

## ASIA PACIFIC ECONOMICS PACIFIC QUARTERLY

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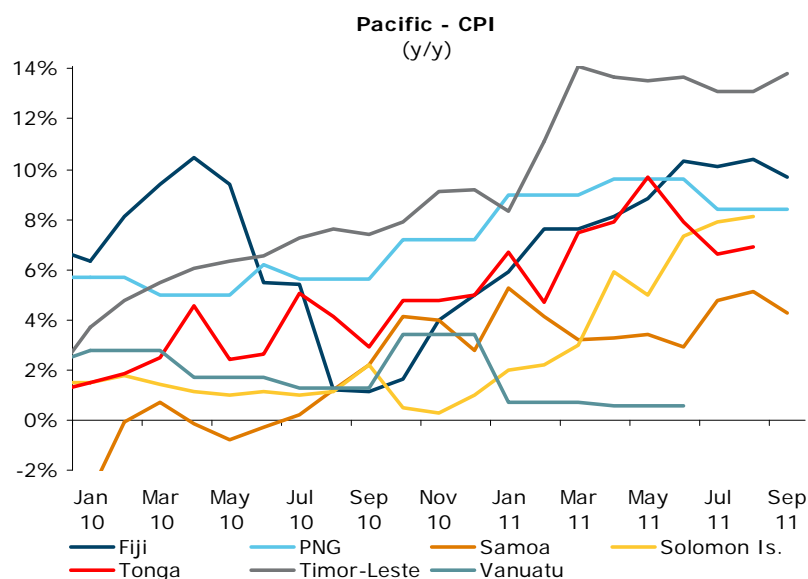
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### HIGHLIGHTS

- The pace of activity remains split in the Pacific with the export boom economies of Papua New Guinea, Timor L'este and Solomon Islands outperforming. Domestic activity remains soft, particularly in Fiji and Polynesia.
- Inflation remains elevated across much of the region owing to high food and commodity prices. However, like elsewhere in Asia, we expect inflation to begin to decline as global prices ease.
- Regional currencies maintained a stable to appreciating trend against the USD (and the AUD); the PGK, however, outperformed regional currencies quite strongly.
- Our Feature Note looks at the outlook for the coming three years. We think the Pacific is well-placed to outperform given its reliance on commodities (not manufactures), its geographical advantage of being in a strong growth "neighbourhood" and weak financial links to the North Atlantic. PNG and Timor should continue to lead the region in growth.

### CHART OF THE QUARTER

#### INFLATION REMAINS ELEVATED, BUT IS BEGINNING TO STABILIZE



Sources: ANZ Research, Pacific Central Banks

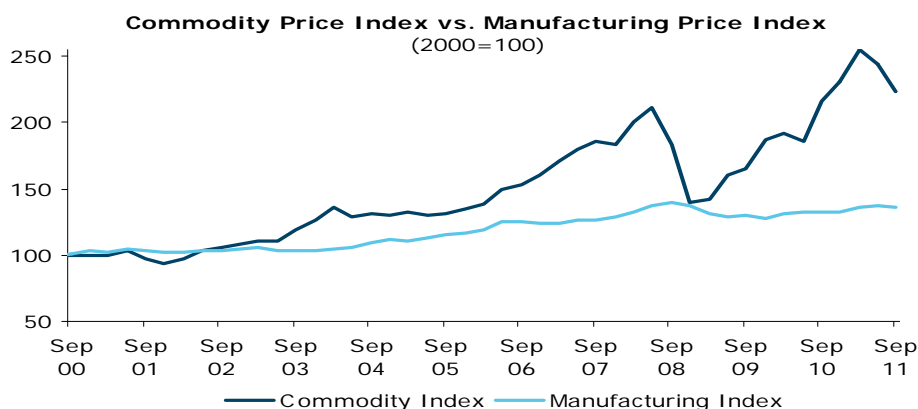
## FEATURE NOTE

**PACIFIC OUTLOOK: IT'S GOOD TO BE FAR FROM EUROPE!**

In this final Feature Note of 2011 we present our macroeconomic outlook for 2012-14. In short, it is good to be far from Europe, as well as to be dependent on commodities rather than manufactures and to not have a financial sector that is well connected with global money centres. Therefore, relative to the rest of the world, the Pacific should do well, with the more (hard) commodity reliant economies of Papua New Guinea, Timor-L'este and the Solomon Islands leading the way.

As far as economic performance is concerned, 2012 is setting up as a reasonably good year for the Pacific. Specifically, it will be good: (1) to be far from Europe (and preferably in or close to Asia); (2) to be a commodity producer; and (3) not to have a financial sector too closely intertwined with global system. The Pacific meets the bill on all three. Let us take these in turn.

1. It is good to be located in a part of the world where growth is still decent.
  - Led by China and India, Emerging Asia continues to drive global growth. Moreover, the ongoing industrialisation and urbanisation in much of Emerging Asia is keeping global commodity prices high. In addition, a rising middle class that consumes and eats more is supporting soft commodity prices. Both of these trends are good for the Pacific.
  - It is also good to have strong links to Australia and New Zealand. These are the only industrialised countries showing any signs of growth, benefitting from the hard and soft commodity booms, respectively, as well as strong macroeconomic frameworks.
2. It is also good to be commodity reliant, non-manufacturing economy. As with the rise of the US in the late 19th century, the rise of China in particular is leading to a boom in commodity prices (shifting the demand curve for those goods to the right) whilst depressing prices for manufacturing prices (shifting the supply curve for those commodities to the right). The hard commodity and energy exporters in the Pacific—Papua New Guinea and Timor L'este—have benefitted most, but everyone has done better than manufacturing-based economies. As we have written earlier (*see our Pacific Quarterly, from August 15, '11*) these terms of trade gains drive a positive wedge between income and GDP growth, with PNG as the biggest beneficiary.



*Commodity Index is proxied by the CRB,  
Manufacturing is proxied by Australia's manufacturing PPI*

Sources: Bloomberg, ANZ Research

## FEATURE NOTE

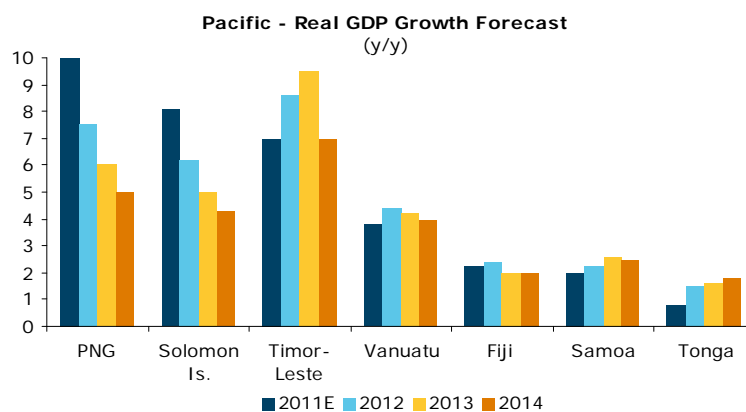
3. Finally, it is good not to have a financial sector that is not too closely intertwined with the major money centres. Given the ongoing (and at the time of this writing, escalating) financial turbulence in Europe, and the contagion to the rest of the world through PIIGS creditor bank exposures and counterparty risk, it is perhaps better to be disconnected at the current juncture. If we are looking for an example in the Asia Pacific region, Indonesia stands out as a country that did reasonably well through the Global Financial Crisis and continues to do well. Every country in the Pacific to some extent qualifies on this basis.

## OUR PACIFIC VIEW

Our Pacific view is therefore a relatively upbeat one given what is going on elsewhere in the global economy. As we have done previously, we divide the region into the higher growth and lower growth economies.

**Higher growth (Papua New Guinea, Timor L'este, Solomon Islands).** These economies continue to benefit from resources booms, albeit each slightly different.

