II. OVERVIEW OF ECONOMIC DEVELOPMENTS DURING THE SECOND QUARTER OF 2017.

The World Economy

***The second quarter of 2017** highlighted ongoing solid improvements in the world economy, with positive economic performances in both advanced economies and emerging & market developing economies. Firm economic activities were supported by low inflationary pressures and favourable labour market conditions across most of Samoa's major trading partners. Against this backdrop and in the presence of downside risks, most monetary authorities maintained accommodative monetary policies in pursuit of sustainable economic recoveries and price stability targets.*

Of Samoa's main trading partner countries:

- The United State of America's economic recovery was firm in the June quarter, with an annual growth of 2.2 percent reflecting robust consumer spending, business investment and government consumption. The labour market continued to record positive gains, with the unemployment rate dropping to 4.3 percent from 4.5 percent in the March quarter. Softening inflationary pressures underpinned a 1.6 percent inflation rate in June compared to 2.4 percent in the previous quarter.
- The Australian economy grew at an annual pace of 1.8 percent in the June quarter unchanged from the previous quarter. Economic growth was supported by strong domestic demand and net exports. In the labour market, the unemployment rate dropped to 5.7 percent in June, from 5.9 percent in March as employment numbers improved. Reflecting lower transportation and housing prices, the annual inflation rate edged down to 1.9 percent in June from 2.1 percent in the previous quarter.
- New Zealand's economy grew at 2.5 percent over the year to June of 2017, matching market expectations and unchanged from the growth recorded in the previous period. Strong exports and domestic demand provided the biggest contribution to the increase in GDP. An increased number of employed people in the June quarter resulted in NZ's unemployment rate declining to 4.8 percent, its lowest rate since December 2008 at the start of the global financial crisis.
- Similarly, the inflation rate fell to 1.7 percent from 2.2 percent in the previous quarter. (Please refer to Table 1.)

Table 1: Selected economic indicators for Samoa's main trading partners

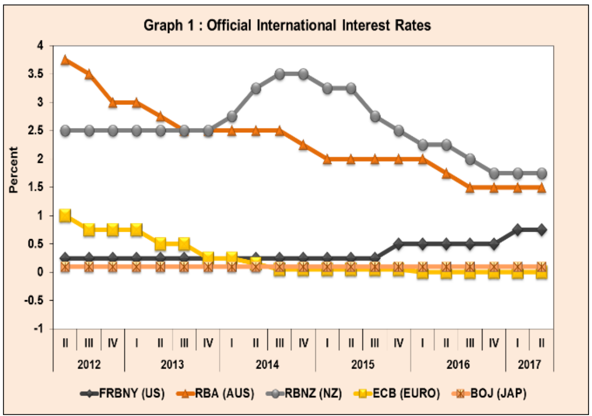
	NZ			Australia			USA			UK			Eurozone			China		
	Real GDP Growth	CPI Inflation	Unemployment Rate	Real GDP Growth	CPI Inflation	Unemployment Rate	Real GDP Growth	CPI Inflation	Unemployment Rate	Real GDP Growth	CPI Inflation	Unemployment Rate	Real GDP Growth	CPI Inflation	Unemployment Rate	Real GDP Growth	CPI Inflation	Unemployment Rate
	Year on Year Change (%)																	
Mar-15	2.9	0.3	5.4	2.3	1.3	6.2	3.3	-0.1	5.6	2.6	0.0	5.5	1.3	-0.1	11.2	7.0	1.5	4.1
Jun-15	3.3	0.4	5.5	2.0	1.5	6.1	3.0	0.1	5.4	2.4	0.0	5.6	1.6	0.2	11.0	7.0	1.3	4.0
Sep-15	2.2	0.4	5.5	2.7	1.5	6.1	2.2	0.0	5.2	2.2	-0.1	5.3	1.6	-0.1	10.8	6.9	1.6	4.1
Dec-15	2.2	0.1	5.0	3.0	1.7	5.8	1.9	0.7	5.0	2.1	0.2	5.1	1.7	0.2	10.4	6.8	1.6	4.1
Mar-16	2.8	0.4	5.2	3.1	1.3	5.7	1.6	0.9	5.0	2.0	0.5	5.1	1.7	0.0	10.2	6.7	2.3	4.0
Jun-16	3.4	0.4	5.1	3.3	1.0	5.8	1.3	1.0	4.9	2.2	0.5	4.9	1.7	0.1	10.1	6.7	1.9	4.1
Sep-16	2.9	0.4	4.9	1.8	1.3	5.6	1.7	1.5	4.9	2.2	1.0	4.9	1.7	0.4	9.9	6.7	1.9	4.04
Dec-16	3.5	1.3	5.2	2.4	1.5	5.8	2.0	2.1	4.7	1.9	1.6	4.8	1.7	1.1	9.6	6.8	2.1	4.02
Mar-17	2.5	2.2	4.9	1.8	2.1	5.9	2.0	2.4	4.5	2.0	2.3	4.6	1.9	1.5	9.4	6.9	0.9	3.97
Jun-17	2.5	1.7	4.8	1.8	1.9	5.7	2.2	1.6	4.3	1.7	2.6	4.4	2.1	1.3	9.1	6.9	1.5	3.95

