



# RESERVE BANK OF FIJI

## ECONOMIC REVIEW

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04

April 2005

### OVERVIEW

Global economic and financial conditions stayed unchanged over the month. Growth outlook for our trading partners and selected non-Japan Asian Countries (China, Hong Kong and Singapore) remains favourable. The International Monetary Fund's (IMF) latest World Economic Outlook maintains the forecast for this year's world growth at 4.3 percent. However, soaring international oil prices pose some downside risk to this assessment. In the currencies market, the US dollar strengthened against major currencies, after the Federal Reserve Bank raised its interest rate to curb future inflation. The stronger US dollar weakened gold prices, and sugar prices declined on expectations of higher supply.

Domestically, economic activity is expected to slow down this year. From an aggregate expenditure point of view, consumer spending is again likely to be the principal driver for growth in 2005, with VAT collections in the first quarter rising by 14 percent.<sup>1</sup> Latest data confirms that the construction sector performed really well last year, as \$160 million was spent on capital works. Moreover, prospects for the sector look promising, given that several major projects have or are about to commence. Other real sector developments revealed a rise in copra, while gold output remain depressed.

Labour market conditions continue to hold up well. This is evidenced by partial indicators of employment as well as survey data. Cumulative to March, 4,300 new taxpayers were registered. Moreover, the Reserve Bank's Survey of Job Advertisements, conducted at the end of the March quarter, reported a rise in firms' recruitment intentions by 21 percent. Looking ahead, Reserve Bank's Fiji Employers Federation (FEF) Expectations Survey conducted in

March also predict growth in employment over the next twelve months. On wage expectations, the Survey largely suggests wage growth of between 0 to 5 percent.

On the fiscal front, provisional data from the Ministry of Finance show an improvement in Government's fiscal position. The underlying deficit for 2004 equated to 3.3 percent of GDP, compared with a shortfall of 4.8 percent of GDP estimated earlier. The better-than-expected outcome was due to improved revenue collections and lower capital expenditure. For this year, deficit is expected to be around 4.3 percent of GDP.

Inflation stood at 3 percent in March, compared with 3.5 percent in February. Reduction in domestic fuel costs and seasonal fall in food prices led to the lower inflation rate in March. However, during the March quarter, the Building Material Price Index, which measures costs on construction materials, rose by 8.1 percent; a similar magnitude was recorded in the preceding quarter. Higher prices of building materials can partially be attributed to the strong construction activity.

In February, total value of outstanding loans increased by 19 percent (\$1.6 billion). This was largely underpinned by higher lending to private individuals, real estate and wholesale & retail, hotels & restaurant and manufacturing sectors. Moreover, new loans amounted to \$71 million, an increase of around 19.8 percent. On the supply side, outstanding deposits with commercial banks expanded by 9 percent to around \$2 billion. The weighted average lending rate of commercial banks was 6.92 percent and the time and savings deposit rate were 1.77 percent and 0.36 percent, respectively. However, interest rate on new loans offered by commercial banks have decreased by

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

53 basis points over the month to 7.03 percent. In contrast, the new deposit rate rose by 29 basis points to 1.59 percent.

Overseas Exchange Transactions (OET) data showed that cumulative to February, merchandise exports contracted by 40 percent. The decline in receipts was largely attributed to negative contributions from sugar, textiles, clothing & footwear, fish, merchanted goods, other exports and gold, which more than offset positive contributions from ginger and re-exports of mineral fuels. On the flip side, merchandise imports fell by around 0.3 percent. The lower import payment was attributed to declines in payments for consumption goods, which more than offset the increase in investment goods and intermediate goods.

As at April, reserves were estimated at around \$725 million, sufficient to cover 3.1 months of imports of goods and non-factor services or 4.8 months of imports of goods only.

## **SECTORAL DEVELOPMENTS**

Domestically, sectoral developments were generally positive during the review period. Consumption remained robust, while individual incomes continued to improve over the year. Latest data also indicates that the construction sector performed well last year. The copra and electricity industries noted annual growth during the review period, while the output in the gold industry remained weak. On the fiscal front, latest provisional data indicates an improvement in Government's underlying deficit for 2004.

