

14 August 2009

**Global Markets – Asia Team :**

EconsAndResearchAsia@anz.com

**Paul Gruenwald**

Chief Economist, Asia  
+65 6216 1814  
Paul.Gruenwald@anz.com

**Tamara Henderson**

Director, FX and Rates Strategy  
+65 6216 1845  
Tamara.Henderson@anz.com

**Yeo Han Sia**

Associate Director,  
FX and Rates Strategy  
+65 6419 7930  
HanSia.Yeo@anz.com

**Franklin Poon**

Economist, North East Asia  
+852 3929 5340  
Franklin.Poon@anz.com

**Chang Wei Liang**

Analyst, Economic Research  
+65 6216 1838  
Weiliang.Chang@anz.com

**Research Interns:**

Zhou Hao  
Ray Lam  
Raj Gopalakrishnan

**Our Vision:**

For Economics & Markets Research to be the most respected, sought-after and commercially valued source of economics and markets research and information on Australia, New Zealand, the Pacific and Asia.

## Highlights

- The global crisis continues to take a toll on the Pacific economies as external inflows—exports, tourism, and remittances—are down sharply in most countries.
- Domestic demand performance has been mixed across the region since the onset of the crisis. Inflation has proved resilient in a number of economies, limiting the room for central banks to ease monetary conditions. Most governments continue to use fiscal policy to support demand and activity.
- The Pacific currencies have strengthened against the USD in tandem with the improvement in global risk appetite and further appreciation is expected as the global recovery gains momentum. Samoa's WST has out-performed, rising more than 10% year-to-date, while Papua New Guinea's kina has under-performed.
- Like elsewhere in the global economy, the pace of recovery in the Pacific should be slow. A positive factor going forward is the region's strong linkages to Australia, which has outperformed amongst the advanced economies.

## Table of Contents

<b>Feature Article: The Effect of the Crisis on Tourism in the Pacific.....</b>	<b>2</b>
<b>Financial Markets Update .....</b>	<b>4</b>
<b>FX and Policy Interest Rate Forecasts .....</b>	<b>5</b>
<b>Macroeconomic Forecasts .....</b>	<b>6</b>
<b>Country Updates:</b>	
• Fiji.....	7
• Papua New Guinea.....	8
• Samoa.....	9
• Solomon Islands.....	10
• Timor-Leste.....	11
• Tonga.....	12
• Vanuatu.....	13

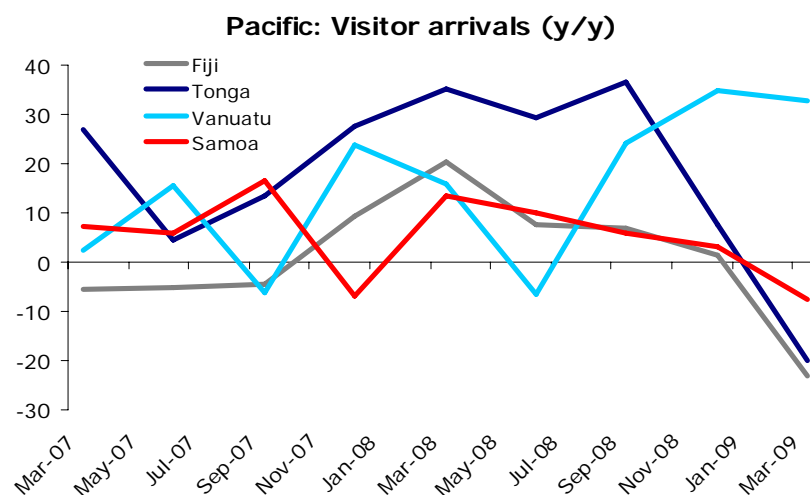
## Feature Article – The Effect of the Crisis on Tourism in the Pacific

While much focus has been placed on the trade transmission channel from the advanced economies to the rest of the world, tourism is an important source of foreign exchange for a number of Pacific economies. This is particularly true for Fiji, Samoa, Tonga and Vanuatu. In this article we look at recent trends in tourism across the relevant Pacific economies and conclude that the worst is likely over and that there is some evidence of positive “substitution effects.” Given limited data availability, these findings are more suggestive than definitive.

**Tourism, as opposed to trade in goods, is a key part of the external sector in several Pacific economies.** As noted in our November 2008 *Pacific Quarterly*, the dependency of the region on tourism employment is nearly twice the global average, and a number of countries rely heavily on tourism flows in the balance of payments. This high level of dependency is particularly true for Fiji, Samoa, Tonga and Vanuatu.<sup>1</sup> In the current environment, it is important to know how the demand shock arising from the global economic crisis has affected the main source of foreign exchange for these economies—tourism receipts. Much of the rest of the Pacific region relies more on goods, especially commodity exports, as the main source of foreign exchange.

**We would stress up front that our analysis is constrained by data coverage and timeliness, and the usual caveats apply.** Data often are available with long lags and coverage across countries is not necessarily consistent. This places considerable constraints on our ability to undertake rigorous analysis. As a result, the findings of this article should be taken as suggestive rather than definitive.

**An interesting question is whether Pacific tourism has benefited from “substitution effects.”** The drop in incomes worldwide has led to a sharp drop in discretionary consumption, including luxury goods and tourism. At the same time, there has been some substitution away from consuming luxury goods toward consuming more “normal” lower cost goods. In the tourism sector, this could be, for example, an Australian family taking a trip to the Pacific as opposed to Europe.

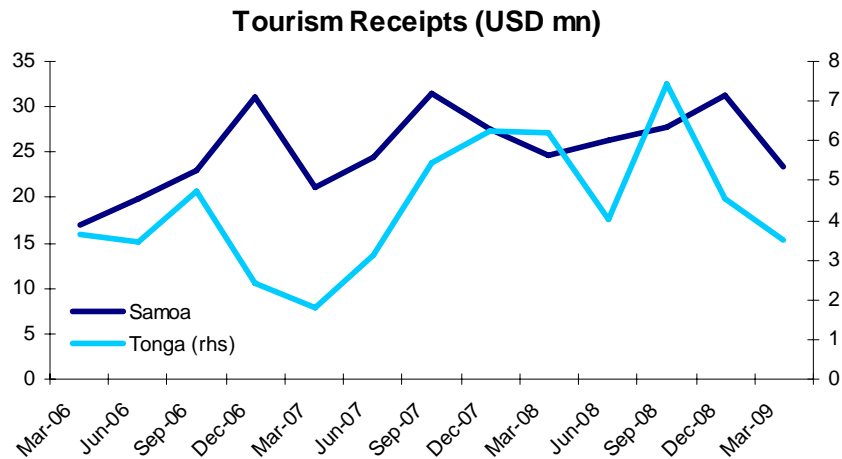


**The data show that visitor arrivals to the Pacific have dropped sharply, although there has been some substitution of tourism flows within the region.** Looking at arrivals numbers through early 2009, there has been a noticeable decline over the past few quarters as the global economic crisis has intensified. However, one market, Vanuatu, has seen arrivals rise sharply over the same period. This rise has been attributed to Vanuatu’s proximity to Australia, as well as a sharp increase in air service capacity over the past two years.<sup>2</sup>

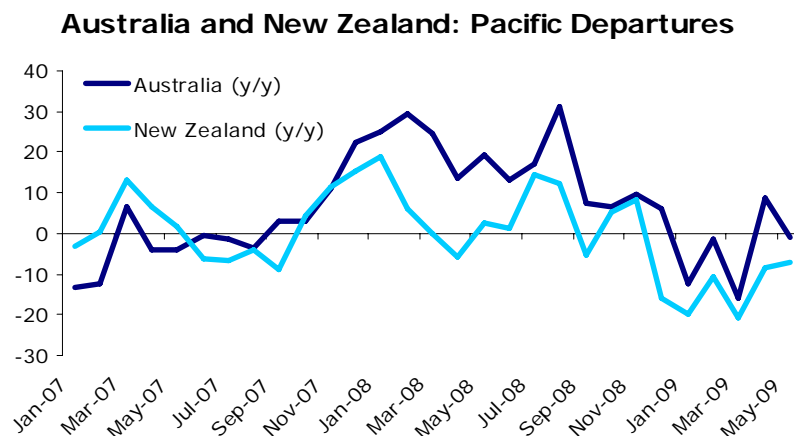
<sup>1</sup> The Cook Islands, which is not covered in this report, derives over 50% of its GDP from this tourism.