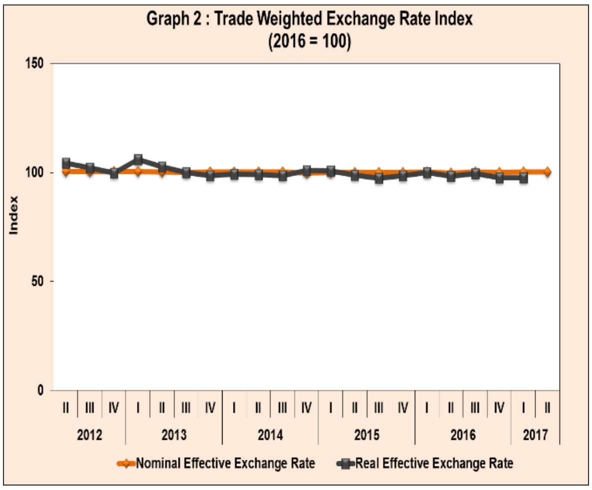
Source: Trading economics website

Despite the pickup in global economic activities so far in 2017, downside risks persist. This includes uncertainty in US policies, particularly the timing and magnitude of its earlier anticipated fiscal stimulus; post-Brexit negotiations between the United Kingdom and the European Union; China's economic slowdown; Australia's housing market; geopolitical tensions and natural disasters. As a result, most central banks have maintained their accommodative monetary policy stances, as reflected through their unchanged policy rates in the June quarter. The only exception is in the US, with the Federal Reserve Bank raising its Fund Rate range by another 25 basis points from 0.75 percent to 1.00 percent, to 1.00 percent to 1.25 percent in June. This reflects their efforts towards normalising their monetary policy, in view of an expected strong US economy in the medium term. (Please refer to Table 2).

Table 2: Major Central Banks' Policy Interest Rates					
Fiscal year to end June	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17
Official international interest rates	Percentage (%)				
US Federal Reserve	0.25 - 0.50	0.25 - 0.50	0.50 - 0.75	0.75 -1.00	1.00 - 1.25
Reserve Bank of Australia	1.75	1.50	1.50	1.50	1.50
Reserve Bank of New Zealand	2.25	2.00	1.75	1.75	1.75
Bank of England	0.50	0.25	0.25	0.25	0.25
European Central Bank	0.00	0.00	0.00	0.00	0.00

Source: Reserve banks' publications and information releases.





Note: Information on overseas economies and currencies were sourced from Bloomberg, Westpac Economics updates and Trading Economics website.

In the currency markets, the US dollar strengthened against the New Zealand and Australian currencies but weakened against the Euro in the second quarter of 2017. Positive economic data releases out of the USA and the European region contributed to these exchange rate movements during the June quarter. A string of weak economic data releases out of Australia and New Zealand as well as declining commodity prices during the quarter added downward pressure on their currencies. As a result, the Tala depreciated against the US dollar and Euro currency but appreciated against the Australian and New Zealand dollars.

In terms of the Samoan Tala's nominal effective exchange rate (NEER), the overall value of the Samoan currency appreciated against the currency basket by an average 0.16 percent in the year to June 2017. On the other hand, Samoa's real effective exchange rate (REER) depreciated 0.37 percent in the same period, reflecting lower consumer prices in Samoa compared to its main trading partners over the period. This real depreciation indicates an improvement in Samoa's international competitiveness to some extent, with cheaper goods and services relative to its foreign counterparts.

