SUMMARY

- *Growth in the global economy is expected to maintain momentum driven by buoyant exports in emerging Asia, particularly China and India and demand from the developing economies. Strong demand from China and India has pushed up commodity prices exported by Vanuatu such as copra; as well as the incomes of countries such as Australia and New Zealand, in turn boosting tourism in the Pacific region. Growth in many advanced economies remains volatile and fragile.*
- *The Vanuatu economy is showing signs of a pick-up in growth in the third quarter of 2010 compared to the previous two quarters with much of the growth being driven by activity in the tourism and construction sector (private business investment). Private construction projects such as the Tana Ruzet and the Furret Construction project have now started.*
- *The September quarter outcomes are consistent with the 3.0 per cent growth forecast contained in the recently released Budget 2011. The outlook at Budget is for growth to slow from 4.0 per cent in 2009 to 3.0 per cent in 2010, before accelerating to 4.2 per cent in 2011 and a further 4.5 per cent in 2012.*

INTERNATIONAL ECONOMY[1]

The International Monetary Fund (IMF) expects the global economy to expand by 4.8 per cent in 2010 and by 4.2 per cent in 2011. The easing in growth in 2011 is in line with expectation that the slowing that has occurred in the second half of 2010 will continue into the first half of 2011.

The world's economic recovery continued to strengthen during the first half of 2010 with an annual growth rate of around 5.3 per cent, about 0.5 per cent higher than that predicted in the IMF's July 2010 World Economic Outlook (WEO). However, significant concerns remain surrounding the ability of several major European economies to fund their rising budget deficits, which has impacted on the global financial sector and forcing many EU economies to reduce public expenditure. There are signs that this fiscal tightening is negatively affecting growth in the EU region (at a time with global growth is already fragile).

The extent of economic recovery varies across regions, with emerging Asia in the lead. Recent data suggest growth rates may have picked up in the US but have remained weak in Japan. Growth remained strong in emerging and developing economies (in particular China and India). Closer to home, growth rates in the Australia and New Zealand economies have continued to strengthen and are expected to remain robust in 2011.

Many developing economies were less affected by the global recession and now seem to be sharing in the pickup in world trade, and estimates for their growth in 2010 are generally encouraging. By contrast, economies that were hit by the crisis are struggling to return to sustain growth, including in the emerging Europe and the Commonwealth of Independent States, where the recoveries remain much more subdued.

DOMESTIC ECONOMY

The recently released Budget 2011 predicted GDP growth in 2010 will be 3.0 per cent. The September quarter outcomes appear to be consistent with Budget 2011 forecast, with partial data outcomes such as visitor arrivals, copra and beef exports and imports of construction materials continuing to rise in the September quarter. In addition, there are signs that kava exports have risen strongly to their highest level since 2006. The increase in volumes of major export commodities such as copra and beef is in line with the rising global demand.

[1] Source: International Monetary Fund.

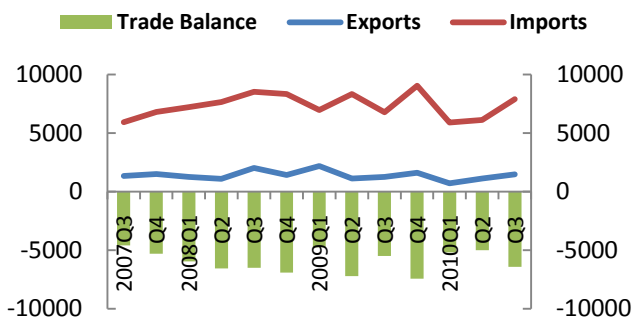
Possibly reflecting the restoration in business confidence, there are signs that a pick-up in construction activity is underway, with growth in the imports of construction materials increasing in the quarter. This data outcome is in line with reports that a large retail project (Tana Ruzet) and a few commercial developments funded by the private sector have commenced. That said, it is not clear at this stage if the recent change in government has had any impact on investor confidence.

Overall, these outcomes points to moderate economic growth over the remaining months of this year. Over the medium term, economic growth is projected to accelerate, with the pickup in activity in the construction sector that began towards the second half of 2010 expected to flow into 2011 and 2012. This development largely reflects the anticipated commencement of a large number of public and private infrastructure projects, some of which were suppose to kick start this year but are now expected to start in 2011. This includes construction of the new court house, a new State Law Office and other significant private construction projects. Other major projects include the construction of the convention center, new international wharf (expected to start in 2012), and the Sub-marine Cable project.

