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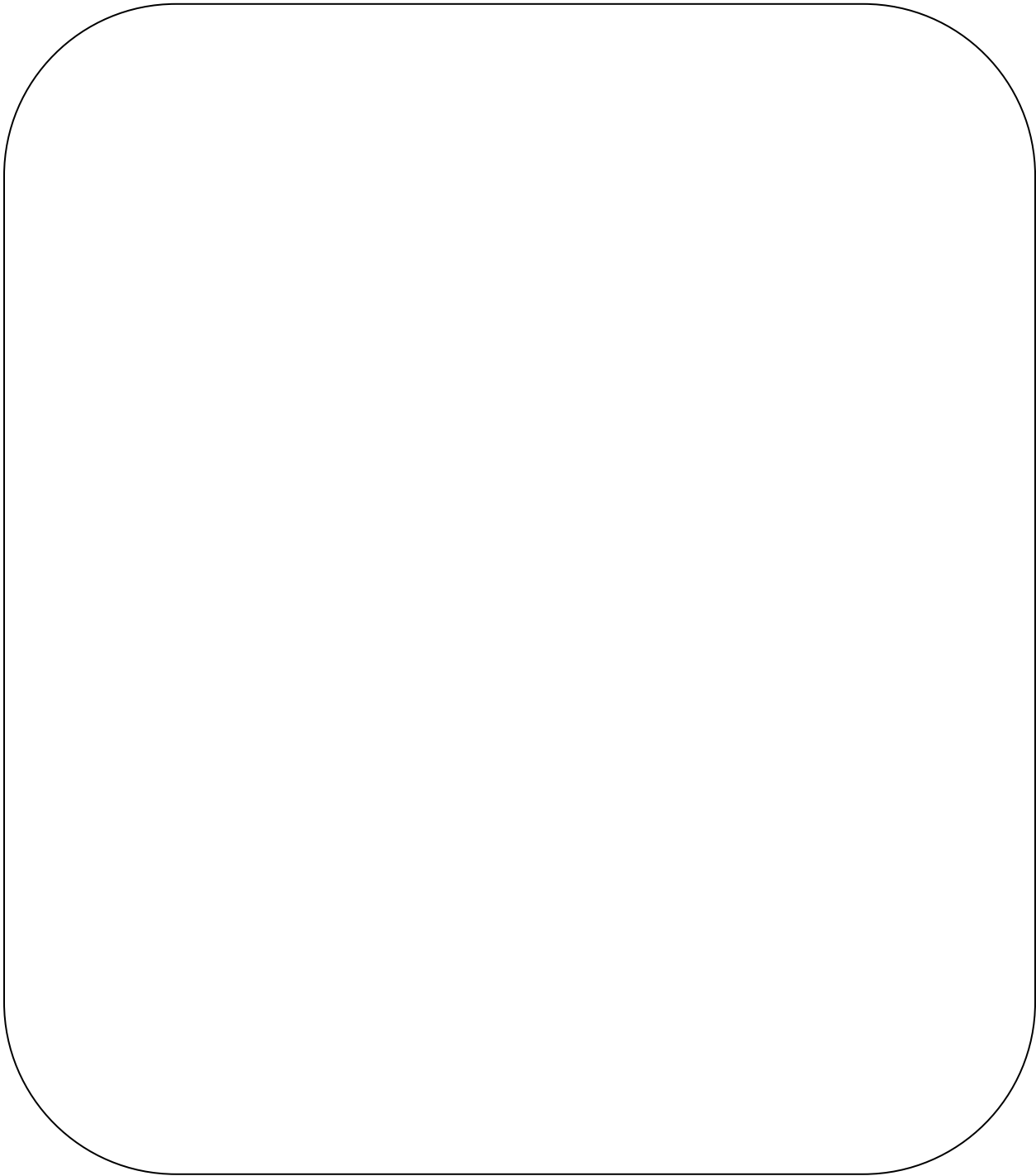
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| Q1 March 1987 | Press Announcement from Minister of Finance concerning The Cyclone UMA – Economic recovery program |
| | (A) Duty Exemptions on replacement materials & equipment |
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| | Banking Loans for reconstruction |
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| Q3 September 2000 | Notice to Commercial Banks concerning Money Laundering |
| Q4 December 2000 | Money is Lubricant of the economy |
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| Q2 June 2004 | Governor's Speech for Education Economics Workshop |

| | |
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| Q2 June 2004 | Governor's Speech for Media Freedom Day |
| Q2 June 2004 | Press Release on Biri Group |
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| Q4 December 2004 | Governor's speech for the association of financial supervisors of the pacific countries meeting |
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| Q1 March 2005 | Summary of Business Survey 2005 |
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1. Executive Summary

The financial turmoil in August and September threatens to detail what has been an excellent half decade of global growth. The problems in credit markets have been severe and there are expectations that global growth will slow in 2008 but remain at a buoyant pace. Growth in the United States is expected to remain subdued. Problems in the housing sector are more intense than previously expected and the disruption of credit is likely to have further impact. For the first time, China and India are making the largest country level contributions in the world growth. The main risk for the region is a sharper-than-expected global slowdown. China is also making their largest contributions in market price.

The dollar fell to a record low against the euro after trading losses drove down profit at the second-largest U.S. bank and raised speculations that the Federal Reserve will cut interest rates again. At the time of writing this report, the FED had cut interest rate by half a point in October 18th in trying to defend the pressure in housing markets. The world price for oil rose to \$76.76 in September from \$68.12 in June.

Domestic economic conditions continue to depict an expansion in the economy follow-on from the previous quarter. Growth is commendable, as it was achieved amidst the rising oil prices and strong rising international prices for major commodities which could contribute to increases in domestic price of goods. The consumer price index (CPI) rose by 0.2 percent over the quarter and 3.9 percent over the year. Rising prices for drinks & tobacco, recreational/education, housing utilities and food contributed significantly. Part of the inflation increase can be traced back to the impact of the increase in import duties in January which is expected to fully sink in next quarter.

For the third quarter of 2007, Government financed recorded growth on the overall fiscal operations showed a surplus of VT367.5 million. Some VT551 million above the deficit seen in the second quarter, and a similar VT463 million higher than in the same quarter last year. Improvement this quarter was mainly brought forward by expanded revenue through increase in cash grants and Value Added Tax collection.

Total money supply expanded further by 4.5 percent during the reviewed quarter as compared to a pick up in growth from 3.7 percent witnessed over the preceding

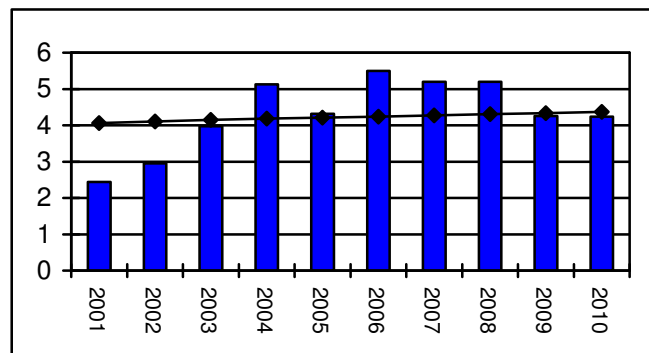
quarter. This growth positioned the volume of money supply at VT49,979.2 million at the end of the September quarter. Both determinants of money supply contributed to the aforementioned expansion, of which net foreign assets increased by 5.1 percent, while domestic credit by 0.7 percent.

The Balance of payments for September quarter of 2007 further expanded the official international reserves (net reserves) by MVT151 from last quarter. Along this line, there was also a shift in the monthly import cover from 7.5 to 7.6. The economy continues to expand given the magnitude of domestic activities currently ongoing and expected this year. The Current account deficit has marginally expanded; mainly due to the increase in trade deficits and reduced transfers offsetting improvements in services and income. The Capital and Financial account was reduced in half, despite another surplus for the quarter, although the decrease in this account financing was still adequate through other sources.

The International Economy

The world economy had continued to experience steady growth during the first half of 2007. Growth has been fairly broad –based across countries, with rapid growth in China and other emerging economies. Firm growth has been achieved in Europe and Japan. Growth in the United States remains below trend.

Figure 1: World Real Economic Growth and Forecasts



Source: IMF World Economic Outlook, April 2007
2007 and 2008 are the IMF forecast in July 2007

Consumer Price Inflation (CPI) rebounded in September. For the OECD countries, annual CPI inflation was 2.2 per cent, up from 1.8 per cent in August. However, CPI inflation excluding food and energy remained broadly unchanged at an annual rate of 1.9 per cent. Survey evidence on inputs from the

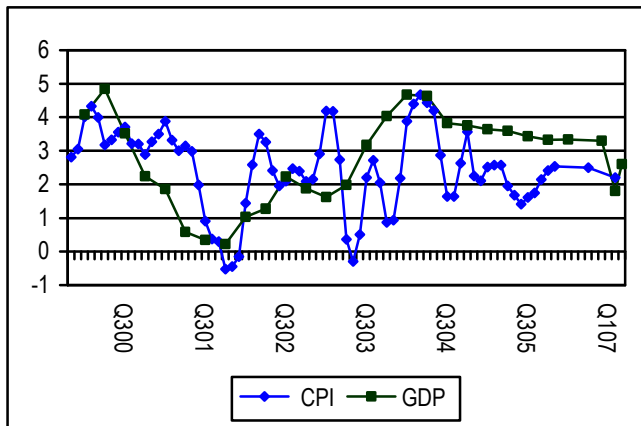
European Central Bank suggests that price pressure remain at an elevated level. The renewed increase in oil and other commodity prices is likely to lead to further upward pressures on global inflation.

The US Economy

According to the preliminary results of the Bureau of Economic Analysis there was a slight acceleration in real GDP growth for the third quarter 2007. This saw an increase in the output of goods and services produced by labour and property located in the US, at an annual rate of 3.9 per cent on the previous quarter and by 2.6 per cent on the same quarter last year.

This was attributed to the acceleration in personal consumption expenditures and exports, although these were largely offset by an increase in imports, and a larger reduction in residential fixed investment combined with a fall in construction of non residential structures. It would appear that the depreciation of the dollar has helped output remain high.

Figure 2: US GDP and CPI



Source: Bureau of Economic Analysis

Asia

Domestic growth in China appears to be slowing. However, GDP growth remains high, primarily due to the strong levels of exports accompanied with a fall in the level of imports. GDP growth for Q3 was 11.5 per cent up on the same quarter last year. If external demand is removed, it can be seen that domestic GDP is beginning slowdown. Credit and profit growth alongside FDI have all slowed. The growth in machinery and equipment imports give another indication that the economy is

beginning to slow to a more sustainable pace of growth in the period ahead.

Annual CPI for the month of September in China was 6.2 per cent (National Bureau of Statistics China).

Japan

Economic activity has continued to recover while inflation has remained close to zero. Output has been supported by domestic demand and increases in exports. The results of the Bank of Japan's September 2007 Tankan Survey showed that business conditions have remained firm in Japan, despite some loss of confidence among the small and medium sized enterprises.

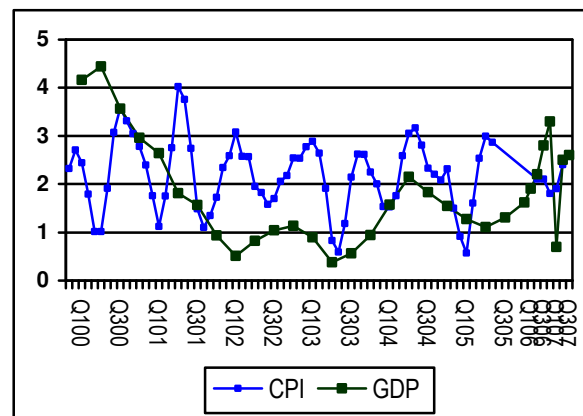
Inflation has remained subdued due to persistent downward pressures, especially on wages. The September CPI was down 0.2 per cent on the year.

Europe

GDP grew by 0.7 per cent in the Euro area during the third quarter of 2007 compared to the previous quarter. Compared with the same quarter of the previous year GDP grew by 2.9 per cent. This steady and robust growth is expected to continue with the decline in the industrial and construction sectors being more than countered in the uplift from the service industries.

It is expected that increasing oil prices and the global acceleration of food prices are likely to push inflation up in the coming months. EU annual inflation was up 2.6 per cent in the third quarter of 2007.

