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Our Vision:

For Economics & Markets Research to be the most respected, sought-after and commercially valued source of economics and markets research and information on Australia, New Zealand, the Pacific and Asia.

Highlights

- The Pacific region will not escape negative spillovers from the global economy, which will contract this year for the first time since World War II.
- The main contagion channels from the advanced economies at the epicentre of the crisis to the Pacific will be tourism/remittances and commodities prices.
 - Lower discretionary spending in the advanced economies will lower tourism flows to the region as well as remittances.
 - Lower commodity prices stemming from the sharp global slowdown will have a negative impact on the resource/commodity exporting economies.
- Overall, growth will slow markedly throughout much of the region, although financial sector contagion is expected to be relatively modest given weak linkages to the rest of the world. Commodity-dependent economies will do better in real terms.
- Inflation is no longer a threat and, where feasible, both monetary and fiscal settings should be eased, albeit within the context of medium-term sustainability.
- The timing of a recovery for the Pacific region depends heavily on developments in the advanced economies. Our current call is for a gradual recovery to take hold in 2010. The risk is for a prolonged, though not necessarily deeper, downturn.

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Overview – The Global Economic Outlook Remains Challenging¹

Near-term prospects for the global economy have continued to deteriorate over the first few months of this year. In company with institutions such as the IMF and the World Bank, we now expect that the global economy will contract this year, for the first time since the end of World War II. And the ensuing recovery, which we expect to have begun by the turn of the year, is likely to be unusually slow and gradual.

World economic forecasts

GDP growth (%)	2008	2009(f)	2010(f)	2011(f)
Australia	2.1	-0.9	0.7	2.9
New Zealand	0.2	-2.8	2.4	4.7
United States	1.1	-2.6	1.8	2.2
Euro zone	0.7	-2.4	0.4	1.2
Japan	-0.7	-3.8	0.4	0.7
China	9.1	6.9	8.5	10.0
Other East Asia*	3.2	0.4	4.4	5.6
World (PPP)	3.0	-0.1	3.0	3.9

*Asia excl. Japan & China

The contours of the dramatic downturn in economic activity have become clearer. US household net worth dropped by 9% in the fourth quarter of 2008, bringing the cumulative decline since mid-2007 to 20%. This is, by a wide margin, the largest fall in personal wealth in the US since at least the end of World War II. Much the same appears to have occurred in the UK as household net financial worth (i.e. excluding real estate) fell by 16% between the second quarter of 2007 and the third quarter of 2008. Net wealth is also likely to have declined, albeit by smaller proportions, in most other countries. These large wealth declines prompted a surge in household saving and abrupt falls in spending, especially on big ticket items such as motor vehicles and housing.

The dramatic declines in spending on consumer durables and housing in turn led to an unanticipated surge in retailer and producer inventories. And this is where the declines in wealth combined with the financial crisis to produce the economic firestorm which spread across the world in late 2008. With manufacturing supply chains having become increasingly globalised over the past two decades, it was inevitable that this inventory cycle would be transmitted rapidly around the world through a slump in merchandise trade. Moreover, since merchandise trade is also heavily dependent on finance (given the lags between the shipment of and the receipt of payment for goods), the impact of the financial crisis on the availability of trade finance magnified the drop in trade flows.

The trade slump has dragged Asia into the vortex as most countries have experienced sharp year-on-year export declines. For those economies where exports represent a very large proportion of GDP (such as Korea, Taiwan, Malaysia and Singapore), or where exports have been the most important source of recent economic growth (such as Japan), the result has been sharper contractions in activity than in the US or Europe, where the financial crisis originated. China has also been affected by the global trade slump, although the abrupt slowdown in the second half of 2008 owes more to the collapse of China's own construction bubble. There are encouraging indications that the fiscal, monetary and other policy actions undertaken by the Chinese authorities since November 2008 are beginning to take effect. But recovery elsewhere in Asia will require a sustained increase in domestic demand, as well as a revival in external demand.

Despite the rally in equity markets during March 2009, the global financial crisis is not yet over and it will not be over until confidence in the solvency of the global banking system has been restored. That in turn requires credible programs to ensure that banks have enough capital to support normal levels of lending after providing for the impact of the economic slump on the assets which remain on their balance sheets. The Public-Private Investment Program unveiled by US Treasury Secretary Geithner in late March appears to provide much more credible detail as to the means by which 'toxic assets' will be removed from the balance sheets of American banks, and as such may represent a key step in drawing the crisis to a close. At the time of writing, however, it remains unclear to what extent the program will draw in private capital.

¹ This sub-section draws liberally from the ANZ *Economic Outlook* (June quarter 2009).

In combating the crisis, unconventional economic policy is vital. The current slump in the United States and Europe has in several key respects more in common with the economic downturns of the 19th and early 20th centuries than with the ‘recessions’ that have occurred since 1945. Most post-war recessions were induced by tight monetary policy; and recovery from them was prompted by easier monetary policy, sometimes accompanied by easier fiscal policy. By contrast, monetary policy played very little role in inducing the current downturn; rather, it has resulted primarily from a collapse in asset prices and an abrupt reduction in both the demand for and supply of credit. This, emphatically, does *not* mean that the current slump must turn out to be as deep or as protracted as the Great Depression. But it *does* mean that the economic policies which have worked in post-war recessions will probably not work in current circumstances. And it also means that governments and central banks *have* to implement policies which, in more ‘normal’ circumstances, would be considered risky or even ‘irresponsible’.

In that context, the willingness of central banks to engage in quantitative easing (or printing money) in order to expand their balance sheets, including by purchasing government bonds, is appropriate rather than irresponsible. Comparisons with the hyperinflations in Weimar Germany or present-day Zimbabwe border on being fatuous. The situation in the US, the UK and Japan (among others) today is one of deficient demand, not deficient supply. Rising inflation (let alone hyper-inflation) is a remote possibility in such circumstances; indeed, deflation looms as a greater risk than inflation in the period immediately ahead, and deflation is much harder to cure than inflation.

Central banks do need to formulate ‘exit strategies’ from ‘quantitative easing’ to guard against the possibility of rising inflation once the financial system returns to normal; and governments need to devise credible strategies for restoring fiscal sustainability once economic recovery begins (strategies which may well entail tax increases). But the alternative to what central banks and governments are now groping towards is *not* standing back and allowing the slump to run its course; rather, it is rising public pressure for protectionist and other measures which would not only be economically devastating but also threaten the maintenance of peaceful relations among nations.

