



RESERVE BANK OF VANUATU

FINANCIAL & ECONOMIC NEWS

SUMMARY

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Issue 152

September 2010

MONETARY SURVEY

Total money supply (M2) continues contracting, falling by a further 0.4 percent during August on the heel of 1.9 percent decline recorded in July. This contraction reflected declines in both net foreign assets (NFA) and domestic credit. Owing to this monthly decline, the annual growth rate of M2 for the year ending August 2010 declined to 7.3 percent.

Chart 1 below shows that the annual growth rate of M2 was largely determined by the trend in NFA. Growth in domestic credit though slowed recently, continued to remain strong.

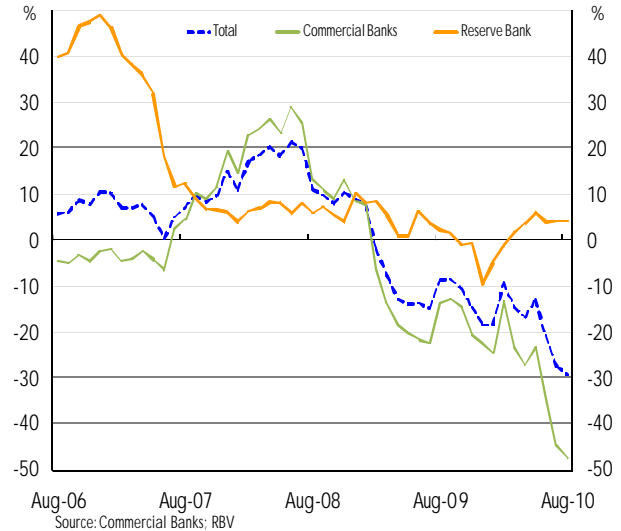
Chart 1: Total Money Supply
(Percentage Change; Year-on-Year Growth)



Determinants of Money Supply

Total NFA continued trending downwards, contracting by 2.3 percent in August, driven by declines in the NFA holdings of both the Reserve Bank and commercial banks by 0.5 percent and 4.2 percent, respectively. The year-on-year growth rate of NFA remained negative at 29.3 percent.

Chart 2: Net Foreign Assets
(Percentage Change; Year-on-Year Growth)



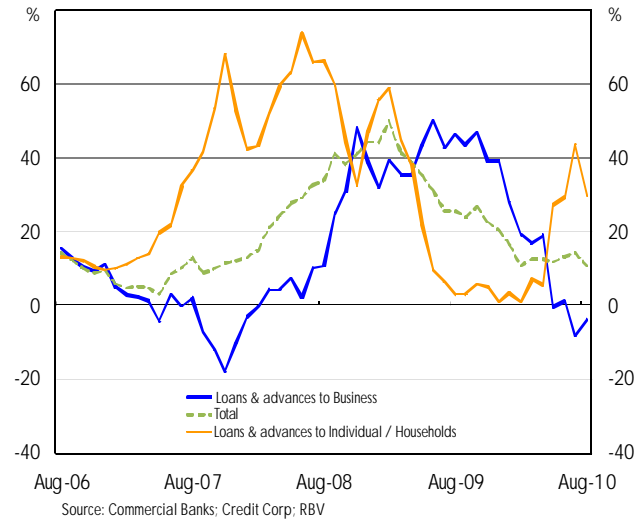
The decline in the NFA of the Reserve Bank mainly reflected an increase of 3.1 percent in its foreign liabilities, which outweighed the growth of 0.2 percent in its foreign assets. Despite a decline in the overall NFA, the Bank recorded net inflows of foreign exchange during the month. The bulk of these inflows were via cash and project grants on behalf of the government, by foreign embassy and interest on official reserves. These inflows offset foreign exchange outflows, which were mainly for import financing by commercial banks. With these inflows, projected months of import cover remained unchanged at 6.1, the same level recorded in July. The year-on-year records showed an improvement of 4.2 percent in the Reserve Bank's NFA position.

Commercial banks' NFA declined further during August as a result of their foreign asset holdings contracting by 1.5 percent. Furthermore, commercial banks' foreign liabilities continued to increase, registering 1.1 percent during the month. Over the year to August 2010, the growth in

commercial banks' NFA remained negative at 47.3 percent.