Figure 3: Euro-area GDP and CPI

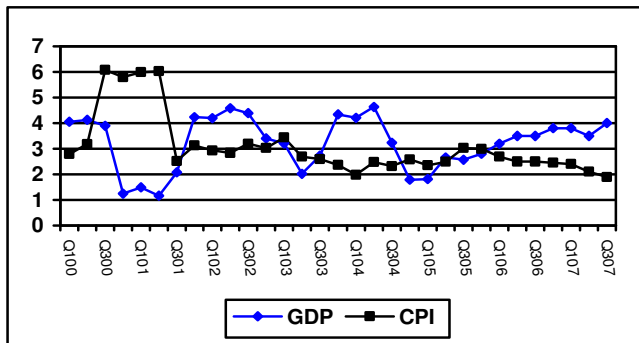


Source: The Economist August Issue

Australia's

CPI in September was 1.9 per cent as on the same month last year. This is slightly down on the month before where CPI was 2.1 per cent. Australia appears to be faring well in the turbulent economy, however, a slow down may be on the cards with GDP increasing 1 per cent on the quarter. That said GDP growth on the same quarter last year remained healthy at 4 per cent.

Figure 4: Australia CPI and GDP

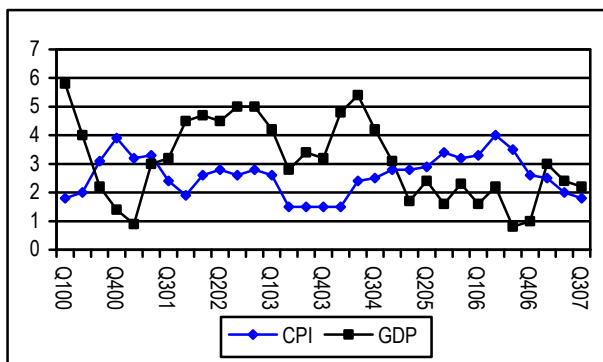


Source: Reserve Bank of Australia

New Zealand

CPI for the third quarter in 2007 increased by 1.9 per cent on the same month last year, a marginal decline from 2 per cent the previous quarter. GDP increased by 2.2 per cent on the same quarter last year, and 0.7 per cent on the quarter. As would be expected these figures are similar to Australia and show the resilience of both economies to the uncertainty in the global market.

Figure 5: New Zealand CPI and GDP

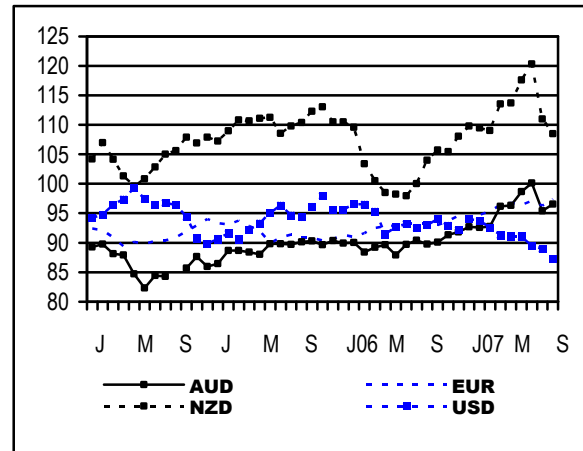


Source: Reserve Bank of New Zealand.

Market Developments

The pattern of monthly exchange rate movements of some of the world's most prominent currencies is shown below in 1990 prices (i.e. 1990=100).

Figure 6: Exchange Rates



Source: Bank of England

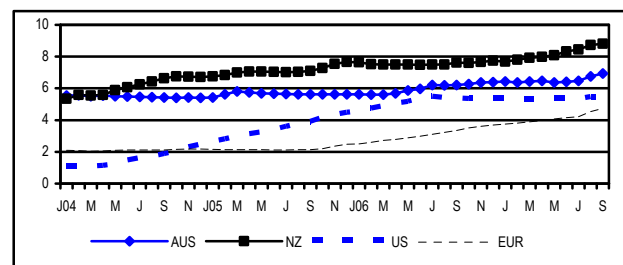
The US dollar continued on its downward path amid concerns over the strength of the US economy. Overall the US dollar has fallen by 10 per cent in value since the steady decline started in February 2006.

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.

Short Term Interest Rates

The graph below shows the pattern for short term interest rates for some of the world economies relevant to Vanuatu. The rate shown in each case is a 3 month or 91 day money market rate.

Figure 7: Short Term-interest Rates



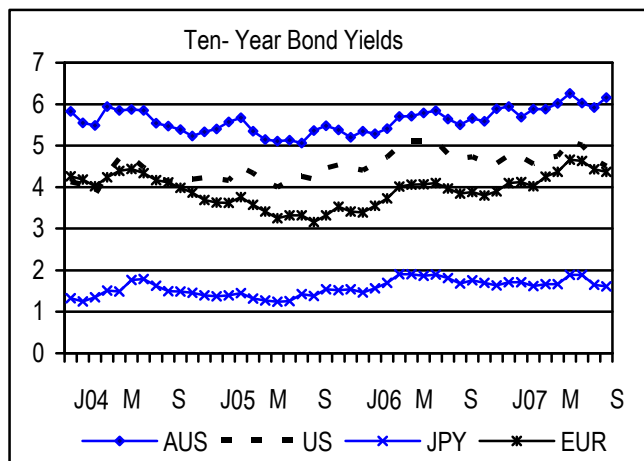
Source: Reserve Bank of Australia, Reserve Bank of New Zealand, European Central Bank, Bank of England

Over the period all of the interest rates continued on their upward trend. The EURIBOR increased by 14 per cent on the previous quarter. This demonstrates the increasing strength against the US dollar. In contrast the US short term rate increased by a modest 2 per cent over the quarter. New Zealand and Australia increased by 6 per cent and 8 per cent respectively, demonstrating their ability to weather the economic uncertainty in the period.

Long term interest rates

The graph below shows the changes in long term interest rates in some of the world's major economies.

Figure 8: Long-Term Interest Rates



Source: Reserve Bank of Australia, Reserve Bank of New Zealand, Bank of England, European Central Bank.

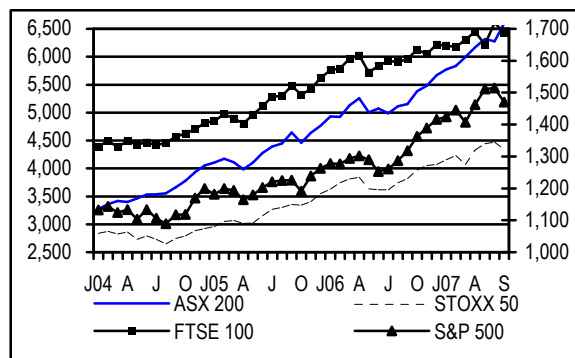
In contrast to the short term interest rates, the 10 year government bond yields have all declined. Australia experienced the smallest decline, of only 2 per cent, while Japan experienced the largest fall at 15 per cent. The US and the Euro fell by 12 and 16 per cent respectively.

It is suspected that this stems from the persisting economic turbulence driven by the weak dollar and increasing price of oil. This also corresponds to the increasing interest rates which will increase the incentive for investors to hold money rather than investing it in long term assets.

Stock Markets

The following graph shows the movements in share indices from some of the world's largest markets.

Figure 9: Stock Markets



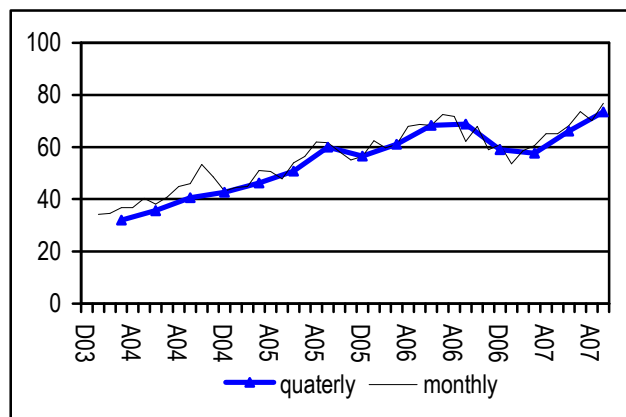
Source: Financial Times, European Central Bank, Reserve Bank of Australia.

Despite the turbulent times in the stock market all of the indices increased over the third quarter. The only exception was the S&P 500 which was slightly down in September. Growth in the ASX 200 continues to outperform the other markets as the Australian economy rides the economic downturn well. There is still a great deal of uncertainty in the market place with much speculation on the strength of the US dollar and concerns over the sub prime lending market. It is expected that the markets will be increasingly sensitive until this is resolved.

Oil Markets

Speculation on the price of oil led to many analysts claiming we would inevitably see a \$100 barrel. Oil prices have risen by 60per cent in 2007. Brent Crude peaked at \$98.62 on 7th November prompted by fears raised over the ever weakening dollar.

Figure 10: Average Spot Price for Crude Oil (USD/barrel)



Source: World Bank Pink Sheet

The average spot price for a barrel of oil over the third quarter of 2007 was \$73.50, an increase of 11 per cent on the previous quarter.

Key Interest Rates

The US Federal Reserve cut interest rates by 50bps to 4.75 at its September meeting, with the aim of reducing the impact of the liquidity squeeze on the economy. The accompanying statement explained that the cut was to “help forestall some of the adverse effects on the broader economy that might otherwise arise from the disruptions in the financial markets”. Additional signs of weakness in Q4 are likely to prompt further rate cuts, with many analysts speculating a further cut before the end of the year.

Unemployment in the Euro zone is currently at a 15 year low and rapid increases in the money supply are indicative of inflationary pressures going forward so it seems unlikely that the ECB will cut rates in the near future.

Growth in the Australian economy has, for some time, been aided by strong global demand and high commodity prices. Since August, sentiment in financial markets has improved although it still remains fragile. As a consequence it is likely that inflationary pressures will begin to grow and analysts expect a 25bps within the next six months.

| Key Interest Rates (per cent, end of period) | | | | | |
|--|-------------------|----------------|-----------------|---------------|--------------------------|
| | US Fed Funds Rate | Euro Refi Rate | Aust. Cash Rate | N Z Cash Rate | Vanuatu Red-iscount Rate |
| 2006 Q1 | 4.75 | 2.50 | 5.50 | 7.25 | 6.25 |
| Q2 | 5.25 | 2.75 | 5.75 | 7.25 | 6.00 |
| Q3 | 5.25 | 3.00 | 6.00 | 7.25 | 6.00 |
| Q4 | 5.25 | 3.50 | 6.25 | 7.25 | 6.00 |
| | | | | | |
| 2007 Q1 | 5.25 | 3.75 | 6.25 | 7.50 | 6.00 |
| Q2 | 5.25 | 4.00 | 6.25 | 8.00 | 6.00 |
| Q3 | 4.75 | 4.00 | 6.75 | 8.25 | 6.00 |

Sources: US Federal Reserve, European Central Bank, Reserve Bank of Australia, Reserve Bank of New Zealand and Reserve Bank of Vanuatu

New Zealand is still facing strong inflationary pressures which are countered by strong vulnerabilities to the global markets in terms of commodity prices. It is expected that high and restrictive interest rates remain for some time.

1. Domestic Economic Development

1.1 Real Economy

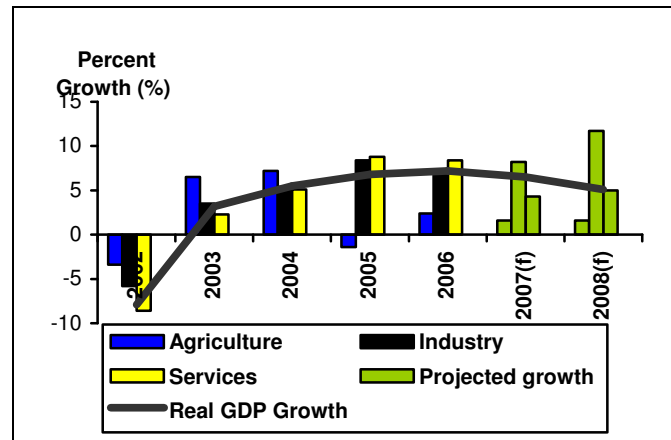
Economic conditions continue to depict an expansion in the economy follow-on from the previous quarter. Growth is commendable, as it was achieved amidst the rising oil prices and strong rising international prices for major commodities which could contribute to increases in domestic price of goods. Inflation was slightly contributed by the high fuel related costs associated with housing utilities such as electricity and the on-going economic activity growth which continues to drive up domestic demand.

Wholesales and Retail trade, Hotels and Restaurants and government services continue to contribute significantly to the country's GDP as imports of goods continues to rise to accommodate the increasing economic activity and demand for services. Over the first nine months of the year, imports increased by 24 percent compared to the same period of last year. This is associated with the increase in visitor arrivals this year to the two main towns: Port Vila and Luganville. Total non-resident was higher by 3.3 percent in the first 9 months of 2007 over the same period of 2006.

