GOVERNMENT DEBT REPORT

FOR THE YEAR ENDING DECEMBER 2011

MINISTRY OF FINANCE

SUVA

FIJI

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INTRODUCTION

A government's debt portfolio is usually the largest financial portfolio in the country which often contains complex and risky financial structures and can generate substantial risk to the government's balance sheet and to the country's financial stability.[1]

The 2011 Budget adopted an expansionary stance with the deficit level targeted at 3.5% of Gross Domestic Product. The expansionary fiscal stance was adopted to generate economic activity in light of low private sector investment and foreign direct investments (FDI). To fund the budget deficit, government raised US$250million from the International capital market in March 2011.

The 2011 Government Debt Report presents the actual debt position and the debt portfolio as at the end of 2011. Particular emphasis is drawn to the efforts by Government to achieve a sustainable debt level in the medium term with the debt to GDP ratio falling to 52.1% at the end of 2011.

1.0 OVERALL DEBT POSITION

The Overall debt position of the Fiji Government stood at **$3.566 billion** as at 31st December 2011, which comprises $2.734 billion domestic debt and $832.1 million external debt. This represents an increase of 5.4 percent when compared to the 2010 debt level of $3.383 billion. Financing of the 2011 budget deficit was mostly through raising of the US$250million bond in the international market and $117.2m was financed from the domestic bond market for capital projects.

[1] Guidelines for Public Debt Management- IMF and World Bank, 2001

Table 1: *Total Debt Stock*

Year	2007	2008	2009	2010	2011
Domestic Debt	2,337.8	2,411.0	2,605.0	2,834.7	2,734.4
External Debt	397.0	476.0	527.2	548.5	832.1
Total Debt	2,734.8	2,887.0	3,132.2	3,383.2	3,566.5
% of GDP	49.9%	50.8%	56.6%	57.7%	52.1%

2.0 GOVERNMENT DOMESTIC DEBT

2.1 Domestic Debt Stock

Domestic debt is the sum of outstanding Treasury Bills and Bonds at any given time. The domestic market continues to be major source of funding for Government over the years. On a year to year basis, the total domestic debt decreased by $100.3 million or 3.5% from $2.834 billion the previous year to $2.734 billion at the end of December 2011.

Tabulated below is the 5 year trend for domestic debt.

Table 2*: Domestic Debt ($M)*

Year	2007	2008	2009	2010	2011
Bonds	2,196.2	2,346.3	2,505.1	2,759.3	2,663.3
Treasury Bills	141.6	64.7	99.9	75.4	71.1
Total Domestic Debt	**2,337.8**	**2,411.0**	**2,605.0**	**2,834.7**	**2,734.4**
% of GDP	**42.6%**	**42.4%**	**47.1%**	**48.4%**	**39.9%**

As stated in Table 3, total domestic debt outstanding at the end of 2011 decreased by $100.3 million to $2.734 billion. The decrease was associated with net reduction of bonds issued in the domestic market as Government sourced US$250million from the overseas bond market to finance the 2011 Budget deficit. Outstanding Treasury bills also recorded a reduction of $4.3million or 5.7% at the end of 2011.

2.2 Domestic Debt by Holder Category

The Government's bond holding at the end of 2011 totaled $2.663 billion whereby 90 percent is held by Non Bank Financial institutions, 5 percent by the Reserve Bank, 3 percent by Commercial Banks and other investors including individuals hold 2 percent.

Table 3: *Government Bond Holders-December 2011*

Investor	$m
Commercial Banks	91.30
Non Bank Financial Institutions	2,385.67
Reserve Bank	130.51
Others	55.80
Total Bonds Outstanding	**$2,663.28**

An analysis of short term debt holdings as of December 2011 saw the Commercial banks holding 74%, Non Bank Financial institutions held 15% respectively whilst individuals and other holders held 11%.