### **Consumption**

Consumer spending remains upbeat, evident by the buoyant performance of net Value Added Tax (VAT) collections, a partial indicator of spending. Net Value Added Tax (VAT) collections, amounted to \$102 million during the first 3 months of the year, representing a 14 percent increase over the previous comparable period.

This growth was underpinned by higher collections from the Government Department<sup>2</sup> and also from domestic collections. Nonetheless, collections by the Customs Services recorded an annual decline during the review period.

### **Income**

In line with favourable labour market conditions, Pay

As You Earn (PAYE) collections, a partial indicator for individual incomes, amounted to around \$45 million during the January to March period, representing a 6 percent increase over the comparable period last year.

### **Gold**

Output in the gold industry remained weak. Total gold production, cumulative to February this year, amounted to almost 18,000 ounces, 7 percent lower than the corresponding level in 2004. According to Emperor Gold Mining Company Limited (EGM), the decline in production is a result of lower quality ore extracted at the mines.

Accordingly, earnings also declined on an annual basis by 4 percent to \$12.7 million, during the review period.

### **Copra**

Production in the copra industry remained positive. Latest statistics from the Coconut Industry Development Authority (CIDA) show that cumulative to February this year, copra production amounted to around 1,100 tonnes, representing an increase of around 6 percent over the corresponding period last year.

The minimum mill gate price of copra for the month of February stood at \$500 per tonne.

### **Building & Construction**

The construction sector performed strongly last year, evident by the value of work put-in-place. According to the Fiji Islands Bureau of Statistics 2004 Annual Building and Construction Survey,<sup>3</sup> \$160 million was spent on capital works during the year. This represents an increase of 26 percent on an annual basis.

In terms of categories of investment, the total value of work put-in-place by the private sector in 2004 rose by around 33 percent (\$105.1 million), followed by the public sector, which recorded an increase of 15 percent (\$54.8 million) during the review period.

### **Public Finance**

Provisional cashflow data from the Ministry of Finance indicates an improvement in Government's fiscal position last year. The underlying fiscal deficit for 2004 is currently estimated at \$150.4 million or

<sup>2</sup> VAT from the Customs Services, Government Departments and Domestic collections are 3 separate categories of net VAT collections.

<sup>3</sup> The survey covers all private sector enterprises operating in the private and public sectors of the construction sector.

3.3 percent of GDP. This compares favourably with the deficit of \$220.5 million (or 4.8 percent of GDP) earlier estimated for 2004.

Underpinning the favourable fiscal outturn last year was an 11 percent rise in revenue collections and a relatively lower growth in net expenditure.<sup>4</sup>

For the current year, the Government is expecting an underlying deficit of around \$207.1 million, equivalent to 4.3 percent of GDP.

### **Inflation**

In March, inflation was 3 percent, compared with 3.5 percent in February. Over the month, consumer prices fell by 0.4 percent. During March, lower prices were also recorded in heating & lighting, transport, clothing & footwear, food, alcoholic drinks & tobacco, miscellaneous items and durable household goods. The fall in heating & lighting and transport costs is namely due to the reduction in domestic fuel prices at the beginning of the month. Prices of housing rose, largely due to higher prices of certain house repair items, while prices of services were unmoved.

The underlying measure of inflation, the trimmed mean, was 1.4 percent in March, up from 1.3 percent in February.

The year-end inflation forecast remains at 4.5 percent. However, the current high crude oil prices still pose some upside risks.

### **Building Material Price Index**

The Building Material Price Index (BMPI) survey is compiled by the Fiji Islands Bureau of Statistics (FIBOS) on a quarterly basis. The index is constructed using retail prices collected from selected hardware and building merchants in Suva. In the year to March 2005, the BMPI rose by 8.1 percent. Over the quarter, prices increased by 0.2 percent. Higher prices were recorded in iron & steel, wood & related materials, electrical products and cement & related materials. The increase in prices of building materials can be partially attributed to strong construction activity.

### **Labour Market**

Labour market conditions continued to show optimism over the month, evidenced by improvements in partial indicators of employment as

well as survey data. Cumulative to March, 4,300 new taxpayers were registered with the Fiji Islands Revenue & Customs Authority. Community, social and personal services sector recorded the most new taxpayers followed by the finance, insurance, real estate & business services; wholesale, retail trade, restaurants & hotels and manufacturing sectors.