Over the third quarter, Agriculture sector through commercial agriculture, forestry and logging shows little sign of improving from the previous quarter. The drop in copra and beef production over the reviewed quarter was outweighed by the improvement in cocoa, kava, logging and coconut oil exports after farmers tend to supply the coconut oil mills after copra prices increased. The emergence of the services sector continues to drive growth was contributed by the continuous investment on tourism, land development, infrastructure and economic related sectors.

As predicted in the previous quarter, construction the largest sub-sector in the Industry sector is expected to strengthen inline with the current economic perspective of real GDP growth estimated at 6.5 percent in 2007 from the 7.2 percent in 2006. So growth would be broad-base, with all sectors contributing to positive growth in the medium term with growth driven by Industry and Services sector followed by the agriculture sector.

Figure 11. GDP Growth Rate



Source: Ministry of Finance and Economic Management (MFEM), Department of Economic and Sector Planning (DESP), National Statistics Office

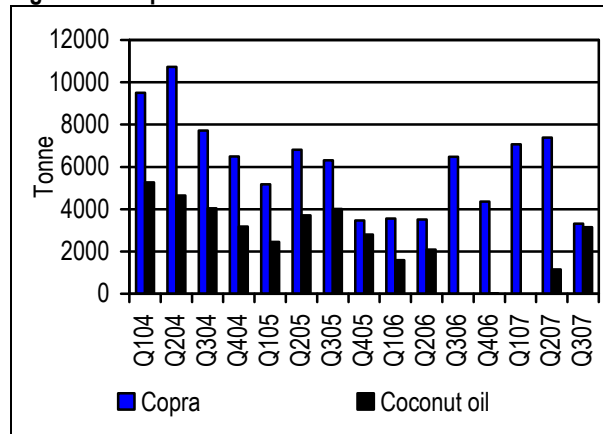
For the second consecutive quarter, total non-resident visitors showed a drop mainly attributed by the decline in cruise-ship arrivals. Although cruise-ship arrivals dropped over the quarter, air visitors continue to show an impressive improvement from the previous year supported by the continuous promotion of Vanuatu Tourism Office of Vanuatu as a tourist destination and the increase in air-craft capacity that show new flights introduced to Brisbane, Australia, a major tourism market for Vanuatu.

The effect of price increases was a result of price increases in the Drinks and Tobacco group in the first quarter is slowly easing since import tariff of like-goods were increased. Inflation over the third quarter was a result of price increases in Recreational, Education, Transport and Communication and Housing Utilities.

1.2a. Copra and Coconut Oil

Over the third quarter of 2007, copra production dropped from 7,387 tons in the second quarter to 3,317 tons valued at VT95.6 million. Likewise, production dropped over the same period of last year. Copra exports also showed a drop from 2,698 tons exported in the previous quarter to 1,007 tons valued at VT218 million. The average domestic price for copra increased from VT26,973 per ton to VT28,518 per ton. Average world price for copra continues to show an increasing trend from US\$ 599.2 per ton to US\$607.2 per ton.

Figure 12: Copra & Coconut Oil Production



* Coconut oil is export figures
Source: VCMB, National Statistics Office

While improvement in the coconut oil sector was noted in the second quarter, the pick up in supply of copra sold to the two coconut oil mills attributed to the increase in output from coconut oil manufacturing sector during the quarter. As a result, coconut oil export more than double in the third quarter to record a total of 3,153 tons exported valued at VT198 million over the third quarter, which was an improvement from the previous year. Over the quarter, average price for coconut oil in the world market increased from US\$900.80 per ton to US\$922.80 per ton, an upward trend inline with copra price.

1.2b. Cocoa

Cocoa production for the third quarter increased from 320 tons to 498 tons valued at VT36.8 million. Average domestic price of copra declined slightly from VT92,737 per ton to VT92,649 per ton. Level of production increased over the same period of the previous year by 81 tons. Likewise, cocoa exports increased from 308 tons to 742 tons valued at VT133 million. Average world price for cocoa declined slightly from US\$200.0 per ton to US\$199.9 per ton.

| Domestic Data Annual | 2002 | 2003 | 2004 | 2005 | 2006 |
|--------------------------------|-------------|-------------|--------|--------|--------|
| Real GDP Growth (%) | -7.9 | 3.2 | 5.5 | 6.8 | 7.2 |
| Annual inflation rate (%) | 2.3 | 2.9 | 0.8 | 1.8 | 1.8 |
| <u>Production</u> | | | | | |
| Copra(t) | 25,608 | 28,925 | 36,822 | 21,482 | 19,462 |
| Cocoa(t) | 868 | 1,346 | 865 | 926 | 1,314 |
| Beef(t) | 2,531 | 3,099 | 2,984 | 3,185 | 2,708 |
| Coconut oil exports (t) | 9,856 | 7,725 | 17,111 | 12,967 | 3,696 |
| Kava exports (t) | 601 | 491 | 828 | 686 | 575 |
| Air arrivals(no.) | 49,462 | 50,400 | 60,670 | 62,082 | 68,179 |
| Cruise arrivals(no.) | 49,447 | 51,995 | 37,870 | 63,554 | 85,922 |
| Hotel Occ. Rate | 44.20% | 46.50% | 51.90% | 52.30% | 51.5% |
| Energy Consumption | 41,874 | 41,341 | 42,849 | 44,669 | 45,906 |
| <u>Quarterly</u> | <u>2006</u> | <u>2007</u> | | | |
| | Q306 | Q406 | Q107 | Q207 | Q307 |
| Real GDP Growth (%) | - | - | - | - | - |
| Inflation rate (yearly - %) | 2.9 | 1.8 | 3.4 | 4.0 | 3.9 |
| Inflation rate (quarterly - %) | 0.2 | 0.3 | 2.1 | 1.3 | 0.2 |
| <u>Production</u> | | | | | |
| Copra(t) | 6,484 | 4,357 | 7,071 | 7,387 | 3,317 |
| Cocoa(t) | 378 | 244 | 49 | 320 | 498 |
| Beef(t) | 895 | 735 | 727 | 789 | 758 |
| Coconut oil exports(t) | - | 22 | - | 1,154 | 3,153 |
| Kava exports (t) | 166 | 119 | 32 | 70 | 98 |
| Tourist arrivals(no.) | 18,712 | 19,486 | 16,482 | 18,807 | 24,682 |
| Cruise arrivals(no.) | 22,506 | 18,625 | 26,215 | 21,093 | 12,588 |
| Hotel Occ. Rate (room) | 50.00% | 57.6% | Na | na | na |
| Energy Consumption | 11,500 | 11,460 | 13,062 | 10,965 | 12,228 |

Source: National Statistics Office

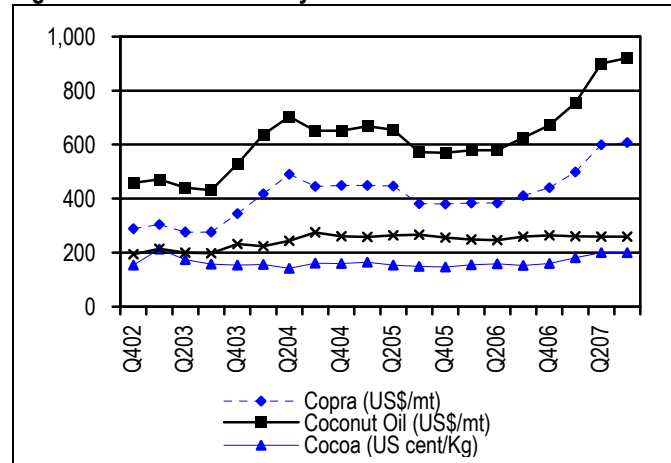
1.2c. Kava

Over the third quarter, the kava sector continues to receive high demand from both the domestic market for local consumption while both major kava export markets of Fiji and New Caledonia, continues to remain imperative. Kava exports increased from 70 tons to 98 tons valued at VT137 million. As compared to the previous year, production exports dropped by 68 tons. This is yet attributed by various policy implications concerning kava export followed by the ban by the Australian Government on kava exports into Australia. As a result, kava exports dropped by 41 percent over the same quarter of the corresponding year.

1.2d. Beef

Total beef production dropped by 3.9 percent from a revised 789 tons in the previous quarter to 758 tons in the third quarter. Over the same quarter of the previous year, Santo Meat Packers Ltd Abattoir recorded a drop by 42 percent in the number of cattle received for whilst VAL Pacific Limited in Port Vila recorded an increase of 7.6 percent over the same period. Overall, total beef production dropped by 21 percent over the same quarter of the previous year. Domestic and export markets remain imperative throughout the June quarter, though the cattle supply shortage to the abattoirs may drive up price of beef in the domestic market. Likewise the increase in demand could drive price in the world market especially from major markets. Vanuatu's major market for beef includes Australia, New Zealand, Japan and the Pacific island countries such as Solomon Islands and New Caledonia and Fiji. Beef exports increased from 151 tons in the previous quarter to 153 tons valued at VT54 million. The average price for beef in the world market increased from US\$259.90 per ton to US\$260.30 per ton, although price was relatively stable over the last few years.

Figure 13: World Commodity Price

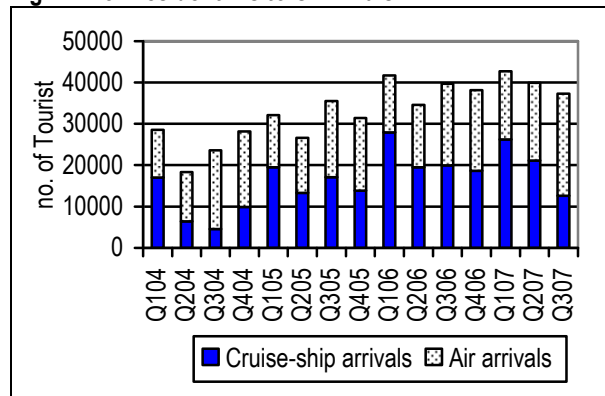


Source: World Bank Commodity Price

1.2e. Tourism

Over the third quarter of 2007, total non-residential visitors to Vanuatu dropped by 7 percent from 39,900 visitors in the previous quarter to 37,270. This level is lower by 6.0 percent from the same period of last year. The decline was driven by a drop noted in day visitors by 40 percent to 12,588. This was a result of the decline in cruise-ship visits during the month of August after a cyclone affecting one of the P&O cruise-ship upon its voyage to Port Vila. As a result, the cruise-ship underwent maintenances and repairs before recommencing its voyage to Port Vila. On the other hand, air visitors continued to show significant improvement from the previous quarter. At a 3-quarter high, visitors arrivals by air were recorded at 24,682, higher over the previous quarter and over the same period of last year by 31 percent and 30 percent, respectively. This growth was attributed by the continuous promotion by VTO of Vanuatu as a tourist destination and new additional flights by Air Vanuatu to Brisbane buoyed by the code-sharing partnership with air carriers such as Air New Zealand, and low frill fares by Virgin Blue, Vanuatu continues to receive more visitors from its major markets: New Zealand (up 84 %), Europe (up 6-%), Other Pacific countries (up 57%), Japan (up 55%), while Australia (up 17%) continues to remain as Vanuatu's major tourism market mainly holiday visitors which recorded a 36 percent increase from the last quarter.

Fig 14: Non-resident Visitors Arrivals

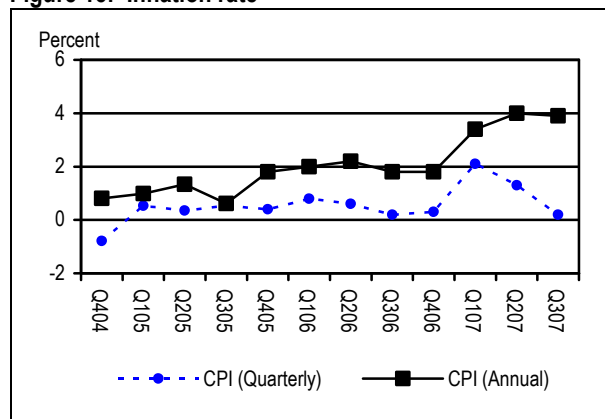


Source: National Statistic Office

1.2f. Inflation

The Inflation rate eased in the third quarter from 4.0 percent to 3.9 percent. Likewise, quarterly inflation eased from 1.3 percent to 0.2 percent in the reviewed quarter. Apart from the lower prices in clothing and household supplies, the slight ease in the price for food and Drinks & Tobacco has an easing impact on overall prices. This outweighs the marginal price increases in Recreation/Education/Health, Housing Utilities and Transport and Communication. The increase in CPI over the third quarter was contributed by increases shown for the following expenditure groups over the same quarter of the last year: Drinks & Tobacco (7.3%), Recreational/Education/Health (5.9%), Housing Utilities (4.3%), Food (3.6%), and Transport and Communication (3.0%). While slight increases were shown for clothing (-0.1%) and Household Supplies (-1.2%).

