RESERVE BANK OF FIJI

QUARTERLY REVIEW

September 2004

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QUARTERLY REVIEW OF THE ECONOMY & FINANCIAL CONDITIONS

OVERVIEW

Global economic and financial conditions improved in the September quarter, driven by growth in the United States (US), with strong support from Asia. The International Monetary Fund (IMF) now expects this year's growth to be 5.0 percent, the highest in nearly three decades. The upward revision is mainly underpinned by the well-established growth between mid-2003 and mid-2004, following strong growth in industrial countries and exceptionally rapid expansion in emerging markets, notably China.

However, there are several downside risks. Firstly, continued uncertainties in the oil market, due to concerns of inadequate supply to meet growing global demand, could further weaken the current economic expansion. Secondly, inflationary pressures could gain momentum, consistent with the current robust growth and rising oil prices. This may necessitate tighter monetary policies in various countries. Finally, geo-political risks, while hard to quantify, remain a concern and has the ability to derail global growth prospects.

Amongst our major trading partners, the economic outlook continues to be favourable. In the US and Japan, prospects remain solid. The Australian and New Zealand economies are expected to record robust growth, underpinned by buoyant domestic demand. For the Euro-zone, growth is expected to gain momentum, on the back of growing external demand.

Meanwhile, international financial markets recorded mixed performances. On exchange rates, the US dollar generally weakened against Fiji's other major trading partner currencies except the Yen. The Dow Jones and Nikkei fell, while bond prices generally rose.

The domestic economy is expected to continue to expand this year, although not as strongly as last year. General business sentiments and anecdotal data suggest that the domestic economy has been performing well, to date. The expectation for good growth this year is based on favourable performances of several key sectors of the economy. The tourism industry continues to perform robustly, in line with expectations, while investment has strengthened, led by increased activities in the construction sector. In addition, output in the cane and sugar, garments, gold, and timber industries have all risen on an annual basis.

In the year to September, inflation stood at 3.4 percent, compared with 2.7 percent recorded in June. The underlying measure of inflation, the trimmed mean, was 1.2 percent in September, up from 1.1 percent in the previous quarter. In the coming months, inflation is expected to remain around existing levels.

Conditions in the labour market remained firm during the September quarter, as indicated by partial indicators of employment as well as survey data. Growth in the number of newly registered taxpayers, a partial indicator for employment, was positive.

Activity in the building and construction sector has continued to underpin strong investment levels into the September quarter, with major projects still underway and some just getting off the ground. Furthermore, commercial bank lending to the construction sector rose again in the September quarter.

On the fiscal front, provisional figures indicate that, cumulative to August, Government recorded a net headline deficit of $46.4 million, equivalent to 1.5 percent of GDP. This position was underpinned by a 1 percent rise in net expenditure (excluding loan repayments), which more than offset a 7 percent increase in revenue.

On the external front, recent Overseas Exchange Trade (OET) data showed that cumulative to August, merchandise exports and merchandise imports both rose over the year, by around 14 percent and 17 percent, respectively. Both surpassed the growth rates recorded for the same period last year.

Foreign reserves at the end of September were around $739 million, sufficient to cover 3.2 months of import payments of goods and non-factor services or 4.9 months of imports of goods only.

THE INTERNATIONAL ECONOMY

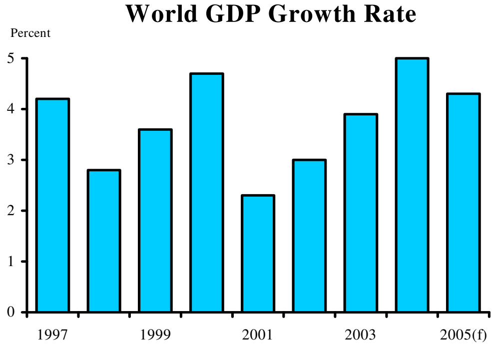
International Economic Conditions

Global economic and financial conditions improved in the third quarter, driven by growth in the United States, and strong support from Asia. Moreover, economic activity in Latin America and some other emerging markets has also picked up strongly.

The IMF now expects this year's growth to be 5.0 percent (Graph 1), the highest in nearly three decades. The upward revision is mainly underpinned by the well-established growth between mid-2003 and mid-2004, following strong growth in industrial countries and exceptionally rapid expansion in emerging markets, notably China. For 2005, world growth is projected to moderate to 4.3 percent, consistent with the ongoing withdrawal of fiscal and monetary stimulus.

Graph 1

World GDP Growth Rate



Source: IMF World Economic Outlook - September 2004

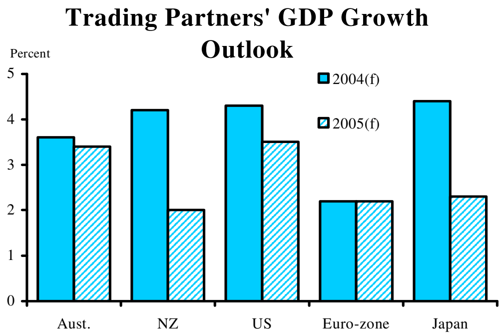
However, there are several downside risks. Firstly, continued uncertainties in the oil market, due to concerns of inadequate supply to meet growing global demand could further weaken the current economic expansion. Secondly, inflationary pressures could gain momentum, consistent with the current robust growth and rising oil prices. This may necessitate tighter monetary policies across countries, and hence impact global economic and financial markets. Finally, geo-political risks, while hard to quantify, remain a concern and has the ability to derail global growth prospects.

Global inflation picked up since mid-2003, in line with rapid world growth and rising oil prices. However, inflationary risks appear moderate, given substantial excess capacity in most countries.

During the June quarter, international financial markets recorded mixed performances. On exchange rates, the US dollar generally weakened against our other major trading partner currencies except the Yen. The Dow Jones and Nikkei fell, while bond prices generally rose.

Growth prospects for Fiji's major trading partners remain positive for this year (Graph 2). Despite the economic slowdown in the second quarter, notably in the US and Japan, prospects remain solid. The Australian and New Zealand economies are expected to record robust growth as well, underpinned by buoyant domestic demand. For the Euro-zone, growth is expected to gain momentum, on the back of growing external demand.

Graph 2



Source: IMF World Economic Outlook - September 2004

The **Australian economy** grew by 0.6 percent in the June quarter, following a 0.2 percent growth in the previous quarter. This was underpinned by higher personal consumption and increased company investments.

Recent indicators have largely been positive. In July, consumer and business confidence increased, led by the government's large fiscal stimulus package. Consistent with an increase in new orders and inventories, service industries' activity also rose in the same month. Moreover, the index of leading economic indicators, a gauge of growth for the next 6 months, rose in July.

The Reserve Bank of Australia left its key interest rate unchanged at 5.25 percent, for the ninth consecutive month in September, as inflationary pressures remained subdued.

The economy is anticipated to record a higher growth of 3.6 percent this year, compared to 3.0 percent last year. Inflation is expected to remain moderate at 2.8 percent this year.

New Zealand's economic growth slowed to 0.9 percent in June, after growing a revised 2.1 percent in the March quarter. The slowdown was a result of the central bank's interest rate hikes, which curbed consumer spending.

However, recent data generally signal a strengthening economy. Business confidence rose in July, while retail sales recorded a third month gain in the same period, buoyed by renewed consumer spending. Manufacturing also accelerated, in line with increased domestic and overseas orders.

The Reserve Bank of New Zealand increased its key interest rate twice during the September quarter, by 25 basis points each in July and September, to 6.25 percent. These moves were prompted by rising inflationary pressures, associated with the housing boom and gains in retail sales, which threatened to push inflation beyond the bank's medium term target of 1-3 percent.

In line with the strengthening economic indicators, the economy is forecast to expand by a robust growth rate of 4.2 percent this year, compared to 3.4 percent in 2003. Consumer prices are expected to be around 2.4 percent this year.

The **US economy** grew by 3.3 percent in the June quarter, underpinned by higher personal expenditure, business investment, government spending and exports.

Recent economic indicators have been mixed. Consumer confidence rebounded in July, amid improving labour market conditions. Industrial production expanded and retail sales rose in August, as consumer spending accelerated. In addition, the federal budget deficit narrowed in August, as tax revenues increased.

However, on a negative note, manufacturing slowed in August, as fewer companies reported an increase in orders and production. Furthermore, an index of leading economic indicators, a gauge of economic performance in the next 3 to 6 months, fell for the third consecutive month in August.

In line with growing inflationary pressures stemming from the robust economic growth, the Federal Reserve raised its key interest rate twice in the September quarter by 25 basis points each, in August and September to 1.75 percent.

Growth in the US economy is projected to reach 4.3 percent this year, higher than the 3.0 percent last year. Inflation is expected to remain moderate at 3.0 percent this year.

The **Euro-zone** economy recorded a weak growth of 0.5 percent in the second quarter, mainly attributed to depressed consumer spending and falling exports.

Economic activity remained subdued in the third quarter. Manufacturing in the Euro-zone slowed in August. Retail sales also fell, as concerns about job losses discouraged spending. Moreover, the unemployment rate held at 9 percent in September for the third consecutive month. In addition, the inflation rate rose to 1.8 percent in July, amid record crude oil prices.

Nevertheless, Germany, France and Italy, which account for half of the Euro-zone economy, yielded encouraging economic indicators in the third quarter. In July, German industrial production rose to a 9-month high, underpinned by increased consumer demand, while inflation slowed to 1.8 percent in September. In addition, French household spending rose in August, while Italian consumer confidence surged in September, indicating a pick-up in domestic demand in the second half of the year.

The outlook for consumer prices in the medium term remained favourable. As such, the European Central Bank maintained its benchmark interest rate at 2 percent during the September quarter.

Growth in the Euro-zone economy is expected to gather momentum and thus expand at a faster pace of 2.2 percent this year, compared with 0.5 percent in 2003. Year-end inflation is forecast at 2.1 percent, based on a moderate outlook for domestic and import prices.

The **Japanese** economy grew at a slower rate of 0.3 percent in the June quarter, after a recovery in consumer spending weakened and companies curbed investment.

However, recent indicators signal generally positive outcomes. In July, consumer confidence rose to a 13-year high, while industrial production remained unchanged from the previous month. Moreover, retail sales also rose in the same month, led by increased spending on summer clothing and as consumers bought more televisions.

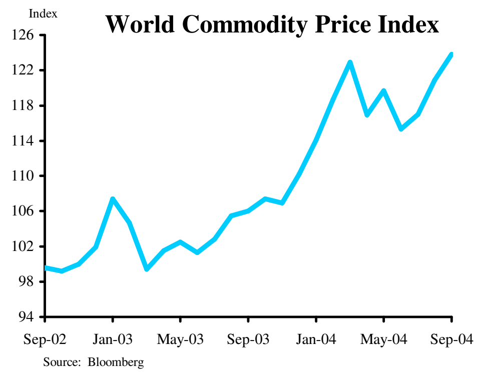
In addition, the trade and current account surplus also widened in July, led by a decline in imports and a rise in returns from overseas investments, respectively. Furthermore, an index of leading economic indicators rose for the eleventh consecutive month in July, signalling growth for the next 6 months.

This year, the Japanese economy is

expected to record a strong growth of 4.4 percent, compared to 2.5 percent last year. Inflation is forecast at –0.2 percent this year, equivalent to last year.

World commodity prices rose by around 7 percent during the quarter, reaching a historical high in September, largely underpinned by higher crude oil, sugar and gold prices (Graph 3).

Graph 3

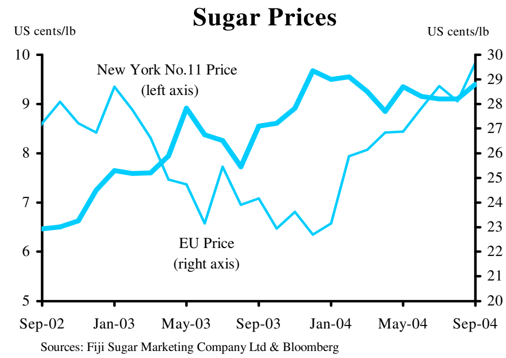


World market sugar prices rose by around 10 percent over the September quarter (Graph 4), reaching a 3-year high of around US9.8 cents, on speculation of lower supply from India[1].

However, in the months ahead, sugar prices are anticipated to decline, in line with higher estimated supplies from Brazil and Australia.