- PNG has the LNG project, which has pushed growth up near double-digits last year and will continue to drive above trend activity over the medium term. The challenge is to capture this windfall and invest it for the benefit of future generations. (6% growth over 2012-14).
- Timor L'este continues to enjoy an oil boom, which is located and managed almost fully off-shore. The task, again, is to use these funds, combined with UN donor funds, to build the foundation of this new nation. (8½% growth over 2012-14).
- The Solomon Islands will also enjoy growth above the regional average, owing to wood and gold exports. At issue here is resource management, with the risk of over-logging casting a cloud over the longer-term prospects. Unlike PNG and Timor, there is no (planned) sovereign wealth fund so the benefits of the boom will be shorter-lived (5% growth over 2012-14).



Sources: Central Banks, IMF, ADB, ANZ Research

**Lower growth (Fiji, Samoa, Tonga, Vanuatu).** These economies can be characterised as more “traditional” from a Pacific perspective. The production and export bases are more agricultural and there is also a reliance on tourism and/or remittances for external financing.

- Fiji's growth will continue to track around 2% based largely on tourism and agriculture. In relative terms, the economy will continue to fall behind PNG. Sugar sector reforms and tourism could provide some upside to medium-term growth. (2% growth over 2012-14).

## FEATURE NOTE

- Samoa will see growth over the next few years of 2% to 3% boosted by post-Tsunami construction. These effects will fade and give way to the traditional drivers of manufacturing and tourism. Fiscal consolidation will be a break on growth. (2½% growth over 2012-14).
- Tonga continues to emerge slowly from the GFC with growth prospects weak. We are looking for sub-1% growth again this year and sub-2% over the medium term. Investment remains weak, and the upside from commodity exports remains limited.
- Vanuatu is the best performer in this group. The key for raising the growth profile is infrastructure. As always, tourism from Australia and commodity exports will be the motors of growth (4% growth over 2012-15).

A more detailed medium-term macroeconomic forecast description including inflation and the fiscal accounts, as well as the accompanying tables, appear in the Appendix.

### RISKS

The risks to Pacific growth relative to our baseline forecasts are moderately on the downside.

The main risk is global commodity prices, which will reflect global demand developments. Should events in Europe continue to deteriorate and spill over to the rest of the global economy, then we would expect commodity prices to decline nearly across the board. This would have an outsized impact on the Pacific given its relatively high reliance on commodities for exports and incomes. The symmetric case applies for a better than expected resolution of the debt crisis; in that "risk on" scenario commodities and growth would outperform.

China is another risk given Australia's links that country's infrastructure and lending boom. We have recently revised our assessment of the Chinese economy to one where the risks of a hard landing have increased, although a soft landing remains our baseline scenario. We continue to believe that the structural growth stories (urbanisation, rising middle class) are robust and should support commodity prices going forward.

*Paul Gruenwald*

## FEATURE NOTE

**APPENDIX – 2011-14 PACIFIC MACROECONOMIC FORECAST DETAILS**

**Fiji.** Growth will face greater global headwinds in 2012 but will be aided by substantial monetary policy easing in 2011 and greater fiscal spending. Consumption, supported by agriculture, remittance and tourism inflows, will remain the main driver. Beyond 2012, growth is seen as settling to around the long-term rate of 2%, which is consistent with an inflation rate of 5%. The external current account deficit is expected to be contained to within 10% of GDP. This reflects gradual fiscal retrenchment as well as a modest improvement of external competitiveness through reforms in the sugar industry and strong tourism receipts.

**Papua New Guinea.** We expect above trend growth and inflation to characterise PNG's macro performance over the medium term reflecting the LNG project induced boom. While growth likely peaked at around 10% in 2011, the infrastructure and related spending should keep GDP and inflation momentum in the high single digits for the next three years. Strong terms of trade should bolster income growth as well. Government revenues should also outperform and result in a continuation of the string of budget surpluses. A key challenge for PNG will be managing expectations in the context of a return to trend GDP and, more importantly, wage growth.

**Samoa.** We expect the economy to grow by 2% to 2.5% over the medium term. In 2011, the economy is likely to expand by around 2.0% bolstered by post-tsunami reconstruction. Though this construction stimulus will fade, we think growth will be supported by i) a recovery in manufacturing, which is currently quite weak; and ii) reasonably healthy domestic demand. With pressures both from the demand and supply side intact, we expect inflation to trend upward and settle around 4%. Fiscal consolidation will also be a key theme, as the government will rein in expenditure and try to stabilize public debt levels following post-tsunami easing. The external sector is likely to record more modest outturn as lower global growth affects commodity exports and tourism.

**Solomon Islands.** The outlook is a mixed commodity story, with GDP growth of over 5%. Log production and exports will continue to drive growth in the near term, however unsustainable practices will result in significantly lower production ahead. Gold production is expected to reach 100,000 ounces next year and for at least nine years after, becoming a key driver of growth. High reserves of other commodities, particularly nickel, suggest further economic potential if legal impediments can be overcome. The current account will improve dramatically, as the importation of machinery for the Gold Ridge mine falls off and exports increase. On the fiscal side, stronger revenues with high commodity prices will allow the government to spend more money on development.

**Timor L este.** Growth is expected to remain strong this year and in the medium term despite bad harvests which are currently weighing down coffee production (and, which accounts for almost all of non-oil domestic exports). Underpinning the growth outlook are: i) terms of trade gains from global crude prices which improve incomes and ii) a strong public investment and infrastructure drive. However, the private sector has only marginally contributed to growth and in the near term has limited capacity to fully capitalise on income and investment efforts.

**Tonga.** Growth is expected to remain below 2% over the next four years as the economy relies heavily on donor aid, remittances, and tourism. The threat of natural disasters has mitigated investment in manufacturing plants and infrastructure; however the sea is also Tonga's most valuable asset. Inflation should begin to ease as commodity prices come off and global food prices fall. Fiscal policy remains reliant on aid, while expenditure consolidation is necessary for the government to achieve its development objectives. The current account will remain negative reflecting a reliance of imports and low levels of saving.

**Vanuatu.** The buildout of infrastructure is the key to medium-term growth. Due to delays in project implementation, construction activity has only picked up slightly in 2011 but due to stronger manufacturing we expect growth of around 3.8%. Going forward, construction momentum should increase, which should allow for growth to be above 4%. Though this will likely add to supply side price pressures in the short term, in the medium term we expect inflation to remain stable at around 3%. Consumption should remain healthy, which will allow for higher tax revenue and an improved fiscal profile. Meanwhile, the external sector's growth contribution will be more modest, as weaker global growth will weigh in on commodity exports and tourism.

## FEATURE NOTE

## REAL GDP GROWTH (%)

	2011E	2012	2013	2014
Fiji	2.2	2.4	2.0	2.0
PNG	10.0	7.5	6.0	5.0
Samoa	2.0	2.2	2.6	2.5
Solomon Is.	8.1	6.2	5.0	4.3
Timor-Leste	7.0	8.6	9.5	7.0
Tonga	0.8	1.5	1.6	1.8
Vanuatu	3.8	4.4	4.2	4.0

## NOMINAL GDP (US\$ bn)

	2011E	2012	2013	2014
Fiji	3.4	3.6	3.9	4.1
PNG	13.7	16.0	18.2	20.4
Samoa	0.6	0.6	0.7	0.7
Solomon Is.	0.8	0.9	1.0	1.1
Timor-Leste	0.7	0.8	0.9	1.0
Tonga	0.4	0.4	0.4	0.4
Vanuatu	0.7	0.8	0.8	0.9

## INFLATION (%)

	2011E	2012	2013	2014
Fiji	7.0	5.0	5.0	5.0
PNG	9.0	9.0	7.0	7.0
Samoa	3.5	3.8	4.0	4.0
Solomon Is.	8.0	6.0	5.5	4.2
Timor-Leste	12.2	11.0	9.0	6.0
Tonga	6.6	5.5	5.0	5.0
Vanuatu	2.9	3.5	3.0	3.0