Figure 15: Inflation rate



Source: National Statistics Office

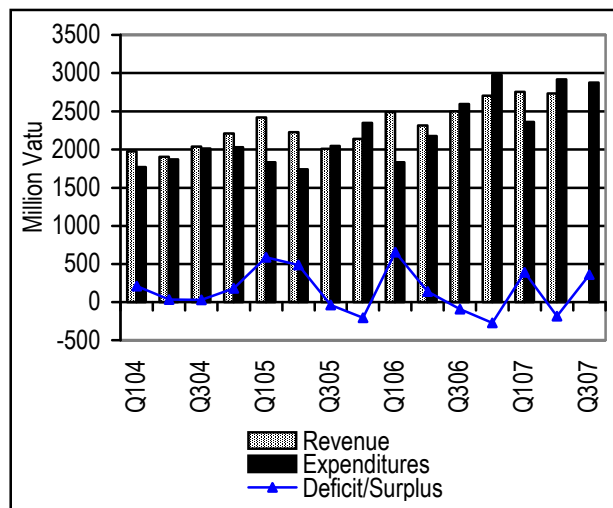
3.2. Fiscal Operations

Since 2003 Vanuatu has been enjoying its longest period of sustained growth since it gained independence in 1980 with GDP averaging 5.6 per cent per annum. Alongside this the Vanuatu Government continues to incur a positive operating account with the Reserve Bank of Vanuatu.

For the third quarter of 2007 the overall fiscal operations showed a surplus of VT367.5 million. Some VT551 million above the deficit seen in the second quarter, and a similar VT463 million higher than in the same quarter last year. This increase in government funds stems from the increase in revenues and grants, largely accounted for by a 22 per cent increase in tax revenues on the previous quarter. This could be from an increase in consumer expenditure (either from buying more goods or the same basket of good has become more expensive) increasing the VAT returns.

Expenditure and Net Lending was down by 1 per cent on the previous quarter to VT2.8 billion. This was largely underpinned by a fall of 5 per cent in recurrent expenditure. Development expenditure offset this somewhat by doubling on the previous quarter to VT 190.5 million in the third quarter of 2007.

Figure 16: Government Expenditures and Revenue.

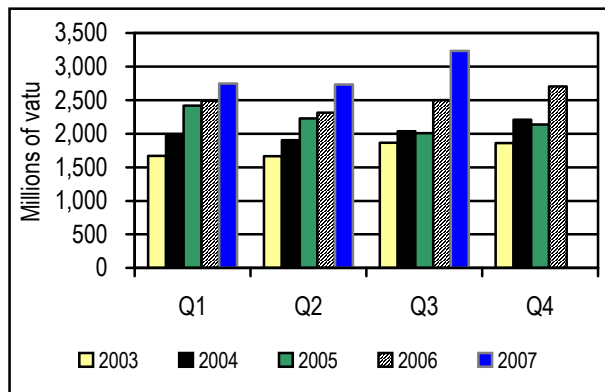


3.2a. Revenue

As previously mentioned the third quarter of 2007 saw a 22 per cent increase in tax revenues on the previous quarter, and 42 per cent increase on the same quarter last year. However, there was a slight decline in non tax revenue (3 per cent) on the previous quarter now running at VT 204.5 million. Grants from abroad were VT 213.2 million this saw the total

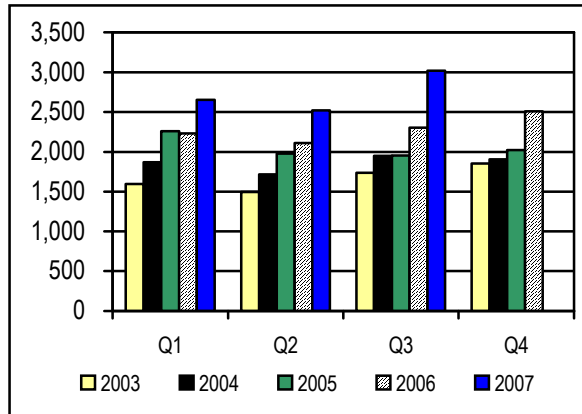
position for Revenue and Grants increase to VT 3232.7 some 18 per cent higher than the previous quarter.

Figure 17: Revenue and Grants



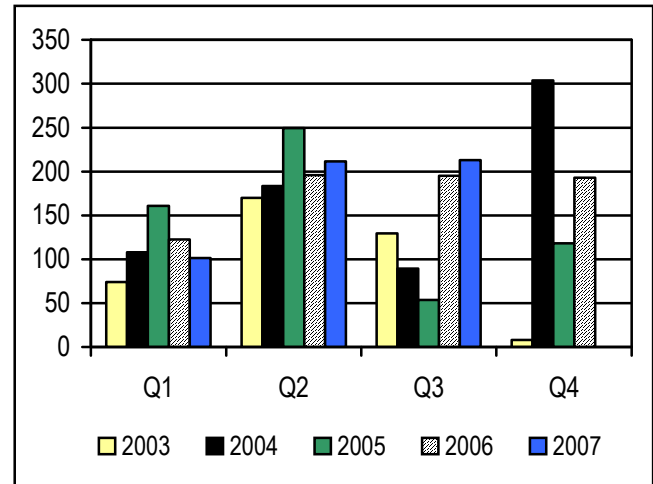
New revenue initiatives undertaken by the Government are increases in import duties and excise taxes on some imported items, to boost domestic revenue in light of the increase in the overall budget. Improved administrative systems and strengthening of compliance in Government ministries are also expected to contribute to revenue collection couple with another positive economic growth.

Figure 18: Domestic Revenue



Non tax revenue was down on both the quarter and the year, falling by 3 and 36 per cent respectively, to VT204.5 million. Tax revenue increased to just over VT 3 billion. This was 31 per cent higher than the same quarter in 2006 and 20 per cent higher than the second quarter of this year.

Figure 19: Grants



Grants from abroad were VT 213.2 million, an increase of 1 per cent on the previous quarter and 9 per cent higher than the previous year. This accounts for almost 7 per cent of total revenue and grants.

3.2b. Expenditures

Total expenditure for the third quarter was VT 2865.2 million. This was slightly down on the previous quarter and 10% higher than the same quarter in 2006.

Total recurrent expenditure was 5 per cent down on the month and 20 per cent up on the year at VT 2674.7 million.

The proportion of recurrent expenditure that salaries and wages account for increased to 67 per cent. Expenditure on salaries and wages was VT 1472.5 million 7 per cent higher than quarter three in 2006, but 16 per cent lower than quarter two.

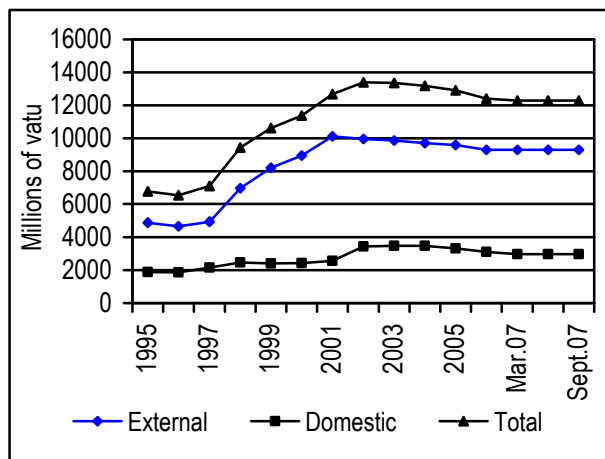
3.2c. Financing

The overall finance position for the government for the nine months of 2007 saw a healthy surplus of VT 514.7 million, 62 per cent of this came from domestic financing. Continuous tight fiscal control by the Department of Finance had ensured that the Government had not resorted to the overdraft facility with the Reserve Bank of Vanuatu. Another main instrument commonly utilized by the central government to finance its deficits is domestic borrowing.

3.2.d. Outstanding Government Debt

Total outstanding external debt of the country remains at the estimated level of VT1.2 billion. This is approximately 26.5 percent of nominal GDP. External debt accounts for an estimated 75.7 percent. Domestic debts in terms of bond holding remained at VT2, 982.9 million. From the total bond holding, corporate bodies have a share of 54.6 percent, the RBV 28.9 percent, commercial banks 16.4 percent and others 0.1 percent.

Figure 20: Public Debt



Total external debt of the country remains at approximately VT 9,298.0 million. There are no new debts given the high amount of domestic debt that will mature in 2008.

MONETARY DEVELOPMENTS

Broad money supply expanded further by 4.5 percent during the reviewed quarter, this represents a pick up in growth from 3.7 percent witnessed over the preceding quarter. This growth positioned the volume of money supply at VT49,979.2 million at the end of the September quarter. Both determinants of money supply contributed to the aforementioned expansion, of which net foreign assets increased by 5.1 percent, while domestic credit, 0.7 percent. Owing to the quarterly expansion in money supply, the yearly growth rate up to the September quarter of 2007 was 12.5 percent, a substantial growth from 4.6 percent recorded over the year to the June quarter of 2007.

Commercial Banks liquidity¹ further contracted during the quarter as the Reserve Bank continued to be aggressive its Open Market Operation (OMO), this is indicated by a substantial increase in the volume of new RBV notes issued in the market during the quarter.

Short-term interest rates have continued to depict a declining trend during this quarter ever since the previous quarter, seeing that bids for the RBV notes have continued to remain very competitive in OMO's conducted during the quarter. Quarterly interest rates of Commercial banks on the other hand have increased, given the further widening of interest rate spread during the quarter.

The Reserve Bank during the quarter continued to maintain the current monetary policy stance by upholding the rediscount rate at 6.00 percent.

Determinants of Money Supply

Net Foreign Assets

Total net foreign assets (NFA) of the banking system rose by 5.1 percent to reach VT34,645.5 million at the end of the reviewed quarter. This trend was attributable to expansions in the NFA holdings of both the monetary authorities and commercial banks, respectively. By means of this increase the annual growth of NFA noted a 9.9 percent increase over the year to September 2007, in contrast to a growth of merely 0.5 percent recorded over the year to the June quarter of 2007

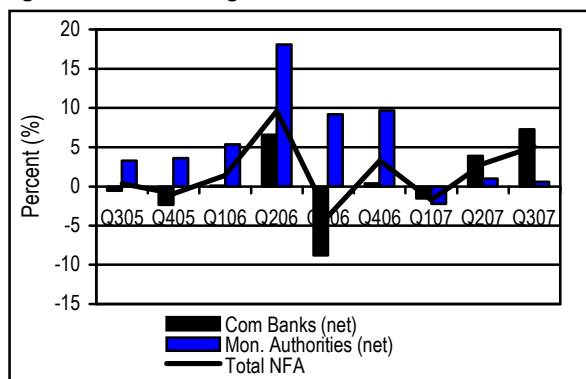
The NFA holdings of the monetary authorities, (Reserve Bank (RBV)) increased further by 0.6 percent to level at VT10,890.8 million during the reviewed quarter. In comparison to the June quarter, the volume of net foreign exchange inflows reached almost VT186 million, this as an indication that net foreign exchange purchases continued to surpass foreign exchange sales. Major inflows during the quarter were sourced from few bilateral deals and funds towards the establishment of the new domestic bank. The outflows of foreign exchange were through Government debt services and foreign exchange sales to commercial banks.

The abovementioned improvement in net foreign reserves prompted months of import cover to increase to 7.61 percent in September 2007 as compared to 7.52 months as recorded over the previous quarter. Furthermore, monetary authorities

¹ Commercial banks liquidity consists of commercial banks excess reserves and holdings of RBV notes.

NFA have risen substantially by 9.0 percent from the same quarter of 2006.

Figure 21: Net Foreign Assets

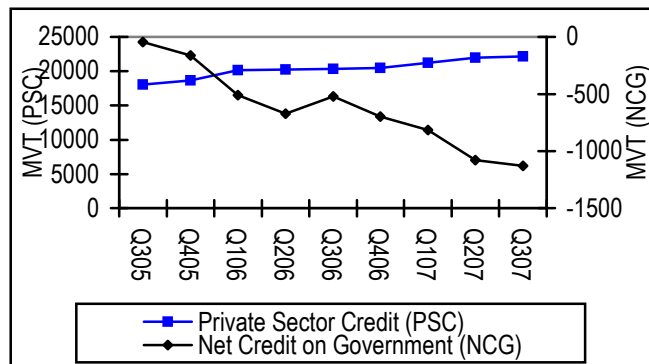


Commercial Bank's NFA expanded by 7.3 percent, from the previous quarter to level at VT23,754.7 million, at the end of the reviewed quarter. The said improvement was driven mainly by a decline in commercial banks' liabilities to non-residents, in particular balances due to non-resident banks which declined substantially by 46.8 percent. This decline was principally attributed to a repayment of a financing arrangement by a domestic bank to their head office overseas at the end of the September quarter. In addition, commercial banks' holdings of foreign assets expanded by 3.4 percent. Commercial banks' NFA moreover improved by 10.2 percent from the corresponding quarter of the previous year.