The likely impact of the crisis on the Pacific region

When assessing the likely impact of the crisis on the Pacific, we should keep in mind that we are in the midst of a global *economic* crisis along with a trans-Atlantic *financial* crisis. Thus, the main transmission channels to the Pacific will be real rather than through the banking or financial sector. We would highlight the following four effects on the region:

- **Commodity prices.** The sharp slowdown in global demand that began last year has put downward pressure on a range of commodity prices, including for those goods (including petroleum and raw materials) exported by some Pacific economies. According to the IMF’s *World Economic Outlook* (WEO) of April 2009, oil prices are projected to fall by 40% in USD terms this year; food prices are slated to fall by 28% while agricultural raw material prices will decline by 22%. Lower commodity prices will reduce export and import values, lower incomes of commodity producers (as well as government revenues based on those incomes or related profits) but benefit consumers and other end-users. Overall, “long” commodity economies—Timor-Leste, Papua New Guinea and Solomon Islands—will see the largest negative effects.
- **Tourism and remittances.** Related to the decline in discretionary spending in the advanced economies will be a decline in tourism, which is typically considered to be a luxury good whose consumption can be postponed. Dependence on the source markets of Australia, Japan, New Zealand and the United States, all of which are near or in recession, suggests that tourism related flows to the Pacific region will weaken, perhaps substantially. A similar argument applies to remittances, as employment and incomes of overseas Pacific region nationals will be negatively affected by the crisis, with likely knock-on effects on the amount of remittances sent to the region. The tourism and remittance channel will be most important for Fiji, Samoa, Tonga and Vanuatu.
- **Wealth effects.** While direct contagion from the trans-Atlantic banking crisis on the Pacific will be modest, the asset price effects will be felt, particular in those countries managing sovereign wealth funds or their equivalents: Papua New Guinea and Timor Leste. The impact will depend heavily on the fixed income-equity mix of these portfolios, with the former outperforming the latter, along with the currency composition, where USD and JPY exposures would have benefited since the onset of the crisis owing from “flight to quality” effects.

- **Trade volumes.** The global recession has resulted in a sharp decline in world trade volumes, which has affected all regions, including the Pacific. According to the IMF's WEO, trade volumes are projected decline by 11.5% in 2009 following growth of 6.6% in 2007 and 3.2% in 2008. The available evidence so far suggests that consumption of discretionary goods—as opposed to necessities like food and clothing—have been most affected as wealth and incomes decline, as evidenced by the steep drop in shipments of autos and electronic good from East Asian economies. Nonetheless, the slowdown will also lead to a slowdown in petroleum products and raw materials, which as noted are exported by some economies in the region. This volume effect will compound the price effect and put further pressure on current accounts, company profits and government revenues. Overall, we suspect that the impact of the crisis on trade volumes for the Pacific will be relatively modest.

To sum up, the impact of the crisis on the Pacific will be negative but with differing effects based mainly on (i) the composition of output and (ii) dependence on “discretionary” flows to finance the balance of payments. The resource dependent economies will see a decline in nominal incomes owing to lower commodity prices, but we suspect the real declines will be manageable, particularly with commodities such as oil where production is less elastic. Economies dependent on the combination of tourism and remittance flows will likely be harder hit as these discretionary activities will be more affected by the sharp downturn in the advanced economies. In these instances, slower inflows from abroad will reduce transfer payment related income, and thus expenditure and GDP.

The inflation fears of mid-2008, which at least in the first round were related largely to food and commodity prices, have clearly peaked so price pressures will not be a major concern for the Pacific in the near term. Relatedly, a slower pace of activity in most countries implies slower credit growth. Taken together, these imply that monetary conditions can be eased in order to cushion the effects of the downturn. Fiscal policy, where available, can help as well, although a number of countries face binding constraints from donors and may need to hold the line on public wages in order to make room for other spending. For those few countries with public assets accumulated during the resource price boom, these can be drawn (or the rate of accumulation slowed) as well in order to cushion the downturn, as long as this is done in the context of medium-term sustainability.

The risks for the Pacific region are on the downside in 2009. While the worst of the crisis appears to be over at the time of this writing, the state of advanced country banking systems and the state of the US housing market remain key unknowns. Until the former is resolved and the latter stabilises, the pre-conditions for a recovery will not be met. Moreover, once these are met, the pace at which risk appetite is rebuild and the rate at which consumers begin to spend on discretionary items, which would determine the pace of the recovery, is another key unknown. (Corporates look to be in reasonably good shape, so the ability to initiate a CAPEX cycle to meet any rise in consumer demand is less of a concern.) For the small, open and externally-dependent economies of the Pacific, this would be a longer, though not necessarily deeper, slowdown.

Financial Markets Update

Exchange Rates:

- Volatility in financial markets has abated since the peak in November 2008, but nevertheless remains elevated. The pace of gains in the US dollar has similarly slowed in line with episodes of improved risk appetite during December and March.
- The Australian and New Zealand dollars have benefited from the recent improvement in risk appetite, having rallied 12% and 16%, respectively, from March lows. Since the Lehman Brothers' bankruptcy in mid-September of last year—which triggered the meltdown in global financial markets—the Australian and New Zealand dollars have each shed roughly 12% against the US dollar.
- Most currencies across the Pacific have experienced similar directional swings over the last six months, albeit with much less volatility. The notable exception has been the Kina, which has tumbled 14% against the US dollar since mid-September, including a drop of 11% year-to-date.

Commodities:

- Having tumbled 45% from a year ago, commodity prices appear to have bottomed. The CRB commodity index has been broadly stable since December, underpinned by stockpiling programmes and, more recently, hopes that global demand will improve in the second half of 2009.
- Oil prices have also stabilized, with the one-month NYMEX futures contract for light sweet crude oil hovering around the \$50/bbl mark since the middle of March, above the December low near \$32/bbl. The corresponding 12-month contract is priced just above \$60/bbl, suggesting further improvement ahead. Signs that China's fiscal stimulus measures are gaining some traction have helped to arrest the downtrend in oil prices.
- Gold has been in a downtrend since hitting a peak of \$1,006/oz in February, currently trading just below the 900/oz threshold. Improved risk appetite and an announcement by the IMF that it is contemplating the sale of 403.3 metric tons to boost its finances have weighed on the precious metal as of late.
- Base metal prices are expected to benefit from further signs of recovery in China, particularly in the second half of 2009. The Chinese government's stockpiling program has likely finished for the time being. However, South Korea has recently embarked on its own stockpiling program.
- Commodity prices are expected to recover in the second half of 2009. Improvement will likely be tepid, in tandem with the shallow recovery that we anticipate in global demand.

