



RESERVE BANK OF FIJI

ECONOMIC REVIEW

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OVERVIEW

Growth prospects remain positive for all our major trading partner countries and selected Asian (China, Hong Kong & Singapore) economies this year. However, the growth projections for this year are lower, when compared to 2006, for most of these countries. The exceptions are Australia, which expects higher growth, and New Zealand, which anticipates a growth level similar to 2006. Crude oil prices have fallen from a peak of US\$78 per barrel in August 2006 to current levels of around US\$55, while sugar prices are around US12 cents per pound when compared to the highs of US19 cents in the first quarter of last year.

Domestically, economic growth in 2006 was adversely affected by a slowdown in the tourism industry as well as the closure of the Emperor Gold Mining Company Limited (EGM) in early December. The visitor arrivals projection for 2006 has been downgraded from 576,000 to 540,000, and as a result, growth in related industries will be affected. The closure of the gold mine on 5 December caused the mining & quarrying sector to decline by 49 percent, in the year to December. Taking into account the political situation in the final months of last year and the closure of the gold mine, economic growth estimated for 2006 is likely to be slightly lower than the previous forecast of 3.6 percent.

Inflation in December stood at 3.1 percent, compared with 3.5 percent (revised) in November. On a monthly basis, consumer prices rose by 0.8 percent. The underlying measure of inflation, the trimmed mean, remained unchanged at 1.9 percent on an annual basis.

Employment conditions deteriorated for certain sectors of the economy during the last two months of 2006. Political tensions caused a slowdown in tourist arrivals, forcing some major resorts and hotels to lay

off casual and part-time employees. Some permanent employees in hotels are also working on reduced hours. Further exacerbating the negative labour market impact was the announced closure of the EGM and the ensuing loss of employment for around 1,800 people.

Nevertheless, it appears that the fall in employment was mainly within the hotel and mining sectors. Cumulative to December, around 7,200 taxpayers were registered with the Fiji Islands Revenue & Customs Authority (FIRCA), representing an annualised increase of around 20.0 percent.

However, the recent political developments stalled recruitment intentions in several sectors during the quarter. The December Survey of Job Advertisements registered a decline of around 13.0 percent over the comparable period last year.

Commercial banks' credit rose by 21.4 percent in the year to December following a growth of 23.9 percent in the previous month. The growth was underpinned by higher commercial bank credit disbursements to private individuals (mainly for housing purposes) and the building & construction, real estate, manufacturing and wholesale & retail trade sectors. Credit outstanding for consumption purposes rose by 10.9 percent on an annual basis, but fell by 1.0 percent over the month. Investment loans outstanding also increased, rising by 59.7 percent during the review period, to \$415.5 million.

Lending by Licensed Credit Institutions (LCIs) also rose in the year to December, increasing by 14.3 percent (to \$320.7 million) after a growth of 17.5 percent in the previous month. The increase was underpinned by higher lending for the real estate sector and to private individuals.

Interest rates generally rose during the review period. Both the commercial banks' time and savings deposit rates increased by 106 basis points and 3 basis points to 9.05 percent and 0.84 percent, respectively. The commercial bank lending rate fell over the month by 21 basis points to 7.89 percent. Moreover, interest rates on new deposits rose by 150 basis points to 12.41 percent, while the interest rate on new loans extended by commercial banks fell by 94 basis points to 9.75 percent. Additionally, banks were offering as much as 14 percent to wholesale depositors in December. Similar trends emerged from LCIs. In December, the interest rate on new deposits rose to 12.11 percent from 10.47 percent in November.

Exports continue to show dismal performance. Latest Overseas Exchange Transactions (OET) data showed that cumulative to October this year, merchandise export earnings fell by around 4.7 percent, compared with a decline of around 11.4 percent in the corresponding period in 2005. Excluding sugar, however, merchandise export earnings rose by around 1 percent, compared to a fall of around 20.0 percent in the same period in 2005.

During the same period, merchandise import payments rose by around 11.6 percent cumulative to October this year, compared to a growth of around 10.6 percent in the corresponding period in 2005. The higher import payments continue to be evident in all categories: investment goods (5.0 percent), consumption goods (4.3 percent) and intermediate goods (2.2 percent).

The 2006 year-end official foreign reserves level was \$823 million (provisional), sufficient to cover 3.3 months of goods imports.