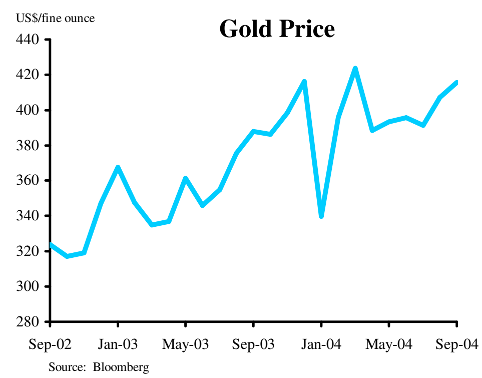
At the end of September, the European Union (EU) sugar price was around US29 cents per pound. Over the quarter, the EU sugar price rose by around 2 percent, reflecting a stronger Euro against the US dollar.

Graph 4



Gold prices rose by around 5 percent over the quarter, reaching a 9-month high of US$416 in late September (Graph 5). Gold prices fell during the first month of the quarter, as a stronger US dollar against the Euro lowered demand from European buyers. However, prices rose in the remainder of the quarter, after terrorism concerns raised demand for the metal as a safe haven investment. Moreover, a stronger Euro against the US dollar during the same period also raised demand from European investors.

Graph 5



In the approaching months, gold prices are expected to remain high (above US$400 per fine ounce), on terrorism concerns.

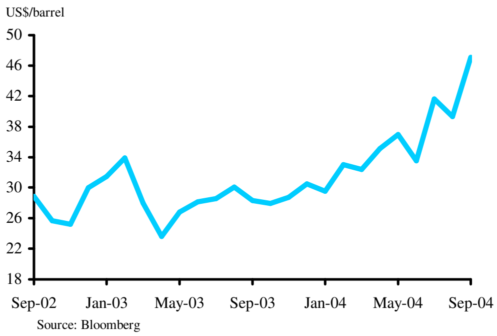
At the end of September, the **Brent crude oil price** was around US$47 per barrel, 40

[1] For the year ending October, India cut its forecast production by 25 percent, due to unfavourable weather conditions.

percent higher than at the end of June (Graph 6).

Graph 6

Crude Oil Price



In July, crude oil prices rose, due to a combination of factors: concerns of supply disruptions in light of geo-political tensions, the increasing global demand for oil and declining inventories. However, prices fell slightly in August, after concerns of possible supply disruptions from Iraq eased.[2] Nevertheless, prices surged to a historical high of US$48 in late September, on concerns of possible disruptions to supply, particularly from Nigeria.[3] Prices also rose as US supplies neared a 29-year low, on account of strong domestic demand, exacerbated by production losses and damages incurred from Hurricane Ivan.[4]

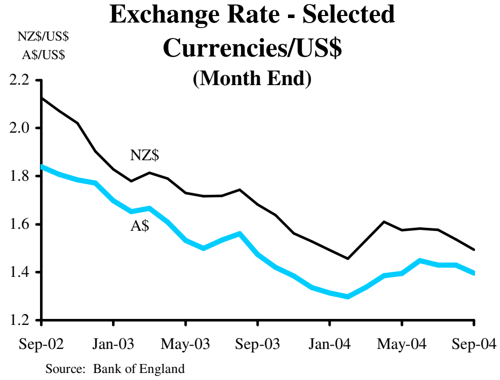
In the coming months, crude oil prices are expected to remain high, (above US$40 per barrel), on concern that production will not be adequate to meet increasing demand, in line with strong economic growth in the US and China.

International Financial Markets

Over the third quarter, the US dollar generally weakened against our major trading partner currencies except the Yen.

Over the third quarter, the Australian and New Zealand dollars generally strengthened against the US dollar (Graph 7).

Graph 7



The Aussie dollar rose against the Greenback in July, on speculation that the interest rate gap with the US will not narrow as rapidly as expected. However, it weakened in August, on concerns that high oil prices will slow global growth and reduce demand for Australia's exports. The Aussie dollar strengthened again in September, on expectation that a relatively higher yield premium on Australian bonds will lure investors to

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2 The August cease-fire in Najaf eased concerns that shipments from Iraq will be disrupted.

3 Crude oil prices rose as Nigerian rebels threatened oil output from the Niger River delta, causing the closure of a pumping station. Nigeria is the 5th largest OPEC member and Nigerian oil contains low sulphur, which is preferred by many refiners because it has a greater yield of high-value products such as gasoline.

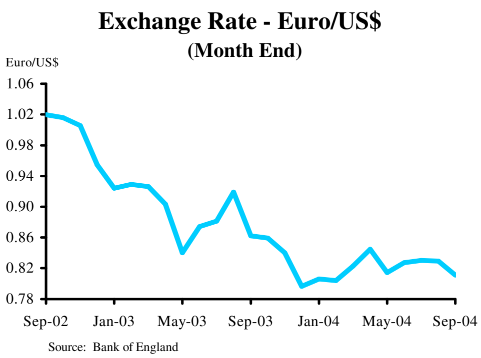
4 Hurricane Ivan prompted US oil producers to reduce output by 1.4 million barrels a day, or 83 percent of total US output from the Gulf of Mexico. Further output will be lost while oil companies try to restore the platforms and as refiners prepare to resume processing.

Australian assets.

The Kiwi-dollar also strengthened against the US dollar throughout the quarter, as a relatively higher yield premium on Kiwi assets lured investors away from US dollar-denominated assets.

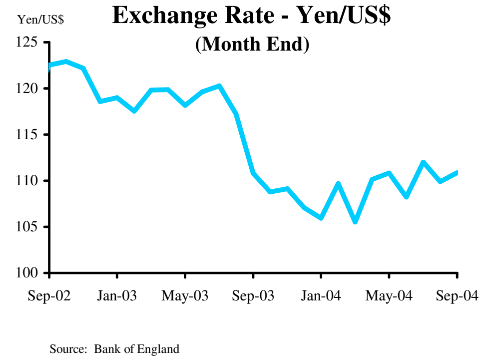
The Euro generally strengthened against the Greenback during the quarter (Graph 8). The Euro weakened in July, as expectations of higher returns on US bonds after the Federal Reserve raised its key interest rate in June, prompted investors to switch from Euro to US dollar denominated assets. However, the Euro strengthened throughout the remaining period of the quarter, as concerns of a slowing US economy, prompted investors to switch to Euro denominated assets.

Graph 8



During the quarter, the Yen generally weakened against the US dollar (Graph 9). The Yen weakened in July after a decline in Japanese equities lowered demand for the Yen. However, the Yen strengthened in August, as concerns over the pace of the US economic expansion, led investors to switch to Yen-denominated assets. Nevertheless, the Yen fell again in September, following the lower-than-expected June quarter growth, which dampened demand for Yen-denominated assets.

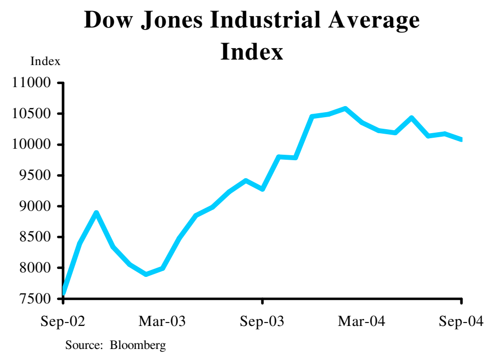
Graph 9



Equity prices generally fell during the three months to September.

Over the September quarter, the Dow Jones Industrial Average Index fell by around 3 percent (Graph 10). The Dow fell in the first month of the quarter, after higher crude oil prices raised concerns about the outlook for corporate profit growth. However, the Dow rose in August, as receding crude oil prices, boosted the US economic outlook. In September, the Dow Jones fell again, after a surge in crude oil prices renewed concerns about the outlook for corporate profit growth.

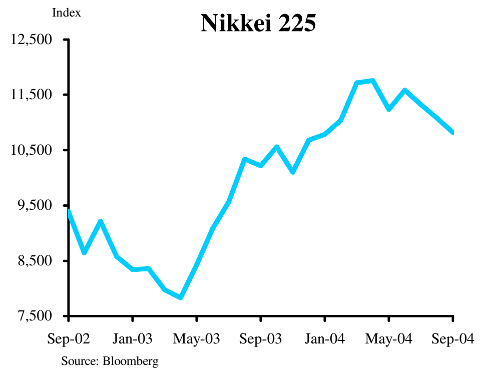
Graph 10



Over the three months to September, the Nikkei 225 Stock Average Index declined by around 7 percent (Graph 11). The Nikkei fell throughout the September quarter, as higher crude oil prices, raised concerns that rising energy costs may slow corporate earnings, thus reducing demand for Japanese stocks.

Graph 11

Nikkei 225

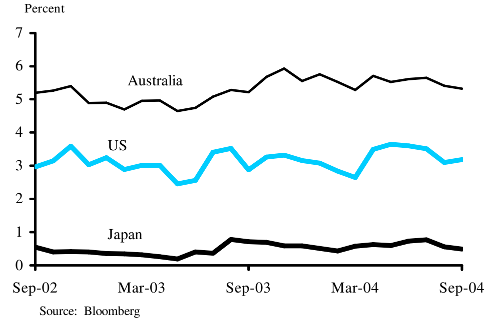


During the September quarter, 10-year bond yields for the US, Japan and Australia generally fell (Graph 12).

US bond yields fell in the first 2 months of the quarter, after concerns of slowing US economic growth, increased demand for the safety of government debt. However, yields rose in September, after positive sentiments about the US outlook, reduced demand for government debt.

Graph 12

Ten-Year Bond Yields



Japanese bonds fell at the beginning of the quarter, as lower yields dampened demand for the long-term debt instrument. However, demand for the debt asset rose throughout the remaining months of the quarter, on speculation that the slowing economic recovery will affect Japanese exports, thus boosting demand for the safety of government debt.

Australian bond yields rose at the beginning of the month, after positive economic indicators boosted the outlook for the economy, thus reducing demand for the debt instrument. Nevertheless, yields for the government debt fell throughout the remainder of the quarter, as a pessimistic outlook on corporate profits, prompted investors to demand bonds as opposed to stocks.

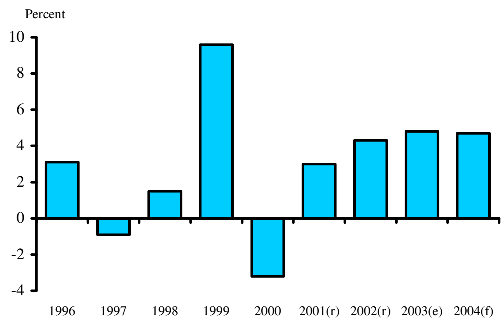
THE DOMESTIC ECONOMY

Domestic Economic Conditions

General business sentiments and anecdotal data suggest that the domestic economy has been performing well to date (Graph 13). The expectation for good growth this year is based on positive performances of several key sectors of the economy.

Graph 13

GDP Growth Rate



Sources: Fiji Islands Bureau of Statistics & Reserve Bank of Fiji

Consumer Spending

Consumption remained upbeat during the third quarter of the year, evident by the growth in partial indicators of **consumer spending**.

For the year to August, total Value Added Tax (VAT) collections from retail activities increased by around 17 percent over the previous comparable period. Discounting for Government's VAT payments, total VAT grew by almost 14 percent, suggesting that private demand remains robust. The favourable outturn in consumption was further supported by increased currency in circulation and higher lending for consumption purposes during the review period.

Additionally, imports of consumption items also rose during the review period, and favourable labour market conditions continued to underpin the prevailing buoyant performance in consumer spending.

Production

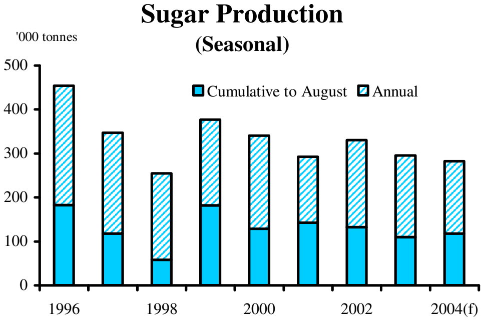
The general performance of most major sectors has been positive so far this year.

In line with expectations, the tourism industry continues to perform robustly, while investment has strengthened, led by increased activities in the construction sector. In addition, output in the cane and sugar, garments, gold, and timber industries have all risen on an annual basis in the review period. On the downside though, output in the fisheries and copra industries have been weak.

The **cane** and **sugar** industries have continued their strong performance into the third quarter of the year (Graph 14).