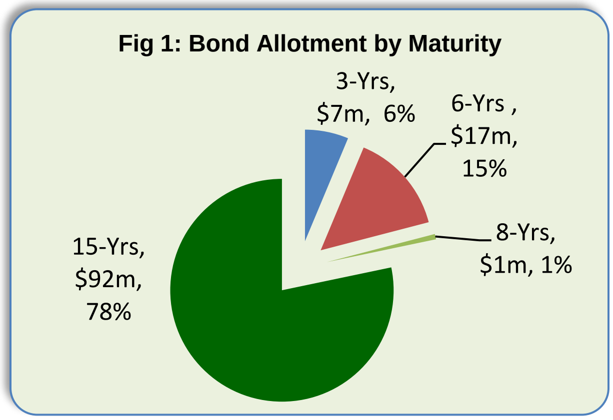
Table 4*: Government T-Bill Holders-December 2011*

Investor	$m
Commercial Banks	52.56
Non Bank Financial Institutions	11.02
Others	7.52
Total T-Bills Outstanding	**$71.10**

2.3 Domestic Debt Allotment by Instrument

Domestic debt is mainly comprised of government bonds with maturities ranging from 3 years to 15 years. Apart from bond raising to meet the budget deficit, the issuance of medium to long term bonds is vital for the development of the domestic financial markets.

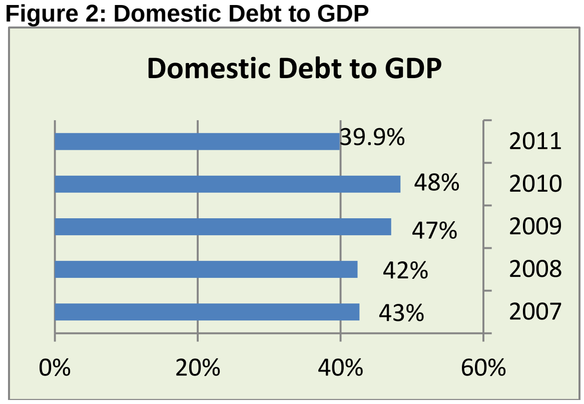
In 2011, Government allotted $117million in bond and *Figure 1* shows the distribution of bond allotment by maturity with $92million allotted under the 15 year maturity, $17million for the 6 years, $1milion for 8 years and $7milliion for 3 years. No transaction was recorded for the 10 Year bond.



2.4 Domestic Debt to GDP

As depicted in Figure 2, the Government domestic debt to GDP decreased significantly over the last year with Domestic Debt to GDP falling from 48 percent in 2010 to 39.9% percent in 2011. As a result of sourcing most of its deficit externally in 2011, Government was able to contain domestic debt to GDP ratio below 40%.

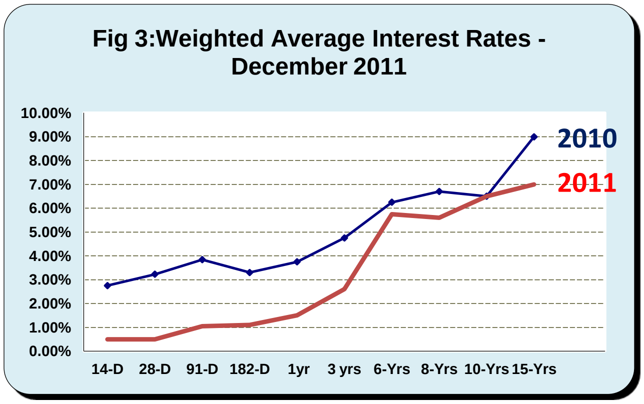
Figure 2: Domestic Debt to GDP



2.5 Domestic Interest Rates Structure

In 2011, interest rates for both short and long term debt instruments declined progressively during the year. This was largely attributed to Government's lower domestic funding requirement and surplus liquidity in the banking system. The former in particular resulted in an oversubscription of tenders which exerted downward pressure on rates.

The yield curve in figure 3 depicts the reduction in interest rates for Government securities.



Treasury Bills as a means of short term borrowings for Government were raised with the maturities of 14 days, 28 days, 56 days, 91 days and 182 and 245 days.