Moreover, the Reserve Bank's Survey of Job Advertisements, conducted at the end of the March quarter, reported a rise in firms' recruitment intentions by around 9 percent over the previous quarter and 21 percent over the year. Demand for workers were high in the community, social & personal services, finance, insurance, real estate & business services, construction and transport, storage and communications related firms.

Furthermore, according to the Reserve Bank's FEF Expectations Survey, employment prospects over the next twelve months are anticipated to remain optimistic. A net of around 66 percent of respondents expect permanent employment to increase, while a net of around 54 percent of respondents expect a rise in temporary employment. On the wages front, the recent FEF Expectations Survey revealed that the majority of respondents expect wages to rise between 0 to 5 percent over the next twelve months.

### **Financial Aggregates**

In the year to February 2005, the total value of outstanding loans in the banking system increased by 19 percent to \$1.6 billion. This outcome was largely underpinned by higher lending to private individuals, real estate and wholesale & retail, hotels & restaurant and manufacturing sectors. 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 \$71 million in February 2005, an increase of 24.6 percent and 19.8 percent over the month and year, respectively.

In addition, total loans and advances of licensed credit institutions (LCIs) grew at an annual rate of 22 percent during the review period, with more loans extended mainly to private individuals. The weighted average lending rate of LCIs was 11.70 percent at the end February, a marginal increase over the month.

Also, during the review period, total outstanding deposits of commercial banks totaled \$2 billion, 9 percent higher than the level a year ago. Higher demand deposits placed by private individuals and

<sup>4</sup> According to the Ministry of Finance, there was a 16 percent decline in capital expenditure by the Government in 2004.

domestic business enterprises contributed to the increase in total deposits.

On the interest rates front, the weighted average lending rate of commercial banks and savings deposit rate remained unchanged at 6.92 percent and 0.36 percent respectively at the end of February, while the weighted average commercial bank time deposit declined by 1 basis point to 1.77 percent.

During the same period, interest rates on new lending fell by 53 basis points to 7.03 percent as a result of new loans extended at lower rates. On the contrary, the new deposit rate offered by commercial banks rose by 29 basis points to 1.59 percent over the month.

Meanwhile, interest rates offered by LCIs on new loans and advances increased by 74 basis points to 14.15 percent over the month, while the new time deposit rates also increased to 3.56 percent at the end of February 2005.

### **Exchange Rates**

In March 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 Euro (0.9 percent), Yen (0.5 percent), and the Australian (0.4 percent) and New Zealand dollars (0.3 percent) but weakened against the US dollar (1.6 percent).

The Nominal Effective Exchange Rate index<sup>5</sup> of the Fiji dollar rose by 0.1 percent in the year to March, indicating an appreciation of the Fiji dollar against the basket of currencies.

The Real Effective Exchange Rate (REER) Index<sup>6</sup> of

the Fiji dollar, a gauge of our international competitiveness, rose by 0.7 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 was 3.0 percent in March 2005, while average trading partner inflation was around 2.4 percent during the same period.

### **External sector**

On the external front, latest OET data showed that merchandise exports fell by around 40 percent cumulative to February, compared with an increase of 8.5 percent in the corresponding period in 2004. The decline in receipts was largely attributed to negative contributions from sugar, textiles, clothing & footwear, fish, merchanted goods, other exports and gold, which more than offset positive contributions from ginger and re-exports of mineral fuels.

Merchandise imports fell by around 0.3 percent cumulative to February this year, compared to a growth of around 12 percent in the corresponding period in 2004. The lower import payment was attributed to declines in payments for consumption goods (6.7 percent), which more than offset increase in investment goods (4.1 percent) and intermediate goods (2.3 percent). The decline in imports of consumption goods was mainly underpinned by negative contributions from other imports, food, beverages, & tobacco and transport equipment, while higher payments for machinery & electrical equipment and chemicals underpinned the increase in investment goods. Moreover, the increase in intermediate goods was underpinned by positive contributions from mineral fuels, which more than offset the decline in raw materials.

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<sup>5</sup> 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

<sup>6</sup> 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.