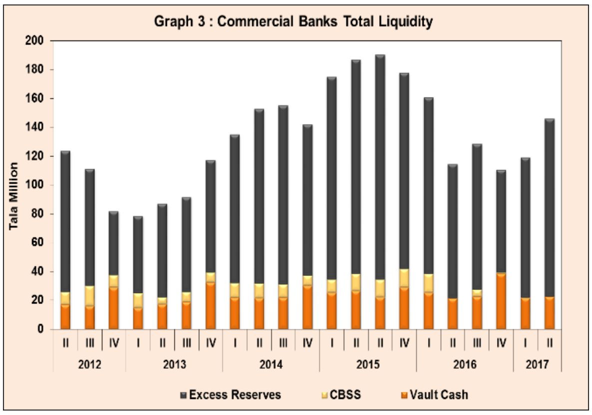
B. The Domestic Economy

The second quarter of 2017 (or end of financial year 2016/17) saw mixed developments for most macroeconomic indicators. Real Gross Domestic Product (Real GDP) registered a 2.4 percent annual growth reflecting recoveries in most sectors of the economy. Despite the drop in interest rates, domestic credit edged down while commercial banks liquidity expanded. Improvements were recorded for exports whereas visitor earnings and remittances fell.

Monetary Sector

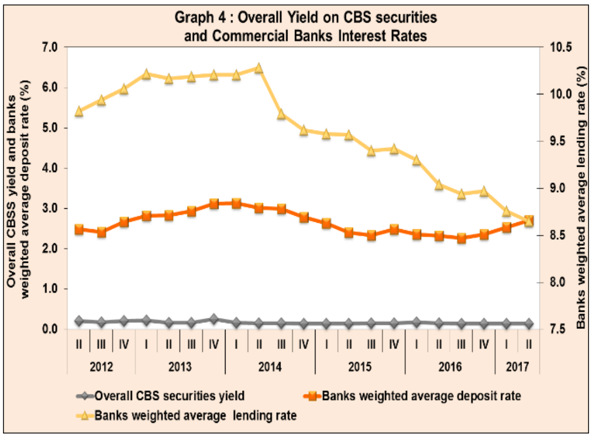
The end of FY2016/17 closed off with an $11.06 million surplus in government's net position with the monetary system to $171.22 million at end June 2017, consistently rising for the third consecutive quarter. The current level was much higher, up by $37.88 million over June last year.

The banking system average liquidity increased by $9.01 million to $132.77 million from the previous quarter. This increase was due entirely to a $13.11 million expansion in exchange settlement account (ESA), offsetting reductions of $2.50 million and $1.60 million in the average levels of Central Bank of Samoa Securities (CBSS) and bank's vault cash respectively. (See Graph 3.)



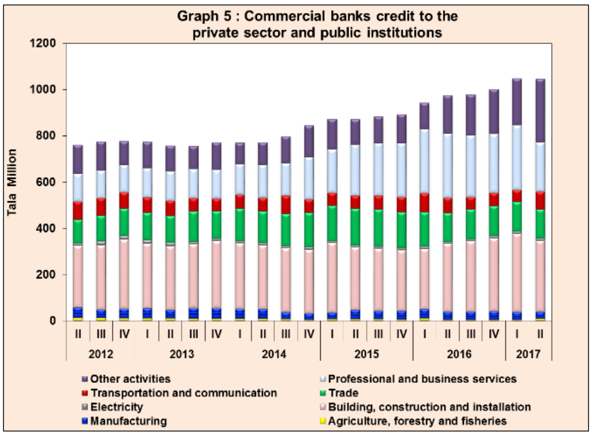
Graph 3 : Commercial Banks Total Liquidity

The overall weighted average yield on Central Bank of Samoa Securities (CBSS) remained at 0.14 percent from the previous quarter but was slightly lower than 0.15 percent in June 2016. On commercial banks' interest rates, the weighted average deposit (WAD) rate increased by 17 basis points to 2.70 percent over the previous quarter or 38 basis points higher than that of June 2016. However, the weighted average lending (WAL) rate edged down by 4 basis points to 8.65 percent or 36 basis points lower than June last year. As a result, the interest rate margin narrowed to its lowest rate yet of 5.95 percent in June 2017 from 6.17 percent at end March 2017. (See Graph 4.)