Graph 14

Sugar Production
(Seasonal)



Sources: Fiji Sugar Corporation Ltd, Fiji Islands Bureau of Statistics & Reserve Bank of Fiji

For the season to August, total cane produced amounted to around 1.1 million tonnes, representing a 6 percent increase over the same period last year. Consequently, total sugar produced during the same period was around 118,000 tonnes, 7 percent higher than the output during the corresponding period.

The performance of the **garment** industry was stable during the review period. Total garment exports in the first seven months of the year amounted to $165.3 million, representing a marginal increase on an annual basis.

On other developments in the industry, the South Pacific Regional Trade and Economic Cooperation Agreement (Textiles, Clothing and Footwear Provisions) Scheme was extended in principle for another seven years by the Australian Government in August. However, the US Quota Trade Agreement under which one of the largest garment factories exports to the US market, will expire on 1 January, 2005. An extension to this trade agreement, at this point in time, remains uncertain.

The **tourism** industry has continued its outstanding performance well into the third quarter of the year (Graph 15).

According to the Fiji Islands Bureau of Statistics (FIBOS), total visitor arrivals for the January to July period totalled around 277,000, representing a 20 percent increase over the review period on an annual basis.

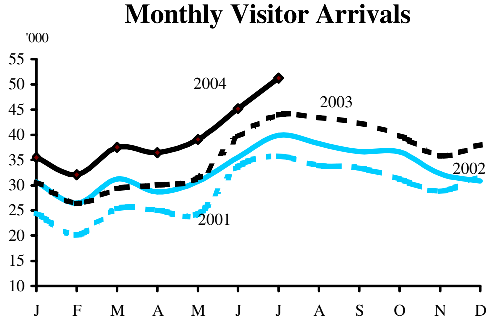
The robust growth in visitor arrivals was led by increased arrivals out of Australia, New Zealand, the US, Canada and Japan. Nonetheless, arrivals from Continental Europe continued to be a drag on growth during the review period. Australia, representing 32 percent of all arrivals, remained our largest source market followed by New Zealand (20%), the US (14%) and the UK (11%). Other countries including Japan, Continental Europe and Canada, accounted for the remaining 23 percent of the market.

As the industry nears the end of the peak season, growth in monthly arrivals is expected to slow down. However, anecdotal evidence suggests that the year-end arrivals level will likely surpass the current projection of 445,000 visitors for the year.

After several months of recording declines in output, the performance of the **mining and quarrying** sector improved in the September quarter (Graph 16).

Graph 15

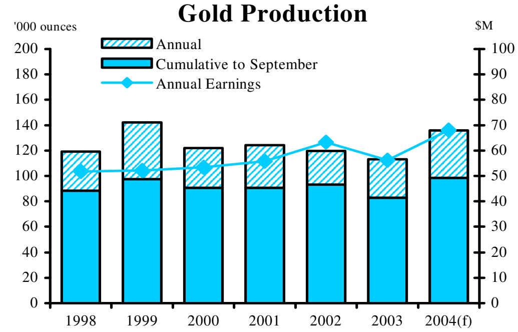
Monthly Visitor Arrivals



Source: Fiji Islands Bureau of Statistics

Graph 16

Gold Production



Source: Emperor Gold Mining Company Limited

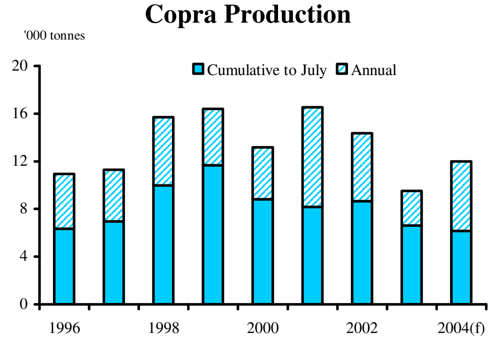
Cumulative to September, total gold production amounted to 98,000 ounces, 19 percent higher than last year's level. The strong growth in gold production provides support for Emperor Gold Mining Company Limited's (EGM) intention of gradually increasing its production level towards an annual production target of 180,000 ounces by 2006.

On other industry developments, Durban Roodepoort Deep's (DRD) takeover offer for more shares of Emperor Mines Limited (EML) - the parent company of EGM - was finalised at the end of July. DRD is now the majority shareholder of EML, holding 45 percent of EML's shares.

The performance of the **copra** industry remained weak into the third quarter. Latest statistics from the Coconut Industry Development Authority (CIDA) show that cumulative to July, copra production amounted to around 6,200 tonnes (Graph 17), representing a decline of around 7 percent over the comparable period last year.

Graph 17

Copra Production



Source: Coconut Industry Development Authority

The minimum mill gate price of copra remained at $500 per tonne in July. Government's subsidy towards the mill gate price was $38.56 per tonne.

Output in the **fisheries** industry remained subdued during the January to July period. Total fish export earnings amounted to around $42 million, a decline of around 12 percent over the first 7 months of last year.

Cumulative to July, receipts from **timber** exports totalled $23.6 million, a marginal increase over the corresponding period last year. The outlook for the industry this year is that good growth would be recorded over 2003 levels.

Consistent with the rise in economic activity, electricity production continued to strengthen over the quarter. Cumulative to August, total **electricity** production increased by around 2 percent over the corresponding period of 2003.

Moreover, in July the Fiji Electricity Authority (FEA) completed its $10 million Wainikasau hydroelectricity power station, situated further up the Monasavu dam. This mini-station is expected to generate around 18 million kwh of electricity per annum and will allow FEA to provide electricity to more rural areas and supplement supply to the whole of Fiji.

Investment

The **building & construction** sector has continued its robust performance this year. Latest statistics from Fiji Islands Bureau of Statistics revealed that the total value of work put-in-place in the second half of the year totalled $66.8 million, an increase of around 18 percent over the comparable period last year. By categories, cumulative to June this year, the value of work put-in-place by the private sector rose significantly by around 34 percent, while the public sector recorded a decline of 4 percent.

Major private sector projects that began in the September quarter included construction work on the Labasa Court Complex, preliminary works on Momi Bay Resort and Natadola Beach Resorts. This is in addition to on-going work at the Suva Central Project, Sofitel Island Resort and Spa, residential developments at Denarau and expansion work at the First Landing Resort.

On the public front, development work at the Maritime & Ports Authority of Fiji is in progress along with construction of the Rewa Bridge, the Colonial Centre, extension to the Lautoka Teachers College, and the Fiji School of Medicine campus. On a similar note, the Fiji Public Service Association Shopping Centre was completed during the quarter.

In line with the robust performance of the building and construction sector, partial indicators also suggest a steady growth in **investment** over the quarter. Lending to the construction sector during the third quarter has generally trended upwards.

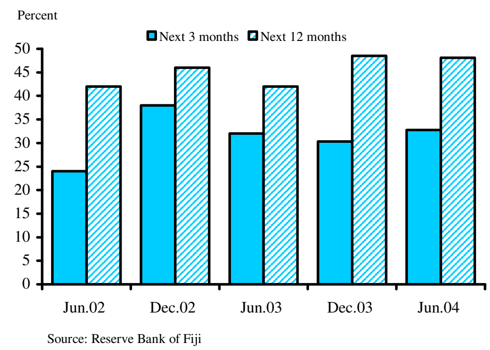
Furthermore, amendments to the Foreign Investments Act and the Broader Approvals Process are progressing well. In light of these amendments, Fiji Islands Trade and Investment Bureau has set up a Registry Unit, which is responsible for carrying out credential checks on foreign investors and registering their application within five working days, in order to foster a fast, transparent and efficient investment approvals process. Additionally, other ministries and agencies related to the investment approvals process have also commenced reforms at organisational levels.

Looking ahead, investment prospects reported in the June Business Expectations Survey have recorded optimistic sentiments for the medium term. A net 48 percent of respondents are anticipating increased investment in plant and machinery over the next 12 months (Graph 18). The building & construction sector and the communications and tourism industries dominated this outlook.

Graph 18

Investment

(Plant & Machinery)

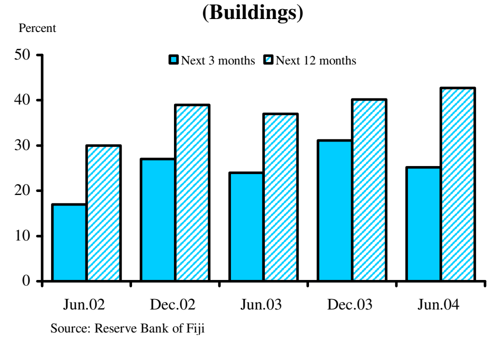


Similar positive sentiments were expressed for investment in new buildings, with a net 43 percent of respondents anticipating investment to rise in this category, over the medium term (Graph 19).

Graph 19

Investment

(Buildings)



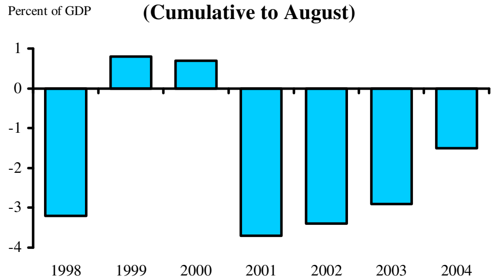
The building & construction sector and the tourism, insurance, real estate industries underpinned this outlook.

Public Finance

On the fiscal front, provisional figures from the Ministry of Finance[1] indicate that, cumulative to August, Government recorded a net headline deficit of $46.4 million, equivalent to 1.5 percent of GDP (Graph 20).

Graph 20

Government Fiscal Headline Balance
(Cumulative to August)



Source: Ministry of Finance

This position was underpinned by a 1 percent rise in net expenditure (excluding loan repayments), which more than offset a 7 percent rise in revenue[2]. A comparison of Government's performance so far against its budget reveals that net expenditure was lower by 15 percent, while net revenue surpassed projections by 7 percent.

A closer examination of Government expenditure in the review period reveals that on an annual basis, net operating expenses (excluding loan repayments), increased by 10 percent, while capital expenditure declined by 17 percent.

Government's revenue collection remained buoyant into August, with the 7 percent increase in total revenue underpinned by annual increases in both customs and excise (8 percent) and inland revenue (8 percent) collections. Notably, both customs and excise and inland revenue collections surpassed the targeted levels by 2 percent and 15 percent, respectively.

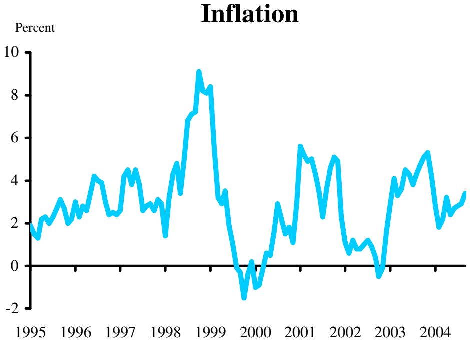
As for Government borrowing for the first eight months of this year, net domestic borrowing by Government was $49 million, against $100 million in the comparable period last year. As at the end of August 2004, total outstanding domestic debt was around $2 billion, 12 percent more than that recorded a year ago.

Inflation

In the year to September, inflation stood at 3.4 percent, compared with 2.7 percent recorded in June (Graph 21).

Graph 21

Inflation



Source: Fiji Islands Bureau of Statistics

Over the quarter, consumer prices rose by around 0.1 percent. The prices of heating & lighting, transport, alcoholic drinks &

[1] Sourced from the State of Government Finances.
[2] There were no asset sales recorded in the review period.

tobacco, durable household goods, and clothing & footwear rose. These were partly offset by falls in the prices of miscellaneous items, food and housing. The prices of services remained unchanged over the quarter.

The underlying measure of inflation, the trimmed mean, was 1.2 percent in September, up from 1.1 percent in the previous quarter.

Over the next quarter, inflation is anticipated to remain around current levels. On the external front, some upward price pressures are expected, due to higher oil prices and stronger world demand. On a positive note, these adverse effects are likely to be mitigated by some spare capacity in certain sectors of the domestic economy. The year-end inflation forecast is around 3.5 percent.

Labour Market

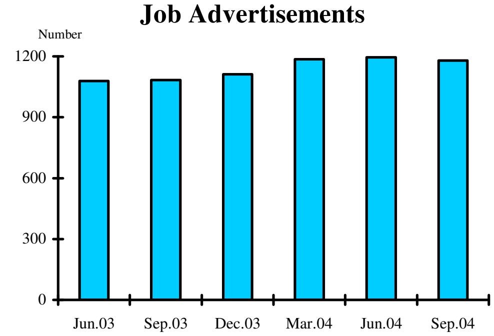
Conditions in the labour market remained firm during the September quarter, as indicated by partial indicators of employment as well as survey data.