Domestic Credit

Domestic credit noted a deceleration in growth from 3.5 percent noted during the June quarter to 0.7 percent recorded during the September quarter. The slow growth was due to offsetting movements in its components, of which increases in credit to private sector and municipalities were offset by declines in net credit to the government and credit to non-financial public enterprises. Domestic credit furthermore expanded by 7.2 percent against the level recorded over the corresponding quarter of 2006.

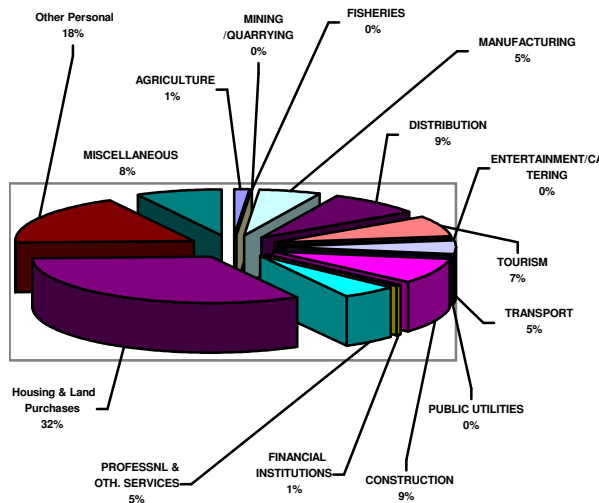
Figure 22: Domestic Credit



The Government's net credit position vis-à-vis the banking system improved further during the reviewed quarter. This improvement was attributed to a decline in the Government's net lending from the monetary authorities by 4.9 percent. It's net lending from commercial banks in contrary increased by 9.7 percent. The improvement in the Government's net credit position with the Reserve Bank continued to reflect the accumulation of Government deposits with the Bank during the quarter. In accordance with the improvement in the Government's net position mentioned above, Government finance statistics recorded a budget surplus of VT356.9 million at the end of the third quarter. The Government's net lending position with the banking system has hitherto remained comfortable as compared to the corresponding quarter of 2006.

Outstanding loans and advances granted to the private sector witnessed a slow down in growth rate from a 3.6 percent recorded over the previous quarter to a mere 0.8 percent experienced during the reviewed quarter. The current growth positioned the volume of loans and advances at VT22151.3 million at the end of the September quarter. The deceleration in private sector credit growth was predominantly attributed to repayments of major loans at the end of the quarter. Economic sectors which contributed to the quarterly growth were; the manufacturing sector, of which loans rose by 5.9 percent, transport sector (9.0%), public utilities (22.3%), construction (2.1%). Housing and land loans and other personal sectors received increases in loans of 13.3 percent and 8.5 percent, respectively. The annual growth of loans to September 2007 was 8.9 percent; this continues to reflect the positive growth currently witnessed in the economy.

Figure 23: Breakdown on sectoral Loans

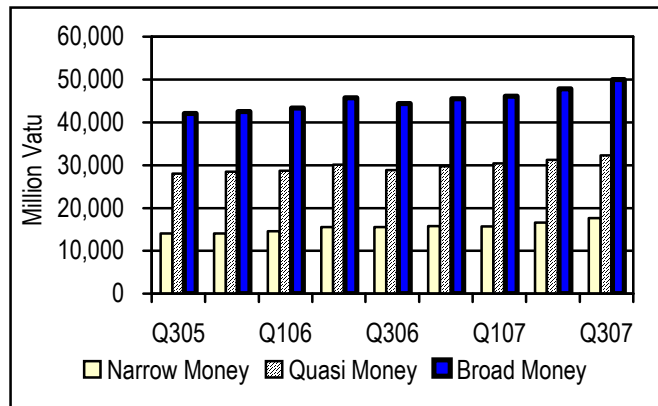


The four major sectors which consume the largest share of total loans during the quarter were housing and land loans, which have maintained the leading share of total loans for the last five years. During this quarter it increased its share to 32 percent, up from 27.0 percent noted in the previous quarter. This corresponds to the reduction in interest rates to the housing and land market effected during the second quarter. The second largest share of 17.9 percent goes to other personal sectors, which noted an increase of 100 basis points from the preceding quarter. This trend is an indication of mounting personal consumption during the quarter. The construction sector supersedes the tourism sector to grab the third largest share of 8.9 percent, while the fourth largest share was maintained by the distribution sector, though the share declined from 10.4 percent noted in the second quarter to 8.6 percent in the reviewed quarter.

Components of Money Supply

Both components of money supply recorded quarterly expansions hence attributed to the overall growth in money supply during the reviewed quarter.

Figure 24: Money Supply



Narrow money supply which represents the volume of money flowing into the economy expanded further by 6.8 percent to level at VT17,650.1 million during the September quarter. This denoted a pick up in growth rate from 5.6 percent recorded in the previous quarter. Demand deposits which are the major element of narrow money increased by 7.6 percent, seeing that the level of deposits denominated in both the local and foreign currency went up by 9.4 percent and 7.5 percent, respectively. Currency outside the banking system also rose by 3.3 percent from the level recorded in the previous month. The abovementioned increases in the components of narrow money signified the increasing preferences of residents with regards to gaining direct access to immediate cash to cater for the current growth in economic transactions; this is well supported by the growth in private sector credit. In addition, to accommodate for the rising domestic consumption seeing that Value Added Tax returns have increased by 13.5 percent during the quarter, as well as the increase in imports of almost 12 percent to accommodate for domestic demand. Owing to the quarterly improvement in narrow money, the annual growth rate increased to 13.7 percent in the year to September 2007 in contrast to 6.3 percent in the year to June 2007.

Quasi-money also grew by 3.3 percent from the previous quarter to reach VT32,329.1 million at the end of the September quarter. This improvement was attributable to expansion in time and savings deposits denominated in both the Vatu and foreign currency by 4.7 percent and 2.2 percent, respectively. The growth quasi-money in local currency reflected attractive interest rates offered on fixed term deposits by one bank, this is also revealed by the quarterly increase in the weighted average interest rate on fixed deposits. Quasi-money moreover expanded by 11.8 percent as compared to the corresponding quarter of the previous year.

Deposits with Commercial Banks

Commercial Bank's liabilities with regards to resident's deposits (exclusive of Government deposits) expanded by 4.6 percent during the quarter to reach VT46,669.9 million. Deposits of individuals and joint accounts hitherto maintained the leading share of deposits with 47 percent. The second largest share of 41 percent was maintained by the private sector companies. The third and fourth largest shares were acquired by non-financial public enterprises and other sectors by 7.2 percent and 4.6 percent, respectively. Municipalities attained the least share of deposits with 0.1 percent.

Interest Rates

Subsequent to downward movements in Interest rates witnessed during the second quarter of 2007, interest rates have again increased during the reviewed quarter. This is characterized by the widening of interest rates spread during the quarter.

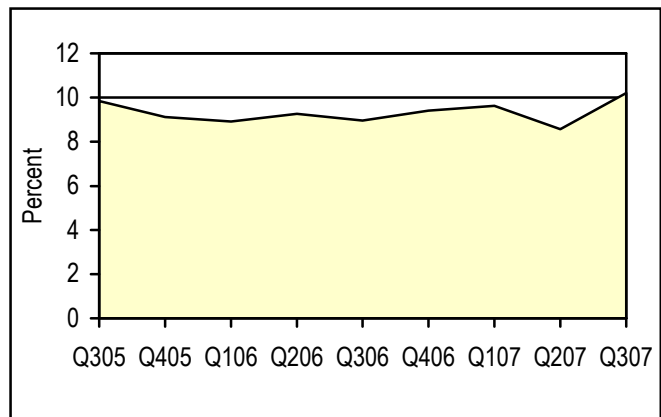
Interest rates on savings deposits have been maintained as in the previous quarter. Upward movements were noted in interest rates on fixed deposits. The maximum interest rates on maturities from two to six months and those above six months has been raise by 25 basis points, respectively. This uptrend reflected high interest offered by one bank during the quarter. Interest rate ranges on other maturities of fixed deposits have been maintained as in the previous quarter (see table 9). The effect of the upward movement in interest rates as abovementioned caused the upward movement in the weighted average rate of interest rates on fixed deposits to 4.10 percent. Despite the increase in the weighted average interest on fixed deposits, the weighted average interest rates on total bank deposits was maintained at 1.92 percent as recorded in the previous quarter.

Lending Interest rate ranges offered on sectoral loans have been maintained as in the previous quarter (see table 9). Though the scope on various lending interest rates have been maintained, individual interest rates movements within various ranges were unaccounted for therefore may have contributed to the upward trend in lending rates. Additionally Banks ought to subsidize for the increase in interest on fixed deposits rate therefore increase interest rates for most risky loans. The above mentioned factors triggered the increase in the weighted average lending rates to 12.12 percent in contrast to 10.49 percent recorded over the June quarter.

Interest Rates Spread

The effects of the upward movement in the average rate of interest for total bank deposits to a stable movement in the weighted average interest on total bank deposits triggered interest rates spread to further widen to 10.20 percent as compared to 8.57 percent recorded over the previous quarter.

Figure 25: Interest Rate Spread



Reserve Money

After an expansion noted during the preceding quarter, reserve money² contracted by 5.8 percent to reach VT8,015.6 million during the current quarter. The decline was particularly attributed to excess reserves which contracted substantially by 32.9 percent. This trend reflected the Reserve Bank's aggressiveness in conducting its open market operation during the quarter. Consequently, outstanding RBV notes issued in the market has risen largely by 52.6 percent at the end of the quarter. Currency in circulation and SRD on the other hand noted increases from the previous quarter by 5.6 percent and 4.9 percent respectively. Despite the quarterly decline, reserve money expanded by 8.4 percent from the corresponding quarter of 2006.

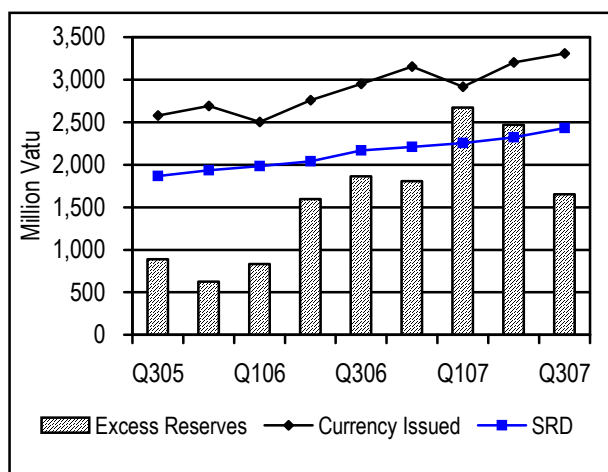
² Reserve Money comprises of currency in circulation, Statutory Reserve Deposit (SRD) and Excess Reserves.

MONEY MARKET DEVELOPMENT

Open Market Operation

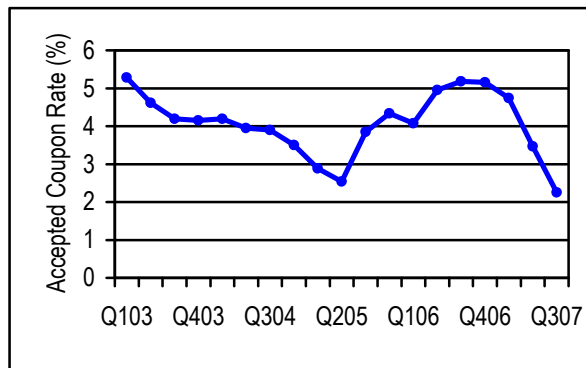
The Reserve Bank continued to tighten up monetary conditions during the 3rd quarter of 2007 with total RBV notes issue of VT3,300 million compared to VT1,365 million and VT1,400 million in the first and second quarter respectively. Consequently, the banking system liquidity fell drastically to less than VT2,000 million, in line with RBV objective to achieve a target level of VT1,200 by this year end.