SECTORAL DEVELOPMENTS

Performances of most sectors of the economy were upbeat in the last few months of 2006, with the sugar, tourism, electricity and building & construction industries recording higher outcomes. On the downside, however, gold output fell sharply on an annual basis.

Gross Domestic Product

Economic growth estimated for 2006 is expected to be affected by the slowdown in the tourism industry as well as the closure of the EGM in early December. The visitor arrivals projection for 2006 has been downgraded from 576,000 to 540,000, and as a result, the wholesale & retail trade and hotels & restaurants industries are now estimated to have expanded by less than originally envisaged. The closure of the

Vatukoula gold mine by EGM on 5 December will cause the mining & quarrying sector to register a stronger decline of 49 percent, when compared with a 44 percent contraction anticipated in October. The economic growth projection for 2006 is likely to be slightly lower than the previous forecast of 3.6 percent.

Cane and Sugar

The sugar industry registered a good performance up to December 2006. Mill reports indicate that around 3.2 million tonnes of cane was crushed up to the end of December last year, representing an annual growth of 9.3 percent. The Tonnes Cane to Tonnes Sugar ratio was around 10.4, slightly higher than 9.7 recorded during the corresponding period in 2005, indicating that the quality of cane had worsened.

Sugar production amounted to around 307,000 tonnes, representing a growth of 2.0 percent on an annual basis.

Tourism

According to provisional data from the Fiji Islands Bureau of Statistics (FIBOS), the tourism industry recorded a modest performance up to the third quarter of 2006. Visitor arrivals in the first nine months totalled around 419,000, representing a 0.9 percent growth on an annual basis. In addition, provisional tourism earnings for the first three quarters of 2006 totalled \$555.2 million, 1.9 percent higher than the \$544.6 million recorded in the corresponding period of 2005.

More recently, travel advisories issued by certain Governments following the political events of December 2006 slowed the flow of visitors to Fiji. This resulted in the loss of jobs for some casual workers and reduced hours for permanent staff at various tourist establishments in the country.

Industry stakeholders re-activated the Tourism Action Group (TAG) in December 2006 – first formed in the aftermath of the 2000 crisis – in a bid to revive visitor arrivals to Fiji and take the industry forward into 2007. The TAG comprises hoteliers, airline companies, tour operators and the Fiji Islands Visitors Bureau.

The TAG's recovery plan involved extensive marketing in the two major markets of Australia and New Zealand, targeted at improving the relatively low hotel occupancy rates for the final quarter for 2006 and increasing the forward bookings for the first quarter of 2007. In particular, the TAG's marketing

plan centred on a 40 percent discount on wholesale contract rates offered by hotels, resorts and other operators coupled with a child's fare initiative by Air Pacific Limited of \$199 (tax inclusive).

The TAG's entire marketing campaign is likely to cost around \$5 million. Similar campaigns are expected for Japan, North America and other significant Asian markets, as the TAG aims to restore visitor arrival numbers to pre-December 2006 levels by mid-2007.

Building & Construction

The construction sector continued to perform robustly, evident by the value of work put-in-place. According to the September 2006 Building and Construction Survey¹ report released by FIBOS, around \$242 million was spent on capital works during the first nine months of last year, a significant increase of 30.0 percent on an annual basis.

By categories, in the year to September, the value of work put-in-place by the private sector significantly rose by 37 percent (to \$195 million), followed by the public sector recording an increase of 9 percent (to \$47 million).

Electricity

Electricity production continue to indicate increases in economic activity. Cumulative to December, total electricity generated by the Fiji Electricity Authority was around 737,399 mega watt hours (Mwh), an increase of 7.7 percent on an annual basis.

Labour Market

Employment conditions deteriorated for certain sectors of the economy during the last two months of 2006. Political tensions during the review period caused a slowdown in tourist arrivals and hence forced some major resorts and hotels to lay off casual and part-time employees. It was also reported that some permanent employees in hotels were working on reduced hours. Further exacerbating the negative impact on the labour market was the announced closure of the EGM Company and the ensuing loss of employment for around 1,800 people in December 2006.

