



# RESERVE BANK OF FIJI

## ECONOMIC REVIEW

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### OVERVIEW

World GDP growth this year remains projected at 4.3 percent. The global economic expansion is being led by the United States and Chinese economies. Strengthening global manufacturing and trade have so far offset the dampening effects from the high oil prices, as well as, from hurricanes Katrina and Rita in the US. Consistent with these favourable international developments, prospects for our major trading partners and selected non-Japan Asian economies (China, Hong Kong & Singapore) remain optimistic. Nonetheless, further increases in oil prices could upset the current momentum in global economic growth.

On the domestic front, consumer demand has remained relatively firm, supported by strong credit growth. A low interest rate environment also continues to provide the stimulus for investment growth. On the contrary, net exports continue to drag down overall aggregate demand growth, as well as depress foreign reserves levels.

From a production standpoint, developments in the real sector remained mixed during the review period. On an annual basis, positive contributions were noted from cane, sugar, copra and electricity production. The construction sector also performed robustly, evident from the relatively higher value of work put-in-place in the first half of this year. However, on the downside, gold output remained weak during the review period.

Inflation was 1.7 percent in September, compared with 2.2 percent in August. The year-end inflation forecast is now at around 3.0 percent, as an increase in transportation cost is not expected to filter through this year. Looking further ahead, inflation in the medium term could rise if the indirect effects of the current high oil prices intensify. Moreover, if an

increase in transportation cost eventuates next year, this could raise inflation further.

Over the month, developments in monetary and credit conditions remained strong. In the year to August, broad money rose by 15.4 percent<sup>1</sup> attributed to an increase in all forms of deposits. On the demand side, domestic credit rose by 22 percent, fuelled primarily by a 24.3 percent growth in private sector credit. This growth in private sector credit has been aided largely by the 23.5 percent expansion in commercial bank lending during the 8 month period, the highest growth level recorded in the last 6 years. Lending by Licensed Credit Institution (LCIs) also grew strongly by 15.2 percent, with the major beneficiaries again being private individuals and the real estate sector.

On the interest rate front, both the time deposits and savings deposit rates remained unchanged at 1.81 percent and 0.40 percent respectively, while the weighted average lending rate fell by 9 basis points over the month to 6.68 percent. A similar trend has been noted for new lending rate, which declined by 57 basis points to 6.87 percent. Overall, weighted average commercial bank rates are still declining.

On the labour market, partial indicators continue to point to a slowdown in employment growth. Cumulative to September, new taxpayer registrations with the Fiji Islands Revenue and Customs Authority (FIRCA) declined by around 18 percent. During the September quarter, active compulsory membership of the Fiji National Provident Fund (FNPF) also fell by around 4 percent. However, the results of the recent Reserve Bank's Fiji Employers Federation (FEF) Expectations Survey indicate that employment is expected to pick up in the coming months, as the

<sup>1</sup> Percentages are reported as annual growth rates, unless stated otherwise.

economy regains momentum. Reflecting this pattern of demand for labour, wage growth is likely to rise moderately in the medium term.

On the external trade front, the Overseas Exchange Transactions (OET) data showed that cumulative to August, merchandise exports fell by around 17 percent; largely attributed to negative contributions from textiles, clothing & footwear, sugar, fish, merchanted goods, other re-exports and other exports. Conversely, merchandise imports rose by around 12 percent, underpinned by positive growth in the imports of investment, intermediate and consumption goods.

Foreign reserves are expected to remain at adequate levels this year. Official reserves at the end of September stood at around \$940 million, sufficient to cover 3.9 months of imports of goods and non-factor services, or 5.3 months of imports of goods only.

## **SECTORAL DEVELOPMENTS**

Real sector developments have been generally mixed during the first nine months of the year. Cumulative to September, output in the cane and sugar industries grew by 21 and 19 percent respectively. The construction sector also performed strongly, driven in large part by private sector tourism-related projects. Copra production also rose over the year, while Gold output has remained depressed.

### **Cane and Sugar**

The cane & sugar industries registered good performance, achieving substantial levels of output during the first four crushing months. The Fiji Sugar Corporation's (FSC) recent mill report indicates that around 2.0 million tonnes of cane was crushed during June to September this year, representing an annual increase of 21 percent. The relatively early start to the season this year, steady cane supply to the mills and lower number of mill breakdowns contributed to the improved performance from 2004 levels.

