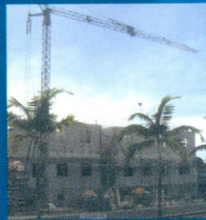


Reserve Bank Vanuatu
Annual Report 2007



OUR VISION

Providing the conditions for Vanuatu to build a strong economy by ensuring confidence and stability in our financial system.

OUR MISSION

- . Establish appropriate monetary conditions for price stability
- . Establish financial conditions and adopt policies that will ensure an adequate level of foreign exchange reserves to meet external obligations
- . Provide proactive and sound advice to the Government
- . Develop an internationally reputable financial system
- . Inspire public confidence in the Reserve Bank
- . Meet the currency needs of the public
- . Disseminate timely and quality information
- . Recruit, develop and retain a professional team dedicated to the pursuit of quality practices
- . Ensure sound banking practices so as to provide protection of depositors

PRINCIPAL OBJECTIVES

- . to regulate the issue, supply, availability and international money exchange.
- . to advise the Government on banking and monetary matters.
- . to promote monetary stability.
- . to promote a sound financial structure.
- . to foster financial conditions conducive to the orderly balanced economic development of Vanuatu.
- . Section 3, Central Bank of Vanuatu Act [CAP 125].

Letter to the Minister

The Honourable Minister of Finance
Government Building
Port Vila

Dear Minister,

Pursuant to Section 42(1) of the Reserve Bank of Vanuatu Act [CAP 125], I have the honour to transmit to you:

- (a) A report of the operations of the Reserve Bank of Vanuatu for the Year 2007; and
- (b) A copy of the Bank's Annual Statement of accounts for 2007 certified by the Auditors.

Yours faithfully,



Odo Tevi

Governor and Chairman of the Board of Directors

Private Mail Bag 062, Port Vila, Vanuatu. Facsimile: (678) 24231 | Telephone : (678) 23333

Email : resrvbnk@rbv.gov.vu. | Website: <http://www.rbv.gov.vu>

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Board of Directors



Mr. Odo Tevi

Governor and The Chairman of the Board.

Governor of the Reserve Bank of Vanuatu since 22 April 2003. Served as the principal economist in the Ministry of Finance and Economic Management (MFEM). Alternate Governor for Vanuatu in the International Monetary Fund. Mr. Tevi has a masters degree in Economics from Sussex University in England. His term will expire on April 2008.



Mr. Geordie Mackenzie-Reur

Member since 27 June 2002. Managing Director, Fiberglass Vanuatu Limited. Managing Director, Pacific Poly tanks Limited. Executive Member of Central School Council. Served as: Principal Agriculture Extension Officer, General Manager, Syndicat Agricol, General Manager, Vanuatu Chamber of Commerce. Mackenzie-Reur has a Masters in Agriculture from the University of Queensland in Australia. His term expired on July 2007.



Mrs. Anniva Tarilongi

Member since 27 June 2002. Deputy Financial Controller, Telecom Vanuatu Limited (TVL). Formerly Administrative Accountant and Funds Accountant, Coopers & Lybrand Chartered Accountant (1991-1993). Has worked as an Accountant/Auditor with KPMG Peat Marwick from 1993-1995. Mrs Tarilongi has a degree in Accounting from the University of New England in Australia, and carries with her a wealth of experience. Her term expired on July 2007.



Mr. Simeon Malachi Athy

Member since 14 June 2004. Director General in the Ministry of Finance and economic Management (MFEM). Served as Director of the Department of Research at the Reserve Bank of Vanuatu. Mr. Athy has a Bachelor of Economics from the University of Papua New Guinea (PNG). His term expired on July 2007

Executive Management



Odo Tevi

Governor



Peter Tari

Deputy Governor



Philip Arubilake

Director of Research and
Statistics Department



Nelson Shem

Director of Corporate
Services Department



Noel Vari

Director of Banking
Supervision Department



Branan Karae

Director of Accounts and
Customer Services Department



Micheal Hililan

Director of Financial
Markets Department

Chairman's Report



It is indeed a great pleasure for me to report another year of Vanuatu's economic success in 2007.

Vanuatu continued to maintain a strong positive growth rate in 2007. It is recorded that the domestic economy has been expanded by about 6.6 percent in 2007 compared with a stronger growth in 2006 by about 7.2 percent. Growth in 2007 was broad-based, driven mainly from the services sector and the construction sectors. Agriculture sector also grew by about 4.1 percent in 2007, mainly due to improvements in copra and coconut oil that were buoyed by high copra prices.

I am pleased to note that the robust growth rate of the world economy in 2006 by 5.4 percent and further growth in 2007 by 4.9 percent has to some extent contributed to our economic success in 2007. The global economic growth has eased in the last quarter of 2007 after a very strong growth in the first half of 2007 particularly due to the US sub prime mortgage crisis. However, Emerging markets still remain the main engine of growth within the global economy. This growth is led by China and India, while Japan, on the other hand, has experienced a slower rate of growth.

In terms of the Bank's monetary policy stance, the Bank has kept its official interest rate, the rediscount rate, unchanged at 6.00 percent. The official interest rate has been left unchanged since March 2006. The Board of Directors of the Bank took a decision to keep the official interest rate at 6.0 percent, due mainly to the comfortable level of reserves held by the Bank, covering about 8 months of imports while on the one hand the Board considered other factors including the increasing rate of inflation. The

inflation rate at end 2007 was about 4.1 percent compared to 1.8 percent in 2006. The Bank's monetary policy stance was further supplemented by the ongoing open market operations of the Bank. Monetary policy in the first half of the year was generally accommodative with the volume of RBV Notes issued in the market being reduced significantly as the Bank undertook a review of the appropriateness of its monetary policy process. However, liquidity conditions became tighter in the second half of the year as the Bank became more aggressive in open market operation.

Exchange rate has been stable over the year; however, Vatu has appreciated substantially against USD due to the strong depreciation of USD against the major trading currencies.

The Reserve Bank of Vanuatu continues to ensure that financial system is sound and stable. Bank supervision and regulation has been ongoing with the Bank's regular on-site and offshore assessments. Domestic banks in 2007 are well capitalized and have recorded an increase of 6.9 percent to Vt69.6million in their total domestic assets from Vt65.1million in 2006. Earnings of banks have continued to show positive growth in 2007. Impaired assets have been on the downward trend in 2007. During the year, Vanuatu experienced two additional entries in the domestic banking sector. The Bank issued two domestic new licensees to Bred (Vanuatu) Limited, a subsidiary of Banque Populaire in France and Credit Corporation (Vanuatu) Ltd, a subsidiary of Credit Corporation (PNG) Limited. The Reserve Bank of Vanuatu has also declined a domestic banking license in 2007.

On the international banks, there has been a new entrant in the market, marking a total of 8 banks. It has been noticed in 2007 that a number of inquiries to establish international banks has generally increased during the year. Bank continues to monitor and ensure that all international banks are sound and to adhere to all relevant policies and legislations.

Other supervisory responsibilities cover the supervision of the Vanuatu National Provident Fund.

The Bank has participated in a number of international meetings in 2007, including the IMF/ World Bank annual meetings. Our participations have continued to strengthen our relationships with other central banks and other international organizations.

I am pleased to note that the human resources capacity building has been ongoing with the help of our neighboring central banks and the international institutions such as the International Monetary Fund, Australian Prudential Regulatory Authority, Reserve Bank of New Zealand and the Reserve Bank of Australia.

The Bank has undergone an independent human resource review by an independent specialist. The review covers the job evaluation and remuneration structure, performance appraisal system and a reality check. This review is part of the process of modernizing the Bank.

In 2007, we have continued to support the Government and other communities in terms of financial assistance and also providing central bank awareness to a number of secondary schools in Vanuatu. The Reserve Bank of Vanuatu made another major contribution of one million vatu to the Vanuatu Chamber of Commerce to assist them in hosting the National Trade Show, promoting local products to the public as well as making exposure to the export markets.

Reserve Bank continues to embark on its new projects, the new Bank building commenced construction on the 12th February 2007 and is expected to complete in early 2008. The Bank has also undergone an improvement in its

communications system by revamping its local server technology hardware and the software and communications medium. The outdated in-house financial accounting software was also replaced by a new corporate software- Epicor.

I am pleased that the Bank has continued to perform satisfactory in 2007 to meet its statutory obligation. The Bank recorded another profitable year and has recorded a net operating profit of Vt266, 217,000. In terms of the Reserve Bank of Vanuatu Act, I am delighted to announce that the Bank will transfer Vt213, 831,000 as dividend to the Government of Vanuatu.

The current macro-economic and political stability will continue to sustain the economic growth in Vanuatu. It is forecasted to grow about 5-6 percent in the medium term, driven mainly from the tourism sector, rising construction activities and increasing aid inflows. Inflation could be expected to moderate from the current year to about 3 percent and international reserves is projected to remain comfortable level. On the downside risks, there is increasing challenge in the price pressures, given the supply constraints of the economy as well as the global price pressures on basic food items and oil.

Last but not the least; I would to extend my sincere gratitude to the Honourable Minister of Finance and Economic Management, Honourable Willie Jimmy Tapangararua for his continuing support towards the Bank and the Reserve Bank Board for their continuous guidance towards the Bank. Last but not the least; I would also like to thank Team RBV for their continuous commitment to ensure that the Bank continues to meet its statutory objectives.



Odo Tevi

**Governor and Chairman
Board of Directors**

Economic Overview

International Economy

Following a robust growth rate of 5.4 percent in 2006, the world economy grew by 4.9 percent in 2007. Growth in the global economy eased off in the final quarter of 2007 after strong growth was registered in the first half of 2007 through to the third quarter. This marked reduction in global growth stems from the global financial markets, and the US sub prime mortgage crisis which has weighed heavily on the momentum of world economic growth.

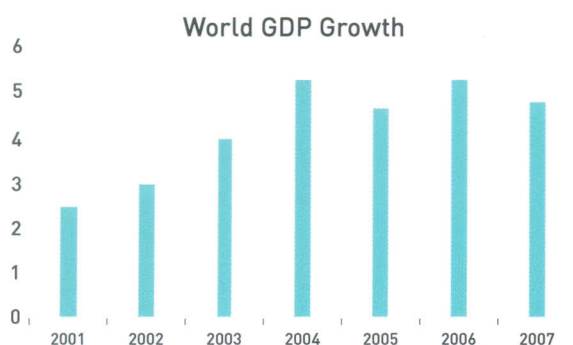
In the United States of America, economic growth has slowed noticeably in the final quarter of the year, and there are indications that the weaknesses seen in the housing market have extended to the other sectors of the US economy. In Europe, growth has moderated in the fourth quarter of 2007 after robust growth in the third quarter. Emerging markets still remain the main engine of growth within the global economy. This growth is led by China and India, while Japan, on the other hand, has experienced a slower rate of growth than previously.

The trading partners of Vanuatu, especially Australia and New Zealand, have continued to remain strong against the economic uncertainty stemming from the US. Rising world commodity prices have supported growth in these countries. In Australia, there are indications that the economy has remained solid in the second half of 2007. December quarter data showed an increase in GDP of 3.9 percent on the previous year.

Developments in the global financial markets have seen a marked depreciation of the US dollar against the other major currencies based on concerns over the strength of the US economy. Overall the US dollar has fallen by 10 per cent in value since the steady decline started in February 2006. The Australian dollar, New Zealand dollar and the Euro have all benefited from the depreciation of the US dollar. The Euro has had the most noted upturn and is at its strongest level since its introduction in 1999.

Interest Rates

In the US, the Fed has been cutting interest rates since August 2007. In the last quarter of 2007, the US Federal Reserve cut interest rates by 50bps. Further rate cuts have been expected in 2008 as the fall out of the sub prime market is expected to cause further reverberations in the US economy. On the other hand, Japan and the euro area have held their policies unchanged in the second half of 2007 while emerging market economies continue to tighten monetary policy to combat inflation.





World Tread

The economic success story for China still continues with China's merchandise trade expansion remaining strong. Office and telecom equipment continued to be the main source of Chinese exports growth. However, it expanded its trade base by making significant developments in exporting clothing, iron and steel. Chinese imports again rose faster than global trade but continued to lag behind export growth.

The real merchandise exports of the United States rose by 10.5 per cent, which was the highest growth rate since 1997 and almost twice as fast as its import growth. Weaker domestic demand in the US, a lower real effective (i.e. trade weighted) dollar exchange rate, and stronger global demand growth contributed to this favourable development.

Asia's real merchandise exports remained the most buoyant of all regions, with imports rising faster than

in the preceding year and faster than world trade but still continuing to lag behind its export growth.

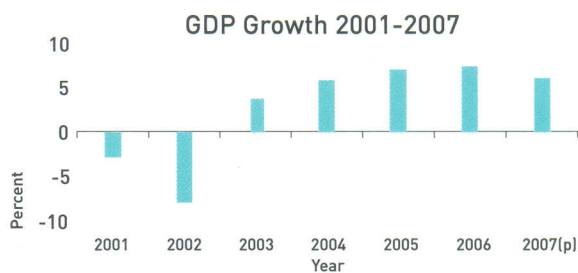
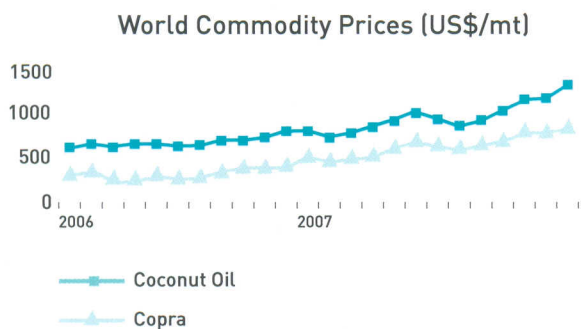
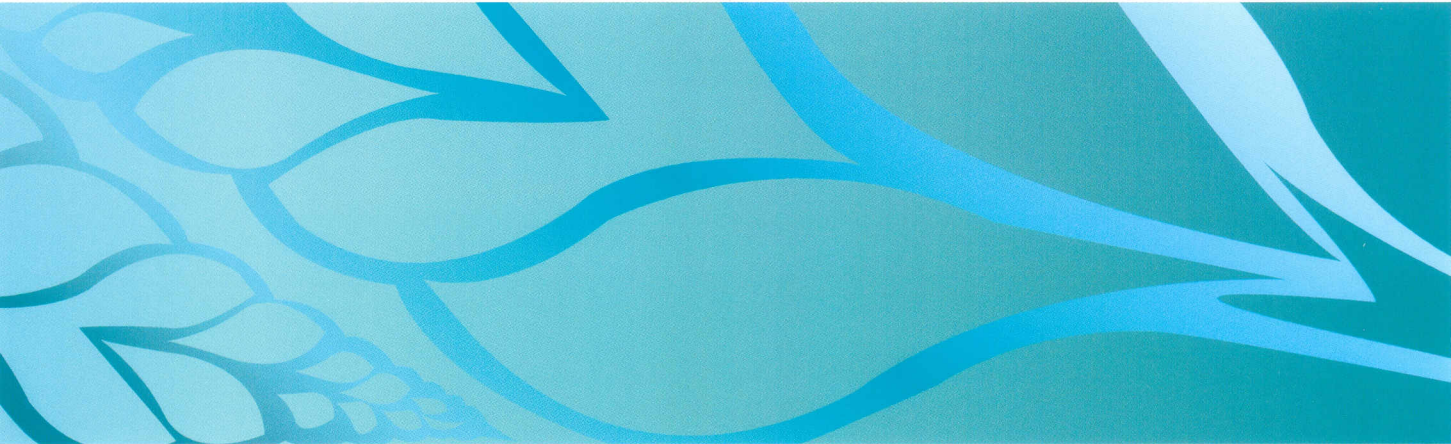
Europe's real merchandise exports recorded their strongest annual growth since 2000, exceeding import growth (estimated at 7 per cent) but continued to lag behind the global rate of trade expansion.

2007 also saw the deadline for the European Partnership Agreements and only Fiji and Papua New Guinea signed up from the Pacific region.

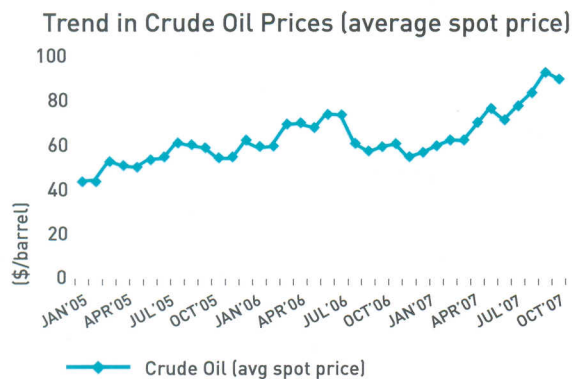
Commodity Prices

Since the middle of 2007, both headline inflation and core inflation have increased for both advanced and emerging market economies. Much of the inflation pressure has been associated with sharp increases in commodity prices while in neighboring countries like Australia and New Zealand; inflation pressures have been associated with long years of robust growth.

