Quarterly Economic Developments[1]

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Table of Content

EXECUTIVE SUMMARY 3

I. INTERNATIONAL DEVELOPMENTS 4

II. DOMESTIC DEVELOPMENTS 5

Table 1.0 Fiscal Statistics 5

Chart A Quarterly Growth Rate (%) of Major Revenue Items 6

III. FINANCIAL DEVELOPMENTS 6

Table 2 Sectoral Distribution of Commercial Bank Loans and Advances 8

REFERENCE 10

Executive Summary

Economic recovery has been reported in the fourth quarter of 2009 in most parts of the world, thanks to the timely intervention of massive fiscal and monetary stimuli that shielded most economies from the full effects of the Global Credit Crisis (GCC). In its January 2010 World Economic Outlook (WEO), the IMF wrote that recovery will be sluggish in most advanced economies, where as in many developing and emerging economies activity is expected to be vigorous, largely driven by internal demand.

For Vanuatu, activity in the domestic economy was weak in the last quarter of 2009. The Vanuatu Government undertook several ex-budget expenditures throughout the year but they were not enough to resurrect domestic consumption. Impacts of external shocks have affected Vanuatu's trade balance and the way business has been conducted domestically. Outcomes of expansionary fiscal and monetary policy have been mixed in the quarter while some recovery is expected to be delayed until 2010.

I. International Developments

The impact of the Global Credit Crisis (GCC) is still being felt throughout the globe. Though most economists predicted gradual economic recovery towards the last quarter of 2009 and into 2010, recent economic data appears to be mixed.

The upshot of financial institutions tightening credit conditions continues to affect new businesses around the world obtaining financial backing for their start –up activities, especially from informal investors. The number of new businesses being set up around the world has declined in the face of the global recession. According to the Global Entrepreneurship Monitoring, (GEM), new start-ups were down 10 per cent last year 2009 in 20 of the world's richest nations. Clearly, the slowdown has led to changes in the environment for entrepreneurs with investors holding back financing and consumers buying less.

In Europe most economies have returned to growth but the broader picture of the GCC is that output fell sharply over the twelve months until March and has not changed very much since then, although evidence of a recovery is starting to emerge. Year ended real GDP growth in the Euro area has seen a slight improvement from a low of around - 4.2 per cent in early 2009 to - 3.8 per cent in the last quarter. Year ended consumer price inflation in the Euro area remains below zero.

In the United States (U.S.), the economy's recovery continued at the end of 2009, spreading to more parts of the country. However, economic activity remains too weak to bring down unemployment due to weaknesses in labour and commercial real estate markets. Most districts reported that consumer spending in the recent 2009 holiday season was slightly greater than in 2008, (but still far below 2007 levels), thanks to the massive government stimulus. Labour market conditions remained soft in most parts of the U.S. and with the stimulus fading a persistently high jobless rate combined with low inflation are expected to lead the Federal Open Market Committee keeping the fed funds rate near zero when it next meets later this month.

In contrast, Australian unemployment has fallen to an eight month low, boosting confidence in the economy. According to the Australian Bureau of Statistics (ABS), the rate of unemployment fell to 5.5 per cent in December from 5.6 per cent in November. The fall was driven by a rebound in employment led by finance and the property industries, both of which shed a lot of staff during the downturn; meanwhile the mining sector is also strong with increasing demand from China for iron ore fuelling growth. However, the unexpected strength of the economy has increased pressure on the Government to reduce budget spending through winding back the stimulus, which could be achieved by cutting other programs. Furthermore, the Government now faces a risk

that the official Reserve Bank of Australia's (RBA's) interest rates will rise considerably higher this year than the 5.0 per cent previously predicted by financial markets, particularly if wages and prices start rising more quickly.

There is evidence of economic recovery in Asia[2] with year-ended real GDP growth of -2.4 per cent experienced from a low of – 5.0 per cent to the first quarter of 2009. Year -ended consumer price inflation remains around zero. Growth in China is at its fastest pace in two years, keeping it on target to overtake Japan as the world's biggest economy but raising fears the nation will overheat as it roars out of the GCC.