<sup>2</sup> There is evidence—namely, an uplift in forward bookings—that tourism-related flows to Fiji are picking up following the devaluation in April 2009, although there are insufficient data at present to substantiate this.

**Data for tourism receipts show a similar story.** Here data are limited to Samoa and Tonga and in both cases receipts have fallen considerably since recent peaks. Samoa's receipts have fallen by one-quarter from a peak in Q4 2008, although they are down only 5% year-on-year in the first quarter of 2009. Tonga's receipts have been hit hard, having fallen by more than one-half since a peak in Q3 2008 and are down 45% year-on-year in Q1 of this year.



**Near-term Pacific tourism flows can be proxied by departures data from Australia and New Zealand, which have begun to turn around.** These two countries are the principal “supply side” of Pacific tourism flows. (The United States and Japan are important source markets as well, but data on Pacific departures are not published.) The pattern of departures appears to be a “high-beta” on the real economy, underscoring the notion that tourism is a luxury good. Departure growth measured on a year-on-year basis from Australia was running in the double digits until Q3 2008, when growth declined and turned negative in early 2009. For New Zealand, the up-turn in 2008 was less pronounced, but departure growth turned down at the same time as Australia and fell at double digit rates earlier this year. Departure growth bottomed in both economies in Q2 2009, although it remains negative on a trend basis.



**A recovery in tourism related flows to the Pacific should be modest.** This forecast tracks our house call for a gradual recovery in discretionary consumption spending from the advanced economies over the next year or two. While the worst has likely past, we see considerable scope for soft tourist spending growth going forward. At the sub-regional level, we may continue to see some substitution effects within the Pacific and in this regard Fiji will be important to watch given the devaluation as well as some recent international recognition of some tourist facilities there.

*Paul Gruenwald*  
*Raj Gopalakrishnan*  
*Ray Lam*

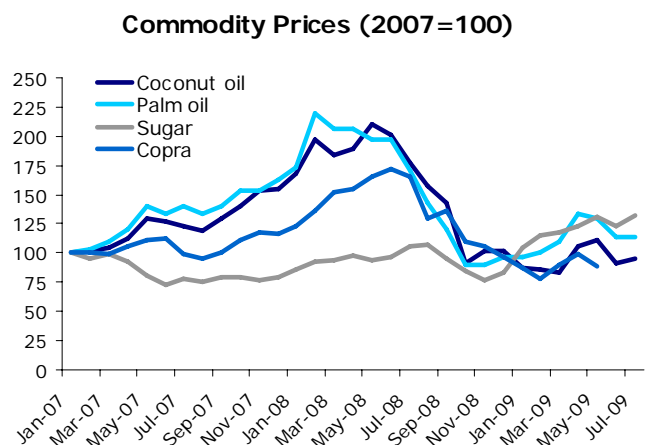
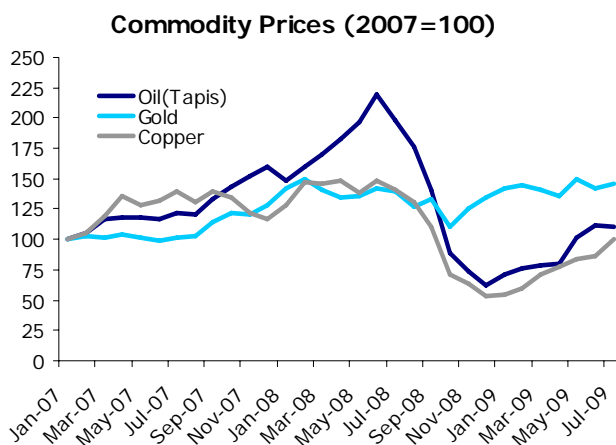
## Financial Markets Update

### Exchange Rates

- Risk appetite has been rebuilding since March, weighing on the US dollar as liquidity starts to get put back to work.
- The Australian and New Zealand dollars have rallied sharply this year against the US dollar, up 19% and 16%, respectively.
- The Pacific currencies have similarly strengthened against the US dollar, albeit with much less volatility.
- Samoa's WST has out-performed within the group of countries that we cover, rising more than 10% year-to-date, while Papua New Guinea's kina has under-performed.

### Commodities

- Commodity prices have troughed, supported by signs that the contraction in global growth has bottomed. Going forward, commodity prices are broadly expected to exhibit a shallow uptrend during the second half of 2009 in line with our outlook for a tepid recovery in global demand.
- Crude oil prices are back near the \$70/bbl level, compared with the cyclical low near \$34 last December. Our year-end target in WTI NYMEX crude is \$80/bbl.
- Gold has been largely range-bound since hitting a peak of \$1,006/oz in February. Admittedly, the range has been wide (between \$864 and \$1006), and it would seem that a pattern of slightly lower highs is slowly emerging. The current range should continue to hold in the second half of 2009. Our year-end forecast is set at \$980/oz compared with the current level near \$960.
- Base metal prices should continue to benefit from further signs of recovery in China.



Tamara Henderson  
Ray Lam  
Raj Gopalakrishnan

## FX and Policy Interest Rate Forecasts

		Jun 09	Current	Sep 09	Dec 09	Mar 10	Jun 10	Sep 10	Dec 10
<b>Fiji</b>	FJD-USD, eop	0.489	0.498	0.483	0.472	0.469	0.476	0.480	0.486
	FJD-AUD, eop	0.608	0.594	0.589	0.590	0.586	0.574	0.571	0.565
	Short term rates*	4.25	4.25	4.25	4.25	4.25	4.25	4.50	4.75
<b>Papua New Guinea</b>	PGK-USD, eop	0.382	0.382	0.395	0.374	0.392	0.381	0.395	0.386
	PGK-AUD, eop	0.473	0.456	0.481	0.468	0.491	0.459	0.470	0.449
	Short term rates**	8.00	8.00	8.00	8.25	8.50	9.00	9.50	9.50
<b>Samoa</b>	WST-USD, eop	0.374	0.380	0.386	0.379	0.377	0.385	0.387	0.393
	WST-AUD, eop	0.464	0.454	0.471	0.474	0.472	0.464	0.461	0.457
<b>Solomon Islands</b>	USD-SBD, eop	7.926	7.901	7.873	7.982	8.012	7.962	7.972	7.972
	AUD-SBD, eop	6.392	6.609	6.46	6.39	6.41	6.61	6.70	6.86
<b>Tonga</b>	USD-TOP, eop	2.051	1.965	1.91	1.86	1.85	1.91	1.94	1.98
	AUD-TOP, eop	1.654	1.644	1.57	1.49	1.48	1.59	1.63	1.70
<b>Vanuatu</b>	USD-VUV, eop	105.68	105.10	107.0	105.0	100.0	95.0	95.0	95.0
	AUD-VUV, eop	85.22	87.92	87.7	84.0	80.0	78.8	79.8	81.7
	Short term rates***	6.00	6.00	6.00	6.00	6.25	6.50	6.50	6.50

Note: The source of FX data is Bloomberg. As the currencies are illiquid with wide bid/offer spreads, the rate published is only indicative. (\*) 91-day RBF notes, (\*\*) Kina Facility Rate, (\*\*\*) Rediscount rate, (Current) 7 August 2009.