Tamara Henderson

FX and Policy Interest Rate Forecasts

		Mar 09	Current	Jun 09	Sep 09	Dec 09	Mar 10	Jun 10	Sep 10
Fiji	FJD/USD, eop	0.558	0.565	0.537	0.520	0.499	0.482	0.486	0.491
	FJD/AUD, eop	0.807	0.782	0.814	0.825	0.845	0.860	0.852	0.846
	Short term rates*	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25
Papua New Guinea	PGK/USD, eop	0.333	0.339	0.320	0.320	0.350	0.350	0.360	0.360
	PGK/AUD, eop	0.481	0.469	0.485	0.508	0.593	0.625	0.632	0.621
	Short term rates**	8.00	8.00	8.00	8.00	8.00	8.50	8.50	9.00
Samoa	WST/USD, eop	0.336	0.343	0.335	0.324	0.311	0.300	0.303	0.306
	WST/AUD, eop	0.487	0.474	0.507	0.515	0.528	0.536	0.532	0.527
Solomon Islands	USD/SBD, eop	7.978	8.089	8.220	8.411	8.720	9.064	9.034	9.034
	AUD/SBD, eop	5.515	5.846	5.425	5.299	5.145	5.076	5.149	5.240
Tonga	USD/TOP, eop	2.165	2.130	2.071	1.973	1.850	1.763	1.792	1.792
	AUD/TOP, eop	1.497	1.539	1.367	1.243	1.091	0.987	1.021	1.039
Vanuatu	USD/VUV, eop	114.3	112.3	118.1	121.9	127.5	132.0	130.5	130.5
	AUD/VUV, eop	79.02	81.14	77.93	76.83	75.23	73.94	74.38	75.68
	Short term rates***	6.00	6.00	5.75	5.75	5.75	5.75	5.75	5.75

Note: The source of FX data is from Bloomberg. As the currencies are illiquid with wide bid/offer spreads, the rate published is only indicative. (*) 91-day RBF notes, (**) Kina Facility Rate, (***) Discount rate, (Current) 13 April 2009.

Macroeconomic Forecasts

Real GDP Growth (%)

	2008e	2009f	2010f
Fiji	1.2	-2.0	-1.0
PNG	7.0	5.0	6.5
Samoa	0.3	-1.0	1.6
Solomon Is.	6.4	3.0	3.0
Timor-Leste	10.0	8.0	8.0
Tonga	1.2	-2.0	0.0
Vanuatu	6.6	4.0	4.5

Nominal GDP (US\$ bn)

	2008e	2009f	2010f
Fiji	3.4	3.4	3.5
PNG	8.1	9.2	10.4
Samoa	0.5	0.5	0.6
Solomon Is.	0.5	0.5	0.5
Timor-Leste	0.4	0.4	0.5
Tonga	0.3	0.3	0.3
Vanuatu	0.5	0.5	0.6

Inflation (%)

	2008	2009f	2010f
Fiji	7.8	3.0	3.0
PNG	10.7	8.0	6.0
Samoa	11.5	7.0	4.0
Solomon Is.	16.5	9.0	5.0
Timor-Leste	8.4	6.0	6.0
Tonga	9.9	5.0	2.0
Vanuatu	5.8	4.0	3.5

Fiscal Balance (% of GDP)

	2008e	2009f	2010f
Fiji	-1.5	-3.5	-2.5
PNG	4.5	-1.8	-1.2
Samoa	-3.2	-5.5	-3.0
Solomon Is.	-5.6	-3.0	-3.0
Timor-Leste	-43.0	-65.0	-60.0
Tonga	2.0	-1.5	-1.0
Vanuatu	2.3	1.5	1.8

Current Account Balance (% of GDP)

	2008e	2009f	2010f
Fiji	-21.0	-25.0	-25.0
PNG	2.8	-7.0	-6.0
Samoa	-9.1	-8.4	-5.3
Solomon Is.	-4.9	-10.1	-12.1
Timor-Leste	408.3	66.2	49.4
Tonga	-10.4	-8.8	-8.7
Vanuatu	-11.4	-13.2	-13.0

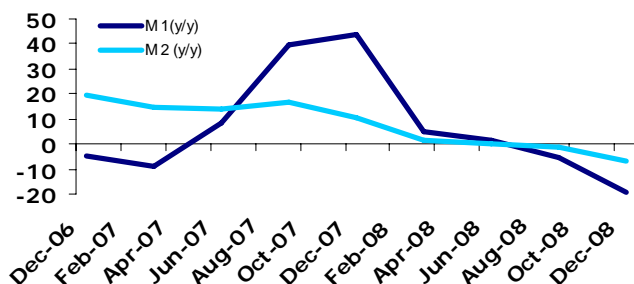
Foreign Exchange Reserve (US\$ mn)

	2008e	2009f	2010f
Fiji	559	530	500
PNG	2,090	2,200	2,400
Samoa	81	95	105
Solomon Is.	93	85	80
Timor-Leste	4,640	5,333	6,676
Tonga	58	54	50
Vanuatu	109	105	100

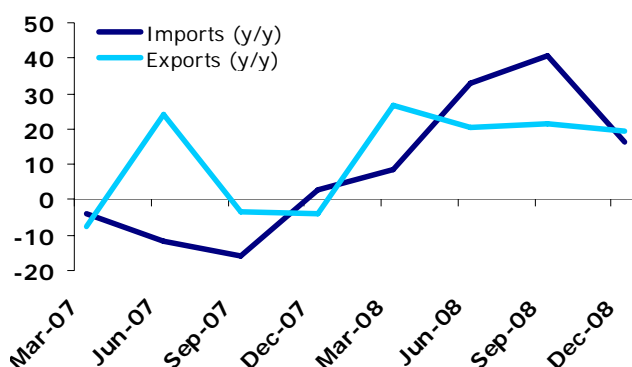
Sources: Asian Development Bank, various country websites, ANZ Economics.

Country Update: Fiji

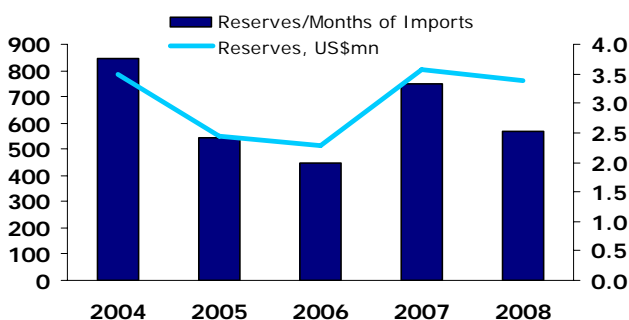
Fiji - Monetary Aggregates



Fiji - Trade Developments



Fiji - FX Reserves



In response to persistent balance of payments pressures, including falling reserves, on 15 April the authorities devalued the FJD by 20% and imposed capital controls. Indicators suggest that activity has slowed, including in response to the global recession. Labour market developments are mixed, with the number of new taxpayers declining, but with job advertisements rising. The outlook will remain weak until tourist, remittance and official flows return to more normal levels.