## FISCAL BALANCE (% OF GDP)

	2011E	2012	2013	2014
Fiji	-2.8	-3.3	-3.2	-3.0
PNG	2.0	1.0	0.0	-1.0
Samoa	-10.2	-8.5	-7.0	-6.0
Solomon Is.	2.2	-1.8	-1.9	0.5
Timor-Leste*	225.2	194.3	130	100
Tonga	-5.2	-4.2	-4.0	-3.8
Vanuatu	-1.3	-1.5	-0.3	-0.8

## CURRENT ACCOUNT BALANCE (% OF GDP)

	2011E	2012	2013	2014
Fiji	-10.3	-9.0	-9.5	-9.2
PNG	-19.0	-12.0	-7.0	-7.0
Samoa	-12.5	-13.0	-13.6	-12.0
Solomon Is.	-10.0	-12.0	-16.0	-15.0
Timor-Leste*	246.9	217.6	154.8	124.8
Tonga	-12.2	-11.2	-11.2	-11.5
Vanuatu	-5.7	-6.0	-6.0	-6.0

## FOREIGN EXCHANGE RESERVES (US\$ mn)

	2011E	2012	2013	2014
Fiji	880	800	750	700
PNG	4000	4500	4750	5000
Samoa	254	286	320	350
Solomon Is.	356	450	475	500
Timor-Leste	300	325	350	375
Tonga	132	140	150	155
Vanuatu	180	195	210	220

Sources:

PNG: Department of Treasury, Central Bank of PNG, ANZ Research

Timor-Leste: ADO, WEO, ANZ Research

Vanuatu: IMF, Reserve Bank of Vanuatu, ANZ Research

Samoa and Tonga: IMF and ADB

Solomon Islands: Central Bank of Solomon Islands, IMF, ANZ Research

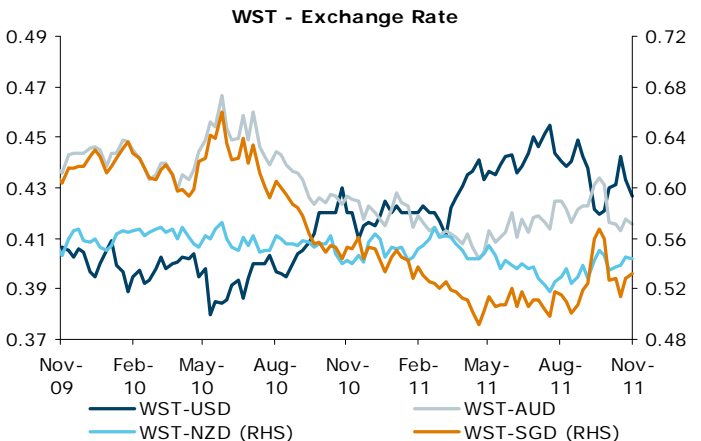
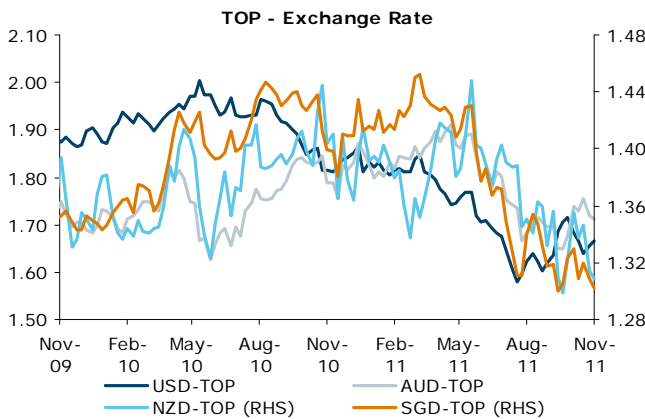
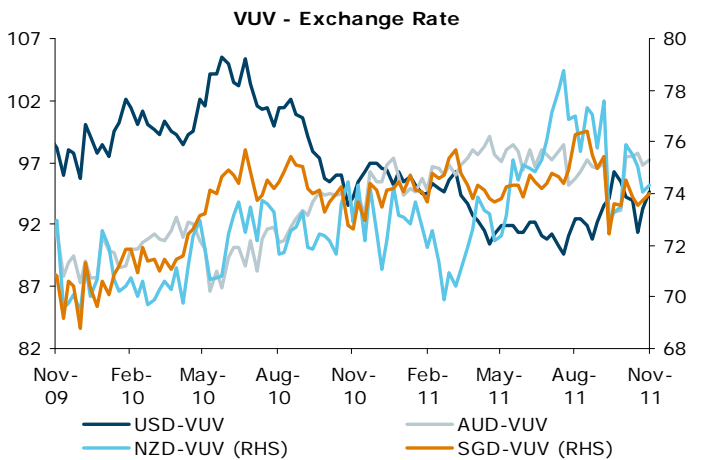
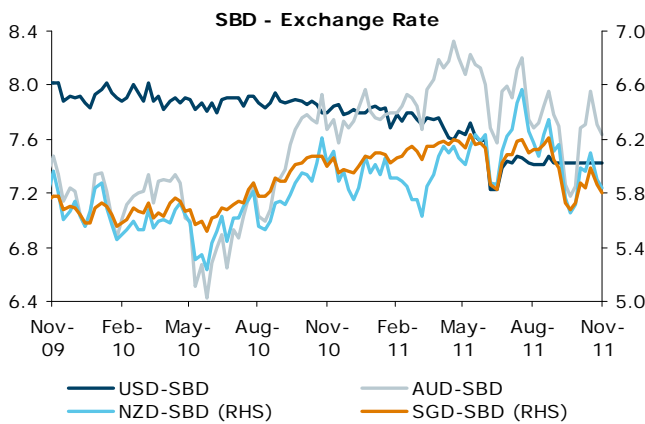
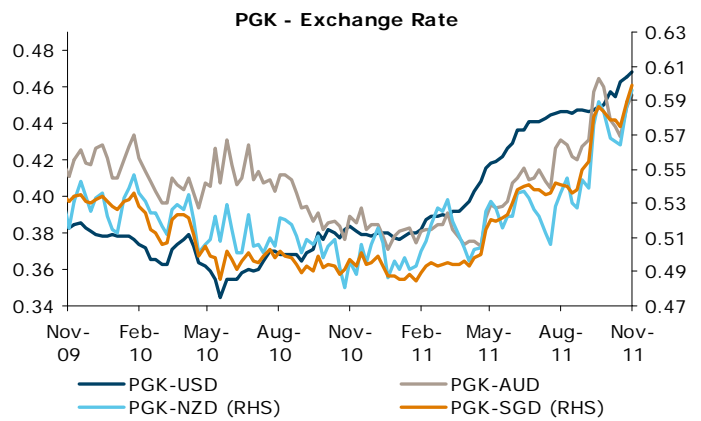
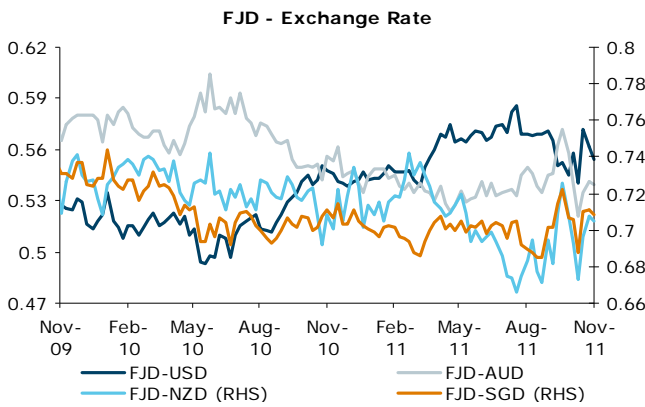
Vanuatu-IMF: Research Bank of Vanuatu, ANZ Research

\* as % of non-oil GDP

# FX AND POLICY INTEREST RATES

## CURRENCIES

The Pacific currencies were little changed over the last month except for the PGK, which appreciated over 2.4% (ytd: +23.8%) against the USD. We continue to see a modest appreciation trend given the strengthening terms of trade and greater capital inflows related to energy projects in the pipeline. The TOP (+0.9%) is the second best performer, as the currency is pegged to a basket consisting of the AUD and NZD which had strengthened considerably in this recent period. However, a weakening trade balance remains a risk.