Consistent with the good harvest thus far, sugar production totalled 206,000 tonnes, around 19 percent higher than the level recorded over the previous comparable period. The Tonnes Cane to Tonnes Sugar ratio was around 9.7:1, slightly higher than the ratio of 9.5:1 recorded over the same period last year.

### **Copra**

Copra production remained favourable. Latest statistics from the Coconut Industry Development

Authority (CIDA) show that cumulative to August, copra production amounted to around 8,000 tonnes, representing an increase of 10 percent over the corresponding period last year.

### **Building & Construction**

The construction sector continues to perform robustly, evident by the value of work put-in-place. According to the June Quarter Building and Construction Survey<sup>2</sup> report released by Fiji Islands Bureau of Statistics, around \$116 million was spent on capital works during the first half of this year, a strong increase of 74 percent on an annual basis. Looking at the categories, in the year to June, the total value of work put-in-place by the private sector rose significantly by 106 percent (\$90m), followed by the public sector recording an increase of 14 percent (\$26m) during the review period.

### **Gold**

Gold production remains weak. Total gold output, cumulative to September this year, amounted to around 70,000 ounces, 29 percent lower than the corresponding level in 2004. According to industry sources, the mine faces some major challenges and output is expected to fall dramatically this year. Similarly, earnings declined on an annual basis by 26 percent to \$50.3 million.

### **Inflation**

The inflation rate in September was 1.7 percent, compared with 2.2 percent recorded in August. Over the month, consumer prices rose by 0.2 percent, underpinned by higher prices of transport, heating & lighting, and alcoholic drinks & tobacco. The underlying measure of inflation, the trimmed mean, was 1.3 percent in September, unchanged from the previous month.

Inflation continues to remain low despite high crude oil prices. This favourable outcome is mainly due to several key factors. While the direct effects of stronger oil prices are reflected in retail prices of domestic fuel, the knock-on effects have been largely benign. Lower prices of domestically produced goods and services are also suppressing consumer prices.

In the coming months, inflation is likely to gather pace in view of the possible shortage of primary produce due to the recent flash floods. Further, the approaching festive season is likely to boost demand for locally produced goods and thus nudge prices

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<sup>2</sup> The survey covers all private sector enterprises operating in the private and public sectors of the construction sector.

higher. These implications are adequately factored in the current inflation outlook, and as such, the year-end inflation forecast remains unchanged at around 3.0 percent. Looking further ahead, inflation in the medium term may rise if the indirect effects of the current high oil prices intensify.

### **Labour Market**

Partial indicators continue to point to a softening in labour market conditions. During the January-September period, around 5,500 individuals were registered as taxpayers with FIRCA, representing a fall of around 18 percent over the year. To date, the community, social and personal services sector has recorded the highest number of new taxpayers this year, followed by the finance, insurance, real estate & business services sector; wholesale, retail trade, restaurants & hotels sector; manufacturing sector and construction sector.

Over the September quarter, active compulsory membership of the FNPF also fell by around 4 percent. Cumulative to September this year, an aggregate of almost 9,300 individuals were registered as compulsory members with FNPF.

There are, however, some positive market signals concerning employment growth in the coming months. The Reserve Bank's Survey of Job Advertisements for the September quarter, showed an increase in advertised vacancies by around 18 percent. Recruitment intentions were highest in the community, social & personal services sector, followed by the wholesale & retail trade, restaurants & hotels; finance, insurance, real estate & business services; transport storage & communication sectors, and construction based companies.

Furthermore, the Reserve Bank's recent FEF Expectations Survey, suggested a net<sup>3</sup> of around 65 and 59 percent of the respondents expected permanent and temporary employment, respectively, to increase over the next 12 months (from September 2005). The majority of survey respondents also expected wages to increase, within a range of 0 to 5 percent, over the same 12 month period.

### **Monetary & Credit Aggregates**

Broad money rose by a further 15.4 percent in the year to August, following an increase of 16.2 percent in July. The strong growth has been underlined by a

general preference for more liquid forms of money, with large increases in demand deposits (31.3 percent) observed during the period. Some of the broad money expansion also stemmed from growth of the other less liquid forms of deposits, namely, savings deposits (11.0 percent) and time deposits (10.7 percent).

Looking at the demand for funds, total domestic credit rose by a further 22.0 percent over the year in August, following an equally strong increase of 20 percent recorded in July. This performance was fuelled primarily by private sector credit, which grew by 24.3 percent. The growth in private sector credit was in line with higher commercial bank lending, which rose by 23.5 percent, representing the highest annual growth recorded in six years. For the first three quarters of this year, the three main drivers of this strong growth momentum have been private individuals, the wholesale & retail trade & hotels & restaurants and real estate sectors.