Figure 26: Components of Reserve Money



Allotments made in terms of notes issued are as follow; VT900 million each to 14 and 28 days while the two remaining maturities were allotted VT750 each. Total maturities during the quarter summed up to VT2,700 million leaving the RBV notes outstanding at quarter end at VT1,750 million compared to VT1150 million at end of quarter two.

Figure 27: 91-days RBV Notes Yield



Yields on reached their lowest levels during the quarter with RBV notes for 91 days maturity hit a record low of 2.25%. The downtrend in the interest rates reflects the stiff competition for RBV notes which continued during the 3rd quarter.

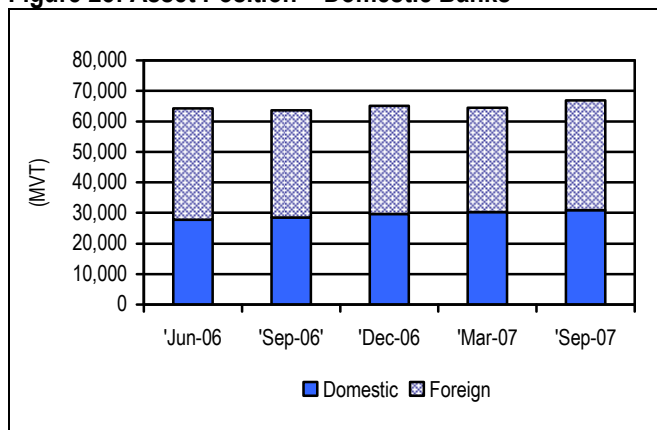
BANKING SECTOR

Domestic Banks

Balance Sheet

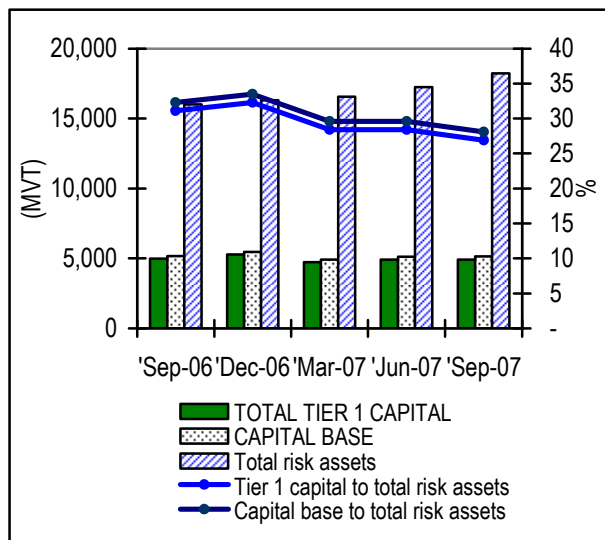
The industry recorded further growth in its balance sheet over the quarter under review. Total assets increased by 1.7 percent to Vt68.9 billion (Jun-07: Vt65.8 billion). The increase reflects mainly growth in foreign assets by 2.4 percent to Vt35.9 billion (Jun-07: Vt35.1 billion). Domestic assets also increased by 0.8 percent to Vt30.9 billion (Jun-07: Vt30.6 billion).

Figure 28: Asset Position – Domestic Banks



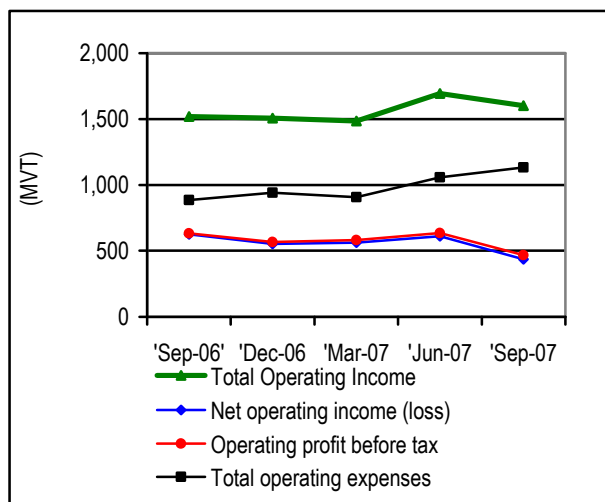
The industry's total liabilities (less capital) increased by 2.1 percent to Vt60.9 billion (Jun-07: Vt59.6 billion). The increase is sourced mainly from growth in domestic liabilities by 3.9 percent to Vt48.7 billion (Jun-07: Vt46.9 billion). Foreign liabilities on the other hand declined by 4.2 percent to Vt12.2 billion (Jun-07: Vt12.7 billion).

Figure 29: Capital Adequacy & Tier 1 Ratio



Capital base of the industry continues to remain robust despite recording a decline in its capital adequacy ratio over the quarter to 28.1 percent (Jun-07: 29.6 percent). The industry's Tier 1 capital to total risk assets also declined from 28.4 (Jun-07) percent to 26.9 percent (Sep-07). The industry's capital base increased by 0.4 percent to Vt5.13 billion (Jun-07: Vt5.11 billion). The increase is attributable to growth in disclosed reserves and retained earnings by 0.2 percent to Vt4.1 billion (Jun-07: Vt4.0 billion). Total risk assets rose by 5.7 percent to Vt18.2 billion (Jun-07: Vt17.3 billion).

Figure 30: Earnings – Domestic Banks

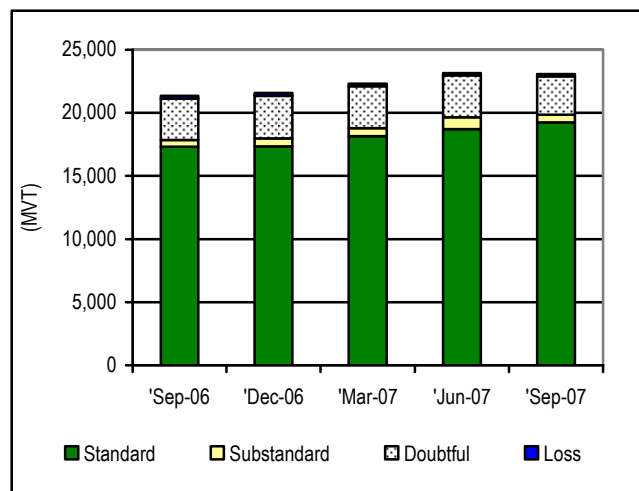


Profit before tax write offs and provisions declined by 21.6 percent to Vt467.2 million (Jun-07: Vt595.7 million). Taking into account provisions and bad debts written off

during the quarter, net profit now stands at Vt434.7 million (Jun-07: Vt576.5 million). The decline was mainly driven from growth in total expenses by 23.8 percent to Vt1.1 billion (Jun-07: Vt915.2 million). This generally, reflects staff salary increases and new staffs hired into the industry. Total income of the industry also increased by 5.9 percent to Vt1.6 billion (Jun-07: Vt1.5 billion)

The industry's return on asset (ROA) declined from 0.9 percent to 0.7 percent and return on equity (ROE) declined from 9.4 percent to 7.6 percent.

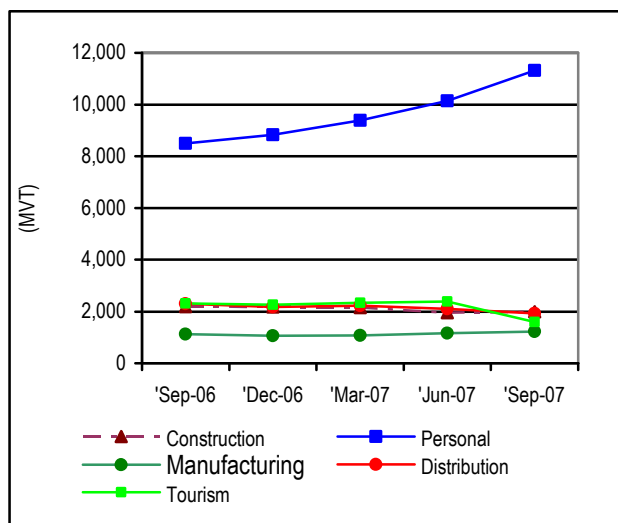
Figure 31: Asset Quality – Domestic Banks



The industry's total lending declined by 0.3 percent to Vt23.0 billion (Jun-07: Vt23.1 billion) despite recording a 2.8 percent increase in standard loans over the quarter to Vt19.2 billion (Jun-07: Vt18.7 billion). The decline was attributable to the paying-off of a large tourism exposure, as well as reclassification of loans specifically for doubtful loans which declined by 8.6 percent to Vt3.0 billion (Jun-07: Vt3.3 billion). Substandard loans also declined by 34.6 percent to Vt615.9 million (Jun-07: Vt934.5 million). Standard loans accounted for 83.3 percent of total loans.

The industry's level of non performing loans declined by 7.8 percent to Vt3.2 billion (Jun-07: Vt3.5 billion). The decline resulted in a drop in specific provisions by 3.9 percent to Vt1.05 billion (Jun-07: Vt1.09 billion) while general provisions increased by 520.9 percent to Vt47.6 million (Jun-07: Vt7.7 million). Security held by the industry also increased by 0.7 percent to Vt14.6 billion (Jun-07: Vt14.5 billion).

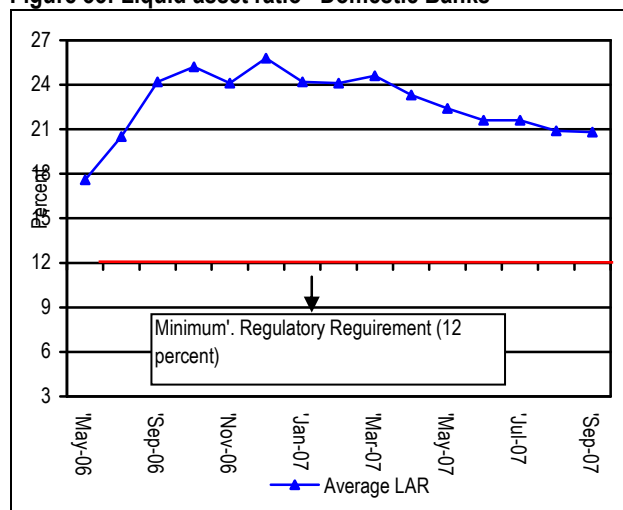
Figure 32: 5 Largest Sector Claims Domestic Banks



The industry's five largest sectoral lending remained to personal (Vt11.3 billion), construction (Vt1.9 billion), distribution (Vt1.9 billion), tourism (Vt1.6 billion) and manufacturing sector (Vt1.2 billion).

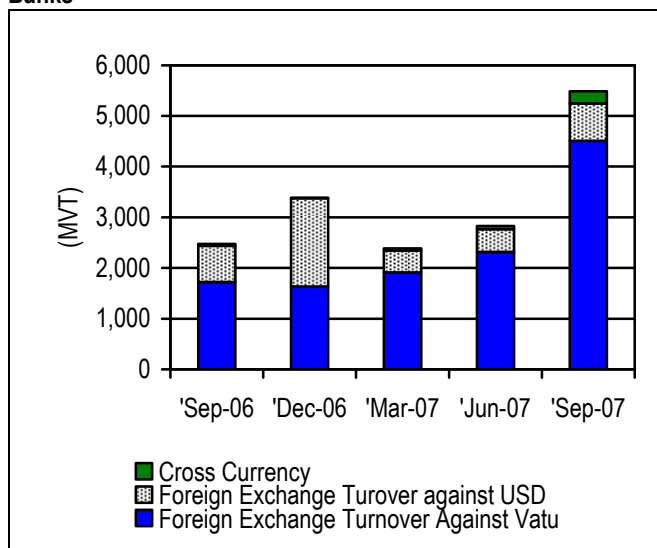
Growth over the quarter showed major shift in personal lending by 11.5 percent to Vt11.3 billion (Jun-07: Vt10.1 billion) and manufacturing by 5.9 percent to Vt1.2 billion (Jun-07: Vt1.1 billion). Lending to the construction sector also increased by 2.1 percent to Vt1.99 billion (Jun-07: Vt1.95 billion). During the quarter, lending to distribution and tourism sector however declined by 9.4 percent and 33.5 percent to Vt1.2 billion (Jun-07: Vt1.1 billion) and Vt1.5 billion (Jun-07: Vt2.3 billion) respectively.

Figure 33: Liquid asset ratio –Domestic Banks



Liquidity position of the industry at the end of September 2007 stood at 20.8 percent down from 21.6 percent in the previous quarter. Although the trend is declining, it is still well above the minimum regulatory requirement and Reserve Bank is closely monitoring this position.

