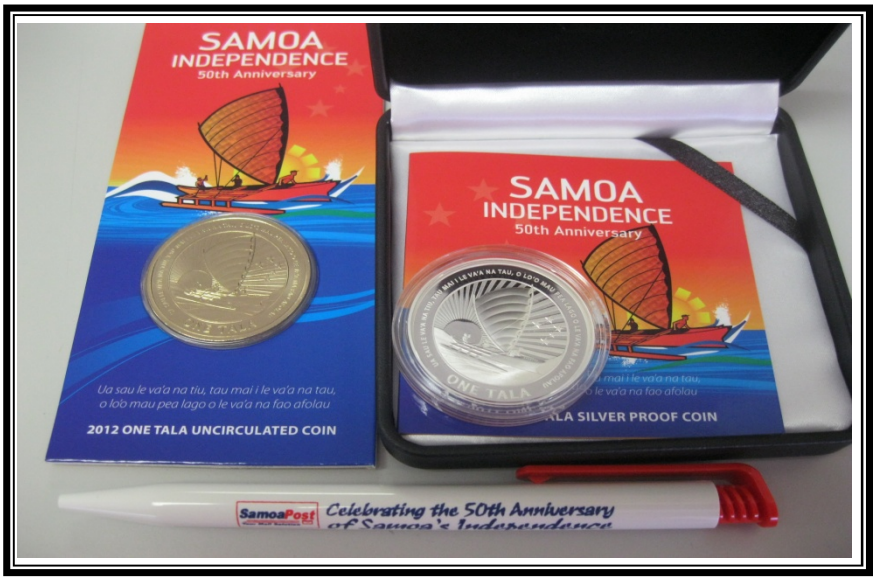
CENTRAL BANK OF SAMOA



Celebrating the 50th Anniversary of Sāmoa's Independence from 1962 - 2012

MONETARY POLICY STATEMENT FOR THE FINANCIAL YEAR 2012/2013

APIA
November 2012

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1. INTRODUCTION

In line with Government's emphasis on transparency and accountability, Monetary Policy Statements (MPS) serve as the main vehicle to communicate and promote public awareness of the main objectives of monetary policy and the targets that would be pursued by the Central Bank in the year ahead. As well, these Statements are issued in accordance with the Central Bank's Corporate Plan and the latest of Government's Strategy for The Development of Samoa. The main objective of the Central Bank's monetary policy is to promote sustainable real economic growth by maintaining price stability and international reserves viability. In order to achieve these objectives, monetary policy decisions are conducted via open market operations through the issuance and trading of Central Bank Securities.

In pursuing the goal of price stability, the Central Bank relates Samoa's inflation rate to those of its major trading partners. The annual inflation rates for Samoa's main trading partners currently average around 3.0 percent and this is the target that the Central Bank normally aims to achieve and maintain each year. However, there are times that the changes in prices are beyond the realms of monetary policy and the control of the Central Bank. The experience of recent years have shown that persistently sharp hikes in international prices for crude oil and food have exerted significant pressures on the domestic prices of petroleum and food items. During such periods, attention is focused more on the underlying or core inflation rate.

Samoa is a small open economy with total merchandise trade alone representing around 60 percent of nominal GDP. It is crucial therefore that Samoa maintains a sufficient level of international reserves to withstand unforeseeable economic shocks. Under present circumstances, the Central Bank considers a level of gross official international reserves, equivalent to no less than 4.0 months

of imports of goods, as adequate for maintaining the country's long term international viability. On the exchange rate, the main objective of the Central Bank's policy is to ensure that export-oriented industries remain competitive in overseas markets whilst at the same time minimizing imported inflation. While there is no specific target level for the nominal effective exchange rate (NEER) of the Tala, the Central Bank aims to avoid a substantial real appreciation of the Tala since it can adversely affect the international competitiveness of the export sector.

2. EXECUTIVE SUMMARY

World Economy

The world economy grew 4.45 percent in 2010/11 and it is projected that growth by end June 2012 will be lower at 3.55 percent, revised down from initial forecasts published by the International Monetary Fund (IMF) in its July 2012 World Economic Outlook. The weaker outlook for global growth is a reflection of the worsening of economic conditions in the Euro region as financial market stress continues on the rise amid political and financial uncertainty in several economies of the Euro region. The Advanced economies are expected to have grown by 1.45 percent while the Emerging and Developing countries are forecasted to have grown by 5.75 percent, a notable revision from its 5.90 percent forecast.

Inflation in 2010/11 was recorded at 4.3 percent and is estimated to have edged up to 4.48 percent in 2011/12. Inflation rates for Advanced economies is estimated to reach 2.30 percent in 2011/12 while the rates for the Emerging and Developing economies is expected to reach 6.65 percent.

Monetary policies across all major central banks continued to remain highly accommodative in 2011/12 to support the ongoing recovery from the global financial crises. In collaboration with extremely expansionary monetary policies, some central banks, such as the Federal Reserve Bank of New York and the Bank of England, undertook quantitative easing measures to help boost growth. The Reserve Bank of Australia on the other hand, lowered its cash rate further as a result of weakening demand conditions, especially in view of the deterioration of financial conditions in the Euro economy with regard to the handling of its debt crisis. By the end of 2011/12, the Fed funds rate stood unchanged at its target range of 0 – 0.25 percent, the Bank of England also left its official policy rate unchanged at 0.5 percent. The Bank of Japan, the

European Central Bank and the Reserve Bank of New Zealand also followed suit and left their key interest rates respectively unchanged at 0 – 0.1 percent, 1.0 percent and 2.50 percent. The Reserve Bank of Australia lowered its cash rate of the financial year by a total of 125 basis points to 3.50 percent by end June 2012.

In the financial markets, the US dollar often found support from its haven status whenever economic updates from major industrialized economies surprised on downside, fuelling speculations for weakening global growth. However, it also lost support when global growth statistics and subsequently stock market performances improve, boosting investors' risk sentiment and demand for risk assets. The Euro was generally heading downhill over 2011/12 largely as a result of the debt crisis in the Euro area. The Australian dollar and the New Zealand dollar continued to fare well against the Greenback, with the occasional trough as a result of any weak economic data, especially in relation to the Euro area debt crisis, giving rise to expectations of further weakness in the global recovery.

Domestic Economy

With subtle signs of recovery at the start of the 2011/12 fiscal year, the Central Bank further eased its monetary policy stance in order to prop up flagging demand and business confidence and ensure growth momentum could be sustained. The Central Bank continued its Credit Line Facility to non monetary financial institutions, namely the Development Bank of Samoa and the Samoa Housing Corporation, as a means of injecting much needed liquidity into Samoa's main priority sectors such as tourism, agriculture and fisheries, manufacturing and housing.

The economy grew by 1.3 percent in 2011/12 driven by improvements in the 'Construction', 'Commerce', 'Food & Beverage manufacturing', 'Finance & business service' and 'Electricity & water' sectors.

With higher current and financial account inflows, the external sector posted a $10.4 million surplus in the balance of payments. Due to high level of imports, international reserves fell to a level equivalent to 5.7 months of imports in 2011/12.

Headline inflation was slightly problematic in the year under review with domestic pressure stemming from Government price regulated reviews, higher tax revenue measures and adverse weather conditions earlier in the financial year, pushing the headline rate to a high of 6.2 percent at end 2011/12. Underlying inflation, on the other hand, crawled up in the first half before declining in the latter half to 2.2 percent by end of the financial year.

The economy is expected to improve further, albeit at a snail's pace, with real growth of 1.5 percent for 2012/13. This slight improvement is expected to be driven by 'Construction', 'Public Administration' and 'Electricity & Water' and 'Transport & Communications' sectors, highlighting the various building projects (private and public) in the pipeline, some winding down and others gradually starting in the latter part of the year. The balance of payments is expected to register an overall surplus of $11.8 million in light of external loans disbursements by Government, increased project grants and marginal improvements in exports, tourism earnings and private remittances.

Inflation is expected to decelerate further in 2012/13, with the headline rate dropping to around 0.9 percent in light of expected declines in both local and imported components of the CPI. Similarly, the underlying rate of inflation is expected to drop to around 0.5 percent.