## Macroeconomic Forecasts

**Real GDP Growth (%)**

	2008e	2009f	2010f
<b>Fiji</b>	1.2	-2.0	-1.0
<b>PNG</b>	7.0	5.0	6.5
<b>Samoa</b>	-3.4	1.9	2.2
<b>Solomon Is.</b>	6.4	3.0	3.0
<b>Timor-Leste</b>	10.0	8.0	8.0
<b>Tonga</b>	1.2	-2.0	0.0
<b>Vanuatu</b>	6.6	4.0	4.5

**Nominal GDP (US\$ bn)**

	2008e	2009f	2010f
<b>Fiji</b>	3.4	3.5	3.6
<b>PNG</b>	8.1	9.2	10.4
<b>Samoa</b>	0.5	0.5	0.5
<b>Solomon Is.</b>	0.5	0.5	0.5
<b>Timor-Leste</b>	0.4	0.4	0.5
<b>Tonga</b>	0.3	0.3	0.3
<b>Vanuatu</b>	0.5	0.5	0.6

**Inflation (%)**

	2008	2009f	2010f
<b>Fiji</b>	7.6	5.0	3.0
<b>PNG</b>	11.2	10.0	9.0
<b>Samoa</b>	11.4	7.6	6.5
<b>Solomon Is.</b>	16.5	9.0	5.0
<b>Timor-Leste</b>	8.4	6.0	6.0
<b>Tonga</b>	9.9	5.0	2.0
<b>Vanuatu</b>	5.8	4.2	3.5

**Fiscal Balance (% of GDP)**

	2008e	2009f	2010f
<b>Fiji</b>	-1.5	-3.5	-2.5
<b>PNG</b>	4.5	0.0	2.0
<b>Samoa</b>	-3.2	-8.0	-4.0
<b>Solomon Is.</b>	-5.6	-3.0	-3.0
<b>Timor-Leste</b>	-43.0	-65.0	-60.0
<b>Tonga</b>	2.0	-1.5	-1.0
<b>Vanuatu</b>	2.2	1.5	1.8

**Current Account Balance (% of GDP)**

	2008e	2009f	2010f
<b>Fiji</b>	-21.0	-25.0	-25.0
<b>PNG</b>	69.3	-0.8	50.0
<b>Samoa</b>	-7.8	-9.8	-8.5
<b>Solomon Is.</b>	-4.9	-10.1	-12.1
<b>Timor-Leste</b>	408.3	66.2	49.4
<b>Tonga</b>	-10.4	-8.8	-8.7
<b>Vanuatu</b>	-7.4	-7.0	-6.5

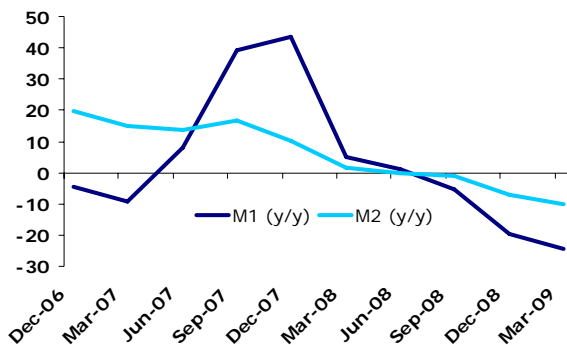
**Foreign Exchange Reserve (US\$ mn)**

	2008	2009f	2010f
<b>Fiji</b>	497	530	500
<b>PNG</b>	2,093	2,200	2,400
<b>Samoa</b>	81	115	120
<b>Solomon Is.</b>	93	100	100
<b>Timor-Leste</b>	4,640	5,333	6,676
<b>Tonga</b>	58	54	50
<b>Vanuatu</b>	109	100	105

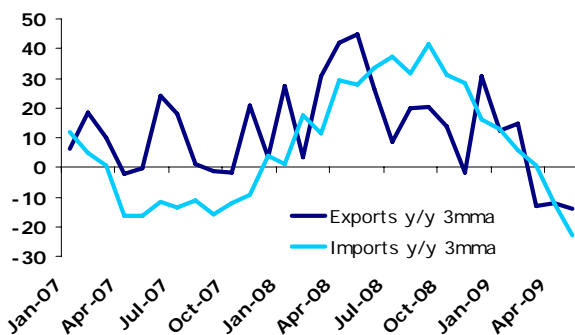
Sources: Asian Development Bank, various country websites, ANZ Economics.

## Country Update: Fiji

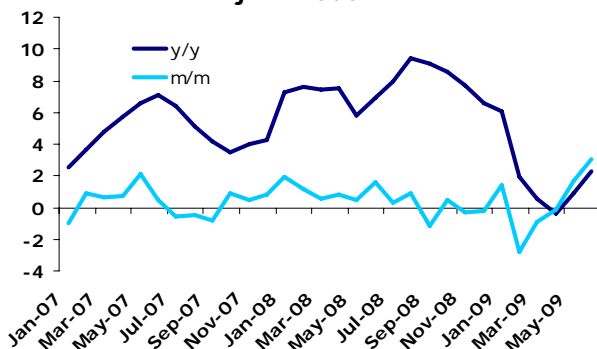
Fiji - Monetary Aggregates



Fiji - Trade Developments



Fiji - Inflation



**Demand developments are mixed with consumption soft but some resilience in investment. Exports remain weak, although remittances and tourism may benefit from the recent devaluation. Inflation pressures have picked up as the effects of the devaluation pass through; the RBF rightfully maintains its tight policy stance. The recovery is likely to be slow.**

- Consumption indicators remain sluggish as evidenced by annual declines in VAT collections (2%), new vehicle sales (22%) and import payments (16%). In contrast, building and construction activity is improving with work put in place rising 29% in Q1 and building certificates rising by 3½% in volume and 68% in value.
- Trade data remain weak. Provisional numbers show imports falling 37.7% (y/y) in May with imports from Singapore (led by oil) dropping 72.9%. Exports declined by 12.6% and the trade deficit halved from a year ago to FJD98.8mn.
- Inflation slowed to 2.3% (y/y) in Jun from 2.8% in Mar. For the month, though, inflation was 2.9% (the highest since Feb 1998) reflecting the pass-through from the April 2009 devaluation.
- Tourist arrivals have fallen 19.4% (y/y, YTD) through April, although the devaluation and hotel promotions may spark some upside. Remittances in FJD rose by 14.9% (y/y, YTD) through May, driven mainly by a weaker exchange rate.
- Narrow and broad money continued to decline reflecting a fall in demand deposits. Narrow money fell 26.7% (y/y) in May, while broad money fell 5.7%. Cumulative to May, credit for consumption fell 27.9% while investment credit declined sharply by 57.5%.
- At its Jul meeting the Reserve Bank of Fiji (RBF) retained its policy indicator rate at 4.25%. The RBF said a "tight ... stance" is required owing to ample liquidity and inflation pressures related to the devaluation.
- We retain our call for a 2% contraction in activity this year. The outlook remains weak owing to sluggish growth in Fiji's trading partners as well as weak domestic consumption. The RBF will need to remain vigilant in order to contain any second-round inflation effects from the devaluation.

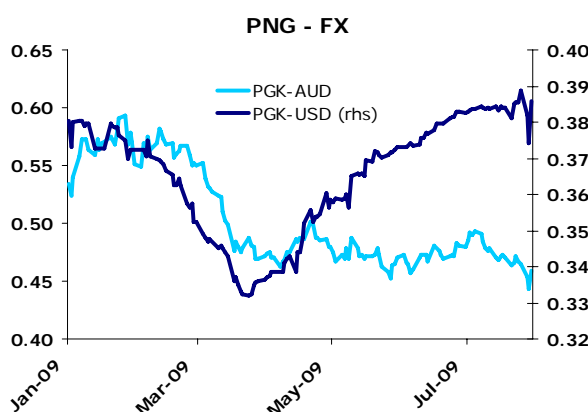
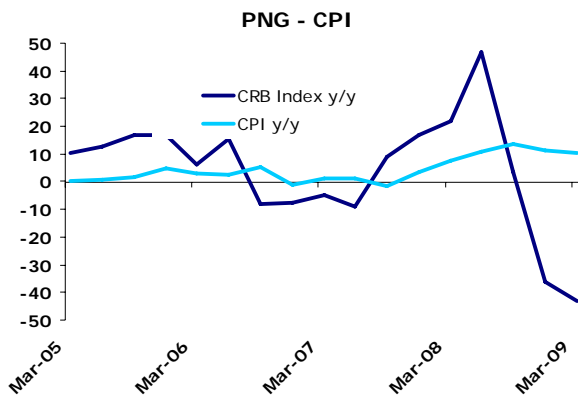
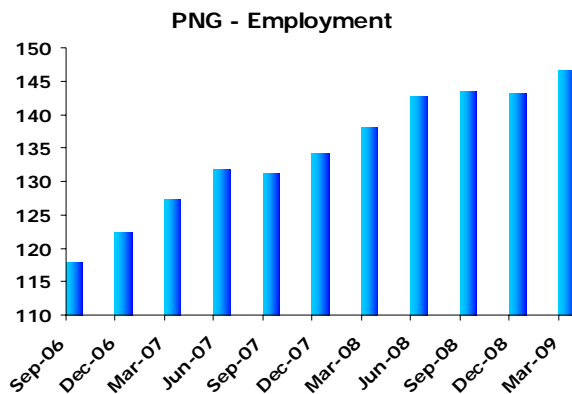
Paul Gruenwald

