

# POLICY BRIEF

**LOWY INSTITUTE**  
FOR INTERNATIONAL POLICY

APRIL 2009

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## FIJI: THE FLAILING STATE

### WHAT IS THE PROBLEM?

*Fiji President Iloilo's abrogation of the 1997 constitution has entrenched a military dictatorship in Australia's backyard. Commodore Voreqe Bainimarama's dominant leadership of the interim government and his exclusion of dissenting voices will exacerbate and accelerate economic decline in Fiji and cause unprecedented hardship to Fiji's population. The economic implications threaten the whole Pacific Islands region and challenge Australia's capacity to demonstrate regional leadership.*

### WHAT SHOULD BE DONE?

*Australia's response to developments in Fiji must differentiate between political responses – which need to be strong and unambiguous – and economic responses, which need to take into account the rapidly deteriorating economic situation in Fiji and the impact of Fiji's economic collapse and the global financial crisis on the wider Pacific Islands region. The Australian government should work with the international financial institutions to develop a package of assistance for the region. In addition, a second-track process of dialogue should be established between Australian and Fiji private sector representatives and the international financial institutions to build bilateral confidence and plan for future financial assistance for Fiji which links assistance to measurable reforms by the interim government.*



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**POLICY BRIEF**

**FIJI: THE FLAILING STATE**

**The political situation**

Fiji's President Ratu Josefa Iloilovatu Uluivuda announced on 10 April 2009 that he had abrogated Fiji's 1997 constitution, appointed himself head of state, revoked the appointment of all judicial officers and would direct an interim government to hold parliamentary elections by September 2014. The President's announcement followed a Court of Appeal judgement on 9 April which ruled that Commodore Voreqe Bainimarama's December 2006 coup was illegal and directed the President to appoint an independent third person to lead an interim government and call for fresh elections under the 1997 constitution. On 11 April, President Iloilo reappointed Bainimarama as interim Prime Minister, who subsequently imposed strict censorship on the media, deported Australian journalist Sean Dorney, arrested a number of opponents and removed the Reserve Bank Governor, Savenaca Narube.

The President's decision and Bainimarama's actions have entrenched a new political and economic reality for Fiji and a military dictatorship in Australia's backyard. The developments in Fiji have attracted international condemnation, including most loudly from Australia and New Zealand. Fiji is likely to be suspended from the Pacific Islands Forum and the Commonwealth.

Australia, having employed almost every manoeuvre from the diplomatic playbook on responding to coups to no avail, nevertheless must continue to protest against developments in Fiji and isolate the interim government. Australia has to send a clear message to Commodore Bainimarama that his actions are

not only unacceptable politically but have serious economic implications that go beyond Fiji. The economies of a number of Pacific Island countries will feel the consequences of his actions. The Australian government, in concert with Pacific Island governments, will need to develop a strategy to pressure Fiji's interim government to deliver on its responsibilities to its people and its partners in the region. Bainimarama's moves have severely limited Fiji's capacity to respond to the global financial crisis and deliver on its regional responsibilities.

Politically, Australia cannot reward Fiji's interim government for Commodore Bainimarama's actions. Rather it should use its economic influence to apply pressure to stabilise Fiji's economy and prevent a meltdown and the ensuing regional contagion.

**Economic consequences**

Fiji's economy, once a leader in the Pacific Islands region, has been hit by a triple whammy of the loss of business confidence following the December 2006 coup, the impact of the global financial crisis on demand for Fiji tourism and exports, and devastating floods in January 2009. Tourism, wholesale and retail trade, hotels and restaurants, manufacturing, agriculture (including sugar), forestry and fisheries sectors, have all slumped and further decline is predicted in the finance, insurance, real estate and business services sector.<sup>1</sup> Private sector losses from the floods alone are estimated at over US\$160 million.<sup>2</sup>

The events of 10 to 14 April, and in particular the removal of the respected Reserve Bank

**POLICY BRIEF**

**FIJI: THE FLAILING STATE**

Governor, will destroy what is left of business confidence and deter potential foreign investors. Fiji faced a serious liquidity crisis even before 10 April; the negative outlook for the economy will be dramatically worse as a result of the actions of President Iloilo and Commodore Bainimarama.

