to F$200 plus a small annual increase	FY24	+0.48
Total revenue impact in percent of GDP			+0.64

Background, analysis, and reform recommendation

Prior to the pandemic, departure tax was charged at F$200 and has been a stable source of revenue for Fiji, yielding an average of 1.3 percent of GDP over FY15–FY19. While this is higher than in comparator countries, such as the Cook Islands (F$108 equivalent), Samoa (F$33) and Tonga (F$50), this did not undermine Fiji's leading position as a regional tourism hub. As part of pandemic response measures, the tax was reduced to F$100 with the aim of ensuring Fiji's competitiveness as a tourism destination and supporting its recovery as travel restrictions were lifted in December 2021. As tourism rebounds, it is recommended to increase the departure tax back to pre-crisis levels (either at once or in steps). In addition, an automatic annual increase could help maintain the real value of the tax. The Cook Islands are an example in the region where the departure tax is increased by 2 percent yearly since 2014.

Supplementary Revenue Measure

Improving Revenue Administration

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	None		
1	None		
2	Implement a revenue administration improvement program	FY23-FY25	+0.50*
Total revenue impact in percent of GDP			+0.50

* This is the estimated net impact taking into account program costs, including for additional staffing and system improvements.

Background & analysis

Overall, Fiji's revenue administration is relatively sound by regional standards. Tax collection costs are moderate, amounting to 2.2 percent in 2018-19 and 2.5 percent in 2020, which is slightly above the typically recommended range of 1-2 percent of revenue collections. In recent years, the Fiji Revenue & Customs Service has introduced several important reforms to improve revenue administration, including through a new tax information system, validated taxpayer registration information, risk management strategies, and tax communication programs. However, audits have revealed increasing tax avoidance and evasion in Fiji, with practices such as transfer pricing, profit-shifting, and customs valuation issues on the rise. The FRCS also reports taxpayers' failure to register for various taxes, limited uptake of the online taxpayer platform, non-filing of tax returns, no or delayed payment of applicable taxes, and inadequate record keeping mainly by small and medium taxpayers as tax administration issues. The accumulation and aging of tax arrears is also a growing problem. Moreover, between 2017 and 2020, staff levels at FRCS were reduced by an estimated 15 percent, impacting field inspections and taxpayer awareness programs, in addition to a general lack of specialized expertise in transfer pricing and international taxation.

Reform recommendations

Financing and implementation of a revenue administration improvement program could generate positive returns, resulting in a revenue uplift of up to 0.5 percentage points of GDP (net of program costs). The key focus of the program should be to: (i) increase tax registration, encourage greater use of the new online tax system, and reduce tax avoidance; (ii) reduce tax arrears; and (iii) increase staff capacity and capabilities to ensure optimal and efficient tax collection operations.

BUILDING BLOCK B

Efficient Expenditure Allocation & Management

Expenditure reforms considered across the baseline and two reform scenarios have the potential to contribute 5.3 percent of GDP to fiscal consolidation by FY27. The major share of these is expected to come from the phasing out of extensive pandemic support in line with the FY23 Budget and constraint in wage bill and other current spending broadly in line with the GoF's forward estimates of the FY22 Revised Budget and FY23 Budget, which are mostly included under the baseline. Implementing these as planned forms the basis for successful expenditure side consolidation. Selected, well-targeted additional measures comprise the transitioning out of sugar sector support, improving the targeting of social assistance and tertiary education support, and improving the quality of capital spending, which are required to achieve fiscal consolidation and growth trajectories under Scenarios 1 and 2. Prudent wage bill and capital investment management as well as sugar industry reforms are discussed respectively in detail in Background Chapters C, D and E while the three supplementary reforms are briefly discussed in Background Chapter A and the two measures supporting better public social spending in more detail in the forthcoming CEQ report and education sector PER for Fiji.

TABLE 6 Overview of Expenditure Reforms

Reform #	Main purpose	Cumulative impacts by FY27 (percent of GDP)		
		Baseline	Scenario 1	Scenario 2
B.1 Controlling the wage bill	To prevent growing upward pressures, partially driven by growing inflation, from materializing	-0.40	-0.80	-1.20
B.2 Prudently managing capital outlays and making public investment more efficient	To moderate growth in capital spending and improve value-for-money of investments	+0.30	+0.30	+0.30
B.3 Transitioning out of sugar sector support	To reduce ineffective subsidies to sugar industry and encourage diversification of the agriculture sector	0.00	-0.20	-0.40*
B.4 Phasing out pandemic support and restraining other current spending	To implement cuts to COVID-19 support and other current spending	-3.50	-4.00	-4.20
SUPPLEMENTARY MEASURE				
Improving the targeting of social protection schemes and introducing additional social assistance spending	To ensure social assistance reaches the poorest households and to compensate low-income households for negative effects from the reversal of VAT zero-ratings on essential items	0.00	0.60	0.60
Reforming the tertiary education scholarship and loan schemes	To better target tertiary education support to low-income households	0.00	-0.30	-0.40
Total net change in revenue in percent of GDP		-3.60	-4.40	-5.30

* This excludes an increase in revenue in the extent of 0.35 percent of GDP from the introduction of an excise tax on sugary products that is captured in revenue measure #A.3 under Building Block A. above.

Expenditure B.1

Controlling the Public Wage Bill

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	Reduce the wage bill relative to GDP to 8.9 percent	FY23-FY24	-0.40
1	Reduce the wage bill relative to GDP to 8.5 percent	FY24	-0.40
2	Further reduce the wage bill relative to GDP to 8.1 percent	FY25	-0.40
Total expenditure impact in percent of GDP			-1.20

Background & analysis

Fiji's public sector wage bill comprises expenditure on established staff (SEG 1), government wage earners (SEG 2), and other pensions, gratuities and compassionate allowances (SEG 11). It constituted around 30 percent of total spending over FY16-FY21. In that period, there were two distinct stages in the trajectory. In the first phase—between FY16 to FY19—the wage bill grew in both nominal and real terms, driven by a combination of growth in wage levels and staffing numbers. In the second phase, when the pandemic hit, the Government acted quickly to address fiscal pressures and contain wage bill growth. As a result, personnel spending in 2021 fell by 8.8 percent compared to 2019 levels. Most cuts were achieved through reductions in the contribution rate for the Fiji National Provident Fund (FNPF) and allowances, with a hiring freeze and some staffing reductions complementing these efforts.