- Money and liquidity conditions remain tight. Narrow money contracted by 19.7% (y/y) in December while broad money fell 6.9%, reflecting a steep decline in demand deposits. Meanwhile, domestic credit growth slowed to 4.8%. Lending rates remained relatively high in early 2009 at 7.86% as of January and new time deposit rates rose to 5.63% in the same period.
- Inflation has declined along with growth. Consumer prices rose 1.9% (y/y) in February 2009, down from 6.1% January and 7.6% a year earlier. Food price inflation was 7.9%, down from 15.5% in January and 10.7% in February 2008. A weaker currency following the devaluation imparts some upside to inflation.
- The external position continues to weaken. Domestic exports rose by 18.6% in 2008 following a marginal decline in 2007, led by sugar, fish and gold. However, imports grew even faster, by 23%, in 2008 and the trade deficit reached \$2.1bn or a whopping 34.7% of GDP (up from 13.7% of GDP in 2007). Reported official reserves declined to \$672mn at end-Feb 2009, equivalent to 2.7 months of import cover, down from 3.4 months a year earlier.
- 2009 looks like a difficult year for Fiji. GDP growth is likely to fall well below the official forecast of 2.4% (ANZ expects negative growth). Structural balance of payments pressures are likely to persist although the combination of slower growth and imports, the devaluation and the imposition of capital controls may help dampen pressures in the short run.
- A lasting solution to Fiji's current dilemma requires the return of tourism and remittance flows and foreign credits that can bolster consumption and capital accumulation, and raise productive potential.

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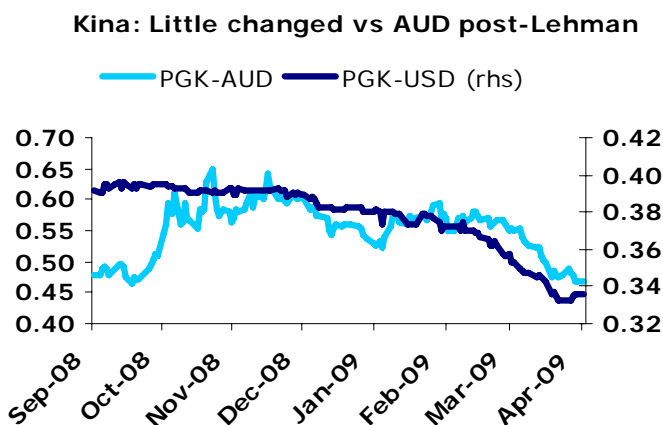
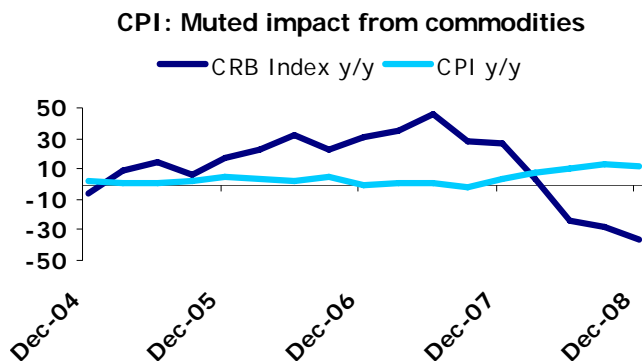
Economic Data – Fiji

Quarterly data	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Consumer Price Index, % YOY	3.6	6.4	5.2	3.9	7.6	6.8	N/A	N/A
Domestic Credit, % YOY	16.7	12.5	8.5	3.2	3.3	3.3	N/A	N/A
Exports, % YOY	-3.1	34.2	-9.7	5.4	39.6	19.6	N/A	N/A
Imports, % YOY	0.2	-3.7	-8.9	12.5	19.6	43.4	N/A	N/A
Trade Balance, US\$ mn	-253	-240	-274	-310	-275	-384	N/A	N/A
Official Reserves, US\$ mn	473	535	539	615	602	585	N/A	N/A

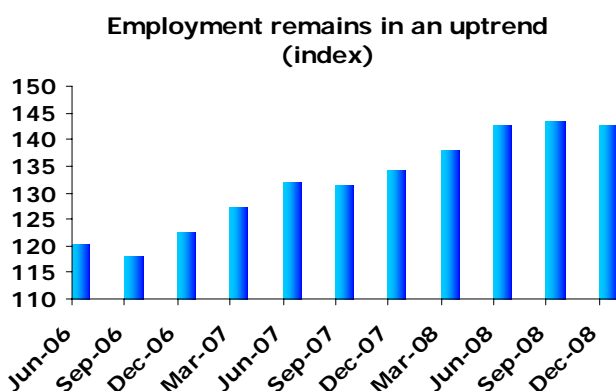
Sources: Reserve Bank of Fiji, ADB, IMF

Country Update: Papua New Guinea

GDP growth has moderated, while inflation remains above the BPNG's apparent comfort level. Meanwhile, global demand collapsed in Q4 of 2008—dragging the CRB commodity price index 45% (y/y) lower—and, by all indications, global trade failed to revive in Q1. Nevertheless, domestic demand momentum remained robust into year-end 2008, and BPNG surveys suggest that sentiment remains buoyant given the prospective LNG project.



- Acute risk aversion from the meltdown in global financial markets has produced a 14% surge in the USD versus the kina since the Lehman Brothers bankruptcy in Sep. Over the same period, the AUD tumbled roughly 12% against the greenback, leaving the kina little changed against the currency of its largest trading partner. As such, exchange rate movements—the most important determinant of inflation in PNG, according to the IMF—would seem to have been broadly balanced over the last six months.
- In its March assessment of monetary policy, BPNG maintained its tightening bias, citing numerous upside risks to inflation and omitting any reference to downside growth risks. As a testament to the robustness of domestic demand, BPNG is a rare sight: a monetary authority in the G10-Asia-Pacific realm that has yet to shift its focus on downside risks from growth. Going forward, BPNG will likely opt for steady policy rates in 2009, as the bank navigates fierce cross-currents in the local and global economies.
- Given our expectations for a still challenging external environment throughout 2009 and what is likely to be a protracted recovery period for global trade, commodity prices and foreign investment—we have downgraded our GDP forecast, looking for growth of 5.0% in 2009 compared with our Nov projection for 5.5% and estimated 7.0% growth in 2008.