INTERNATIONAL TRADE

The latest September 2010 Quarterly Statistical Indicator from the NSO shows a trade deficit of VT 6,436 million for the September Quarter 2010, indicating a deterioration of VT 931 million compared to the corresponding quarter of 2009. However, compared to the September quarter of 2008, the trade deficit has improved by VT73 million. The sizeable increase in trade deficit over September quarter of 2010 was attributed mainly to an increase in imports reflecting strong domestic demand.

Chart 1: Export, Import and Trade Balance (in Vtmillion)



Source: Vanuatu Statistic Office

EXPORTS AND IMPORTS

Total domestic exports have shown a significant improvement over the previous quarter in all agricultural commodities except cocoa. The improvement in export volumes has seen copra growth increase by 67.4 per cent, coconut oil increase by 52.9 per cent, and beef rises by 22.2 per cent, cowhides increase by 52.8 per cent and finally kava increase by 33.9 per cent.

The increase in agricultural commodity exports is being driven by increases in prices that Vanuatu farmers receive for these commodities.

On the service side, air visitor arrivals for quarter 3 of 2010 were marginally lower (5.9 per cent) than their level a year ago but significantly (37.1 per cent) above the previous quarter. Whilst cruise ship arrivals recorded a 40.5 per cent higher than their level in the corresponding quarter of 2009.
The increase in the trade deficit over the September quarter of 2010 is largely attributed to a rise in imports of all major commodities. Goods imports were up by 29.2 per cent on their level a year ago.

EXPORT (Goods)

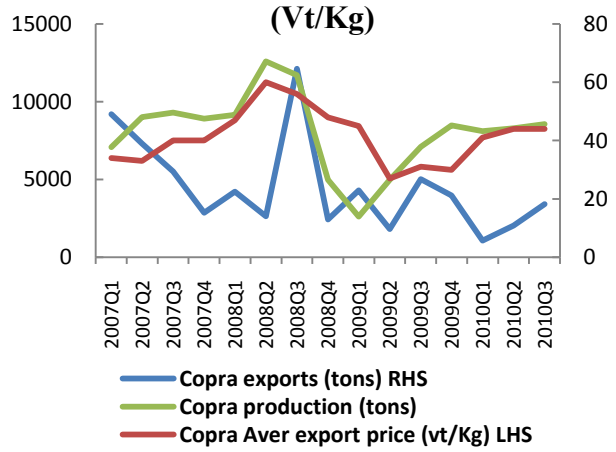
Copra

The coconut industry has seen significant improvements since the beginning of the year with subsequent increases in the price of copra from VT

31,000 per ton (early part of 2010) to VT 41,000 per ton during the second quarter; and two price increases during the month of November.

In early November copra price increased to VT 44,000 per ton and recently as from 24th of November there was a further increase to VT 47,000 per ton. The increase in price was well reflected in the increase in the volume of copra export from 2,042 tons in the previous quarter to 3,419 tons during the reviewed quarter. Total copra production during the September quarter, according to recent NSO September Quarterly Statistical Indicator totaled to 8,870 tons; higher than the previous quarter and the corresponding quarter of 2009 by 14.9 per cent and 24.9 per cent respectively.

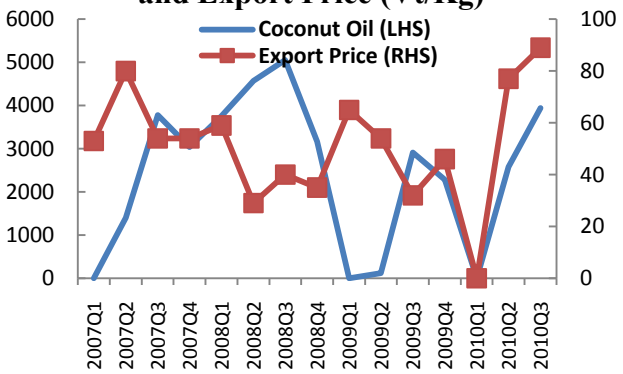
Chart 2: Copra production, Export (tons) and Average Export Price (Vt/Kg)



Source: Vanuatu Statistic Office

Coconut Oil exports during the quarter totaled 3,943 tons which is an increase over the corresponding quarter of 2009 and the previous quarter by 35.5 per cent and 52.9 per cent, respectively. The increase corresponds with the rise in export price from VT 32 per kg in the September quarter of 2009 to VT 89 per kg during the review quarter.