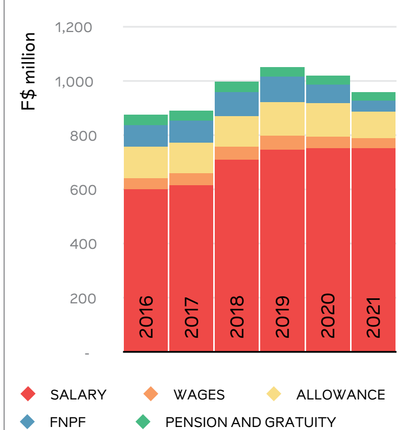
While spending remains lower than global and regional averages, managing the wage bill is becoming increasingly challenging as several factors create upward pressure. The main drivers are the reversal of the FNPF contribution rate reduction, which will add a large share of nominal cuts back onto the wage bill, and growing inflationary pressures, with the unified salary scale last reviewed in 2017. Absent formal agreements to review salaries, pressure will mount to adopt less transparent mechanisms as a back-door means to increase total remuneration, such as through allowances and performance pay funded by unfilled vacancies.

Reform recommendations

Keeping the wage bill on a sustainable growth path without impacting service delivery will require civil servants to increase their productivity. In addition, it will be important to manage upward pressures and limit nominal increases to below GDP growth, reducing personnel spending relative to GDP. In line with Government's FY22 Revised Budget forward estimates, a fiscal target of 8.1 percent of GDP for the medium-term (and subsequently maintained), which would bring spending back to 2016 levels, appears achievable, allowing for FNPF contribution increases and additional nominal growth in FY23-25. More robust data and systems are needed to assess pay and employment practices and make informed decisions on trade-offs involved in managing the wage bill. These should be prioritized in line with information system improvements outlined in the PFM Improvement Program 2020–2025. Lastly, a compensation benchmarking survey and a regular review of wages can contribute to strategic wage bill management, while functional reviews can help identify potential for rationalizing organizational arrangements within and across ministries and agencies.

FIGURE 25

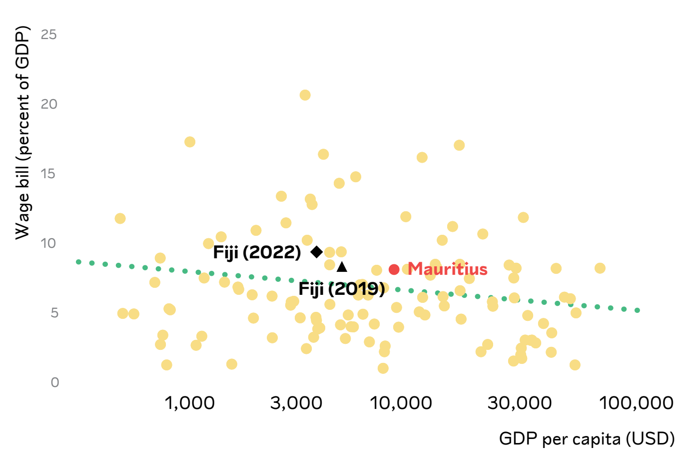
The Public Wage Bill Saw Real Growth Prior To The Pandemic, Followed By Cuts During COVID-19...



Sources: Fiji MoF, World Bank staff estimates

FIGURE 26

...and, While Not Excessively Large, There is Room for Restraint When Compared to Fiji's Peers.



Sources: Fiji MoF, World Bank World Development Indicators.

Expenditure B.2

Prudently Managing Capital Outlays & Making Public Investment More Efficient

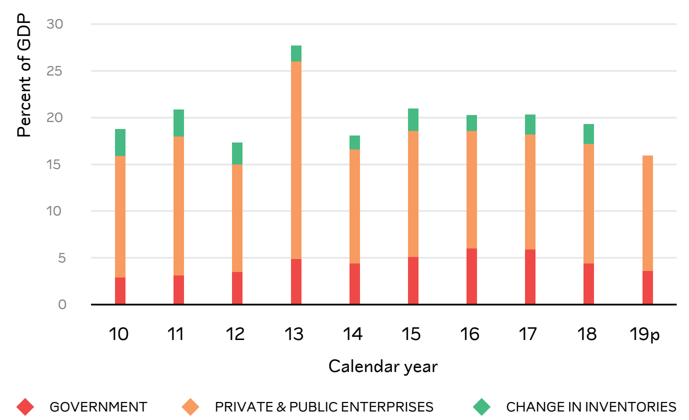
Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	Gradual increase capital outlays to 9.0 percent of GDP	FY24	—
1	No changes to baseline spending, while strengthening PIM	FY23-FY27	—
2	No changes to scenario 1 spending, while strengthening PIM	FY23-FY27	—
Total expenditure impact in percent of GDP			+0.30

Background & analysis

Fiji has a high degree of access to infrastructure and sophistication of its public governance comparative to its regional peers and has historically demonstrated relative maturity in public institutional investment. However, there is substantial scope to improve the quality of spending, with public investment processes poorly rated in the 2019 PEFA assessment (IMF, 2020b). A Public Investment Management Assessment undertaken as part of this PER arrives at similar findings, which are summarized on the next page. The challenges are numerous and include a lack of a strategic planning framework to inform investment priorities, limited coordination between government entities, weak substantive appraisals, and lacking systematic maintenance allocations.