Growth in the number of newly registered taxpayers, a partial indicator for employment, remained firm. Cumulative to September, around 9,000 new taxpayers were registered with the Fiji Islands Revenue and Customs Authority. This represented an increase of around 6.0 percent over the corresponding period in 2003. Sectors that recorded the most new taxpayers included the finance, insurance, real estate & business services, community, social and personal services; and wholesale, retail trade, restaurants & hotels sectors.

Furthermore, the Reserve Bank's June Survey of Job Advertisements reported a rise in firms' recruitment intentions (Graph 22). Over the year, the number of advertised positions rose by around 9 percent. Demand for workers was high in the services related industries and companies operating under the wholesale & retail trade & restaurants & hotels sector.

Graph 22

Job Advertisements

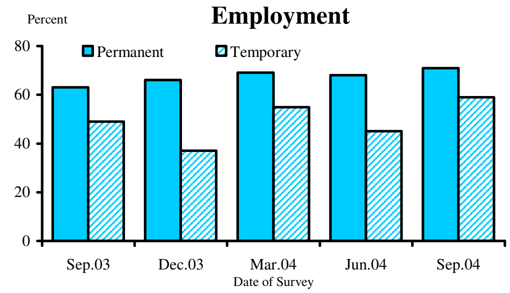


Source: The Fiji Times

Looking ahead, the results of the Reserve Bank's Fiji Employers Federation (FEF) Expectations Survey, conducted in September, showed broad-based optimism for employment over the next twelve months (Graph 23).

Graph 23

Net Proportion of Respondents Expecting an Increase in Employment



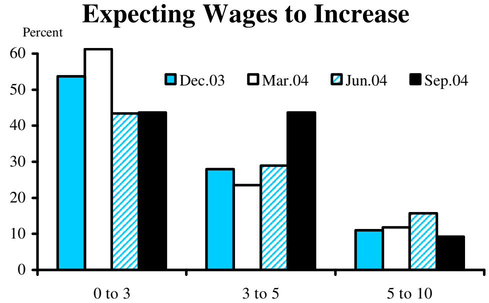
Source: Reserve Bank of Fiji

According to the survey results, overall employment is expected to increase over the next 12 months. A net of around 71 percent of respondents expect permanent employment to increase, while a net of around 59 percent of respondents expect a rise in temporary employment.

Expectations for wage growth are in line with expectations of employment growth (Graph 24). The FEF Expectations Survey revealed that around 44 percent of the respondents expect wage increases in the 0 to 3 percent range, with another 44 percent expecting increases of between 3 to 5 percent.

Graph 24

Proportion of Respondents Expecting Wages to Increase



Source: Reserve Bank of Fiji

Emigration levels declined over the year. Cumulative to July, around 3,300 people emigrated, representing a decline of 6 percent.

During the review period, fewer workers under the professional & technical and clerical, sales & services categories migrated relative to last year. However, this was partially offset by an increase in the number of agriculture & production and administrative workers leaving Fiji.

The External Sector

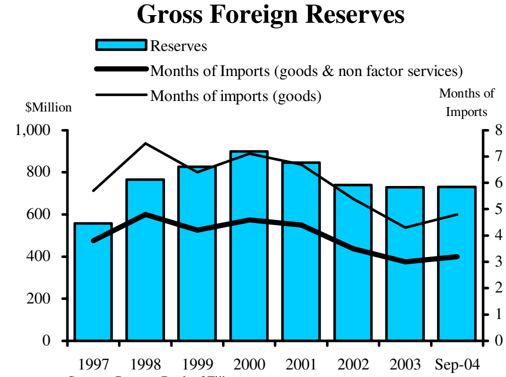
On the external front, recent Overseas Exchange Trade data showed that cumulative to August, merchandise exports rose by around 14 percent, when compared with an 8 percent decline in the corresponding period last year. The increase in exports was largely attributed to positive contributions from textiles, clothing & footwear, merchanted goods, gold, sugar and timber, which more than offset the negative contributions from other re-exports, other exports and copra.

Cumulative to August, merchandise imports rose by around 17 percent, when compared with a 12 percent gain in the corresponding period last year. The increase was credited to higher import payments for all categories of goods. The increase in intermediate goods was led by higher payments for mineral fuels, raw materials and textiles, clothing & footwear, while machinery & transport equipment and chemicals led the increase in investment goods. The positive contribution from merchanted and duty free goods underpinned the increase in payments for consumption goods.

Foreign reserves at the end of September were around $739 million, sufficient to cover 3.2 months of import payments of goods and non-factor services or 4.9 months of imports of goods only (Graph 25).

Graph 25

Gross Foreign Reserves



Source: Reserve Bank of Fiji

June 2004 Business Expectations Survey

Introduction

The Reserve Bank of Fiji conducted its latest Business Expectations Survey in June 2004. Bi-annually each year, over 250 business owners and senior executives representing major industries across Fiji are asked if they expect an increase, decrease or no change in their upcoming quarterly and annual sales, employment, capital investment, inventories, inflation, borrowing requirements and input costs.

The June 2004 Business Expectations Survey was conducted to gauge the outlook for the economy in the three months to September 2004 and over the medium-term period of twelve months to June 2005. A total of 258 companies were surveyed. The response rate for the survey was 51 percent.

Survey Results

The survey results indicate a relatively optimistic outlook for the short term (3 months). For the medium term (12 months), however, prospects are encouraging, but at the same time, mildly subdued when compared to the December 2003 BES.

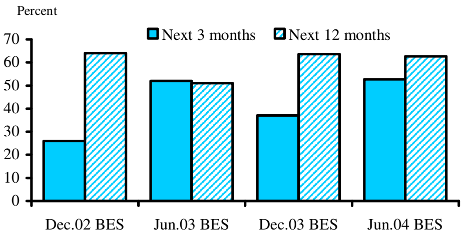
Overall Expectations

General Business Conditions

For the quarter ahead, a net 53 percent of respondents expect business conditions to pick up (Graph 26). Notably, there is greater optimism, with the building & construction sector and tourism, insurance, real estate, finance, communications industries underpinning this sentiment.

Graph 26

Outlook for General Business Conditions



Source: Reserve Bank of Fiji

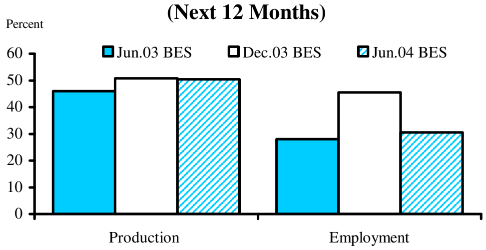
As for the 12-month outlook, 63 percent of respondents are optimistic about the medium term outcome. Although this sentiment was slightly lower (decreasing by 1 percentage point) than in the December 2003 survey, expectations have been broad-based across the economy, with relatively stronger expectation from the building & construction sector and communications, insurance, real estate, tourism, wholesale & retail trade and finance industries.

Production and Employment Plans

Over the next twelve months, sentiments for production is slightly down compared to the last survey. A net 50 percent of respondents anticipate production to rise (Graph 27). The communications, real estate, insurance and the building & construction and non-garment manufacturing sectors dominated this outlook.

Graph 27

Outlook for Production and Employment
(Next 12 Months)



Source: Reserve Bank of Fiji

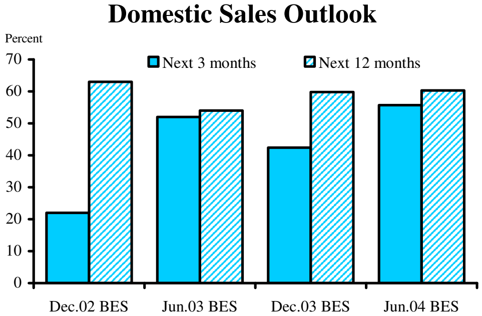
As for employment, a net 31 percent of respondents anticipate employment to increase during the medium term. This represented a decline from a net 46 percent recorded in the last survey. Nevertheless, for the 12-months ahead, survey data suggests that firms' employment intentions are significantly stronger in the building & construction sector and insurance and tourism industries.

Sales Prospects

For the short-term, a net 56 percent of respondents expect an increase in domestic sales (Graph 28), mainly driven by positive sentiments from the communications, real estate, insurance and tourism industries.

Graph 28

Domestic Sales Outlook



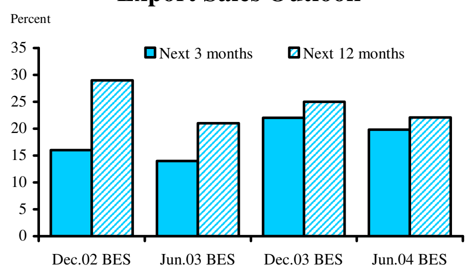
Source: Reserve Bank of Fiji

Over the medium term, prospects for domestic sale remained unchanged, with a net 60 percent of respondents expecting domestic sales to rise. The non-garment manufacturing sector and the wholesale & retail trade, insurance communications, real estate, and tourism industries dominated this optimistic medium-term outlook.

Sentiments for export sales, was slightly down with a net 20 percent of respondents expecting exports to rise in the third quarter of 2004 (Graph 29). The lower sentiments were experienced across all sectors of the economy. Similarly, for the medium-term expectations were down, a net 22 percent of respondents anticipating exports to increase during the review period. These results further strengthen the subdued outlook for exports growth, and is a reason enough for authorities to aggressively pursue strategies to develop the export sector in the country.

Graph 29

Export Sales Outlook



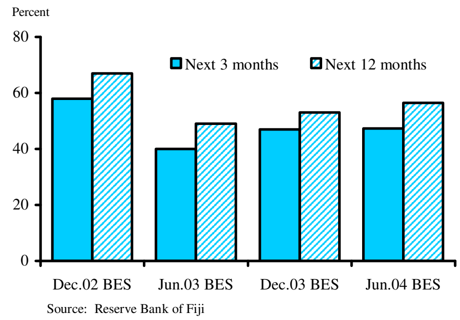
Source: Reserve Bank of Fiji

Inflation

Compared with the previous survey, a larger proportion of the respondents anticipate a higher inflation rate over the next 12 months. As shown in Graph 30, a net 57 percent of the respondents, compared with 53 percent in the December 2003 survey, think that the rate of inflation will increase in the medium term.

Graph 30

Inflation



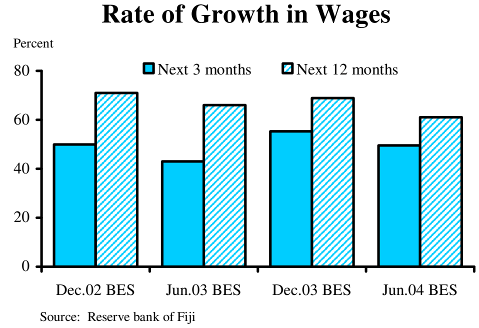
The industries influencing this outlook were communications, insurance and wholesale & retail trade. This is consistent with the higher oil prices, which is adequately reflected in the upgrade of the Reserve Bank of Fiji's inflation forecast from 3 percent to 3.5 percent for 2004.

Input Costs

With regards to input costs, a net 61 percent of the respondents, down from a net 69 percent recorded in the December 2003 survey, expect the rate of growth in wages (Graph 31), to accelerate in the medium term. The insurance, tourism, garment, wholesale & retail trade and the non-garment manufacturing and building & construction sectors dominated the sentiment for wages.

Graph 31

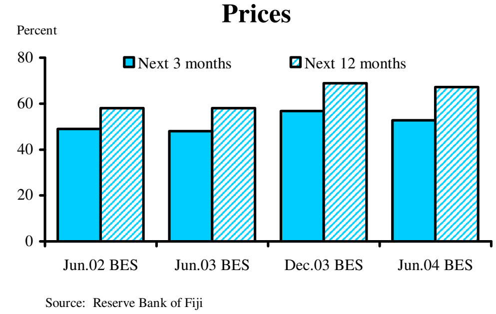
Rate of Growth in Wages



Additionally, compared with the previous survey, a slightly lower percentage of respondents expect prices of raw materials (Graph 32) and import prices (Graph 33) to increase during 2004. The tourism, wholesale & retail trade and the non-garment manufacturing sector dominated the medium-term outlook for the increase in prices of raw materials and imports.