Chart 3: Coconut Oil Export (tons) and Export Price (Vt/Kg)



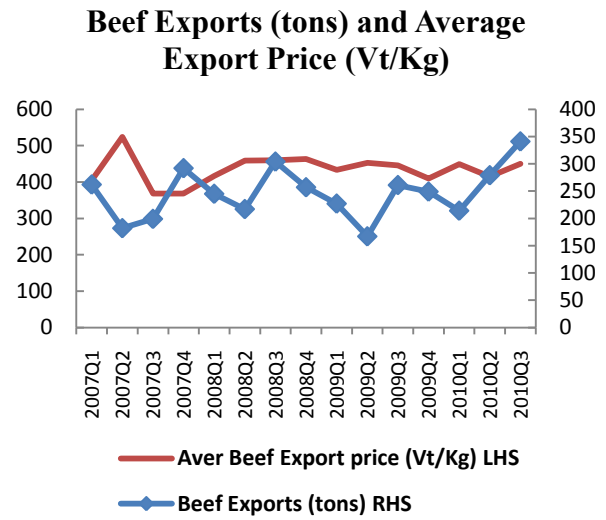
Source: Vanuatu Statistic Office

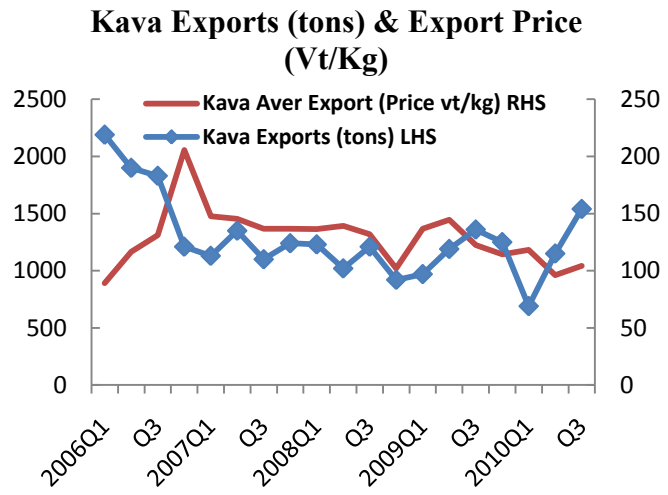
The outlook over the medium term for the copra industry looks bright, in light of current global economic recovery and increase international demand. However, the long run outlook remains vulnerable to both the global demand and prices for raw materials.

Beef

According to the September Quarterly Indicator from NSO, the volume of total cattle slaughtered from the Abattoirs has increased over the previous quarter and the corresponding quarter of 2009 by 23.4 per cent and 44.1 per cent respectively.
The volume of beef exports during the September quarter of 2010 totaled 341 tons, an increase from the previous quarter and the corresponding quarter of 2009 by 22.2 per cent and 30.6 per cent respectively.

Chart 4: Beef Productions, Exports and Prices





The increase over the previous quarter attributed to increase in the average beef export prices from VT 415 per kg to VT 450 per kg in the previous quarter and an increase from VT 446 per kg in the corresponding quarter of 2009 to VT450 per kg during the reviewed quarter. The outlook for the beef industry in the medium term is positive, in light of, the increase price and international demands especially in the major beef markets of Papua New Guinea, Australia and the Solomon Islands. The robust local demand for beef is also contributing to the increase in beef production.

Kava

Kava production and export, according to VCMB, increased this quarter as compared to the previous quarter, although a price floor was imposed. The previous projection was that production will see a decline due to the price floor. However, buyers, according to VCMB, are still buying kava from farmers at different prices; thus, have not affected the level of production during the September quarter. According to the Department of Agriculture, Kava production remains strong with the domestic market maintaining a larger market share.

