



RESERVE BANK OF FIJI

ECONOMIC REVIEW

22

03

March 2005

OVERVIEW

Growth prospects for all our major trading partners and selected non-Japan Asian (China, Hong Kong & Singapore) economies are expected to be positive this year. The optimistic outlook is based on the strengthening US recovery and the rapidly expanding Chinese economy. Nevertheless, renewed concerns of further increases in international oil prices, from their current record high, could dampen the world economic growth momentum.

Domestically, the performance of our economy last year was consistent with that of the global economic environment. In 2004, Fiji's economy is estimated to have grown by 3.8 percent on the back of strong performance of the construction; and wholesale & retail trade and restaurants & hotels sectors. For 2005, however, aggregate growth is expected to be in the vicinity of 1.5 percent.

The relative "small" growth for this year is largely due to a contraction in the performance of the garment sector. It is well known now that the US has cancelled its garment quota system (to which Fiji was a beneficiary) to align itself with WTO rules on free trade. As such, Fiji's garment production is likely to be adversely affected. Consequently, the manufacturing sector is anticipated to shrink considerably. This is expected to lower our overall economic performance in 2005.

The other sectors of the economy (like tourism and gold production) are expected to maintain their 2004 momentum into 2005. Additionally, an increase in sugar production is forecast given the reforms that are presently being undertaken within the industry.

Inflation stood at 3.5 percent in February, compared

with 2.9 percent in January. Food prices rose mainly due to increase in prices of market items. Service costs increased largely due to higher charges for domestic and medical services. These were partially offset by declines in the costs of miscellaneous items, durable household goods and clothing & footwear, while prices of heating & lighting and transport remained unchanged.

The outlook for year-end inflation remains at 4.5 percent. However, if the proposed increase in transport costs does not come into effect, then the year-end inflation forecast would be around 3.5 percent.

From an expenditure point of view, household purchases is again likely to dominate aggregate demand, that is, total spending in 2005. From the data collected to February this year, net Value Added Tax (VAT) collections, a partial indicator of spending, has already surpassed the February 2004 figures by 18 percent. Investment expenditure, however, continues to be a drawback for the economy. While latest data on the construction sector is encouraging, the aggregate investment expenditure falls a long way short of government's target of achieving at least a quarter of Gross Domestic Product through investment spending.

On the interest rates front, the weighted average lending rate of commercial banks decreased by 11 basis points to 6.92 percent at end-January 2005, while the weighted average commercial bank time deposit rate moved up by 1 basis point to 1.78 percent. The savings deposit rate remained at 0.36 percent during the review period. Furthermore, interest rates on new lending rose by 65 basis points to 7.56 percent in January. The new deposit rate

offered by commercial banks declined by 13 basis points to 1.3 percent over the month.

Overall credit extended by financial institutions shows no sign of abating. Lower interest rates, favourable labour market conditions meaning improved income capacity for workers, and strong economic performance of recent years resulting in greater business confidence, are all contributing to the demand for credit.

Net exports continue to be a disappointment for the production sector and the country as a whole. Latest accrual data shows that merchandise exports fell by 7.7 percent in 2004 while merchandise imports fell by 0.4 percent. A correction in this adverse situation remains high on the nation's economic agenda so as to guarantee sustainable growth.

As of February (28/02), reserves were estimated at around \$761 million, sufficient to cover 3.3 months of imports of goods and non-factor services or 5.0 months of imports of goods only.

SECTORAL DEVELOPMENTS

Developments on the domestic front remained favourable during the first two months of the year. Visitor arrivals continued to rise while consumption activities and individual incomes remained upbeat. Total electricity generation also grew during the review period.

Consumption

Consumer spending continues to remain buoyant, evident by the robust performance of net VAT collections, a partial indicator of spending. Net VAT collections totalled around \$74 million cumulative to February this year, an increase of around 18 percent over the comparable period last year.

Income

Consistent with favourable labour market conditions, Pay As You Earn (PAYE) collections, a partial indicator for individual incomes, noted an increase during the review period. Total PAYE collections, cumulative to February, amounted to around \$29 million, representing an increase of around 4 percent over the corresponding period last year.

Electricity

Electricity production continued on an upward trend. Cumulative to February, total electricity generated

was around 119 million-kilowatt hours (kwh), an increase of 8 percent over the comparable period last year.