II. Domestic Developments

The Vanuatu economy continues to ease in the fourth quarter with a relatively weak outcome underlying softness in an economy that has sheltered itself from direct impacts of the GCC. On a quarterly basis recurrent revenue (seasonally adjusted) contracted in the fourth quarter by -6.3 per cent but expanded by 16.1 per cent in the third quarter. The recurrent revenue yearly growth rate eased to 12.9 per cent in 2009, but much stronger at 26.3 per cent, one year previously. VAT contracted by 0.8 per cent and import duty slighted to 0.9 per cent in the fourth quarter and remains -4.0 per cent and 1.5 per cent lower than a year earlier. Amidst weak revenue receipts, recurrent revenue came in 5.0 per cent lower than the Budget 2009 forecast.

Table 1.0 Fiscal Statistics

	Quarterly Growth (%)		Annual Growth (%)	
	Dec-09	Sep-09	Dec-09	Dec-08
Recurrent Revenue	*(6.3)*	*16.1*	*12.9*	*26.3*
VAT	0.8	7.6	(4.0)	21.3
Duties	0.9	12.4	1.5	13.0
Non Tax Revenue*	(40.8)	60.0	15.4	(8.0)
Recurrent Expenditure	*164.1*	*56.8*	*35.2*	*22.6*
Goods and Services	0.9	(0.3)	2.9	8.8
Transfers	(48.1)	67.5	8.4	9.1
Acquisition of Capital assets	211.3	(10.4)	23.9	4.7

* excludes sales of fixed capital assets

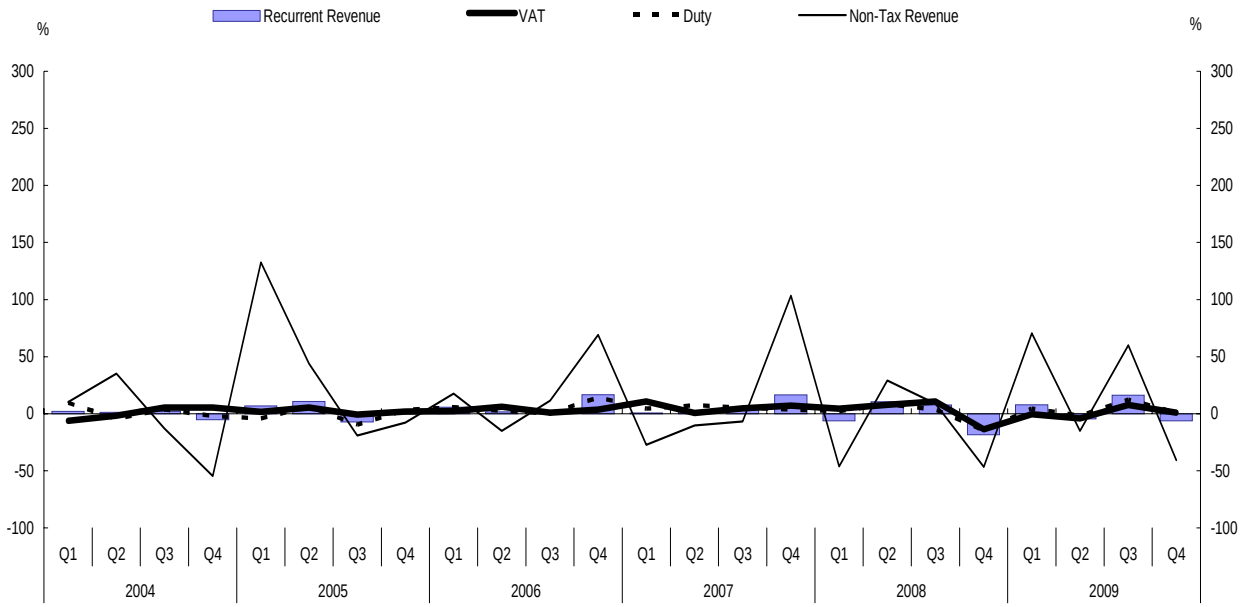
Source: Department of Finance and Treasury

Seasonally adjusted recurrent revenue was eased to -6.3 per cent this quarter on the back of a solid performance in the third quarter at 16.1 per cent and with nominal

[2] Hong Kong, Indonesia, Korea, Malaysia, Philippines, Singapore, Taiwan and Thailand

annual growth of 12.9 per cent. The main contributors to the decline are VAT with slow growth of 0.8 per cent; duties posted 0.9 per cent growth and non-tax revenue at -40.8 per cent. VAT is an indicator of the level of consumption in the economy and thus final demand. Year-on-year growth rates were weak, adding to fears of softness in economic activity while the impacts of the GCC continue to diffuse through the real economy.