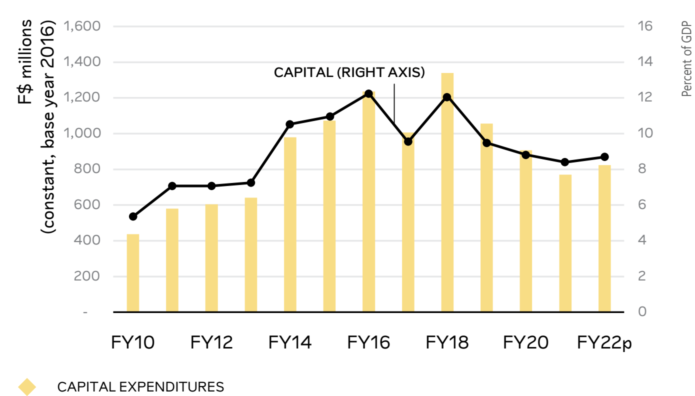
Government capital spending saw a substantial upward shift in FY14, with further real increases up to FY18 (except for a fall in FY17 driven by low budget execution). Capital outlays began declining in FY19 as part of a government-wide fiscal consolidation effort. This was exacerbated by the impacts of the COVID-19 pandemic, which saw substantial cuts in capital spending to 8.4 percent of GDP in FY21 before a slight recovery to 8.7 percent of GDP in FY22. In view of significant investment needs to improve the delivery of social and economic services, and increase resilience against climate change, there appears to be no further room for consolidation. Instead, there is a need for gradually increasing spending that is well-targeted and high quality.

FIGURE 27 Following a Period of Growing Public Investment, Consolidation Affected Capital Outlays in FY19...



Source: Reserve Bank of Fiji.

FIGURE 28 ...With Further Cuts in Real Terms and Relative to GDP in FY20 FY21 that Should Be Reversed Going Forward.



Note: Capital classification in FMIS includes multiple subsidies and transfers, overstating capital spending.
Sources: Fiji MoF FMIS, World Bank estimates.

Reform pathways

Further cuts to capital spending are not recommended, but spending increases need to be gradual and should stabilize at around 9 percent of GDP in the medium term until public debt is reduced and additional fiscal space created that would allow a further increase to around 10 percent of GDP in the long-run. In parallel, ongoing reforms to improve the planning, appraisal, selection, design, and implementation of capital projects (e.g., through the ongoing development of a National Infrastructure Investment Plan and Public Sector Investment Program guidelines and an accompanying user manual) should be prioritized. These should support strategic investment decisions (including to address climate and disaster risks); standardize project appraisal methodologies; consider realistic maintenance funding needs; introduce selection processes using objective technical, economic, financial and environmental criteria; and ensure budgetary coherence (including through multi-year budgeting), among others. As discussed in Section 3.3, this can help partially offset adverse impacts of temporarily limiting capital spending.

TABLE 7 Findings from the Public Investment Management Assessment Show Substantial Improvement Potential

Indicator	Assessment		Reform recommendations	
	Institutional Strength	Effectiveness	Priority	Activities
		A. PLANNING		
Fiscal targets and rules	Medium: Limits on debt and a MTFF is prepared, however no permanent fiscal rule exists	Medium: Govt targets debt reductions but MTFF doesn't prioritize capital needs	Medium	Provide greater transparency around medium to long term priorities for capital expenditure, consistent with MTFF projections
National and Sectoral Planning: Are investment allocation decisions based on sectoral and inter-sectoral strategies?	Low: Plans do not identify priority projects and are not costed	Low: Plans not driving investments.	High	Develop objective criteria to maintain a prioritized and costed database of high-priority infrastructure investment projects aligned with measurable national development outputs and outcomes targets. Publish investment plans, standards and targets. MOF activities such as the development of the PSIP guideline and the FIJI national infrastructure investment plans should address these recommendations and mainstream these improvements into MOF current processes.
Coordination between Entities: Is there effective coordination of the investment plans of central and other government entities?	Medium: Major SOE capital spending and contingent liabilities are published alongside central government investments	Low: Limited integration of SOE and subnational government capital budgeting, with many SOEs	Low	Where appropriate, consider further integration of SOEs and SNGs investment plans with central Government, aligned to national and sector plans, to improve the overall coherence of public sector infrastructure investments
Project Appraisal: Are project proposals subject to systematic project appraisal?	Low: No systematic project appraisal	Low: No standard methodology or central support for appraising projects, except for donors	High	Develop a standard methodology and central support for project appraisal including rigorous technical, economic, and financial analysis, and selected results of this analysis are published or undergo independent external review.
Alternative Infrastructure Financing: Is there a favorable climate for the private sector, PPPs & PCs to finance infrastructure?	Medium: Established laws and institutions, including comprehensive consumer law	Medium: Limited competition in some markets, PPP regulatory arrangements incomplete but being worked on	Medium	Continue to follow through on in-flight reforms and initiatives to reform enabling laws and institutions, raise awareness, and improve the attractiveness of key infrastructure sectors to take advantage of growing interest
		B. ALLOCATION		
Multi-Year Budgeting: Does the Government prepare medium-term capital spending projections on a total cost basis?	Medium: Projections of capital spending disaggregated by ministry or sector are published over three years.	Medium: Select major projects have budget allocation published, but total cost is not consistently reported	Medium	Provide greater transparency for the pipeline of major capital projects, including total construction costs and associated recurrent costs in medium-term and long-term projections
Budget Comprehensiveness and Unity: To what extent is capital spending & related recurrent spending undertaken through the budget process?	Medium: Most capital projects including donors, but not all SOE projects	Low: Recurrent and capital expenditure by project is not identifiable in the budget document	Medium	Provide greater transparency for the pipeline of major capital projects, including total construction costs and associated recurrent costs in medium-term and long-term projections
Budgeting for Investment: Are investment projects protected during budget implementation?	Medium: Project costs are allocated funding through the annual budget process with limitations to virements	Medium: Post COVID –19 budgets have prioritized funding for underway projects	Low	Continue to monitor the effectiveness of year-to-year budget allocations for major capital projects, given the ongoing challenges associated with COVID-19
Maintenance Funding: Is maintenance receiving adequate funding?	Low: No standard methodology for maintenance, not systematically identified in budgets	Low: Minimal planning or prioritization of maintenance to prolong the life of assets	High	Establish and promote the use of a standard methodology for determining capital and routine maintenance projects. Include maintenance costs national or sectoral plan. Promote routine maintenance and capital maintenance to be systematically identified in the budget and reported as instructed by the NAMF. Review NAMF implementation.
Project Selection: Are there institutions and procedures in place to guide project selection?	Low: No published standard criteria for selection	Low: Selection process undocumented. No evidence of guiding project selection.	High	Establish processes and objective criteria for project selection, focusing on robust technical, economic, financial and environmental assessments.