Given that inflation will not be a major threat in the year ahead and real GDP growth remains sluggish, the Central Bank has decided to support economic recovery by continuing its easing monetary policy stance in order to bring down the interest rates to boost the weak private sector credit demand and ultimately revive business and consumer confidence. Improved credit demand and strong

inflows from abroad will improve the level of money supply (M2). (See Table 1.)

Table 1

Selected Domestic Economic Indicators

Fiscal year to end June	2007/08	2008/09	2009/10	2010/11	2011/12	
	(Percentage change over the previous year)					
Real sector						
Nominal GDP	9.7	-2.3	1.9	4.3	3.9 est	
Real GDP	4.3	-5.1	0.4	2.0	1.5 est	
Prices						
Headline Consumer Price Index (annual average)	6.2	14.6	-0.2	2.9	6.2	
Underlying Consumer Price Index (annual average)	6.9	17.2	1.2	3.1	2.2	
Implicit GDP Deflator (annual average)	5.2	3.0	1.5	2.2	2.5 est	
Monetary aggregates						
Net foreign assets (annual average)	9.5	2.1	20.1	22.4	-24.1	
Government's net monetary position (end of period)	-11.6	-2.3	109.0	-5.6	8.9	
Bank credit to private sector						
Annual average	6.1	7.2	6.2	4.9	5.9	
End period	6.9	5.7	5.1	6.0	1.9	
Money Supply, M2						
Annual average	12.1	8.9	9.2	5.8	-5.5	
End period	12.1	7.7	10.9	3.6	-4.0	
Exchange rate						
Nominal Exchange Rate (annual average)	-0.16	2.65	1.13	0.43	1.11	
Real Exchange Rate (annual average)	2.99	8.72	-1.43	-0.53	2.76	
International reserves						
Gross International Official Reserves (Tala million)	254.5	260.28	410.72	356.82	366.76	
Gross International Official Reserves (Months of imports)	5.1	5.0	7.6	6.4	5.7	
Weighted average interest rates	(End of period, percent p.a.)					
CBS 14 days Securities	4.08	1.48	0.12	0.12	0.11	(1)
CBS 28 days Securities	4.04	1.68	0.14	0.13	0.12	(1)
CBS 56 days Securities	5.35	2.20	0.14	0.14	0.14	(1)
CBS 91 days Securities	5.38	3.10	0.44	0.40	0.40	(1)
CBS 182 days Securities	-	-	-	-	-	
CBS 365 days Securities	-	-	-	-	-	
CBS Securities overall weighted average yield (annual average)	4.70	2.28	1.72	0.15	0.15	(1)
Commercial bank deposits	6.10	5.14	2.78	2.31	2.41	(1)
Commercial bank credit	12.72	12.20	10.88	9.92	9.81	(1)
Commercial bank interest rate spread	6.60	7.06	7.34	7.61	7.40	(1)

Source: Central Bank of Samoa
(1) Interest rate as at end August 2012
na - not available

3. WORLD ECONOMY

Despite registering a 3.70 percent growth in 2011/2012, the world economy slowed down from 2010/11 despite earlier optimism in the year on recovery prospects. Although world growth, surprised on the upside in the first quarter due to easing financial conditions and recovering confidence, alongside budding global trade led by strong industrial production growth, the second quarter turned out weaker growth statistics. Activity is projected to weaken in late 2012, than had been expected in the April and July WEO reports, led by an expected lower growth forecasts for emerging market economies than previously estimated. The growth pulse slowed in various emerging market economies, notably in Brazil, China and India, which partly reflected the weaker external environment and decelerating domestic demand in response to capacity constraints and policy tightening in the past year. The Euro area also remains at the core of escalating financial market stress triggered by increased political and financial uncertainty in Greece, banking sector problems in Spain and doubts about governments' ability to deliver on fiscal adjustment and reform. Data out of the US suggested less robust growth than previously expected in April, a softening explained not only by an unusually mild winter but also by an underlying loss of momentum. Unemployment remains elevated in many advanced economies while consumer prices have inherently softened amid the weakening pace of global recovery.

World growth forecasts are slightly lower in the October 2012 update compared to the July 2012 IMF World Economic Outlook projections. The world output is expected to grow by 3.55 percent in 2011/12, down from 3.70 percent expected in the July 2012 update. A growth of 1.45 percent is expected for the advanced economies compared to an earlier estimate of 1.50 percent, while Emerging and developing countries are now expected to have grown by 5.75 percent, down from 5.90 percent in the July WEO forecast. The US and Japan are expected to grow by 2.00 and 0.70

percent, the former revised up from 1.85 percent and the latter, revised down from 0.85 percent. Growth for China and India are expected around 8.50 and 5.85 percent respectively, revised down from July 2012 WEO forecast of 8.60 percent and 6.60 percent respectively. (See Table 2.)

Table 2

Selected World Economic Indicators

Fiscal year to end June	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13 Forecast
Real growth rate	4.1	1.1	2.3	4.6	3.6	3.5
Inflation rate	5.0	4.2	3.1	4.3	4.5	3.9
Official international interest rates,			(End of period, percent p.a)			
US Federal Reserve	2.00	0.25	0.09	0 - 0.25	0 - 0.25	0-0.25
Reserve Bank of Australia	7.25	3.00	4.50	4.75	4.50	2.75
Reserve Bank of New Zealand	8.25	2.50	2.75	2.50	2.50	3.50
Bank of Japan	0.50	0.10	0.10	0 - 0.10	0 - 0.10	0-0.1
Bank of England	5.00	0.50	0.50	0.50	0.5	0.5
European Central Bank	4.00	1.00	1.00	1.25	1.25	1.00
Reserve Bank of Fiji Notes, 91 days	n/a	n/a	n/a	n/a	n/a	n/a

Source: IMF and reserve banks' publications and information releases.
n/a : not available

New Zealand

The New Zealand economy continued to expand in 2011/12 albeit at a modest pace and this is despite the boost to activity from favorable weather conditions, strength in export commodity prices and spending associated with the Rugby World cup. However, the key drivers of growth have shifted from the external sector towards domestic demand. There has been a continued lift in housing market activity as house sales, building consent issuances and housing loan approvals increased in recent months, with developments in part, relating to the reconstruction activity in Canterbury. Although indicators of strength in the household sector

improved over recent months due to an increase in incomes and consumer confidence, households have still remained cautious as they continue to focus on debt consolidation. Business indicators were mixed but remain consistent with a gradual improvement in activity. While the economy is still operating with some spare capacity, especially given the elevated unemployment level, there were signs that pressures are building in the construction sector, particularly in Canterbury.

In the second quarter of 2012, the New Zealand economy reported growth of 2.0 percent, up from 1.7 percent in the previous quarter. The largest contributor to growth came from agriculture, followed by increases in construction and manufacturing. In the labor market, employment growth continued but at a slightly slower rate than in the previous quarter. The unemployment rate however, rose to 6.8 percent in June quarter 2012 from 6.7 percent in the previous quarter. Consumer prices in June quarter 2012 rose 0.3 percent over the quarter to be 1.0 percent higher than a year ago and down from the 1.6 percent annual rate reported in the first quarter.

New Zealand	Current	Forecasts		
		2012	2012/13	2013
GDP	Jun Quarter 12 0.6% *q/q* 2.0% *y/y*	2.3%	2.8%	3.2%
CPI	Jun Quarter 12 0.3% *q/q* 1.0% *y/y*	2.1%	2.3%	2.4%
Unemployment	Jun Quarter 12 6.8%	6.0%	5.7%	5.4%
OCR	2.50%	2.50	2.50	3.00
Exchange Rate (vs. USD)	End June 12: US$0.7871	US$0.80	US$0.83	US$0.82

Australia

The Australian economy grew more rapidly in the past year than previously suggested by data available at the time. Growth was around trend in the second half of 2011 and was stronger in the first quarter of 2012. Resource investment continued to expand rapidly and capital imports grew strongly. Iron ore exports rebounded from previous weather-related disruptions but coal production was hampered, partially due to disputes in Queensland. The high Australian dollar and weak conditions in the housing market also weighed on production and investment and some non-resource industries. Nevertheless, business credit continued to grow at its fastest pace. Recent data suggest that household consumption also grew strongly in the first half of 2012 as retail sales growth picked up in the first and second quarters of this year. Housing market conditions appeared to be improving, with low interest rates, rising rental yields and population growth expected to provide support for growth in the housing sector. Employment growth remains strong in resource and resource-related industries but job shedding continued in the manufacturing, hospitality and building construction industries. Nevertheless, the unemployment rate remained relatively low at 5.25 percent. Inflation eased over the year, with the annual rate influenced heavily by the earlier large falls in the prices of fruit and vegetables from flood-affected levels a year ago.