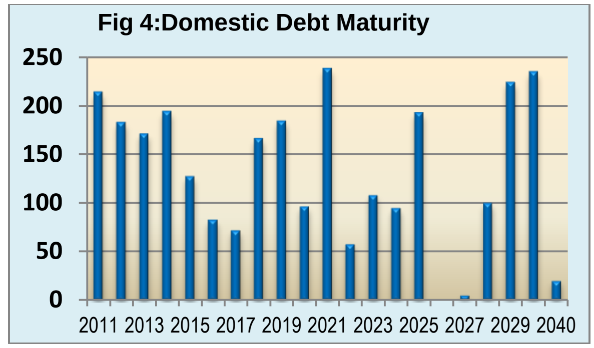
2.6 Domestic Debt Servicing

Table 5: Domestic Debt Servicing: 2006-2011 ($M)

	2007	2008	2009	2010	2011
Principal	205.0	191.2	245.4	198.5	213.4
Interest	147.5	147.6	165.3	190.7	213.2
T-Bill Interest	13.0	0.6	1.2	4.3	2.1
Total Domest Debt Service	**365.5**	**339.4**	**411.9**	**393.5**	**428.7**

Source: MOF

The Government managed to settle all principal and interest payments due in 2011. Of the total $428.7m, Government successfully repaid $213.4 million for maturing loans. Figure 4 shows the government's maturity structure.



2.7 Domestic Loans Fully Paid in 2011

A total of eight domestic loans raised in the form of government bonds were fully paid in 2011. This consisted of bonds raised between 1996 to 2006, with interest rates ranging from 8.0% to 8.92%.

Table 6: Bonds Fully Paid in 2011

Loan	Rate	Amount
1996 FDL 3	8.80%	$10.00m
1996 FDL 5	8.60%	$ 1.81m
1996 FDL 6	8.86%	$7.7m
1996 FDL 7	8.89%	$4.25m
1996 FDL 8	8.92%	$4.0m
1997 FDL 2	8.80%	$6.0m
1997 FDL 8	8.00%	$0.65m
2006 FDL 9	8.70%	$5.0m

Source: MOF

3.0 GOVERNMENT EXTERNAL DEBT

At the end December, 2011, the total external disbursed outstanding debt stood at $832.1m an increase of $288.6m as compared to the disbursed outstanding debt for the same period last year. The increase was mainly attributed to the disbursements of the Second Global Bond and on-going capital projects financed by the Asian Development Bank, Exim Bank of China and the Exim Bank of Malaysia.

Table 7: Government External Disbursed Outstanding Debt

	2008	2009	2010	2011 est
External DOD Central Govt	476.0	527.5	548.5	832.1
Total External Debt Service of which	**33.0**	**45.6**	**41.3**	**331.6**
Principal Payment	12.5	21.2	17.6	285.0
Interest Payments	20.8	24.4	23.7	46.5
External Debt to GDP Ratio	**8.4%**	**9.5%**	**9.4%**	**12.1%**
External Debt Service as % age of Export of goods and services	1.0%	1.0%	1.0%	1.0%

During the year, there were major highlights in terms of debt servicing and disbursement of loan funds. The Government in September settled its Global Bond valued at USD$150m (FJD$263.0m) and in November it prepaid a total of EUR$3.5m (FJD$8.7m) for its last three EIB loans. The prepayment of these EIB loans started in 2010 and was completed in November, 2011. This brought to close the Government's loan commitment to the European Investment Bank.

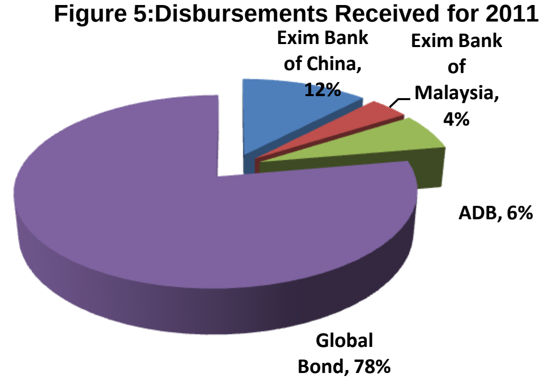
In terms of the disbursement of borrowed funds, the Government received the proceeds of the recently contracted Second Global Bond valued at USD$250m (FJD$455m) in March as well as drawdown's of loan funds in various currencies from on-going capital projects which was disbursed throughout the year and valued at around FJD$130m.