## FIJI: FINANCIAL STATISTICS

| <b>KEY INDICATORS</b>   | <b>Mar-05</b> | <b>Feb-05</b> | <b>Jan-05</b> | <b>Mar-04</b> |
|---|---------------|---------------|---------------|---------------|
| <b>1. Money and Credit</b><br>(year-on-year % change)   |               |               |               |               |
| Narrow Money  | n.a.          | n.a.          | 33.99(p)      | -11.77        |
| Currency in Circulation (monthly average)   | 10.44         | 10.64         | 12.45         | 18.53         |
| Quasi-Money (Time & Saving Deposits)  | n.a.          | n.a.          | 5.84(p)       | 23.13         |
| Domestic Credit   | n.a.          | n.a.          | 12.08(p)      | 12.68         |
| <b>2. Consumer Prices</b> <sup>1/</sup><br>(year-on-year % change)  |               |               |               |               |
| All Items   | 3.0           | 3.5           | 2.9           | 2.2           |
| Food  | 3.5           | 3.8           | 1.7           | 3.0           |
| <b>3. Reserves</b><br>(end of period)   |               |               |               |               |
| Gross Foreign Reserves (\$m)  | 715.2         | 760.7         | 755.0         | 725.1         |
| Months of Imports (goods & non factor services)   | 3.1           | 3.3           | 3.3           | 3.2           |
| Months of Imports (goods)   | 4.7           | 5.0           | 5.0           | 4.9           |
| <b>4. Liquidity</b><br>(end of period)  |               |               |               |               |
| Liquid Assets Margin to Deposit Ratio (%)   | n.a.          | 12.3          | 11.6          | 12.6          |
| Banks' Demand Deposits (\$m)  | n.a.          | 85.5          | 72.3          | 63.1          |
| <b>5. Interest Rates (% p.a.)</b><br>(monthly average)  |               |               |               |               |
| Lending Rate (Excluding Staff)  | n.a.          | 6.92          | 6.92          | 7.27          |
| Savings Deposit Rate  | n.a.          | 0.36          | 0.36          | 0.43          |
| Time Deposit Rate   | n.a.          | 1.77          | 1.78          | 1.61          |
| 91-day RBF Note Rate (month end)  | 1.75          | 1.75          | 1.75          | 1.25          |
| Minimum Lending Rate (MLR) (month end)  | 2.25          | 2.25          | 2.25          | 1.75          |
| Overnight Inter-bank Rate   | 1.29          | 0.82          | 0.80          | 0.80          |
| 5-Year Government Bond Yield  | 2.66          | 2.64          | n.i.          | 2.56          |
| 10-Year Government Bond Yield   | 5.15          | 5.08          | n.i.          | 4.66          |
| <b>6. Exchange Rates</b> <sup>2/</sup><br>(mid rates, F\$1 equals)<br>(end of period)   |               |               |               |               |
| US dollar   | 0.5978        | 0.6074        | 0.6011        | 0.5807        |
| Pound sterling  | 0.3181        | 0.3166        | 0.3185        | 0.3179        |
| Australian dollar   | 0.7757        | 0.7724        | 0.7770        | 0.7708        |
| New Zealand dollar  | 0.8448        | 0.8420        | 0.8465        | 0.8835        |
| Swiss francs  | 0.7167        | 0.7060        | 0.7136        | 0.7444        |
| Euro  | 0.4626        | 0.4586        | 0.4611        | 0.4772        |
| Japanese yen  | 64.25         | 63.90         | 62.21         | 61.36         |
| <b>7. Commodity Prices (US\$)</b><br>(monthly average)  |               |               |               |               |
| UK Gold Price/fine ounce <sup>2/</sup>  | 435.13        | 422.69        | 424.82        | 405.46        |
| London Daily Sugar Price/tonne <sup>3/</sup>  | 260.44        | 265.37        | 261.18        | 200.70        |
| Crude Oil/barrel <sup>4/</sup>  | 53.12         | 45.56         | 44.48         | 33.80         |
| <p>n.a. - Not available/No activity<br/> n.i. - No issues<br/> n.t. - No trading</p> <p>Sources: <sup>1/</sup> Fiji Islands Bureau of Statistics<br/> <sup>2/</sup> Bloomberg and Reserve Bank of Fiji<br/> <sup>3/</sup> Fiji Sugar Marketing Company Limited<br/> <sup>4/</sup> Bloomberg</p> |               |               |               |               |