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Foreign Direct Investment in the Pacific – A Study of Fiji

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Abstract: The South Pacific region has been lagging behind in growth in comparison to similarly placed island countries globally. This paper undertakes a descriptive study on the contributing crucial determinants of foreign direct investment (FDI) inflows into Fiji using secondary data in making critical data analysis. Fiji has the distinction of being a leading country in the region with skilled labor. After the impact of the various political instability, the Fijian economy seemed to be have made a sustained recovery ever since. However, the recovery was not as great as forecasted by the Reserve Bank of Fiji. A stable political climate is important for Fiji's future economic performance and sustained economic growth in the long run with macroeconomic stability coupled with enhanced business environment with governments continued structural reforms and economic policy, with emphasis on exports. The findings strongly suggest that Foreign Direct Investment is growth enhancing in Fiji yet the impact of FDI depends on the threshold levels of absorptive capacities measured by the levels of human capital, infrastructure, and technology. In order to effectively sustain a robust economy, the government needs to have a clear understanding of the roles and responsibilities of all stakeholders in the community.
Keywords: Foreign Direct Investment, South Pacific, Fiji, Economic Growth, Human Capital

INTRODUCTION

Direct foreign investment in recent times has increasingly become one of the main elements of liberalization of the world economy. Direct foreign investment is considered as a potential facilitator for economic development through dissemination of technologies, linkages with domestic firms, enhanced production technique and network, and access to overseas markets. In a survey by Jayaraman and Choong, [4]observed that although traditionally FDI inflows were primarily those seeking to exploit natural resources, since the late 1980s, there had been an increasing trend in FDI inflows in service and manufacturing sectors. It is now referred as non-asset activities by foreign investors by way of licensing, joint ventures and research and development [1]. In early 20th century, the most notable investment in Fiji was in the sugar industry, but later, in the 1970s and onwards, the hotel industry and the development of resorts and hotels received greater attention from overseas investors [4]. The FDI inflows (as a percentage of GDP) into Fiji have been on the rise, despite fluctuations during the coup years of 1987, 2000 and 2006.

Fiji has been one of the main aid recipients since her independence from 1970 however foreign investment has been low when compared to aid inflows. As the aid inflows decline and attention changed towards specific growth-enhancing projects. Fiji is emphasizing now on direct foreign investment and embarking on a new era that would like to see positive changes in the business climate in Fiji for foreign investors.

BRIEF BACKGROUND OF FIJIAN ECONOMY

Fiji Islands is categorized as an upper middle-income country. Its per capita income is USD4375 with a population growth rate of 1 percent. The growth rate is regarded low in a dispersed economy with its high cost of living and comparatively endowed with few natural resources and is also an aid-dependent country [4]. Hence economic growth is critical to enhancing social and economic development. The country has forest, mineral, and fish resources. Tourism is a leading growth sector. The manufacturing sector employs about 26,000 workers and is one of Fiji's growing sectors, sugar, garments, food processing, beverages (including mineral water), and wood-based industries are significant. Sugar is the mainstay of the rural economy, with the industry employing about 3,000 people, while another 200,000 depend on it for their livelihoods. The economy has a strong service and light-industrial component; activities range from boatbuilding to brewing and paint manufacture.

Fiji's growth performance has been adversely affected by the country's vulnerability to both internal and external shocks. These include political unrest (four coups since 1987), natural disasters (cyclones and floods), global oil and food price shocks, and global financial and economic crises. Since its independence in 1970, Fiji has registered steady improvements in several areas of social development, including life expectancy at birth, food security, and access to safe drinking water and sanitation. Although the country has strong social indicators, Fiji's human development ranking dropped from 66th place in 1998 (out of 174 countries) to 100th (out of 187 countries) in 2011. Fiji recorded the highest value and ranking in Human Development Index (HDI) among the Pacific island countries in the 1990s but fell behind Tonga and Samoa in the Human Development Index (HDI) rankings by the mid-2000s [5]. Fiji's selected economic indicators are provided in Table one.

Table 1: Fiji Islands Economic Indicators

Land area (Sq.km.'000)	18,270
Population numbers in '000 (2013)	881
GDP per capita (US$)	4,375
Aid percent of GDP (2013)	2.4
Human development ranking (2013)	88/187
Average GDP growth rate (%) (1980 – 13)	1.8
Average Inflation (%) (2009-13)	4.8
Government fiscal balance (% of GDP) (2009-13)	-7.4
Trade balance (% of GDP) (2009-13)	-6.0

Source: World Development Indicators 2014.