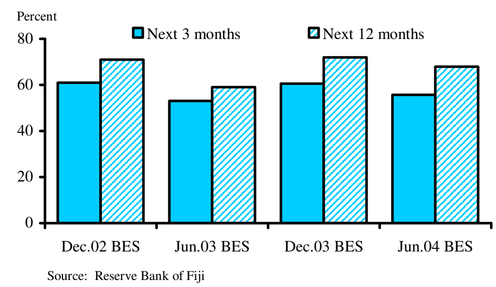
Graph 32

Rate of Growth in Raw Material Prices



Graph 33

Rate of Growth in Import Prices



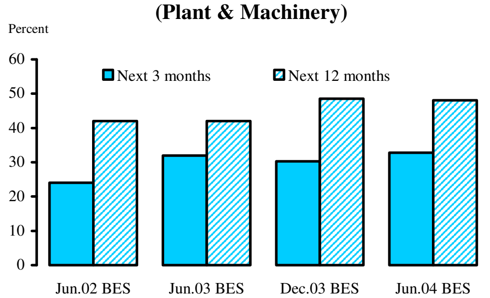
Although the number of respondents expecting a growth in input costs have fallen relative to the previous survey, this still remains quite high at above 60 percent.

Investment (Plant & Machinery and Buildings)

The outlook for investment in the June Survey remained optimistic. Over the next 12 months, a net 48 percent of respondents expect increased investment in plant & machinery (Graph 34). Although, this outlook decline by 1 percentage point from the December 2003 Survey, it was encouraging to note that the building & construction sector and the communication and transport industries were dominating this outlook.

Graph 34

Investment
(Plant & Machinery)

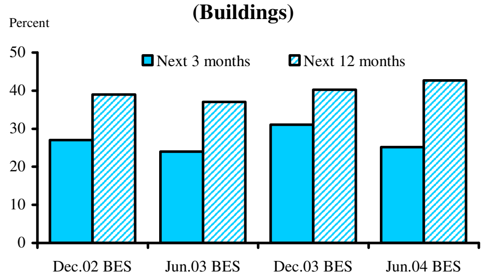


Source: Reserve Bank of Fiji

Additionally, a net 43 percent anticipate higher investment in buildings (Graph 35). This is an all-time high, surpassing the previous highest, recorded in 1999 (also the year for the country's highest GDP growth) for this category. The building & construction sector and the tourism, insurance, real estate industries dominated this encouraging medium-term outlook.

Graph 35

Investment
(Buildings)



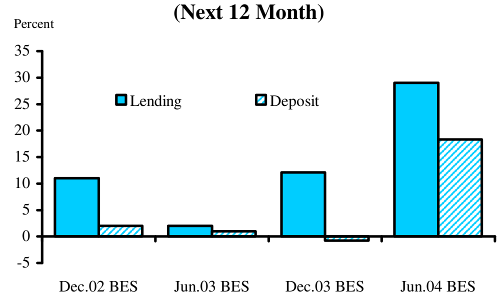
Source: Reserve Bank of Fiji

Interest Rates

For the medium-term, a net 29 percent of respondents anticipate that commercial bank lending rates would increase (perhaps, in view of the interest hike of May). As for commercial bank deposit rates, a net 18 percent of respondents expect a decline in deposit rates (Graph 36).

Graph 36

Commercial Bank Interest Rates
(Next 12 Month)



Source: Reserve Bank of Fiji

Summary

The survey results indicate that the quarter-ahead outlook for general business conditions is up beat. In fact, the optimistic three-month outlook is broad-based with relatively stronger expectations from the communications, tourism, insurance, real estate and the building & construction and non-garment manufacturing sectors.

For the medium term outlook business sentiments were slightly down, but remained encouraging, with a bullish outlook for the tourism, communications, insurance and real estate industries.

Notably, sentiments for domestic sales, inflation, investment and interest rates were up, while expectations for export sales, production employment and input costs were mildly down.

The survey results are consistent with latest production data and monetary aggregates.

Domestic Financial Conditions

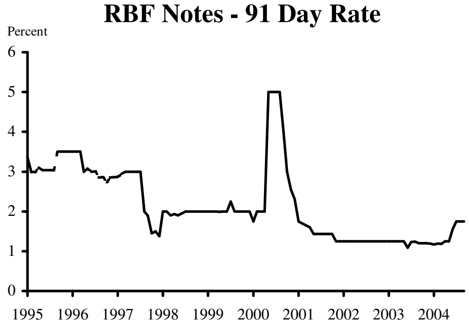
Money Markets

There was a slowdown in inter-bank activity during the September quarter, as turnover in the market fell to $54.5 million from $74.7 million in the previous quarter. This slowdown in inter-bank trading reflected sufficient liquidity held by commercial banks arising from net inflows of foreign reserves and net redemptions of RBF Notes recorded during the quarter. The inter-bank lending rate rose sharply to 1.02 percent in the September quarter from 0.82 percent in the June quarter.

The Reserve Bank's monetary policy stance remained unchanged during the quarter, with the target interest rate on 91 day RBF Notes maintained at 1.75 percent (Graph 37).

Graph 37

RBF Notes - 91 Day Rate



---: no issues
Source: Reserve Bank of Fiji

As part of open market operations, around $296.6 million worth of RBF Notes were allotted in the September quarter, compared with $305.7 million issued in the previous quarter. The yield on the 91-day RBF Notes during this period averaged 1.74 percent, 1 basis point below the policy indicator rate.

During the same period, Government made 2 issues of Treasury Bills totalling $20 million, compared with 4 issues made in the previous quarter amounting to $43 million. The weighted average yields for almost all maturities of Treasury Bills increased during the quarter.

Of the statutory corporations, the Fiji Development Bank, Fiji Sugar Corporation and Public Rental Board also raised funds in the market through the issue of promissory notes during the quarter. Total promissory notes issued by the end of the September quarter totalled $23.0 million.

Capital Markets

The Government was the principal issuer of long-term debt instrument in the market during the September quarter. It raised $160 million through bonds with maturities ranging between 3 and 15 years to finance part of its fiscal deficit. Yields on government bonds have risen during the review period with the greatest increases noted in the 7, 10 and 15-year maturities.

In the secondary market for bonds, a pick-up in trading was noted over the quarter. There were 40 trades amounting to $5.6 million during the review period compared with 6 trades amounting to $2.5 million during the June quarter.

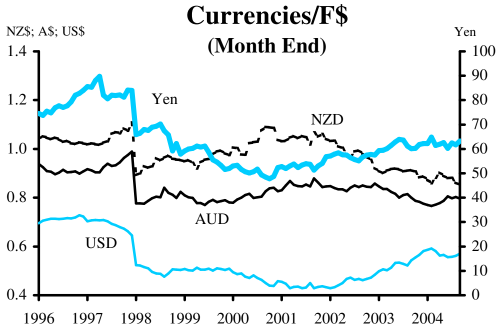
However, trading of equities slowed at the South Pacific Stock Exchange over the quarter. There were 0.9 million shares traded over the quarter, amounting to $1.8 million, compared with 3.7 million shares valued at $4.3 million in the previous quarter.

Foreign Exchange Markets

Movements in the exchange rates were generally mixed over the quarter (Graph 38). Compared with the end of June 2004, the Fiji dollar strengthened against the Japanese Yen (5.2%), US dollar (2.7%) and Euro (0.6%) but weakened against the New Zealand (3.1%) and Australian dollars (1.1%).

Graph 38

Exchange Rates - Selected Currencies/F$
(Month End)



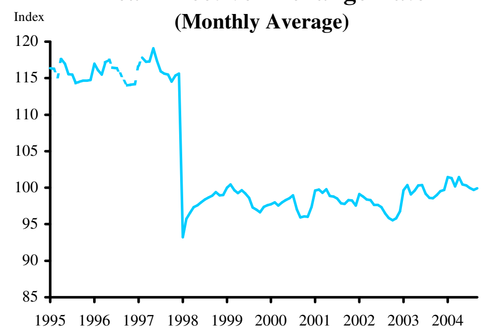
Source: Reserve Bank of Fiji

The Nominal Effective Exchange Rate Index (NEER), which reflects aggregate exchange rate movements between the Fiji dollar and currencies of major trading partners, rose marginally over the quarter, indicating an appreciation of the Fiji dollar against the basket of currencies.

During the same period the Real Effective Exchange Rate Index of the Fiji dollar, which adjusts the NEER for inflation differentials across Fiji's major trading partners, declined by 0.4 percent (Graph 39).

Graph 39

Real Effective Exchange Rate
(Monthly Average)



Source: Reserve Bank of Fiji

Financial Intermediaries

Latest movements in commercial bank interest rates generally reveal an upward trend.

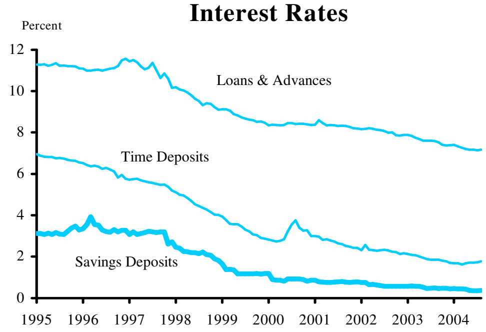
The weighted average lending rate on commercial bank outstanding loans remained unchanged at 7.17 percent in August, compared with the end of the June quarter (Graph 40).

In the same period, the saving and time deposit rate rose by 1 basis point and 6 basis points to 0.36 percent and 1.77 percent, respectively.

Broad money continued its strong growth during the first two months of the review period, growing by 20.5 percent in the year to August. During the same period, narrow money, which consists of demand deposits and currency in circulation, rose by 39.5 percent, reflecting higher demand for transaction balances amidst strong household spending and retail trade activities.

Graph 40

Interest Rates

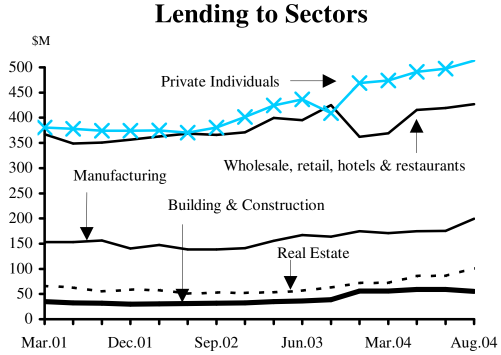


Source: Commercial Banks

In the year to August, private sector credit rose by 13.1 percent following an expansion of 13.8 percent in the previous month. During the same period, the total amount of loans outstanding in the banking system increased by 14.3 percent with increased lending noted for private individuals, real estate, manufacturing sector, public enterprises, building & construction and the wholesale, retail, hotels & restaurants sectors (Graph 41).

Graph 41

Lending to Sectors



Source: Commercial Banks

In contrast, commercial bank lending to the agriculture, mining & quarrying, central & local government sectors declined during the same period.

Total outstanding loans and advances by Licensed Credit Institutions (LCIs),[3] rose by 23.0 percent in the year to August underpinned mainly by higher lending to private individuals, building & construction, real estate, wholesale & retail trade, and manufacturing sectors. On the downside, lending to the professional & business service sector and central & local government declined during this period. Compared with the previous quarter, the weighted average lending rate on LCIs' outstanding loans fell by 3 basis points to 11.82 percent.

Banking Industry Quarterly Condition Report – June 2004

Overview

The financial position of the banking system[4] in the second quarter of 2004 was satisfactory[5] and the key prudential indicators remained favourable. The satisfactory performance was characterised by:

- High levels of capitalisation, as a result of higher retained profits;
- Adequate liquidity, with sufficient liquid assets to cover unexpected withdrawals;
- Increased lending activities across all major sectors;
- Higher profitability due to higher non-interest income for banks and higher net interest income for credit

[3] LCI's include Merchant Finance Investment Company Limited, Credit Corporation (Fiji) Limited and Home Finance Company Limited.
[4] Banking system comprises five banks and three credit institutions licensed under the Banking Act 1995.
[5] Licensed financial institutions are rated on a scale between I (the highest) and V (the lowest). A Satisfactory rating is equivalent to a II on that scale.

institutions, as well as lower bad debts and provisioning expenses;

- Improvements in classified exposures, with major reclassifications of non-performing loans to performing status, coupled with higher recoveries.