The Reserve Bank of Fiji had just forecast a contraction of the economy by 0.3 per cent in 2009.<sup>3</sup> This follows very low growth of just 0.2 per cent in 2008 and a contraction of 6.6 per cent in 2007. Exports are projected to decline by 12.2 per cent in 2009. Investment in 2009 is estimated to fall to about 13 per cent of GDP, down from an estimated 15 per cent of GDP in 2008.<sup>4</sup>

Official foreign reserves at the end of February 2009 were FJ\$674 million, equivalent to around 2.7 months of goods imports.<sup>5</sup> The very real risk that the abrogation of the constitution will worsen the liquidity situation was recognised by the Reserve Bank of Fiji's introduction of measures to tighten exchange controls on 14 April in order to protect foreign reserves.<sup>6</sup>

Fiji's interim government announced a 50 per cent cut to the operations of all public sector agencies on 30 March. Reductions of this magnitude will translate into job losses and cuts to essential service delivery. The public sector in Fiji employs some 52,000 people.

Tourism, which contributes 20 per cent of Fiji's GDP and provides 10,000 jobs, is already under threat from the softening demand caused by the global financial crisis. An estimated 540,000 tourists visited Fiji in 2008 (43 per cent of whom were Australians).<sup>7</sup> Heavy

discounting has meant that even though tourist arrival numbers were high, revenue derived from tourism had been low for some time and many resorts have been operating at a loss. Fiji tourism may suffer further from the negative images of public emergency rule being broadcast on Australian and New Zealand television screens and from heightened government travel warnings.

**Social consequences**

The relative calm in Fiji since the 2006 coup and the lack of obvious public protest following the President's abrogation of the constitution suggest there is little likelihood of a violent uprising. Many prominent citizens of Fiji attribute the apparent apathy in the country to fear of repercussions from the security forces rather than acceptance of the political realities.<sup>8</sup> However, the possibility of civil unrest, particularly when job losses and service delivery decline increasingly hurt families, cannot be ruled out. The introduction of formal censorship on 11 April and action by the security forces against opponents of the interim government will make it more difficult for opposition to be voiced and will cause significant frustration in society.

The Fiji Bureau of Statistics estimates the average incidence of poverty across Fiji at 35 per cent.<sup>9</sup> Poverty is found in urban squatter settlements and also in rural areas.<sup>10</sup> While poverty in Fiji has traditionally been manifested by low incomes, inadequate housing, and poor access to health and education services, rather than hunger, the liquidity crisis and rising unemployment in 2009 will put increasing pressure on family incomes and the cost of

**POLICY BRIEF**

**FIJI: THE FLAILING STATE**

living. As 51 per cent of Fiji's population live in urban areas, the option to resort to subsistence lifestyles is not available to all. A humanitarian crisis requiring food aid to the poor cannot be ruled out.

**Regional fallout**

Fiji's political crisis is indeed grave but the economic crisis already hurting Fiji citizens also has serious implications for the Pacific Islands region and therefore for Australia. The full effects of the global financial crisis on the region are yet to be realised and the ripple effect of the deterioration of the Fiji economy on the wider region is difficult to predict with accuracy. However, Fiji's importance as a regional economic hub means what happens in Fiji matters to the region.

It is unlikely that many countries in the region, linked to Fiji through vital transport, trade and education services, will be able to afford to suspend their relationships with Fiji for a prolonged period. Some leaders in the region have reportedly already expressed concern that Fiji's suspension from the Pacific Islands Forum could be harmful to their own economies.<sup>11</sup> Australia's own efforts to launch PACER Plus trade negotiations in the region require the participation of Fiji in order to be successful. In responding to the crisis, Australia will need to be sensitive to the economic needs of the region and find a way of persuading Fiji's interim government to deliver on its regional economic responsibilities.