Nevertheless, indications are that the fall in employment was mainly within the hotel and mining sectors and did not become a systemic problem that affected the other sectors of the economy. Cumulative to December, around 7,200 taxpayers were registered

with the FIRCA, representing an annualised increase of around 20.0 percent. The highest number of new taxpayers so far have been registered in the community, social & personal services sector followed by the wholesale, retail trade, restaurants & hotel; finance, insurance, real estate & business services; manufacturing; transport, storage & communications and construction sectors.

However, the recent developments had the effect of stalling recruitment intentions in several sectors during the quarter. The December Survey of Job Advertisements registered a decline of around 13.0 percent over the comparable period last year. Subdued recruitment intentions were noted largely in the mining & quarrying, manufacturing; agriculture, forestry & fishing; construction; finance, insurance, real estate & business services; electricity & water and transport, storage & communication sectors.

Inflation

Inflation in December stood at 3.1 percent compared with 3.5 percent (revised) in November. On a monthly basis, consumer prices rose by 0.8 percent. This was led by higher prices of food, durable household goods, clothing & footwear, alcoholic drinks & tobacco, housing and miscellaneous items. Costs of heating & lighting, transport and services remained unchanged. The higher cost of food items was largely underpinned by higher prices of market items and some bakery and wheat products while the rise in cost of clothing & footwear was due to marginal price increases in men's & women's wear, fabric material and women's & children's footwear. The increase in prices of durable household goods on the other hand, was mainly due to an increase in prices of furniture, soft furnishings, jewellery and garden tools. Likewise, the growth in housing costs was driven by higher private house rent and an increase in the cost of some repair items.

The underlying measure of inflation, the trimmed mean, remained unchanged at 1.9 percent on an annual basis.

Upward price pressures are likely to remain given possible supply side constraints for market items. This is expected to be further supported by the possible rise in cost of services as this subgroup is surveyed once every year during January by the FIBOS. However, these could be partially offset by lower domestic fuel prices as indications suggest that a decline is expected from the current Prices and Incomes Board bi-monthly review.

¹ The survey covers all private sector enterprises operating in the private and public sectors of the construction industry.

Monetary and Financial Developments

• Lending

Commercial banks' credit rose by 21.4 percent in the year to December following a growth of 23.9 percent in the previous month. The growth was underpinned by higher commercial bank credit disbursements to private individuals (mainly for housing purposes) and the building & construction, real estate, manufacturing and wholesale & retail trade sectors.

The annual growth rate of credit outstanding for consumption purposes rose by 10.9 percent during the review period. Investment lending outstanding of commercial banks also increased, rising by 59.7 percent during the review period to \$415.5 million.

Lending by LCIs also rose in the year to December, increasing by 14.3 percent to \$320.7 million after a growth of 17.5 percent in the previous month. The increase was underpinned by higher lending to the real estate sector and to private individuals.

• Deposits

Total commercial bank deposits rose by 19.9 percent (\$474.5 million) in the year to December 2006 to around \$2.9 billion, following a growth of 18.8 percent in November. The outturn was underpinned mainly by higher time deposits which rose by 81 percent (\$581 million) to around \$1.3 billion on the back of higher interest rates offered by commercial banks on term deposits. Of the total deposit in December, time deposits accounted for 45.3 percent, demand deposits 33.3 percent and savings deposits 21.4 percent. On a monthly basis, total commercial bank deposits rose by 2.9 percent.

• Interest Rates

Interest rates generally rose during the review period. Both the commercial banks' time and savings deposit rates increased by 106 basis points and 3 basis points, to 9.05 percent and 0.84 percent, respectively. The commercial bank lending rate fell over the month by 21 basis points to 7.89 percent. Moreover, interest rates on new deposits rose by 150 basis points to 12.41 percent while the interest rate on new loans extended by commercial banks fell by 94 basis points to 9.75 percent. Additionally, banks were offering as much as 14 percent to wholesale depositors in December.

Similar trends emerged from LCIs. In December, the interest rate on new deposits rose to 12.11 percent from 10.47 percent in November. This denotes an

increase of 164 basis points in December, emerging from attractive rates offered by credit institutions.

External sector

Latest OET data showed that cumulative to October this year, merchandise export earnings fell by around 4.7 percent, compared with a decline of around 11.4 percent in the corresponding period in 2005. Excluding sugar, merchandise export earnings rose by around 1 percent, compared to a fall of around 20.0 percent in the same period in 2005.