MOF = Ministry of Finance, Strategic Planning, National Development & Statistics; MTFF = medium-term fiscal framework; NAMF = National Asset Management Framework; PPP = public-private partnership; PSIP = Public Sector Investment Program; SOE = state-owned enterprise.
Source: World Bank staff assessment.

Transitioning Out of Sugar Sector Support

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	None		
1	Partially phase out sugar sector subsidies	FY23-FY25	-0.40
	Temporary compensate farmers and increase targeted investment in agriculture sector	FY23-FY26	+0.20
			Total: -0.20
2	Fully phase out remaining sugar sector subsidies*	FY25-FY26	-0.20
Total expenditure impact in percent of GDP			-0.40

* This should be complemented by the introduction of an excise tax on sugary products in the extent of 0.35 percent of GDP that is captured under Revenue #A.3 above.

Background & analysis

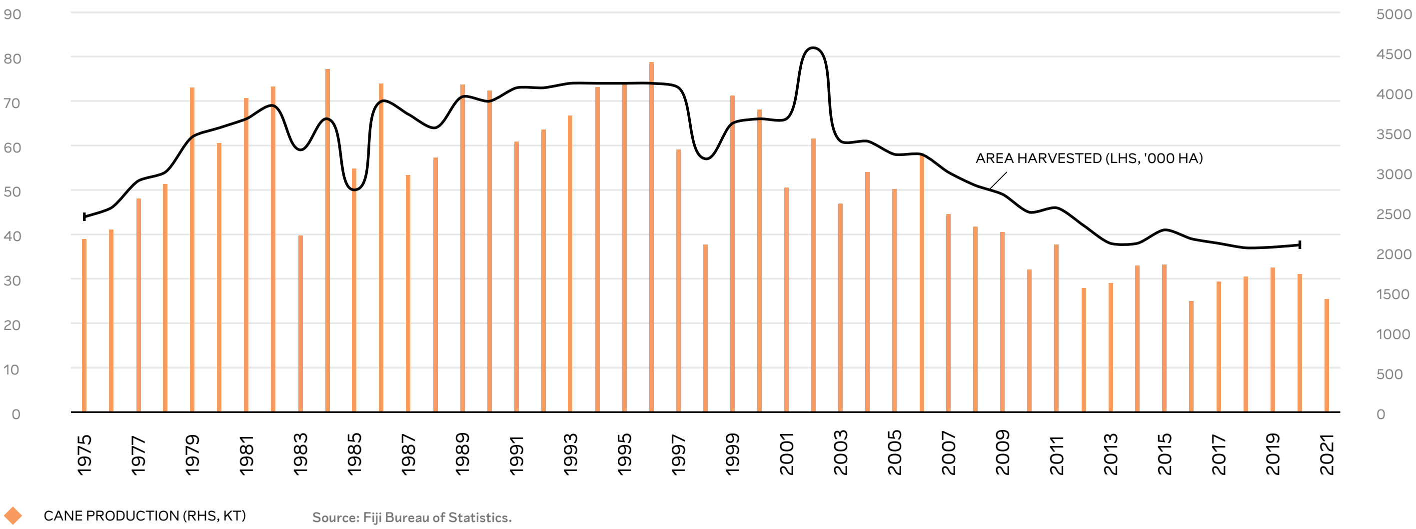
Sugar production in Fiji has historically been a major agricultural activity, and source of income and export earnings. However, the industry has been in long-term decline, exacerbated by the phasing out of preferential access to the high-priced, subsidized sugar market of the European Union. The GoF initially responded by injecting significant funds into the industry from 2011, but this failed to stem the decline despite a temporary rebound in production levels between 2011 and 2015. The GoF expanded support for the sugar industry in 2018 by guaranteeing a minimum price through the Sugar Stabilization Fund. The total cost of the subsidy equated to F$116 million per year between 2018-21, equivalent to 10 percent of agricultural value added, 5 percent of government revenues, and 1 percent of GDP. Around 70 percent of the costs are directly covered by the Government, with consumers absorbing the remainder through higher prices (effectively a consumer tax), although the proceeds go to producers rather than the Government.

The subsidies are regressive, benefiting the largest and wealthiest sugar producers relatively more because the benefits are directly proportional to holding size. Moreover, they have primarily benefited inefficient providers without profitable alternatives and increased environmental pollution. Finally, the expanded support has had little impact on sugar production and the sector continued to decline in importance, falling from 11 percent of GDP in 1995 to 1 percent of GDP by 2021. Fiji's sugar production levels are now one-third of the peak in 1996 and yields per hectare have fallen from 94 percent of the global average in the 1980s to barely 60 percent in 2021.

The case for reforming Fiji's sugar support policy and restructuring its rural sector is strong. The urgency for reform has been increasing over the years as the Sugar Stabilization Fund policy has proven costly, inefficient, inequitable and, ultimately, largely ineffective. The export price is forecast to remain low for the foreseeable future, reliance on research-driven productivity growth has been insufficient to prevent a decline in Fiji sugar's international competitiveness, and the costs of subsidies is growing, contributing to the country's growing fiscal deficits and debt. There are ways to get much better value for money from the Government revenue that is currently supporting sugar producers and more efficient and targeted ways to support rural households. It is high time, therefore, to take a realistic review of the sector's (long-term) prospects and re-assess the case and the viability of GoF's policies to support the sector.