In the June quarter 2012, the Australian economy grew 3.8 percent over the same quarter a year ago, up from 3.6 percent in the first quarter. The main industry contributors to growth were wholesale trade, transport, and professional, scientific and technical services. The Australian housing market was generally soft; house prices showed some signs of stabilizing but building approvals continued to trend down. While labor market conditions steadied in early 2012, household income registered moderate growth, thus resulting

in a gradual uptrend in retail trade. June quarter statistics showed an unchanged unemployment rate of 5.2 percent, while inflation was 0.5 percent on the quarter and 1.2 percent in annual terms.

Australia	Current	Forecasts		
		2012	2012/13	2013
GDP	Jun Quarter 12 0.8% *q/q* 3.8% *y/y*	3.0%	3.3%	3.5%
CPI	Jun Quarter 12 0.5% *q/q* 1.2% *y/y*	2.7%	2.9%	3.0%
Unemployment	June 12 5.2%	5.2%	5.2%	5.2%
Cash Rate	3.5%	3.0%	2.75%	2.75%
Exchange Rate (vs. USD)	End June 12: US$1.0036	US$1.01	US$1.05	US$1.03

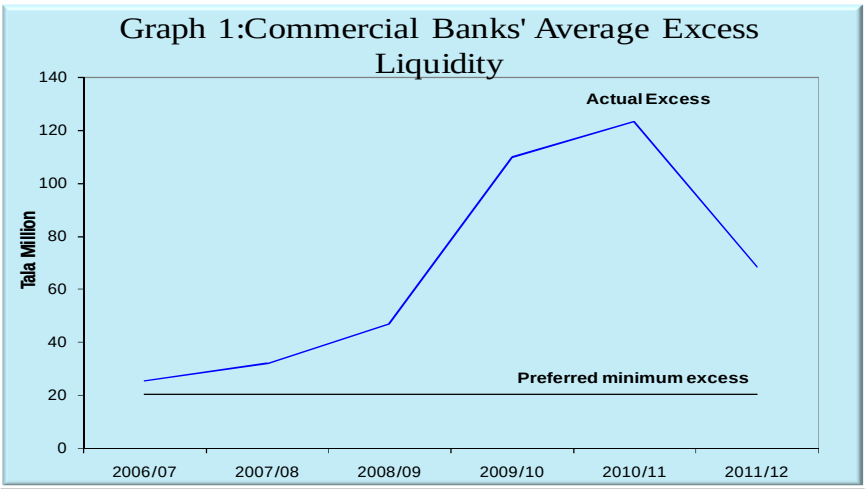
4. DOMESTIC ECONOMY

4.1 Policy Developments

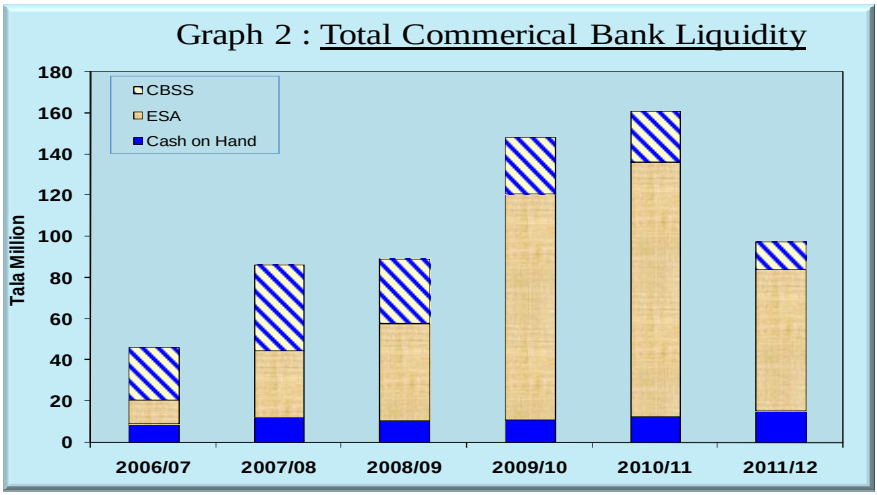
Fiscal policy in 2011/12 continued on an expansionary path, with an overall Government Budget deficit of $104.9 million (equivalent to 6.5 percent of nominal GDP) approved by Parliament, aimed at sustaining economic growth as it consolidates gains made since the global financial crisis and tsunami in 2009. While relatively large, this budget deficit, which was financed mainly by official soft term foreign loans, was much lower when compared to the previous year's budget deficit of $150.7 million, an indication of Government's fiscal consolidation efforts to reduce the budget deficit down to manageable levels in the medium term.

The economy in 2011/12 was initially expected to grow by 3.1 percent, but weakness in most macroeconomic indicators up to February 2012 led to the updated Central Bank forecasts estimating a 0.9 percent growth for the year. However, real GDP for the fiscal year 2011/12 registered a 1.3 percent growth, down from 2.0 percent in 2010/11. The sluggish economic activities earlier in the year resulted in the Central Bank Board approving, at its March 2012 meeting, the continuation of the Central Bank's accommodative monetary policy stance to stimulate the economy.

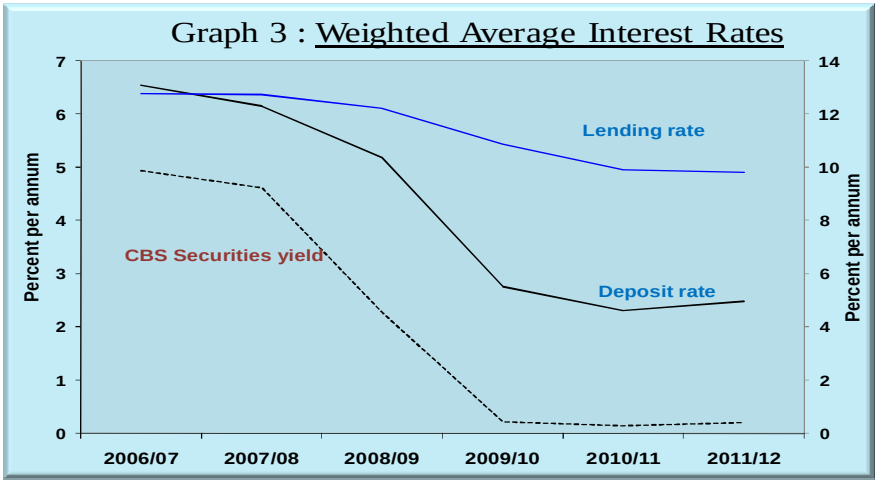
While commercial banks' excess reserves declined from the previous years, it remained elevated at high comfortable levels. Averaging $97.6 million, commercial banks' liquidity in 2011/12 declined from $161.2 million in 2010/11 but remained above the desired monthly levels of $50-$55 million. In particular, the average monthly level of excess reserves was reduced from $123.5 million in 2010/11 to $68.6 million; a level that was also well above the minimum comfortable level of $20.5 million. (See Graph 1.)



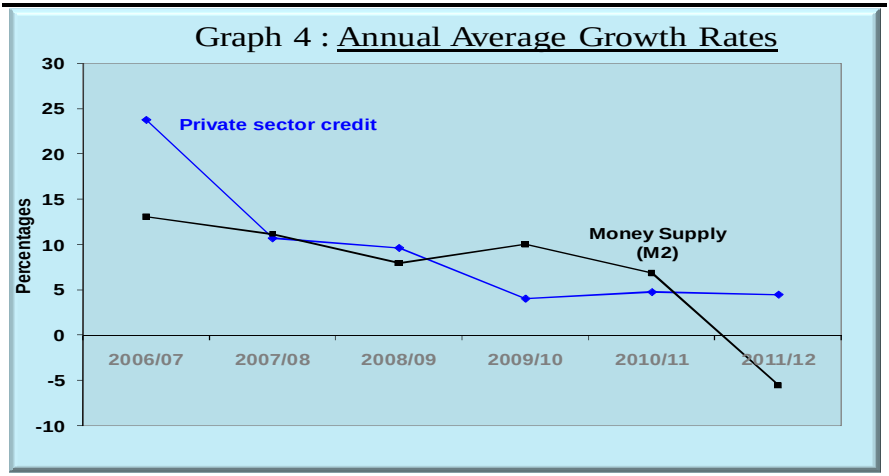
Similarly, the average monthly level of CBS securities outstanding dropped 11 percent from $24.9 million in 2010/11 to $13.5 million in 2011/12. (See Graph 2.) Nevertheless, despite matured securities issued at lower yields, the bulk of these papers were held in the medium term maturity range, which saw the weighted average yield of CBS securities at end June 2012 climb up to 0.21 percent, from 0.15 percent at end June 2011.