Suva is home to the secretariat of the Pacific Islands Forum and a number of other important regional institutions. The main

campus of the University of the South Pacific, serving up to 10,000 students from twelve Pacific Island nations, is in Suva. Fiji is also home to the regional offices of a large number of international organisations and non-government organisations, which use Suva as a base for their regional operations. The restrictions on free speech and assembly imposed by Commodore Bainimarama and Fiji's economic decline will make the operations of regional organisations more difficult.

Fiji is also an aviation hub for the region. A number of airlines provide international services through Nadi airport, including Qantas, Air Pacific, Air New Zealand, Korean Airlines, and a number of Pacific Islands airlines.<sup>12</sup> Air Pacific, which has been serving the Pacific region since the 1940s, operates services to Australia, New Zealand, Samoa, Tonga, Vanuatu, Solomon Islands, Kiribati, Tuvalu, Hong Kong and the United States. The micro states of Kiribati and Tuvalu rely on Fiji-based airlines and flight connections, which transport not only passengers but essential goods.

Fiji's ports are an important crossroads for shipping services between North America, Asia, Australia, New Zealand and the island states. Fiji's two biggest towns, Suva and Lautoka, have important trans-shipment ports for the Pacific Islands region. Fiji was due to be the hub of the Pacific Islands Forum's proposed bulk oil purchasing initiative, designed to mitigate the negative effect of high oil prices on the region. This initiative will be more difficult to implement without Fiji.<sup>13</sup>

**POLICY BRIEF**

**FIJI: THE FLAILING STATE**

**Implications for Australia**

The crisis precipitated by events in Fiji has provided the Rudd government with its most significant foreign policy challenge in the region to date. Ongoing instability in Fiji has reputational consequences for Australia's political leadership in the region. The United States and European Union look to Australia to solve problems in the South Pacific. The Rudd government came to power promising to improve Australia's relations with the Pacific. Australia is hosting the Pacific Islands Forum leaders' summit in Cairns in August 2009 and will then take over the chair of the Forum for a year. A failure to deal effectively with the serious domestic and regional effects of the crisis in Fiji, however complex the policy challenge it poses, will harm the Australian government's regional standing.

Australia rightly abhors the political leadership of countries like Myanmar, North Korea and Zimbabwe, and shares the concerns of the international community about the lack of human rights and level of poverty in these countries. The Australian government lacks the leverage to improve the situation in any of these countries. Our people-to-people links, trade and investment in the three countries are minimal. Canberra relies on like-minded governments with greater influence to push for changes in Myanmar, North Korea and Zimbabwe. Now the onus is reversed. In the case of Fiji, the international community looks to Australia to exploit its deep connections with Fiji and exert influence for change.

Fiji, following difficulties in its diplomatic relationships with Australia and New Zealand, has been pursuing a 'look north' policy,

courting investment and aid from China. China has provided loans for major hydroelectric and highway projects and is perceived by to be a friendly partner because of its uncritical approach to the interim government.

Australia's deep connections with Fiji, however, mean it remains the dominant foreign influence in Fiji. Australia is by far the largest investor in Fiji, with the value of total investment estimated at up to A\$2 billion.<sup>14</sup> Australian investors in Fiji range across a number of sectors, including banking, financial, insurance and legal services, tourism, transport, logistics and manufacturing. Three of Australia's four major banks – ANZ, Westpac and Commonwealth (Colonial) – dominate the Fiji market. Australian insurance companies with a presence in Fiji include Queensland Insurance (Fiji) Ltd (QBE), Fiji Care Insurance Ltd, AON, Marsh Ltd and Tower Insurance.<sup>15</sup> The partnership between Air Pacific, Fiji's national airline and Qantas is the most enduring in the Pacific.<sup>16</sup> Qantas owns 46 per cent of Air Pacific, with the government of Fiji holding 51 per cent.