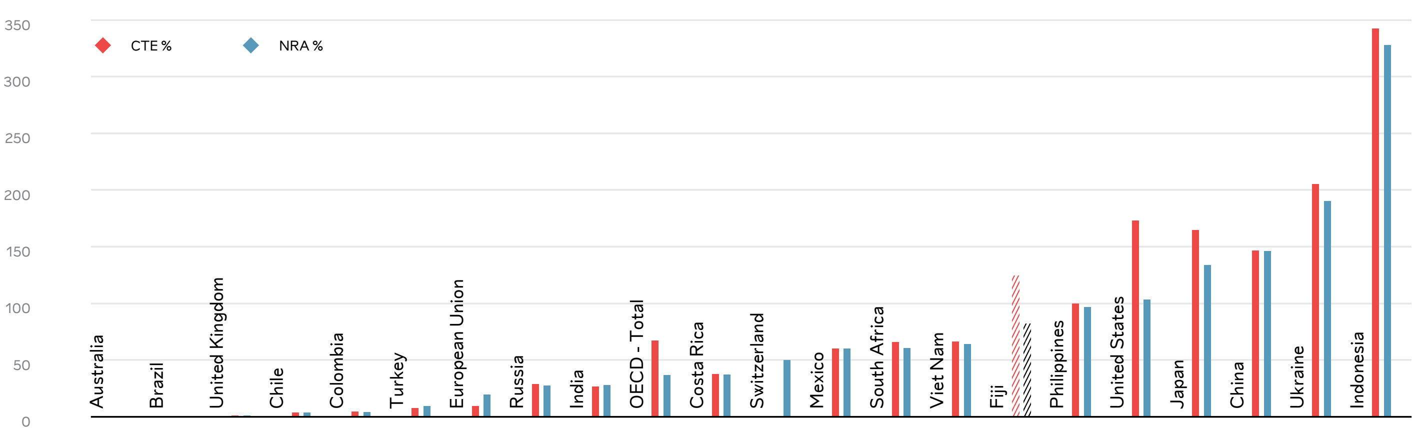
> **"There are ways to get much better value for money from the Government revenue that is currently supporting sugar producers and more efficient and targeted ways to support rural households"**

FIGURE 29 The Production of Sugar Cane and Harvested Area Have Been in Strong Decline in Fiji Over the Past Decade...



Source: Fiji Bureau of Statistics.

FIGURE 30 ...Despite High Nominal Rates Of Assistance (NRA) and Consumer Tax Equivalents (CTE) of Sugar Policies.



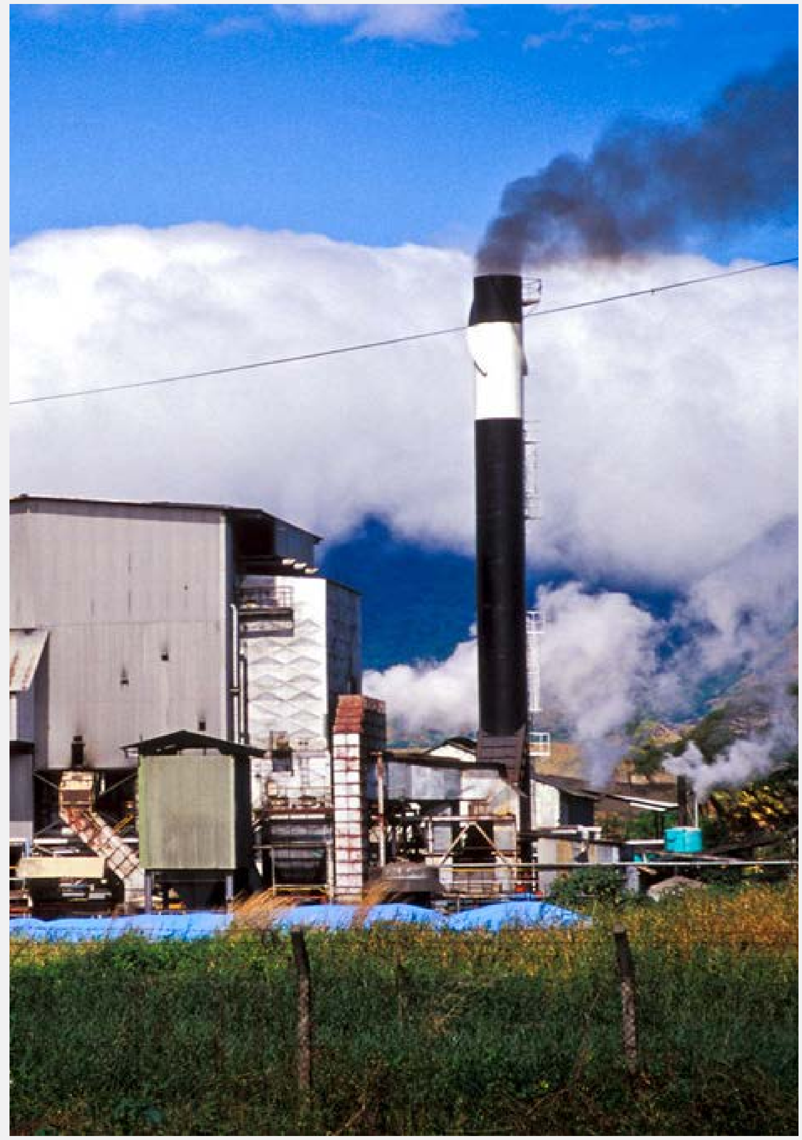
Source: World Bank staff estimates for 2018-20 based on OECD and Government of Fiji data.

Reform recommendations

The GoF could reform its sugar industry support by incentivizing sugar cane growers to diversify into other crops and activities, announcing a clear roadmap for reform, and providing temporary industry transition support. The most efficient way to improve incentives for sugar cane growers to diversify is to phase out the current assistance to cane production. This will be politically difficult and face many challenges. However, the political difficulty will only increase the longer that support remains in place and the larger it becomes. These political difficulties were partly overcome in other countries, such as Australia, by announcing a reform roadmap well in advance of the actual implementation date and by compensating the key losers from the reform for several years during an adjustment period. Elements of a reform roadmap and industry support package could include:

1. Replacing the current arrangement for setting the wholesale price of sugar with an excise tax on all sugar-rich processed foods and beverages, both domestic and imported
2. Removing the subsidies on fertilizer and weedicides for cane growers
3. Removing the monopoly provided to the Fiji Sugar Corporation by making its activities contestable to improve its incentive to boost productivity, and
4. Compensating existing sugar cane growers with a time-bound series of government payments based on their past production (to de-couple it from current production), which could be generous initially but be gradually phased out by 2026.