Domestic credit fell 0.3 percent during August, while the annual growth slowed to 12.8 percent. The decline in growth during the month was attributed by decreases in loans extended to the private sector and non-financial public enterprises. Net claims on the government and loans to municipalities have, however recorded increases in credit.

Chart 3: Private Sector Credit
(Percentage Change; Year-on-Year Growth)



Private sector credit¹ contracted by 0.6 percent in August 2010 following an expansion of 1.5 percent in July. The annual growth moderated further to 11.0 percent in August from 14.5 percent over the year to July. The month on month decline could be partly explained by the increase in the SRD ratio at the beginning of August. Private sector credit has continued to slow progressively since 2009 as commercial banks tightened their lending practices, as seen in the improvement in their quality of loans.

The decline in growth over the month consisted largely of loans and advances to individuals & households which declined by 9.3 percent, offsetting the increase of 9.8 percent in business loans. Over the year a similar picture can be seen, with a slowing in total growth reflected a slowdown in growth of loans to individuals &

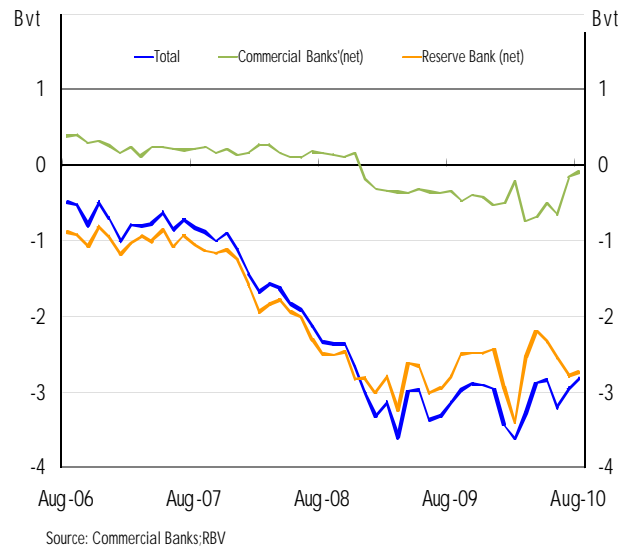
¹ Credit to the private sector includes data from commercial banks, Credit Corp and the RBV.

households, while loans to business though increased, albeit moderately.

Loans extended to municipalities increased by 13.3 percent during the month, but declined by 14.8 percent over the year. At the same time, loans to non-financial public enterprises decreased 1.8 percent during the month but rose by 11.0 percent over the year.

The government's net credit position vis-à-vis the banking system deteriorated in August 2010. This was reflected in increases of 1.8 percent and 44.0 percent in the Reserve Bank and commercial banks' net claims on the government, respectively. The increase in the banking system, net claims on the government during the period reflected a decline in government deposits held with both institutions. Similarly, the government's net credit position deteriorated over the year to August 2010 (Chart 4).

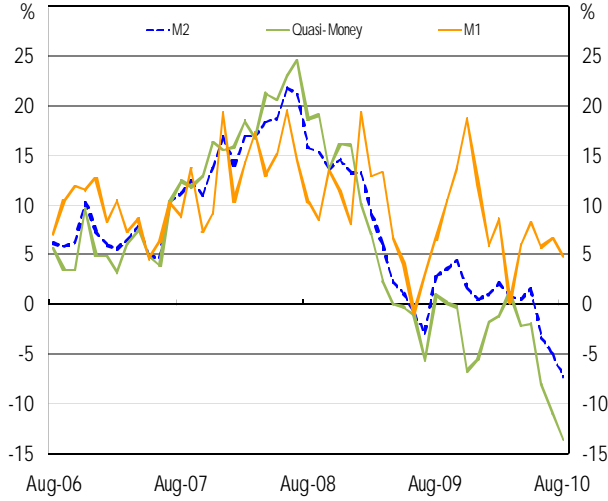
Chart 4: Net Lending Position of Government
(Billions of Vatu; Monthly Data)



Measures of Money Supply

The contraction in M2 was mirrored in both its components, with M1 falling by 0.7 percent and quasi-money by 0.3 percent. Over the year ending August 2010, the decline in M2 was driven mainly by quasi-money, which fell 13.5 percent, outweighing the growth of 4.9 percent in M1 (Chart 5).