Chart A Quarterly Growth Rate (%) of Major Revenue Items



Source: Department of Finance and Treasury

III. Financial Developments

Positive contributors to GDP through Government services on the expenditure side were public fixed capital formation which rose by 211.3 per cent in the fourth quarter, staging a strong growth of 23.9 per cent annually and 19.2 percentage point growth from two years previously. Meanwhile, transfers to households expanded by 0.9 per cent over the fourth quarter. The year on year growth on household consumption eased to 2.9 per cent after its peak at 8.8 per cent over the past year. The largest negative contributor is transfers to government bodies (including government local authorities), tracking behind at -48.1 per cent. Annual growth under this category is soft at 8.4 per cent, 0.7 percentage point from a year before.

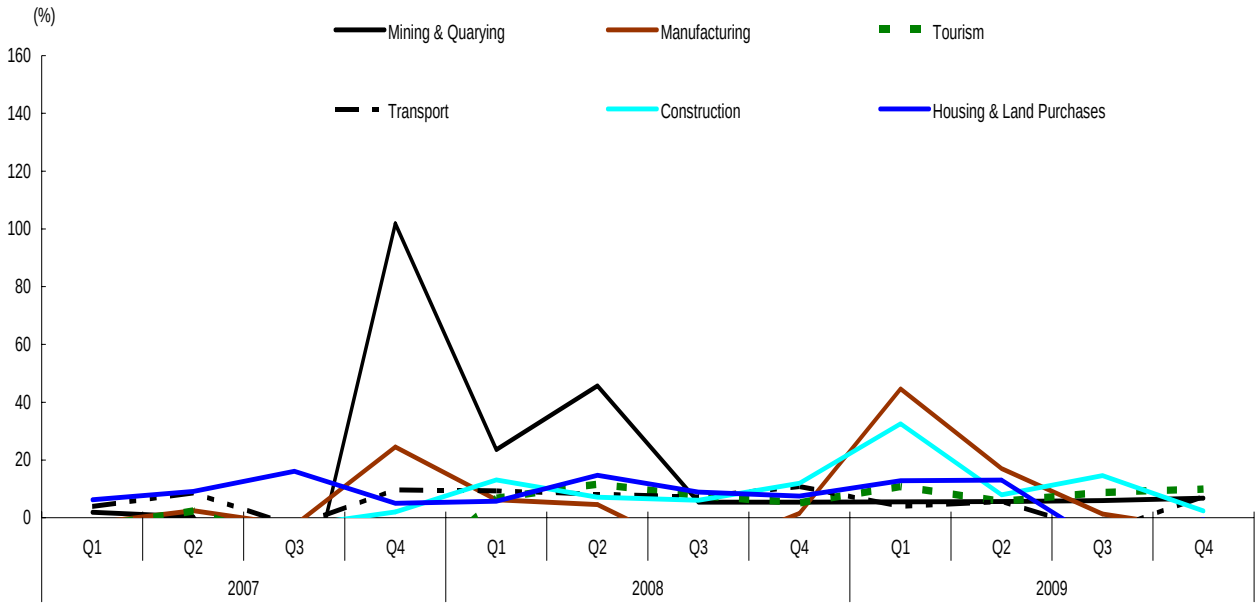
These mixed results reflect the importance of government expenditure in supporting the economy. Expansionary monetary policies at the end of 2008 and in early 2009 (for

example, relaxation of capital controls) have also been very positive; these have ensured that there is sufficient liquidity in the financial system. Government investment into infrastructure, schools and public health has borne fruit. Further the Government stimulus in the tourism sector has assisted in driving 9.9 per cent tourism activity growth in the quarter, up 1.1 percentage point from quarter 3.