In response to the continued easing of monetary policy, the commercial banks' average lending rates dropped 10 basis points to 9.82 percent at end June 2012, from 9.92 percent at end June 2011. Commercial banks' deposit rates, on the other hand, increased 17 basis points to 2.48 percent, from 2.31 percent over the referenced period. (See Graph 3.)



Despite the reduction in borrowing costs, demand for bank credit was sluggish, with loans to the private sector and public institutions combined, shrinking to 4.55 percent in 2011/12, from 4.84 percent in 2010/11. And, together with a net outflow of foreign exchange throughout the year, this contributed to total money supply (M2) contracting 5.5 percent, a huge contrast to the 5.9 percent growth rate in the previous financial year. (See Graph 4.) The relatively slow rate of credit expansion in the last three financial years indicate that the reduction in commercial banks interest rates so far was insufficient to boost credit demand under the current weak economic conditions.



In 2011/12, the nominal effective exchange rate (NEER) of the Tala appreciated 1.1 percent on an annual average basis against the currencies in its exchange rate basket. The real effective exchange rates (REER) also appreciated 2.8 percent in the course of the year. The exchange rate of the Tala was allowed to appreciate in order to ease pressure coming from imported inflation.

4.2 Macroeconomic performance

4.2.1 Real Sector

For the fiscal year 2011/12, the economy expanded by 1.3 percent in real terms, slowing down from the 2.0 percent real growth in 2010/11.

The downturn in economic activities in the 2011/12 fiscal year was consequent of a 6.0 percent contraction in the 'Other manufacturing' sector, reflecting a decline in overseas demand for Yazaki production. Likewise, the 'Agriculture' output fell 8.8 percent on low production, exacerbated by drought-like conditions in the first half of the year, while the output of the 'Fishing' sector edged down 0.5 percent reflecting the current slump in fish catch

during 2011/12. Similarly, the 'Hotels and restaurant' sector slipped 1.2 percent. Stemming some of these downturn was significant Budget spending as Government expedited many of its planned projects with 'Construction' gaining 5.5 percent while the 'Food and Beverage Manufacturing' sector expanded by 15.7 percent on increased export sales and demand for beer, one of the main industry in this category. Likewise, the 'Transport and communications' and 'Commerce' sectors grew by 1.2 percent and 2.3 percent respectively while 'Finance and business services' and 'Electricity and water' improved by 3.7 percent and 3.6 percent in that order. 'Public and Finance Administration' also rose 3.7 percent. (See Table 3.)

Table 3
Real Gross Domestic Product by Industry
(At 2002 prices, amounts in Tala Million)

During the period	2007/08 Actual	2008/09 Actual	2009/10 Actual	2010/11 Actual	2011/12 Actual	2012/13 Forecast
Agriculture	68.0	58.6	56.0	56.4	51.4	54.3
Fishing	51.7	48.2	47.3	45.5	45.2	44.6
Food & Beverage manufacturing	24.9	17.4	20.5	20.4	23.6	23.1
Other Manufacturing	126.3	88.9	91.1	80.7	75.9	75.7
Construction	137.2	127.0	127.4	139.0	146.7	146.8
Electricity and water	49.3	51.3	53.2	55.0	57.0	56.8
Commerce	195.3	193.4	192.2	198.8	203.3	208.4
Hotels, restaurants	37.8	39.4	31.5	35.9	35.5	36.1
Transport, Communication	147.1	156.3	163.2	167.4	169.4	176.7
Public administration	85.8	88.9	92.1	94.3	96.2	97.4
Finance and business service	102.6	104.6	106.1	108.2	112.2	112.0
Less: Enterprise share of FISIM (1)	-13.0	-13.6	-13.9	-14.3	-14.5	-14.7
Ownership of dwellings	31.1	31.2	31.3	31.4	31.5	32.0
Personal and other service	60.7	56.4	53.9	54.6	53.8	54.2
Total	1104.8	1048.1	1051.9	1073.3	1087.1	1103.5
Annual percent change	6.3	-5.1	0.4	2.0	1.3	1.5
Implicit GDP deflator	132.1	136.0	138.1	141.1	143.4	147.7
Annual percent change	5.1	3.0	1.5	2.2	1.6	2.0

Source: Samoa Bureau of Statistics
(1) FISIM : Financial Intermediary Services Imputed

4.2.2 Balance of payments

Following the huge deficit of $53.9 million in 2010/11, the balance of payments recorded a $10.4 million surplus in 2011/12. This favorable outcome reflected improvements in exports, remittances and tourism earnings as well as large disbursement of government loans. (See Table 4.)

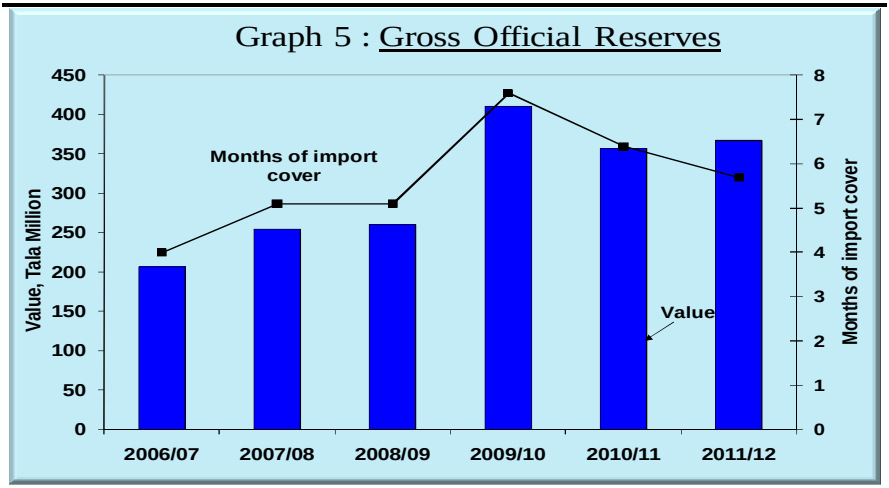
Table 4
Balance of Payments
(Amounts in Tala Million)

During the period	2007/08 Actual	2008/09 Actual	2009/10 Actual	2010/11 Actual	2011/12 Update	2012/13 Forecast
A. Current Account Balance	-92.8	-39.4	-95.1	-115.6	-161.0	-143.9
Merchandise Trade Balance	-561.1	-598.0	-608.7	-618.4	-710.2	-691.7
Exports *	32.4	28.1	41.4	51.0	62.6	63.8
Imports	-593.5	-626.1	-650.1	-669.4	-772.8	-755.5
Services, net	249.3	253.3	233.6	221.0	264.2	277.4
Income, net	-110.4	-47.4	-46.5	-62.9	-84.1	-98.5
Current Transfers, net	329.4	352.7	326.5	344.6	369.0	368.8
Private transfers	323.0	342.6	326.6	345.1	369.0	368.8
Official transfers	6.4	10.1	-0.1	-0.5	0.0	0.0
B. Capital Account Balance	60.9	100.3	174.8	144.3	177.8	121.6
Official Grants	68.0	101.9	152.8	142.9	179.7	139.6
Other	-7.1	-1.5	22.0	1.4	-1.9	-18.0
C. Financial Account Balance	63.0	48.9	57.3	-51.5	36.1	8.1
Direct Investment	11.7	23.1	3.0	17.7	42.6	-5.0
Portfolio Investment	-0.5	1.0	-2.1	-4.7	-1.0	-15.3
Other Investment	51.8	24.9	56.4	-64.5	-5.5	28.4
D. Reserve Assets	-47.8	-7.1	-150.4	53.9	-10.4	-11.8
E. Net Errors & omissions	16.7	-102.9	13.4	-31.0	-42.5	26.0