Inflation

Inflation stood at 3.5 percent in February, compared with 2.9 percent in January. Over the month, consumer prices rose by 0.3 percent. During February, higher prices were recorded for services, food, alcoholic drinks & tobacco, and housing. Food prices rose mainly due to increase in prices of market items. Service costs increased largely due to higher charges for domestic and medical services. These were partially offset by declines in the costs of miscellaneous items, durable household goods and clothing & footwear, while prices of heating & lighting and transport remained unchanged.

Looking ahead, inflationary pressures from domestic factors may pick up slightly in the coming months, emanating largely from the proposed increase in bus and taxi fares. On the external front, the possibility of persistent higher crude oil prices has the potential to alter the current inflation forecast upwards. The outlook for year-end inflation remains at 4.5 percent. However, as mentioned earlier, if the proposed increase in transport costs does not come into effect, then the year-end inflation forecast would be around 3.5 percent.

Labour Market

Cumulative to February, over 2,900 new taxpayers were registered, representing a marginal decline on an annual basis. The decline was largely due to fewer registrations in the manufacturing, agriculture, forestry and fishing and the wholesale, retail trade, restaurants & hotels sectors, over the same period last year.

The community, social and personal services sector recorded the most new taxpayers. This was followed by the finance, insurance, real estate & business services; and wholesale, retail trade, restaurants & hotels sectors.

Financial Aggregates

Monetary indicators remained strong in January. During this period the total value of outstanding loans in the banking system increased by 19.9 percent to \$1.6 billion. This outcome was largely underpinned by higher lending to private individuals, real estate and wholesale & retail, hotels & restaurant sectors. Lending to public enterprises continued to increase as well. On the downside, lending to mining & quarrying, agriculture and central & local government

sectors contributed negatively to lending growth during the review period. Moreover, new loans by commercial banks stood at around \$57 million in January 2005, a decline of 33.9 percent over the previous month.

Provisional data indicates that broad money expanded at an annual rate of 17.4 percent at end-January 2005 (10.3% in December). The outturn was largely attributed to increases in narrow and quasi money, which in turn was influenced, by rises in demand deposits and savings deposit. Narrow money grew at an annual rate of 34.0 percent, while quasi money rose by 5.8 percent during the review period.

The determinants of broad money, comprising domestic credit and net foreign assets, grew by 12.1 percent and 6.9 percent respectively over the year. The increase in the former was spurred by higher credit to private sector, which rose by 18.6 percent.

During the review period, total outstanding deposits of commercial banks totaled \$2.0 billion, 0.7 percent lower than the previous month and 11.9 percent higher than the level a year ago. Higher demand deposits by private individuals and domestic business enterprises contributed to the increase in total deposits.

On the interest rates front, the weighted average lending rate of commercial banks decreased by 11 basis point to 6.92 percent at end-January 2005, while the weighted average commercial bank time deposit rate moved up by 1 basis point to 1.78 percent. The savings deposit rate remained at 0.36 percent during the review period.

Furthermore, interest rates on new lending rose by 65 basis points to 7.56 percent in January, with new loans extended at higher rates. The new deposit rate offered by commercial banks declined by 13 basis points to 1.30 percent over the month.

Exchange Rates

In February 2005, the performance of the Fiji dollar was mixed against the major currencies. Bilateral movements in the exchange rate showed that the Fiji dollar strengthened against the Yen (2.7 percent) and

the US dollar (1.0 percent) but weakened against the Australian (0.6 percent) and New Zealand dollar (0.5 percent), as well as Euro (0.5 percent).

The Nominal Effective Exchange Rate index¹ of the Fiji dollar fell by 0.2 percent in the year to February, indicating a depreciation of the Fiji dollar against the basket of currencies.

The Real Effective Exchange Rate (REER) index² of the Fiji dollar, a gauge of our international competitiveness, rose by 0.9 percent during the review period. The increase in the REER Index over the year reflects deterioration in our international competitiveness and was largely due to higher domestic inflation outcomes. Domestic inflation increased to 3.5 percent in February 2005, while average trading partner inflation was around 2.3 percent during the same period.

External sector

On the external front, latest accrual trade data showed that merchandise exports fell by 7.7 percent in 2004 compared with an increase of 6.6 percent in 2003. The decline in receipts was largely attributed to negative contributions from re-exports and sugar, which more than offset the positive contributions from other exports, gold, garments, textiles & footwear, and mineral water. However, domestic exports rose by 1.6 percent in 2004, compared with a decline of 0.1 percent in 2003. The increase in domestic exports was attributed to higher receipts recorded for gold and garments, textiles & footwear, which more than offset the decline in sugar receipts.