### Economic Data – Fiji

Quarterly data	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08	Mar 09
Consumer Price Index, % YOY	6.4	5.2	3.9	7.6	6.8	9.0	7.6	2.8
Domestic Credit, % YOY	12.5	8.5	3.2	3.0	3.8	4.7	4.8	5.0
Exports, % YOY	24.0	-3.3	-4.0	26.8	20.2	21.3	19.6	-13.0
Imports, % YOY	-11.6	-15.9	2.7	8.6	38.2	40.9	16.1	-0.2
Trade Balance, US\$ mn	-240	-274	-310	-275	-384	-375	-310	-478
Official Reserves, US\$ mn	542	630	751	699	663	646	497	368

Sources: Reserve Bank of Fiji, ADB, IMF

## Country Update: Papua New Guinea



**Economic growth and inflation moderated in Q1, but both are likely to pick up during the course of the year. The central bank (BPNG) has remained vigilant on inflation, holding the policy rate steady amid the sharp contraction in global trade and aggressive stimulus measures elsewhere in the world. Fortuitous timing of LNG-related investment flows has sustained domestic sentiment and strengthened the country's external position.**

- Economic growth is still expected to slow to 5.0% in 2009 from an estimated 7.0% in 2008, but the balance of risks to this forecast has shifted to the upside.
- Goods exports fell 34.9% (y/y) in Q1 (despite a sharp increase in the shipment of gold, one of PNG's primary exports), the trade surplus has shrunk sharply, and there has been little sign of a pickup in global demand thus far.
- Domestically, the impact of the global slowdown on labour market conditions has been relatively benign with private sector employment still rising 6.1% (y/y) in Q109 compared with growth of 6.7% in Q408.
- Inflation has moderated, but remains in the double-digits at 10.2% (y/y) as of Mar compared with 11.2% in Dec.
- Money growth (M3) slowed to 5.0% (y/y) in May from 11.2% at the end of 2008, and the average lending rate increased to 10.2% in May versus 8.8% in Dec. However, outstanding loans by commercial banks were still up nearly 48% (y/y) in Mar compared with 38.4% a year before.
- BPNG has left its Kina Facility Rate unchanged for eight consecutive months, compared with aggressive easing over the same period by central banks elsewhere in the world, but the kina has weakened in trade-weighted terms.
- Given signs that PNG is weathering the global slowdown relatively well and that the dissipation of domestic inflationary pressures has been limited, there is increasing risk that BPNG will resume its tightening cycle before year-end. As the economy will still face cross-currents from the local and global economies until foreign demand normalises, any monetary tightening will likely be gradual for some time to come.

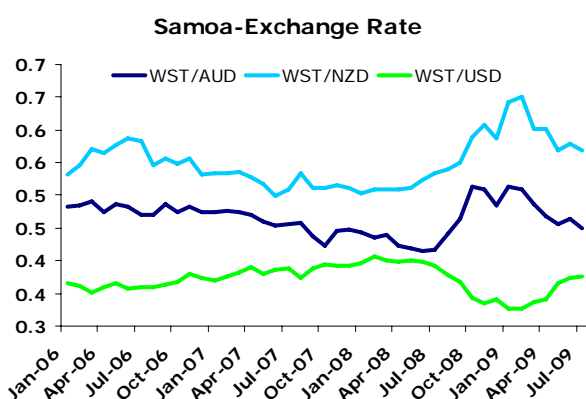
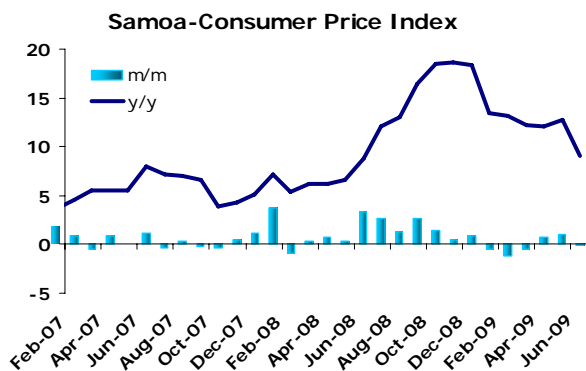
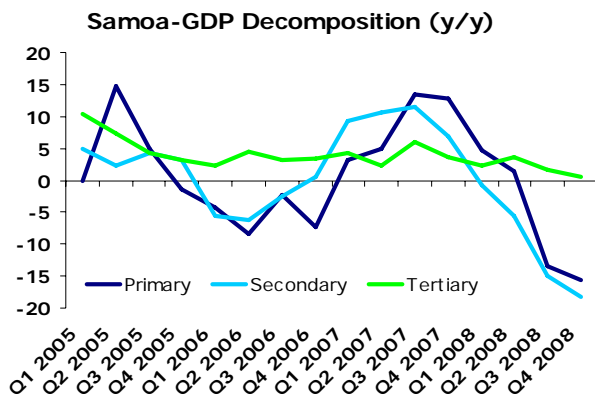
Tamara Henderson

### Economic Data – Papua New Guinea

Quarterly data	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08	Mar 09
Employment Index, % YOY	9.5	11.7	10.4	8.5	8.3	9.3	6.7	6.1
Consumer Price Index, % YOY	1.0	-1.6	3.2	7.5	10.7	13.5	11.2	10.2
- BPNG Trimmed mean, % 000	2.9	3.6	5.3	8.7	11.4	13.0	11.7	7.9
- NSO exclusion based, % 000	7.5	9.0	6.3	7.7	10.2	12.2	11.0	10.7
Exports of goods (BOP basis), % YOY	6.9	-40.6	12.9	24.2	11.2	112.4	-2.6	-34.9
Imports of goods (BOP basis), % YOY	26.4	117.7	25.1	6.0	29.2	-36.8	-8.3	-16.2
Trade Balance (goods, BOP basis), US\$ mn	2,083	1,493	1,411	1,724	1,994	1,909	1,496	734
Foreign Exchange Reserves, US\$m	1,545	1,856	2,053	2,039	2,418	2,454	2,093	1,950

Source: Bank of Papua New Guinea

## Country Update: Samoa



**The economy contracted by 3.4% in 2008, the worst performance in a decade. However, the economy is positioned for a modest boost given government stimulus efforts and seasonal remittance and tourism inflows.**

- The economy contracted by 3.4% (y/y) in 2008 as a whole, with the biggest contribution coming from Q4, when GDP fell by 7.3% (y/y). Although the services sector remained resilient, poor performance in primary and secondary industries dragged overall growth into negative territory.
- Headline inflation slowed to 9.1% (y/y) in Jun from May's 12.8% and Apr's 12.1%. Monthly inflation was flat in June following increases of 0.7% and 1.0% in Apr and May, respectively.
- Exports remain weak, falling 21.3% (y/y) in Q2 after contracting 2.6% in Q1. However, the contraction in imports fell by 7 pts to -18.5% (y/y) in Q2, reflecting the rising cost of construction related to government stimulus efforts. The trade deficit widened to \$42.5mn in Q2 from Q1's -\$39.4mn.
- Tourism receipts and private remittances are important to finance the long-existing trade deficit. Tourist arrivals (including cruise ships, which impart a sizeable amount of volatility to the data) in Q2 remained unchanged from a year earlier, compared with a decline of 7.6% (y/y) in Q1. Meanwhile, private remittances rose 6.0% in the fiscal year 2008/09 (ending in Jun).
- Money supply and credit rose steadily, expanding 7.7% (y/y) and 9.2% respectively in Q2. This reflected a pick-up in foreign reserves (owing to unsterilised inflows) as well as the central bank's efforts in easing monetary conditions.
- Foreign reserves rose to \$100.4mn at end-Jun, up \$15.7mn from Q1 on the back of private remittance inflows and a pick-up in tourism receipts.
- The WST has continued to appreciate, rising more than 10% year-to-date, largely due to a weaker US dollar.
- Looking ahead, year-on-year GDP growth will likely remain negative through the middle of 2009, but turn positive toward the end of this year as the global downturn eases and domestic demand recovers.