These suggested reforms were reflected in the fiscal consolidation scenarios. The baseline does not include any reform, consistent with the authorities' forward estimates in the FY22 Revised Budget that continue current subsidy allocations to the sugar industry.[11] Scenario 1 assumes the partial phasing out of sugar sector subsidies in the extent of 0.4 percent of GDP over FY23-FY24. This is partially offset by temporary compensation payments to farmers and targeted investments in the transition of the agriculture sector over FY23-FY26 (such as investment in agriculture research & development), resulting in an expected net consolidation contribution of 0.2 percent of GDP. Scenario 2 incorporates the reform recommendations fully by phasing out remaining sugar sector subsidies over the same period and introducing an excise tax on sugar products (see measure #A.3 above), resulting in a net reduction of spending by 0.4 precentage points of GDP.



11 The FY23 Budget includes a cut in sugar sector subsidies from the FY22 Revised Budget allocation of F$82 million to F$45 million, broadly in line with the recommended reduction under Scenario 1. However, supplementary budgets and actual outturns have regularly surpassed original budgets (e.g., the FY22 Budget's original allocation was F$71 million, i.e., F$11 million less than the FY22 Revised Budget, while the actual outturn in FY20 was F$111 million compared to an original budget allocation of F$61 million), highlighting the need for follow-through on cuts introduced in the FY23 Budget.

Expenditure B.4

Phasing Out Pandemic Support & Restraining Current Spending

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	Phase out pandemic support	FY23-FY24	-2.70
	Restrain non-salary recurrent spending in line with government plans	FY24-FY26	-0.80
			Total: -0.20
1	Further restrain non-salary recurrent spending	FY24-FY26	-0.50
2	Further restrain non-salary recurrent spending	FY26-FY27	-0.20
Total expenditure impact in percent of GDP			-4.20

Pandemic support & other current spending

In response to the impacts of the COVID-19 pandemic, the GoF introduced several expenditure-side support programs amounting to an estimated 2.7 percent of GDP. This included a new unemployment benefit scheme, support to infected and quarantined workers (including in the informal sector), and a concessional loan scheme for micro, small and medium-size enterprises, among others. The phasing out of these support programs as pandemic impacts subside constitutes the single largest recommended consolidation measure. The most recent national budgets have further set out restraint in non-salary recurrent spending, including for expenses on travel, communication, and selected current transfers. The continued implementation of both measures broadly in line with the forward estimates of the FY22 Revised Budget and FY23 Budget is critical and provides the foundation for a sustainable fiscal consolidation path.

Supplementary Expenditure Measure

Improving Social Protection Schemes

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	None		-
1	Compensate low-income households for negative effects from the reversal of VAT zero-ratings on essential items	FY24-FY25	+0.60
	Improve targeting of social assistance programs	FY23-FY27	-
2	No changes to scenario 1 spending, while strengthening social assistance targeting	FY23-FY27	-
Total expenditure impact in percent of GDP			+0.60

Social assistance

Despite direct social assistance transfers in Fiji being overall progressive, a significant share reaches wealthier households, according to the parallel CEQ analysis. About 36 percent of households in the top 60 percent of the market income distribution have been receiving direct transfers, accounting for almost half of total spending on direct transfers. For example, 10 percent of the benefits from the Poverty Benefit Scheme went to households in the richest quintile. Similarly, a large share of spending on the Social Pension Scheme is concentrated among households in the three richest quintiles (57 percent), despite this program being targeted at individuals with no access to any other form of pension. Reforms to improve the targeting of social assistance and rebalance spending toward more effective social assistance programs could (temporarily) boost growth given higher consumption spending of lower income households and/or lead to fiscal savings without cutting benefits to the poor. Using direct transfers to compensate low-income households for negative effects from the reversal of VAT zero-ratings on essential items is an example for such a reform, reducing fiscal costs compared to the non-targeted VAT zero-ratings.

Supplementary Expenditure Measure

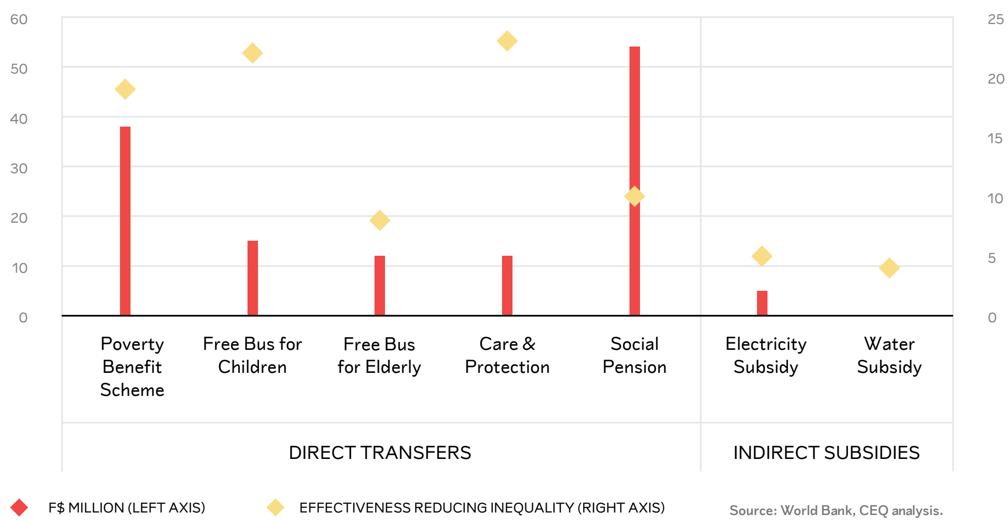
Reforming Tertiary Education Financing

Scenario	Key consolidation recommendations	Timeline	Est. impact (% of GDP)
Baseline	None		-
1	Improve targeting of tertiary education financing	FY24-FY26	-0.30
2	Further improve targeting of tertiary education financing	FY26-FY27	-0.10
Total expenditure impact in percent of GDP			-0.40