Banks

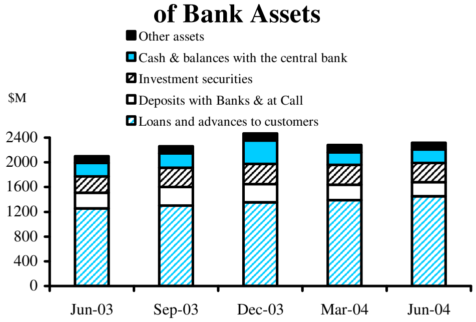
Sources and Uses of Funds

In June 2004, total assets of the banking industry[6] grew over the quarter by 1.6 percent to $2.3 billion and over the year by a significant increase of 10.4 percent.

The higher assets over the quarter were reflected in higher lending (4.4%) and increased cash and settlement account balances (13.3%). The increase in the cash and settlement account balances resulted from maturing investments at the end of June 2004 (Graph 42).

Graph 42

Structural Change and Growth of Bank Assets



Source: Commercial Banks

On the liabilities side, deposits grew by 1.5 percent. Demand deposits rose 3.0 percent over the quarter and accounted for 38.3 percent of total deposits. Time deposits comprised 34.4 percent, with holders continuing to exhibit preference for deposits with longer maturities given the larger interest differentials between short and longer term deposit rates.

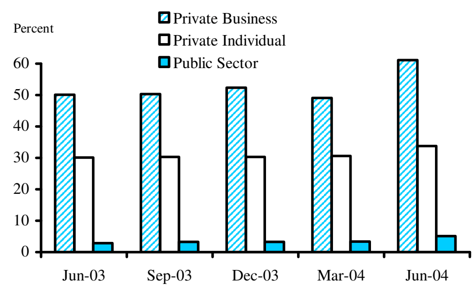
In terms of holders, private individuals accounted for 44.4 percent of total deposits as at end June 2004, followed by private sector business entities (26.9%).

Direction of Credit

The lending profile of the banking industry was relatively unchanged from the first quarter of 2004. Lending continued to be dominated by the private business sector, which comprised 61.1 percent ($1.5 billion) of total loans and advances (Graph 43).

Graph 43

Loans and Advances by Sector as Percentage of Total Loans



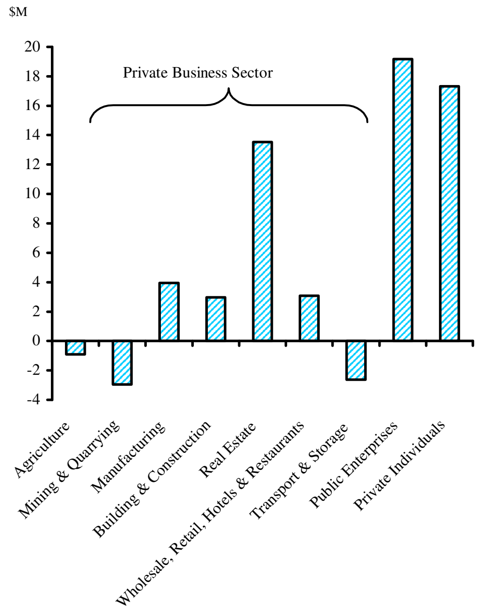
Source: Commercial Banks

The highest lending growth in the June 2004 quarter was again to the private business sector, which rose by $19.2 million (2.2%) to $888.4 million. The bulk of the new lending was for real estate (Graph 44).

[6] Banking industry comprises five banks: Australia and New Zealand Banking Corporation, Westpac Banking Corporation, Colonial National Bank, Bank of Baroda and Habib Bank Limited.

Graph 44

Changes in Loans & Advances by Sector over the June 2004 Quarter



Source: Commercial Banks

Lending to the public sector rose by $19.1 million (34.8%) from $54.8 million in March 2004, largely attributed to public enterprises.

Private individuals sector loans increased by $17.3 million (3.7%) from $473.8 million. The demand for loans and advances for housing purposes was higher (up by 4.2%), whilst transport loans declined by 0.5 percent.

Profitability

Against the backdrop of improving economic conditions, the pre-tax profit of banks increased by 4.0 percent to $20.9 million over the June quarter, driven primarily by higher net income,[7] coupled with declines in bad debts and loan loss provisions. Compared to June 2003, the pre-tax profit was a marked improvement by 31.6 percent.

The return on equity (annualised) of the banking industry increased to 38.8 percent from 30.6 percent in March 2004 (June 2003: 35.8%).

The net income of the banking industry rose by 3.1 percent to $22.9 million in June 2004, resulting mainly from higher non interest income and marginally lower operating expenses.

Total bad debts and loan loss provisions of the banking sector declined by 5.6 percent during the second quarter, attributed mainly to higher recoveries contributed by improved debt servicing capacity of borrowers. This can be attributed to the improved wealth position of private individuals reflected by an increase in lending to that sector.

Net interest income, however, decreased by 2.9 percent over the quarter, with interest income declining by 3.8 percent.

Interest expense contributed positively to net interest income, declining by 8.5 percent. This was due to a reduction in interest paid out on deposits.

The major component that contributed to non interest income rising over the quarter was income from foreign exchange transactions, which rose by $0.4 million. Other income also rose by a corresponding amount.

[7] Net Income = Net interest income plus Non Interest Income minus Operating Expenses.

Bank Profitability

	Jun-03	Mar-04	Jun-04	% Change	
	$M			Over Qtr	Over Jun-03
Net interest income	24.56	26.31	25.54	**-2.9**	**4.0**
Add: **Non interest income**	16.87	18.75	19.56	**4.3**	**15.9**
Income from overseas exchange transactions	6.67	6.87	7.27	**5.8**	**9.1**
Commission	1.29	2.73	2.61	**-4.3**	**101.7**
Fee Charges	8.90	8.94	9.05	**1.3**	**1.7**
Other income	0.01	0.21	0.63	**200.9**	**5531.4**
Equals:					
Total operating income	41.43	45.05	45.10	**0.1**	**8.9**
Less: Operating expenses	21.83	22.89	22.25	**-2.8**	**1.9**
Less: Bad Debts & provisions	3.75	2.12	2.00	**-5.6**	**-46.8**
Equals:					
Profit before tax	15.85	20.05	20.85	**4.0**	**31.6**
Less: Tax	1.85	7.19	5.52	**-23.3**	**198.1**
Equals:					
Net profit after tax	14.00	12.87	15.34	**19.2**	**9. 6**

Source: Commercial Banks

Declining operating expenses resulted in the improvement of the efficiency ratio from 50.8 percent to 49.3 percent.

The reduction in operating expenses was due to a reduction in management expenses by 14.1 percent[8] while other expenses rose by 5.0 percent over the quarter. Personnel expenses continued to make up the majority of operating expenses, comprising 47.9 percent of operating expenses this quarter.

The annualised return on assets (pre-tax) to average assets improved from 3.4 percent to 3.6 percent in June 2004 (June 2003: 3.0%).

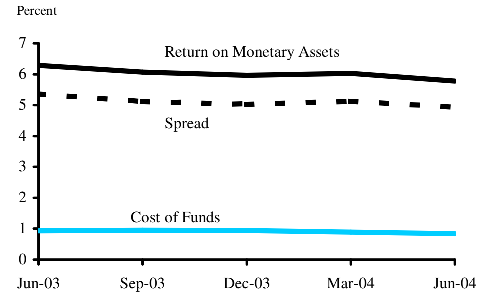
[8] Banks record Management Expenses at different times over their financial period.

Interest Margin and Spread

Over the quarter, the cost of funding liabilities (annualised) declined slightly by 4 basis points to 0.84 percentage points, while the yield on earning assets (annualised) fell by 28 basis points resulting in an overall decrease in the interest spread[9] of 20 basis points (Graph 45).

Graph 45

Margins and Spreads



Source: Commervial Banks

The gap between the yield on earning assets and the cost of funding liabilities has slightly narrowed.

As at end June 2004, the weighted average cost of funds stood at 0.67 percent while the average return on interest earning assets was 5.70 percent. The weighted average lending rate was 7.26 percent.

Asset Quality

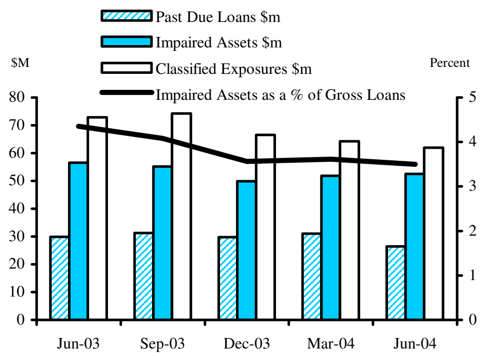
Classified exposures (credit facilities falling under substandard, doubtful and loss categories of loans as defined in the Banking Supervision Policy Statement Guideline Number 3 of the Reserve Bank of Fiji) of the banking industry declined by 3.5 percent from $64.2 million in

[9] Interest Spread = difference between the average rate on interest earning assets and the average rate on interest bearing liabilities.

March 2004 (Graph 46). Compared to June 2003, classified exposures substantially dropped by 14.9 percent to $62.0 million in June 2004.

Graph 46

Asset Quality



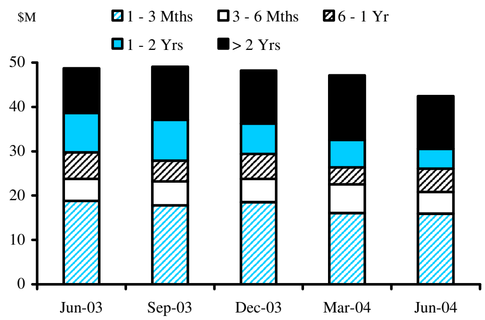
Source: Commercial Banks

Improvements in the level of classified exposures were due to major reclassifications of impaired assets under substandard categories to performing loans, coupled with strong recoveries and some write-offs of bad loans, under loss categories. This, as earlier mentioned, may be attributed to the improvement in the wealth position of private individuals, indicated by the increase in loans to them.

Impaired assets[10] of the banking industry increased by 1.3 percent to $52.5 million in the June quarter (June 2003: $56.6 million). Doubtful loans continued to represent the majority of impaired assets, comprising 71.2 percent of total impaired assets as at end June 2004. Loss and substandard loans represented 25.5 percent while total impaired assets comprised 3.2 percent.

Graph 47

Past Due Status



Source: Commericial Banks

Total past due loans[11] decreased significantly by 14.8 percent to $26.5 million in June 2004 (Graph 47). Substantial reductions were noted for all the past due levels except for the 6 months to 1 year category, which rose by 36.9 percent over the quarter.

In line with decreasing classified exposures, specific provisions of the banking sector declined to $21.0 million from $22.5 million in March 2004 (Graph 48).

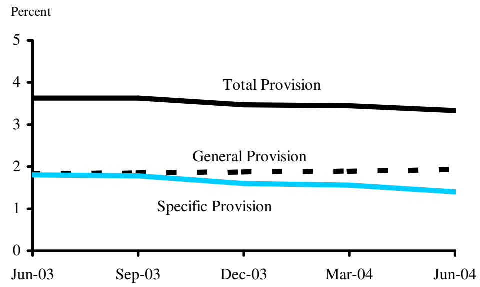
General provisions continued to trend upwards with a 6.7 percent increase reported as at end June 2004. As a percentage of gross loan portfolio, general provisions rose slightly to 1.9 percent. The trend in general provisions may be attributed to a conservative stance taken by banks in Fiji, and providing for an increasing loan portfolio, rather than a reflection of an increase in risks of doing business.

[10] Impaired assets are those credit facilities, which are not fully performing, in terms of where the full amount of originally contracted interest is not being accrued or where the need for a specific provision is identified and allocated on a particular credit facility.

[11] Excludes the 1–3 month category.

Graph 48

Provisioning as a Percentage of Total Gross Loans



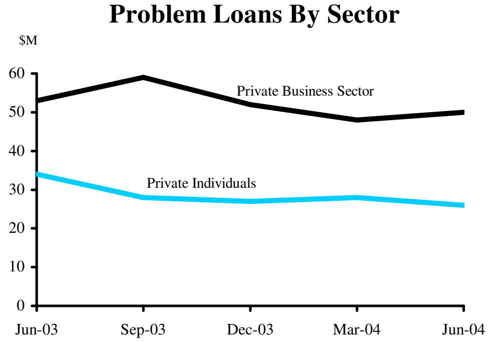
Source: Commerical Banks

In terms of problem loans by sector, loans to private individuals improved by 7.0 percent over the quarter, indicating greater commitment by private individuals to servicing their debt.