Figure 34: Foreign Exchange Turnover Position of Domestic Banks



The industry's total foreign exchange turnover for the September quarter increased by 94.1 percent to Vt5.5 billion (Jun-07: Vt2.8 billion). The increase was mainly attributable to growth in foreign exchange turnover against the Vatu currency by 94.8 percent to Vt4.5 billion (Jun-07: Vt2.3 billion). Foreign exchange turnover against USD also increased by 65.1 percent to Vt741.3 million (Jun-07: Vt449 million).

International Banks

Overview

During the 3rd quarter of 2007, the Reserve Bank of Vanuatu conducted several on-site reviews on offshore banks as part of its on-going supervision to ensure prudent and sound operations of the offshore industry. Offshore banks were also encouraged to always operate their banking business within the prudential guidelines of Reserve Bank of Vanuatu, International Banking Act No: 4 of 2002 (IBA) and other laws of the country, such as FTRA.

A new offshore bank was also granted a license during September 2007 quarter, making a total of 8 such banks with valid licenses.

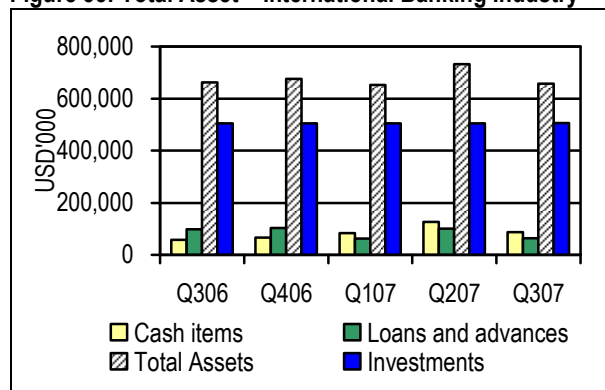
The Bank continues to maintain good working relationship with offshore banks through constant dialogue between the two sectors.

Statement of Financial Position

The third quarter of 2007 showed significant decrease in the industry’s statement of financial position footings by 10.26 percent to USD656.8 million (Jun-07: USD731.9 million) as a result of significant decrease in cash items of 31.07 percent to USD\$87.4 million (Jun-07: USD126.8 million).

The major component of the industry’s assets continues to be investments accounting for 76.92 percent (USD505.6 million) of the industry’s total assets. (Refer to Figure 1).

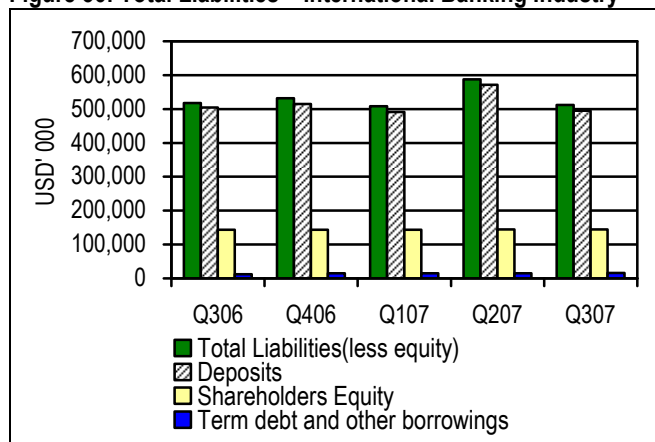
Figure 35: Total Asset – International Banking Industry



On the liability side, the industry’s total liabilities (excluding shareholders equity) decreased by 12.84 percent to USD512.3 million (Jun-07: USD587.8 million) as a result of decrease in deposits by 13.33 percent to USD495.1 million (Jun-07: USD571.4 million).

The major components of liabilities are deposits which accounted for 75.38 percent of total liabilities and shareholders equity. (Refer to Figure 2).

Figure 36: Total Liabilities – International Banking Industry

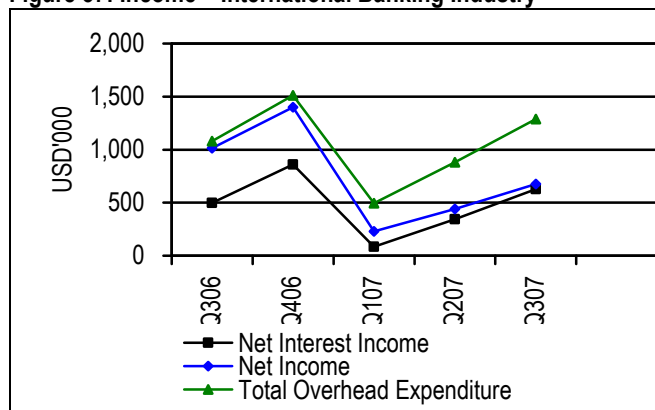


Earnings

The industry recorded a net profit of USD677 thousand during the third quarter of 2007. This is an increase of 53.86 percent compared to the second quarter of 2007 (Jun-07: USD440 thousand). The improvement in industry’s earnings is attributable to increases in both *Net Interest Income* and *Non-Interest Income* by 81.98 percent to USD626 thousand (Jun-07: USD344 thousand) and 45.93 percent to USD1.31 million (Jun-07: USD897 thousand) respectively. Overhead expenses increase by 46.20 percent over the reviewed quarter. (Refer to Figure 3).

The industry’s ROA and ROE ratios for September 2007 quarter are 0.097 percent (Jun-07: 0.06 percent) and 0.47 percent (Jun-07: 0.31 percent) respectively.

Figure 37: Income – International Banking Industry



3.4. Financial Development

3.41. Shipping Registration

Over the third quarter of 2007, the number of ships on the registry at quarter ends increased to 602 vessels, compared to 585 and 586 vessels recorded during the previous quarter and the year ago level. The increase was attributed to the addition of 32 new ships to the registry, while 15 ships de-registered.

3.42. Company Registration

The number of companies registered with the Vanuatu Financial Services Commission (VFSC) recorded a total of 5,365 companies in the third quarter. This represents a net decline 1,042 companies over the second quarter and a net decline of 920 companies over the third quarter of 2006. This net decline was attributed by the registration of 146 new companies, while 1,120 companies deregistered with the VFSC.

Out of the total number of companies registered with the VFSC, those which hold licenses includes 7 Exempted Banks, 1 Exempted Financial Institution, 70 Insurance Companies and 15 Trust Companies.

From the total number of companies, international³ companies represent 67.2 percent, local companies made up 30.2 percent, while exempt⁴ and overseas⁵ companies accounted for 2.6 percent.

Balance of Payments

Developments in the Balance of Payments for September quarter of 2007 further expanded the official international reserves (net reserves) by MVT151 from last quarter. Along this line, there was also a shift in the monthly import cover from 7.5 to 7.6. The economy continues to expand given the magnitude of domestic activities currently ongoing and expected this year. In the Reserve Bank of Vanuatu policy objectives, the Bank has to maintain a minimum target level of 4

³ Companies incorporated under the international Companies Act and do not operate business in the country

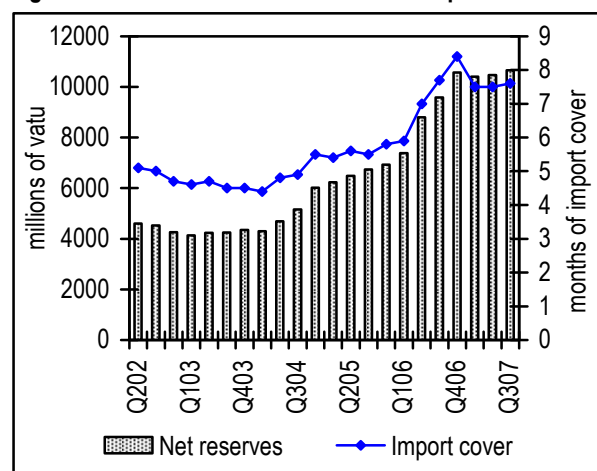
⁴ Companies registered or re-registered as exempt companies and do business overseas

⁵ Companies incorporated outside Vanuatu and do business in the country

months of import cover as it is one of the vital key indicators of monetary stability. As you can see, the Bank is comfortable with the current level foreign exchange and continues to monitor developments.

The Current account deficit has marginally expanded; mainly due the increase in trade deficits and reduced transfers offsetting improvements in services and income. The Capital and Financial account was reduced in half despite another surplus for the quarter. The reduction was caused by significant decrease in liabilities through deposits of non residents. Despite the decrease in this account financing was till adequate through other sources.

Figure 38: Net Reserves and months of import cover



Merchandise trade

The provisional trade deficits expanded by 2% in September mainly caused by an 11% increase in exports offsetting in value terms the 56% increase in exports. All items had shown marginal increase Significant contributions were recorded from food and live animals (35%); mineral fuels (40%) and basic manufacturers by 15%. Most of Vanuatu imports are directed from Australia and the depreciation of the Vatu against the Australian dollar continue take effect on high import bills. is expected to rise. This is in addition to high domestic activity and project implementations which should further increase imports in medium term.

Exports including re-exports were up by MVT401 in the review period. This was around the level of the same quarter last year. Exports of all major commodities showed increases with re-exports rose by 35%. Re-export items include personal effects and jet fuel. Exports to the

European Community, Japan and New Caledonia increase significantly during the quarter.

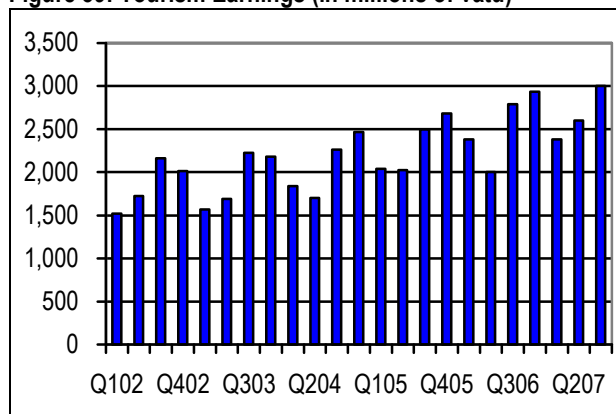
The coconut oil industry that was revived in June industry after the closure of the COPV mill in early 2006 further expanded its earnings by 29% in the period review. Kava exports that had been disturbed by domestic trade policies and international ban, however registered MVT 137 in September.

Services Account

Inward travel or tourism earnings are the main source of surplus of the services account. Tourism earnings rose by 14% in September quarter reflecting large increase in the number of visitor arrivals. Around 53% of Vanuatu tourists originate from Australia and the appreciation of Australian dollar during the period had contributed to more inflows of Australian dollar into the economy. The surplus in net services rose by 30% during the quarter from 3.2% up in June.

Although services payment was hefty during the quarter due to increase in freight bills, this could not offset inflows through tourism earnings and other services items.

Figure 39: Tourism Earnings (in millions of vatu)



Income Account

Vanuatu income account is deficit in nature representing bulk of foreign direct investment re-invested earnings and distributed branch profits. Movement in world interest rates have also impacts on the investment income account of Vanuatu. Investment on AUD and NZD have yield well in September given the attractive interest rates of the two currencies and the appreciation

of their exchange rates. However, further losses have been recorded from USD investments in September as it was in June. This channelled mainly through deposits and loans.

Overall, September quarter saw a decrease in the income deficit reflecting reduction in interest income through other investment. This could not offset reduction in reinvested earning and dividends paid abroad by foreign enterprises. Dividends and distributed branch profits of foreign direct investment enterprises was much lesser than the large amount remitted in March and June.

2.54 Current Transfers Account

As a large proportion of current transfers represent official grant flows, the level is driven by donor grants to the Government of Vanuatu. The total estimated grants were lower by 8 percent in September quarter a significant drop in technical assistance that could not be matched from a marginal increase in cash grants. Other official transfers was also reduced due to periodical recipient dates of shipping fees which is usually high in March and low in other quarters.

2.55 Capital and Financial Account

Estimated capital account for this period saw a slight increase in project funded goods. It is projected that aid in kind for capital related goods will be high in late 2007 and 2008 when the Millennium Fund projects commence. Continuous net outflows of migrant's transfers continue to be recorded. It is important to note that information on estimate migrant's transfers is derived from migrant model.

The Financial account record flows of transactions through external assets and liabilities and are usually used as source of financing to the balance of payments. Foreign direct investment inflows almost doubled in September caused by reinvested earnings of current equities plus fresh investments. In addition, net withdrawal of foreign assets from other sectors was recorded. However, all this could not offset withdrawal of non resident's deposits in Vanuatu plus net placing abroad by the monetary authority. At end of September quarter, financing continues to be sufficient.