Foreign Direct Investment Trends in the Fiji Islands

Operational rigidities in land lease issues, the system of bureaucracy, and political instability have been obstacles to various investment initiatives. Despite this, Australia, New Zealand, United Kingdom and China have positively influenced FDI inflows in Fiji together with some bilateral interests shown by Korea, Japan, Malaysia, and Singapore in recent years. Fiji has reserved some the activities for Fijians in which there are restrictions on Foreign Direct Investment. Some restricted activities with conditions which must be met by foreign investors who wish to pursue them. These restrictions, rather the prohibitions and conditionality's, are conceived and put in place, as effectively as possible with a view to promoting employment, incomes of people and revenues of government. These ends are a responsibility of a popular democratic government. If there are no restrictions with regard to the arrival of capital, equipment, manpower and export of raw materials (like coal, wood, minerals etc.), there may be no encouragement to manpower training and incomes of people may be in jeopardy. In effect restrictions with regard to FDI and encouragement will be a dynamic, planned administrative/legal policy.

Since independence Fiji have been assisted by official development assistance (ODA) in terms of bilateral grants from international donors which provided substantial budgetary support. The annual aid flows were used for both financing recurrent expenditures of running the government as well as enabling t government to undertake capacity enhancing public investments.

Table 2: FDI Inflow and Aid in Fiji: 2005 - 2013

Year FDI	**US$ Millions**	**FDI Percent of GDP**	**Aid Percent of GDP**
2005- 2009	279.45	8.55	1.83
2010	356.73	11.06	2.37
2011	416.72	11.10	2.10
2012	267.15	6.62	2.66
2013	272.08	6.75	2.41

Source: World Bank, World Development Indicators 2014.

Economic Analysis post-2006

The immediate economic effect of the 2006 coup was resonant of political instability and a crisis of confidence. Two months after the coup, the Reserve Bank of Fiji noted that around 3000 jobs had been lost. Prasad [2] has argued that the basic cause of the sluggish economic recovery and low growth from 2007 to 2009 was mainly tied to the perceived political instability and uncertain economic policies. Some of the factors attributed to the negative and low growth could be due to a spike in food and fuel prices in 2008 and the global economic crisis in 2009, however, the major contributor has been the static, as well as the dynamic, consequences of the 2006 coup.

Fiji's financial and capital markets are undeveloped and domestic investment activities are small, hence capital inflows have not been significant. Furthermore, there are significant institutional and structural rigidities in factor markets as well. The economic recovery to be sustainable, Fiji has to restore macroeconomic confidence, structural reforms, and policy reorientation. The government acknowledges the fact of declining aid flow, hence the emphasis on FDI inflows, which is the most constructive of all flows for the emerging markets like Fiji.

OBJECTIVES

The aim of this study is to examine the determinants of Foreign Direct Investment in Fiji and evaluate the impact on the domestic investment. This aim will be researched by the following objectives:

- to investigate what factors significantly affect foreign direct investment location distribution in Fiji;
- to investigate the factors that determine foreign direct investment sector investment choice; and
- to investigate whether or not increasing foreign direct investment inflows have any displacement effect in the domestic market.

METHODOLOGY

This research study employed secondary source data to address all research objectives in depth. There are no disaggregated data on FDI in different sectors; however, it is known that a considerable proportion of FDI inflows have been in the tourism, manufacturing and service industries. Various articles from different writers are used on how foreign direct investment affects the host country.

LITERATURE REVIEW

Dunning [10] explained ownership, location and internationalization as the main determinant of FDI and several other empirical studies have examined various other determinants of FDI such as skilled labor, trade and investment policy factors. However, the literature on determinants of FDI inflow on developing Island economies is limited. There are a number of other factors affecting FDI inflow: the market size of host economy, labor force, the degree of trade openness, distance, relative economic development, tax rates, economic stability, and infrastructure development. Various other scholars claim that FDI inflow is reliant on infrastructure growth in Africa. They suggest that economies with less political crisis and sound physical infrastructure attract high levels of FDI. Jayaraman T K, and Choong Chee-Keong [4] in their article entitled “Foreign direct investment in the South Pacific Island Countries: a case study of Fiji” have highlighted the factors attracting FDI. In this paper, an empirical study is undertaken that establishes that the rate of growth, market size, openness policy and real exchange rate are crucial determinants of foreign direct investment (FDI) inflows into Fiji. The analysis confirms the hypothesis that the effectiveness of macroeconomic policies is crucial in creating an economic environment which is attractive to FDI. In turn, FDI promotes economic growth via the ‘catchup’ process in technology and through knowledge transfer. They conclude that Fiji should adopt an appropriate policy environment for encouraging the growth inducing FDI inflows. Schneider Friedrich and Frey B [6] in their article “Economic and Political Determinants of Foreign Direct Investment” explained the flow of FDI in 80 less developed countries using econometric analysis. Bilateral and multilateral aids have a stimulating effect on the flow of FDI, however, political instability significantly reduces the inflow of foreign direct investment. In conclusion, it was found that multinational firms invest less in emerging economies with high inflation. Graham Edward Ma and Krugman P R [7] in their article “Foreign Direct Investment in the United States” in the report highlights that the United States will remain an attractive destination for foreign investment, and this investment will help bolster the economy. This paper reviews the factors that individually and collectively make the United States a sought-after destination for foreign investment. They also point out that an open investment regime, a large economy, skilled labor force, community colleges, world-class research universities, predictable and stable regulatory regime and adequate infrastructure will further enhance the investment base. Gurmeet Singh [8], ‘Political Environment and Its Impact on Tourism Marketing: a Case Study of Fiji, in his analysis of the political environment in Fiji, revealed that political unrest in the country has affected the image and consequently the international relations with countries who have been immensely contributing to the revenue from the tourism industry. This has ultimately affected the marketing effort. Results obtained by a study conducted by Hossain and Hossain [9] examined the cointegration and causal relationship between FDI and GDP in the short and long run of Bangladesh, Pakistan and India over the period of 1972-2008. Econometric models- Augmented Dickey-Fuller (ADF) test, Engle-Granger two-step cointegration test, Vector Error Correction Mechanism (VECM) and Granger causality test have been used. The results suggest that in Indian case there is no co-integration between FDI and GDP in the long and short term. Granger causality test reveals the presence of unidirectional relationship in India which runs from FDI to economic growth. Various empirical studies reveal the relationship between FDI and economic growth to be mixed hence deserves a fresh inquiry into this issue.