Key Interest Rates (per cent, end of period)						
	US Fed Funds Rate	Euro Refi Rate	Australian Cash Rate	Bank of Japan	New Zealand Cash Rate	Vanuatu Rediscount Rate
2006 Q1	4.75	2.50	5.50	0.25	7.25	6.25
Q2	5.25	2.75	5.75	0.25	7.25	6.00
Q3	5.25	3.00	6.00	0.25	7.25	6.00
Q4	5.25	3.50	6.25	0.25	7.25	6.00
2007 Q1	5.25	3.75	6.25	0.5	7.50	6.00
Q2	5.25	4.00	6.25	0.5	8.00	6.00
Q3	4.75	4.00	6.75	0.5	8.25	6.00
Q4	4.25	4.00	6.75	0.5	8.25	6.00



Source: Ministry of Finance and Economic Management



World commodity prices relevant to Vanuatu's main export commodities have increased to higher levels in 2007. Similarly, world prices for copra and coconut oil continue to trend upward, they have increased sharply in the second half of 2007. Likewise, world prices for cocoa have shown an increasing trend while the prices for beef have stabilized above US 25c/kg.

Domestic Economy

World crude oil prices have increased to high levels (see chart above). Oil prices remained high in the final quarter of 2007 driven by much uncertainty

in both the political and financial fronts. The fourth quarter saw the price of Brent Crude increasing above \$90 a barrel and this shows no sign of let-up in the near term.

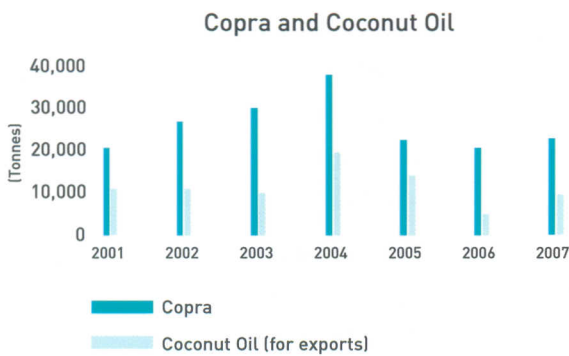
Vanuatu's economy has continued to maintain a strong positive growth rate in 2007. According estimates by the Ministry of Finance and Economic Management (MFEM), the domestic economy has expanded by around 6.6 percent in 2007. This follows on from a 7.2 percent growth in 2006.

Growth in 2007 was broad-based, driven primarily by the services sector and the construction sub-sector whereas few other sub-sectors of the economy have also showed improvement in performance. The services sector sprung from growths in wholesales and retail trade, finance and insurance, real estates and other services as well as the increase in visitor arrivals. The Industry sector grew at an estimated 5.0 percent over the period supported by various on-going construction projects.

The Agriculture sector grew at an estimated 4.1 percent in 2007 mainly due to improvements in copra and coconut oil sector which were buoyed by high copra prices. The volume of copra output has increased by 13 percent from of the preceding year



to 21,644 tons, while coconut oil exports increased by 98 percent to a total of 7,336 tons in 2007 as production increased towards the second part of the year, after the coconut oil mill in Santo (COPV Ltd) became operational by a new owner, CL Agencies, in May 2007.

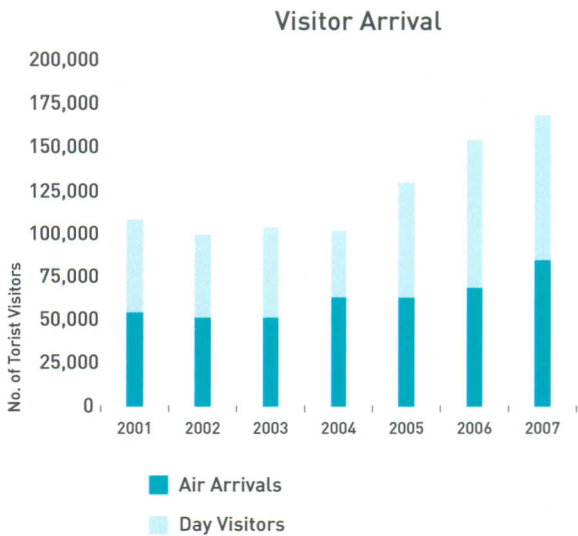


Source: National Statistics Office, VCMB

The volume of cocoa production fell by 27 percent; however production and exports improved towards the third quarter of the year reflecting seasonal harvesting patterns. Other commodities such as kava and beef also showed declines in production, however the regional export markets continues to remain competitive. Beef production in 2007 was some 15 percent lower in volume compared to 2006.

The services sector is estimated to have grown by 7.3 percent in 2007. Improvement in this sector was driven by increases in visitor arrivals during the year which grew by 8.4 percent from 154,101 to 167,082. Air arrivals increased by 19.3 percent as the country received more visitors during the third quarter of the year supported by extended incoming

flights from Brisbane to Pekoa International airport in Santo, code-sharing flight agreements between Air Vanuatu and Air New Zealand, and low cost airline fares by Pacific Blue. Visitors from Vanuatu's major tourism market, Australia, increased by 17 percent on the 2006 level. Due to increases in the number of P&O Cruise-ship calls to Port Vila port, the country received 85,737 day visitors in 2007.



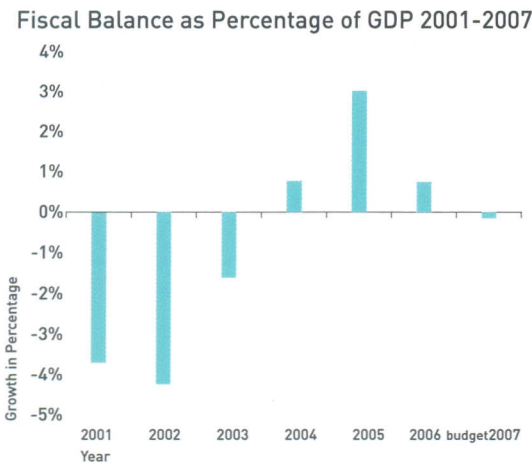
Source: National Statistics Office

The year-end rate of inflation has increased from 1.8 percent in 2006 to 4.1 percent in 2007. This increase has been attributed to increases in import duties on various imported alcohol beverages and food items in January. The increase in inflation was seen in higher prices for food and electricity. Other items such as prices of housing supplies and clothing and footwear noted minimal increases in prices reflecting the shift



in Vanuatu's imports pattern towards Asian countries for these particular items which are relatively cheap. Core or underlying inflation is estimated to have increased by 2.5 percent over the year.

Government finances from 2004 onwards showed large surpluses with growth in expenditure being more than matched by strong growth in revenue. However, the fiscal position for 2007 is somewhat weaker, and preliminary figures suggest that there will be a small deficit this year as projected expenditure is higher than projected growth in revenue.



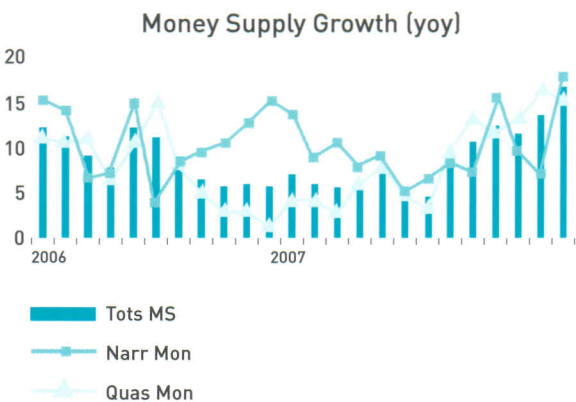
The total recurrent revenue for the first half of 2007 was VT5,169.1 million, approximately 49 per cent of the budgeted revenue for the fiscal year and 2 per cent than the same period last year. This improvement in revenue was driven by increased VAT collections due to greater compliance and enforcement measures. This improvement in performance is expected to have continued in the second half of 2007 suggesting that government revenue may be slightly higher than forecast.

A large amount of supplementary occurred in the first half of 2007 which will pressure on the budget deficit. The 2007 budget forecast a deficit of VT39.2 million, however preliminary figures suggest this may be higher.

Monetary conditions improved substantially during 2007. The levels of both monetary and credit aggregates showed hefty increases against the 2006 levels. Total money supply (M2) expanded by 16 percent to VT52,908 million during 2007 as narrow money and quasi money grew by 17 percent and 15 percent, respectively.

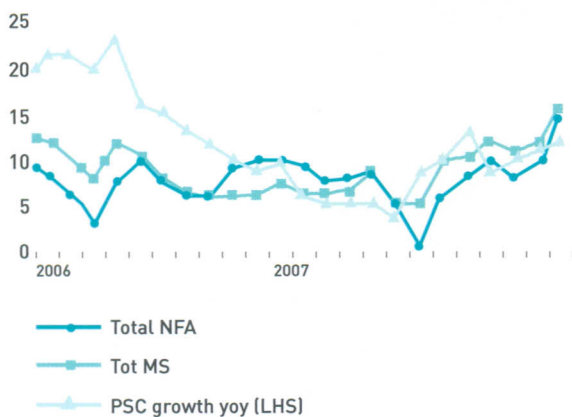
Amongst the determinants of money supply growth, total net foreign assets (NFA) expanded by 15 percent to VT37,497 million at the end of 2007. This expansion was driven by the growth in the NFA position of the monetary authorities and of commercial banks by 6.0 percent and 19.6 percent, respectively.

Domestic credit expanded further by 10.5 percent





Counterparts of Money Supply Growth (YoY)



at the end of 2007, mainly driven by an increase in credit extended to the private sector and municipalities. Net credit to the Government and credit to non financial public enterprises on the other hand noted decline in credit.

Private sector credit growth has accelerated to 12.3 percent in 2007 from 9.6 percent in 2006. Increases in credit to the fisheries sector, mining and quarrying, manufacturing, transport, public utilities, professional & other services, housing & land loans and other personal loans, attributed the said growth. Loans to other economic sectors have shown declines in credit primarily due to repayments of loans. Housing & land loans accounted for the largest share of total loans with 33%, other personal loans followed with 23%, the third and fourth largest share of loans were attained by the construction and tourism sector with 9% and 7%, respectively.

Commercial bank's interest rates on average have shown some reductions in the final quarter of 2007. This has been due to competition in the market with

the addition of a new bank which will start operation in early 2008. Nevertheless, the spread between the weighted lending rates and weighted deposit interest rates has widened in 2007.

Developments on the country's international accounts have seen an increase in foreign exchange (less IMF positions) by 7.0 percent from VT10,572 million at the end of 2006 to VT11,363 million at end 2007. Gross official reserves have risen to VT11,939 million (USD121 Million) at the close of the year. This increase was driven by significant tourism earnings and inflows of grants from donor partners reflecting extensive bilateral agreements. Foreign Direct Investments and Real Estates via acquisition

Interest Rates



of non financial assets all expanded and contributed significantly to the growth of foreign exchange.

The current account deficit expanded in 2007 due to high import bills partly contributed to by the appreciation of the Australian dollar. In addition, foreign direct investment reinvested earnings and distributed profit abroad noted a momentous increase. All this could not offset the 18 percent rise in tourism earnings in 2007. Proceeds of exports

have always been volatile and dependent on a few commodities hence export earnings were lower in 2007.



International Investment Position (MVT)

	2005	2006	2007
Net Position	5836	5890	6029
Assets	57361	63333	57300
Direct Investment	1492	1573	1636
Portfolio Investment	1568	1582	1723
Other Investment	46705	48983	42002
Reserves	7596	11195	11939
Liabilities	63197	69223	63329
Direct Investment	16694	21725	24993
Portfolio Investment	60	1	1
Other Investment	46443	47497	38335

The capital and financial account recorded another surplus, significant enough to finance the current account deficit of 2007. Foreign direct investment in Vanuatu has continued to expand in terms of existing equities and fresh investments reflecting a favorable investment environment.

The net International Investment Position of Vanuatu stood at VT -6029 million at end December 2007. This has increased Vanuatu's net indebtedness position by 2.3 percent, driven by large reduction in other liabilities rather than foreign direct investment. Assets were also reduced.

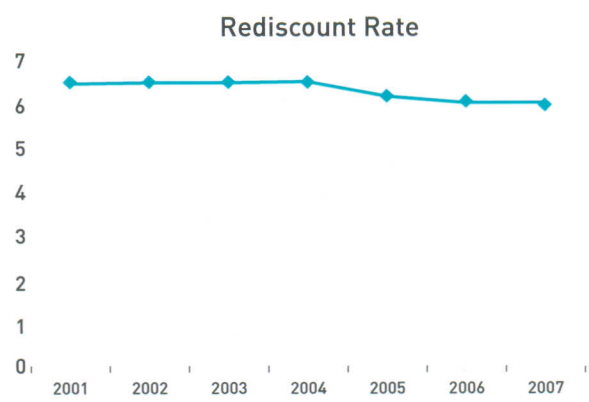
Monetary Policy Formulation

The Monetary Policy Formulation function of the Reserve Bank of Vanuatu is carried out by the Department of Research and Statistics. The Department comprises three units, namely the Economic Analysis Unit, the Statistics Unit, and the Library.

Inside the Economic Analysis Unit, there are four sections namely the Real Sector, Government Finance, Money and Banking, and External Sector. The Department continues to monitor developments in international and domestic macro economy, in particular the macroeconomic variables that have an influence on the policy settings of the Bank, and provides advice on monetary policy to the Bank's Monetary Policy Committee (MPC) through the Policy Coordination Committee (PCC) which comprises mostly technical staff in the Department of Research and Statistics and the Director of Financial Markets Department.

The Statistics Unit is responsible for the entire data requirement for the Department and the Department's data base.

One of the primary objectives of the Reserve Bank of Vanuatu is to promote monetary stability. This objective has an internal aspect as well as an external aspect. The internal aspect of price stability requires the maintenance of low and stable inflation. The Bank interprets this to mean inflation measured by the annual change in the Consumer Price Index (CPI) between 0 – 4 percent. Four percent is considered the maximum comfortable threshold. At the end of 2007, inflation rose to 4.1 percent.



The external aspect of the price stability objective is to maintain an adequate level of official international reserves to meet the country's external obligations. The Bank targets a level of official international reserves that is equivalent to at least 6 months of import cover. However, the Bank is comfortable with a level of reserves that is equivalent to at least 4.0 months of import cover. During 2007, the object of adequate reserves was achieved.

Throughout 2007, the Bank has kept its official interest rate, the rediscount rate, unchanged at 6.00 percent. The official interest rate has been left unchanged since March 2006. During May 2007, the Board of Directors of the Bank took a decision to keep the official interest rate at 6.0 percent at its meeting held at the USP sub center in Luganville, Santo. While the official interest rate has remained unchanged; the Bank continues to adjust monetary conditions through Open Market Operations.

Monetary Policy in the first half of the year was generally accommodative with the volume of RBV Notes issued in the Market being reduced significantly as the Bank undertook a review of the

Monetary Policy Implementation

Since its inception in 2006, the Financial Markets Department (FMD) took over most of the functions of monetary policy implementation which were previously shared between the Research and Statistics Department and the Accounts and Customer Services Department. These functions include reserve management, exchange rates setting, liquidity management and forecasting and money market operations. The primary aim of these functions is to create appropriate monetary conditions necessary for price stability.

The FMD's Office of the Director oversees the overall implementation process while daily operations are manned by the Department's Domestic (DMU) and External Markets Units (EMU).

Given the importance and high risk nature of these responsibilities, these daily tasks are conducted in line with the following guiding documents; the RBV Board approved Investment Guideline, the Foreign Exchange Dealing Manual, the Open Market Operations Manual and the Open Market Operations Procedures Manual. Furthermore, policy settings and other important operational decisions are normally made by the Bank's Monetary Policy and the Investment Committees.

The Department's 2007 Business Plan outlined the Department's core activities for the year with expected outputs geared towards the four broader mission objectives of the Bank which include; (a) establishing monetary conditions for price stability, (b) establishing financial conditions and adopt policies that will ensure adequate level of reserves to meet external obligations, (c) disseminating

timely and quality information, and (d) recruiting, developing and retaining a professional human resource team dedicated to the pursuit of quality practices.

In order to determine the progress made by the Department in achieving its key targets for the year, a number of outputs and performance indicators have been identified and imputed into the Business Plan. These expected outcomes and performance indicators are regularly reviewed and reported to the management and the Board of Directors of the Reserve Bank.

Despite the Department's effort in developing and maintaining a skilled and qualified workforce, it went down by one after the resignation of a staff member during the year. Consequently the number of staff reduced to five out of a total of 8 positions in the Department. The resultant gap was temporarily filled through mobilisation of FMD's personnel.

The Bank continues to rely largely on open market-type operations (OMO) for policy intervention, using RBV notes as its main instrument. Additionally, a statutory reserve requirement of ten percent and a liquid asset ratio of eight percent were continued to be imposed on the commercial banks. Other standby instruments which the Bank can utilize through its window of last resort operations to fund banks' overnight shortfalls include the repurchase and re-discount facilities. However, these were hardly used during 2007 due to commercial banks' holdings of large excess reserves.

The Bank's past open market operations were aimed at achieving an overall excess reserves level of VT

500 million. However, the prevailing high banking system liquidity which persisted through to 2007 from mid 2006 foreign currency inflows called for an immediate review of the Bank's monetary policy operations. The review was deemed eminent also because despite of the high excess reserves, private sector credit growth was quite minimal and the Government's net position with the Bank was quite comfortable and thus the Bank did not foresee any major risks for price hikes from domestic demand pressures. Thus, the exercise was initiated in early months of 2007 and culminated by end of May. Subsequent to this review, the excess targeted level was revised upward to VT1,200 million while the official cash rate remained unchanged at 6 percent. Also during this exercise, the RBV cut down on the volume of its OMOs causing a large built up of excess reserves, hitting close to VT3,200 million.