Merchandise imports fell by 0.4 percent last year, compared to a growth of 13.4 percent in 2003.³ The fall in import payments was attributed to declines in payments for investment goods (10.1 percent), and intermediate goods (1.6 percent), which more than

¹ The Nominal Effective Exchange Rate (NEER) index is the sum of the indices of each trading partner currency against the Fiji dollar, adjusted by their respective weight in the basket. Each weight reflects a trading partner's contribution to Fiji's total trade in goods and services. This index measures the overall movement of the Fiji dollar against the basket of currencies. An increase in this index indicates a slight appreciation of the Fiji dollar against the basket of currencies and vice versa

² The Real Effective Exchange Rate (REER) index is the sum of each component of the NEER index, adjusted by the relative price differential between Fiji and each of the major trading partners. This index measures the competitiveness of the Fiji dollar against the basket of currencies. A decline in the REER index indicates an improvement in Fiji's international competitiveness and vice versa.

³ Merchandise import excluding aircraft rose by 9.6 percent in 2004, compared to 3.1 percent in 2003.

offset the increase in consumption goods (7.7 percent). The decline in imports of investment goods was mainly underpinned by negative contribution from machinery & transport equipment, while the fall in mineral fuels and oil & fats underpinned the decline in intermediate goods. However, higher payments for consumption goods were largely

attributed to an increase in manufactured goods, food and miscellaneous manufactured goods.

At present, (22/03), reserves are estimated at around \$761million, sufficient to cover 3.3 months of imports of goods and non-factor services or 5.0 months of imports of goods only.

RESERVE BANK OF FIJI

FIJI: FINANCIAL STATISTICS

KEY INDICATORS	Feb-05	Jan-05	Dec-04	Feb-04
1. Money and Credit (year-on-year % change)				
Narrow Money	n.a.	33.99(p)	13.05(p)	-1.88
Currency in Circulation (monthly average)	10.64	12.45	11.35	12.79
Quasi-Money (Time & Saving Deposits)	n.a.	5.84(p)	8.07(p)	24.65
Domestic Credit	n.a.	12.08(p)	12.60(p)	14.95
2. Consumer Prices ^{1/} (year-on-year % change)				
All Items	3.5	2.9	3.3	1.8
Food	3.8	1.7	2.4	1.5
3. Reserves (end of period)				
Gross Foreign Reserves (\$m)	760.7	755.0	786.2	743.5
Months of Imports (goods & non factor services)	3.3	3.3	3.5	3.3
Months of Imports (goods)	5.0	5.0	5.3	5.0
4. Liquidity (end of period)				
Liquid Assets Margin to Deposit Ratio (%)	n.a.	11.6	14.1	15.6
Banks' Demand Deposits (\$m)	n.a.	72.3	101.0	80.5
5. Interest Rates (% p.a.) (monthly average)				
Lending Rate (Excluding Staff)	n.a.	6.92	7.03	7.30
Savings Deposit Rate	n.a.	0.36	0.36	0.44
Time Deposit Rate	n.a.	1.78	1.77	1.69
91-day RBF Note Rate (month end)	1.75	1.75	1.75	1.19
Minimum Lending Rate (MLR) (month end)	2.25	2.25	2.25	1.75
Overnight Inter-bank Rate	0.82	0.80	0.81	0.79
5-Year Government Bond Yield	2.64	n.i.	2.61	n.i.
10-Year Government Bond Yield	5.08	n.i.	5.03	n.i.
6. Exchange Rates ^{2/} (mid rates, F\$1 equals) (end of period)				
US dollar	0.6074	0.6011	0.6079	0.5910
Pound sterling	0.3166	0.3185	0.3159	0.3175
Australian dollar	0.7724	0.7770	0.7799	0.7665
New Zealand dollar	0.8420	0.8465	0.8465	0.8608
Swiss francs	0.7060	0.7136	0.6881	0.7494
Euro	0.4586	0.4611	0.4458	0.4753
Japanese yen	63.90	62.21	62.61	64.82
7. Commodity Prices (US\$) (monthly average)				
UK Gold Price/fine ounce ^{2/}	422.69	424.82	442.62	405.07
London Daily Sugar Price/tonne ^{3/}	265.37	261.18	261.87	185.69
Crude Oil/barrel ^{4/}	45.56	44.48	39.64	30.87
<p>n.a. - Not available/No activity n.i. - No issues n.t. - No trading</p> <p>Sources: ^{1/} Fiji Islands Bureau of Statistics ^{2/} Bloomberg and Reserve Bank of Fiji ^{3/} Fiji Sugar Marketing Company Limited ^{4/} Bloomberg</p>				