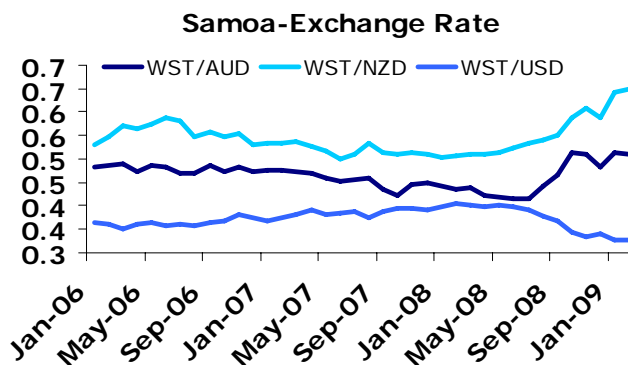
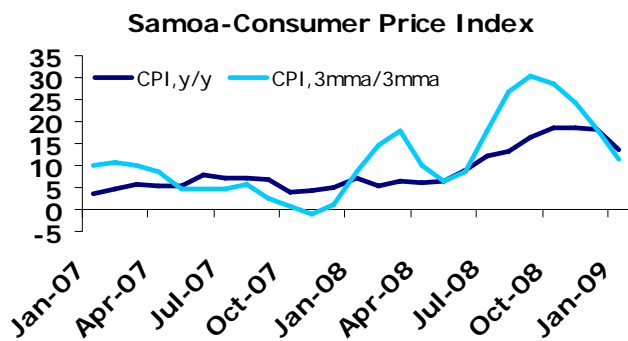
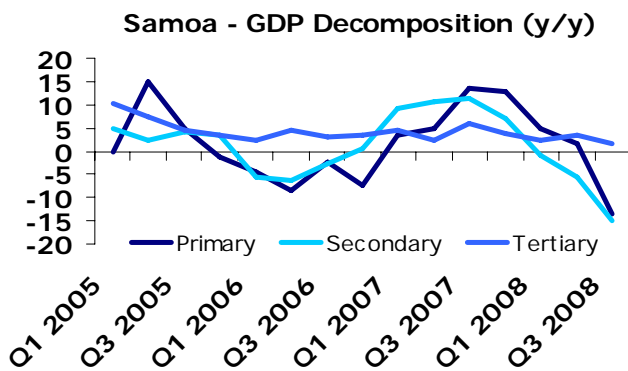
Tamara Henderson

Economic Data – Papua New Guinea

Quarterly data	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Employment Index, % YOY	9.9	9.5	11.7	10.4	8.5	8.3	9.3	6.3
Consumer Price Index, % YOY	1.1	1.0	-1.6	3.2	7.5	10.7	13.5	11.2
- BPNG Trimmed mean, % 000	2.5	2.9	3.6	5.3	8.7	11.4	13.0	11.7
- NSO exclusion based, % 000	7.1	7.5	9.0	6.3	7.7	10.2	12.2	11.0
Exports, % YOY	7.3	14.2	9.3	21.8	37.4	12.2	N/A	N/A
Imports, % YOY	37.4	31.3	28.4	36.0	17.3	25.0	N/A	N/A
Trade Balance, US\$ mn	347	748	498	499	607	761	N/A	N/A
Foreign Exchange Reserves, US\$m	1,364	1,545	1,856	2,053	2,039	2,418	2,454	2,093

Sources: Bank of Papua New Guinea and IMF

Country Update: Samoa



Growth fell sharply in 2008 as manufacturing activity declined along with tourist receipts and remittances. Inflation surged on higher food and commodity prices, but the risks have passed. In order to boost domestic demand, the central bank eased monetary policy further in February 2009, and the government unveiled a planned budget deficit equivalent to 6% of GDP for FY09. The outlook is weak for this year.

- GDP growth fell to just 0.3% in 2008 following 5.5% growth in 2007. Available data show that primary and secondary industry output fell by 13.4% and 14.9%, respectively in the first three quarters of 2008, while the tertiary industry reported growth of 1.8%.
- The trade account of the balance of payments remained in large deficit (almost one-half of GDP) in 2008 as exports fell by 28.7%. Imports rose owing to the spike in global commodity and food prices. The trend reversed in January, as exports rose 18.5% (y/y), while imports declined by 32.7%, allowing the monthly trade deficit to narrow to US\$12.9mn, a two-year low.
- Inflation, which was relatively high in the second half of 2008, has started to ease, reflecting lower food and fuel prices. Headline inflation slowed to 13.6% in January from 18.5% in December. Monthly inflation fell 0.5% after ten consecutive months of strong growth.
- Tourism receipts fell by an estimated 7.6% in real terms in 2008. Private remittances fell by 4.6% for the year, with most of the decline coming in the latter part of the year, led by remittances from the US.
- To boost the economy, the Central Bank of Samoa (CBS) cut the lending rate for commercial banks by 280bps to 5% in February. In addition, the term for such lending was increased from 7 to 30 days. In order to ease the pressure on international reserves, CBS has discouraged outflows of foreign exchange.
- Year-to-date, the tala has depreciated by 4.1% against the US dollar, but has strengthened 5.4% against the AUD and 10.9% against the NZD.
- The economy is likely to contract in 2009 with continued weak manufacturing, tourism receipts and remittances. Moreover, we see the risks to growth on the downside.