Chart 5: Measures of Money
(Percentage Change; Year-on-Year Growth)



Source: Commercial Banks, RBV

The month-on-month decrease in M1 was driven by currency in circulation, which declined by 4.2 percent offsetting the increase of 0.2 percent in demand deposits. The level of currency in circulation has normalized after the seasonal high spending recorded at end July. The growth in demand deposits was mainly attributed to an increase of 5.8 percent in its local currency component, which offset a 5.7 percent decline in demand deposits denominated in foreign currency.

The fall in the level of interest bearing deposits resulted from declines of 0.1 percent and 0.6 percent in time and savings deposits denominated in both the local and foreign currencies, respectively.

Reserve Money

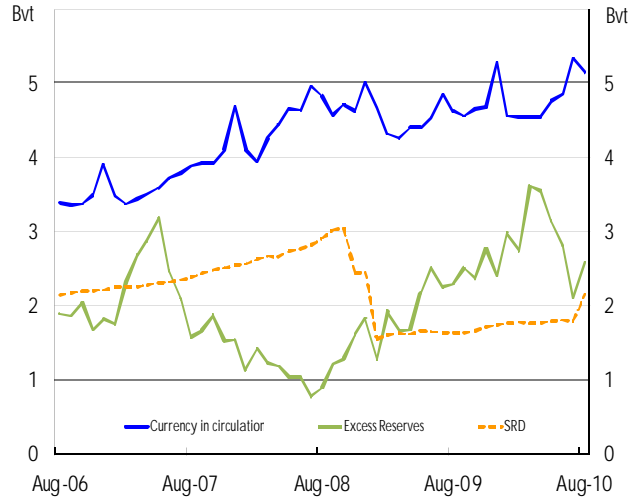
Reserve money² rose 7.1 percent in August and 16.5 percent on a year-on-year basis. The increase was due to increases in excess reserves and SRD by 23.4 percent and 20.4 percent, respectively. The rise in the level of SRD reflected the increase in SRD requirement ratio from 50 percent to 6.0 percent during the month.

The increase in the excess reserves of commercial banks can be attributed to (i) the decline in outstanding RBV notes (ii) the deterioration in the governments net position with the Reserve Bank (iii) net inflows of foreign exchange and (iv) the

²Reserve money comprises currency in circulation, Statutory Reserve Deposits (SRD) and Excess Reserves.

offsetting effect of the decline in currency in circulation.

Chart 6: Components of Reserve Money
(Billions of Vatu)



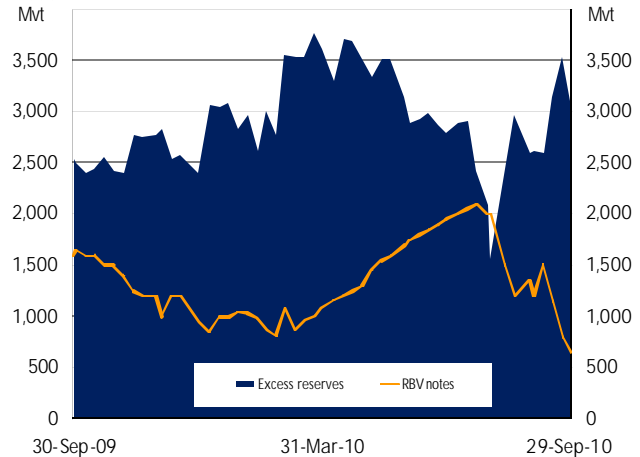
Source: Commercial Banks; RBV

Open Market Operations (OMO) – September 2010

The Bank conducted two OMOs during September 2010 where VT800 million worth of RBV notes were issued compared to VT600 million in August 2010.

Total subscription received for these issues was VT1,250 million compared to VT1,500 million received during the previous month. This high level of subscription compared to the total offer reflects the fairly high level of liquidity in the system in September.