Aiding the credit momentum in Fiji is the credit activities of LCIs. Loans disbursed by LCIs rose by 15.2 percent in the year to August, following a similar increase of 15.2 percent in July. As with commercial banks, the major recipients of LCIs loan disbursements were private individuals and the real estate sector. As housing market loans typically fall under the private individuals and real estate categories, their robust credit growth is an indicator of the strong level of competition amongst commercial banks and LCIs in the booming housing market.

Looking closely at new loans disbursed by both commercial banks and LCIs, it is evident that there is still a strong demand for credit in the economy. Cumulative to August, new loans disbursed by commercial banks increased by 31.7 percent over the year, to \$591.5 million. The main driver for new loans growth amongst commercial banks were private individuals, followed by the electricity, gas & water and manufacturing sectors. Similarly, LCI's cumulative new loans rose by 5.2 percent in the year to August, to \$91.8 million from \$87.3 million recorded during the same period in 2004. Again, private individuals partially underpinned this increase with added impetus from the real estate and building & construction sectors.

Since loans disbursed to private individuals have been a consistent driver of overall lending, this category deserves some attention. Private individuals are the largest category to which commercial banks lend, currently holding 33.2 percent (\$608.8 million) of all outstanding commercial bank loans and advances as

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<sup>3</sup> Net is calculated by subtracting the number of respondents expecting a decrease from the number of respondents expecting an increase.

at the end of August. Within the private individuals' category are three main sub-categories which include, *housing*, *personal transport* and *others*. The largest disbursements are made for *housing* (\$483.6 million) and the *others* (\$100.6 million) sub-categories. The *others* sub-category mainly includes consumer loans (travel, education, home appliances etc) and credit card debt. While both these sub-categories have been showing consistent annual growth since 2002, it has mainly been the *housing* loans that have been driving the demand for credit. In August, commercial bank loans for private individuals *housing* rose by 22.9 percent over the year, while the *others* sub-category increased by 5.2 percent in the same period.

On the supply side, total commercial bank deposits rose by 17.7 percent in the year to August 2005 to around \$2.3 billion, following a growth of 17.3 percent in July. The increase reflected mainly higher placements by private sector business enterprises and private individuals in demand deposits and savings deposits. On a monthly basis, total commercial bank deposits also rose by 2.7 percent underpinned by rises in demand deposits of statutory bodies.

Total LCI's deposits increased to \$146.1 million, representing an over the year rise of 19.2 percent. The growth in deposits was largely underpinned by an increase in time deposit placements by private individuals and non-bank financial institutions. Over the month, LCIs total deposits rose by 2.6 percent, mainly supported by private individuals' time deposit placements.

### **Interest Rates**

Interest rate movements stabilised somewhat in August. Both the weighted average commercial bank time deposit rate and savings deposit rate remained unchanged at 1.81 percent and 0.40 percent, respectively. The commercial bank lending rate, however, fell over the month to 6.68 percent by 9 basis points. The prevailing low lending rates continue to provide impetus to the strong credit demand. This trend is continuing with interest rates on new loans and advances also recording a decline (by 57 basis points) in August to 6.87 percent.

Lending interest rates offered by LCIs are also on a downward trend, serving as an indicator of the growing level of credit competition between LCIs and commercial banks. The weighted average LCI lending rate fell in August by 2 basis points to 11.41 percent. However, the lending rate on new loans disbursed by LCIs rose by 52 basis points to 12.48 percent. In terms of deposits, the weighted average

time deposit rates for LCIs fell to 4.12 percent by 2 basis points. On the other hand, the weighted average deposit rates on new time deposits for LCIs rose by 41 basis points to 3.43 percent.

### **External sector**

On the external front, latest OET data showed that, cumulative to August, merchandise exports fell by around 17 percent, compared with an increase of around 14 percent in the corresponding period last year. The decline in receipts was largely attributed to negative contributions from textiles, clothing & footwear, sugar, fish, merchanted goods, other re-exports, and other exports, which more than offset the positive contributions from re-exports of mineral fuel and ginger.

During the same period, merchandise imports rose by around 12 percent, compared to a growth of around 17 percent in the corresponding period in 2004. The increase in import payments was due to positive contributions from all categories; investment goods (5.8 percent), intermediate goods (5.4 percent), and consumption goods (1.1 percent). The growth in investment goods was underpinned by the increase in payments for machinery & electrical equipment and chemicals, while the rise in intermediate goods was largely made up of increases in imports of mineral fuels. The higher payment for consumption goods was largely attributed to the increase in contribution from other imports, duty free goods and government imports.