Tertiary education financing

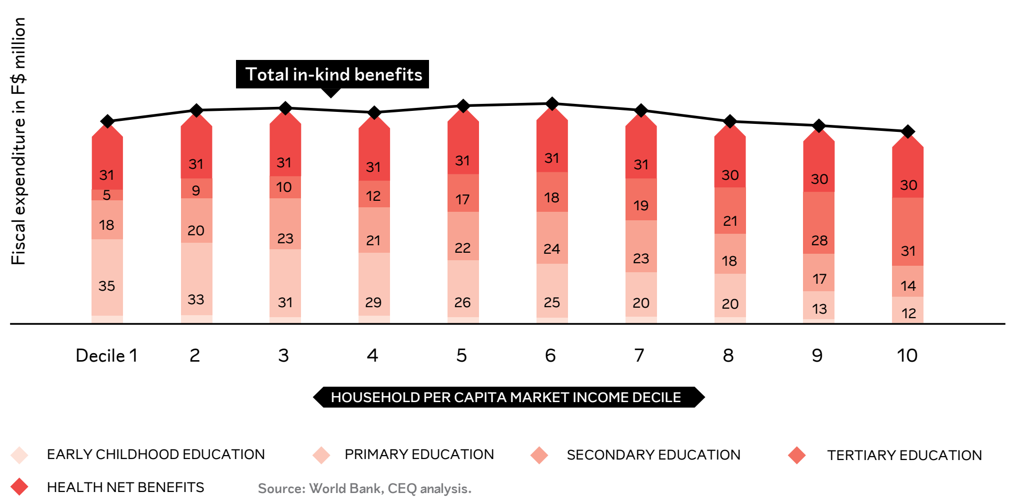
A parallel education sector PER found that Fiji's tertiary education spending has been high, both absolute and relative to other education levels, risking to crowd out resources for lower education levels. In 2019, relative spending saw a measurable shift from tertiary to early childhood and primary education, but tertiary education continued to dominate spending in comparison with countries at Fiji's income level. The analysis shows that particularly Fiji's substantial tertiary education scholarship and loan schemes offer potential for fiscal savings through improved targeting. While interest rates for student loans are progressive with growing household income, a considerable discount (up to 50 percent of the loan amount) for early repayment favors richer households whose children are more likely to enroll in tertiary education in the first place. As a result, benefit incidence analysis as part of a parallel CEQ exercise shows that net benefits from tertiary education spending increase across household income deciles. The government has taken first steps to improve the allocation of financial support for tertiary education, but room for better targeting remains.

FIGURE 31 Budget and Effectiveness of Main Social Assistance Programs



Source: World Bank, CEQ analysis.

FIGURE 32 Distribution of In-Kind Benefits of Education and Health Spending



Source: World Bank, CEQ analysis.

Effective Liabilities & Fiscal Risk Management

Liabilities C.1

Continuing Prudent Borrowing & Strong Debt Management

Background, analysis, and reform recommendations

Fiji substantially strengthened debt management and reporting over the past years. As a result, the 2019 PEFA assessment assigned an overall score of B for debt management (on a scale from A=best to D), which would have since improved to a score of A following the publishing of a medium-term debt management strategy (MTDS) covering FY21-FY23 (IMF, 2020b). This assessment is confirmed by the Debt Reporting Heat Map 2021 of the World Bank's Debt Transparency where only information on recent contracted loans remains a gap, after the government published for the first time an annual borrowing plan for FY22 and a second plan for FY23.. These improvements were supported by changes to the legal and policy framework, including an amendment of the Financial Management Act (Amendment) 2021 that mandates the preparation of an MTDS and a Liability Management Operations Policy. The latter enables the Government to pursue active debt management operations such as buybacks, switches and callbacks, with the primary objectives of enhancing market liquidity and mitigating refinancing risk consistent with the MTDS. Going forward, the focus should be on continued compliance with established good practices to avoid backsliding.

The pandemic-induced substantial increases in nominal debt levels were contracted on favorable domestic terms and on highly concessional terms in the case of the increasing share of external borrowing. As a result of this, cost and risk indicators show positive trends, except for the increasing foreign exchange risk from the larger share of external borrowing. Further, Fiji had participated in the Debt Service Suspension Initiative. Still, interest payments are projected to increase from an average of 2.7 percent of GDP over FY15-FY19 to 4 percent of GDP over FY23-FY27. This highlights the importance of fiscal consolidation and prudent, least-cost borrowing to limit projected increases in interest payments and avoid crowding out of other recurrent spending and capital investment.

Liabilities C.2

Continuing Monitoring & Gradually Reducing Contingent Liabilities

Background, analysis, and reform recommendations

The authorities monitor contingent liabilities and have put into place policies to minimize the associated risks. The government introduced a Government Guarantee Policy in 2019 and an On-Lending Policy in 2020 for Government entities, including public enterprises. Further actions taken include applying commission fees to guaranteed debt, recovering funds, and closely monitoring guaranteed entities to ensure that fiscal risks are identified and mitigated. To enhance the performance of (guarantee-receiving) state-owned enterprises, the government passed the Public Enterprises Act 2019 and corresponding regulations, which establish a harmonized public enterprise framework and a non-commercial obligation regime, assign clear duties to the responsible minister, and strengthen the director appointment process and director's duties and responsibilities. Implementation guidelines for public-private partnerships and a privatization policy complete the picture. Going forward, compliance with established legal and policy frameworks as well as monitoring practices is critical to limit fiscal risks from contingent liabilities.

Contingent liabilities grew by almost 7 percentage points of GDP from July 2019 to 17.6 percent of GDP by July 2021, with a large share stemming from guarantees to Fiji Airways. While this was largely driven by pandemic impacts, contingent liabilities had already been growing in the years prior to COVID-19 and pose significant fiscal risks to Fiji. Particularly Government guarantees and lending to the agricultural sector are considered high risk, with Fiji Sugar Corporation Limited having received additional guarantees in the past two years, despite the corporation's unsustainable business model (see Chapter E) and a guarantee call of FJ$25.5 million (0.3 percent of GDP) for its bonds in FY21. Further guarantees and loans should be avoided and existing liabilities gradually reduced going forward.