Chart 7: Commercial Banks Liquidity
(Levels; Millions of Vatu; Weekly Data)



Source: RBV

Table 1: Amount Allotted (Millions of Vatu)

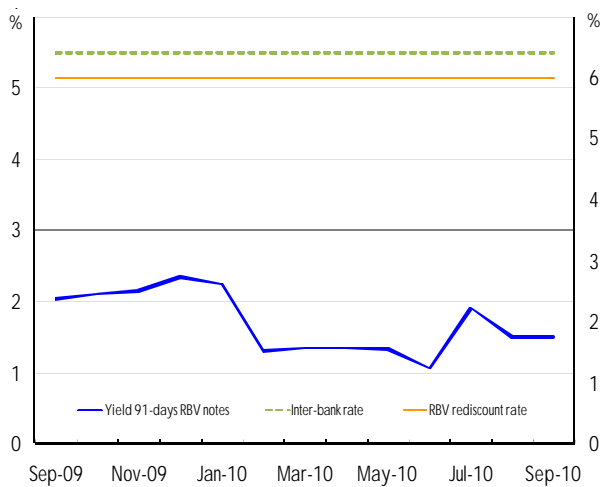
Term	Amount Allotted
7 days	200
14 days	200
28 days	150
63 days	150
91 days	100

Total maturity for the month was VT1,500 million leaving outstanding notes at VT650 million as of end September compared to VT1.2 billion at the end of the previous month.

Table 2: Yields on RBV Notes (Percent)

Term	End Sept. 2010	End Aug. 2010
7 days	0.88	0.89
14 days	0.88	0.89
28 days	0.88	0.89
63 days	1.50	1.50
91 days	1.50	1.50

Chart 8: Short-term Interest rates



Source: Commercial banks; RBV

The inter-bank rate remained at 5.5 percent.

Interest Rates

Table 4: Interest Rates (Percent)

		Deposit Interest Rates			
	Savings	1 -Mnth	2-6 Mnths	Above 6 Mnths	
Jun-10	0.5-5.00	1.50-7.50	1.60-7.00	2.50-9.80	
Jul-10	0.5-5.00	1.50-7.50	1.60-7.00	2.50-9.80	
Aug-10	0.5-5.00	1.50-7.50	1.60-7.00	2.50-8.00	
		Lending Rates			
	Commercial	Personal	Housing	Agriculture	
Jun-10	8.95-23.0	5.5-26.5	8.9-13.0	9.99-19.5	
Jul-10	8.95-23.0	5.5-26.5	8.9-13.0	9.99-19.5	
Aug-10	8.95-23.0	5.5-26.5	8.9-13.0	9.99-19.5	

As shown in Table 4, commercial banks' deposit and lending rates in general remained unchanged, with the exception of upper interest rates on maturities above 6 months registering an increase during the month, see table 4.

Exchange Rate Developments – September 2010

The exchange rate developments of the vatu vis-à-vis its major trading currencies for the month of September are shown in the following table and charts.

Table 3: Exchange Rates

	Vatu/USD	Vatu/AUD	Vatu/NZD	Vatu/EUR
Sep-10	95.23	92.25	70.24	147.49
1 month ago	100.15	82.29	70.62	126.85
% Change	-4.9	12.1	-0.5	16.3
3 months ago	102.96	87.38	71.25	125.50
% Change	-7.5	5.6	-1.4	17.5
12 months ago	98.91	86.13	70.68	144.30
% Change	-3.7	7.1	-0.6	2.2

Note: (€) appreciation of vatu

Chart 9: Exchange Rate against USD and AUD (Indices; September 2006=100)