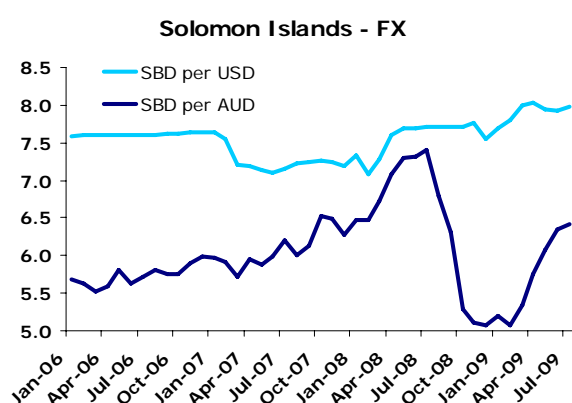
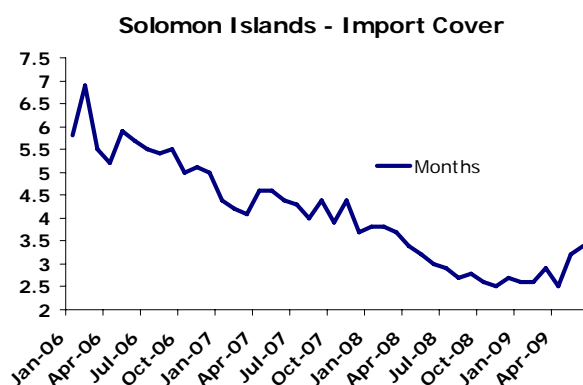
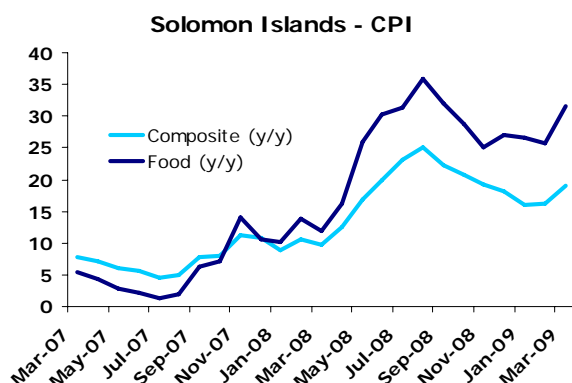
Zhou Hao

### Economic Data – Samoa

Quarterly Data	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08	Mar 09
Consumer Price Index, % YOY	6.3	7.0	4.5	6.3	7.2	13.9	18.4	13.0
Domestic Credit, % YOY	16.3	20.1	15.9	8.4	11.9	6.7	9.9	6.9
Exports, % YOY	55.6	79.0	33.7	-4.5	-18.7	-26.5	-42.0	-2.6
Imports, % YOY	17.3	12.3	-10.2	-15.2	-0.4	13.9	12.6	-25.9
Trade Balance, US\$ mn	-52.3	-61.9	-50.2	-54.4	-52.5	-72.2	-58.5	-39.4
Foreign Exchange Reserves, US\$ mn	80.4	82.3	90.2	100.6	101.5	90.2	81.3	84.8

Sources: Central Bank of Samoa, Samoa Ministry of Finance

## Country Update: Solomon Islands



***Inflation remains high, but pressures have eased. Meanwhile, improved export and tourism earnings have led to some improvement in the balance of payments. That said, continued tight monetary and fiscal policies are required to further reduce BOP pressures and a resurgence of inflation. We now see the risks to growth as broadly balanced.***

- Reflecting the slump in Asian demand, log production dropped by 40% (y/y) during Jan-May. In Jun, however, output was more than double May's level, driven by improvements in weather conditions as well as the stockpiles at log ponds around the country. Log prices also rose 4.8% (y/y) in Jun.
- Exports rose 5.4% (m/m) in Jun, helped by receipts from logs, cocoa and copra, which increased by 0.7%, 7.8% and 35.9%, respectively.
- Reflecting new Pacific Blue flights from Brisbane, total visitor arrivals by air grew 44% (y/y) in Q1 with Australia accounting for 45% of the total.
- The increase in export and tourist earnings, together with foreign exchange revaluation gains, boosted gross external reserves to \$98.2mn in Jun. The level of reserves is now equivalent to 3.4 months of imports, having moved back above the 3 month benchmark.
- The CPI rose 19.1% (y/y) in Mar, on food and petrol prices partly related to flooding. Mar's inflation was higher than the pace of 16.0% and 16.2% recorded for Jan and Feb, but was slower than the 25% peak in Aug last year.
- The government debt stock stood at \$177.4mn in Jun, equivalent to 35% of GDP, largely unchanged from May's level. The government needs to run a tight stance to help further strengthen the country's BOP position.
- The central bank has tightened monetary policy in response to strong inflation in H2 2008 and suggested in its recent policy statement that it would not loosen its stance anytime soon.
- We maintain our growth forecast at 3% for 2009, with the risks now broadly balanced given the Solomon's relatively high exposure to China.

*Franklin Poon*

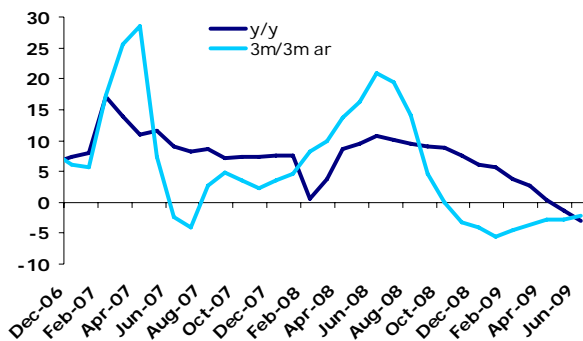
### Economic Data – Solomon Islands

Quarterly data	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08	Mar-09
Domestic Credit, % YOY	60.1	74.4	56.6	47.8	63.3	35.9	39.0	27.7
Consumer Price Index, % YOY	6.3	5.8	10.0	9.7	16.5	23.5	19.4	17.1
Exports, % YOY	9.7	35.1	72.3	24.0	93.6	44.5	2.2	-11.1
Imports, % YOY	21.7	27.5	39.2	1.4	34.9	13.5	15.8	35.5
Trade Balance, US\$ mn	-33.0	-36.7	-31.7	-27.2	-23.1	-26.5	-41.9	-52.7
Foreign Exchange Reserves, US\$ mn	118.4	124.1	127.8	117.9	100.8	98.3	93.3	84.7

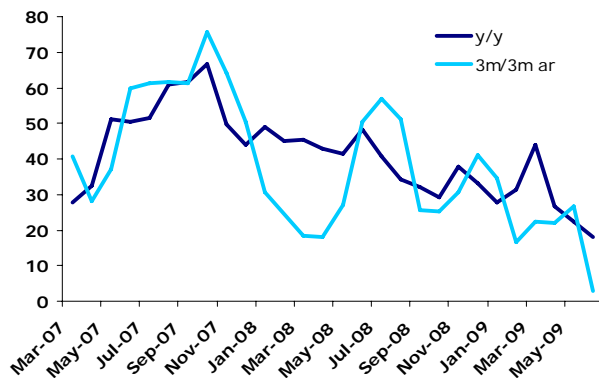
Sources: Central Bank of Solomon Islands, ADB, IMF