Problem loans to the private business sector rose by 3.8 percent to $50.2 million, attributed to the deterioration of loans mainly in real estate and manufacturing sectors (Graph 49). This is consistent with the growth of loans depicted in these sectors.

Graph 49

Problem Loans By Sector



Source: Commercial Banks

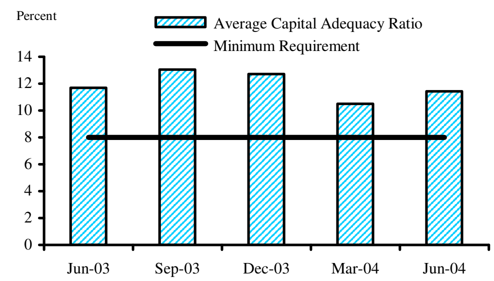
Capital Adequacy

The banking sector remained resilient and well capitalised, with the capital adequacy ratio sustained consistently above the minimum required ratio of 8 percent (Graph 50).

The capital base of the banking industry increased by $16.1 million to $168.7 million in June 2004, of which unaudited retained profits under Tier 2 capital contributed $15.3 million.

Graph 50

Banks' Capital Adequacy Ratio



Source: Commercial Banks

Total risk weighted assets increased over the quarter by $30.5 million due to increases in loans to commercial public sector companies ($37.4 million), classified under risk weight of 100 percent and loans fully secured by residential mortgages ($10.6 million), classified under risk weight of 50 percent. The increases in these risk weight categories were somewhat mitigated by declines in other risk weight categories, but not large enough to cause a reduction in the total risk weighted assets.

Liquidity

Liquidity in the banking industry continued to decline, largely resulting from a fall in liquid assets by 2.3 percent to $663.1 million in June 2004 (June 2003: $644.6 million). Liquid assets such as investments and deposits with banks and at call contracted by 3.6 percent and 7.4 percent respectively (Graph 51).

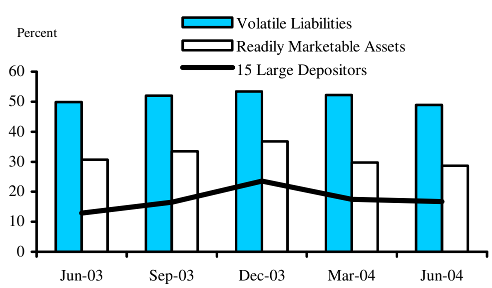
However, this reduction was somewhat offset by cash and settlement account balances, which grew by 13.3 percent.

In terms of liquidity management via maturity mismatch analysis, the banking industry, overall, projected sufficient liquidity to meet the cash outflows and any unexpected withdrawals. There were negative mismatches under '1-3 months' and '6-12 months' categories. However, this was covered by the overall level of liquid assets.

Although deposits expanded, volatile liabilities fell over the quarter by 4.7 percent to $1,134.0 million, attributed mainly to major contractions in non-resident local currency deposits. Volatile liabilities made up nearly half (49.0%) of total liabilities, which was slightly lower over the quarter by 3.2 percentage points.

Graph 51

Volatile Liability Coverage



Source: Commercial Banks

The 15 largest depositors balances of the banking sector declined by 2.5 percent from $397.9 million in the previous quarter. As a percentage of total liabilities, it stood at 16.8 percent compared to 17.5 percent in March 2004. This was mainly due to a reduction in Government's account balances with banks.

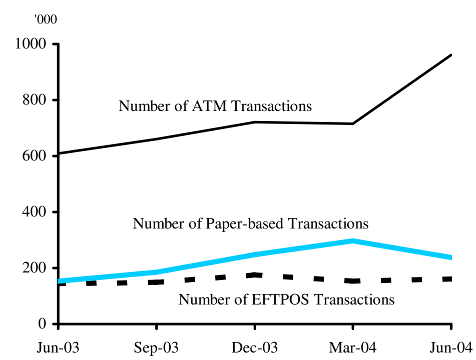
Electronic Banking

Technology is continuing to change the way banks operate and the way they interact with their customers. Electronic Funds Transfer at Point of Sale (EFTPOS), Automatic Teller Machines (ATMs), telephone and internet banking are increasingly becoming a means for customers to carry out financial transactions without having to visit a bank branch.

The volume of ATM transactions rose by 34.3 percent (Graph 52). EFTPOS terminals declined from 950 in March 2004 to 916 this quarter, while the volume of EFTPOS transactions increased by 5.0 percent.

Graph 52

Number of EFTPOS, ATM & Paper-Based Transactions



Source: Commercial Banks

The volume of paper-based transactions exhibited a 19.9 percent decline in June 2004, reflecting the increasing usage of electronic transactions by bank customers.

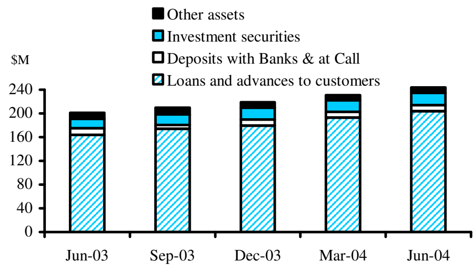
Credit Institutions

Sources and Uses of Funds

Over the June 2004 quarter, credit institutions continued to record growth in total assets, which was largely driven by a notable expansion in loans (Graph 53).

Graph 53

Structural Change and Growth of Credit Institution Assets



Source: Credit Institutions

Total assets stood at $244.0 million as at June 2004, an increase of $13.4 million or 5.8 percent over the quarter. This compares to the yearly increase of 21.3 percent. Gross loans increased by $11.4 million over the quarter.

Growth was also noted in the other assets category through non-equity investments.

On the liabilities side, term deposits held by credit institutions recorded a significant increase of 15.2 percent, over the quarter to end at $137.7 million. This increase was mostly caused by large institutional depositors taking advantage of the deposit rates offered by credit institutions.

Although balances owing to holding companies fell by $5.9 million over the quarter, credit institutions continued to rely on advances from parent companies to fund asset growth.

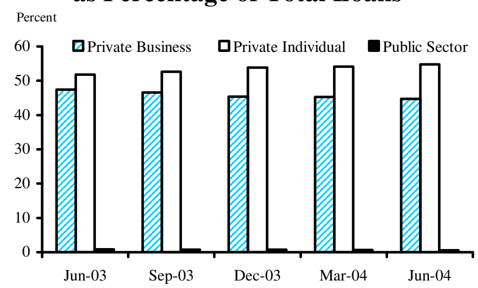
Other liabilities also showed notable increases, the result of an increase in dividends payable as two credit institutions reached their financial year-end.

Direction of Credit

Credit institutions' loans continued to trend upwards, driven mainly by increased lending to both households and businesses (Graph 54).

Graph 54

Loans and Advances by Sector as Percentage of Total Loans



Source: Credit Institutions

Gross loans and advances stood at $217.8 million compared to $206.4 million in March 2004 and $178.0 million in June 2003.

Over the quarter, credit institutions continued to build up lending in the private individuals sector. Loans outstanding to private individuals increased by $7.9 million to $118.2 million. Credit institutions reported new loans of $15.3 million to private individuals over the quarter. As a percentage of gross loans, total loans outstanding to private individuals represented 52.4 percent compared with 51.6 percent in March 2004 and 48.9 percent in June 2003.

Despite a $4.3 million increase over the quarter, loans outstanding to private sector business entities, continued to fall as a portion of total loans and stood at 46.2 percent compared to 46.9 percent in March 2004 and 49.4 percent in June 2003.

This highlights the increase in the concentration of credit institutions loans and advances to private individuals.

Profitability

With the growth in assets led by increased loans and advances, credit institutions recorded a notable increase in profitability. Profit before tax of credit institutions for the 3-month period ending June 2004 stood at $2.7 million, up by $0.3 million compared to the March 2004 quarter. Compared to June 2003, credit institutions recorded a significant increase in profits by $0.9 million (51.2%).

The major contributing factor to the increase in profits was interest income. Interest income increased by $0.4 million (5.4%) over the quarter from $6.8 million to $7.2 million. Credit institutions also recorded a $1.2 million (19.9%) growth in interest income over June 2003.

Non-interest income increased over the quarter by $0.1 million (due to an increase in other income), however, compared to June 2003 there was a slight decrease in non-interest income.

Operating expenses increased by $0.3 million over the quarter to $2.3 million due to increases in administrative costs in the other expenses category. Historically, personnel expenses accounted for the bulk of operating expenses. However, as at June end, other expenses comprised 44.1 percent of total operating expenses, surpassing personnel expenses at 40.7 percent.

Credit institutions' annualised return on assets (before tax) improved to 4.6 percent compared to 3.7 percent in June 2003 while there was only a little change compared to March 2004.

Credit institutions' also noted some improvement in the cost-to-income ratio, decreasing from 46.8 percent in June 2003 to 39.6 percent. The ratio has, however, increased when compared to 37.6 percent recorded in the last quarter.

Credit Institutions' Profitability

	Jun -03	Mar-04	Jun-04	% Change	
		$M		Over Qtr	Over Jun-03
Net interest income	4.1	4.8	5.1	**5.9**	**26.1**
Add: **Non interest income**	0.6	0.5	0.6	**17.0**	**-2.0**
Equals **Total operating income**	4.7	5.4	5.7	**7.0**	**22.4**
Less: Operating expenses	2.2	2.0	2.3	**12.5**	**3.5**
Less: Bad debts & provisions	0.7	0.9	0.7	**-16.5**	**7.2**
Equals: **Profit before tax & extraordinary items**	1.8	2.5	2.7	**10.9**	**51.2**
Less: Tax	1.6	0.4	0.5	**11.9**	**-71.7**
Equals: **Net profit after tax**	0.2	2.1	2.3	**10.7**	**1,214.4**

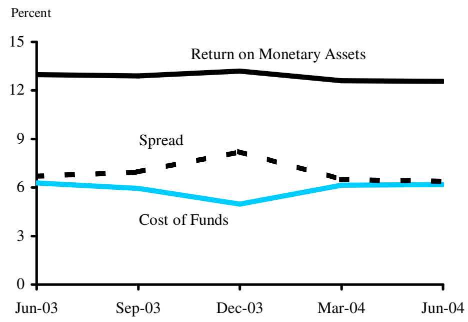
Source: Commercial Banks

Interest Margin and Spread

The annualised interest spread for credit institutions contracted to 6.4 percent from 6.5 percent over the quarter and from 6.7 percent over the year (Graph 55).

Graph 55

Margins and Spreads



Source: Credit Institutions

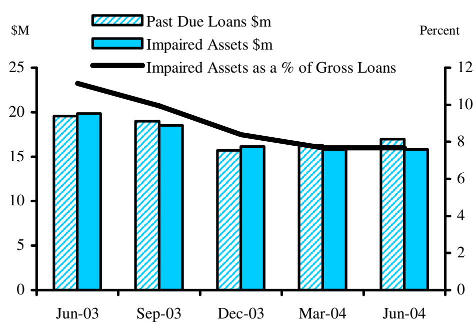
The annualised interest margin remained unchanged at 9.0 percent compared to the last quarter. However, it improved from 8.8 percent over the 12-month period. This is attributed to the increase in interest income.

Asset Quality

Over the quarter, asset quality for credit institutions deteriorated slightly as the level of impaired assets increased by $1.4 million to finish at $17.2 million as at June 2004 (Graph 56).

Graph 56

Asset Quality



Source: Credit Institutions

This represents 7.9 percent of total loans compared to 7.7 percent in March 2004. However, this remains below the value of $19.8 million as at June 2003, which comprised 11.1 percent of total loans.

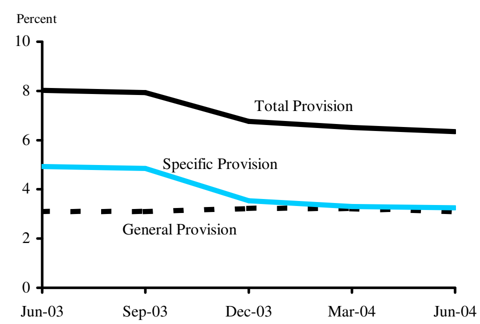
Over the quarter classified loans also increased by $0.7 million (3.8%) to $19.8 million. This comprised substandard accounts of $7.0 million (35.1%), doubtful of $3.4 million (17.2 %) and loss of $10.3 million (52.0%) as at June 2004.