The OMOs conducted during the subsequent months of the year after the review were aimed at the revised target and the Bank was successful in achieving it by year end. In line with these domestic market developments, the OMO Guideline was revised and a new OMO Procedures Manual was also developed and approved in September, 2007. By the December, 2007, the Bank started conducting its OMO on a weekly basis, purposely to better manage the banking system liquidity and to activate the domestic securities market.

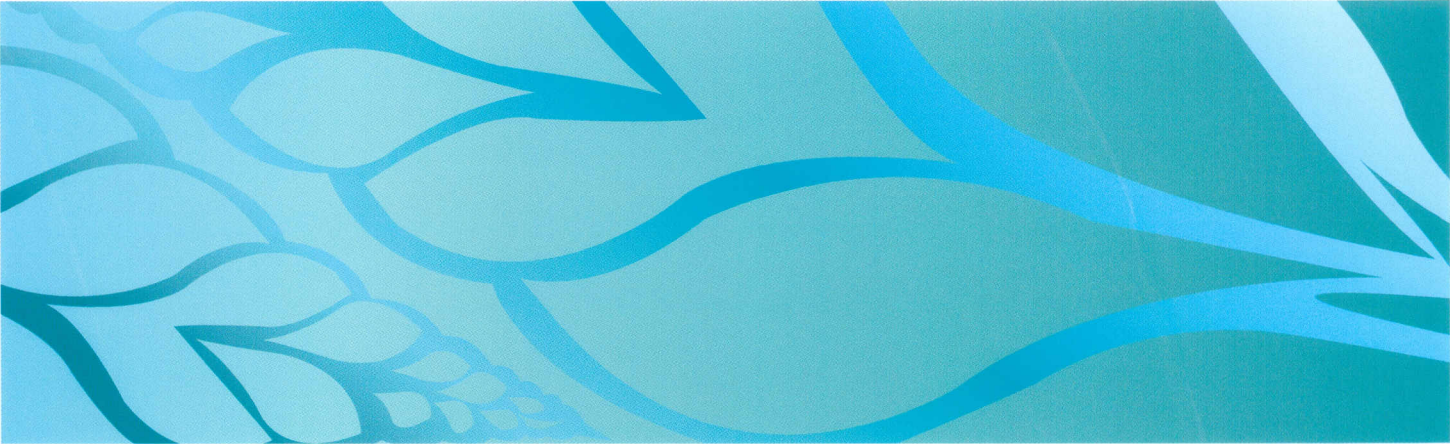
Despite of the Bank's OMO efforts to contain the inflation level below the 4% benchmark, unfortunately, the 2007 annual inflation figure hiked up to 4.10 percent from 1.8 percent in the previous

year. The inflation rise was largely contributed by the increases in the import tariffs on certain import items to cater for the rising government expenditure pressures, thus, demonstrating the import driven nature of the local economy and the limitations of monetary policy in under a pegged exchange rate system.

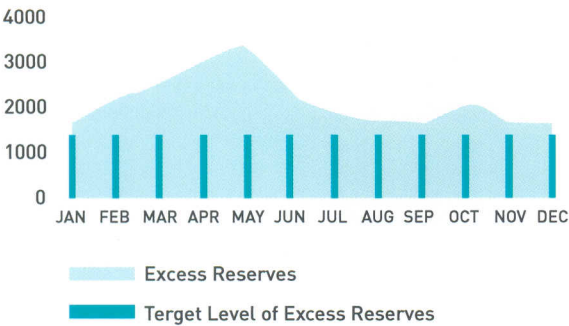
On the external front, the monetary authorities' stance on the exchange rate policy remained unchanged except of a slight adjustment in the basket of currencies which the Vatu is pegged to. However, the major development in this sector was related to the strong depreciation the USD against the major trading currencies, thus causing the Vatu currency also to strengthen against the USD. The depreciation was attributed by the consecutive US Fed fund rate slashes during the year by the Federal Reserve Bank of New York as a counteraction to the expected slow down in US economy caused by the housing market credit crunch.

Open Market Operation (OMO)

Open market operations are conducted on a fortnightly basis through issue of RBV securities (RBV notes) until December when the Bank regularised its OMO into weekly issues. Under this new arrangement, the level of issue is set by the Domestic Market Unite based on the short-term liquidity projections whereas previously, the volume of open market operation was set by the Monetary Policy Committee (MPC). The policy target for open market operations is the volume of banks' excess reserve



Actual vs Target Excess Reserves in 2007



Operations in the Market for
Reserve Bank of Vanuatu Securities: 2007
(VT Million)

	2005	2006	2007
Number of OMO	25	25	27
Flotation	5915	9080	10065
Tenders	9440	11304	20420
Allotments	5205	7057	10065
Outstanding	590	1860	1600

level. In 2007 the desired target level was increased to VT1,200 million basically due to improved economic activities that increased the demand for bank liquidity.

The gap between the actual excess reserves over the target level (depicted in the graph below) significantly dropped towards the second half of 2007 as RBV increased the volume of OMO.

Consequently, the Reserve Bank’s money market operations rose to high levels. An elevated level

of sterilization undertaken by the Reserve Bank is depicted in the table below. During 2007, a total of 27 open market operations were conducted, up from 25 in 2006 and 2005. However, flotation and tenders rose over the level of 2006 by 10.85% and 80.64% respectively.

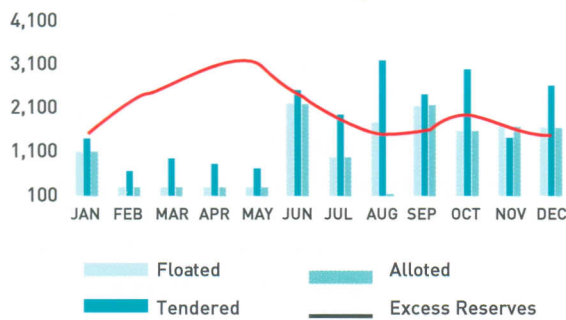
At the end of 2007 outstanding RBV notes amounted to VT1,600 million, a decrease of 14 percent from the 2006 level. The Bank also limited the maturity terms of the notes to the shorter period of 14-day, 28-day, 63-day and 91-day over 2007 to optimise the impact of sterilization without jeopardising the respective cost structure.

Total cost for open market operation over 2007 was recorded at VT59.7 million - or 6.56 percent of the Bank’s total cost in the budget - compared to VT49.1 million in 2006. That increase reflects the active posture that the Bank has pursued in its operations in the money markets.

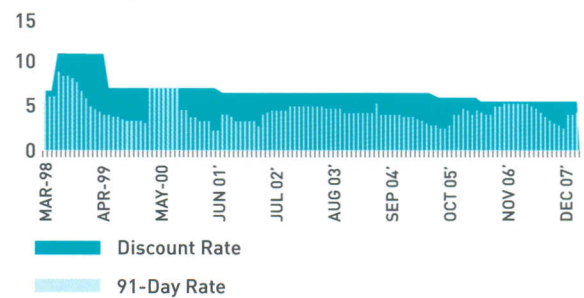
In 2007, RBV raised the volume of its open market operations by 10.85% to VT10,065 million from VT9,080 million in 2006 in response to the rapid surge in the banking system liquidity from foreign inflows observed since mid-2006. Following the Bank request, commercial banks eventually raise their country exposure to absorb the excess liquidity via the Reserve Bank of Vanuatu securities.

The commercial banks have been the primary participants of the RBV notes market and their involvement continued to be active and supportive despite of minor liquidity shortfalls experienced during the year.

Activities in OMO during 2007 (MVT)



Policy and Market Interest Rates



Liquidity and Interest Rates

In spite of the high volume of liquidity experienced during 2007 the RBV notes 91-day yield remained high and margins converged upwards towards the Bank's official Discount Rate at the beginning and the end of 2007.

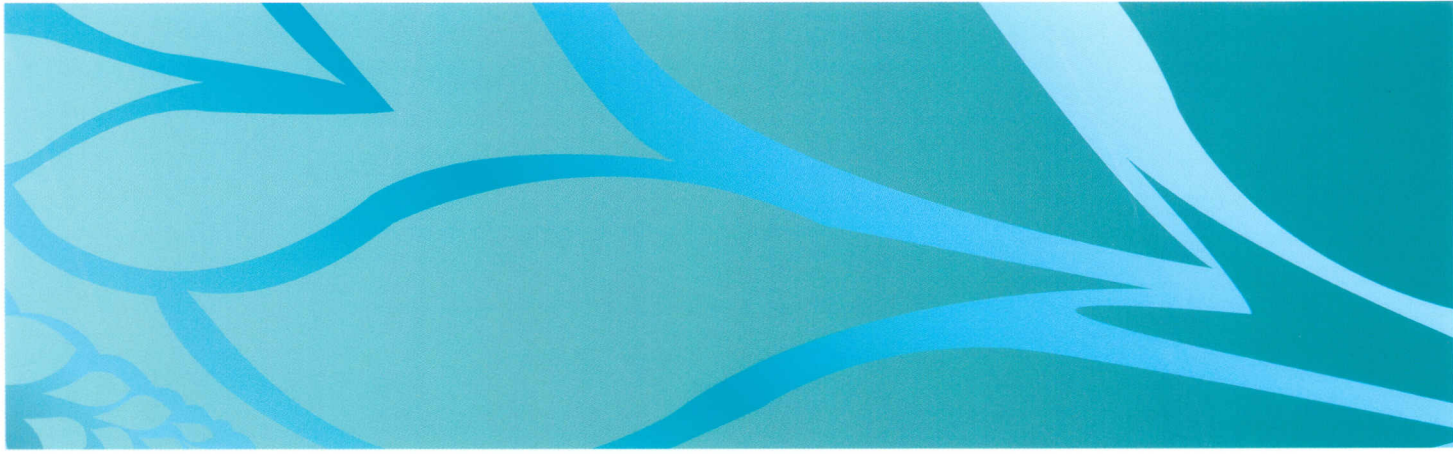
The weighted average yield (WAY) on all RBV securities experienced upward pressure towards the end of 2006 and beginning of 2007 and again at the end of 2007. However, liquidity excesses in the banking system pushed commercial banks to cut down customer deposit rates in order to minimize interest expenditure.

The excess in liquidity began to ease from mid to the end of 2007. The yield of the 91-days RBV security was recorded at 5.08% in the first issue of 2007, and stood at 4.25% during the last issue of 2007 after reaching a low of 2.5% in September 2007.

Liquidity and Interest Rates



The rise in the level of interest rates coupled with the large volume of the OMOs culminated in higher interest costs to the Reserve Bank (noted earlier). The cost of the OMO has been increasing quite substantially since 2004.



Inter Bank Market

Due to high level of excess liquidity in the banking system, there was no inter bank market exercise in 2007.

Reserve Management and Financial Markets Developments

The housing market credit crunch in the United States causing global market to turn sour in the latter part of the year, thus, sending off subsequent market shock waves and uncertainties which loomed the international financial markets for the rest of the year. This had brought about much difficult and challenging times for the international financial market in terms of investment decisions and risks management leading to huge amounts of debt write offs and scaling down of resources including personnel.

These international market developments have called for the Bank to be more vigilant in its reserve management role. Thus, efforts made during the year in this area focussed on the maintenance of the value and safety of the foreign reserves that allows for capital preservation and growth.

The principle of prudential management stands paramount to the daily management of these foreign reserves. Thus, the EMU personnel's conducts are continually guided by the norms and risks benchmarks as stipulated in the Bank's Investment Guideline and the Foreign Exchange Dealing Manual. Any deviations from the stated benchmarks plus other changes made relating to reserve management

are normally approved by the Bank's Investment Committee which oversees the overall function of reserve management in the Bank. Such deviations approved or decisions made are normally carried out in line with the aim of safeguarding capital and minimising risk exposures in the wake of unexpected market developments.

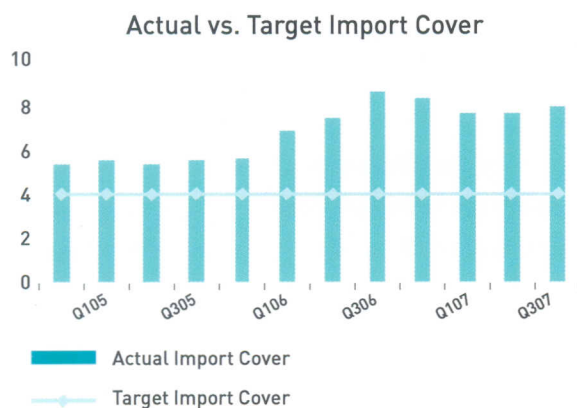
In 2007, a number of major initiatives were undertaken. Firstly, in line with the recommendation from an IMF consultant's report in 2005, the Bank started implementing the new currency composition in its investments in January, 2007. Accordingly, this change was necessary in standardising the then currency composition with the international practice while at the same time minimising large market risk exposures and thus, allowing for capital preservation of the country's foreign reserves. Also, in July 2007, a review of the trade weighted.

Index was completed and a new index was formulated to align the Vatu currency with the world's major currencies given the market developments.

Thirdly, but not the least, FMD had initiated and successfully completed the transfer of investment funds from one of the fund managers to the Bank for International Settlements (BIS) in mid 2007. The motives behind the move included the lower fund manager's fee offered plus the fact that BIS investments were deemed to be more secure.

The high net inflows of foreign exchange during 2007 has contributed to the high level of capital growth and led to achieving the Bank's Strategic Plan's intended outcome of maintaining sufficient

foreign exchange reserves to meet Vanuatu's external obligations and to support the pegged exchange rate. Thus, total reserves (excluding IMF holdings) increased from USD 99.8 million in December ending, 2006 to USD 114.8 million at the end of 2007, positioning the total reserves at 8.10 months of import cover, against a minimum floor of 4 months set by the Bank.

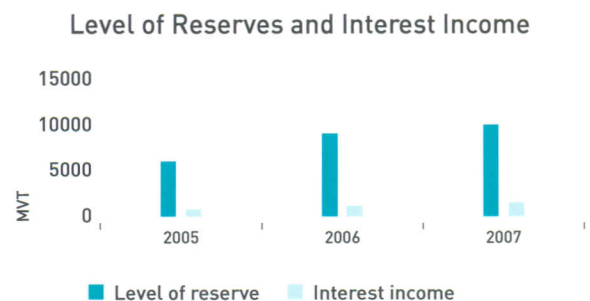


Out of the total investible reserves, 60 percent was managed in house, most of which were held in over night and short term deposits with the foreign counterparty commercial banks, while the remaining 40 percent was outsourced to external fund managers. This ratio stood at 56:44 respectively in the previous year.

Interest income from external assets also improved significantly by 64.7% to VT736.5 million in 2007 compared to VT447.3 million in 2006. This remarkable improvement was due to the increase in the volume of reserves coupled with the high world

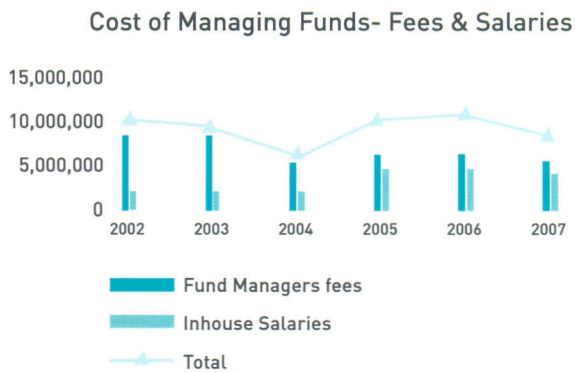
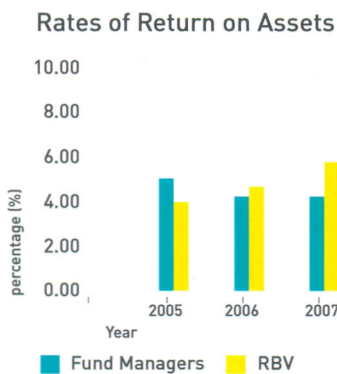
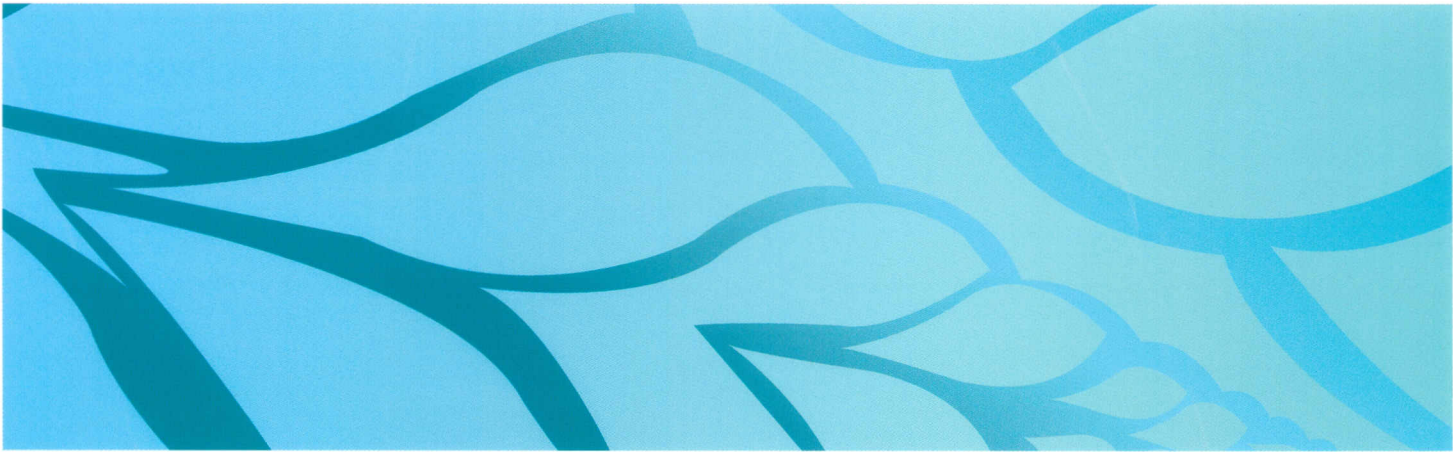
interest rates. Rates of return on external assets continued to be high in 2007 particularly from assets managed in house by the Reserve Bank.