BUILDING BLOCK D

Evidence-based Fiscal Policy-Making

Foundation D.1

Effective Information Systems & Data Collection

Background & analysis

The extraction of data in a readily-useable format from several of the main government information systems has been cumbersome, taking substantial government staff time and hindering analysis across multiple components of the PER. Particularly affected was analysis using financial data from the Government's financial management information system (FMIS) as well as data for the wage bill and human resource management (Chapter C) and more detailed information on the revenue system (Chapter B). A similar conclusion is being drawn in the ongoing education sector PER where limited data availability equally hinders analysis. Further, data quality concerns stem from issues relating to data classification, consistency in recording, and a lack of integration of information systems; the latter leading to inconsistent data across systems. Regarding the FMIS, significant classification issues relate to the functional and economic classifications as well as consistency in recording transactions. While this risks undermining the usefulness of exercises such as this PER, it more importantly impedes evidence-based decision-making of policy-makers, managers and technical staff across government entities.

Reform recommendations

The government's Public Financial Management Improvement Plan (PFMIP) 2020–2025 sets out multiple priorities and activities that help address these issues. Notably, the plan foresees the review of the Chart of Accounts, with changes to be translated into the FMIS. In regard to information systems, it includes the optimization of functionality of the existing FMIS, the procurement of a reporting and a budget module as well as the development of a long-term plan for FMIS replacement. It further lists the interfacing of the payroll system with the FMIS and the HRMIS. Implementing these changes will be critical to provide decision-makers and technical staff with readily available, consistent data to inform analysis and decision-making. The authorities have expressed the intention to fast-track these system improvements, which should be prioritized by the new Government in 2023.

Foundation D.2

Strategic Fiscal Planning & Budget

Background & analysis

Fiji exhibits weaknesses in strategic fiscal planning and budgeting, which is a foundation for fiscal consolidation. The PEFA assessment undertaken in 2019 assigns weak scores in macroeconomic and fiscal forecasting (C+ on a scale from A=best to D), in fiscal strategy (C+) and medium-term perspective in expenditure budgeting (D+), with the latter comprising scores of D for medium-term expenditure ceilings, the alignment of strategic plans and medium-term budgets, and consistency of budgets with previous year's estimates (IMF, 2020b). As a result, there have been large discrepancies between budgets and final outturns for both revenue and expenditure at aggregate and composition levels. In response, the Government introduced legal requirements to prepare a fiscal (and debt management) strategy; rolled out an internal medium-term expenditure framework; and issued a new pre-election economic and fiscal update in May 2022.

Reform recommendations

The government's PFMIP 2020–2025 outlines activities to address the identified issues further. The plan includes the preparation, tabling in parliament, and publishing of a medium-term fiscal strategy as well as the strengthening of the methodology for determining revenue estimates. The latter comprises the alignment of revenue targets to the fiscal strategy and the review of revenue forecast by a revenue Technical Committee comprising MOF, FRCS and the Reserve Bank of Fiji. Strengthening fiscal planning is also critical for climate and disaster resilience. Further, the IMF recommended in its 2021 Article IV staff report establishing a financing plan for climate adaptation and integrating it with the medium-term macro-fiscal framework. This can build, among others, on the government's Climate Vulnerability Assessment from 2017 and the country's National Adaptation Plan from 2018. The new Government should prioritize the implementation of these reforms in 2023 and further strengthen established fiscal planning practices.

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Annex

	CY16	CY17	CY18	CY19	CY20	CY21	CY22 (p)
Real GDP growth (% change)	2.4	5.4	3.8	-0.6	-17.0	-5.1	15.1
Inflation (year-on-year)	3.9	2.8	4.8	-0.9	-2.8	3.0	5.0

	CY16	CY17	CY18	CY19	CY20	CY21	CY22 (p)
			F$ MILLION				
Tax revenue	2,427	2,579	2,832	2,820	2,194	1,413	1,692
Non-tax revenue	267	228	348	295	237	228	259
Asset sales	188	2	1	5	211	210	2
Grants	22	19	49	42	68	284	233
Total revenue	2,905	2,829	3,231	3,162	2,710	2,135	2,185
Recurrent expenditure	1,992	2,036	2,361	2,485	2,408	2,415	2,516
Personnel	876	889	996	1,052	1,020	959	930
Goods & services	238	247	265	277	276	255	252
Current Transfers	510	520	682	706	667	748	878
Other	140	104	126	123	88	83	86
Interest	229	277	292	327	357	370	370
Capital expenditure	1,236	1,024	1,381	1,115	944	775	869
Total expenditure	3,228	3,060	3,741	3,600	3,353	3,190	3,385
Primary balance	-95	45	-219	-112	-286	-685	-829
Fiscal balance	-324	-232	-511	-439	-643	-1055	-1199
Nominal GDP	10,084	10,746	11,399	11,758	10,703	9,234	9,998
GDP deflator	100.0	101.7	103.1	105.5	104.2	100.6	105.4
			PERCENT OF GDP				
Tax revenue	24.1	24.0	24.8	24.0	20.5	15.3	16.9
Non-tax revenue	2.7	2.1	3.1	2.5	2.2	2.5	2.6
Asset sales	1.9	0.0	0.0	0.0	2.0	2.3	0.0
Grants	0.2	0.2	0.4	0.4	0.6	3.1	2.3
Total revenue	28.8	26.3	28.3	26.9	25.3	23.1	21.9
Recurrent expenditure	19.8	18.9	20.7	21.1	22.5	26.2	25.2
Personnel	8.7	8.3	8.7	8.9	9.5	10.4	9.3
Goods & services	2.4	2.3	2.3	2.4	2.6	2.8	2.5
Current Transfers	5.1	4.8	6.0	6.0	6.2	8.1	8.8
Other	1.4	1.0	1.1	1.0	0.8	0.9	0.9
Interest	2.3	2.6	2.6	2.8	3.3	4.0	3.7
Capital expenditure	12.3	9.5	12.1	9.5	8.8	8.4	8.7
Total expenditure	32.0	28.5	32.8	30.6	31.3	34.5	33.9
Primary balance	-0.9	0.4	-1.9	-1.0	-2.7	-7.4	-8.3
Fiscal balance	-3.2	-2.2	-4.5	-3.7	-6.0	-11.4	-12.0

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