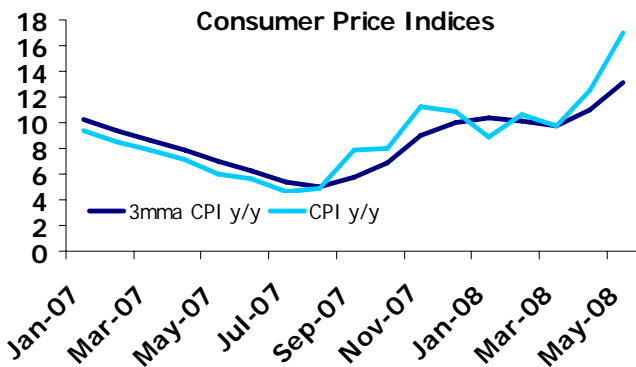
Zhou Hao

Economic Data – Samoa

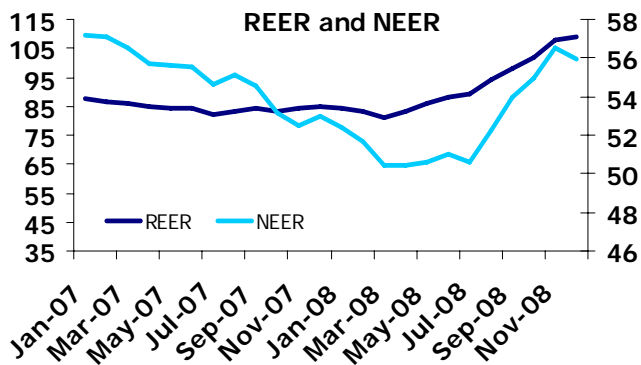
Quarterly Data	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Consumer Price Index, % YOY	4.6	6.3	7.0	4.5	6.3	7.2	13.9	18.4
Domestic Credit, % YOY	21.1	16.3	20.1	15.9	8.4	11.9	6.7	9.9
Exports, % YOY	22.1	55.2	72.0	26.5	-8.3	-27.8	-27.0	-44.9
Imports, % YOY	2.4	15.3	11.8	-12.0	14.1	-1.6	13.6	12.1
Trade Balance, US\$ mn	-47.2	-52.3	-61.9	-50.2	-54.4	-52.5	-72.2	-58.5
Foreign Exchange Reserves, US\$ mn	76.2	80.4	82.3	90.2	100.6	101.5	90.2	81.3

Sources: Central Bank of Samoa, Samoa Ministry of Finance

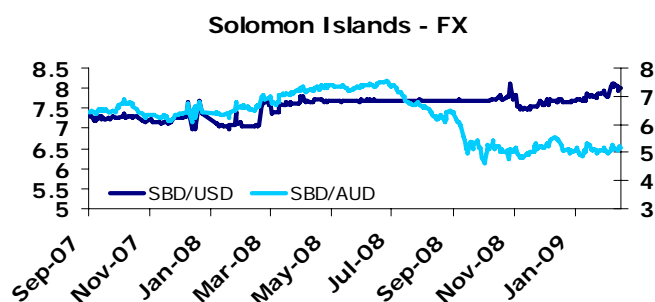
Country Update: Solomon Islands



Growth should slow further and inflation should continue to decline reflecting the drop in commodity prices, particularly for logging. Liquidity with commercial banks has declined due action by the CBSI to reign in credit growth. Going forward, government expenditure needs to be curbed and the current account will come under stress as global commodity prices remain low. Diversification of the export base remains a key challenge.



- The IMF reaffirmed its GDP growth projections for 2008 and 2009 at 7.3% and 4.0%, respectively. Activity has been driven by the productive response to high export prices, particularly in the logging sector, and expansionary fiscal policy.
- Inflation declined in the last quarter of 2008 from an uncomfortable level of 15.9% (y/y) in Q3 as commodity prices fell and activity eased. The Solomon Islands dollar, adjusting to a weakening balance of payments, depreciated by 13% (y/y) as of end-March, adding some upside pressure to inflation.
- The current account balance has deteriorated due to a heavy reliance on imports, and declining tourism and logging related export earnings. Reserve coverage has fallen below the benchmark level equivalent to three months of import cover.
- Tourism receipts fell from \$98mn in Sep 2008 to \$83mn in Nov. On a y/y basis, receipts were down 31.5%.
- Official support from Australia and New Zealand has increased. NZAID provided \$51,000 towards flood relief in 2009 while Australia has agreed to develop economic infrastructure and improve governance.
- 2009 looks to be a challenging year. Growth will continue to slow due to external factors. At the same time, the authorities will need to rein in credit on the monetary side and curb expenditures on the fiscal side in order to control the rate of absorption and protect the balance of payments. A raft of structural reforms, including but not limited to economic diversification, are required to bolster medium-term growth prospects.



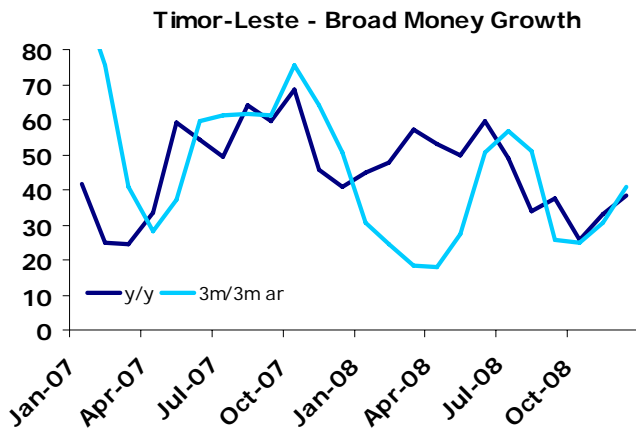
Vimal Balasubramaniam

Economic Data – Solomon Islands

Quarterly data	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Domestic Credit, % YOY	56.6	54.9	56.3	58.5	63.4	73.9	N/A	N/A
Consumer Price Index, % YOY	8.5	6.3	5.8	10.0	9.7	16.5	N/A	N/A
Exports, % YOY	65.2	45.4	11.8	28.7	19.2	N/A	N/A	N/A
Imports, % YOY	23.5	39.0	20.4	38.5	20.2	N/A	N/A	N/A
Trade Balance, US\$ mn	0.9	-0.3	-2.0	-6.6	0.3	N/A	N/A	N/A
Foreign Exchange Reserves, US\$ mn	100.9	118.4	115.7	118.2	108.9	99.9	N/A	N/A

Sources: Central Bank of Solomon Islands, ADB, IMF

Country Update: Timor-Leste

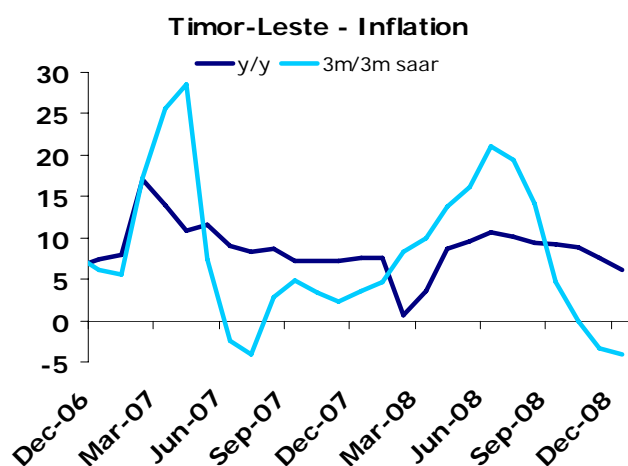


Growth should remain high as the pace of government spending funded by off-shore oil production continues apace. Inflation is fast receding due to a moderation in commodity prices. Domestic demand appears to be holding up, mainly through transfer payments, but credit growth has come off sharply. Reducing rural poverty and managing the attendant risks is a key medium-term challenge.