## Country Update: Timor-Leste

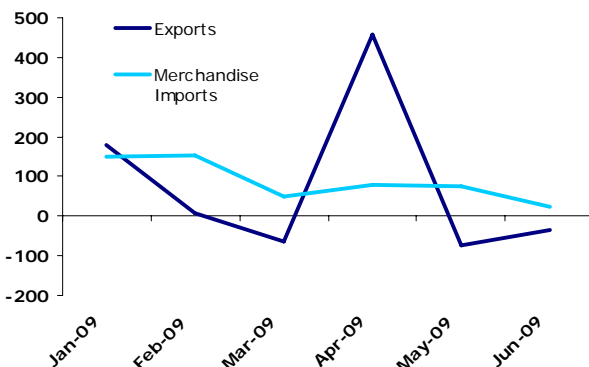
Timor-Leste - Inflation



Timor-Leste - Broad Money Growth



Timor-Leste - Trade (y/y)



**Growth is expected to hold up given expanding government expenditure and strong agricultural sector performance. However, domestic liquidity appears to be tightening as banks are reining in lending due to greater concerns about NPLs. Inflation pressures remain subdued while trade has shown some signs of improvement.**

- Growth should be well supported by increased public spending on infrastructure, and transfer payments.
- Total exports increased 69.3% (y/y) in Q2 this year, standing at \$12mn, as re-exports staged a strong rebound. On the other hand, imports also grew by 55.8% (y/y) in Q2 to reach \$77.2mn. Most of the rise in imports was due to increased purchases of capital goods, machinery and vehicles in line with the budget's expenditure increase.
- June inflation stood at -3.1% (y/y), compared with -1.3% in May. This was largely due to declines in food and transportation costs from their peaks a year ago.
- Domestic liquidity appears to be tightening. Broad money growth continues to slow, growing at a 2½-year low of 18.0% (y/y) in Jun following a 22.5% expansion in May.
- Credit growth remains weak due to concerns about loan quality (from one bank in particular) and limited lending opportunities provided by government-controlled companies. Outstanding loans to the private sector at the end of Q2 remained virtually at the same level as a year earlier, declining by -0.4%. Non-performing loans (NPL) stood at a high level of 28.5% at the end of Q2, although these were concentrated in one lender. However, provisioning has been made to the extent of 1.9 times current NPLs.
- Credit to individuals and the construction sector, the two largest borrowing categories, saw the sharpest decline of 7.2% (q/q) and 18.6% (q/q), respectively. Agriculture and tourism sectors saw the strongest growth in credit at 38.2% (q/q) and 18.6% (q/q), respectively.
- Withdrawals from the state petroleum fund to meet budget programmes are expected to be above sustainable levels this year. Effective utilisation of the withdrawals to fund high-income-generating projects is critical for future growth and the alleviation of unemployment.
- Indonesia has agreed to extend Timor Leste several benefits, including cultural and tourism partnerships. Better relations with Jakarta would be supportive of FDI and allow Timor-Leste to leverage off strong growth in Indonesia.

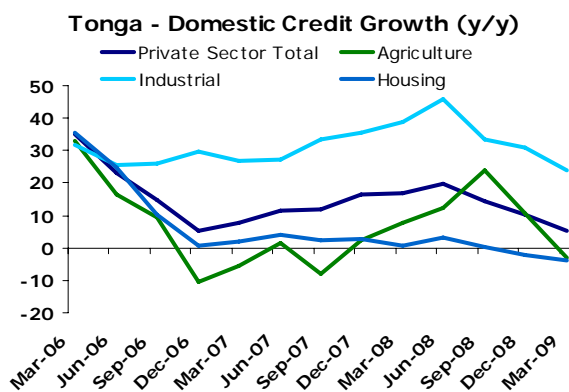
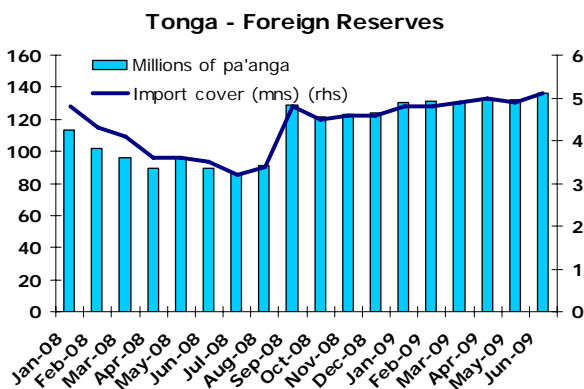
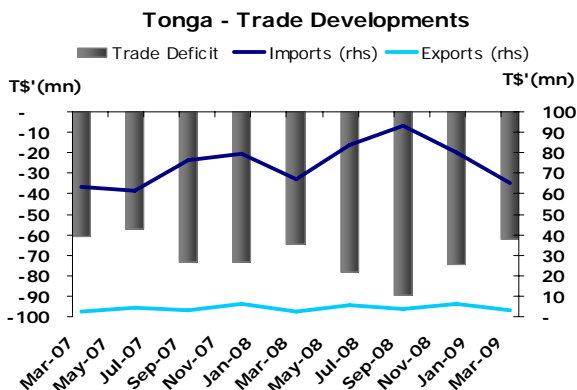
Chang Wei Liang

### Economic Data – Timor-Leste

Quarterly Data	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08	Mar 09
Consumer Price Index, % YOY	9.0	7.2	7.6	3.7	10.7	9.1	6.1	4.2
- Food, % YOY	N/A	10.7	11.0	3.2	13.8	10.9	7.0	5.0
- Transport & Comms, % YOY	N/A	-0.9	3.8	4.3	24.2	22.4	12.5	-5.9
Exports, US\$ mn	0.1	N/A	N/A	10.3	7.1	19.2	11.3	7.0
Imports, US\$ mn	52.3	N/A	N/A	41.6	48.3	66.5	82.0	89.8
Trade Balance, US\$ mn	-52.2	N/A	N/A	-31.2	-41.2	-47.4	-70.7	-82.8

Sources: National Directorate of Statistics, Economist Intelligence Unit

## Country Update: Tonga



**Economic indicators have shown few signs of improvement, with exports, tourism receipts and remittances experiencing further declines. Inflation is benign while liquidity conditions remain tight, thereby constraining business and household spending. Government and central bank measures will support growth but the recovery is likely to be weak.**

- Trade indicators remain weak. Imports rose 14.2% (y/y) in Apr. Exports, on the other hand, continued to fall sharply and declined 40.9% (y/y), compared with a 33.6% fall in Mar. Exports as a proportion of imports remain negligible, and hence, the balance of payments remains heavily dependent on tourism revenues and remittances. The overall BOP registered a small surplus.
- Foreign reserves continue to increase. Reserves reached TOP136.3mn in Jun, from TOP132.1mn in May. The monthly import cover stood at 5.1 at the end of Jun, above the central bank target of 4 months.
- Inflation pressures still remain subdued. The CPI advanced by 1.9% (y/y) in May, marginally higher than 1.4% in Apr. Current inflation rates are near the lowest since Mar 1997.
- Tourism data showed some improvement, but remain soft. Tourist arrivals increased by 6.2% (y/y) in Apr, while tourist receipts increased by 15.0%. However, Apr tourist receipts fell by 14.8% in the month. These data reflect one-off base effects related to the coronation of King George Tupou V in Jul/Aug 2008.
- Remittances continue to decline. Private remittances decreased by 18.0% (y/y) to TOP12.2mn in May, while household remittances declined by TOP3.0mn from Apr.
- Credit growth has slowed further. Private credit growth slowed to 2.4% (y/y) in Apr from 4.5% in Mar. Lending to households declined further by 8.9% (y/y), while lending to businesses grew by 13.5%. The National Reserve Bank of Tonga has reduced the statutory deposit ratio from 10.0% to 5.0% in order to ease liquidity conditions.
- Measures taken by the central bank to ease liquidity are encouraging. A fiscal surplus also gives the government further room for stimulus measures to bolster the domestic economy. Nevertheless, in the absence of a pickup in foreign demand, the economy is likely to contract this year.