The Reserve Bank of Vanuatu continues to maintain a good working relationship with its counterparty banks and the Bank for International Settlements (BIS). The Bank continues to benefit from proactive product management, training and advice from the BIS.



Offshore Fund Managers fees have steadily increased over the years as the reserves accumulate. However, in 2007, a drop of 26% was experienced due mainly to the better rate offered by the BIS as shown on the graph below. Hence, cost cutting being one of the reasons for changing fund managers, had eventually been realised.

A key aspect of exchange rate policies of the Reserve Bank is to ensure a stable exchange rate. As the Vatu is a pegged currency, its nominal movement is determined largely in the international financial and currency markets. The Vatu appreciated sharply



against the US dollar (USD) during the year and broadly against the Yen and the New Zealand dollar (NZD) but depreciated against the Australian dollar (AUD), the Euro and the Pound Sterling (GBP).

In the international market, the USD depreciated against major currencies, especially European currencies in nominal terms during 2007 although it remained stable in trade-weighted terms. Nominal depreciations were registered against the Euro, GBP, the Swiss Franc but it strengthened against the Yen and Canadian dollar.

The Federal Reserve Bank reduced the fed fund rate sharply by a surprise 50 basis point down to 4.75 percent at the end of September in an effort to curb the US credit meltdown infiltrating into the wider financial market.

The credit crisis, characterized by massive fallout in low quality credit across the United States banking sector, started in late 2006 through 2007 and by August it eventually leaked into the American and the Global financial system – pressurising the Fed for more cut in the USD rate. As a result, the USD found itself weakening against most global currency such as the Euro, the AUD, the NZD and the GBP. In effect, the Vatu significantly appreciated against the USD by the end of the year.

The effect of movement of exchange rates is reflected in the Bank’s revaluation reserve account which recorded substantial losses in 2007. Persistent weak USD exchange rates continue to be a concern in this regard. By December end, 2007, the Vatu exchange rate for the USD stood at its strongest at 98.86.

Financial System Supervision

One of the main functions of the Reserve Bank of Vanuatu is to regulate banks. Under the Financial Institutions Act, part of that responsibility extends to the licensing of Financial Institutions. These functions are performed by the Bank Supervision Department through assessing new applications and making recommendations, recommendations for revocation of license, the monitoring and assessment of the established banks' performances based on collection of information, the conduct of both off-site analysis and on-site reviews, prudential consultations as well as ad hoc meetings with banks' senior managements. These consultations also extend to tripartite meetings between the Department, the banks and their respective external auditors.

The Bank Supervision Department continues to conduct its supervisory functions under the Financial Institutions Act no. 2 of 1999 and the International Banking Act no. 4 of 2002. In addition, there are 11 prudential guidelines that are applicable to domestic commercial banks while 12 are applicable to offshore banks.

During the year, the Department reviewed one of the prudential guidelines, while it continues consultation with the industry for two more new ones; the Operational Risk Management Policy and the Disclosures of Interest Rates and Fees and Charges by Financial Institutions Policy. Both should be finalized for implementation in 2008. The Department continues to comprehensively supervise the Vanuatu National Provident Fund.

During the year, the Department's onsite visits focused mainly on Anti-Money Laundering Reviews.

The onsite reviews were done on all domestic banks and offshore banks, while Operational Review was done on VNPF.

Domestic banks supervised by the Reserve Bank in 2007 were; ANZ (Vanuatu) Limited, Westpac banking Corporation, National Bank of Vanuatu and European Bank Limited.

The international banks supervised by the Reserve Bank in 2007 include United Investment Bank, Vianka Bank Limited, Garrison Bank Limited, Nautilus International Bank Limited, Fubon Bank (Vanuatu) Limited, LMM & Cie Banquier Prives Limited and United Investment Bank Limited.

The individual bank's and the industry's offsite analysis are based on the various data submitted to the Bank on a monthly, quarterly and half yearly basis, while the onsite visits to banks focused on specific areas of risks, which includes credit risks, operational risks and Anti-Money Laundering Risks. In 2007, the Department focused its on-site visit on the Anti-Money Laundering risks of banks.

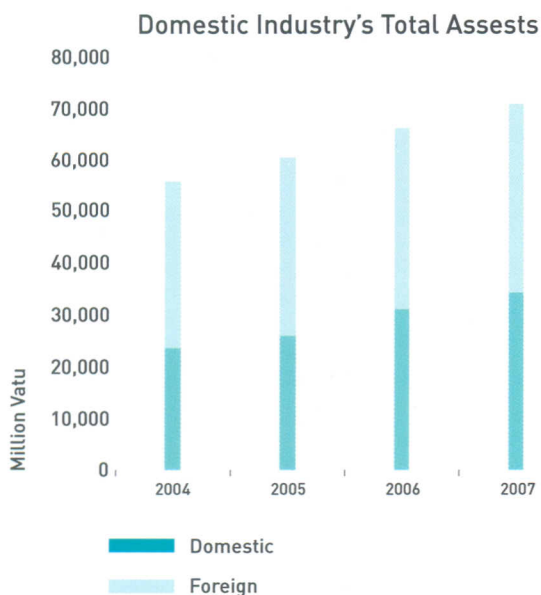
Domestic Banks

During the year, the Bank issued two new licenses; one to a new bank operating under the name BRED (Vanuatu) Limited, a subsidiary of Group BRED Banque Populaire, while the other license was issued to a Credit Institution operating under the name Credit Corporation (Vanuatu) Ltd, a subsidiary of Credit Corporation (PNG) Ltd. The Bank also declined an application for a new domestic bank.



Balance Sheet

This report will cover mainly the financial performance of the four existing domestic banks, while full details of the two newly established financial institutions will be covered in the 2008 annual report. This is due to the fact that in 2007, the two new institutions were still establishing their presence here in Vanuatu.



The domestic banking industry recorded a 6.9 percent increase in total assets over the year ending December 2007 to Vt69.6 billion (Dec-06: Vt65.1 billion). The annual increase was mainly attributable to growth in domestic assets by 8.7 percent to Vt32.3 billion (Dec-06: Vt29.7 billion) and is driven mainly by the increase in private sector lending by 11.8

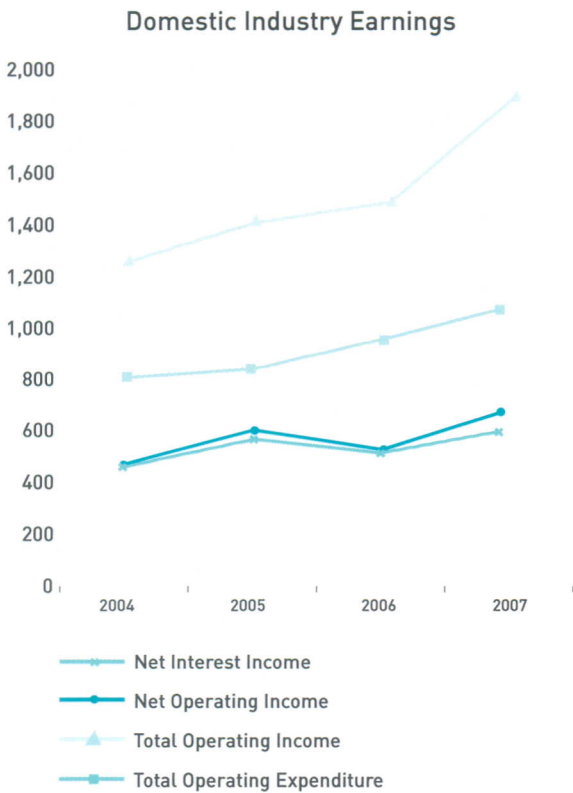
percent to Vt22.8 billion (Dec-06: Vt20.4 billion). Foreign assets also grew by 5.4 percent to Vt37.4 billion (Dec-06: Vt35.4 billion) reflecting mainly growth in balances due from banks and financial institutions outside Vanuatu by 6.0 percent to Vt36.4 billion (Dec-06: Vt34.3 billion).

On the liability side (excluding capital), total liabilities increased by 8.3 percent to Vt62.9 billion (Dec-06: Vt58.1 billion). The increase was mainly attributable to growth in domestic liabilities by 15.0 percent to Vt51.3 billion (Dec-06: Vt44.6 billion). This reflects mainly growth in both Vatu and Foreign Currency deposits with banks by 19.6 percent and 13.0 percent to Vt22.8 billion (Dec-06: Vt19.1 billion) and Vt26.8 billion (Dec-06: Vt23.8 billion) respectively.

Earnings

Earnings of the banking industry over the year ending December 2007 shows further positive growth. Total net operating income recorded over the year was Vt690.2 million. This is an annual increase of 25.3 percent from previous year (Dec-06: Vt550.8 million). The increase was mainly attributable to growth in total operating income by 18.4 percent to Vt1.8 billion (Dec-06: Vt1.5 billion) reflecting mainly growth in non-interest income by 41.7 percent to Vt653.1 million (Dec-06: Vt460.9 million). Interest income of domestic banks also grew slightly over the year by 8.2 percent to Vt1.1 billion (Dec-06: Vt1.0 billion). During the year, total operating expenditure of banks increased by 14.6 percent to Vt1.1 billion (Dec-06: Vt940.0 million).

With the positive growth recorded over the year, domestic banks "Return on Assets" (ROA) increased from 0.9 percent (Dec-06) to 1.0 percent (Dec-07) and "Return on Equity" (ROE) increased from 8.1 percent (Dec-06) to 11.1 percent (Dec-07).



Capital Adequacy

The domestic banking industry is well capitalized despite recording a decline in its capital adequacy ratio from 33.5 percent (Dec-06) to 29.8 percent (Dec-07) and tier 1 capital ratio from 32.3 (Dec-06) percent to 28.6 percent (Dec-07) over the year. During the year, however the industry's capital base

increased by 3.9 percent to Vt5.7 billion (Dec-06, Vt5.5 billion). The increase reflects mainly growth in disclosed reserves and retained earnings by 4.0 percent to Vt4.6 billion (Dec-06: Vt4.4 billion). Total risk assets also increased by 16.9 percent to Vt19.1 billion (Dec-06: Vt16.3 billion), thereby reducing both ratios (capital adequacy & Tier 1 ratios).

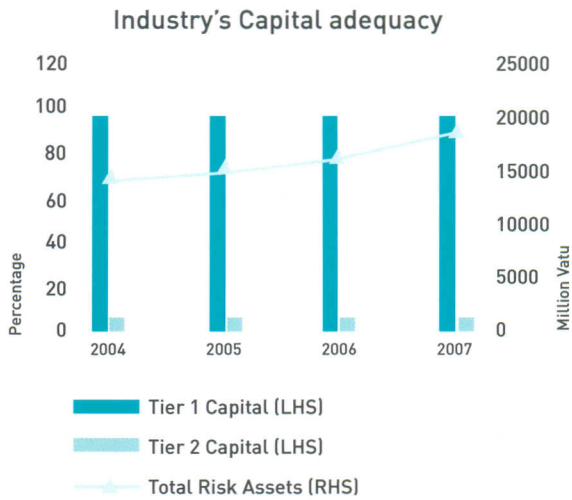


Figure x: Industry's Capital Adequacy

Impaired Asset

December 2007 show improvement in the domestic banking industry's asset quality. Total impaired asset fell by 16.4 percent to Vt3.0 billion (Dec-06: Vt3.6 billion). The decrease was attributable to the migration of doubtful loans to standard loans over the year. During the year, doubtful loans declined by 16.6 percent to Vt2.8 billion (Dec-06:Vt3.4 billion). Loss loans (written off) also declined by 13.0 percent to Vt182.7 million (Dec-06: Vt210.0 million).

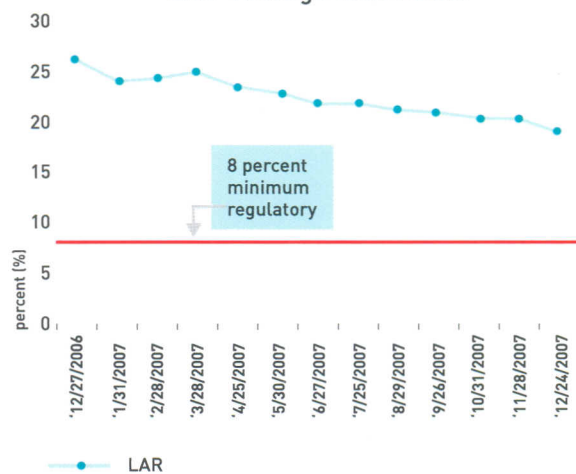
Standard and substandard loans increased by 17.6 percent and 1.2 percent to Vt20.4 billion (Dec-06: Vt17.3 billion) and Vt630.3 million (Dec-06: Vt622.5 million) respectively. Standard loans accounted for 84.8 percent of total loans.

The improvement in the domestic banking industry's asset quality resulted in the declines in both specific and general provisions over the year by 7.9 percent and 2.3 percent to Vt840.7 million (Dec-06: Vt912.8 million) and Vt31.4 million (Dec-06: Vt32.1 million) respectively. The decline in the provisioning level was also partly attributable to the introduction of the IFRS reporting system that banks are now using. Security held by the domestic banking industry continued to remain robust recording a 12.9 percent increase over the year to Vt14.7 billion (Dec-06: Vt13.0 billion).

Liquid Asset Requirement (LAR)

The domestic banking industry's liquidity position as measured through 'Liquid Asset Ratio (LAR)' continued to remain sound. As at 31st December 2007, the industry recorded its LAR ratio at 18.8 percent down from 25.7 percent in December 2006. The reduction reflects partly the reduction of the minimum regulatory requirement from 12 percent to 8 percent in November 2007. RBV is closely monitoring this trend to ensure that the domestic banking industry is maintaining its LAR above the prescribed minimum level.

LAR- Average Total Banks



International Banks

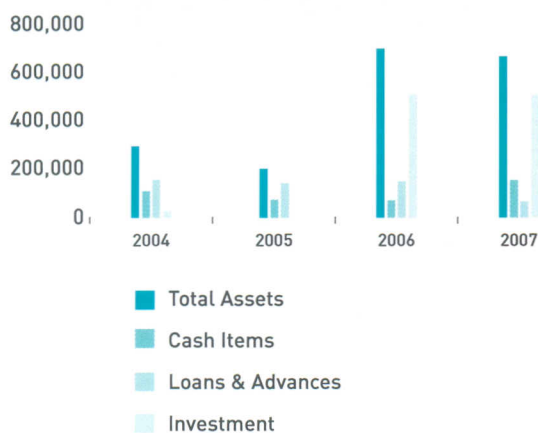
During the year 2007 there was one new entrant making a total of 8 offshore banks under the supervision of Reserve Bank of Vanuatu. The Bank also received many enquiries from investors from around the globe. The Bank is always proactive in ensuring that all legal requirements are satisfied by offshore industry as well as their operations are within the boundaries set internationally.

Anti-Money Laundering issues are paramount therefore all international banks are required to always adhere to the minimum requirements stipulated within the Cap 268.

Statement of Financial Position

The offshore banking industry recorded a negative growth of 2.35 percent in its total assets as at 31 December 2007 of USD659.6 million (Dec-06: USD675.5 million). The negative growth is attributable to Loans & Advances which significantly declined by 41.57 percent to USD60.6 million (Dec-06: USD103.7 million). Major component of total asset is investment which accounted for 76.56 percent (USD504.9 million).