## FX AND POLICY INTEREST RATES

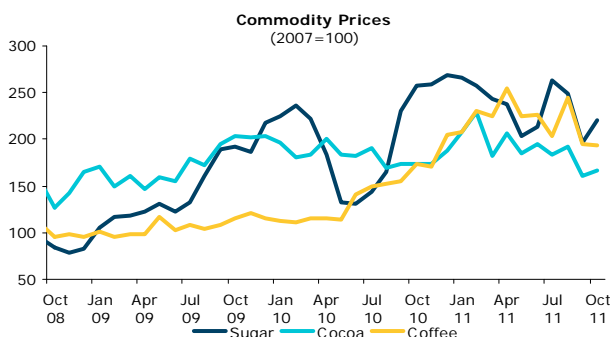
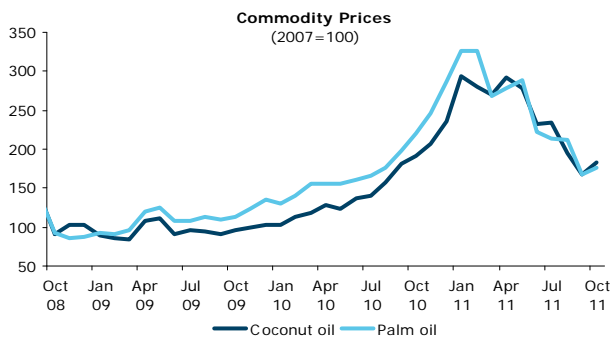
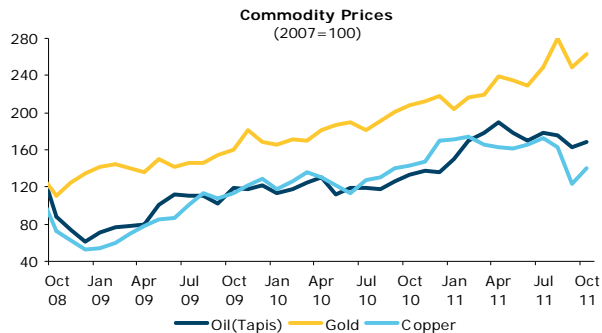
		CURRENT	DEC-11	JAN-12	FEB-12	MAR-12	APR-12	MAY-12
FIJI	FJDUSD	0.566	0.565	0.566	0.567	0.568	0.570	0.570
	FJDAUD	0.550	0.558	0.584	0.579	0.574	0.570	0.561
	Short term rates*	0.50	0.50	0.50	0.50	0.5	1.00	1.00
PAPUA NEW GUINEA	PGKUSD	0.468	0.467	0.467	0.468	0.47	0.471	0.472
	PGKAUD	0.455	0.461	0.481	0.478	0.475	0.471	0.464
	Short term rates**	7.75	7.75	7.75	8.00	8.00	8.00	8.00
SAMOA	WSTUSD	0.433	0.434	0.437	0.44	0.443	0.447	0.450
	WSTAUD	0.420	0.428	0.451	0.449	0.447	0.447	0.443
SOLOMON ISLANDS	USDSBD	7.431	7.430	7.430	7.430	7.420	7.420	7.420
	AUDSBD	7.651	7.527	7.207	7.281	7.346	7.420	7.544
TONGA	USDTOP	1.688	1.69	1.69	1.70	1.71	1.71	1.71
	AUDTOP	1.737	1.712	1.639	1.666	1.690	1.709	1.739
VANUATU	USDVUV	93.25	93.3	93.50	93.13	92.75	92.38	92.00
	AUDVUV	96.01	94.52	90.70	91.27	91.82	92.38	93.53
	Short term***	6.00	6.00	6.00	6.00	6.00	6.00	6.00

Note: The source of FX data is Bloomberg. As the currencies are illiquid with wide bid/offer spreads, the rate published is only indicative. (\*) overnight policy rate, (\*\*) Kina Facility Rate, (\*\*\*) Discount rate.



# COMMODITY MARKETS

## COMMODITY MARKET DEVELOPMENTS



Commodity prices rebounded in Oct after the massive 'risk off' selling in Sep. Although developments in the euro zone were generally negative for risk, favourable demand-supply fundamentals as well as stronger data from the US and China supported prices. Gold (as the safe haven) did well, base metals and ags were robust, while oil was choppy, although it traded higher.

- Oil traded choppy in Oct. Though the euro zone debt crisis weighed in negatively on prices; slightly stronger US economic data, falling oil stockpiles and forecasts for a cold US winter were sources of support. Overall, oil benchmarks ended the month on a much stronger note (m/m Tapis: 3.0%, Brent: 5.7%, WTI: 13.7%).
- Gold traded higher in Oct (5.6% m/m), supported by safe haven buying (risk aversion due to the Euro crisis) as well as a weaker USD. However, the rise was slightly constrained as clearing houses increased margins for trading gold.
- Ags, except coffee, ended Oct on a higher note. Sugar prices jumped 12.2% m/m, mostly due speculative buying by funds. Both coconut oil and palm oil saw a reversal in their downtrend. Rice, meanwhile rose by a modest 1.1%, though prices will be biased upwards as the ongoing Thai floods affect production.
- Base metals were broadly strong in Oct, rebounding from the large selloff in Sep. Copper stood out, rising 14.1% m/m, as destocking of Chinese copper inventory and ongoing strikes in mines around the world supported prices. Lead (6.6%) and Nickel (5.6%) were the other top performers.

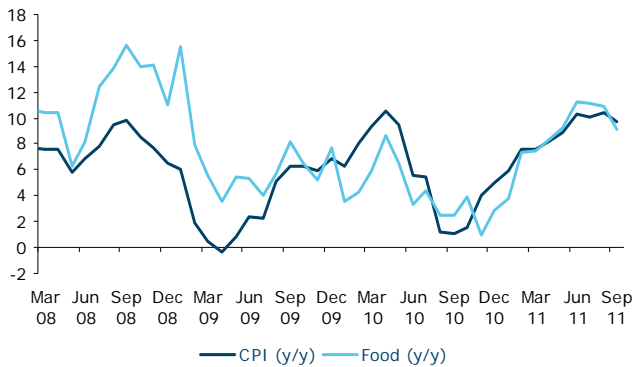
*Raj Gopalakrishnan*

COMMODITY PRICE CHANGES	OIL (TAPIS)	GOLD	COPPER	COC. OIL	PALM OIL	SUGAR	COFFEE	COCOA	RICE
M/M %	3.0%	5.6%	14.1%	9.2%	4.6%	12.2%	-0.9%	3.4%	1.1%
3M Change	-5.8%	5.3%	-18.6%	-22.2%	-17.6%	-16.5%	-5.3%	-9.3%	16.0%
Y/Y %	26.6%	26.1%	-2.5%	-5.0%	-20.0%	-14.5%	11.6%	-3.6%	23.7%

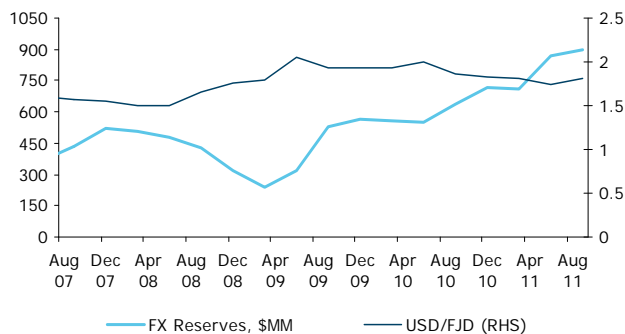
Source: Bloomberg

## COUNTRY UPDATE

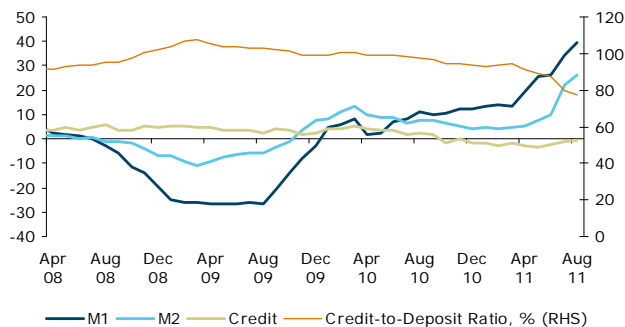
Fiji - Inflation



Fiji - FX Reserves and FX Rate



Fiji - Money and Credit Growth (y/y %)