Debt servicing for the year, totaled FJD$331.6m with principal repayment amounting to FJD$285.0m and the remaining FJD$46.5m went towards interest and other payments such as commitment fee, management fees etc. The repayment of the Global Bond made up over 75% of the principal and interest repayment during the year. External Debt to GDP increased significantly to 12.1% in 2011 compared to 9.4% in 2010.

3.1 External Loan Disbursements

At the end of December, 2011 the total value of all disbursements received from all on-going capital projects and the Global Bond amounted to FJD$585.4m. The Global Bond made up 78% of the total disbursements, followed by the Exim Bank of China at 12%, ADB at 6% and Exim Bank of Malaysia the remaining 4 %. Bulk of the disbursements received from the ADB, Exim Bank of China and the Exim Bank of Malaysia were paid directly to the contractors whilst the proceeds of the Global Bond was deposited into the Government JP Morgan account.

Figure 5:Disbursements Received for 2011



External Debt to GDP increased significantly from 9.4% to 12.1% over the same period last year.

3.2 External Debt Composition

3.2.1 By Creditor Category

At the end of December, 2011, the distribution of debt by creditor category continued to be lead by the Commercial Lenders which registered an outstanding debt of FJD$455.1m (55%), followed by Multilateral Lenders FJD200.6m (24%) and Bilateral Lenders FJD$176.4m (21%).

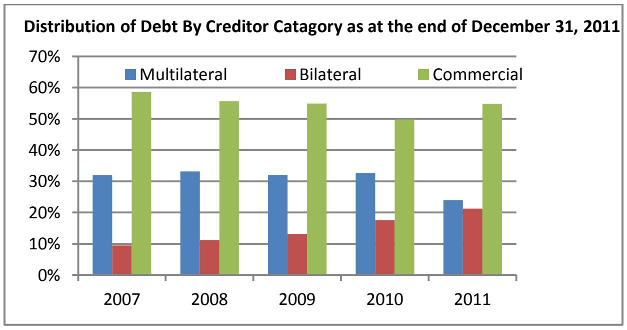


Fig 6: Distribution of Debt Creditor Category – December 2011

In the past years, bulk of Government borrowing from external sources has always been contracted from multilateral lenders mainly from ADB. However recently, Government has shifted its borrowings externally towards its bilateral lenders and bulk of its loans is now contracted from China. In 2011, the total disbursed outstanding debt on a bilateral basis stood at FJD$176.4m of which 75% were disbursements from Chinese funded project. This will continue to increase as on-going loans from China are disbursed.

3.2.2 By Economic Sector

In terms of distribution by sectors, the global bond dominates with 49%, followed by the Road Transport sector 22%, Water & Sanitation sector 13%, IT sector 5%, Multisector 9% and Housing Development sector the remaining 2%.

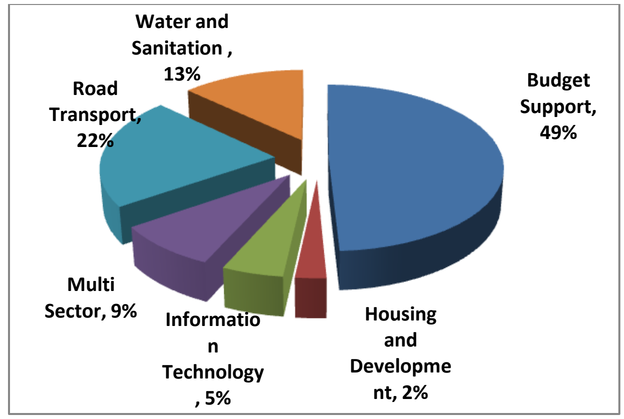


Fig 7: Distribution of Debt by Economic Sector

Development of infrastructural services in the country continues to be a priority for Government with bulk of the funding channeled towards the Road sector 22% and Water & Sanitation sector 13% within the economy. The Housing and Development other hand is another sector which the Government has invested in recently, with 2 loans contracted from China to develop the Public Rental Board Flats and the Housing project in Tacirua Heights