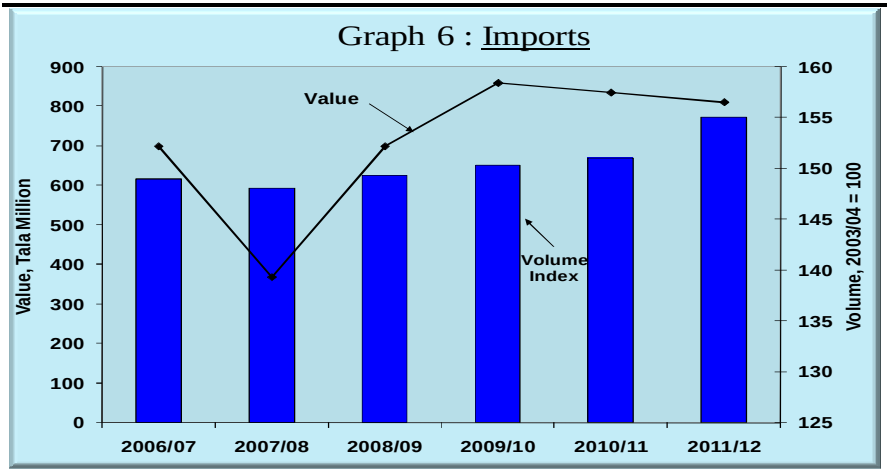
** Export figures now include the re-export of fuel for foreign aircrafts and shipping vessels (from 2010 onwards).*

Source: Central Bank of Samoa

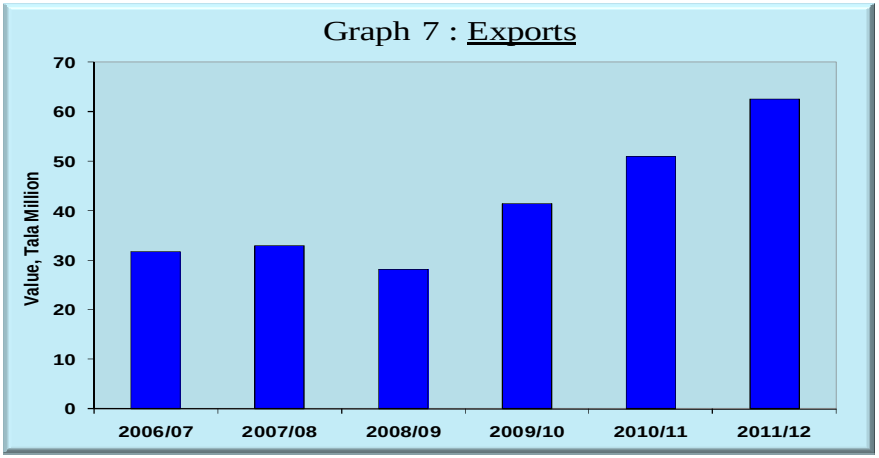
Nevertheless, due to very high import payments during the fiscal year, the level of international reserves in 2011/12 was equivalent to 5.7 months of imports, dropping from 6.4 months in 2010/11 but was well above the long term benchmark of 4.0 months cover. (See Graph 5.)



Total import payments grew 16 percent (or $103 million) to $772.8 million in 2011/12, largely underpinned by increased private sector imports. In particular, non-petroleum imports rose sharply by 15 percent (or $72.3 million), mainly on account of increased merchandise foods and a few large one-off items that included a new EPC generator worth $45 million; as well as petroleum imports, which grew significantly by 32 percent (or $44.0 million), reflecting increased oil prices during the year as well as strong local demand for fuel. On the other hand, Government imports fell 23 percent (or $12.8 million) over the year. (See Graph 6.)

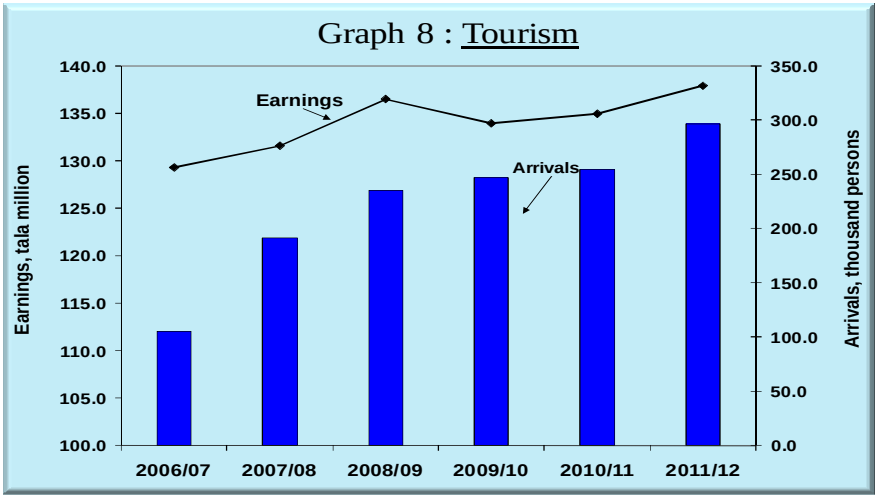


Exports grew 23 percent in 2011/12 mainly resulting from increased earnings from crude coconut oil, nonu juice, re-exports[1], beer, copra meal and scrap metals to name a few. These were partially offset by lower proceeds from fish, coconut cream, taro and bottled spring water exports. Nevertheless, with the larger increase in import payments offsetting the improvement in export revenues, the merchandise trade deficit widened 14.8 percent. (See Graph 7.)



[1] Total exports now include the re-fueling of foreign aircrafts and shipping vessels.

Tourism activities were robust in 2011/12, with total arrivals increasing 3.7 percent due largely to a strong second half performance, which included the lead up to the celebration of Sāmoa's 50th Independence in early June 2012. With the exception of lower tourist numbers from Europe and USA, the higher arrivals in the year were from 'other countries' (up 13 percent), Australia (up 9 percent), American Sāmoa (up 4 percent) and New Zealand (up 1 percent). The higher visitor numbers in 2011/12 also highlighted the growing number of regional conferences and sporting events held in Sāmoa as well as those 'visiting friends and relatives', offsetting a slight drop in genuine holidaymakers. And, with higher average tourist expenditures during 2011/12, total tourism earnings increased 8.5 percent to $332.3 million in 2011/12. (See Graph 8.)



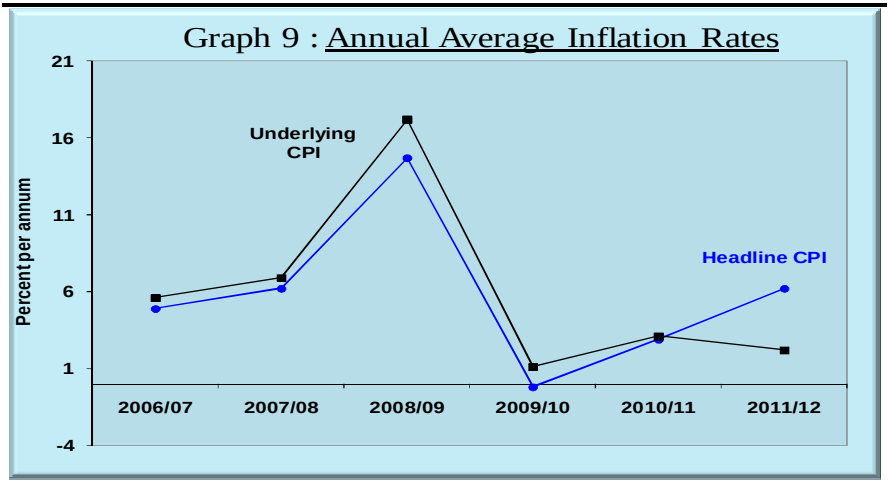
In 2011/12, private remittances increased 6 percent to $392.2 million, mainly resulting from an 11 percent jump in household remittances and a 7 percent improvement in funds for churches; highlighting increased private transfers from the large Samoan communities in Australia and New Zealand offsetting lower inflows from USA and American Sāmoa.