## Fiji

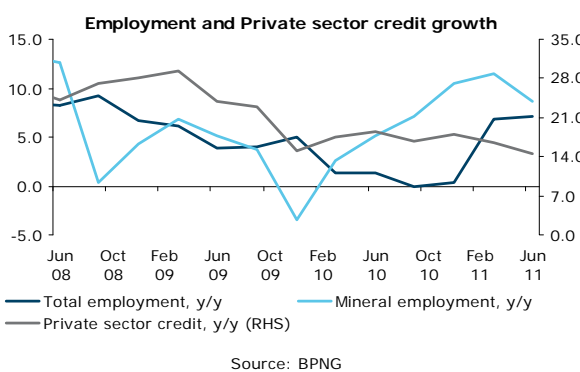
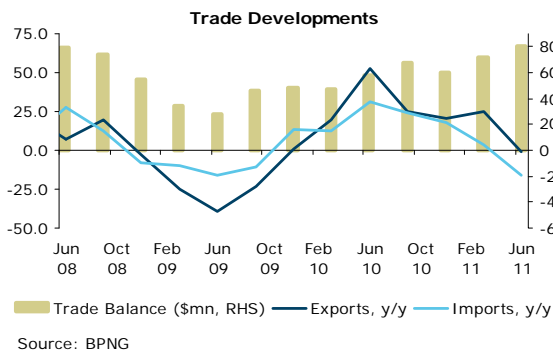
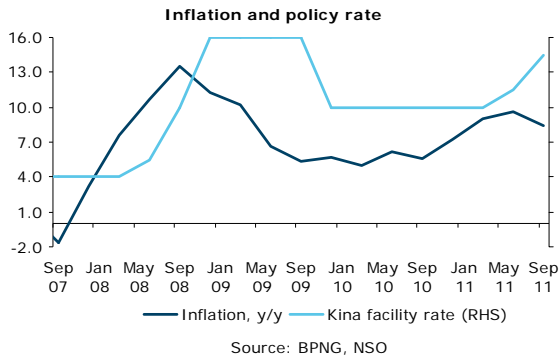
**Growth should pickup in 2012 on account of monetary stimulus this year and a pickup in public expenditure. Price pressures have recently begun falling as supply-side pressures are easing. However, low real rates and large money supply growth could raise price risks.**

- Growth is expected to reach 2.2% y/y in 2011, short of the official 2.7% target. Consumption remains an important driver, and is supported by increasing incomes on account of rising remittances, and healthy tourism receipts.
- Investment remains subdued, but should pickup as borrowing costs remain low, resort development projects pickup, and as government capital projects come on stream.
- CPI inflation fell to 9.7% y/y in September from 10.4% the previous month. The slowdown was mainly due to an easing of food and transport prices.
- Credit growth remains weak (-0.5% y/y in Aug) as modest private sector credit growth (+5%) was offset by a sharp reduction in credit (-43%) to the government sector.
- Government borrowing has diminished on account of VAT tax rate hikes and greater utilization of foreign borrowings.
- The Reserve Bank reduced its benchmark Overnight Policy Rate to 0.5% from 1.5% on the weakening global outlook and sluggish domestic activity.
- Foreign reserves have grown sharply, reaching nearly \$900mn at the end-Sep on account of sizable foreign borrowings. The current level of reserves provides 4.8 months of import cover.
- However, not all of the increase in reserves appears to have been sterilized, resulting in a sharp increase in M2 growth, which reached 25.9% y/y in Aug.
- Over the near-term, the economy should withstand global headwinds. However, looking further ahead, structural reforms to heighten the competitiveness of key sectors and the economy's overall financial absorption capacity will become important.

Aninda Mitra

QUARTERLY ECONOMIC DATA	DEC-09	MAR-10	JUN-10	SEP-10	DEC-10	MAR-11	JUN-11	SEP-11
Consumer Price Index, % y/y	6.8	9.4	5.5	1.1	5	7.6	10.3	9.7
Domestic Credit, % y/y	4.1	5.4	2.9	1.6	-0.6	-2.3	-2.4	-.5
Exports, % y/y	-13.0	22.9	49.1	14.5	23.7	6.2	N/A	N/A
Imports, % y/y	-26.2	-9.6	27.5	62.4	32.7	-0.9	N/A	N/A
Trade Balance, US\$ mn	-181.5	-247.3	-242.8	-404.5	-272.0	-249.3	N/A	N/A
Foreign Exchange Reserves, US\$ mn	566	557	548	637	716	707	866	899

Sources: Reserve Bank of Fiji, ADB, IMF



## Papua New Guinea

The outlook is favourable as strong growth continues reflecting the LNG project build-up. Inflation has eased for now, but price pressures should remain elevated. Inflation and wage expectations will need to be managed down as growth returns to trend in the coming years.

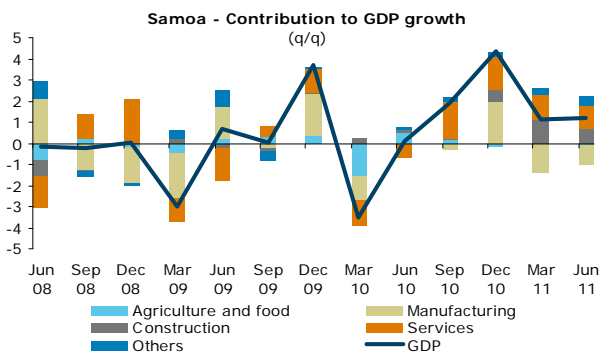
- GDP growth could reach 10% this year, fuelled by the LNG product and its spin-offs.
- Q2 employment grew 7.1% y/y according to the Bank of Papua New Guinea (BPNG) employment index. Transport, wholesale and agriculture led the rise.
- Headline CPI inflation eased to 8.4% in Q3 from 9.6% previously, due to falling food and oil prices. That said, inflation pressures remain high due to fast growth and supply bottlenecks.
- Credit growth remains weak as most of the LNG project build-out is being financed from abroad. Liquidity remains high reflecting government deposits in the banking sector and lack of demand for credit. Government deposits reflect the operating surplus and trust accounts; efforts are being made to transfer these balances to BPNG. The 28-day central bank bill rate remains well below inflation, at around 3%.
- The BPNG raised its benchmark Kina Facility Rate to 7.75% in Sep. This was the third 25bp increase this year. In addition, the cash reserve requirement was raised by 100bps in Aug to 6.0% the second rise of that magnitude this year.
- Budgetary performance remains strong owing to high mineral revenues. The surplus this fiscal year remained at around 2% of GDP, leading to another supplementary budget. There has been little progress in setting up the sovereign wealth fund.
- Reserves reached \$4.0bn in late October boosted by high commodity exports and buoyant government mineral tax receipts.
- Near term, growth looks in very good shape; the challenge is to raise real interest rates to more neutral levels to combat inflation. Over the coming years, currently high wage and growth expectations will need to be managed down as growth returns to trend, and the sovereign wealth fund needs to be implemented and funded to invest in human capital.