Getting rid of old inventories continue to pose problems for suppliers as they struggle through the early stages of recovery in 2010, meanwhile businesses confidence remains uncertain as consumption tumble. There are possibilities that private sector growth will resume although its contribution to overall growth is expected to be smaller. On the other hand, State consumption was again solid gaining 0.9 per cent this quarter with spending on road and equipment repairs, utility consumption and general government services driving the gains.

In relation to distribution of loans and advances, on the production side, both the services and industry sectors are weak in the quarter. Financial institutions were the stand out performer, with 192.5 per cent growth this quarter and contributing 50.0 percentage points to GDP growth. This came after declining by 7.2 per cent in quarter 3 this year. Housing and Land purchases and construction came in softer this quarter growing at -0.7 per cent and 2.3 per cent respectively. Housing and land purchase was 8.2 percentage points stronger than quarter 3 growth at -8.9 per cent. Tourism went up this quarter at 9.9 per cent growth after its seasonal peak at 10.7 per cent growth in quarter one. These indicators (Housing and Land purchases and construction) seem to be almost tracking the fortunes of Vanuatu's residential property market.

Chart B Quarterly Growth (%) of Commercial Bank Sectoral Distribution of Loans and Advances



Source: Reserve Bank of Vanuatu

Table 2 Sectoral Distribution of Commercial Bank Loans and Advances

Quarterly Growth (%)

	2007				2008				2009			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Agriculture	12.6	(3.4)	(6.4)	5.5	(4.3)	1.9	4.1	5.1	31.9	16.4	1.7	0.4
Fisheries	11.7	(4.0)	(8.6)	58.4	0.6	10.7	98.9	2.3	12.5	3.3	(4.9)	(31.4)
Mining & Quarying	1.9	0.3	(46.3)	101.7	23.6	45.7	5.4	5.3	5.5	5.6	5.9	6.7
Manufacturing	(1.9)	2.4	(2.6)	24.5	6.3	4.5	(12.6)	1.5	44.6	17.1	1.2	(4.1)
Tourism	(2.9)	2.3	(9.7)	(25.3)	6.7	11.6	7.6	5.2	10.7	5.7	8.8	9.9
Entertainment & Catering	(33.7)	(3.7)	(11.3)	(14.5)	(4.9)	8.9	19.9	42.8	53.4	28.7	32.1	(16.1)
Transport	3.9	8.6	(2.8)	9.6	9.3	8.1	7.1	10.8	3.9	5.6	(4.9)	7.3
Public Utilities	(4.6)	(4.8)	22.2	32.6	31.3	1.2	0.9	(12.6)	64.4	115.7	2.7	(0.4)
Construction	(3.4)	(3.7)	(3.0)	2.0	13.1	7.1	6.1	11.9	32.6	7.9	14.6	2.3
Financial Institutions	(5.9)	0.7	(6.4)	(7.4)	3.3	6.1	(38.0)	71.3	21.3	10.4	199.7	192.5
Professional & Other Services	1.3	10.8	5.0	(2.2)	(1.3)	26.9	11.4	2.7	2.9	(1.4)	15.0	8.6
Housing & Land Purchases	6.3	9.1	16.1	5.0	5.7	14.7	8.8	7.5	12.7	13.0	(8.9)	(0.7)
Personal: Others	4.9	3.4	11.3	24.7	(8.4)	12.1	22.7	(5.4)	(12.9)	(23.1)	42.8	(9.8)
Miscellaneous	14.9	(1.7)	5.9	(9.2)	(9.0)	15.6	(4.3)	78.6	4.7	12.8	4.6	19.0

Source: Reserve Bank of Vanuatu

Although out of the worst of the downturn, the real sectors of the economy are still struggling against headwinds including the weak Vatu, weak demand for exports and softer local retail demand. Pleasingly, mining, tourism and transport all manage to post higher output growth this quarter at 6.7 per cent, 9.9 per cent and 7.3 per cent in the quarter. For both mining and tourism, this was the fourth quarter of positive quarterly growth; transport meanwhile posted 7.3 per cent of quarterly growth, following its trough in quarter 3 at -4.9 per cent. Mining remains 56.3 per cent down from a year ago.

Reference

http://www.rba.gov.au/graphicalsummary/complete sets (15/01/10)