Offshores Banking Industry's Total Assets

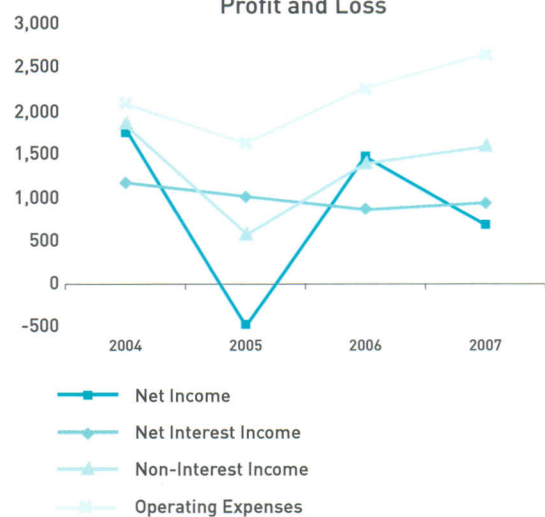


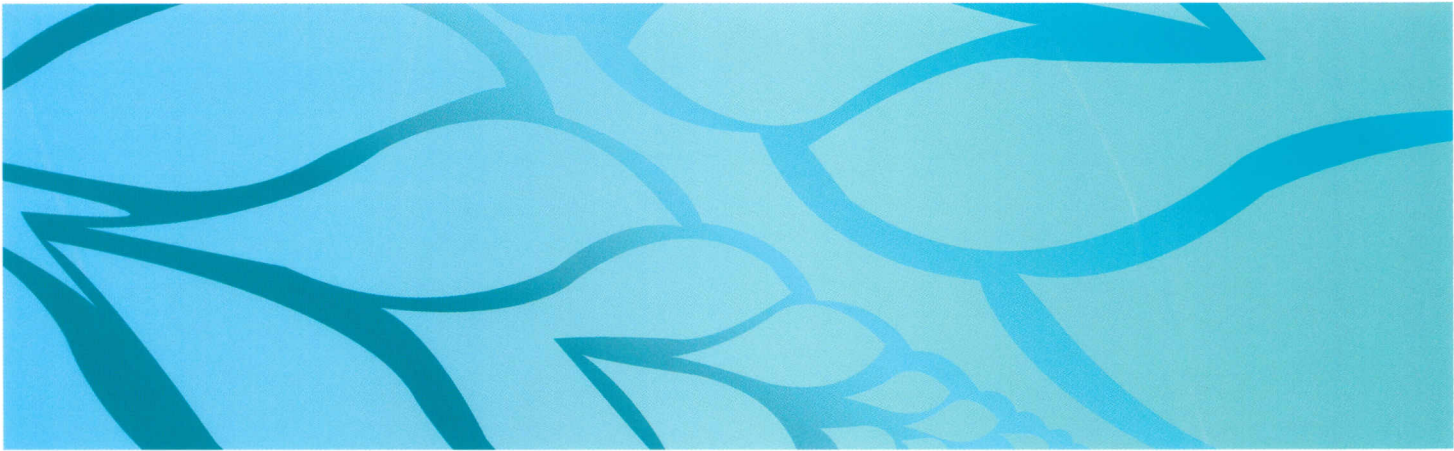
On the liability side, a decline in total liability of 3.11 percent to USD514.9 million has been reported as a result of 6.62 percent reduction on deposits to USD480.5 million (Dec-06: USD514.5 million). Deposits accounted for 93.32 percent of total liabilities (less shareholders equity)

Earnings

The Industry reported a net profit of USD705 thousand, 49.64 percent lower compared to December 2006 profit of USD1.4 million. The increase in operating income of 15.61 percent failed to offset the increase in overhead expenditure of 20.86 percent to USD2.5 million (Dec-06: USD2.1 million), and foreign exchange losses of 133.23 percent to USD209 thousand (Dec 06: USD629 thousand gain) incurred resulting in lower profit for 2007.

Profit and Loss





VNPF Supervision

The Bank through the department continues to supervise the VNPF. As VNPF acts as a trustee for the employees' funds, it is proper that the Bank supervise and regulate it to ensure that the members' funds are managed in the best interest of through sound and prudent practices. During the year, the Bank conducts its annual onsite review on operational risks. The Bank also conducts ad hoc meetings with the managers of the Fund where the need arises. Where issues of concerns are noted during the reviews, there is continuous monitoring of same until issue is sorted out.

Staff trainings and workshops

The Department continues to emphasize the importance of capacity building and staff development through internal and external trainings. One of the external trainings that the departments benefited most from was the Pacific Governance Support Program through AUSAID and APRA. This program is more practical, and participants from other jurisdictions join the host country to conduct onsite review of a particular institution. This program includes scoping exercise to wrap-up meetings, presenting findings and report writings. The Department also attends series of meetings including the AFSPC.

Anti-Money Laundering

The Reserve Bank of Vanuatu through the department continues to work closely with relevant authorities, in particular Finance Intelligence Unit to ensure Vanuatu complies with the revised FATF 40 recommendations on combating the financing of terrorism.

The onsite review of banks for the year focused on AML risks. The reviews assessed each bank's AML policy and review their operations against the AML policies, especially with regards to opening of accounts procedures, monitoring and reporting of transactions as required by FTRA.

Corporate Services

The Corporate Services Department has the primary responsibility for providing internal support services including: information communications technology, the Bank's current and future human resources needs, plant and properties, security, and general administration.

Official Representation

The Bank staff participated in several international meetings in 2007, which continued to help maintain the Bank's relationship with other central banks, and international institutions. Besides, the Bank continually maintained its relationship, with two of the prominent international financial institutions, the international Monetary Fund (IMF), the World Bank. During the year, the Governor accompanied the Minister of Finance to the Commonwealth Finance Ministers' meeting and the International Monetary Fund and World Bank Annual Meeting. Besides other meetings attended by the Governor in 2007, he also attended an annual survey on the success of the Pacific 2020 process, a survey founded, initiated and funded by AusAID, which provided a framework for analysis and debating of challenges and opportunities for economic growth in the Pacific and East Timor.

Community Service

In 2007, the Bank made several donations to both Private and Government institutions which included the Bank's major contribution of another Vt1 million to the Vanuatu Chamber of Commerce

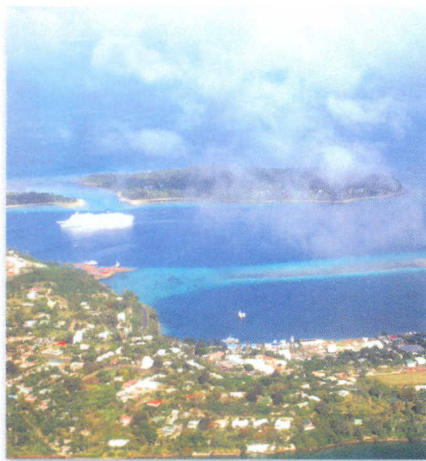
towards hosting of the "National Trade Show", which primarily focused on promoting local products to the public as well as exposure to potential overseas export markets.

Human Resources Unit

The Human Resources Unit is responsible for developing and implementing strategic approaches to meet the Bank's current and future human resources needs. The unit is responsible for providing advice and assistance to directors with the application of human resources policies and practices including recruitment, resource planning, performance management, staff training, remuneration, and employment conditions.

Staff

Upon the end of year 2007, The Reserve Bank of Vanuatu effectively had 66 staff in house. This is a significant increase in staffing numbers and can be accounted for in the three new security officers, the new Manager of Building and Support services, an Assistant Statistician, a Banking Officer, a Human Resource Officer, and an Assistant Bank Supervisor. Year 2007 also witnessed the departure of two long serving members of staff to the Bank, Research Department's Senior Economist and the Support Officer of Corporate Services, along with Financial Market Department's sole Dealer. The resident Legal Counsel also departed nonetheless the Bank anticipates the arrival of her successor in early 2008.



Human Resources Review

The year has produced change and improvement through the approved Independent review of the Human Resources. The review was single handedly performed by an HR Specialist from New Zealand. The review is divided into phases and the areas covered to date are as follows: Job Evaluation and Remuneration structure, Performance Appraisal of staff, and Reality Check survey project. The Bank for the first time has seen a distinct rise in staff turnover, where 5 staff exited the Bank in the course of the year alone, for various reasons, among them a retirement case, and replacements are gradually being sourced from the pool of interested applicants.

Training and Development

In the current year alone, there were 3 staff absent on study leave in Australia, NZ and Fiji respectively, two returned in December 2007 to take up their jobs, while the third is yet away for another two years completing his Masters at Lincoln Univeristy in New Zealand. And in accordance with the training policy, the Bank maintains its stance in ensuring nominated staff attend relevant courses, seminars, conferences and workshop training to build and develop their capabilities and desired skills on the job.

Work Experience attachments

The Bank has provided much opportunity for students to join up for work experience attachments. This is beneficial in boosting their confidence to be able

to cope with the pressures of work once they are actively employed in the workforce. In 2007, the Bank appointed a total of 10 students to attach with the Bank and the duration of attachments varied from 2 weeks to 3 months at the most. The students all hailed from different vocations and schools from Port Vila to as far as Laucala Campus Suva, all designated to all departments of the Bank. They were charged with a range of tasks and responsibilities and displayed a good level of commitment and maturity in achieving what was required of them.

Information and Communications Technology

New technologies continually come and go in today's digitized economy. The pursuit of opportunities through information and communications technology must be driven, not only by what is technologically feasible, but by what is strategically desirable. In line with the Bank's mission statements, information continues to remain a vital asset of the Bank hence the Information and Communications Technology Unit (ICT) continues to provide a stable computer network infrastructure for the Reserve Bank of Vanuatu for the dissemination of timely and quality information. The Information and Communications Unit embarked on a few significant projects during the year. What follows are accomplishments and future outlook of the unit.

The internet has had a significant impact on information flow between individuals, business entities and corporate organizations.



Communications and business transactions are taking place online and in a very effective and efficient manner. RBV realizes the power of the Internet and also the consequences of using this network infrastructure. To take greater advantage of the capabilities of the Internet, the RBV local area network underwent a major revamp mainly in terms of the server technology hardware and software and the communications medium. 64bit server hardware were installed, windows 2003 x64 server operating system replaced the windows 2000 server platform, network link was upgraded from 10/100 Mbps to 1G link, leased line was replaced with ADSL link creating a 512Mb download capacity and existing firewall configuration was upgraded to suite new network architecture and to tighten up the Bank's perimeter that is exposed to the Internet.

SWIFT System – ISP Local Loop

The Reserve bank of Vanuatu uses the SWIFT system for its payments and settlements function. In the SWIFT system the ISP local loop network provides the option of SWIFT customers with no or little choice of a SWIFT local Network Partner to access SWIFT's secure IP network. This is made possible by leveraging the infrastructure of the local Internet Service Providers (ISPs).

Given the monopoly of the telecommunications industry in Vanuatu and the non-existence of a SWIFT Network Partner in the country, the cost of operating and maintaining the SWIFT system in terms of network connectivity can be quite high. SWIFT customers have the option of reducing its

SWIFT connectivity costs by acquiring ISP-Local Loop. By acquiring ISP-Local Loop the Bank now enjoys the efficient connectivity to SWIFT network and should also see a reduction in its SWIFT network connectivity costs.

Local Intranet

The previous Intranet site was replaced with one driven more by content and collaboration needs. Microsoft SharePoint is now the framework of the local Intranet site which provides an environment for users to share, acquire, post and edit information without having to be technically skilled in ICT.

Administration and Training

ICT officers performed alternating role to manage the unit in the absence of the ICT Manager who was away on study leave. ICT officers during the year attended short courses and acquired training in Windows 2003 operating system, SQL Server 2000, PACINET workshop and Epicor training in order to especially support the new financial accounting system. A senior staff of the unit also returned at the end of the year after successfully completing a Masters program in Business Information Systems.

2008-2009 Outlook and Goals

- Working closely with the departments on their technology plans as stipulated by their individual requirements in meeting the objectives of the Bank's 2006 to 2008 strategic plan.



- Successfully implementing a new ICT Planning/ Advisory body.
- Promoting and leveraging the Bank's application development and content management capabilities.
- Upgrade of the Bank's website - www.rbv.gov.vu. The upgrade will be in the areas of making the site more user-friendly and interactive, more timely update of information, and more dynamic content.
- Continue to raise the profile of ICT related security and privacy issues.
- Continue to monitor size, cost, performance, and capacity of the Bank's ICT infrastructure along with the breadth of services provided.
- Understanding better what mission-driven ICT means and how the ICT advances and opportunities are aligned with the organization's objectives.
- Working closely with the Bank's BCP committee in creating and implementing an IT Disaster Recovery Plan. ICT is to continue to make progress in the areas of security, disaster recovery and risk management policy and practice. Security in particular is a moving target, so this will continue as a priority this year 2008 and the years to come.

Building and Support Services

The Building and Support Services unit is responsible for providing internal support services to facilitate

the smooth operations of the Bank including authorizing payments to both internal and external customers, maintenance of the Bank Building and other properties, providing staff refreshments and arranging staff official travel.

Redevelopment Project

Following the tender award to Brunet Enterprise General, work on the Redevelopment Project commences on 12th February 2007 after the contracts were realized. As planned, the contract duration is 22 months and according to the Contractor, the practical completion date is 13th December 2008, however due to bad weather condition that affected the project, the practical completion date has now moved to 19th January 2009.

As part of the work program, concrete works is expected to complete by the end of February 2008 and roofing to be completed by the end of March 2008. The overall Redevelopment Project is progressing well and even if the practical completion has moved forward, the contractor is working hard to maintain its original work schedule to meet as much as possible the original practical date of 13th December 2008.

New Water Reservoir

Part of the Redevelopment Project was to carefully dismantle the existing Steel Tank, demolish base and remove debris to level off the site for the new

building. The removal of the tank and relocation was part of a joint effort between the Reserve Bank of Vanuatu and UNELCO to construct the new Reservoir for the population of Port Vila Town.

High Voltage and Private Transformer

Reserve Bank of Vanuatu has agreed to include as part of the project a variation to include for a High Voltage Meter and Private Transformer. The cost of such a High Voltage Extension and private transformer is Vt8,370,979 and is contracted to UNELCO to carry out under the supervision of Kramer.

Reserve Bank of Vanuatu is categorized in the category of low voltage user and as such is paying a very sum for every KW Voltage used. With the HVM, Reserve Bank is estimating a saving of over Vt600,000 on electricity per Annum beginning in 2009.

Operation Safety Manual

As safety is paramount in every organization, Corporate Service Department has developed a Safety Operations Manual with a special consultant. The Operation Safety Manual contains detail operations on safety and will be effective in 2008 after trainings which will be contacted by the consultant.

A safety audit was also carried out by the consultant in the existing building which identifies areas that needs urgent attention especially fire safety equipments.

Security

Reserve Bank of Vanuatu since 2004 has recruited its own security personnel to provide 24-hour surveillance. In 2007 there is a need to recruit more Security Officers so the Bank recruited 2 additional

security officers to assist in security operations. The Bank now has a total of eight(8) Security Officers.

In addition to daily activities, support service section is from time to time asked to organize function. Some of the major functions organized in 2007 are the unveiling of the new Redevelopment Project, the launching of Epicor accounting program and the dividend handing over to the government on 3rd September.

As always, in December of every year, the Corporate Services Department through its support services organizes the End of year function for the bank. 2007 year of year function was organized at the Tara Beach just outside of town towards devils point. It was also incorporated in the function the fare welling of a long time serving secretary to the department of Research & Statistics, serving the bank for over 20 years.

Library

The library plays an active role to disseminate timely and quality information. In 2007 the library coordinated a series of seminar presentation on the Role of Central Banking to four senior colleges around Port Vila; a presentation was also conducted at the Parliament House for the Honourable Members of Parliament. Also, in 2007, the library undertook an upgrading in its program with a conversion of the Inmagic DB/Textworks version 5.0 catalogue stand-alone to Maxus library 5.0. Students and external visitors continued to access library materials and served in the library. The library continued to maintain its relationship with other central bank libraries and organizations.

Accounts and Customer Services

The Accounts and Customer Services Department is responsible for the customer services and the accounting functions. This comprises of maintaining of the customers accounts, facilitation of the payment transactions through the Port Vila Clearing House and SWIFT system, maintaining of the financial records, in charge of the budgeting and control process of the Bank and the managing of the stock and quality of the vatu currency.

This year the department embarked on a number of projects which lead to a number of new initiatives implemented. The changes are in line with the market developments as the Bank moves forward to modernize its operations. Further funding assistance was also received during the year from IMF.

1. Banking & Settlements

Banking transactions conducted through the Clearing House in 2007 by number of effects grew by 29 percent to 370,738. This is compared to 2006 at 286,615 while in value terms the total value of the transactions fell slightly by 10 per cent to VT 60.3 billion to the previous year's level.

The SWIFT payment system was upgraded from version 3 to SWIFTNet 6.0. The upgrade is in line with the global SWIFT upgrade requirement that has been set to complete in year 2007. A few features of the upgrade in the area of Relationship Management Authority (RMA) will be implemented in 2008.

Work also commenced during the year on the upgrading of the SWIFT connectivity from the dial up connectivity set up to a more comprehensive ISP Local Loop that is linked to the internet access. The change will improve the capacity of the back office to carry out the SWIFT payment transaction with the Bank's customers more effectively and at a reasonable cost to the Bank. The upgrade is expected to complete in 2008.

2. Accounts

PricewaterhouseCoopers the new appointed external auditor of the Bank for a term of five years commenced its duty with the Bank in 2007.

The external auditor's role was previously held by Hawkes Law Chartered Accountant Vanuatu for some years. The change follows the Board's direction to adopt current best practices in tendering the external

Operation of Clearing House

Period	No. of Effects	Value(MVT)
1999	370,352	34,224
2000	398,286	32,622
2001	378,016	34,995
2002	335,462	33,878
2003	263,664	28,230
2004	264,859	31,985
2005	279,162	38,562
2006	286,615	67,548
2007	370,738	60,343



auditor's role at the end of every five years. The move also is in line with the Bank's objective to move forward in implementing the IFRS requirements.