*Paul Gruenwald*

QUARTERLY ECONOMIC DATA	DEC-09	MAR-10	JUN-10	SEP-10	DEC-10	MAR-11	JUN-11	SEP-11
Employment Index, % y/y	5.0	1.3	1.3	-0.1	0.3	6.8	7.1	N/A
Consumer Price Index, % y/y	5.7	5.0	6.2	5.6	7.2	9.0	9.6	8.4
Exports, % y/y	1.3	19.6	54.0	24.7	20.1	25.0	-0.7	N/A
Imports, US\$m	13.7	12.8	30.9	23.8	18.0	3.3	-16.2	N/A
Trade Balance, US\$ mn	484	471	590	575	599	721	808	N/A
Foreign Exchange Reserves, US\$ mn	2604	2372	2581	2912	3147	3190	3738	N/A

Sources: Bank of Papua New Guinea, ANZ Research



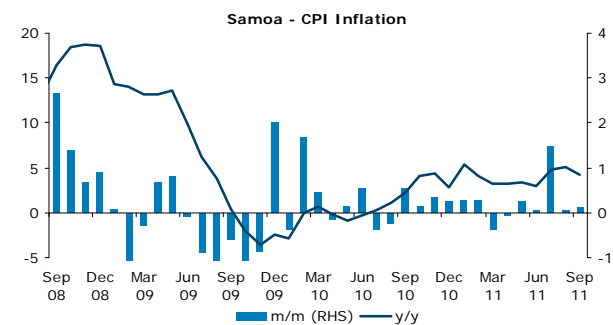
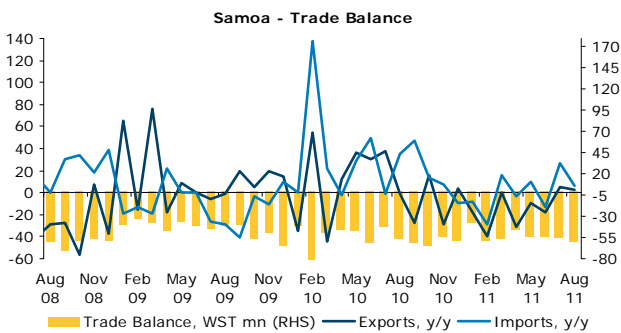


## Samoa

**Samoa's economy grew by 1.2% y/y in Q2, driven by construction, while manufacturing contracted. External indicators were broadly weak. Inflation pressures have begun easing.**

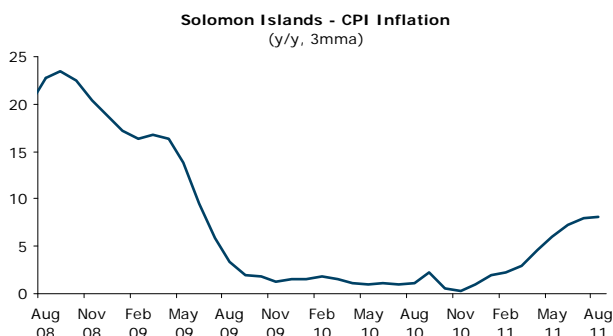
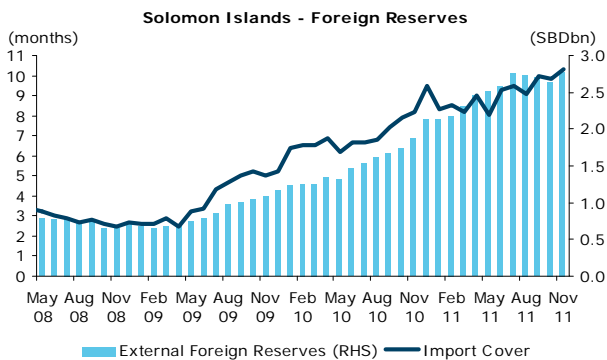
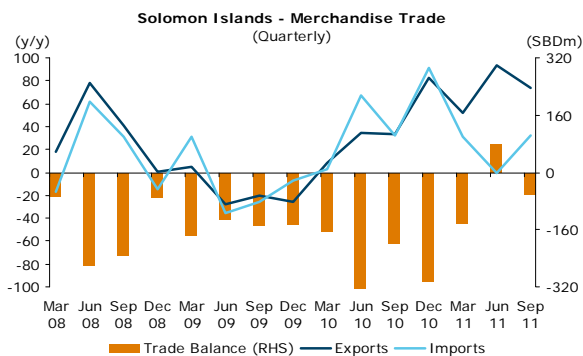
- GDP expanded by 1.2% y/y in Q2. Construction (+0.7ppt contribution to growth) was the main driver, followed by communications (+0.6ppt) and agriculture (+0.5ppt), while manufacturing (-0.9ppt) was the main drag. On a q/q basis, GDP fell 0.1%.
- CPI inflation eased to 4.3% y/y in Sep from Aug's 5.1%. Increases in household equipment and fuel prices were more than offset by a decline in food. On a m/m basis, the CPI rose 0.1%; imported inflation fell 0.9%, while domestic inflation rose 0.7%.
- Export growth fell to 2.5% y/y in Aug following Jul's 4.6% print. A decline in exports of fresh fish and beer more than offset a rise in coconut oil. Import growth fell to 5.8% y/y in Aug from 27.3% in Jul. The Aug trade deficit widened to WST60.3mn from WST55.4mn in Jul.
- Private remittances rose 5.8% y/y in Aug to \$31.4mn following a 2.7% rise in Jul. On a m/m basis, remittances rose 1.1% following a 2.0% drop in Jul. A stronger USD led to an improvement in remittances from the US.
- Visitor arrivals plunged 13.8% y/y in Sep following a 2.2% gain in Aug. Air arrivals fell 13.6%, while cruise arrivals fell 31.0%. Total arrivals, which include resident arrivals as well, fell by 9.5%.
- Bank credit to the private and public sectors rose 7.0% y/y in Aug, 0.3ppt up from Jul. The rise was driven by loans to the trade, transport and communication and storage sectors.
- With domestic activity expanding at a sluggish pace and an external sector facing headwinds due to lower commodity prices, we expect GDP growth of around 2.0% this year. A stronger manufacturing sector could lead to better outcomes in 2012.

*Raj Gopalakrishnan*



QUARTERLY ECONOMIC DATA	DEC-09	MAR-10	JUN-10	SEP-10	DEC-10	MAR-11	JUN-11	SEP-11
Consumer Price Index, % YOY	-2.5	0.7	-0.3	2.2	3.8	3.2	2.9	4.3
M2, % YOY	9.1	9.0	12.2	13.4	7.8	5.5	0.1	N/A
Exports, % YOY	33.8	-33.7	35.2	-23.9	2	-22.3	-17.7	N/A
Imports, % YOY	22.7	44.7	55.1	54.5	10.5	-10.8	-2.9	N/A
Trade Balance, US\$ mn	-24.2	-19.3	-23.7	-25.2	-25.2	-23.7	-23.8	N/A
Foreign Exchange Reserves, US\$ mn	144.5	140.13	159.49	191.75	209.4	158.4	159.3	N/A

Sources: The Central Bank of Samoa, Samoa Bureau of Statistics



## Solomon Islands

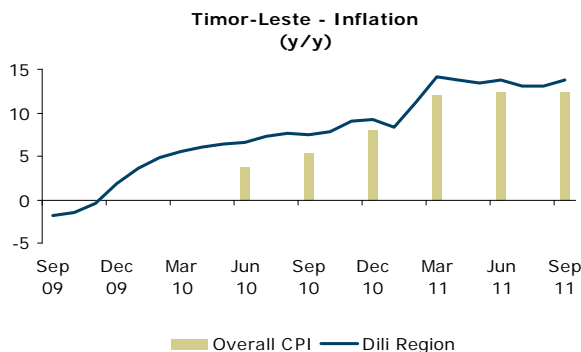
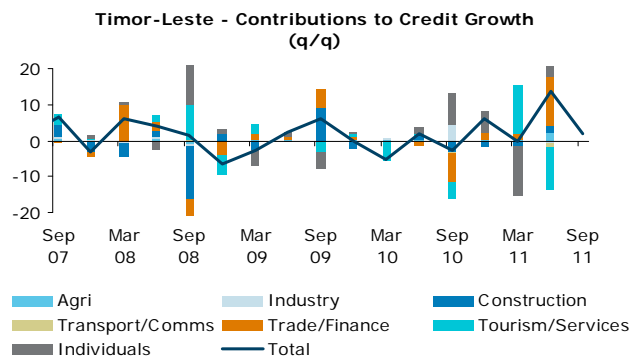
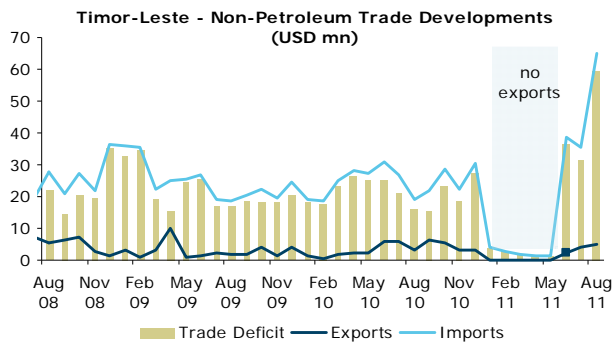
Growth has been strong in 2011. Domestic production of soft commodities remains solid and gold production is quickly picking up speed. However, domestic credit growth continues to contract. Shipments abroad remain high, while inflation pressures have stayed elevated.