3.2.3 By Debt Maturity & Currency Profile

At the end of December 2011, the maturity structure for the Government's external debt portfolio showed that 56% of its external debt will mature from 4 – 5 years time, 5% from the next 5 – 10 years time and the remaining 39% over the next 10 years.

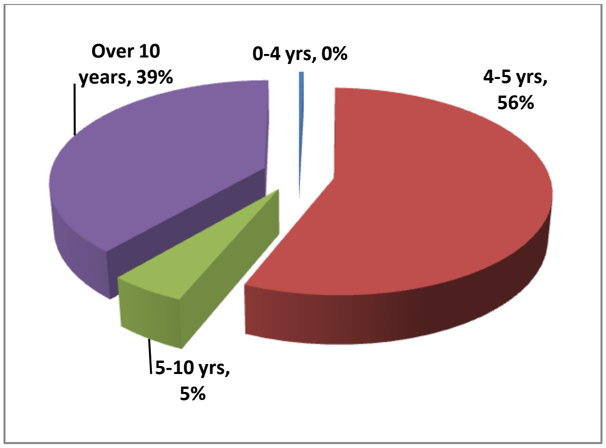


Fig 8: Maturity Structure of External Outstanding Debt as at end of December, 2011

Moreover, the currency composition continued to be dominated by the US dollar 80.2% followed by the Chinese Yuan 13.5% Japanese Yen 6.3%. As compared to the same period last year, it can be noted that the composition of the Chinese Yuan has surpassed the Japanese Yen by 3.2% from 9.4% to 13.5% in terms of the structure of currency composition for Government. The Euro currency has now been phased since all remaining Euro denominated loans have been paid off.

3.3 External Loans Prepaid in 2011

In November, 2011 the Government in its continuous quest to reduce its outstanding external debt in the medium to long term prepaid the last three remaining Euro denominated loans. The total prepayment amounted to FJD$8.7m (EUR$3.5m) and this brings the Government's commitment to European Investment Bank to an end. These three loans are as follows: Investment and Export Development Project, Rural Electrification Project and Outer Island Airstrip Project

4.0 CHALLENGES IN MANAGING DEBT

4.1 Sustainability

Sustainability is the ability of the Government to continue to service its debt, and is measured by the ratio of Government debt to the Gross Domestic Product. The internationally recognized benchmark for the percentage of debt to the Gross Domestic Product is 40% of GDP for developing economies like Fiji. For the last ten years Fiji's Government Debt as percentage of GDP exceeded 40%, which reveals that Fiji's debt level is costly to government as it consumes most of the fiscal resources that can be directed to other important sectors of the economy.

Table 8: Debt to GDP

Year	Government Debt ($m)	GDP ($m)	Govt. Debt as a % of GDP
2000	1,438.7	3,049.1	47
2001	1,686.1	3,199.5	53
2002	1,891.0	3,442.9	55
2003	2,133.8	4,325.4	49
2004	2,282.2	4,539.0	50
2005	2,421.5	5,084.5	48
2006	2,858.7	5,371.5	53
2007	2,734.8	5,483.2	50
2008	2,887.0	5,682.9	51
2009	3,132.2	5,531.3	57
2010	3,383.2	5,861.9	58
2011	3,566.5	6,839.62	52.1

Source: MOF

The total Government debt as a percentage of GDP as at 31st December 2011 was 52.1%.

In 2011, government debt relative to the GDP decreased by 6 percentage point to 52% compared to year 2010. It should be noted that total Debt level increased by 5.4% while Debt to GDP decreased by 6% based on the revised 2011 GDP.