Graph 4 : Overall Yield on CBS securities and Commercial Banks Interest Rates

Despite the lower cost of borrowing, total commercial bank lending[1] to the private sector and the public institutions combined edged down by 0.2 percent (or $2.09 million) to $1,046.88 million in the June 2017 quarter. This was highlighted by reductions in loans directed to sectors such as 'professional and business services', building, constructions and installations', 'manufacturing' and 'trade'. As a result, the annual average credit growth rate dropped to 12.1 percent in June 2017 from 13.1 percent in the previous quarter but was higher than 9.1 percent in June 2016. (See Graph 5.)



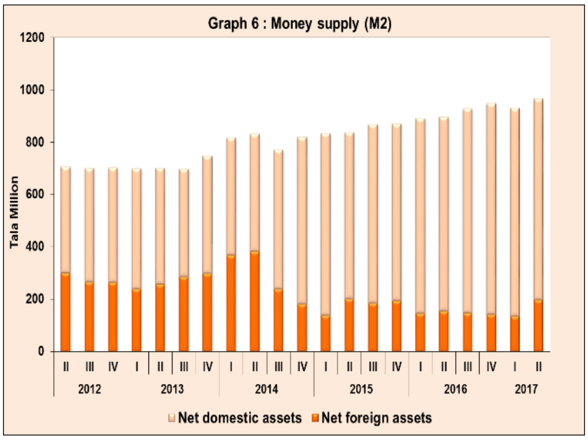
Graph 5 : Commercial banks credit to the private sector and public institutions

On the other hand, non-monetary financial institutions[2] (NFIs) lending expanded by 1.4 percent (or $10.29 million) to $739.05 million in the June 2017 quarter. This

[1] Revised back to June 2016, to reflect the reclassification of foreign currency loans (FCLs) to correct entries.
[2] Also known as Other Financial Institutions (OFCs)

reflected increased credit to both, the private sector and government corporations. The quarterly increase was mainly due to an expansion in loans to the 'building, constructions, installation and purchase of land' sector.

Overall, the total broad money[3] (M2) recorded a substantial increase of $35.37 million to $965.22 million in the last quarter of FY2016/17. Underpinning this increase was mainly a significant jump of $63.25 million in net foreign assets (NFA) despite a decline of $27.88 million in net domestic assets (NDA). The hike in NFA reflected a sharp increase in CBS held foreign reserves, mainly due to higher inflow of government funds coupled with a large net purchases of foreign exchange from the banking system. As a result, the annual average growth of M2 accelerated to 6.6 percent from 6.2 percent in the previous quarter but was lower than 7.7 percent at end June 2016. (See Graph 6.)



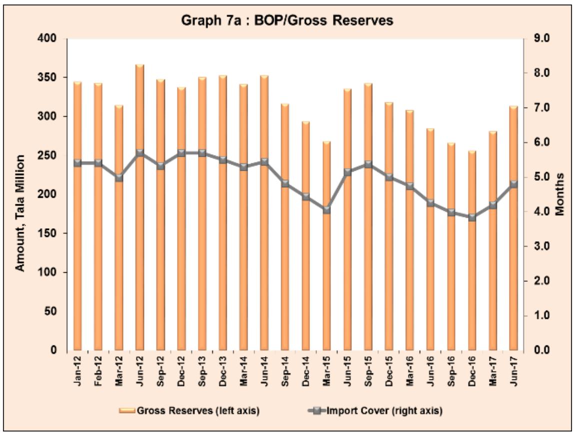
Gross Domestic Product

According to the latest national account figures from the Samoa Bureau of Statistics (SBS), total real gross domestic product (RGDP) in the June quarter of 2017 fell further by 3.6 percent when compared to the previous quarter and was 0.5 percent lower than the same quarter last year. Underpinning this contraction over the previous quarter were seasonal reductions in "Food & Beverages manufacturing", "Other Manufacturing", "Commerce", "Transport", "Communication", "Public Administration", "Financial Services", "Ownership of Dwellings" and "Personal and other services" sectors.

In contrast, the annual growth rate of RGDP up to June 2017 dropped to 2.4 percent compared to 4.2 percent at end March 2017 and 7.1 percent at end June 2016. In addition, nominal GDP per capita also contracted by 4.4 percent to $2,595.0 per person from $2,715.6 per person in the previous quarter. For the twelve months to June 2017, nominal GDP per capita ($10,902.5 per person) was 3.0 percent higher than the same period up to June 2016.