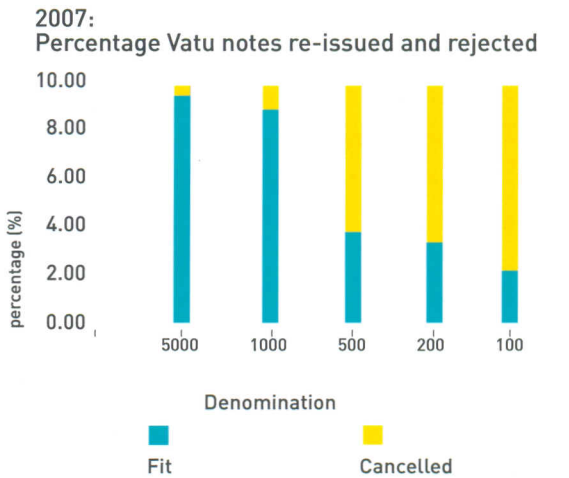
The biggest challenge during the year is the introduction of the new accounting software, EPICOR. The project was spearheaded by DATEC in liaison with the accounts office. Initial stages of the project commenced in the second week of August 2007 with the help of the DATEC project manager who conducted thorough trainings on the first stages of the project and test datas, before a parallel run was conducted in the month of December to test out the system. The old system was switched off following the successful parallel run of the new system.

Mr. Bernie Thompson, the IMF Accounting Advisor's follow-up visits in early 2007 focused on the initial stages of the implementation of the new accounting software and also assisted with the preparations of the 2006 financial accounts.

3. Currency Operations

a. Currency Examination

A total of 2,525,150 notes were examined by the Currency Office in 2007. These notes were sorted into those "fit for reissue" into public circulation and "unfit notes" to be destroyed. A total of 463,353 notes were canceled in 2007. The rejection rate for all the notes examined in 2007 is 18 percent compared to 17 % in the previous year.



Notes Examination				
Denomination	Quantity	Fit for Reissue	Cancelled	Rejection Rate
5000	562,490	542,360	20,130	4%
1000	1,592,745	1,382,739	210,006	13%
500	168,843	70,243	98,600	58%
200	180,817	61,476	119,341	66%
100	20,255	4,979	15,276	75%
Total	2,525,150	2,061,797	463,353	18%



On the denominations level, the lower denominations recorded the highest rejection rates compared to the higher denominations, reflecting the high demand of these notes in the market and their durability capacity.

b. Counter Transactions

The level of counter transactions increased for both in issues and withdrawals of currency to and from public circulation. The Bank issued more currency than its withdrawal by 16 percent during the year and by 13 percent over the previous year. This development saw the value of currency in circulation posted at a new peak level of VT4, 689.1 million registering a 20.2 percent increase from previous year.

The year also registered some changes in the value of Vatu denomination in circulation with the VT5000

Counter Transactions			
Period (Year)	Deposits (MVT)	Issues (MVT)	Total (MVT)
2000	4,136	4,143	8,281
2001	3,980	4,098	8,078
2002	3,873	3,902	7,775
2003	3,965	4,235	8,200
2004	3,390	2,864	6,255
2005	3,442	3,773	7,215
2006	4,199	4,719	8,918
2007	4,576	5,311	9,887

regaining the lead position from the VT1000 with an increase of 33.9 percent from previous year. The VT100 maintained its third position followed by VT500 while the VT200 took fifth position ahead of the VT20, followed by VT10, VT50, VT5, VT2 and VT1.

c) Counterfeits

A total of 22 counterfeits notes were examined and confiscated in 2007 compared to 18 in the previous year. The counterfeits confiscated during the year were mainly of the higher denomination and were of better quality to those identified in the previous

Counterfeits Summary				
Denomination	2005	2006	2007	Total
5000	31	10	4	45
1000	12	6	18	36
500	1	2	-	3
200	4	-	-	4
Total	48	18	22	88

years making it more difficult in general for their distinguish to the genuine notes. The Bank continues to take appropriate steps in advising the public on the distinction between a fake note to a genuine note.

d) Numismatics

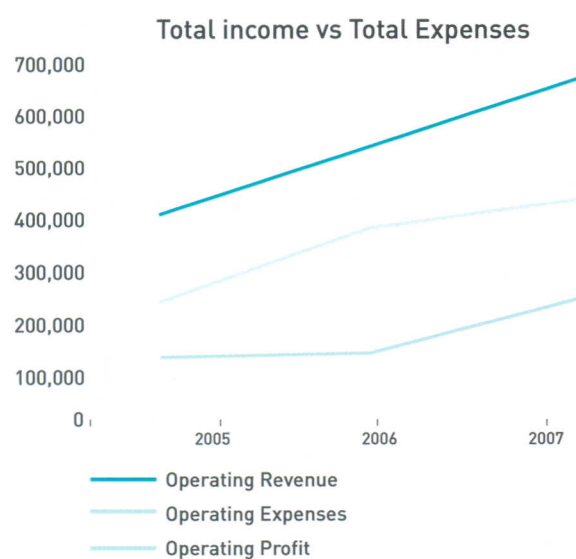
A total of Vt 6.3 million was received in coins sales royalties in 2007. This is from sales commission received from the sales of collectors' items and

royalties from the international sales of proof sets of coins struck under contracted Agreements with renowned international mints.

e) Financial Performance

Income

A total revenue of Vt 687.3 million was recorded at the end of 2007 showing an increase of 27 per cent over last year's level at Vt 539.3 million. The increase is attributed again to a further strong growth recorded during the year in interest income at Vt 647.8 million (Vt 521.8 million, 2007). Trend wise this year's result continues to place the Bank's revenue earnings at a steady upward trend. Other income which contributed to this year's growth also came from the net unrealized gains in foreign securities market price movements.



Expenditure

Total expenditure for year 2007 stood at Vt 421 million recording a slight increase from the 2006 level at Vt 388.4 million. Staff costs remains the major share of the Bank's expenditures at Vt 182.1 million showing a 5 per cent increase over year 2006 level at Vt 174.1 million.

Operating Profit

Total net operating profit for the year stood at Vt 266.2 million showing a 76.3 per cent growth over the 2006 position at Vt 151 million.

Payment to Government

A total of Vt 213.8 million in dividend is declared to the Government of Vanuatu based on the 2007 results under section 7 (3) of the Reserve Bank's Act. This amount is arrived at after 10 per cent of the operating profit of Vt 26.6 million was moved to the general reserve account under section 7(1) of the Bank's Act and Vt 25.8 million under section 7 (2) to cleared off the non-interest notes (NIBN) issued by the Government in 2006.

A further debit balance was recorded in the Revaluation Reserves account of Vt 108.9 million at the end of this year. Under the requirement of section 25(2) of the Bank's Act the Government of Vanuatu issued a non interest bearing note equal to the sum of Vt 108.9 million.

(VT 000's)	
Operating Profit	266,217
Less	
Transfers to General Reserves	26,622
Transfer to write down Gov't NIB note	25,764
Add	
1/5 portion of Revaluation Reserve Acc	
Total paid to Government	213,831

The background of the entire page is a solid green color. Overlaid on this background is a large, stylized graphic of green leaves and stems. The leaves are elongated and pointed, with some showing internal vein-like patterns. The stems are thick and curved, creating a sense of organic growth. The overall design is minimalist and modern.

RESERVE BANK OF VANUATU FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007



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Financial Statements

31 December 2007

RESERVE BANK OF VANUATU

DIRECTORS' REPORT

In accordance with a resolution of the Board of Directors, the directors herewith submit the Balance Sheet of the Bank as at 31 December 2007, and the related Income Statement, Statement of Changes In Equity, and Cash Flow Statement for the year ended on that date and report as follows:

1. DIRECTORS

The following were directors of the Bank at any time during the financial year and up to the date of this report:

Odo Tevi – Chairman
Geordie Mackenzie-Reur
Anniva Tarilongi
Simeon Athy

2. PRINCIPAL ACTIVITIES

The Reserve Bank's role as a central bank, as defined in the Reserve Bank of Vanuatu Act, shall be:

- (a) to regulate the issue of currency and the supply, availability and international exchange of money;
- (b) to promote monetary stability;
- (c) to promote a sound financial structure;
- (d) to foster credit and exchange conditions conducive to the orderly and balanced economic development of the country.

3. TRADING RESULTS

The operating income of the Bank for the year ended 31 December 2007 was Vt266.217m (2006: Vt150.978m).

4. RESERVES

In accordance with Section 7(1) of the Reserve Bank of Vanuatu Act, the Bank transferred Vt26.622m to the General Reserves

5. PAYABLE TO GOVERNMENT

In accordance with the Reserve Bank of Vanuatu Act Section 7(3), the amount of Vt213.831 m is payable to the Government of Vanuatu.

6. BAD AND DOUBTFUL DEBTS

The directors took reasonable steps before the Bank's financial statements were made out to ascertain that all known bad debts were written off and adequate provision was made for doubtful debts.

At the date of this report, the directors are not aware of any circumstances which would render the amount written off for bad debts, or the amount of the provision for doubtful debts, inadequate to any substantial extent.

7. PROVISIONS

There were no material movements in provisions during the year apart from the normal amounts set aside for such items as doubtful debts, depreciation and employee entitlements.

Financial Statements

31 December 2007

DIRECTORS' REPORT - Continued

8. ASSETS

The directors took reasonable steps before the Bank's financial statements were made out to ascertain that the assets of the Bank were shown in the accounting records at a value equal to or below the value that would be expected to be realised in the ordinary course of business.

At the date of this report, the directors are not aware of any circumstances which would render the values attributable to the assets in the financial statements misleading.

9. DIRECTORS BENEFIT

No director of the Bank has, since the end of the previous financial year, received or become entitled to receive a benefit by reason of contract made by the Bank with the director or with a firm of which the director is a member, or with a company in which the director has substantial financial interest.

10. EVENTS SUBSEQUENT TO BALANCE DATE

Since the end of the financial year the directors are not aware of any matter or circumstances not otherwise dealt with in the report that has significantly affected the operations of the Bank, the results of those operations or the state of affairs of the Bank in subsequent financial years.

11. BASIS OF ACCOUNTING

The Directors believe that the basis of preparation of accounts is appropriate and the Bank will be able to continue in operation for at least 12 months from the date of this statement. Accordingly, the Directors believe that the classification and carrying amounts of the assets and liabilities as stated in the accounts to be appropriate.

12. OTHER CIRCUMSTANCES

At the date of this report, the directors are not aware of any circumstances not otherwise dealt with in this report or financial statements which render any amounts stated in the financial statements misleading.

13. UNUSUAL TRANSACTIONS

The results of the Bank's operations during the financial year have not in the opinion of the directors been substantially affected by any item, transaction or event of a material and unusual nature other than those disclosed in the financial statements.

For and on behalf of the Board of Directors in accordance with a resolution of the Directors
this 4th day of, July 2008.



Governor (Director)



Chairman



Financial Statements

31 December 2007

STATEMENT BY DIRECTORS

In the opinion of the Directors:

- (a) the accompanying income statement is drawn up so as to give a true and fair view of the results of the Bank for the year ended 31 December 2007,
- (b) the accompanying statement of distribution is drawn up so as to give a true and fair view of the results of the Bank for the year ended 31 December 2007,
- (c) the accompanying balance sheet is drawn up so as to give a true and fair view of the state of affairs of the Bank as at 31 December 2007,
- (d) the accompanying statement of movements in equity is drawn up so as to give a true and fair view of the movement in equity for the year ended 31 December 2007, and
- (e) the accompanying cash flow statement is drawn up so as to give a true and fair view of the cash flows of the Bank for the year ended 31 December 2007.

For and on behalf of the Board of Directors by authority of a resolution of the Directors this 4th day of July 2008.

Governor (Director)

Chairman



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INDEPENDENT AUDIT REPORT

To the Board of Directors of the Reserve Bank of Vanuatu

Scope

We have audited the financial statements of the Reserve Bank of Vanuatu for the financial year ended 31 December 2007 as set out on pages 5 to 28. The Bank's directors and management are responsible for the preparation and presentation of the financial statements and the information they contain. We have conducted an independent audit of these financial statements in order to express an opinion on them to the Board of Directors of the Bank.

Our audit has been conducted in accordance with International Standards on Auditing to provide reasonable assurance as to whether the financial statements are free of material misstatement. Our procedures included examination on a test basis, of evidence supporting the amounts and other disclosures in the financial statements. An audit also includes assessing, within the context of applicable laws, accounting policies used and significant accounting estimates made by management as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Audit Opinion

The accompanying financial statements have been prepared in accordance with the Reserve Bank of Vanuatu Act, and the accounting policies described in notes 2 and 3 of the financial statements.

In our opinion, the accompanying financial statements have been prepared, in all material respects, in accordance with the basis of preparation and the accounting policies described in notes 2 and 3 of the financial statements.

Without qualifying our opinion, we emphasise that the accounting policies used and disclosures made are not intended to, and do not, comply with all the requirements of International Financial Reporting Standards.

4 July 2008
 Suva, Fiji


PricewaterhouseCoopers
 Chartered Accountants



Income Statement

For The Year Ended 31 December 2007

(Expressed in 000's Vatu)

	Note	2007	2006
Operating revenue			
Interest income	7	647,825	521,869
Net unrealised gains in foreign securities market prices		28,896	-
Other income		10,585	17,470
Total revenue		<u>687,306</u>	<u>539,339</u>
Operating expenses			
Interest expense	8	72,908	65,527
Net unrealised losses in foreign securities market prices		-	43,567
Personnel expenses	10	182,070	174,053
Other operating expenses	9	166,111	105,214
Total expenses		<u>421,089</u>	<u>388,361</u>
Net operating profit		<u>266,217</u>	<u>150,978</u>

This income statement is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 28.



Statement of Distribution

For The Year Ended 31 December 2007 (Expressed in 000"s Vatu)

	Note	2007	2006
Net operating profit		266,217	150,978
Less:			
Redemption of Governments non interest bearing securities issued under Section 25 (2) as required under Section 7 (2) of the RBV Act	(25,764)	(80,643)	
Amount available for distribution		<u>240,453</u>	<u>70,335</u>
Distribution as follows:	4		
Transfer to General Reserves (Section 7 (1)).		26,622	15,098
Payable to Government of Vanuatu (Section 7 (3))		213,831	55,237
		<u>240,453</u>	<u>70,335</u>

The statement of distribution is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 28.



Balance Sheet

AS AT 31 DECEMBER 2007 (Expressed in 000's Vatu)

Assets	Note	2007	2006
Cash and cash equivalents	11	7,003,559	7,460,253
Treasury notes, bonds and bills	11	4,362,302	3,109,418
Government securities	12	411,101	339,184
Government bonds	13	862,500	862,500
Interest receivable		220,232	173,127
Other receivables	14	168,148	114,090
Stock of currency (notes and coins)	15 (a)	50,187	70,329
Property, plant and equipment	16	734,646	178,291
International Monetary Fund (IMF):	17		
Reserve Tranche position		-	-
Currency subscription		389,707	400,364
Special Drawing Rights	11	186,354	173,438
Total Assets		14,388,736	12,880,994
Liabilities			
Accrued expenses		59,307	21,190
Due to statutory body		3	3
Due to commercial banks		4,117,679	4,020,373
Due to Government		1,936,710	1,564,363
Due to international institutions and agencies		383,179	352,096
Reserve Bank of Vanuatu notes		1,590,915	1,785,296
IMF – Notes currency subscription		389,707	400,364
Currency in circulation	15 (b)	4,688,956	3,901,729
Other creditors		60,104	60,439
Employee provisions		57,504	61,445
Total Liabilities		13,284,064	12,167,298
Net Assets		1,104,672	713,696
Capital and reserves			
Issued capital 18		100,000	100,000
General reserve	4		640,318
613,696			
Revaluation reserve	5	-	-
Fair Value Reserve	6(b)	139,557	-
F/Asset Revaluation Reserve	6(a)	224,797	-
Total Capital and Reserves		1,104,672	713,696

Statement of Movement in the Equity

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

	F/Asset Revaluation	Fair Value Reserve	Issued & paid up capital	General reserve	Revaluation Reserve(s)	Total
2007						
Balance at beginning of the financial year	-	-	100,000	613,696	-	713,696
Transfer from profit and loss account						
- Current year profit (Section 7(1))	-	-	-	26,622	-	26,622
Net loss on foreign exchange (Section 25(1))	-	-	-	-	(108,945)	(108,945)
Non interest bearing securities issued by the Government (Section 25(2))	-	-	-	-	108,945	108,945
1/5 of the total foreign exchange revaluation gain transferred to Government (Section 25 (3))	-	-	-	-	-	-
F/Asset Revaluation	224,797	-	-	-	-	224,797
Fair Value Reserve	-	139,557	-	-	-	139,557
Balance at the end of the financial year	<u>224,797</u>	<u>139,557</u>	<u>100,000</u>	<u>640,318</u>	<u>-</u>	<u>1,104,672</u>
2006						
Balance at beginning of the financial year	-	-	100,000	598,598	-	698,598
Transfer from profit and loss account						
- Current year profit (Section 7(1))	-	-	-	15,098	-	15,098
Net loss on foreign exchange (Section 25 (1))	-	-	-	-	(25,764)	(25,764)
Non interest bearing securities issued by the Government (Section 25 (2))	-	-	-	-	25,764	25,764
1/5 of the total foreign exchange revaluation gain transferred to Government (Section 25 (3))	-	-	-	-	-	-
Balance at the end of the financial year	<u>-</u>	<u>-</u>	<u>100,000</u>	<u>613,696</u>	<u>-</u>	<u>713,696</u>

The statement of movements in equity is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 28.