Two-way merchandise trade between Fiji and Australia was worth A\$502 million in 2007-2008. Australia is the second-largest merchandise import market for Fiji, with Australia holding a 22.8 per cent share of the market. Two-way services trade totalled A\$994 million in 2007-2008, with Fiji holding the lion's share of \$831 million, thanks to the popularity of holidays in Fiji amongst Australians.<sup>17</sup>

It is worth noting that previous delays from Canberra in addressing incipient crises in the

**POLICY BRIEF**

**FIJI: THE FLAILING STATE**

Pacific Islands region have come at a cost. Australia could have intervened in Solomon Islands when ethnic conflicts, land disputes and signs of a break-down in law and order began in 1999. The delay in developing an appropriate response while the situation deteriorated and law and order broke down completely meant the policy response required and eventually implemented became much more complex and expensive, costing the Australian government over \$1 billion in expenditure on the Regional Assistance Mission to Solomon Islands.

**Policy recommendations to prevent economic meltdown**

The impact of the global financial crisis has created new imperatives for domestic economic policy, and for international economic cooperation. Governments all over the world have introduced radical policies to bolster their own economies and agreed to boost cooperation with other governments in unprecedented ways.

The Australian government will be under pressure from regional leaders at the Pacific Islands Forum leaders' summit to assist the region to respond to the global financial crisis and the fallout from Fiji's economic crisis. Prime Minister Rudd, as the host, will want to be seen to be generous and inclusive. An offer of financial assistance to the region which included Fiji would be understood and appreciated by the region and justifiable on humanitarian rather than political grounds.

*Policy recommendation 1: Australia should work with the international financial institutions to develop a flexible package of assistance for the region.*

For example, a coordinated contingent credit line provided by the IMF, ADB and World Bank could be facilitated by Australia and New Zealand and made available to the region – to be drawn on by countries affected by the global financial crisis or by the crisis in Fiji. The credit facility should also be open to Fiji on a conditional basis; this would commit the interim government to reforms.

*Policy recommendation 2: The Australian government will need to relax its principled opposition to lending by international financial institutions to Fiji.*

Direct bilateral engagement on economic assistance is unlikely to be palatable to Australia. The international financial institutions – the IMF, World Bank and Asian Development Bank – are best placed to offer the necessary financial assistance to Fiji as they are able to engage as non-political actors. Financial assistance by these institutions to Fiji can effectively be undertaken only with the tacit approval of Canberra and Wellington. With proper conditionality, the discipline imposed by the international financial institutions will put pressure on the interim government, not reward it.

*Policy recommendation 3: Australia should work with other like-minded countries to encourage China to channel any further financial assistance to Fiji through the international financial institutions.*

The Fiji interim government is likely to request further assistance from China to help it respond to its liquidity crisis. China should be

**POLICY BRIEF**

**FIJI: THE FLAILING STATE**

convinced to direct this assistance through the international financial institutions, consistent with the commitments it made at the G-20 meeting in London on 2 April on delivering resources to developing countries through the international financial institutions,<sup>18</sup> rather than bilaterally. This would send an important signal to Fiji's interim government that its only option was to deal with the international financial institutions and adopt the disciplines they recommend. The Australian government's engagement with China on Fiji would be broadly consistent with its ongoing dialogue with China on the importance of transparency and accountability in the delivery of aid to the Pacific Islands region.

*Policy recommendation 4: Australia should establish a second-track process of dialogue with Fiji to build confidence and plan for future financial assistance.*

Any assistance to Fiji poses a risk that it will signal acceptance of the interim government. Financial assistance in such a difficult economic environment and without sufficient commitment from the interim government may well be ineffective. Australia will need to manage the risks to any assistance very carefully. One potentially useful means of managing this risk would be to establish a second-track process to prepare a path for financial assistance. A second-track process could be presented as helping further to marginalise the interim government while supporting and empowering civil society in Fiji. A carefully structured dialogue between Australian and Fiji economic experts, banks, businesses and NGOs, with the participation of the international financial institutions and with a conduit back to respective governments, would help to build confidence following the

recent significant shocks to the economy. Such a dialogue, which would focus on the immediate economic challenges, could devise modalities for a package of financial assistance that would appeal to the interim government and put pressure on it to make the necessary economic and political reforms.

*Policy recommendation 5: Australia needs to move quickly to safeguard its economic relationship with Fiji and protect Australian investments.*

Fiji's interim government has not yet sought to nationalise private investments, seize private land or deny foreign investors the right to repatriate profits. While there is no precedent for such action in Fiji, the Reserve Bank of Fiji has announced measures that will slow down the process of repatriating profits and give it capacity to defer the process if the foreign exchange situation deteriorates.