Official capital transfers recorded a 26 percent increase to $179.7 million as projected in the 2011/12 Government Budget from $142.9 million in the previous financial year. Government loans liabilities increased substantially reflecting higher loan disbursements compared to last year.

4.2.3 Prices

Consumer prices generally tracked upwards for most of 2011/12, accelerating well beyond the Bank's long term target of 3.0 percent. The prolonged dry spell in the first half of 2011/12 resulted in a sudden spike in local agricultural food prices, pushing the local component of the headline CPI to 8.1 percent, from 1.5 percent at end 2010/11. Other contributing factors included the increase in registration fees by the Land Transport Authority (LTA) and National University of Sāmoa (NUS), raised excise tax for beer and cigarettes as well as increased prices in some household necessities (such as school uniforms and toiletries).

On the import side, weak global demand from the softening of world economic conditions and favorable supplies in some major producing countries during the year saw international prices of food items drop while crude oil prices remained elevated on ongoing geopolitical concerns and civil conflicts in major oil producing countries especially in the Middle East region. The overall net effect on imported inflation was a decline to 3.6 percent at end 2011/12, from a 4.6 percent rate in the previous year. (See Graph 9.)



As a result of the higher local component of the headline CPI, the annual average headline annual inflation rate rose to 6.2 percent at end June 2012 from 2.9 percent at end June 2011. Alternatively, the weak demand conditions associated with the slowing economy saw the underlying inflation rate drop to 2.2 percent in 2011/12, from 3.1 percent in 2010/11. (See Table 5.)

Table 5
Consumer Price Index
(August 2010 = 100)

Fiscal year to end June	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13 Forecast
A. Headline Inflation						
12 months average percent change						
Description						
All Groups	6.3	14.6	-0.2	2.9	6.2	0.9
Food and Non-Alcoholic Beverages	7.1	20.6	-0.9	1.8	9.2	1.3
Import Component	8.0	15.5	-0.6	4.6	3.6	0.2
Local Component	4.8	13.8	0.2	1.5	8.1	1.4
B. Underlying Inflation (1)						
12 months average percent change						
Description						
All Groups	6.9	17.2	1.1	3.1	2.2	0.5
Food and Non-Alcoholic Beverages	7.9	20.5	1.2	4.2	2.6	0.1
Import Component	6.8	17.3	0.6	3.7	2.4	0.5
Local Component	7.1	16.8	2.7	1.2	1.5	0.5

Source: Samoa Bureau of Statistics (formerly Statistical Services Division, Ministry of Finance)
(1) The historical series for this new index started in August 2003.

5. DOMESTIC ECONOMY OUTLOOK FOR 2012/13

5.1 Government Budget

With weak global economic conditions as a backdrop, Parliament approved another expansionary Government Budget for 2012/13 albeit with a lower overall Budget deficit compared to the last financial year's budget deficit. The Budget for 2012/13 is projected to result in an overall deficit of $103.7 million compared to an overall budget deficit of $118.3 million, after supplementary budget adjustments in 2011/12. This budget deficit is about 6.1 percent of nominal GDP, down from 7.3 percent for 2011/12. The current financial year's budget deficit, to be financed largely by external soft term loans and external grants, includes some large public and social infrastructural developments (such as upgrades for roads, bridges upgrades and utility services), large education and health projects as well as support for the revitalization of the agriculture sector. The drop in the relative size of the budget deficit is part of fiscal consolidation to try and get the budget deficit to manageable levels in the medium term.

Total revenue is expected to pick up in 2012/13, mainly on account of increased collection from current revenue measures. External grants are expected to grow to $153.3 million, reflecting increased assistance for sector programs from our main development partners, particularly the European Union and the Australian and New Zealand governments. Overall, total revenue and grants is projected to expand to $670.5 million. Total expenditure, on the other hand, is projected to jump to $774.3 million in 2012/13 from $741.0 million in 2011/12. (See Table 6 and Graph 10.)

Table 6

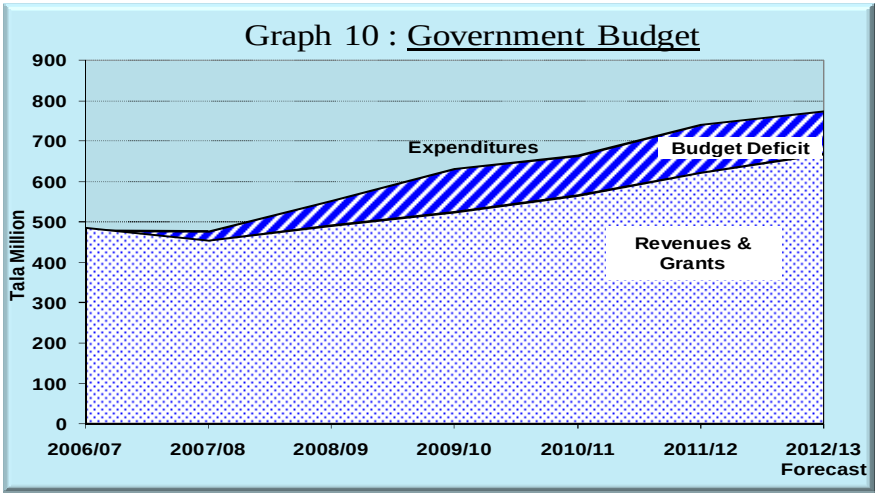
Financial Operations of Government (1)

(Amounts in Tala Million)

During the period	2005/06 Actual	2006/07 Actual	2007/08 Actual	2008/09 Actual	2009/10 Actual	2010/11 Provisional	2011/12 Budget
Total Revenue and Grants	387.1	461.5	454.9	492.0	525.2	567.2	549.0
Total Revenue	315.3	363.0	378.0	381.4	372.4	423.8	415.7
Tax	273.1	317.9	330.2	324.7	324.8	346.0	370.6
Non-tax	42.2	45.2	47.8	56.7	47.6	77.8	45.1
External Grants	71.8	98.5	76.9	110.7	152.8	143.4	133.3
Total Expenditure	391.7	477.6	476.5	552.5	631.7	664.5	695.1
Current Expenditure	281.9	325.1	372.4	358.8	347.0	374.8	440.6
Development Expenditure	86.1	131.7	96.2	182.1	273.8	272.9	200.3
Net Lending (1)	23.7	20.7	7.8	11.7	10.9	16.8	54.2
Overall Surplus / Deficit (-)	-4.6	-16.1	-21.6	-60.5	-106.6	-97.3	-146.1
Financing	4.6	16.1	21.6	60.5	106.6	97.3	146.1
External Financing	6.2	17.8	12.5	44.6	-15.3	82.7	90.4
Disbursements	19.2	33.3	28.5	60.4	144.8	100.6	108.8
Amortisation	13.0	15.5	16.0	15.8	160.1	17.9	18.4
Domestic Financing	-1.6	-1.7	9.1	15.9	-121.1	14.7	55.7
Monetary system	-11.0	0.0	11.9	2.2	-38.2	10.3	0.0
Other	-12.6	-1.7	-2.8	13.7	-82.9	4.4	55.7

(1) GFS Manual 1986 format

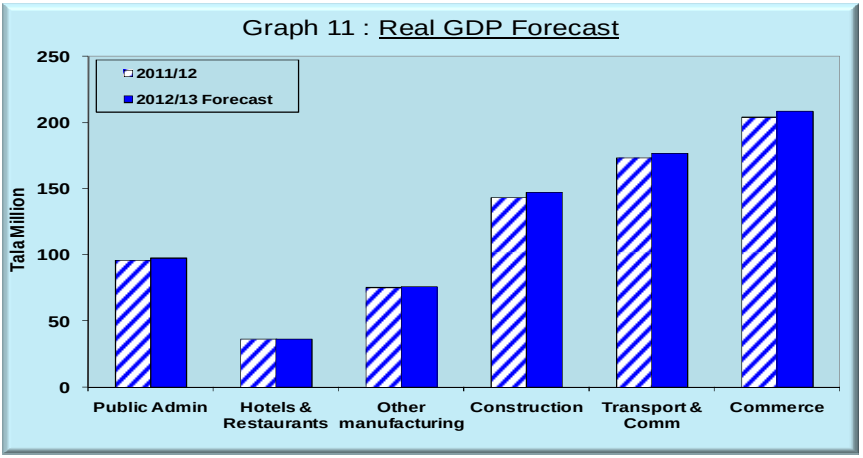
Source: Samoa Bureau of Statistics



5.2 Real Sector

The economy in 2012/13 is expected to continue on its gradual recovery from last year in light of the expected improvements in tourism, remittances and general consumer demand, in addition to the expansionary fiscal and monetary policies. Projects aimed at improving and strengthening the education, health, agriculture, water and electricity sectors, in addition to revitalizing the agriculture sector and continued infrastructural works are prioritized in the Government Budget to stimulate economic growth in 2012/13. These are expected to combine with private sector projects to boost business confidence and add stimulus for economic growth.