Statement of Cash Flows

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

	Note	2007	2006
Cash flows from operating activities			
Interest received		629,615	485,645
Interest paid (79,543)	(54,249)		
Other operating receipts		10,361	34,500
Other operating payments		(304,401)	(222,144)
Net cash provided by operating activities	19	256,032	243,752
Cash flows from investing activities			
Net (increase)/decrease in:			
Special drawing rights		(12,916)	(802)
Treasury notes and bonds		(1,084,431)	(64,281)
Government securities		(17,632)	8,585
Other receivables		(62,061)	-
Purchase of property, plant and equipment		(306,718)	(48,156)
Proceeds from sale of property plant & equipment		225	2,056
Net cash used in investing activities		(1,483,533)	(102,598)
Cash flows from financing activities			
Net increase/(decrease) in:			
Currency in circulation		787,227	523,132
Due to commercial banks		97,306	1,461,293
Due to Government		158,517	186,457
Due to international institutions and agencies		31,083	107,082
Reserve Bank of Vanuatu notes		(194,381)	1,199,926
Net cash provided by financing activities		879,752	3,477,890
Net increase in cash and cash equivalents		(347,749)	3,619,044
Cash and cash equivalents at the beginning of the financial year	11	7,460,253	3,866,973
Effects of exchange rate changes on foreign currency balances	3(b),5	(108,945)	(25,764)
Cash and cash equivalents at the end of the financial year	11	7,003,559	7,460,253

The statement of cash flows is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 10 to 28.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

1 THE LEGAL FRAMEWORK

The Reserve Bank of Vanuatu ("the Bank") operates under the Reserve Bank Act [CAP 125] ("RBV Act").

The Bank is an independent legal entity wholly owned by, and reporting to, the Government of the Republic of Vanuatu. The Bank is responsible for ensuring:

- Regulation of the issue, supply, availability and international exchange of the currency of Vanuatu;
- Supervision and regulation of banking business and the extension of credit;
- Advising the Government on banking and monetary matters;
- Promoting monetary stability;
- Promoting a sound financial structure;
- Fostering economic conditions conducive to the orderly and balanced economic development of Vanuatu, and
- Regulation and supervision of domestic and international (offshore) banks.

Section 6 of the RBV Act states that the Board shall determine the net profit of the Bank for the current financial year after meeting current expenditures and making such provisions as it views appropriate for bad and doubtful debts, depreciation of assets, contributions to staff and pension funds, and other contingencies.

2. BASIS AND FORMAT OF PRESENTATION

(a) Basis of preparation

The financial statements of the Bank have been prepared in accordance with the Reserve Bank of Vanuatu Act and the Bank's accounting policies are based on International Financial Reporting Standards except where the Act requires a different treatment, as noted in Note 3 (b), in which case the Act takes precedence.

The financial statements have been prepared under the historical cost basis as modified by financial assets and liabilities at fair value through profit or loss.

The accounting policies have been consistently applied and, except where there is a change in accounting policy, are consistent with those of the previous year. The financial statements are presented in Vanuatu currency (Vatu) rounded to the nearest thousand.

(b) Comparatives

Where necessary, comparative information has been reclassified to achieve consistency in disclosure with current financial year amounts and other disclosures.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

3. STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted in the preparation of the financial statements are set out below:

(a) Revenue recognition and income presentation

Operating revenue

Operating revenue is recognised on an accruals basis and includes interest income, sundry income and profit on foreign exchange dealing with commercial banks.

(b) Foreign currency assets and liabilities

Foreign currencies

Transactions in foreign currencies are converted to Vatu at the rates of exchange prevailing on transaction dates. Year-end assets and liabilities denominated in foreign currencies are converted at the rates of exchange ruling at the year-end.

All unrealized gains arising from the conversion of foreign currencies are taken to the Revaluation Reserve (Note 3) in accordance with the provisions of Section 25 of the RBV Act and are not included in the computation of the annual profits or losses of the Bank.

Net losses arising from the conversion of foreign currencies are set off against any credit balance in the Revaluation Reserve Account. If the balance of this account is insufficient to cover such losses they are offset against any net profit remaining after the transfer to the General Reserve Account has been made in terms of Section 7 of the RBV Act. If these transfers are not adequate to cover such losses, the Government is required to transfer to the ownership of the Bank, non-negotiable non-interest bearing securities to the extent of the deficiency.

Any credit balance in the Revaluation Reserve at the end of each year is applied first to the redemption of any non-negotiable non-interest bearing securities previously transferred to the Bank by the Government to cover losses; thereafter one-fifth of any remaining balance is payable to the Government.

(c) Coins sold as numismatic items

The Bank sells, or receives royalties on coins which are specially minted or packaged as numismatic items. These coins have not been accounted for as currency in circulation as they were not issued for monetary purposes.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

(d) Financial Instruments

Financial Assets

Loans and receivables

This includes loans and advances, current and calls accounts, short term deposits and cash and cash equivalents. Loans and advances are valued in accordance with note 1 (k).

Fair value through profit and loss financial assets

This includes offshore investment securities which includes treasury notes, bonds and bills. These financial assets are carried at fair value through profit and loss and are valued at market bid prices.

Held to Maturity financial assets

These relates to Vanuatu Government bonds which are held to maturity and are valued in accordance with note 3(j).

Available for Sale

Available-for-sale financial assets are carried at fair value. Unrealised gains and losses arising from changes in the fair value are recognised in a reserve. When available-for-sale financial assets are sold or impaired, the accumulated fair value adjustments are included in the income statement as gains and/or losses.

Financial Liabilities

Other financial liabilities

The following have been classified as financial liabilities: Due to commercial banks, due to government, due to statutory body, currency in circulation and other creditors. These are valued at cost.

(e) Property, plant and equipment

Acquisitions

Items of property, plant and equipment are recorded at cost and depreciated as outlined below. All items of property, plant and equipment are carried at the lower of cost less accumulated depreciation, and any recoverable amount.

Disposal of assets

The gain or loss on disposal of assets is calculated as the difference between the carrying amount of the asset at the time of disposal and the proceeds on disposal, and is included in the result in the year of disposal.

Revaluation

Land and buildings are shown at fair value based on valuations by external independent valuers, less subsequent depreciation for the land and buildings. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset, and the net amount is restated to the revalued amount of the asset. All other plant and equipment is stated at historical cost less depreciation.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

(e) Property, plant and equipment - continued

Revaluation – continued

Revaluation increments are credited directly to the Asset Revaluation Reserve, except where they reserve a decrement previously debited to Loss on Revaluation Expense in the Income Statement in respect of the same class of assets. Revaluation decrements are debited directly to the Income Statement where they could not be offset against a previously recognized revaluation increment in the Asset Revaluation Reserve in respect of the same class of assets.

Depreciation

Depreciation is charged on a straight line basis over the estimated useful lives of the assets. The rates of depreciation used are based on the following estimated useful lives:

- Reserve Bank building - 40 years
- Leasehold land - 30-75 years
- Plant and equipment - 3-10 years

Assets are depreciated from the date of acquisition. Expenditure on repairs or maintenance of property, plant and equipment incurred which does not add to future economic benefits expected from the assets is recognized as an expense when incurred.

Prior to January 1, 2007, an estimated useful life of 10 years was used to depreciate the Reserve Bank building. With effect from January 1, 2007, the building is depreciated on an estimated useful life of 40 years. The revised depreciation rate is a better reflection of the useful life of the building and has the effect of decreasing the depreciation expense for the year by approximately VT653,000.

(f) Notes and coins

The cost of notes and coins are initially capitalized. When currency is issued into circulation, the cost of producing such currency is taken up in the income statement.

(g) Income Tax

The Bank is exempt from income tax in accordance with Section 42 of the RBV Act.

(h) Employee entitlements

Employee remuneration entitlements are determined by the Governor (in consultation with the Board) in terms of Section 10 of the RBV Act. The provision for employee entitlements comprises severance allowance, gratuity and annual leave and represents the present liability resulting from employees' services to the balance sheet date. The provision has been calculated at nominal amounts based on current wage and salary rates.

Vanuatu National Provident Fund

Employer contributions to the above fund are charged against income as incurred.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

5. REVALUATION RESERVE - continued

At 31 December 2006, there was a net revaluation loss in the Revaluation Reserve of Vt25.764 million. In terms of Section 25 (2) of the RBV Act the Government then issued non interest bearing securities to cover this deficit.

At 31 December 2007, there was a net revaluation loss of Vt108,945 million. In accordance with Section 25(2), the Government issued a non interest bearing security of the said amount to cover this deficit. Under Section 7 (2), net profits were applied first to redeem the non interest bearing securities' balance of Vt25.8 million issued by Government in 2006. The residual net profit is payable to the Government of Vanuatu.

6. ASSET REVALUATION RESERVE ACCOUNTS

(a) Fixed asset revaluation reserve

Following the revaluation of the Reserve Bank's land and buildings in 2007, the Bank has established an appropriate Fixed Asset Revaluation Reserve (Refer also Note 3(e)).

(b) Fair value reserve

Unrealised gains arising from changes in the valuation of the Bank for International Settlements investments are recognized in a Fair Value Reserve.

7. INTEREST INCOME	2007	2006
Overseas Investments	5	4
Domestic Investments		
Staff Loans & Advances	6	5
	<hr/>	<hr/>
8 INTEREST EXPENSE	2007	2006
Interest on Government accounts	19,222	16,433
Interest on Reserve Bank of Vanuatu notes	53,686	49,094
	72,908	65,527
	<hr/>	<hr/>
9. OPERATING EXPENSES	2007	2006
Auditor's remuneration	4,303	2,827
Depreciation and amortization	19,519	24,727
Funds managers' fee	6,185	7,995
Loss on sale of bonds	47,287	-
Amortisation of currency costs	22,803	10,441
Communication expenses	12,842	15,559
Bad debt expense	7,053	1,951
Other expenses		46,119
41,714	<hr/>	<hr/>
	166,111	105,214

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

10. PERSONNEL EXPENSES

	2007	2006
Salaries and wages	89,855	87,681
Superannuation contribution (VNPF)	3,622	3,436
Staff training	20,480	18,411
Severance pay, long service leave, accrued annual leave and		
Gratuity expense	22,866	24,009
Other	45,247	40,516
	<u>182,070</u>	<u>174,053</u>

11. EXTERNAL ASSETS

(a) External assets consists of the following:

Cash	518	3,256
Current and call accounts	1,293,790	605,118
Short term deposits	5,709,251	6,851,879
Total cash and cash equivalents	7,003,559	7,460,253
Investment securities at market value - current	4,362,302	3,109,418
Investment securities at market value - non-current	-	-
Special drawings rights department	186,354	173,438
Total external assets	<u>11,552,215</u>	<u>10,743,109</u>

For the purpose of the statement of cash flows, cash and cash equivalents includes coins, notes, cash at bank, money at call and cash held on short term deposits.

Cash and cash equivalents at the end of the financial year as shown in the statement of cash flows is reconciled to the related items in the balance sheet as noted above.

(b) External assets are defined by the Act as including any internationally recognized reserve asset. In these financial statements, external assets also include fully convertible foreign currency balances equivalent to VT16,615 (2006 – Vt23,455) held with local banks in Vanuatu.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

12. GOVERNMENT NON-NEGOTIABLE SECURITIES ISSUED TO THE BANK

	2007	2006
Balance at the beginning of the financial year	339,184	402,648
(Encashment) / net purchase of securities	71,917	(63,464)
Balance at the end of the financial year	<u>411,101</u>	<u>339,184</u>

At 31 December 2006 as a result of the debit balance in the Revaluation Reserve an amount of Vt25.8 million of non negotiable securities was issued by the Government to cover for the deficiency in the Revaluation Reserve. These were then redeemed out of the 2007 net profit as required under Section 7 of RBV Act

At 31 December 2007, as a result of further debit balance in the Revaluation Reserve, non interest bearing securities totaling Vt108.9 million was issued by the Government to cover the deficiency. (Refer also Note 3 (b))

13. GOVERNMENT BONDS

These securities which are valued in accordance with note 3(j) of the financial statements, have varying maturity dates up to 2013. The maturities are set out below:

	2007	2006
Maturities of securities are summarised as follows:		
Not later than 1 year	562,500	-
Between 1 and 2 years	-	-
Between 2 and 5 years	-	562,500
Later than 5 years	300,000	300,000
	<u>862,500</u>	<u>862,500</u>

14. OTHER RECEIVABLES

	2007	2006
Loans and advances	83,415	105,992
Sundry debtors	272	5,192
Royalties	-	1,943
Uncleared cheques	84,434	-
Other	27	63
	<u>168,148</u>	<u>114,090</u>

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

15. CURRENCY ACTIVITIES

(a) Stock of currency (notes and coins)

	2007	2006
Balance at the beginning of the financial year	70,329	56,758
Cost of new currencies	2,662	24,012
Less: issued into circulation	(22,804)	(10,441)
Balance at the end of the financial year	50,187	70,329

Currency costs are treated in accordance with accounting policy in note 3(f).

(b) Currency issued into circulation during the year

Notes	4,123,739	3,391,360
Coins	565,217	510,369
Total currency issued	4,688,956	3,901,729

16. PROPERTY, PLANT AND EQUIPMENT

	Land and Buildings	Computer and Equipment	Other	Work in Progress	Total (VT'000)
Cost/Valuation					
Opening balance	258,326	87,428	38,748	79,683	464,185
Additions	-	13,401	29,693	309,226	352,320
Net revaluation	33,574	-	-	-	33,574
Disposals	-	(1,554)	-	-	(1,554)
Closing balance 31.12.07	291,900	99,275	68,441	388,909	848,525
Accumulated Depreciation					
Opening balance	191,224	67,754	26,916	-	285,894
Revaluation	(191,224)	-	-	-	(191,224)
Charges for the Year	6,940	7,439	5,140	-	19,519
Disposals	-	(310)	-	-	(310)
Closing balance 31.12.07	6,940	74,883	32,056	-	113,879
Net Book Value 31.12.07	284,960	24,392	36,385	388,909	734,646

Work in progress represents expenditure capitalised to date for the new head office building.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

16.	PROPERTY, PLANT AND EQUIPMENT – continued		
	(c) Land and buildings were revalued by an independent valuer, Professional Valuation Practice and Lease Management Services. The revaluation surplus was credited to the Asset Revaluation Reserve.		
17.	INTERNATIONAL MONETARY FUND		
	(a) Vanuatu is a member of the International Monetary Fund (IMF) and the Bank has been designated as both the Government's fiscal agency (through which the Government deals with the IMF) and as the depository for the IMF's holding in Vatu.		
	(b) Vanuatu's subscription to the IMF has been met by:		
	(i) payment to the IMF out of the Bank's external assets which have been reimbursed by the Government by issue of non-interest bearing securities;		
	(ii) the funding of accounts in favour of the IMF in the books of the Bank by the Government.		
18.	SHARE CAPITAL		
		2007	2006
	Authorised capital of 400,000,000 ordinary shares	400,000	400,000
	Issued and paid-up capital of 100,000,000 ordinary shares	100,000	100,000
19.	RECONCILIATION OF OPERATING PROFIT TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
		2007	2006
	Operating profit	266,217	150,978
	Non cash items		
	Depreciation	19,519	24,727
	Bad debts	7,053	1,951
	Amortisation of Currency	22,804	10,441
	Profit on sale of property, plant & equipment	(225)	(2,056)
	Gain/loss on change in fair value	(28,896)	43,567
	Net (increase)/decrease in assets		
	Interest receivable	(47,105)	(36,224)
	Other receivable	(7,053)	19,086
	Currency payments	(2,662)	(24,012)
	Net (decrease)/increase in liabilities		
	Accrued expenses	26,380	55,294
	Net cash provided by operating activities	256,032	243,752

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

20. RELATED PARTIES

Identity of related parties

The Bank's ultimate parent entity is the Government of the Republic of Vanuatu.

The Board of Directors during the financial year ended 31 December 2007 were Odo Tevi (Chairman and Governor), Geordie Mackenzie-Reur, Anniva Tarilongi and Simeon Athy.

During the year, the following executives were identified as key management personnel of the Bank: Branan Karae (Director Accounts and Customer Services), Nelson Shem (Director Corporate Services Department), Noel Vari (Director Banking Supervision), Philip Aru (Director Research and Statistics Department) and Micheal Hililan (Director Financial Markets Department)

Transactions with related parties

In the normal course of its operations, the Bank enters into transactions with related parties identified above. The transactions with the Government of Vanuatu include banking services, foreign exchange transactions and purchases of government bonds.

The Directors are paid sitting allowances for services rendered. The Bank also provides non-cash benefits to the Executive Directors and executive officers in addition to their salaries.

Total remuneration is included in 'personnel expenses' as follows:

	2007	2006
Directors' fees and remuneration	675	208
Executive officers	12,684	12,684
	<u>13,359</u>	<u>12,892</u>

21. EMPLOYEES

The number of full time permanent employees as at 31 December 2007 was 66.(2006: 62).