Factors Promoting Foreign Direct Investment

Fiji has been actively promoting FDI favoring the island’s economic development through utilization of natural resources and expansion of economy’s exports. FDI process delays in the past have seriously discouraged prospective overseas investors hence Fiji Islands Investment Board (FTIB) has been set up to provide assistance to potential investors and facilitate the coordination. The government is aware that there is still a lot of scope for speeding up the clearance process. Favorable conditions make foreign investors face fewer problems. Few vivacious clues for foreign direct investment include political stability, economic stability, lower wages, easy access to raw material, special rights, and person safety. Long-term political stability makes foreign investors confident with their businesses. Besides, economic instability like inflation, foreign exchange fluctuation, and economic crisis also another important environment factor for an investor to consider because can cause the business loss.

Furthermore, foreign investors try to search the country with lower wages to reduce the average cost of production. A country with plenty of raw materials necessary for the production attracts investors more than a country without it and personal safety also vital to foreign investors.

The government advocated export-promotion based on tax-free factories and export-processing zones and this required further trade liberalization measures. The Fiji Government recognizes that trade liberalization measures will have to be accelerated and new opportunities explored for exports. This means greater competition for domestic market producers. Fiji is a signatory to various trade agreements, frameworks, and memoranda of agreement that allows for better market access and provides a conducive investment climate and opportunities in other countries.

RESULTS AND DISCUSSION

Foreign direct investment is a boon to developing countries because it not only brings finance but also technology and manpower associated with it. The Asian tigers are the prime beneficiaries of this kind of change but unfortunately. With the increasing role of Foreign Direct Investment, the countries have to examine the mode and method of inviting FDI for their sustainable development. In this background, Fiji a developing country Island has to carefully draw its plan to embrace this astonishing global magic and cope up with globalization. Fiji has its unique features and socio-economic and political factors have a great influence on policy matters. Direct foreign investment is considered as a catalyst for economic development through diffusion of technologies, linkages with domestic firms, techniques for enhanced production and access to overseas markets. It also helps in domestic saving and investment and helps the receiving economy to end the vicious cycle of low investments and poor income. The effect of direct foreign investment is subject to many other factors, most importantly including the economic policies, quality of labor and domestic investment itself.

FDI would not be able to succeed without the availability of the needed factors, which have been discussed. One of the major factors to attract the attention of foreign investors is an adequate infrastructural facility. Without the availability of these needed facilities, it would be risky for investors to come into any country.

It is imperative for the government to create pre-conditions for foreign direct investment to flow and gross domestic product to grow. A liberal and competitive investment climate generate the basis for FDI to enter and raise the potential for growth. The obligation of providing a conducive environment for foreign investors are in the government.

CONCLUSION

Greater macroeconomic stability and an improved business environment are important for creating the foundation for economic growth. Fiji government should continue with further structural liberalization towards the business environment with an emphasis on export growth strategies after a careful comparative advantage analysis of the agriculture and service sector. Therefore it is imperative that government should emphasize on building infrastructure to further boost the agriculture and service sectors. Empirical research on Fiji [3] related to trading liberalization and growth provides evidence that non-discriminatory trade and gradual unilateral liberalization remains the best option for Fiji in order to maximize welfare. The findings suggest that while FDI policy may be neutral government policy plays a major role through industry policy and providing an investment environment which is stable politically and economically. Overall, the findings would provide policymakers with a better understanding of the nature and outcomes of interaction between foreign and local firms. At the end, it was discovered that foreign direct investment helps in developing the economy of developing countries. It can be concluded that the success of FDI in any host country is dependent upon the level of infrastructural facilities in the country.

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