Leading the decline in receipts were re-exports excluding mineral fuels, sugar, ginger, fish, and mineral water. On the other hand, sectors recording significant increases were textiles, timber, gold, copra, re-export of mineral fuels, merchanted goods and other exports.

During the same period, merchandise import payments rose by around 11.6 percent, compared to a growth of around 10.6 percent in the corresponding period in 2005. The higher import payments continue to be evident for all categories: investment goods (5.0 percent), consumption goods (4.3 percent) and intermediate goods (2.2 percent).

Higher outflows for investment goods were largely underpinned by machinery & electrical equipment. The growth in consumption goods payments was largely attributed to increases in outflows for transport equipment and duty free goods. For intermediate goods, the higher outlays were led by mineral fuels and raw materials.

Exchange Rate Developments

On the domestic front, movements in exchange rates reveal that at the end of 2006, the Fiji dollar strengthened against the US dollar (4.9%), New Zealand dollar (1.3%), and the Yen (5.8%), but weakened against the Aussie (2.8%) and the Euro (5.5%).

The Nominal Effective Exchange Rate Index of the Fiji dollar rose marginally by 0.1 percent in the year to December 2006, and the Real Effective Exchange Rate Index of the Fiji dollar, a gauge of our international competitiveness, also rose by 0.6 percent during the same period. The increase in the latter during the review period indicates a deterioration in our international competitiveness and was largely due to the higher domestic inflation outcome.

RESERVE BANK OF FIJI

FIJI: FINANCIAL STATISTICS

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KEY INDICATORS	Dec-06	Nov-06	Oct-06	Dec-05
1. Money and Credit (year-on-year % change)				
Narrow Money	n.a.	-8.37	-7.59	17.59
Currency in Circulation (monthly average)	5.70	7.49	9.34	11.67
Quasi-Money (Time & Saving Deposits)	n.a.	40.79	35.74	12.76
Domestic Credit	n.a.	27.96	25.39	26.59
2. Consumer Prices ^{1/} (year-on-year % change)				
All Items	3.1	3.5	4.6	2.7
Food	3.3	4.6	4.5	3.1
3. Reserves (end of period)				
Gross Foreign Reserves (\$m)*	823.2	805.9	840.0	822.4
Months of Imports (goods)	3.3	3.3	3.4	4.0
4. Liquidity (end of period)				
Liquid Assets Margin to Deposit Ratio (%)	6.2	4.5	4.0	8.3
Banks' Demand Deposits (\$m)	107.3	71.2	48.3	71.5
5. Interest Rates (% p.a.) (monthly average)				
Lending Rate (Excluding Staff)	7.89	8.10	7.80	6.63
Savings Deposit Rate	0.84	0.81	0.82	0.40
Time Deposit Rate	9.05	7.99	7.19	2.03
91-day RBF Note Rate (month end)	n.i.	n.i.	4.25	2.25
Minimum Lending Rate (MLR) (month end)	5.25	5.25	5.25	2.75
Overnight Inter-bank Rate	5.28	5.64	5.36	2.09
5-Year Government Bond Yield	n.i.	n.i.	n.i.	3.07
10-Year Government Bond Yield	10.75	n.i.	9.94	5.65
6. Exchange Rates ^{2/} (mid rates, F\$1 equals) (end of period)				
US dollar	0.6009	0.5950	0.5861	0.5731
Pound sterling	0.3062	0.3058	0.3081	0.3324
Australian dollar	0.7605	0.7593	0.7611	0.7827
New Zealand dollar	0.8521	0.8764	0.8792	0.8409
Swiss francs	0.7344	0.7196	0.7315	0.7525
Euro	0.4570	0.4524	0.4605	0.4837
Japanese yen	71.45	69.23	68.81	67.53
7. Commodity Prices (US\$) (monthly average)				
UK Gold Price/fine ounce ^{2/}	630.19	626.07	586.76	509.34
London Daily Sugar Price/tonne ^{3/}	12.47	12.35	12.07	356.18
Crude Oil/barrel ^{4/}	62.31	58.48	58.36	56.75
<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: ^{1/} Fiji Islands Bureau of Statistics ^{2/} Bloomberg and Reserve Bank of Fiji ^{3/} Fiji Sugar Marketing Company Limited ^{4/} Bloomberg</p>				