In the event, real GDP is expected to grow by about 1.5 percent in 2012/13, supported by an expected rebound in 'Construction' (up 2.5 percent), 'Public Administration' (up 1.5 percent), 'Electricity & Water' (up 1.1 percent) and 'Transport & Communications' (up 1.9 percent) from various building projects (private and public) in the pipeline for 2012/13. These projects include the ongoing construction of the NHS headquarters, new Nurses building and hospital laboratory, road widening project, Chan Mow complex, the new Fugalei Market and possible start of the Lamana hotel project. There are also estimated improvements for 'Commerce' (up 2.0 percent), 'Finance & Business service' (up 1.9 percent) and 'Hotels & restaurants' (up 0.1 percent) sectors with the 'Agriculture' industry forecast to edge up by 0.5 percent. (See Graph 11.)



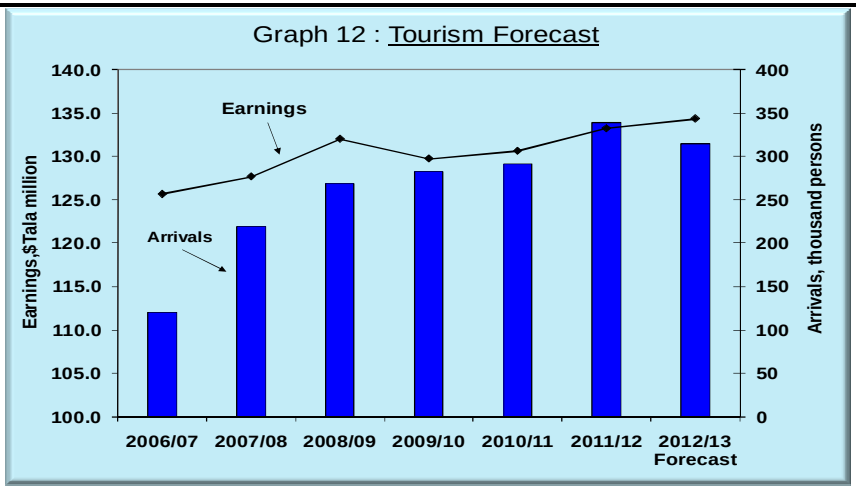
5.3 Balance of Payments

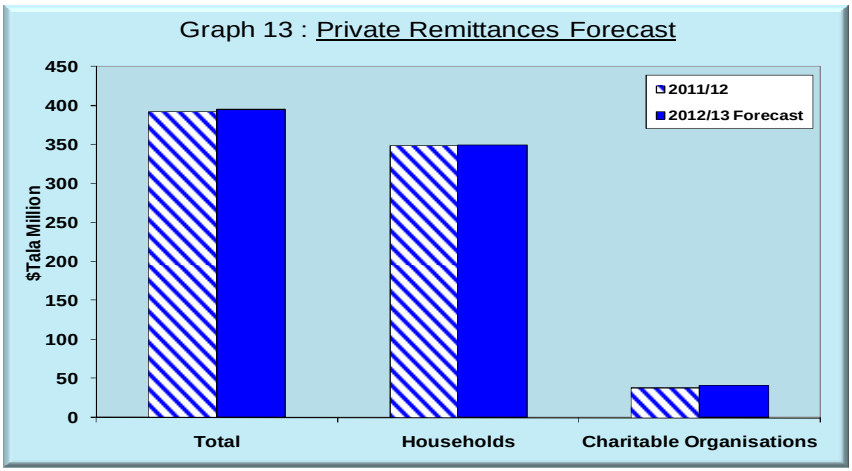
The balance of payments is expected to record an overall surplus in 2012/13, supported by the significant inflows projected in the Budget, such as the $116.9 million net disbursement of Government external loans as well as an increase in project grants to $153.3 million from $133.7 million in 2011/12.

On the current account, exports for 2012/13 are expected to improve modestly due in large part to increased gains projected for nonu juice, copra meal and fish exports. Supported by increased nonu supplies from local farmers and expected high export prices, a healthy return for nonu juice exports is anticipated while strong overseas demand underpins the higher projection for copra meal. While the expected El Nino weather pattern may reduce fish export volumes, its' relatively high price is estimated to bring in higher returns for this export. On the other hand, proceeds from coconut oil exports is projected to tumble in 2012/13 on the back of sliding international prices, despite growing interest among local copra producers. There is a soft outlook for beer in 2012/13 in light of recent hikes on excise tax for beer.

Total imports are expected to drop 2 percent to $755.5 million in 2012/13, reflecting a return to normal levels after last year's level that included around $70 million worth of one-off import items. Government imports are expected to decline 18 percent reflecting the winding down of major public sector construction activities, such as the National Hospital, which is nearing completion. Likewise, the value of non-petroleum imports by the private sector is envisaged to drop by 2 percent as it normalizes although usual consignments of merchandise goods and construction materials are still expected to increase, albeit modestly. On the other hand, petroleum imports are projected to increase by 7 percent, due in large part to an expected growth in volume consequent of an anticipated increase in local demand, offsetting a decline in the international crude oil price.

The tourism sector is expected to continue its steady recovery in 2012/13 in line with ongoing promotion and marketing of Samoa in the main tourist markets of New Zealand and Australia. While visitor numbers are expected to decline by 1.8 percent in light of the ongoing subdued global economic conditions and sluggish demand, average tourist expenditures are projected to expand 5.2 percent. In the event, total tourism proceeds are expected to increase by 3 percent in 2012/13. On the bright side, the Government Budget has allocated $11.6 million for tourism marketing and promotion, recognizing the growing contribution of this sector to the economy. Private remittances, on the other hand, are projected to edge up by 0.3 percent, supported by ongoing efforts to reduce the cost of remittances to the Pacific Island countries from Australia and New Zealand; and modest improvements in the economies of these two main source markets. (See Graph 12 and Graph 13.)





On the whole, the balance of payments is expected to post a surplus of $11.8 million in 2012/13, on top of the $10.4 million overall surplus in the last financial year. The level of international reserves is anticipated to edge up to 6.0 months of imports from 5.7 months cover for 2011/12, thus remaining well above the minimum benchmark target of 4.0 months.

5.4 Prices

Consumer prices in 2012/13 are expected to gradually fall from the previous year as inflationary pressures subsides. Imported inflation is expected to drive this deceleration with weak global demand for internationally traded commodities and ample supply conditions, expected to pull commodity prices down, particularly for most food items. An expected improvement in local food supplies, matched by sluggish domestic demand is projected to reduce domestic inflation, in the absence of any Government regulated fee changes and natural disaster.