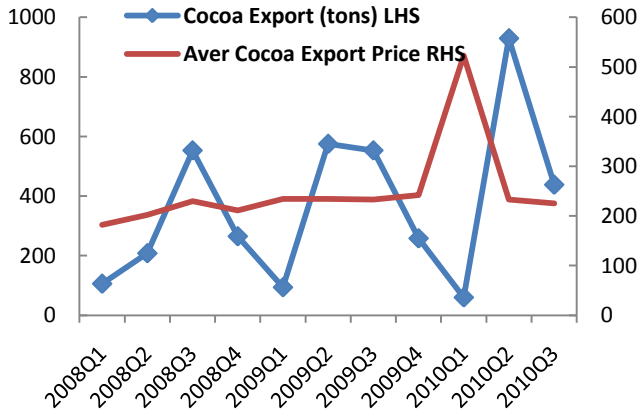
Chart 5: Kava exports

Source: Vanuatu Statistics Office.

Cocoa

The volume of cocoa exported during quarter 3 of 2010 totaled 438 tons, which is lower than the level attained in the previous quarter and the corresponding quarter of 2009 by 52.8 per cent and 20.8 per cent respectively. This also corresponds well with the level of export earnings for the respective quarter. Although past trends shows peak output towards the third quarter, the downtrend during quarter 3 of 2010 is attributed to the low export price (VT 225 per kg) compared to VT233 per kg in both the previous and corresponding quarter of 2009.

Chart 6: Volume of Cocoa Export (tons) and Export Price (Vt/Kg)



Source: Vanuatu Statistic Office

Rice Production (an emerging industry)

Rice production in Vanuatu has great potential for local farmers. However, there are a number of impediments of which a major one, according to the Department of Agriculture, is the lack of proper and efficient rice milling machineries.

With this unfavorable condition, the previous projection of 60 tons for 2010 is not expected to be met. This is reflected in the latest partial data obtained from the Department of Agriculture which shows only 13.5 tons of output that have been produced up to September this year in the Provinces of TAFEA, SHEFA and MALAMPA.

Table 1: Total Rice Production in 2010

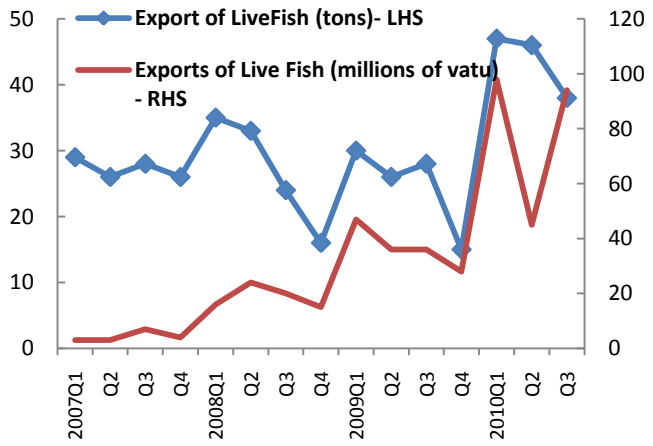
Province	Quantity (tons)
Tafea	10
Shefa	0.275
Malampa	3.245
Penama	0
Sanma	0
Torba	0
Total	13.57

Source: Department of Agriculture

Export of Live Fish

According to partial indicators from NSO, total exports for the September quarter of 2010 stood at 38 tons which is higher than 28 tons recorded in the third quarter of 2009, this is due to the ongoing improvement in the industry with additional facilities and recruitment of qualified workers. Exports for 2010 are projected to be 169 tons, which would be higher than what was exported in 2009.

Chart 7. Exports of Live Fish



Source: Vanuatu Statistic Office

This growth was evidenced from September quarter outcome which saw strong growth in the first, second and third quarter of 2010 with 47 tons, 46 tons and 38 tons respectively.

Coffee

The share of coffee production consumed domestically is about 80 per cent while 20 per cent is exported. The coffee industry is anticipating an increase in production in 2010, as a result of the increase in the number of plants in recent years and improved access to financial services. The financial assistance and Micro loans provided by NBV and the Department of Cooperatives through their savings and loans society, coupled with better management system in place has induced smallholder farmers to increase production. The outlook for coffee in the medium term is for production to remain solid with increasing number of new farms per year.

IMPORTS (Goods)

Total imports during the September quarter 2010 increased over the previous quarter by 20 per cent, The increase is attributed to rise in imports of food and live animals by VT 295 million, mineral fuels by VT 426 million, basic manufactured products by VT 200 million and machines and transport equipment by VT 440 million. The latter, if cars, suggests household consumption levels is recovering.