Medium Term outlook

In medium term (2008), the current account is expected to improve through services accounts and donor grants and

assist in deficits created by high imports. Imports will continue to grow, reflecting expansion of the economy as large amount of capital investment are injected into capital projects. The projected improvement in tourism earnings will continue to provide a boost to the services account while reinvested earnings of foreign enterprises will continue to create deficits in net factor income. The capital and financial account is forecasted to continue in surplus into the medium term and may bound to fluctuate driven by investments in particular foreign direct investment. Barring adverse unforeseen circumstances, official international reserves are therefore expected to remain healthy at around 7 months of import cover at end 2007 and 6 months in 2008. The Reserve Bank continues to monitor external development and encourage sustainable financing policies among all sectors.

International Investment Position

By end September 2007, Vanuatu’s International Investment Position (IIP) expanded its net borrowing position to VT6832 million, from VT6011 million at end June. The new position reflected an increase in liabilities due to foreign direct investment.

2.9 Exchange Rate Development

Exchange rate developments for September continue to reflect developments in international financial markets. The United States Dollar continued to loose grounds against major international currencies over September hitting a lifetime low against the euro and the dollar-index (a gauge of the currency against a basket of six currencies), 28-year low against the Australian dollar, a

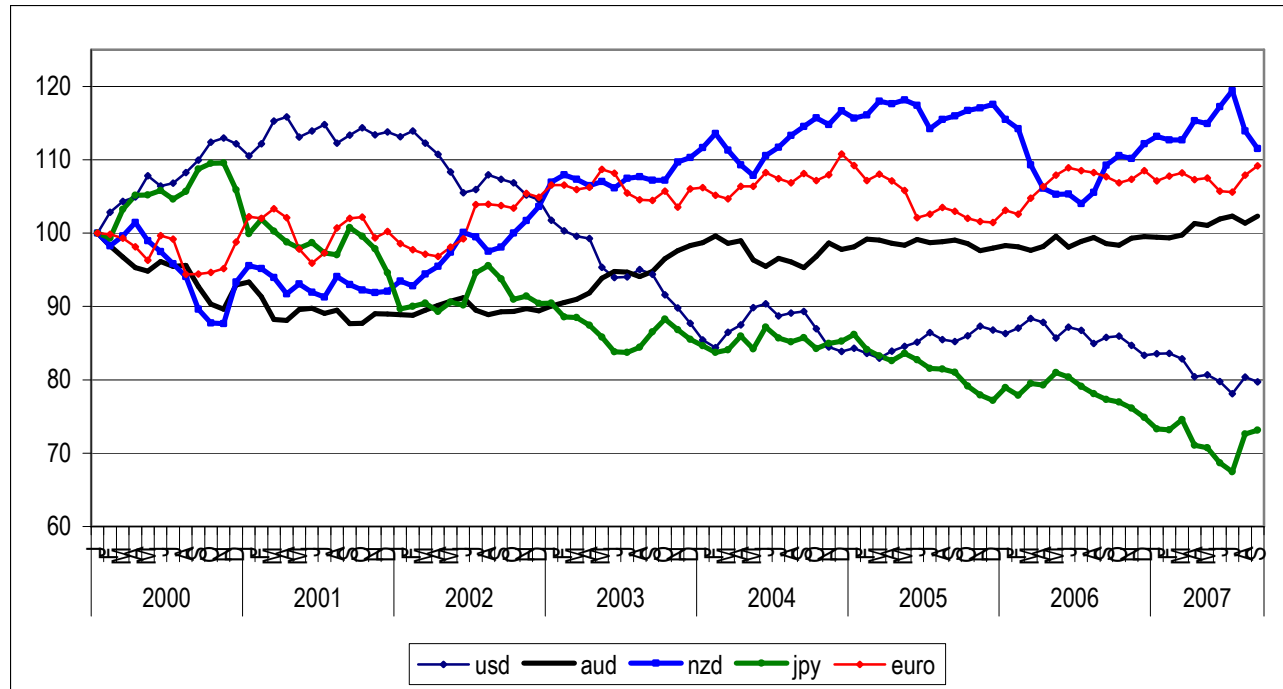
2-month low against the New Zealand dollar and weakened to parity level against the Canadian dollar. The steep tumbling of the US dollar stemmed from an aggressive and an unexpected Fed decision to cut the US official rate by 50 basis points to 4.75 percent from 5.25 percent to shelter the US economy from the housing slump and market upheaval, and as uncertainty persisted about the health of the US economy. Current data continued to indicate slow economic growth in US and persistent low consumer confidence level. The latest US inflation data showed a dropped of 0.1 percent in August, bolstering the view for more Fed fund rate cuts over the coming months.

Growth in the euro zone seemed to have been cooled by the US troubled credit market, in line with forecasts, while inflation jumped above the European Central Bank comfort zone to 2.1 percent in August on a month-on-month basis. The ECB will no doubt be concerned about the slow growth and the market expects the European central bank to postpone any rate increase to next year. These developments had impacts on the exchange rate between major currencies and are reflected on the vatu.

The developments of vatu at end of September as compared to end of June saw the depreciation of USD by 2% and NZD by 4.6 %, Appreciation was recorded for AUD 1.8%, JPY 4.3% and Euro by 3.1% As compared to September last year, the vatu lost ground to AUD, NZD and EURO but strengthened against the other major partner’s currencies.

| Period | USD | AUD | JPY | NZD | EUR |
|----------------------------|--------|--------|--------|-------|--------|
| Closing rate on 30.09.07 | 99.76 | 87.79 | 0.863 | 74.86 | 141.25 |
| Closing rate on 31.06.07 | 101.77 | 86.18 | 0.8263 | 78.33 | 136.87 |
| Closing rate on 30.09.06 | 110.51 | 82.76 | 0.9385 | 72.65 | 140.4 |
| Quarterly % Change | 2.0 | -1.8 | -4.3 | 4.6 | -3.1 |
| Yearly % Change | 10.8 | -5.7 | 8.7 | -3.0 | -0.6 |
| Low for 3rd Quarter -2007 | 99.76 | 24-Mar | 0.8141 | 71.51 | 137.25 |
| | 89/9 | 20/8 | 20/7 | 9-Oct | 2/7 |
| High for 3rd Quarter -2007 | 105.72 | 87.79 | 0.9279 | 79.17 | 143.15 |
| | 20/8 | 28/9 | 17/8 | 17/7 | 11/9 |

Exchange rate of vatu against major trading partners' currencies
 Index 2000=100 (Jan 2000- Sep 2007)



CHRONOLOGY OF MAJOR EVENTS

| NO. | BRIEF DESCRIPTION OF MAJOR EVENTS | EFFECTIVE DATE |
|-----|--|------------------------------|
| 1. | The Finance Minister, Honorable Willie Jimmy paid visit to certain key financial institution in Singapore and Hong Kong to promote the Vanuatu Finance Centre. As part of the visit, Minister Willie Jimmy updated financial institutions on improvement that Vanuatu has made in its financial sector and Vanuatu's commitments to other counties to prevent money laundering and funding of acts of terrorism. <i>(The Independent, 22nd July 2007)</i> | 22 nd July, 2007 |
| 2. | National Authorizing Officers (NAOs) in the Forum Island Countries and the Regional Authorizing Officers (RAO) under the European Development Fund (EDF) have met to discuss programming of the 10 th EDE. The meeting included briefing of the main status of implementation of projects supported under the Pacific Regional Indicative Programme, the new Technical Cooperation Facility project. The outcomes of the NAO/RAO Meeting were submitted to the meeting of Pacific ACP Trade Ministers which took place from the 31 st July to the 1 st of August in Port Vila, Vanuatu. This meeting was attended by 14 PACP Trade Ministers and officially opened by newly appointed Deputy Prime Minister of the Republic of Vanuatu, Honorable Edward Natapei and chaired by the Vanuatu Minister of Trade Commerce, Industries and Tourism, Hon. James Bule. The meeting discussed the need to conclude the Economic Partnership Agreements with European Union (EU) that deliver on the PACP's development objectives. The | 1 st August, 2007 |

likelihood of the 31 December 2007 deadline set by EU for the conclusion of the EPA being met has also been questioned by other ACP negotiation regions in Africa and the Caribbean. The joint PACP-EU Article 37(4) to review exercises concluded that there remained serious challenges to concluding the negotiations in time if the EPA was to be truly development friendly.

(The Vanuatu Daily Post, 1st August 2007)

3. Hu Jin Tao, the Chinese president has promised 20 million yuan renminbi, or roughly VT 256 million to Vanuatu for future development under an agreement signed by the two Heads of States when President Mataskelekele was on an official visit to Beijing. President Hu spoke of China's commitment to continuing the friendly relations. The Vanuatu Head of State was assured of Chinese assistance in building a new court house. The Chinese Import / Export Corporation also assured the Vanuatu President of China's readiness to assist Vanuatu with the extension of Pekoa airport and the oil palm project.
(The Independent, 22nd July 2007) 22nd July, 2007
4. Governor of the Reserve Bank of Vanuatu, Odo Tevi has handed over on Monday 3rd September, 2007, a VT105,764,000 cheque to Finance Minister Willie Jimmy as the Reserve Bank's dividend for 2006. Tevi confirmed 2006 as another firm economic performance year, adding "the amount also reflects the adjustments undertaken by the Bank in 2006 as it moves to comply with the latest International Financial Reporting Standards." *(The Vanuatu Daily Post, 5th September, 2007)* 5th September, 2007
5. The Vanuatu Government has signed contract agreement with the Ambassadors for Vanuatu to the United Nation, Donald Kallpokas Masekivanua and Ambassador to European Union Roy Micky Joy on Friday September 7, 2007. The signing agreement was the final process by the Vanuatu Government before the two will formally carry out their job as the ambassadors to the high level missions. Ambassador Micky Joy will base in Brussels in Belgium and Ambassador Kalpokas will be in New York. Ambassador Micky Joy who support Ambassador Kalpokas in his word of appreciation said though they will be in two different countries they will uphold the sovereignty and the fundamental principle of Vanuatu.
(The Vanuatu Daily Post, 11th July 2007) 7th September, 2007
6. Three thousand proposed project sites for rural electrification in Vanuatu have been identified and are awaiting government approval. Authorities say a technical team is expected to meet to finalize the project submissions before they can be submitted to the Council of Ministers for approval. Recently, the Unelco Company which has electricification in the country, handed over a sum of VT50,242,142 to the government from the Sarakata Hydro fund. Unelco revealed that initial distribution of the fund saw the electrification of the fund saw the electrification of Tanna and Malekula in 2001 and assist in developing electricity in the rural areas in other islands as well. Under the current contract agreement, Unelco is expected to return the save funds to the government each year. *(Vanuatu Daily Post, 11th September 2007)* 11th September, 2007

7. The Pacific Islands Applied Geoscience Commission (SOPAC) has commended the Vanuatu government, for endorsing its National Energy Policy. Vanuatu's Energy Policy was endorsed by cabinet last month. Speaking at a media, SOPAC Gender and Energy Expert Yogita Bhikbhai said "that it's way forward for Vanuatu". "The government's initiative to make energy a priority shows that it is a national concern and an issue that needs to be dealt with immediately." She adds, "Energy issues have been given little priority in national plans over the years but rising fuel prices, countries are pushed to prioritize energy needs for the country." Director of Energy, Leo Moli said, "the next step would be for the government to start implementing the National Energy policy (NEP) and where appropriated, tie this NEP to the implementation and management of the Rural Electrification Master Plan (REMP). Such regional project hosted by SOPAC aims to assist PIC with specialized know how in energy policy, planning and management. The Pacific Islands Energy Policy and Strategic Action Planning Project (PIEPSAP) which is funded by the Government of Demmar through UNDP Samoa have been operational since early 2005 and have supported 14 PIC to improve their energy sector management. Amongst the beneficiaries is Vanuatu, which we see as an encouraging example of integrated energy sector management both on the national and the regional level. The Energy Policy sets a framework for the use of local energy resources, energy conservation and regulation and pricing.
(Pacific News Magazine, SOPAC 24th September 2007)
- 24th September, 2007
8. Vanuatu Law students and members of the public learned during a taxation forum held at the Emalus Campus, USP, that only 25% of the population were involved in taxation in Vanuatu, mostly in the two towns. This was revealed Tuesday by the Director of Customs and Inland Revenue Ben Leeshi during the forum. As part of the talk, Mr. Leeshi provided an overview on Vanuatu's taxation system, describing it as effective, fair, easy to administer and allows for self-assessment. Which compared with other countries, Vanuatu has a very small tax base. He also added that it is important for the government to consider how a tax can encourage economic growth before imposing certain taxes. As part of the forum, other speakers also presented, while a debate by the Vanuatu law Students based on the topic, 'The introduction of income tax in Vanuatu will mean an increase in poverty.'
(Vanuatu Daily post 20th September 2007)
- 20th September, 2007