### **Exchange Rates**

Bilateral movements in exchange rates reveal that the Fiji dollar generally strengthened against the currencies of our major trading partner countries in September. The domestic currency appreciated against the yen (1.87 percent), euro (1.83 percent), NZ dollar (0.08 percent), and US dollar (0.33 percent), while it depreciated against the Australian dollar (1.25 percent).

In September, the Nominal Effective Exchange Rate (NEER) index of the Fiji dollar rose by 0.03 percent over the previous month, indicating a slight appreciation of the Fiji dollar against the basket of currencies. The Real Effective Exchange Rate (REER) Index of the Fiji dollar fell by 0.1 percent during the same period. The decline in the REER Index reflects an improvement in the international competitiveness of our exports, and was largely due to the lower domestic inflation outcomes.

## **RESERVE BANK OF FIJI**

## FIJI: FINANCIAL STATISTICS

<b>KEY INDICATORS</b>	<b>Sep-05</b>	<b>Aug-05</b>	<b>Jul-05</b>	<b>Sep-04</b>
<b>1. Money and Credit</b> (year-on-year % change)				
Narrow Money	n.a.	20.57	23.47	21.10
Currency in Circulation (monthly average)	10.41	8.88	9.14	13.45
Quasi-Money (Time & Saving Deposits)	n.a.	10.83	10.10	7.78
Domestic Credit	n.a.	21.98	20.00	11.23
<b>2. Consumer Prices</b> <sup>1/</sup> (year-on-year % change)				
All Items	1.7	2.2	2.8	3.4
Food	-0.1	1.8	3.3	5.1
<b>3. Reserves</b> (end of period)				
Gross Foreign Reserves (\$m)*	939.5	967.1	962.3	998.4
Months of Imports (goods & non factor services)	3.9	4.1	4.0	4.5
Months of Imports (goods)	5.3	5.5	5.5	6.8
<b>4. Liquidity</b> (end of period)				
Liquid Assets Margin to Deposit Ratio (%)	n.a.	10.7	11.4	12.8
Banks' Demand Deposits (\$m)	n.a.	108.4	127.0	87.1
<b>5. Interest Rates (% p.a.)</b> (monthly average)				
Lending Rate (Excluding Staff)	n.a.	6.68	6.77	7.11
Savings Deposit Rate	n.a.	0.4	0.40	0.35
Time Deposit Rate	n.a.	1.81	1.81	1.77
91-day RBF Note Rate (month end)	1.75	1.75	1.75	1.75
Minimum Lending Rate (MLR) (month end)	2.25	2.25	2.25	2.25
Overnight Inter-bank Rate	1.45	1.27	1.00	1.02
5-Year Government Bond Yield	2.77	2.73	2.74	2.58
10-Year Government Bond Yield	5.39	5.34	5.30	4.90
<b>6. Exchange Rates</b> <sup>2/</sup> (mid rates, F\$1 equals) (end of period)				
US dollar	0.585	0.5831	0.5848	0.5710
Pound sterling	0.3820	0.3264	0.3330	0.3173
Australian dollar	0.7697	0.7794	0.7692	0.7966
New Zealand dollar	0.8467	0.8461	0.8546	0.8526
Swiss francs	0.7563	0.7398	0.7517	0.7188
Euro	0.4858	0.4771	0.4818	0.4629
Japanese yen	66.11	64.89	65.56	63.31
<b>7. Commodity Prices (US\$)</b> (monthly average)				
UK Gold Price/fine ounce <sup>2/</sup>	454.23	437.74	424.86	404.89
London Daily Sugar Price/tonne <sup>3/</sup>	278.12	264.22	266.60	223.02
Crude Oil/barrel <sup>4/</sup>	62.98	64.09	57.58	43.40
<p>n.a. - Not available/No activity  n.i. - No issues  n.t. - No trading  * Official reserves includes foreign reserves holdings of the RBF and Non-Bank Financial Institution, as per the new definition of official reserves</p> <p>Sources: <sup>1/</sup> Fiji Islands Bureau of Statistics  <sup>2/</sup> Bloomberg and Reserve Bank of Fiji  <sup>3/</sup> Fiji Sugar Marketing Company Limited  <sup>4/</sup> Bloomberg</p>				