Imports of Construction Materials

Total imports of construction materials has picked up from a level of VT 175 million a year ago to VT 226 million during the quarter under review.

Chart 8: Total Imports of Construction Materials (in millions of vatu)

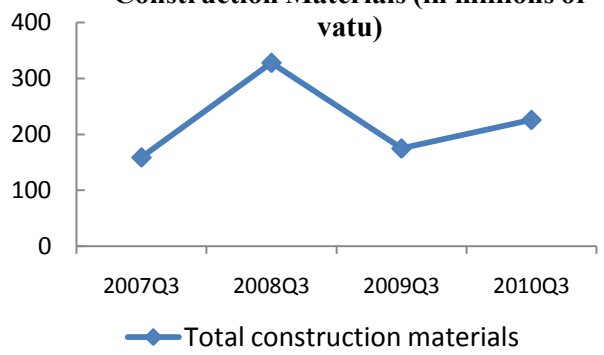
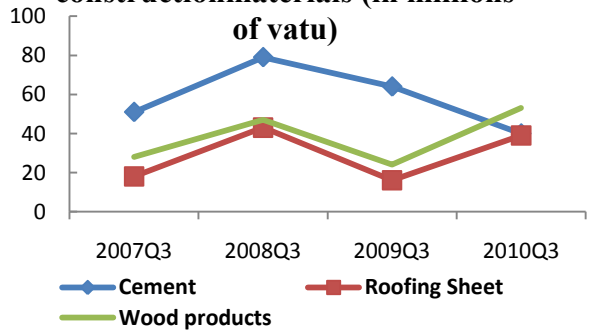


Chart 9: Imports of constructionmaterials (in millions of vatu)



Source: Vanuatu Statistic Office

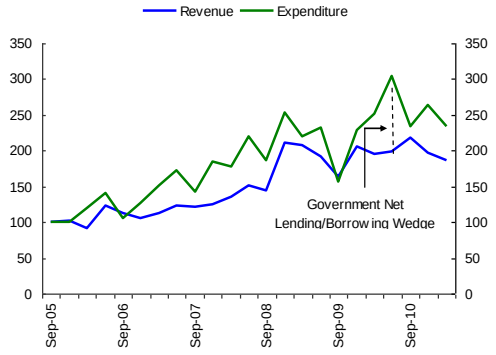
The increase was due to an increase in wood products and roofing sheet imports. Cement, on the other hand has shown a downward trend as from quarter 3 2009 to quarter 3 of 2010. This has been in line also with the latest business survey that most imported cement from the two previous years has been kept in stock.

Fiscal Developments

Despite recording an operating surplus during quarter 3 of 2010, the Government has run an operating deficit for the year so far. Uncertainties continue to surround the strength of economic activity and low levels of revenue collection. However, the increase in visitor arrivals since the middle of 2010 and recent pick up in imports suggests that revenue could increase in the last quarter of 2010.

Compared with the two previous quarters of this year, the levels of VAT and import duty receipts were relatively high in the third quarter. However, the total amount collected for both these major revenue categories for the year so far remains well below initial forecasts as well as equivalent levels at the same point in 2009.

Chart 10: Revenue & Expenditure index for the Government (*2005 Q1=100*)



Source: Department of Finance and Treasury

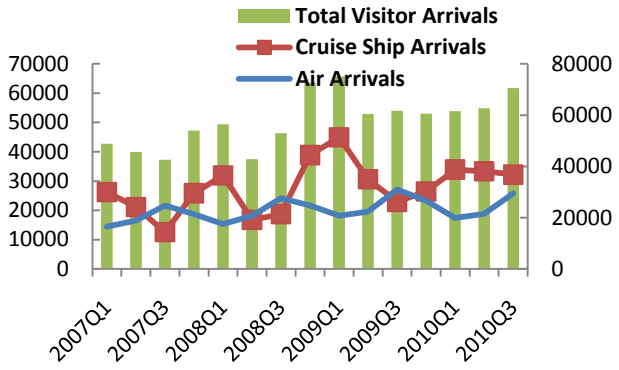
TRADE IN EXPORT SERVICES

Visitor arrivals

Partial indicators from NSO Air visitor arrivals for the Quarter totaled 29,513, which is lower than the corresponding quarter of 2009 by 4.9 per cent. However, this level is higher than the previous quarter by 37.1 per cent.