However, classified loans as a percent of total loans and advances has improved to 9.1 percent as at June 2004 compared to 9.3 percent in March 2004 and 13.1 percent in June 2003.

Although there was a $0.7 million increase over the quarter, past due loans also continued to trend downward from $19.6 million in June 2003 to $17.0 million as at June 2004.

Graph 57

Provisioning as a Percentage of Total Gross Loans



Source: Credit Institutions

Provisions allocated for impaired assets and gross loans are considered adequate and above regulatory requirements. Specific provisions over gross loans remained at 3.3 percent over the quarter and decreased over the year from 4.9 percent (Graph 57). This downward trend is related to the general reduction in impaired assets over the year.

General provisions continued to rise in line with the increases in the loan portfolio of credit institutions. This stood at $6.7 million as at June 2004. As with the banks, this may reflect a conservative stance taken by credit institutions, and providing for an increasing loan portfolio, rather than an increase in risk of doing business in Fiji.

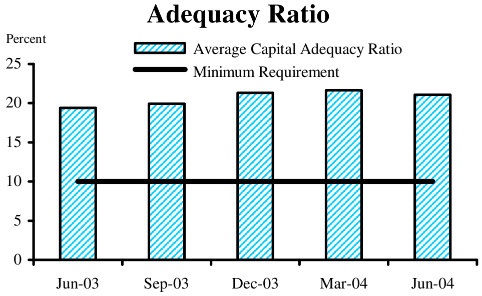
Capital Adequacy

Overall improving trends are noted for capitalisation of credit institutions, as a result of high retained earnings.

As at 30 June 2004, the capital adequacy ratio of all credit institutions stood at 21.1 percent. This was slightly lower than the 21.6 percent reported in March 2004, but above the capital adequacy ratio of 19.4 percent as at June 2003 (Graph 58).

Graph 58

Credit Institutions' Capital Adequacy Ratio



Source: Credit Institutions

The capital base of credit institutions grew by $0.9 million over the quarter and by $8.8 million over the year to finish at $36.5 million as at June 2004. The increase in total capital was largely due to increases in Tier 2 capital over the quarter and over the year.

Risk assets for credit institutions grew by $8.7 million over the quarter to $173.3 million. Compared to growth in total capital, total risk assets rose at a faster pace causing the reduction in capital adequacy ratio over the quarter.

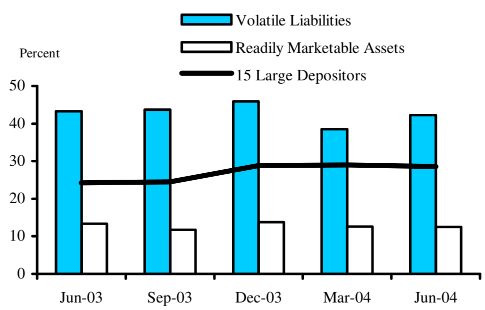
However, all credit institutions maintained capital adequacy ratios well above the RBF minimum requirement of 10 percent.

Liquidity

Over the quarter, there was a slight decline in the liquidity position of credit institutions. Volatile liabilities of credit institutions stood at $103.1 million as at June 2004. This increased over the quarter by $14.2 million or 15.9 percent (Graph 59).

Graph 59

Volatile Liability Coverage



Source: Credit Institutions

Volatile liabilities comprised 42.2 percent of total liabilities in June 2004. This has increased over the quarter from 38.6 percent.

The increase in volatile liabilities is indicative of the fact that the increase in assets of credit institutions has been funded by large institutional depositors.

Total deposits held by the 15 largest depositors for credit institutions increased over the quarter by $2.9 million (4.3%) to $69.7 million. Over the year, deposits from this source increased by $20.9 million (42.9%). Overall, funding from this source has showed a gradually increasing trend.

Readily marketable assets (liquid assets) increased over the quarter by 4.7 percent to $30.5 million. Over the year, liquid assets rose by 13.1 percent. However, as a percentage of total assets, this fell from 13.4 percent in June 2003 to 12.5 percent. There was no significant movement over the quarter.

Insurance Industry Quarterly Condition Report – March 2004

Overview

The first quarter of 2004, showed a marked increase of $28.9 million in the aggregate solvency surplus of assets over the required solvency margin for the insurance industry. The surplus more than doubled to $43.9 million from the corresponding quarter of 2003, with the life insurers accounting for the majority of the surplus. The main contributory factor was the increase in the life insurance admissible assets. The minimum required solvency margin of the industry, also increased but at a smaller rate of increase compared to admissible assets and was largely influenced by general insurers.

Combined insurers assets recorded a growth of 8.0 percent to reach $641.2 million. The growth was driven by both the life and general sectors with life insurers accounting for 72.4 percent of the total industry assets.

Solvency Position ($M)

Quarter Ended 31 March		Admissable Assets	MRSM*	Solvency Surplus
2004	General	25.4	15.8	9.6
	Life	48.5	14.2	34.3
	Total	**73.9**	**30.0**	**43.9**
2003	General	14.4	13.3	1.1
	Life	27.6	13.7	13.9
	Total	**42.0**	**27.0**	**15.0**

* MRSM - Minimum Required Solvency Margin
Source: Insurance Companies

The industry's overall after tax surplus was recorded at $13.1 million for quarter ended March 2004, twice the total recorded for the same period in the preceding year. Major contributing factors to the increase in surpluses was the growth in total revenue as a result of the acquisition of more businesses whilst expenses fell.

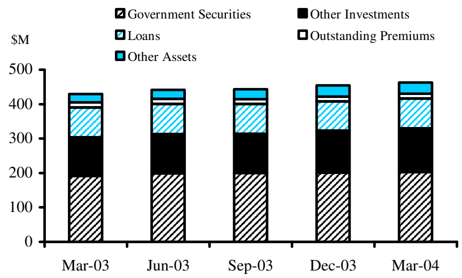
Life Insurers

The two licensed life insurers met the solvency requirement of the Insurance Act for quarter ended March 2004 and both recorded increases in solvency surplus over the year. A solvency surplus of $34.3 million was recorded against $13.9 million in 2003.

Combined life insurers assets recorded an 8.0 percent increase over the year to $463.9 million in 2004 (Graph 60). The asset distribution for life insurers remained unchanged with government securities, property and loans remaining the dominant mode of investment.

Graph 60

Distribution of Assets for Life Insurance Companies

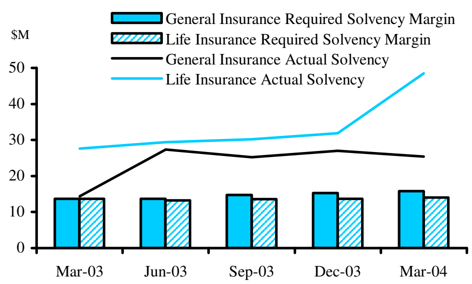


Source: Insurance Companies

The life insurers recorded an increase of 34 percent to $8.7 million in the after tax results (Graph 61).

Graph 61

Actual Solvency & Required Solvency Margin



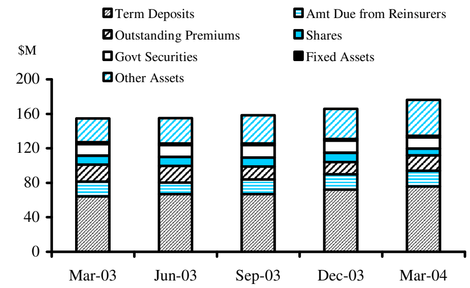
Source: Insurance Companies

General Insurers

All general insurers met the solvency requirement of the Insurance Act for the March 2004 quarter. An increase of 76.0 percent in net admissible assets to $25.4 million (2003: $14.5 million) contributed to the increase in solvency surplus of general insurers to $9.6 million (2003: $1.1 million). Assets are concentrated mainly in term deposits, government securities and outstanding premiums (Graph 62).

Graph 62

Distribution of Assets for General Insurance Companies



Source: Insurance Companies

The general insurers posted a good underwriting result for the quarter and recorded an after tax surplus of $4.4 million. This was a turnaround from the after tax loss of $0.1 million in the same period in the preceding year. The growth in gross and net premium income combined with a decrease in claims, contributed to the after tax surplus for the quarter under review. One of the general insurers net claims incurred reduced substantially to $1.1 million in March 2004 from $5.8 million in March 2003 as a result of a fire and Cyclone Ami claims that occurred in the first quarter of 2003.

Insurance Brokers

Insurance brokers recorded a fall in net after tax profit to $0.6 million in the March 2004 quarter when compared to $0.8 million in 2003. The reduced profit was a result of increase in operational expenses.

Broking account balance stood at $2.7 million (2003: $4.5 million) with 70 percent of this balance being under 30 days hence generally complying with Section 7 of the Insurance Act.

The Bank continued to process offshore placement applications. During the quarter a total of 88 applications were approved with premiums remitted offshore amounting to approximately $4.5 million. A similar number and value of applications were approved in the March quarter of 2003.

For the Record

CONCLUSION OF THE INAUGURAL RBF ECONOMIC SYMPOSIUM

Statement by Governor, Mr S Narube, 16 July 2004.

The inaugural 1½ day Reserve Bank of Fiji Economic Symposium concluded at the Tradewinds Convention Centre today.

The Governor of the Bank, Mr Savenaca Narube, in making his roundup comments at the Symposium said that the first ever Economics Symposium of the Bank was a success. Feedback received from the participants was very encouraging indeed. Moreover, the dual purposes of the Symposium – namely to promote greater economic and financial literacy of RBF policy choices and to obtain feedback from the greater community about how such policy frameworks can be improved – were largely achieved.

Some of the key outcomes of the Symposium include: the need not to be complacent and waste our current good economic performance. Mr Narube stressed that reforms need to be put in place for the nation to continue to enjoy the present good growth into the future. He also highlighted that the nation as a whole should aim to achieve higher growth targets in the years ahead. Higher investment levels, productivity and strengthening of Fiji's capital market were all essential ingredients to raising the growth levels to even higher than the average growth of about 5 percent seen for the last three years. However, growth should be export-led, Mr Narube stressed. The Governor also emphasised that a sound macroeconomic environment is essential for sustainable and balanced economic growth in the future.

While deliberating on the theme of the Symposium, namely - Can the Financial Sector be the Locomotive of Growth in Fiji?; Mr Narube said that there was no argument that a strong and dynamic financial system was a cornerstone of greater economic success for Fiji. He also said that financial system remained sound. "Our strong prudential supervision of licensed financial institutions has meant that the risks of any major financial calamity witnessed in other parts of the world have been minimised," the Governor said. However, we will not rest on our laurels. We will continue to be vigilant and be proactive in the supervision and promotion of a sound financial system in Fiji. This will ensure confidence in the system and will naturally bring about greater economic success for Fiji.

The Prime Minister of Fiji, Honourable Laisenia Qarase while delivering the opening address at the Symposium, also commended the sound status of our financial system and acknowledged that it significantly contributed to the economic prosperity of Fiji. However, he encouraged the financial sector not to forget about the rural community. Honourable Qarase asked commercial banks to take their banking services to the rural community so they too could be encouraged to save and ultimately make contributions to the nation's well being. The Prime Minister felt that this drive to help the poor could also be complemented by the Asian Development Bank now that they have set up a regional office here in Suva.

The speakers during the Conference highlighted various necessary conditions for lasting economic prosperity. These include the need to have strong leadership, good role models, high moral values, transparency in policy, greater regional cooperation, and the need to lower business costs.

Another topical issue of the Conference was the debate about a common currency. The Governor felt that there was no harm is discussing the merits of a common currency for the Pacific region. However, he highlighted that the project of a common currency is something for us to consider over the medium term. He also enunciated the need to take a more considered approach to issues such as the common currency as many of the Pacific Island Economies while similar in size had several unique characteristics.

STATISTICAL ANNEX

LIST OF TABLES

SOURCES:

Reserve Bank of Fiji
Commercial Banks
Fiji Development Bank
Fiji National Provident Fund
Fiji Islands Bureau of Statistics
Ministry of Finance

ABBREVIATIONS

$:	Fiji Dollars unless stated otherwise
m:	Million
bn:	Billion
(b)	Budget
(e):	Estimate
(f):	Forecast
(p):	Provisional
(r):	Revised
n.a.:	Data not available
n.i.:	No issues
n.t:	No trading
-:	Zero
RBF:	Reserve Bank of Fiji
IMF:	International Monetary Fund
CIF:	Cost of goods, including insurance and freight to Fiji
FOB:	Free on board (the value of goods at Fiji ports before export).