5.4.1 Headline Inflation

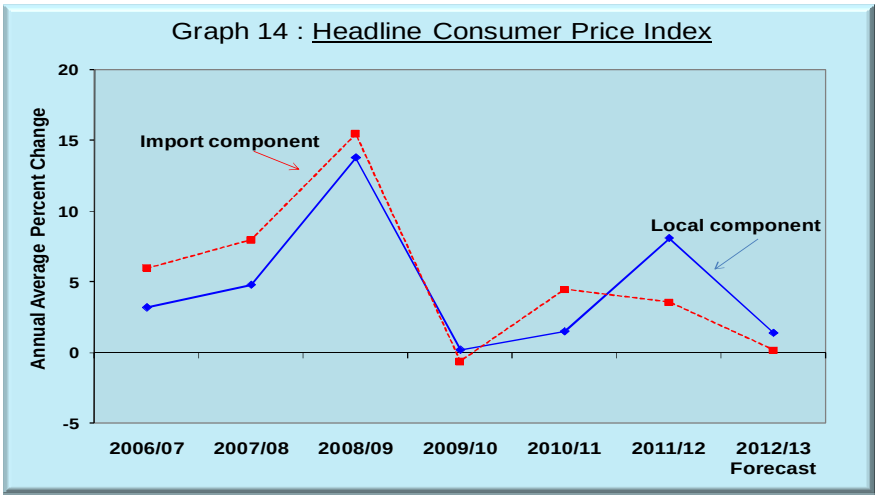
Import Component

The international commodity markets are expected to remain eased following the recent retreat in food and oil prices in mid 2012. In particular, agricultural food supply conditions are projected to improve slightly, with the lower price outlook by the World Bank based on (i) no foreseeable policy response by governments of major producing countries that would impact on the global food markets, (ii) energy and fertilizer prices remaining at current levels and (iii) biofuels expecting to play a more increasing role in the food markets. However, the emerging El Nino weather pattern which is expected in two months is projected to cause disruptive conditions in major producing countries, raising concerns over food prices. In particular, there are fears that this weather phenomenon will harm crops from Australia to India even though its' severity is currently unknown. There is likelihood that the El Nino will mean lower rainfall in India, which may lead to an erratic monsoon that would affect one of the largest food producers in the world as it did three years ago when sugar prices rallied to a 30 year high. Overall, imported food prices are projected to be negligibly higher by 0.6 percent over the year to June 2013. The outlook in the international crude oil markets is favourable with geopolitical risks to oil supplies

abating and expected sluggish demand as the recovery in the global economy continues to show weakness. The IMF's WEO July 2012 Update forecasts a 4.8 percent decline in the global average oil price below that of 2011/12. Overall, the annual average imported inflation is forecast to continue its downward slide, to 0.2 percent at end June 2013, from 3.6 percent at end June 2012.

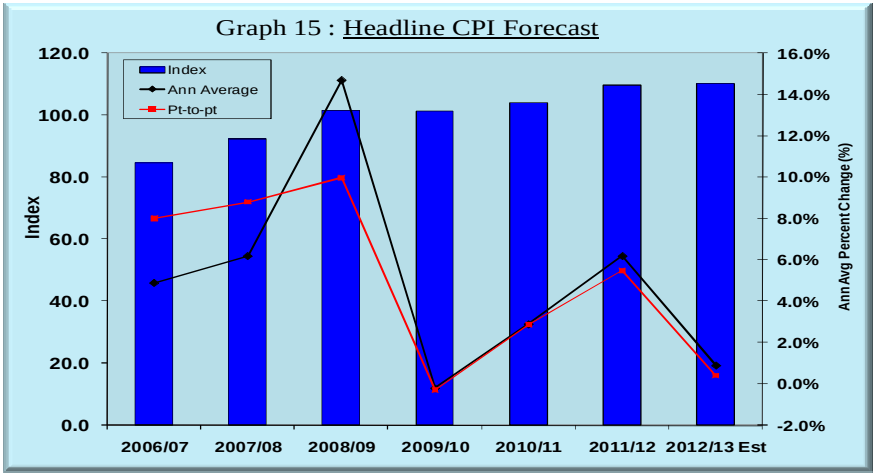
Local component

Similar to imported inflation, the domestic headline inflation rate for the forecast period ahead (2012/2013) is expected to decelerate, on the absence of any Government revenue measures from the current Budget Address compared to 2011/2012, but to a larger extent, consequent of a lower expected expansion in local food prices. The only major event that may lead to a notable deviation from expected forecasts for local food prices is the extent of the impact of the upcoming El Nino effect on local food supplies. The forecast drop in international oil prices is also expected to reduce the fuel surcharge component of electricity costs in the coming months. Overall, the domestic headline inflation rate is projected to gradually decline to 1.4 percent at end June 2013, from 8.1 percent at end June 2012. (See Graph 14.)



Headline Inflation Rate

With the expected disinflationary pressures from local and imported sourced goods in the fiscal year 2012/13, the overall headline inflation rate is projected to decelerate to 0.9 percent, from its 6.2 percent rate in June 2012 (and the latest actual of 6.1 percent in July 2012). (See Graph 15.)



5.4.2 Underlying Inflation

Import Component

It is anticipated that the overall import component of the underlying CPI will continue to decline throughout the current fiscal year underway to 0.4 percent at end June 2013. This forecast largely reflects the moderation of commodity prices in the global markets, particularly those for food products.

Local Component

On average, the domestic underlying inflation rate is expected to slow down to 0.5 percent at end June 2013. A modest improvement

of real GDP growth over the forecast period is the main factor responsible for the estimate for this component.

Underlying Inflation Rate

Taking into account the effects of both external and local pressure on prices for commodities that are not subject to extreme volatility and price regulations, the annual underlying inflation rate is expected to continue its current deceleration to 0.5 percent at end June 2013.

6. MONETARY POLICY STANCE FOR 2012/2013

The Samoan economy is expected to improve slightly, although it will be relatively fragile at 1.5 percent, considering the low growth from 2011/12. This moderate recovery is expected to be driven mostly by an expected rebound in 'Construction', 'Public Administration' and 'Electricity & Water' and 'Transport & Communications' sectors, reflecting various building projects (private and public) in the pipeline for 2012/13. Exports are projected to improve modestly while imports are anticipated to return to normal levels following a record high in 2011/12. In addition, net disbursements of external loans in 2012/13 should see the balance of payments record another modest surplus, with the level of international reserves expected to edge up to the equivalent of 6.0 months of imports.

In addition, inflation is expected to decelerate as international commodity prices decline in light of ongoing weak global demand, slight improvement in some commodity production levels in overseas markets while international oil prices would remain relatively stable at its current levels. Prices have already started to trend downwards, with the annual headline and underlying rates of inflation to decline to 0.9 percent and 0.5 percent respectively at end June 2013.

On the other hand, there is a concern on the slowdown of private sector investment demand with recent data reflecting the stagnant growth rate in credit to that sector despite recent decline in interest rates. To encourage and stimulate activity in the private sector, monetary policy will continue with its easing stance in 2012/13. The main objective is to support and strengthen the private sector in these trying times. The Central Bank Credit Line Facility will also infuse some more liquidity to selected sectors of the economy,

fostering competition in the financial system, reducing or holding down interest rates and boosting private sector credit demand.

In effect, monetary aggregates are expected to be moderate in 2012/13. Following a 5.9 percent growth in 2011/12, average bank credit to the private sector is anticipated to slow down to around 1.5 percent, evidence of the current state of slow growth in demand for credit despite the low lending interest rates. However, with an expected net inflow of foreign funds during the course of the year, total money supply (M2) is forecast to pick up to 3.7 percent, from -5.5 percent in 2011/12.

Table 7
Monetary Survey
(Amounts in Tala million)

End of Period	2007/08	2008/09	2009/10	2010/11	2011/12	Forecast 2012/13
A. Determinants of Money Supply						
Net Foreign Assets	227.7	248.5	364.7	334.1	301.2	328.2
Net Domestic Assets	392.6	419.8	376.5	401.0	404.6	339.5
Government's Net Position	-89.0	-86.9	-181.6	-171.1	-186.7	-204.6
Bank credit to private sector	586.3	619.4	648.7	687.3	700.7	721.3
Bank credit to public institutions	67.6	74.2	93.2	105.7	86.8	71.8
Others, net	-172.4	-186.9	-183.8	-220.6	-196.2	-249.0
B. Money Supply (M2)	620.2	668.3	741.2	735.1	705.8	667.7
Narrow Money	153.6	154.6	204.6	220.2	219.3	197.0
Currency Outside banks	41.0	41.6	43.1	50.7	58.8	46.6
Demand Deposits	112.6	113.0	161.5	169.5	160.6	150.5
Quasi-money	466.6	513.7	536.5	514.9	486.5	470.7
Savings deposits	74.1	78.3	88.0	94.1	95.2	84.7
Time deposits	371.5	416.4	427.1	391.1	363.9	361.4
Foreign Currency Deposits of Residents	21.0	19.0	21.4	29.8	27.3	24.6

Source: Central Bank of Samoa

This monetary policy stance will be reviewed after six months or earlier if necessary.