Cruise ship visitor arrivals for the quarter stood at 32,186; a fall of 3.4 per cent from previous quarter but higher by 40.5 per cent of the corresponding quarter of 2009 and 72.3 per cent of quarter 3 two years previously.

Chart 11: Visitor arrivals (Air and Cruiseship)

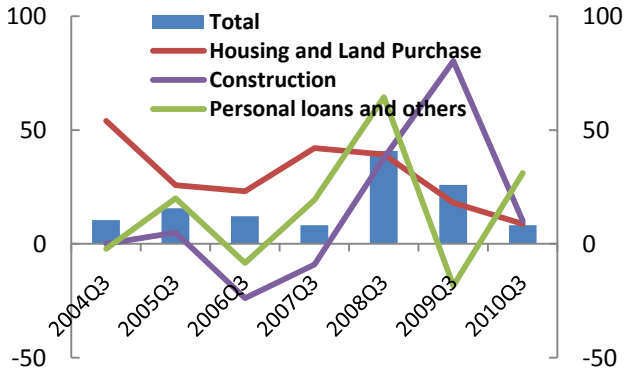


Source: Vanuatu Statistics Office.

PRIVATE SECTOR LENDING

Growth in total private sector credit remained around 8.0 per cent in 2010, this quarter, although down considerably from its annual growth rate of 40.8 per cent two years previously. This signals steady growth. Loans for housing and land purchases were 8.8 per cent, for the construction sector 10 per cent and personal loans were 31.2 per cent higher in the reviewed quarter than a year ago.

Chart 12: Private sector lending (Year ended)

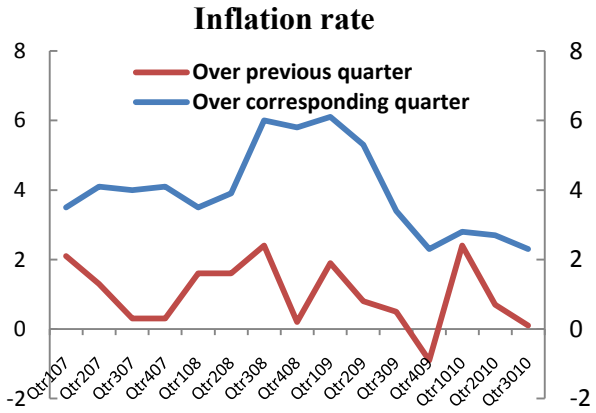


Source: Reserve Bank of Vanuatu.

CONSUMER PRICE INDEX (CPI)

The annual inflation rate, as measured by the Consumer Price Index (CPI) for September quarter of 2010 was 2.3 per cent; showing a slight fall from 2.7 per cent in the previous quarter and 3.4 per cent in the corresponding quarter of 2009. Major items that experienced a decline in their annual inflation rate between the June and September quarter include food, clothing and footwear and household supplies.

Chart 13: Consumer Price Index



Source: National Statistics Office.

EXCHANGE RATES

The exchange rate developments of the vatu with its major trading currencies are depicted in the following charts 14 and 15.

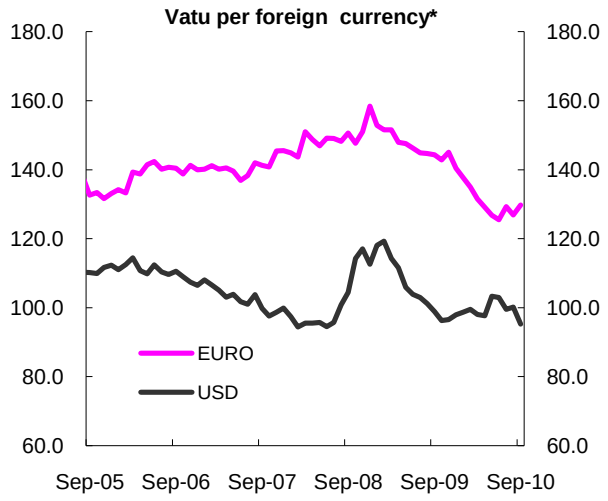
During the month of September 2010, vatu appreciated against the US dollar (USD) by 4.9 per cent over the previous month and by 3.7 per cent from the month of September 2009. On the other hand, Vatu has depreciated against the EURO dollar by 2.3 percent over the previous month, but has appreciated by 10.1 percent from September 2009.