22. CONTINGENT LIABILITIES

The directors are not aware of any contingent liabilities at balance sheet date (2006: nil).

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

23. RISK MANAGEMENT POLICIES

Exposure to operational, credit, liquidity, interest rate, and currency risk arises in the normal course of the Bank's operations. The structure of the Bank's balance sheet is primarily determined by the nature of its statutory functions, rather than commercial considerations. At the same time the Bank continually manages its exposure to risk, through a variety of risk management techniques. Risk management of the Bank is regulated by internal instructions and policies, and closely monitored by the Board.

Operational risk management

Operational risk relates to the risk of loss resulting from human error, lack of control or failure of internal processes and systems.

Managing operational risk in the Reserve Bank is an integral part of the day-to-day operations and oversight. This includes adherence to Reserve Bank's corporate policies and procedures.

Operating risk relating to the activities of foreign currency reserves management is controlled by a number of internal instructions, and there is clear segregation of front office and back office activity. The latter is one of the mechanisms for managing operating risk.

Material financial instruments to which the bank has exposure include:

- (i) External assets
- (ii) Other liabilities.

Credit risk management

The Bank is subject to credit risk exposure. This is the risk that a counter party will be unable to pay amounts in full when due. The Bank's maximum credit risk, excluding the value of collateral, is generally reflected in the carrying of financial assets. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant. The Bank does not require collateral in respect of financial assets except in respect of commercial bank short term borrowing and loans to staff.

Management has a credit policy in place. Credit risk on transactions in foreign currency reserves is managed through the approval of transactions and placement of funds, the establishment of limits restricting risk and constant monitoring of positions. Counter party limits are set based on credit ratings and are subject to regular review. Currency risk and the exposure in the local currency portfolio is also monitored and managed. Credit risk on financial assets is minimized by dealing with recognized monetary institutions with minimum acceptable credit ratings and operational limits.

At balance sheet date there were no significant concentrations of credit risk.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

Liquidity risk management

Liquidity risk is defined as the risk of loss arising due to the mismatch of the maturities of assets and liabilities. The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest and exchange rates and maintaining of the adequate level of liquidity at all times to meet payments.

To minimize the liquidity risk, the Bank maintains an adequate level of reserves and taking into consideration the transaction demand on foreign exchange, ensures that an appropriate amount is maintained in current accounts at all times.

The following tables show assets and liabilities at 31 December 2007 (and 2006 comparatives) grouped by remaining contractual maturity.

2006 Liquidity Risk

	Less than 3 mnths	Betwn 3 to 6 mnths	Betwn 6 to 12 mnths	More than 1 Yr	Undefined Maturity	Total
CURRENT ASSETS						
Cash and Cash Equivalents	7,460,253	-	-	-	-	7,460,253
Treasury Notes, Bonds & Notes	-	-	104,908	3,004,510	-	3,109,418
Government Securities	-	-	-	339,184	-	339,184
Vanuatu Government Bonds	-	-	-	862,500	-	862,500
Interest Receivable	118,178	52,419	2,530	-	-	173,127
Other Receivables	2,895	8,186	-	103,009	-	114,090
Stock of Currency	-	-	-	70,329	-	70,329
Property, Plant and Equipment	-	-	-	178,291	-	178,291
SDR	-	-	-	-	173,438	173,438
Total	7,581,326	60,605	107,438	4,557,823	173,438	12,480,630

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

Less than	Betwn 3 mnths	Betwn 3 to 6 mnths	More than 6 to 12 mnths	Undefined 1 Yr	Total Maturity
Accrued Expenses	21,190	-	-	-	- 21,190
Due to Statutory Bodies	3	-	-	-	- 3
Due to Commercial Banks	4,020,373	-	-	-	- 4,020,373
Due to Government of Vanuatu	422,141	703,754	438,468	-	- 1,564,363
Due to International Inst.	156,792	-	-	195,304	- 352,096
Reserve Bank of Vanuatu Notes	1,785,296	-	-	-	- 1,785,296
Currency Issued	3,901,729	-	-	-	- 3,901,729
Other Creditors	18,831	41,608	-	-	- 60,439
Employee Provisions	4,095	-	-	57,350	- 61,445
Total	10,330,450	745,362	438,468	252,654	-11,766,934

Net Liquidity (Surplus/Deficit)	(2,749,124)	(684,757)	(331,030)	4,305,169	173,438	713,696
CUMULATED NET LIQUIDITY						713,696

2007 Liquidity Risk

	Less than <3 mnths	Betwn 3 to 6 mnths	Betwn 6 to 12 mnths	More than >1 Yr	Undefined Maturity	Total
CURRENT ASSETS						
Cash and Cash Equivalents	7,003,559	-	-	-	-	- 7,003,559
Treasury Notes, Bonds & Notes	-	49,380	276,876	4,036,046	-	- 4,362,302
Government Securities	-	-	-	411,101	-	- 411,101
Vanuatu Government Bonds	562,500	-	-	300,000	-	- 862,500
Interest Receivable	87,310	132,880	42	-	-	- 220,232
Other Receivables	77,530	6,560	-	84,058	-	- 168,148
Stock of Currency	-	-	-	50,187	-	- 50,187
Property, Plant and Equipment	-	-	-	734,646	-	- 734,646
SDR	-	-	-	-	186,354	186,354
Total (Current)	7,730,899	188,820	276,918	5,616,038	186,354	13,999,029

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

	Less than <3 mnths	Betwn 3 to 6 mnths	Betwn 6 to 12 mnths	More than >1 Yr	Undefined Maturity	Total
Liabilities						
Accrued Expenses	21,647	-	-	37,660	-	59,307
Due to Statutory Bodies	3	-	-	-	-	3
Due to Commercial Banks	4,117,679	-	-	-	-	4,117,679
Due to Govt of Vanuatu	99,671	1,272,484	564,555	-	-	1,936,710
Due to International Inst.	121,089	-	262,090	-	-	383,179
Reserve Bank of Vanuatu Notes	1,590,915	-	-	-	-	1,590,915
Currency Issued	4,688,956	-	-	-	-	4,688,956
Other Creditors	60,104	-	-	-	-	60,104
Employee Provisions	-	-	6,045	51,459	-	57,504
	10,700,064	1,272,484	832,690	89,119	-12,894,357	
Net Liquidity(Surplus/Deficit)	(2,969,165)	(1,083,664)	(555,772)	5,526,919	186,354	1,104,672
CUMULATED NET LIQUIDITY						1,104,672

Interest rate risk management

Interest rate risk is the risk of loss arising from the changes in interest rates. The bank limits interest rate risk by investing largely in short term investments of up to 90 days.

The bank's exposure to interest rate risk and the effective interest rates of financial assets and liabilities at the balance sheet date are as follows:

Financial assets:

- Cash and current accounts - floating interest rates.
- Short term deposits - fixed interest rates, maturing in 90 days or less.
- Treasury notes and bonds - fixed interest rates, maturing in 9 years or less.
- Vanuatu government bonds - fixed interest rates, maturing as detailed in note 10.
- Staff loans - fixed interest rates, maturing in 20 years or less.
- Statutory bodies/banks - fixed interest rates, maturing in 30 days or less.
- Government of Vanuatu - fixed interest rates, payable in 30 days or less
- Account No.1
- Redemption of bonds.

Financial liabilities:

- Domestic Institutions - fixed interest rates, payable in 30 days or less.

All other financial assets or financial liabilities are non-interest bearing.

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

2006 Interest Rate Risk

Fixed Coupon Instruments-2006

	Less than 1 Month VT'000'	Btwn 1 month and 3 months VT'000'	Btwn 3 months and 1 year VT'000'	Over 1 year VT'000'	Non interest bearing VT'000'	As At 31.12.06 VT'000'
ASSETS						
Cash and Cash Equivalents	5,418,960	2,041,293	-	-	-	7,460,253
Treasury notes, bonds and bills	-	-	104,908	3,004,510	-	3,109,418
Government securities	-	-	-	-	339,184	339,184
Vanuatu Government Bonds	-	-	-	862,500	-	862,500
Interest receivable	118,178	52,419	2,530	-	-	173,127
Other Receivables	2,894	2,983	-	103,009	5,204	114,090
Stock of Currency	-	-	-	-	70,329	70,329
Property Plant and Equipment	-	-	-	-	178,291	178,291
Special drawings right	-	-	-	173,438	-	173,438
	5,540,032	2,093,712	110,421	4,143,457	593,008	12,480,630
LIABILITIES						
Accrued Expenses	-	-	-	-	21,190	21,190
Due to Statutory Bodies	3	-	-	-	-	3
Due to Commercial banks	-	-	-	-	4,020,373	4,020,373
Due to Government of Vanuatu	603,944	-	-	-	960,419	1,564,363
Due to International institution	-	-	-	-	352,096	352,096
Reserve Bank Notes	714,786	954,403	116,107	-	-	1,785,296
Currency Issued	-	-	-	-	3,901,729	3,901,729
Other Creditors	-	-	-	-	60,439	60,439
Employee Provisions	-	-	-	-	61,445	61,445
Total Liabilities	1,318,733	954,403	116,107	-	9,377,691	11,766,934
EQUITY						
Issued Capital	-	-	-	-	100,000	100,000
General Reserve	-	-	-	-	613,696	613,696
Total Equity	-	-	-	-	713,696	713,696
Total Equity and Liabilities	1,318,733	954,403	116,107	-	10,091,387	12,480,630



Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

2007 Interest rate Risk

	Fixed Coupon Instruments-2007					
	Less than	Btwn 1	Btwn 3	Over 1	Non	As At
	1 Month	month and	months and	year	interest	31.12.06
		3 months	1 year		bearing	
	VT'000'	VT'000'	VT'000'	VT'000'	VT'000'	VT'000'
ASSETS						
Cash and Cash Equivalents	4,207,938	2,795,621	-	-	-	7,003,559
Treasury notes, bonds and bills	-	39,172	-	4,323,130	-	4,362,302
Government securities	-	-	-	-	411,101	411,101
Vanuatu Government Bonds	562,500	-	-	300,000	-	862,500
Interest receivable	87,310	132,922	-	-	-	220,232
Other Receivables	-	-	2,509	84,058	81,581	168,148
Stock of Currency	-	-	-	-	50,187	50,187
Property Plant and Equipment	-	-	-	-	734,646	734,646
Special drawings right	-	-	-	186,354	-	186,354
	4,857,748	2,967,715	2,509	4,893,542	1,277,515	13,999,029
LIABILITIES						
Accrued Expenses	-	-	-	-	59,307	59,307
Due to Statutory Bodies	3	-	-	-	-	3
Due to Commercial banks	-	-	-	-	4,117,679	4,117,679
Due to Government of Vanuatu	53,835	545,301	-	-	1,337,574	1,936,710
Due to International institution	-	-	-	-	383,179	383,179
Reserve Bank Notes	896,306	694,609	-	-	-	1,590,915
Currency Issued	-	-	-	-	4,688,956	4,688,956
Other Creditors	-	-	-	-	60,104	60,104
Employee Provisions	-	-	-	-	57,504	57,504
	950,144	1,239,910	-	-	10,704,303	12,894,357
EQUITY						
Issued Capital	-	-	-	-	100,000	100,000
F/Asset Reserve	-	-	-	-	139,557	139,557
Fair Value Reserve	-	-	-	-	224,797	224,797
General Reserve	-	-	-	-	640,318	640,318
Revaluation Reserve	-	-	-	-	-	-
Total Equity	-	-	-	-	1,104,672	1,104,672
Total Equity and Liabilities	950,144	1,239,910	-	-	11,808,975	13,999,029

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

Currency risk

Currency risk is the risk the value of financial instruments will fluctuate due to changes in foreign exchange rates.

The Bank incurs foreign currency risk on holdings of financial assets (principally external assets) that are denominated in a currency other than Vatu. The currencies giving rise to the risk are disclosed within the investment guidelines of the Bank.

The Bank does not hedge its exposure to exchange fluctuations in these currencies.

In accordance with the RBV Act, the task of maintaining the safety and liquidity of foreign reserve assets, as well as the returns from reserves asset management, are achieved through diversification of investment by entering into transactions in international capital and money markets. Analysis of risks is the process of managing the currency reserves by comparing factual risk levels with set limits. Credit risk is additionally limited by the separate minimum acceptable credit ratings and operational limits.

Currency concentration of RBV assets and liabilities as at 31 December 2007, and corresponding 2006 data. (In Vatu equivalents)

2006	VATU	USD	EUR	YEN	GBP	Other	Total
CURRENT ASSETS							
Cash and Cash Equivalents	-	2,343,604	953,481	991	388,322	3,773,855	7,460,253
Treasury Notes, Bonds & Notes	-	938,702	78,196	-	92,673	1,999,847	3,109,418
Government Securities	339,184	-	-	-	-	-	339,184
Vanuatu Government Bonds	862,500	-	-	-	-	-	862,500
Interest Receivable	47,470	24,541	3,834	-	1,428	95,854	173,127
Other Receivables	114,090	-	-	-	-	-	114,090
Stock of Currency(Notes & Coin	70,329	-	-	-	-	-	70,329
Property, Plant and Equipment	178,291	-	-	-	-	-	178,291
SDR	-	-	-	-	-	173,438	173,438
Total Assets	1,611,864	3,306,847	1,035,511	991	482,423	6,042,994	12,480,630
Accrued Expenses	21,190	-	-	-	-	-	21,190
Due to Statutory Bodies	3	-	-	-	-	-	3
Due to Commercial Banks	4,020,373	-	-	-	-	-	4,020,373
Due to Government of Vanuatu	1,564,363	-	-	-	-	-	1,564,363
Due to International Inst.	198,974	121,006	32,116	-	-	-	352,096
Reserve Bank of Vanuatu Notes	1,785,296	-	-	-	-	-	1,785,296
Currency Issued	3,901,729	-	-	-	-	-	3,901,729
Other Creditors	44,193	16,246	-	-	-	-	60,439
Employee Provisions	61,445	-	-	-	-	-	61,445
Total Liabilities	11,597,566	137,252	32,116	-	-	-11,766,934	
NET POSITION	(9,985,702)	3,169,595	1,003,395	991	482,423	6,042,994	713,696

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

2007	VATU	USD	EUR	YEN	GBP	Other	Total
CURRENT ASSETS							
Cash and Cash Equivalents	517	1,423,592	2,371,330	1,569	341,161	2,865,390	7,003,559
Treasury Notes, Bonds & Notes	-	2,359,863	1,809,535	64,551	87,604	40,749	4,362,302
Government Securities	411,101	-	-	-	-	-	411,101
Vanuatu Government Bonds	862,500	-	-	-	-	-	862,500
Interest Receivable	53,361	79,175	58,593	--	1,951	27,152	220,232
Other Receivables	168,148	-	-	-	-	-	168,148
Stock of Currency(Notes & Coin	50,187	-	-	-	-	-	50,187
Property, Plant and Equipment	734,646	-	-	-	-	-	734,646
SDR	-	-	-	-	-	186,354	186,354
Total Assets	2,280,460	3,862,630	4,239,458	66,120	430,716	3,119,645	13,999,029
Current Liabilities							
Accrued Expenses	59,307	-	-	-	-	-	59,307
Due to Statutory Bodies	3	-	-	-	-	-	3
Due to Commercial Banks	4,117,679	-	-	-	-	-	4,117,679
Due to Government of Vanuatu	1,936,710	-	-	-	-	-	1,936,710
Due to International Inst.	265,398	-	117,781	-	-	-	383,179
Reserve Bank of Vanuatu Notes	1,590,915	-	-	-	-	-	1,590,915
Currency Issued	4,688,956	-	-	-	-	-	4,688,956
Other Creditors	60,104	-	-	-	-	-	60,104
Employee Provisions	57,504	-	-	-	-	-	57,504
Total Liabilities	12,776,576	-	117,781	-	-	-	-12,894,357
NET POSITION	(10,496,116)	3,862,630	4,121,677	66,120	430,716	3,119,645	1,104,672

Notes to and Forming Part of the Financial Statements

For The Year ended 31 December 2007 (Expressed in 000's Vatu)

24. FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

The fair value of an instrument is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arms length transaction.

Quoted market values represent fair value when a financial instrument is traded in an organised and liquid market that is able to absorb a significant transaction without moving the price against the trader.

Financial Assets and Liabilities

The valuation of the Bank's financial assets and liabilities are discussed below:

Treasury notes, bonds & bills

The reported value of external reserves is considered to be its fair value due to the short term nature of the financial assets. Bonds are valued at mark to market.

Government bonds

The reported value of external reserves is considered to be its fair value.

Demand Deposits

The carrying value of deposits are considered to approximate their fair value as they are payable on demand.

Reserve Bank of Vanuatu Notes

The carrying value of the Reserve Bank of Vanuatu Notes are considered to approximate their fair value as they are redeemable on demand in accordance with the Bank's policy.

Currency in Circulation

The carrying value of Currency in Circulation is considered to be its fair value as reported in the accounts.

Other Financial Assets and Liabilities

The reported values of other financial assets and liabilities are considered to be its fair value.

25. EVENTS OCCURRING AFTER BALANCE DATE

There has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely to affect significantly the operations of the Bank, the results of those operations, or the state of affairs of the Bank, in future financial years.