- Government expenditure doubled in 2008 as GDP growth reached an estimated 10%. Agriculture (by far the largest employer in the economy; the government is second) recovered following a year of bad weather.
- Inflation appears to be largely under control given the decline in food and fuel prices. Our short-term 3m/3m 'momentum' measure has dipped into negative territory, indicating that deflation will likely be a predominant theme over the short-term.
- Money supply growth remained healthy at 38.2% (y/y) in December, up from 33.0% in November. Lending opportunities in this government-dominated economy are few and banks' liquid asset ratios continue to rise.
- Bank lending appears restrained in fear of increasing non-performing loans, which stood at 28% at end-2008. Private outstanding credit dropped 23.4% at a q/q annualised rate in Q4, with large declines for tourism and trade finance (-80.3% and -71.8%, respectively). At the same time, construction loans surged 87.7%, likely due to higher public spending on infrastructure. Loans to individuals, the largest share of total credit, continue to grow modestly.
- Timor-Leste's REER has been steadily increasing since August last year with continued strengthening in the USD (the USD has been adopted as the local currency).
- The latest trade figures for FY08 show exports at \$48mn while merchandise imports amounted to \$247mn. The yawning trade deficit took place against the background of a bumper coffee crop (the largest export product after petroleum).
- Growth should continue to be propelled by large government expenditures, especially since the UN Mission has recently been extended into 2010. The drawdown from the \$4.2bn Petroleum Fund (which invests largely in US Treasuries and thus escaped capital losses owing to the crisis) will fund infrastructure imports and additional public wage rises. The main risk is the security situation, which remains fragile.

Commercial Bank Outstanding Credit to Private Sector

Sector	y/y	3m/3m AR	% of Total Loans
Agriculture, Water and Forestry	-83.9	-79.0	0.2
Industry and Manufacturing	-5.8	-48.4	1.8
Construction	-52.4	87.7	14.3
Transport and Communication	2.3	20.4	1.9
Trade and Finance	-19.4	-71.8	10.0
Tourism and Services	101.0	-80.3	12.0
Individuals	43.0	7.7	59.9
Total	4.9	-23.4	100.0



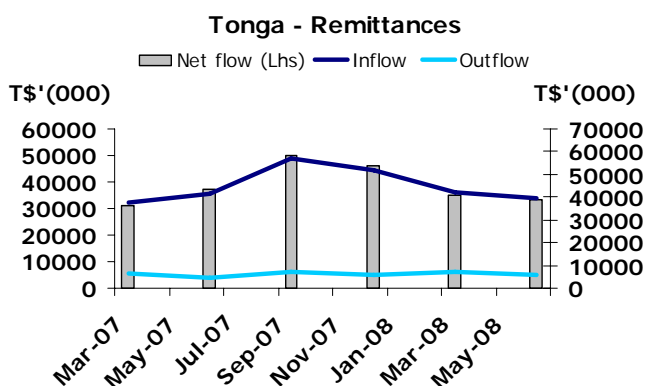
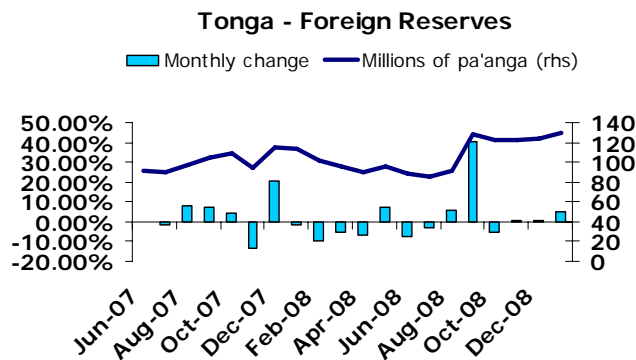
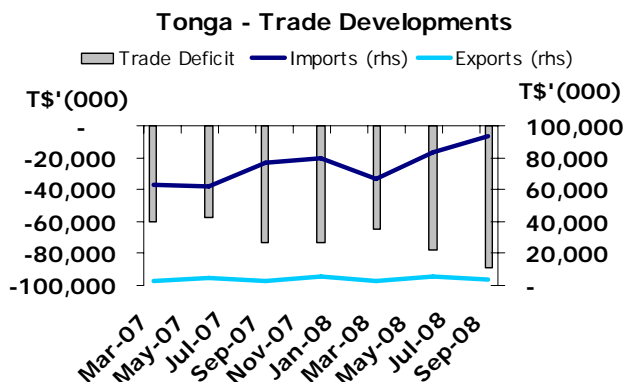
Chang Wei Liang

Economic Data – Timor-Leste

Quarterly Data	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Consumer Price Index, % YOY	13.9	9.0	7.2	7.6	3.7	10.7	9.1	6.1
- Food, % YOY	N/A	N/A	10.7	11.0	3.2	13.8	10.9	7.0
- Transport & Comms, % YOY	N/A	N/A	-0.9	3.8	4.3	24.2	22.4	12.5
Exports+, US\$ mn	0.5	0.1	N/A	N/A	10.3	7.1	19.2	11.3
Imports^, US\$ mn	16.3	52.3	N/A	N/A	41.6	48.3	66.5	82.0
Trade Balance, US\$ mn	-15.8	-52.2	N/A	N/A	-31.2	-41.2	-47.4	-70.7

Sources: National Directorate of Statistics, Economist Intelligence Unit

Country Update: Tonga



Given its reliance on tourism and remittance flows, Tonga is likely to slip back into negative growth this year following the re-emergence of growth in 2008 as recessions in advanced "source" economies hit home. Inflation has peaked as has credit growth, adding further downside impetus to growth. Government spending may provide a partial offset.