Chart 15 shows the exchange rate of vatu against AUD and Vatu against NZD. During the month of September Vatu depreciated against the Australian

dollar (AUD) by 12.1 per cent over the previous month and 7.1 per cent from September 2009. This should be more favorable for the tourism sector as local prices becomes cheaper for Australian tourists. On the other hand, Vatu has appreciated marginally against the New Zealand Dollar (NZD) over the previous month.

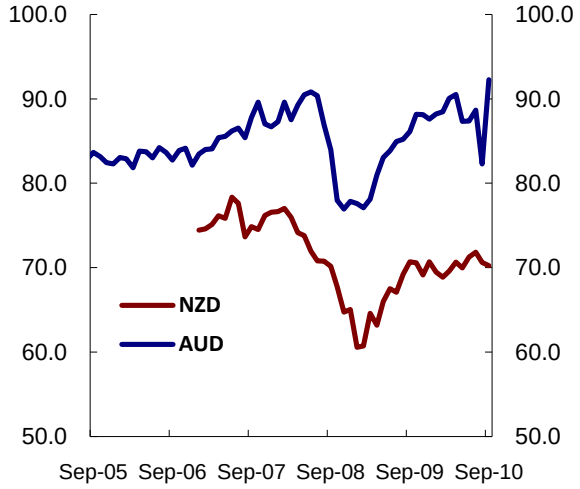
Generally, an appreciation (depreciation) in the exchange rate implies that imports become cheaper (more expensive) while exports become more expensive (cheaper) and therefore less competitive (more competitive).

Chart 14: Vatu per foreign currency^



Source: Reserve Bank of Vanuatu

Chart 15: Vatu per foreign currency^



SUMMARY TABLE

QUARTERLY ECONOMIC DATA	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10
Visitor arrivals by air, (thousands)	27,624	24,778	20,732	22,345	31,030	26,567	19,895	28,144	29,513
Visitor arrivals by air, % y/y	11.9	15.9	18.3	7.8	12.3	7.2	-4.0	31.5	4.9
Visitor arrivals by cruise ship (thousands)	18,673	38,859	44,898	30,587	22,914	26,419	33,930	33,316	32,186
Visitor arrivals by cruise ship % y/y	48.3	50.4	40.7	83.2	22.7	-32.0	-24.4	8.9	3.4
Exports (values), % y/y	70.1	-0.3	5.7	2.5	-45.6	-5.1	-46.7	46.5	36.6
Copra, % y/y	131.9	-5.3	-43.1	-83.1	-70.6	-12.1	-84.9	82.7	5.7
Beef, % y/y	98.7	23.1	10.8	-23.0	-20.9	-24.3	-8.8	52.2	31.3
Cocoa, % y/y	1.9	50.2	16.1	228.9	-5.4	6.8	-32.0	40.8	-21.9
Imports (Values), % y/y	53.1	50.2	41.8	41.3	38.7	52.5	33.5	26.5	20
Consumption goods % y/y	44.0	22.3	-3.5	-8.5	-22.6	8.8	-15.4	-12	20
Construction materials, % y/y	46.1	21.4	-22.7	8.9	-17.0	24.5	17.7	-32.9	29.1
Trade Balance, goods and services (Vatu million)	-1664	-1745	718	-915	-245	-2145	512		
Lending data, % y/y (total)	41.7	43.7	40.1	29.4	22.7	19.8	12.5	12.6	8.2
to households	48.2	31.9	32.7	16.9	3.7	4.7	5.9	13.4	31.2
to businesses	35.2	58.6	48.2	43.5	44.3	35.4	18.6	11.8	5.3
Exchange rates									
AUD	87.1	77.6	77.6	82.6	85.4	88.0	88.9	87.4	92.25
USD	100.3	114.6	117.2	107.1	101.0	96.9	98.8	103.0	93.23
NZD	70.6	65.8	62.0	65.6	69.0	70.1	69.3	81.3	70.24
Euro	149.3	152.4	152.0	147.3	144.6	142.8	134.8	125.5	129.75
Consumer Price Index, % y/y	6.0	5.8	6.1	6.4	3.4	2.3	2.8	2.7	2.3

Source: National Statistics Office, Reserve Bank Vanuatu.