- Strong exports continued, rising 73.7% y/y in Q3, from 93.6% in Q2. Import growth bounced back to 32.3% in Q3, from a 0.6% fall in Q2. The trade balance returned to a deficit at SBD61.2m, from the first surplus in over five years at SBD77.3m in Q2. Exports have been boosted by logs and the resumption of gold exports in April this year.
- Log production rebounded in September, rising 62% m/m; year-to-date production has surpassed 2010's result, and is likely to exceed 2008's historic peak.
- Gold exports tripled in Sep to 13,459 ounces; a total of 26,688 ounces have been shipped. Gold Ridge's reserves were estimated to be 1.28m ounces, as of Jul 2010, with a market value today of \$2.3bn, to be mined over nine years. A full ramp up is expected in 2012, producing 100,000 ounces per annum.
- Inflation climbed to 8.1% (3mma) in Aug compared with a 7.9% rise in Jul. The domestic component of headline inflation rose to 8.5% from 7.4% which outweighed the fall in imported items to 7.7% from 8.1%. Housing and utilities drove domestic prices.
- M3 increased by 19.4% y/y to SBD2331mn as of 2 Nov. Meanwhile, total domestic credit fell sharply; contracting 60.7% y/y to SBD424mn, and declined 1.9% m/m.
- Total gross government debt stands at SBD1,187mn, at the end of Sep 2011, of which 72% is external debt.
- The economy is benefitting from high log prices which have incentivised strong production; however stocks are rapidly being depleted. Gold production will increasingly become more important. Other commodity production remains healthy. Inflation has climbed rapidly and looks to be sticky. The central bank has kept a 'moderate contractionary monetary policy' stance to keep inflation in the single digit levels.

Daniel Wilson

QUARTERLY ECONOMIC DATA	DEC-09	MAR-10	JUN-10	SEP-10	DEC-10	MAR-11	JUN-11	SEP-11
Domestic Credit, % y/y	-7.9	-8.0	-5.7	-10.7	-4.8	-10.6	N/A	N/A
Consumer Price Index % y/y	1.3	1.6	1.0	0.7	1.0	2.9	7.2	N/A
Exports, % y/y	-27.8	1.5	35.3	29.4	82.1	51.6	93.6	73.7
Imports, % y/y	-7.3	-0.8	62.8	32.5	90.2	30.9	-0.6	32.6
Trade Balance, US\$m	-225.4	-164.6	-322.6	-196.5	-304.5	-140.6	77.3	-61.2
Foreign Exchange Reserves, US\$ mn	144.0	156.0	183.9	211.9	265.0	289.0	353.0	N/A

Sources: Central Bank of the Solomon Islands, ANZ Economics



## Timor-Leste

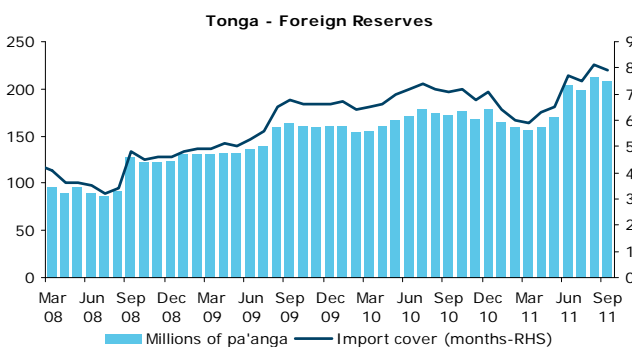
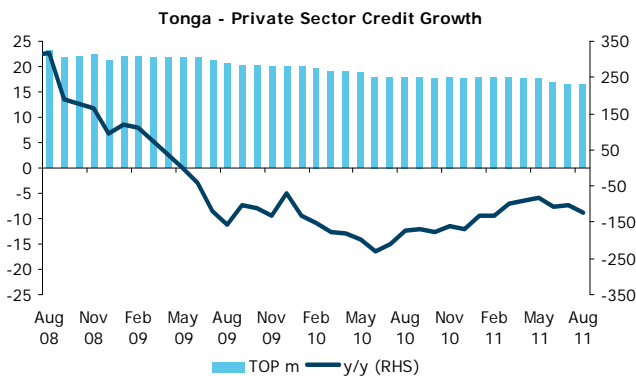
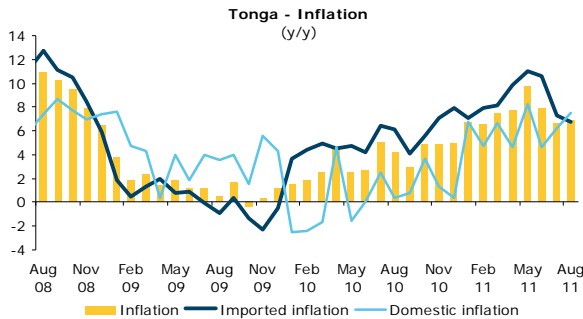
**Non-oil trade figures have been normalising in the past three months, while strong credit growth suggests healthy activity. Inflation pressures persist with the headline still in double digits.**

- Total non-oil exports grew 60.4% y/y in August, up from -28.0% in the previous month. Re-exports grew 118.4%. Total non-oil imports, on the other hand, grew 237.5%, up from 32.6% in July. Non-oil trade flows seem to have recovered from their odd slump from January to May, when flows halted.
- Inflation in the Dili region rose to 13.8% y/y in September from 13.0% previously. Overall CPI for Q3 remained at 12.4%. Main drivers of inflation were food (15.8%), transport (14.8%) alcohol and tobacco (13.2%) and clothing (12.9%).
- Growth in outstanding credit to the private sector rose to 23.1% y/y in Q3 from Q2's 17.4%. However, credit growth moderated to 1.9% on a q/q basis, after its 13.9% spike in Q2. No sectoral breakdown has been released, but there has been no consistent main driver of private sector loans. Meanwhile, the ratio of non-performing loans to total outstanding loans rose further by 0.3ppt to 39.1% in Q3.
- Broad money growth spiked to 24.1% y/y in September, from 14.7% in August. On a m/m basis, money growth increased from -1.1% to 7.1%.
- The value of the Petroleum Fund as of end-August reached \$8.8bn, up from \$8.6bn prior. Net returns for the month of August were \$39.4mn, or 0.4%.
- After five months of negligible non-oil trade flows, activity has begun to pick up again since June. However, these flows form an insignificant part of the overall current account balance, while their negative effect on non-oil GDP may be partially mitigated by the projected 40% rise in government spending for 2011 (IMF). Meanwhile, inflation is still rising, as accelerating money supply growth is adding on to food and transport price pressures.