- The economy grew modestly in FY2008 as a contraction in agriculture and other primary sectors was offset by growth in the transport, communications, finance and real estate.
- Import growth rose 32.6% (y/y) in January from 30.9% in December, supported by an influx of mineral fuels and basic manufacturers. In contrast, exports fell to 29.5% from 32.3% in Dec. Exports are less than one-tenth of imports, and the balance of payments thus relies heavily on tourism and remittances. The overall BOP in FY2008 recorded a small deficit.
- CPI inflation has continued to fall, reaching 3.8% (y/y) in January, the lowest rate in two years. As is the case elsewhere, this is largely the result of falling fuel prices and transportation costs.
- Credit growth continues to slide. Private sector credit growth fell to 4.3% in Dec, with credit growth to households turning negative. Non-performing loans, following swift credit growth in early 2008, are reportedly on the rise.
- The growth in tourism receipts for Jan 2009 slowed to 15.6% (y/y), down from 31.5% in Dec. A 15% decline in US tourist arrivals in 2008 is ominous for 2009 even though the largest source of tourism is from New Zealand and Australia. A new national tourism body, Tourism Tonga Inc. incorporated in Jan 2009 will work closely with the government on legislation to attract more tourists to the kingdom.
- Private remittances continue to decline, falling to TOP\$186.2mn in Jan 2009 from TOP\$190.4mn in Dec.
- 2009 looks like a year of weak growth for Tonga. Recessions in Australia, New Zealand and the United States are likely to dampen both tourism flows to the kingdom as well as remittances from Tongans living abroad. In light of this, we forecast a 2% contraction in activity this year.

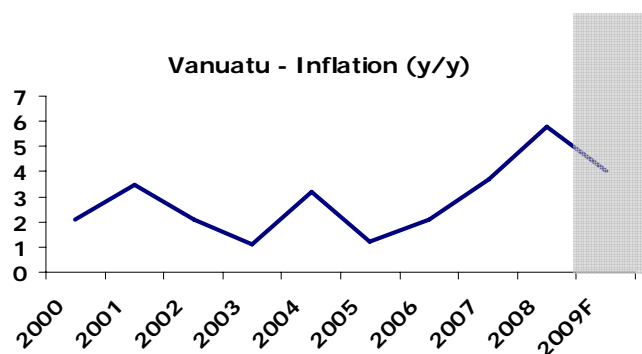
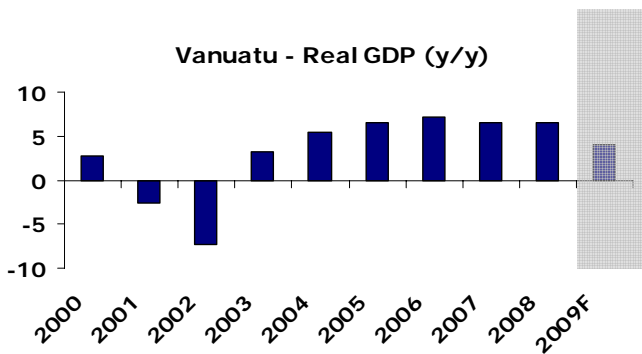
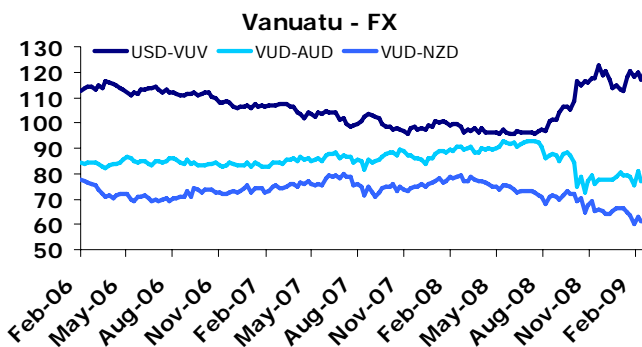
Naresh Navaratnarajah

Economic Data – Tonga

Quarterly Data	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Consumer Price Index, % YOY	3.9	5.7	8.1	6.8	12.0	12.2	N/A	N/A
Private Sector Credit, % YOY	6.7	9.5	12.4	16.3	15.9	17.1	N/A	N/A
Exports, % YOY	-0.9	-5.2	-0.9	-21.1	14.9	N/A	N/A	N/A
Imports, % YOY	20.3	24.9	20.6	-5.0	-6.8	N/A	N/A	N/A
Trade Balance, US\$ mn	-30.0	-37.7	-37.9	-32.9	-27.1	N/A	N/A	N/A
Foreign Exchange Reserves, US\$ mn	47.0	50.1	54.9	61.9	53.9	49.4	N/A	N/A

Sources: National Reserve Bank of Tonga, Tonga Department of Statistics

Country Update: Vanuatu



Vanuatu experienced robust growth in 2008 for the fourth year running, but the pace of activity is expected to decline this year as knock-on effects from the global downturn hit home. The authorities have cut policy interest rates as growth momentum has eased, and inflation is expected to fall back into the 0-4% target band.

- GDP expanded by 6.6% in 2008 (the fourth straight year of 6-plus% growth) buoyed by tourism and construction. Available data show that, as of Q3 2008, visitor arrivals continued to grow at double-digit rates.
- Trade growth remained strong. Exports expanded by 46.8% in 2008 while imports grew by 31% to reach seven times the level of exports. Foreign exchange reserves remained comfortable at 7½ months of import cover at end-year.
- The economy continues to monetise. Credit growth surpassed 40% (y/y) in Nov 2008. Money supply growth remained robust, reaching 14% (y/y) in Nov.
- Inflation was higher than anticipated in 2008, rising to 6% in Q3 and 5.8% for the year. However, declining food and energy prices, as well as slower growth, should ease inflation back into the central bank's 0-4% target range by the end of 2009.
- On the FX front, the Vatu has depreciated against the US dollar but gained against other major currencies over the past two months.
- In light of the rise in inflation in mid-2008, the central bank raised its policy rate in Sep for the first time in two years. However, in a bid to increase liquidity in the financial system, the central bank cut its policy rate and reserve requirement ratio by 25bps to 6% and 300bps to 5%, respectively, in mid-Dec.
- The recent easing in monetary policy and a more accommodative fiscal stance should also help to cushion the impact of the crisis. Growth this year is expected to moderate to 4% as the global economic downturn, especially the slowdown in Australia and New Zealand, weighs on the tourism sector. Foreign investment is also likely to decline, affected by the tightening in credit markets.

Chong, Jun-Jie

Economic Data – Vanuatu

Quarterly Data	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Consumer Price Index, % YOY	3.5	4.1	4.0	4.2	3.6	3.9	N/A	N/A
Tourist Arrivals, '000	42.7	39.9	37.3	47.2	49.4	N/A	N/A	N/A
Exports, % YOY	7.9	9.9	28.1	-4.9	25.0	30.7	N/A	N/A
Imports, % YOY	74.8	-35.5	37.5	55.2	108.8	14.7	N/A	N/A
Trade Balance, US\$ mn	-20.3	-8.0	4.6	-21.7	-98.8	1.4	N/A	N/A
Foreign Exchange Reserves, US\$ mn	99.1	102.9	106.8	113.8	116.6	119.0	N/A	N/A

Sources: ADB, ANZ Economics

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