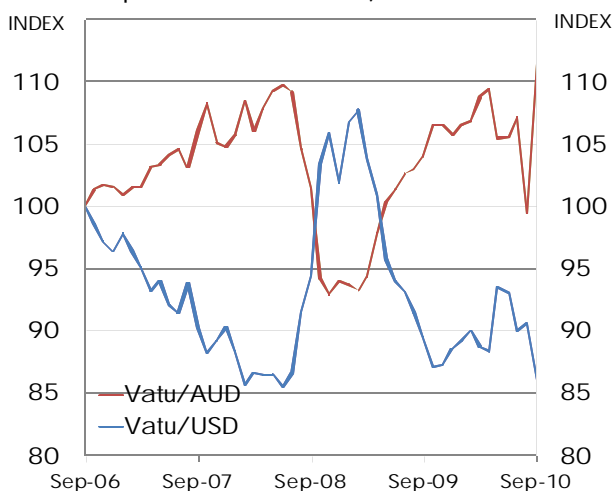
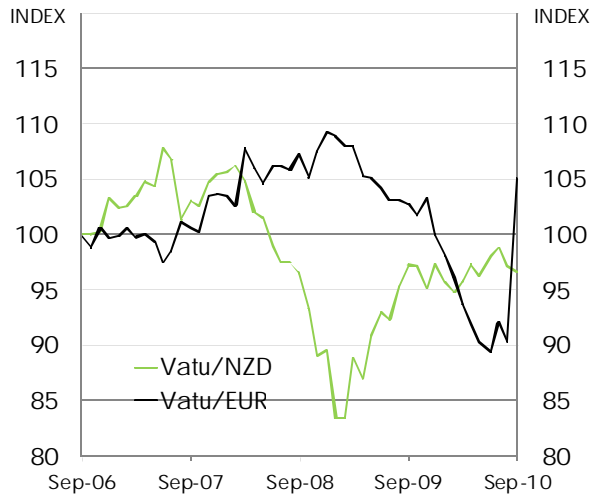


Chart 10: Exchange Rate against NZD and EUR
(Indices; September 2006=100)



Throughout the month vatu appreciated against the US dollar (USD) and New Zealand dollar (NZD), but depreciated against the Australian dollar (AUD) and euro (EUR).

Vatu continued to appreciate against the USD in September, supported by continued indications of a slow and vulnerable recovery in the US. A series of data releases, including figures showing that unemployment has edged up to 9.6 percent in August, prompting the Federal Reserve to suggest that it may take further unconventional measures to support economic activity. Measures likely to be considered by the central bank include the purchase of more government debt, which would

place further downward pressure on the return to holding US assets.

The sharp depreciation of vatu against the AUD during the month was driven by comments from the Reserve Bank of Australia indicating that further monetary tightening was increasingly likely. Despite a moderation in international commodity prices, Australia continued to experience historically very favourable terms of trade, which is expected to underpin growth in the medium term.

The appreciation of the EUR in September was largely driven by the uncertainty surrounding other major currencies. Despite lingering sovereign debt risks in peripheral countries, the more solid results posted by core European economies reduced the perceived probability of further monetary expansion in the currency area and encouraged investors to hold the currency.

The vatu recorded a modest appreciation against the NZD during the month, following the Reserve Bank of New Zealand's indication that the pace of removal of monetary stimulus was likely to be slower than previously indicated. However, despite a softening in the overall outlook, export demand is expected to be supported by continued growth in Australia and China. Towards the end of September, Statistics New Zealand reported that the August trade deficit was half the average of the previous five months.