*Vincent Conti*

QUARTERLY ECONOMIC DATA	DEC-09	MAR-10	JUN-10	SEP-10	DEC-10	MAR-11	JUN-11	SEP-11
Mobile Subscribers, % YOY	180.7	181.8	145.5	N/A	N/A	N/A	N/A	N/A
Visitor Arrivals, % YOY	21.0	14.1	2.8	N/A	N/A	N/A	N/A	N/A
Consumer Price Index, % YOY	1.1	3.7	2.5	8.0	8.0	12.1	12.4	12.4
Exports, US\$m	9.2	3.9	10.4	15.2	12.2	0.1	2.4	N/A
Imports, US\$m	66.4	62.8	86.5	67.5	81.2	8.4	41.5	N/A
Trade Balance, US\$ mn	-57.2	-59	-76.1	-52.3	-69.0	-6.4	-39.1	N/A

Sources: Timor-Leste National Directorate of Statistics, Banking and Payments Authority of Timor-Leste, ANZ Research



## Tonga

The economic recovery remains fragile with private sector credit still under pressure from ongoing consolidation in the banking sector. In addition, exports were again weak while inflation pressures are rising. On a positive note, tourism inflows and private remittances continued to be resilient.

- Tourist receipt growth moderated to 14.6% y/y in August, from 18.9% in July. Receipts totalled TOP58.9mn, down slightly from TOP60.3mn in July.
- Private remittances fell by 7.5% y/y in August, following a 5.9% decline in the previous month. Remittances totalled TOP144.9mn.
- Export growth continued to contract in August, down 2.5% y/y from -4.5% in July. However, import growth remains positive at 5.3%, against 8.2%, previously.
- Inflation rose to 6.9% y/y in August following a 6.6% increase in July. Imported inflation moderated to 6.8%, down 0.5ppt; however, domestic inflation climbed 1.3ppts to 7.5%.
- Official foreign reserves declined to TOP208.1mn (\$127mn) in September from TOP212.4mn, equivalent to 7.9 months of imports.
- Private sector credit growth contracted further in August, falling by 8.9% y/y from -7.4% in July. Credit to households and businesses contracted by 5.9% and 9.0%, respectively.
- Tonga's economy remains heavily dependent upon remittances, tourism, and trade. The constant threat of natural disasters has depressed investment in its manufacturing industry.
- Looking ahead, in a volatile global climate, Tonga may suffer more than other Pacific economies as domestic activity is not spurring growth.

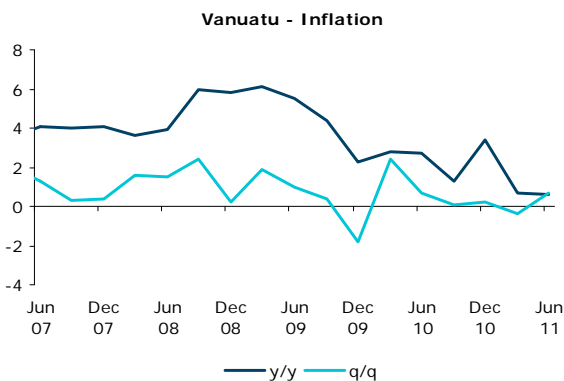
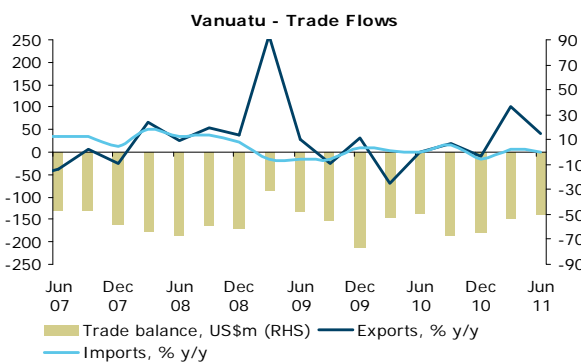
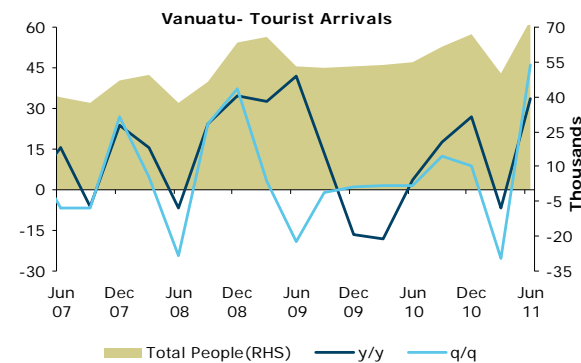
*Daniel Wilson*

QUARTERLY ECONOMIC DATA	DEC-09	MAR-10	JUN-10	SEP-10	DEC-10	MAR-11	JUN-11	SEP-11
Consumer Price Index, % y/y	0.4	2.0	3.3	4.1	4.9	6.9	7.9	6.8
Private Sector Credit, % y/y	-8.2	-10.9	-14.6	-13.2	-12.2	-8.7	-7.6	-8.2
Exports, % y/y	-3.3	-10.0	0.3	2.1	3.4	-22.2	N/A	N/A
Imports, % y/y	2.0	-7.2	-2.1	8.3	12.0	12.4	N/A	N/A
Trade Balance, US\$ mn	-76.1	-57.7	-67.0	-75.8	-85.7	-65.8	N/A	N/A
Foreign Exchange Reserves, US\$ mn	84.8	81.1	87.4	91.5	97.9	86.6	119.4	127.0

Sources: National Reserve Bank of Tonga, Tonga Department of Statistics, ANZ Research

## Vanuatu

Domestic activity, exports and tourism performed well in Q2. However, the external sector faces headwinds from the falloff in global commodity prices. With construction activity yet to see a pronounced pickup, we expect GDP growth will be around 3.8% for 2011.



- Domestic indicators held up well in Q2. Production of copra, a major export commodity, rose 37.0% y/y (3.2% q/q) on account of favourable prices while production and exports of kava and cocoa were also strong. VAT collections, important consumption indicators, were robust as well.
- Exports surged 71.4% y/y in August against a 7.5% decline in July, mostly due to base effects arising from higher shipments of copra, fish and other products. Import growth rose to 15.9% in August vs. July's 11.3%. The trade deficit widened to VUV2.2bn in August from July's VUV2.1bn.
- Visitor arrivals rose 1.3% y/y (27.0% m/m) in July, compared with June's 3.5%. Cruise ship arrivals rose by 22%, but fell sharply (-38.0%) on a m/m basis. Visitor arrivals, meanwhile, rose by a strong 33.7% in Q2.
- Domestic credit expanded 13.5% y/y in August from 11.6% in July. Private sector credit growth advanced to 9.4% in August from July's 7.8%, with loans to businesses and individuals rising by 15.2% and 7.6%, respectively.
- The RBV's macroeconomic committee upgraded its 2011 GDP growth forecast by 1ppt to 4.0% in August. It expects the industrial sector to grow by 10.4%, with an increase in manufacturing activity expected to offset slower construction output. Services and agriculture may grow by 3.1% and 2.9% respectively. 2012 and 2013 forecasts were revised up to 4.9% and 4.7%.
- Though we broadly concur with the central bank on an improved domestic growth profile, we think the external sector will weigh on growth due to the falloff in commodity prices in Q3 and Q4. As a result, we expect 2011 growth to be around 3.8%. 2012 should see stronger results if construction activity picks up.

*Raj Gopalakrishnan*

QUARTERLY ECONOMIC DATA	SEP-09	DEC-09	MAR-10	JUN-10	SEP-10	DEC-10	MAR-11	JUN-11
Consumer Price Index, % y/y	4.4	2.3	2.8	2.7	2.3	3.4	0.7	0.7
Tourist (thousands)	53.9	53.0	53.9	54.8	61.7	67.3	50.1	73.3
Exports, % y/y	-29.8	28.3	-68.0	21.0	18.6	-10.6	99.9	42.3
Imports, % y/y	-14.7	9.8	2.8	-0.9	17.1	-15.9	6.6	-1.2
Trade Balance, US\$ mn	-55.0	-72.6	-52.6	-46.4	-67.0	-65.3	-53.1	-49.9
Foreign Exchange Reserves, US\$ mn	157.0	148.9	151.8	152.0	160.0	159.1	165.1	175

Sources: Reserve Bank of Vanuatu, ANZ Economics



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