4.2 Government Guarantee Exposure

Contingent liabilities represents government guarantees of other state owned entities and statutory authorities' debts, which would have to be settled by government should these entities fail to pay. Table 9 below reflects the level of Contingent liabilities outstanding for Government for the year s 2007 to 2011.

Table 9: Guarantee v GDP

Year	2007	2008	2009	2010	2011 (E)
Govt Guarantee	1,718.6	1,755.2	1,953.1	1,791	1,925
As % of GDP	31%	31%	35%	30%	28%
Total Debt to GDP	49.9%	50.8%	56.6%	57.7%	52.1
Total Exposure % of GDP	81.2%	81.6%	91.9%	89.6%	80%

As of 31st December 2011, the balance was $1.9 billion which was equivalent to 28% of GDP. When compared to the 2010 contingent liabilities, it increased by $134.8 million or 7.5%. For the 5 year period, contingent liabilities as percentage of GDP averaged 30%.

4.3 New Guarantees

Tabulated below are the new guarantees approved in 2011.

Table 10: New Guarantees

Entity	Approved	Utilized	Balance
FDB	$130m	$84m	$46m
FBCL	$3.8m	$3.8m	Nil
FPL	$10m	$5.5m	$4.5m
Total	$143.8m	$93.3m	$50.5m

Cabinet approved $143.8 million in new guarantees in 2011. Fiji Development Bank (FDB) utilized a total of $84 million during the review period and this is in the forms of bonds and promissory notes issue. Further, an extension to the Deed of Guarantee was approved to Fiji Broadcasting Corporation Limited for an additional loan of $3.8m with FDB and also a $10m guarantee was given to Fiji Pine Limited to cater for the Wairiki Chip Mill Project.

5.0 OPPORTUNITIES

5.1 Issuance of Fiji Infrastructure Bonds

The Government would commence the issuance of Fiji Infrastructure Bonds [FIB] in 2012 to fund the major infratructural projects approved within the 2012 Budget. This new bond is expected to boost confidence of investors and attract new partcipaints into the Government bond market.

5.2 Prudent Cashflow Management

In terms of cash management, Government is very stringent with the utilization and release of funds. Close collaboration within the Ministry of Finance, Government agencies and departments and external stakeholders have resulted in the improvement in forecasting and cashflow management on a daily basis for whole of Government. The consistent monitoring of whole of government Cashflow allows Government to meet all 2011 operational, capital, refunds and debt servicing payment on time as well as reduciing its short term debt.

5.3 Increasing the Offshore Sinking Fund

In 2011, Government transferred a total of US$25 million to its offshore Bank Account. Having a sinking fund is increasingly important for the Government in terms of having reserve funds in a separate account to assist in future external debt obligations. Moreover, the funds are invested in US Dollars which is a mitigating factor for foreign exchange risk.

6.0 SUMMARY

For further enquiries, please contact the

Debt and Cashflow Management Unit

Ministry of Finance, Suva

Governmet debt management continues to face numerous challenges bearing in mind the risks associated with public debt. The poor financial performance and failure of certain guaranteed entities to service their debts confirms the major risks to government's fiscal resources. Considering contingent liability being estimated at 28% of GDP at end of 2011, Government's commitment to the various reforms, including the financial sector, civil service and public enterprises are being undertaken at the same time. With other factors being constant, the benefits of these reforms together with positive spin-offs from government capital spending program will boost economic growth and therefore, allow Government to consolidate its fiscal position more strongly in the medium term.

Borrowing for medium and long-term maturity instruments will be the main strategy going forward. Minimising issuing of Treasury-Bills will remain a target as government does not want to commit too much funds in the short-term.Most importantly, to support the repayment of the US$250million global bond in 2016, the strategy of diverting surplus funds to the offshore sinking fund remains a key priority.

In the medium term, should there be improvements in the key macroeconomic variables like decline in interest rates and appreciation of the Fiji dollar, the Government will continue to have savings in the budget through reduced cost in debt servicing and may therefore direct these savings to: retire expensive domestic and external loans; and divert funds to other priority sectors of the economy in order to stimulate economic development in line with the projected annual growth of 2 percent.