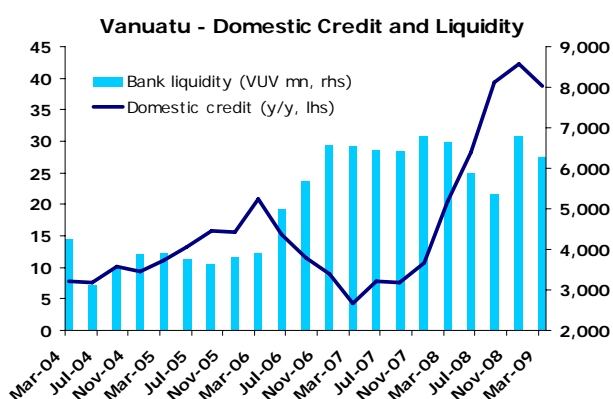
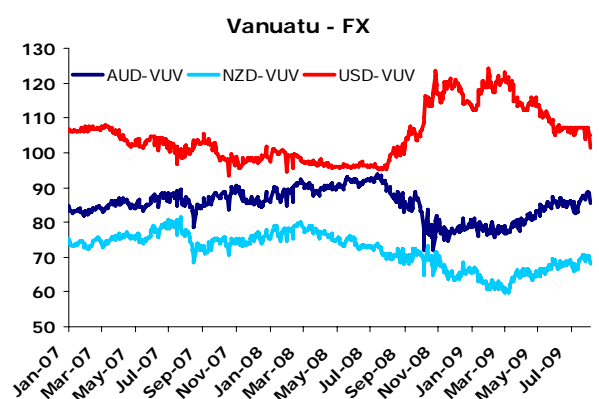
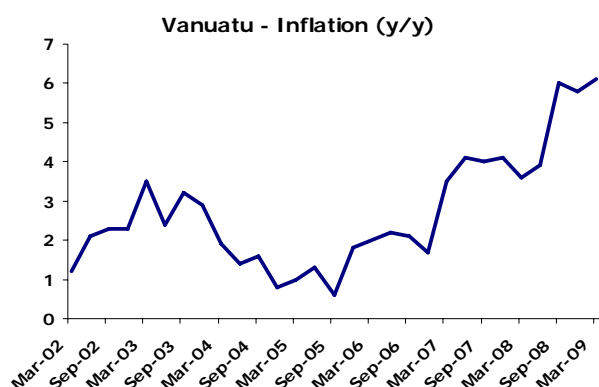
*Raj Gopalakrishnan*

### Economic Data – Tonga

Quarterly Data	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08	Mar 09
Consumer Price Index, % YOY	5.7	8.1	6.8	12.0	12.2	10.1	7.9	2.7
Private Sector Credit, % YOY	9.5	12.4	16.3	15.9	17.1	14.5	10.0	4.5
Exports, % YOY	76.0	-43.4	-63.2	-10.4	23.9	21.3	8.9	34.5
Imports, % YOY	73.1	-40.7	-25.8	6.1	36.0	22.0	0.8	-2.8
Trade Balance, US\$ mn	-37.7	-37.9	-32.9	-27.1	-43.3	-45.5	-34.8	-28.6
Foreign Exchange Reserves, US\$ mn	50.1	54.9	61.9	53.9	49.4	65.0	58.0	60.0

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

## Country Update: Vanuatu



**The pre-emptive easing of monetary policy cushioned the economy from the sharp downturn in external demand. Growth risks are also mitigated by sustained strength in the tourism sector and remittances.**

- The downturn in domestic demand appears to be easing with new vehicle registrations falling at a slower rate of 7.3% (q/q) in Q1 after dropping by 28.0% in the previous quarter. Registrations for motorcars rose 18.1% q/q, while the number of motorcycles registered was unchanged.
- External demand remains weak. Exports fell 67.0% (q/q) in Q1, while imports fell 29.0%. The trade deficit contracted 22.0% over this period to VUV5.4bn. However, the balance of payments deficit widened to VUV648.0mn, substantially higher than recent quarters. Foreign reserves fell 6.0% (q/q) to reach VUV11.6bn in Q1. Import cover declined from 5.8 months in Q4 to 5.2 months but remained well above the official target of 4 months.
- Tourist arrivals held up in Q2. The seasonal lull in inbound tourism saw non-resident arrivals dropping sharply by 32.0% (m/m) in May, but on a y/y basis the island received 19% more visitors during the month.
- Inflation remained above the central bank's year-end target range of 0-4% at 6.1% y/y in Q1 and marginally higher than Q4. Prices rose 1.9% (q/q), supported by higher food and transport costs. The RBV also attributed the rise to the re-weighting of the CPI basket in Q1. A stronger VUV should help ease imported inflation, but the rebound in global commodity prices could pose upside risks to the inflation forecast. The VUV depreciated against the AUD and NZD in Q2, but rose against other major currencies including the USD.
- The RBV left the rediscount rate unchanged at 6% in H1 on improving liquidity conditions in the banking system. Mobilisation of banking resources also improved. Domestic credit expanded by 8.5% from Q4 (33.5% y/y), with growth observed across all sectors. The loan to deposit ratio also grew from 57% to 65% due to an increase in private sector lending and a drop in total deposits held.
- Overall, the pre-emptive easing of monetary policy has cushioned the economy from the sharp downturn in export prices and trade volume. The tourism sector and inward remittances are also holding up, mitigating the downside risks to growth. In contrast, fiscal stimulus was constrained in Q1 due to legislative hurdles, but the passage of the annual budget in Mar should pave the way for a faster pace of disbursements. We continue to expect the economy to grow by 4% in 2009, roughly in line with the government's forecast of 3.8%.

Yeo Han Sia

### Economic Data – Vanuatu

Quarterly Data	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08	Mar 09
Consumer Price Index, % YOY	4.1	4.0	4.1	3.6	3.9	6.0	5.8	6.1
Tourist Arrivals, '000	39.9	37.3	47.2	49.4	37.3	46.3	63.6	65.6
Exports, % YOY	-37.8	6.0	-24.2	66.8	26.0	54.7	20.9	-42.0
Imports, % YOY	22.2	27.5	1.4	45.6	42.7	37.3	34.5	-3.8
Trade Balance, US\$ mn	-35.4	-36.7	-44.2	-48.2	-55.8	-49.1	-52.3	-39.8
Foreign Exchange Reserves, US\$ mn	98.0	103.0	115.0	117.0	118.0	118.0	109.0	99.0

Sources: RBV, ANZ Economics

## Contacts

### ANZ Economics & Markets Research

Warren Hogan	Acting Chief Economist	+61 2 9227 1562	<a href="mailto:Warren.Hogan@anz.com">Warren.Hogan@anz.com</a>
Fiona Allen	Business Manager	+61 3 9273 6224	<a href="mailto:Fiona.Allen@anz.com">Fiona.Allen@anz.com</a>

### Australian Economics and Interest Rates Research

Warren Hogan	Head of Australian Economics and Interest Rates Research	+61 2 9227 1562	<a href="mailto:Warren.Hogan@anz.com">Warren.Hogan@anz.com</a>
Tony Morriss	Senior Rates Strategist	+61 2 9226 6757	<a href="mailto:Tony.Morriss@anz.com">Tony.Morriss@anz.com</a>
Julie Toth	Senior Economist	+61 3 9273 6252	<a href="mailto:Julie.Toth@anz.com">Julie.Toth@anz.com</a>
Riki Polygenis	Economist	+61 3 9273 4060	<a href="mailto:Riki.Polygenis@anz.com">Riki.Polygenis@anz.com</a>
Dr. Alex Joiner	Economist	+61 3 9273 6123	<a href="mailto:Alex.Joiner@anz.com">Alex.Joiner@anz.com</a>
Daniel Bae	Analyst	+61 2 9227 1272	<a href="mailto:Daniel.Bae@anz.com">Daniel.Bae@anz.com</a>

### Global Markets Credit Research

Jason Hill	Global Markets Credit Analyst	0434 312 356	<a href="mailto:Jason.Hill@anz.com">Jason.Hill@anz.com</a>
------------	-------------------------------	--------------	--