**Conclusion**

Australia has deeper links with Fiji than any other country or international organisation. Australia's people-to-people and business-to-business relationships with Fiji, built up over more than a century, need to endure. They impose on both Australian and Fiji authorities a duty of care to protect the bilateral relationship for future generations.

How Australia reacts to Fiji's economic crisis will be remembered by the people of Fiji and the region. If Australia stands aside, no matter how rightly principled its approach to illegal developments in Fiji and how well understood its approach is in educated circles in Suva, it will be sending an important and enduring



**POLICY BRIEF**

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**FIJI: THE FLAILING STATE**

signal about the limits of Australia's interests in its neighbourhood. Much – including much beyond Fiji – now rests on the strength, creativity and wisdom of Canberra's response.

POLICY BRIEF

FIJI: THE FLAILING STATE

NOTES

<sup>1</sup> Reserve Bank of Fiji, *Revised economic projections*, 9 April 2009.

<sup>2</sup> Asian Development Bank, *Asian development outlook 2009: rebalancing Asia's growth*, March 2009, p 240.

<sup>3</sup> Reserve Bank of Fiji, *Revised economic projections*, 9 April 2009.

<sup>4</sup> Reserve Bank of Fiji, *Economic review*, March 2009.

<sup>5</sup> Ibid.

<sup>6</sup> Reserve Bank of Fiji, *Reserve Bank of Fiji announces policy changes to exchange controls*. Press release, 14 April 2009.

<sup>7</sup> Republic of Fiji Ministry of Finance and National Planning, *Raising economic growth and alleviating poverty. Economic and fiscal update: supplement to the 2009 Budget Address*. 2008, p129.

<sup>8</sup> Jenny Hayward-Jones, Interviews conducted with prominent citizens in Fiji during the week of 16 to 20 February 2009.

<sup>9</sup> Fiji Islands Bureau of Statistics. *Poverty indicators*, 2009:

[http://www.statsfiji.gov.fj/Social/poverty\\_indicators.htm](http://www.statsfiji.gov.fj/Social/poverty_indicators.htm).

<sup>10</sup> Asian Development Bank, *Asian development outlook 2009: rebalancing Asia's growth*, p 271.

<sup>11</sup> Samisoni Pareti, Forum leaders issues Fiji an ultimatum. *Islands Business*, February 2009.

<sup>12</sup> Fiji Trade and Investment Bureau. *Investing in Fiji: communications*, 2009: <http://www.ftib.org.fj/fiji-communications.cfm>.

<sup>13</sup> Pareti, Forum leaders issues Fiji an ultimatum.

<sup>14</sup> Australia-Fiji Business Council, Estimate of Australian investment in Fiji. Personal communication to author, 2009.

<sup>15</sup> Australian Department of Foreign Affairs and Trade. *Republic of the Fiji Islands country brief*, 2008: [http://www.dfat.gov.au/geo/fiji/fiji\\_brief.html](http://www.dfat.gov.au/geo/fiji/fiji_brief.html).

<sup>16</sup> Australian Agency for International Development. *Pacific economic survey 2008: connecting the region*,

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<http://www.pacificsurvey.org/UserFiles/file/Pacific%20Economic%20Survey08.pdf>.

<sup>17</sup> Australian Department of Foreign Affairs and Trade. *Fiji fact sheet*. 2009:

<http://www.dfat.gov.au/geo/fs/fiji.pdf>.

<sup>18</sup> G20 meeting London. *Declaration on delivering resources through the international financial institutions*, 2009:

[http://www.g20.org/Documents/Fin\\_Deps\\_IFI\\_Anne\\_x\\_Draft\\_02\\_04\\_09\\_-\\_1615\\_Clean.pdf](http://www.g20.org/Documents/Fin_Deps_IFI_Anne_x_Draft_02_04_09_-_1615_Clean.pdf).

## ABOUT THE AUTHOR

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