MONETARY AND FINANCIAL STATISTICS
TABLE A1 : CONDENSED BALANCE SHEET OF RESERVE BANK OF VANUATU

End of Period	Aug-09	May-10	Jul-10	Aug-10	%Change		
					1 Month	3 months	12months
Foreign Assets	12587.8	15033.4	15364.5	15392.9	0.2	2.4	22.3
Foreign Exchange 1/	11925.6	14408.0	14739.2	14765.6	0.2	2.5	23.8
Reserve Position with IMF	434.2	382.2	382.2	382.2	0.0	0.0	-12.0
SDR Holdings	228.0	243.1	243.1	245.1	0.8	0.8	7.5
Claims on Government	619.9	620.7	620.7	618.9	-0.3	-0.3	-0.2
Advances to statutory Bodies	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Advances to commercial Banks	0.0	0.0	0.0	0.0	0.0	0.0	0.0
O/w under repurchase agreement	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Assets	2092.6	2003.4	2058.3	2128.3	3.4	6.2	1.7
Total Assets	15300.3	17657.5	18043.5	18140.1	0.5	2.7	18.6
Reserve Money	8490.1	9689.9	9230.8	9889.5	7.1	2.1	16.5
Currency outside Banks 3/	3641.1	3878.2	4178.8	4002.2	-4.2	3.2	9.9
Commercial Banks Cash	917.6	875.3	1159.3	1139.5	-1.7	30.2	24.2
Commercial Banks Deposit with RBV	3931.4	4936.3	3892.7	4747.7	22.0	-3.8	20.8
Foreign Liabilities 2/	589.8	2706.3	2805.0	2891.8	3.1	6.9	390.3
Government Deposits, of which	3422.7	2964.0	3409.6	3356.5	-1.6	13.2	-1.9
Government contribution to RTP	434.2	382.2	382.2	382.2	0.0	0.0	-12.0
RBV Notes	1607.3	1696.5	1995.5	1346.5	-32.5	-20.6	-16.2
Other Liabilities	1190.3	600.8	602.6	655.8	8.8	9.2	-44.9
TOTAL Liabilities	15300.3	17657.5	18043.5	18140.1	0.5	2.7	18.6

1/ Reserve Bank's foreign currency accounts with residents' commercial banks are included in foreign exchange holdings of the Bank.

2/ Including deposits by the Asian Development Bank and the Commission of the European Communities (CEC)

3/ Currency Outside Banks was revised to comply with the Monetary and Financial Statistics Manual

TABLE A2 : CONDENSED BALANCE SHEET OF COMMERCIAL BANKS IN VANUATU

END OF PERIOD	Aug-09	May-10	Jul-10	Aug-10	%Change		
					1 Month	3 months	12 Months
Domestic currency	917.6	875.3	1159.3	1139.5	-1.7	30.2	24.2
Deposits with RBV	3931.4	4936.3	3892.7	4747.7	22.0	-3.8	20.8
RBV Notes	1607.3	1696.5	1995.5	1346.5	-32.5	-20.6	-16.2
Foreign Assets, of which	29783.7	26996.2	24720.2	24338.8	-1.5	-9.8	-18.3
Claims on non-residents' banks	27411.5	24129.3	21755.1	20987.1	-3.5	-13.0	-23.4
Claims on Private sector	37854.5	40830.6	42150.5	41887.5	-0.6	2.6	10.7
Claims on Government	434.5	686.7	686.7	686.7	0.0	0.0	58.0
Other claims 1/	125.4	112.4	109.2	108.8	-0.3	-3.2	-13.3
Other Assets	3351.8	3766.5	3704.9	2825.9	-23.7	-25.0	-15.7
TOTAL ASSETS	78006.2	79900.6	78418.9	77081.5	-1.7	-3.5	-1.2
Demand Deposits, of which	16375.3	17029.3	16951.5	16987.7	0.2	-0.2	3.7
Foreign currency	9043.8	8703.0	8200.0	7732.7	-5.7	-11.1	-14.5
Savings deposits, of which	4195.1	4573.5	4899.9	4808.9	-1.9	5.1	14.6
Foreign currency	230.5	395.3	466.5	374.1	-19.8	-5.4	62.3
Time deposits, of which	34508.7	31708.5	28656.6	28656.9	0.0	-9.6	-17.0
Foreign Currency	17384.7	13704.3	10709.8	10735.9	0.2	-21.7	-38.2
Foreign Liabilities, of which	7475.6	10512.3	12448.7	12584.1	1.1	19.7	68.3
Non residents Banks	2253.2	3464.4	3119.6	3016.6	-3.3	-12.9	33.9
Government Deposits	782.0	1185.3	851.2	778.8	-8.5	-34.3	-0.4
Credit from RBV	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Liabilities, including shareholders' funds	14669.5	14891.9	14611.0	13265.1	-9.2	-10.9	-9.6
TOTAL LIABILITIES	78006.2	79900.6	78418.9	77081.5	-1.7	-3.5	-1.2

1/ Includes: Claims on other Financial Institutions and Interbank Claims, Claims on Municipalities and Claims on Public Enterprises