### Commodity and Industry Research

Mark Pervan	Head of Commodity and Industry Research	+61 3 9273 3716	<a href="mailto:Mark.Pervan@anz.com">Mark.Pervan@anz.com</a>
Paul Deane	Rural and Regional Economist	+61 3 9273 6295	<a href="mailto:Paul.Deane@anz.com">Paul.Deane@anz.com</a>
Natalie Robertson	Commodity Research Analyst	+61 3 9273 3415	<a href="mailto:Natalie.Robertson@anz.com">Natalie.Robertson@anz.com</a>

### Property and Financial System Research

Paul Braddick	Head of Property and Financial System Research	+61 3 9273 5987	<a href="mailto:Paul.Braddick@anz.com">Paul.Braddick@anz.com</a>
Ange Montalti	Senior Economist	+61 3 9273 6288	<a href="mailto:Ange.Montalti@anz.com">Ange.Montalti@anz.com</a>
Dr. Alex Joiner	Economist	+61 3 9273 6123	<a href="mailto:Alex.Joiner@anz.com">Alex.Joiner@anz.com</a>
Liam Getreu	Research Assistant		

### Foreign Exchange and International Economics Research

Amy Auster	Head of Foreign Exchange and International Economics Research	+61 3 9273 5417	<a href="mailto:Amy.Auster@anz.com">Amy.Auster@anz.com</a>
Katie Dean	Senior Economist	+61 3 9273 1381	<a href="mailto:Katie.Dean@anz.com">Katie.Dean@anz.com</a>
Amber Rabinov	Economist	+61 3 9273 4853	<a href="mailto:Amber.Rabinov@anz.com">Amber.Rabinov@anz.com</a>

### Foreign Exchange and Interest Rates Research (London)

Tim Riddell	Currency and Interest Rate Strategist		<a href="mailto:Tim.Riddell@anz.com">Tim.Riddell@anz.com</a>
-------------	---------------------------------------	--	--

### Asian Economics Research (Singapore)

Paul Gruenwald	Chief Economist, Asia	+65 6216 1814	<a href="mailto:Paul.Gruenwald@anz.com">Paul.Gruenwald@anz.com</a>
Tamara Henderson	Director, FX & Rates Strategy	+65 6419 7930	<a href="mailto:Tamara.Henderson@anz.com">Tamara.Henderson@anz.com</a>
Yeo Han Sia	Associate Director, FX and Rates Strategy	+65 6419 7943	<a href="mailto:HanSia.Yeo@anz.com">HanSia.Yeo@anz.com</a>
Franklin Poon	Economist, North East Asia	+852 3929 5340	<a href="mailto:Franklin.Poon@anz.com">Franklin.Poon@anz.com</a>
Chang Wei Liang	Analyst, Economic Research	+65 6216 1918	<a href="mailto:WeiLiang.Chang@anz.com">WeiLiang.Chang@anz.com</a>

### New Zealand Economics Research (Wellington)

Cameron Bagrie	Chief Economist, New Zealand	+64 4 802 2212	<a href="mailto:Cameron.Bagrie@anz.com">Cameron.Bagrie@anz.com</a>
Khoon Goh	Senior Economist	+64 4 802 2357	<a href="mailto:Khoon.Goh@anz.com">Khoon.Goh@anz.com</a>
Philip Borkin	Economist	+64 4 802 2199	<a href="mailto:Philip.Borkin@anz.com">Philip.Borkin@anz.com</a>
Steve Edwards	Economist	+64 4 802 2217	<a href="mailto:Steve.Edwards@anz.com">Steve.Edwards@anz.com</a>
Kevin Wilson	Rural Economist	+64 4 802 2361	<a href="mailto:wilsonk1@anz.com">wilsonk1@anz.com</a>

### Research and Information Services

Karen Crothers	Head of Research and Information Services	+61 3 9273 6265	<a href="mailto:Karen.Crothers@anz.com">Karen.Crothers@anz.com</a>
Marilla Rough	Senior Information Officer	+61 3 9273 6263	<a href="mailto:Marilla.Rough@anz.com">Marilla.Rough@anz.com</a>
Manesha Jayasuriya	Publications Coordinator	+61 3 9273 4121	<a href="mailto:Manesha.Jayasuriya@anz.com">Manesha.Jayasuriya@anz.com</a>

## Important Notice

Australia and New Zealand Banking Group Limited is represented in:

**AUSTRALIA by:**

Australia and New Zealand Banking Group Limited ABN 11005 357 522  
10th Floor 100 Queen Street, Melbourne 3000, Australia  
Telephone +61 2 9226 6224 Fax +61 2 9227 5711

**UNITED KINGDOM by:**

Australia and New Zealand Banking Group Limited  
ABN 11 005 357 522  
40 Bank Street, Canary Wharf, London, E14 5EJ, United Kingdom  
Telephone+ 44 20 3229 2121 Fax+44 20 7378 2378

**UNITED STATES OF AMERICA by:**

ANZ Securities, Inc. (Member of FINRA [www.finra.org] and SEC)  
6th Floor 1177 Avenue of the Americas  
New York, NY 10036, United States of America  
Tel: +1 212 801 9160 Fax: +1 212 801 9163

**NEW ZEALAND by:**

ANZ National Bank Limited  
Level 7, 1-9 Victoria Street, Wellington, New Zealand  
Tel: +64 4 802 2000

This document ("document") is distributed to you in Australia and the United Kingdom by Australia and New Zealand Banking Group Limited ABN 11 005 357 522 ("ANZ") and in New Zealand by ANZ National Bank Limited ("ANZ NZ"). ANZ holds an Australian Financial Services licence no. 234527 and is authorised in the UK by the Financial Services Authority ("FSA").

This document is being distributed in the United States by ANZ Securities, Inc. ("ANZ S") (an affiliated company of ANZ), which accepts responsibility for its content. Further information on any securities referred to herein may be obtained from ANZ S upon request. Any US person(s) receiving this document and wishing to effect transactions in any securities referred to herein should contact ANZ S, not its affiliates.

This document is being distributed in the United Kingdom by ANZ for the information of its market counterparties and intermediate customers only. It is not intended for and must not be distributed to private customers. In the UK, ANZ is regulated by the FSA. Nothing here excludes or restricts any duty or liability to a customer which ANZ Bank may have under the UK Financial Services and Markets Act 2000 or under the regulatory system as defined in the Rules of the FSA.

This document is issued on the basis that it is only for the information of the particular person to whom it is provided. This document may not be reproduced, distributed or published by any recipient for any purpose. This document does not take into account your personal needs and financial circumstances. Under no circumstances is this document to be used or considered as an offer to sell, or a solicitation of an offer to buy.

In addition, from time to time ANZ, ANZ NZ, ANZ S, their affiliated companies, or their respective associates and employees may have an interest in any financial products (as defined by the Australian Corporations Act 2001), securities or other investments, directly or indirectly the subject of this document (and may receive commissions or other remuneration in relation to the sale of such financial products, securities or other investments), or may perform services for, or solicit business from, any company the subject of this document. If you have been referred to ANZ, ANZ NZ, ANZ S or their affiliated companies by any person, that person may receive a benefit in respect of any transactions effected on your behalf, details of which will be available upon request.

The information herein has been obtained from, and any opinions herein are based upon, sources believed reliable. The views expressed in this document accurately reflect the author's personal views, including those about any and all of the securities and issuers referred to herein. The author however makes no representation as to its accuracy or completeness and the information should not be relied upon as such. All opinions and estimates herein reflect the author's judgement on the date of this document and are subject to change without notice. No part of the author's compensation was, is or will be directly or indirectly related to specific recommendations or views expressed in this document. ANZ, ANZ NZ, ANZ S, their affiliated companies, their respective directors, officers, and employees disclaim any responsibility, and shall not be liable, for any loss, damage, claim, liability, proceedings, cost or expense ("Liability") arising directly or indirectly (and whether in tort (including negligence), contract, equity or otherwise) out of or in connection with the contents of and/or any omissions from this communication except where a Liability is made non-excludable by legislation.

Where the recipient of this publication conducts a business, the provisions of the Consumer Guarantees Act 1993 (NZ) shall not apply.