TABLE A3 : MONETARY SURVEY: A CONSOLIDATED STATEMENTS OF ACCOUNTS OF THE MONETARY INSTITUTIONS

END OF PERIOD	Aug-09	May-10	Jul-10	Aug-10	%Change		
					1 Month	3 months	12 Months
1. Net Foreign Assets	34,306.1	28,811.1	24,831.0	24,255.8	-2.3	-15.8	-29.3
Monetary Authorities (Net)	11,998.0	12,327.1	12,559.5	12,501.1	-0.5	1.4	4.2
Commercial Banks (Net)	22,308.1	16,484.0	12,271.5	11,754.7	-4.2	-28.7	-47.3
2. Net Domestic Assets	24,414.1	28,378.4	29,855.7	29,722.0	-0.4	4.7	21.7
(a) Domestic Credit	35,478.9	38,869.5	40,147.8	40,013.1	-0.3	2.9	12.8
(i) Net claims on government	(3,150.3)	(2,841.9)	(2,953.4)	(2,829.7)	4.2	0.4	10.2
Monetary Authorities	(2,802.8)	(2,343.3)	(2,788.8)	(2,737.6)	1.8	-16.8	2.3
Commercial Banks	(347.5)	(498.6)	(164.6)	(92.1)	44.0	81.5	73.5
(ii) Claims on Non financial Public enterprises (NFPE)	111.2	99.8	98.5	96.8	-1.8	-3.1	-13.0
(iii) Claims on Private Sector (1)	38,503.7	41,598.9	42,992.1	42,732.9	-0.6	2.7	11.0
(iv) Claims on other financial institutions	0.0	0.0	0.0	1.0	0.0	0.0	0.0
(v) Claims on Municipalities	14.2	12.6	10.6	12.1	13.3		
(b) Other items (net)	(11,064.8)	(10,491.1)	(10,292.1)	(10,291.1)	0.0	-1.9	-7.0
3. Total Assets= Total Money Supply (M2)	58,720.2	57,189.5	54,686.7	54,455.8	-0.4	-4.8	-7.3
(a) Money (M1)	20,016.4	20,907.5	21,130.3	20,989.9	-0.7	0.4	4.9
(i) Currency outside Banks	3,641.1	3,878.2	4,178.8	4,002.2	-4.2	3.2	9.9
(ii) Demand deposits	16,375.3	17,029.3	16,951.5	16,987.7	0.2	-0.2	3.7
(b) Quasi-money	38,703.8	36,281.9	33,556.5	33,465.9	-0.3	-7.8	-13.5
(i) Saving Deposits	4,195.1	4,573.5	4,899.9	4,808.9	-1.9	5.1	14.6
(ii) Time Deposits	34,508.7	31,708.5	28,656.6	28,656.9	0.0	-9.6	-17.0

1) Include RBV staff loans and credit corp

TABLE A4 : MONTHLY CHANGES IN TOTAL MONEY SUPPLY

END OF PERIOD	Aug-09	May-10	Jul-10	Aug-10
1. Net Foreign Assets	109.3	387.7	(2,544.2)	(575.2)
Monetary authorities	(40.9)	206.7	(135.2)	(58.3)
Commercial Banks	150.2	180.9	(2,408.9)	(516.8)
2. Domestic Money creation	1,078.7	(76.8)	1,486.9	(133.8)
(a) Domestic credit	1,142.2	186.6	906.7	(134.8)
Net Claims on Government	175.5	51.4	257.9	123.8
Monetary Authorities (net)	156.0	(137.4)	(239.9)	51.3
Commercial Banks (net)	19.5	188.8	497.8	72.5
Claims on non financial public enterprises	(0.3)	(1.5)	(0.5)	(1.8)
Claims on Private sector	969.4	134.7	654.0	(259.1)
(b) Other Domestic factor	(63.6)	(263.4)	580.2	1.0
3. Money Supply creation (M4)	1,187.9	310.9	(1,057.6)	(231.0)
Money (M1)	207.8	634.5	411.9	(140.4)
Quasi-money	980.1	(323.6)	(1,469.5)	(90.6)

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