External Sector

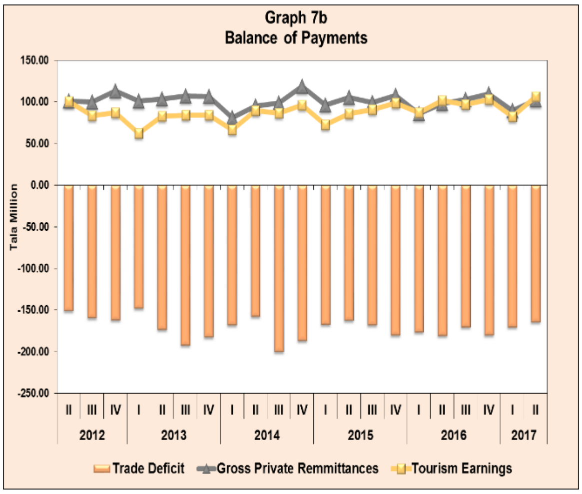
The overall balance of payments (BOP) registered a surplus[4] of $24.3 million in the quarter under review on top of another surplus of $3.0 million in the previous quarter. For the year up to June 2017, gross official reserves improved by $31.7 million to $312.8 million, a level that was sufficient to cover 4.8 months of imports, up from 4.3 months at end June 2016. (See Graph 7a.)



Similarly, the current account balance recorded a surplus in the June quarter in light of large improvements in the "Balance on Trade in Services" surplus coupled with a moderate gain in the "Balance on Secondary Income". (See Graph 7b.)

[3] Also known as Money Supply (M2)

[4] The overall BOP position is not the same as the change in gross official reserves as the overall BOP position excludes exchange rate valuation changes or movements.



The Balance on Trade in Goods (deficit) fell by 3.3 percent over the preceding quarter due to a $7.3 million hike in export earnings, offsetting a $1.6 million increase import payments.

The expansion in total exports rebounded was due to gains of $6.1 million and $1.2 million in both domestically produced exports and re-exports respectively. The hike in the former were primarily due to increased proceeds from fresh fish, spring water, beer, nonu juice, coconut, taro to name a few.

Similarly, import payments widened by $1.6 million to $190.9 million. Largely underpinning this expansion were gains of $6.6 million and $2.0 million in both government and petroleum imports, outweighing a $7.0 million contraction in non-petroleum private sector imports.

Total visitor arrivals in the June quarter are not yet available, however, careful CBS estimates projected a seasonal 25.0 percent increase over the March 2017 quarter. Consequently, visitor earnings are expected to bounce back up by 29.2 percent to $106.7 million in line with its seasonal trend.

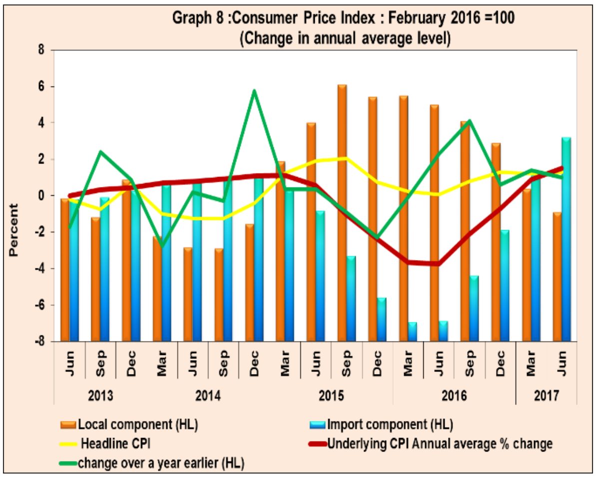
Total private remittances also went up by 14.2 percent to $102.6 million in the reviewed quarter. Primarily underpinning the overall increase were improvements in funds sent from Australia, New Zealand and the United States of America.

Price Developments

The headline Consumer Price Index (CPI) rose by 0.3 percent from the previous quarter and was 1.3 percent higher when compared to the June 2016 quarter.

Primarily responsible for the current increase in the CPI were expansions of 4.0 percent and 0.6 percent in its local and imported components respectively. Moreover, the annual average inflation rate increased slightly to 1.3 percent from 1.2 percent at end March 2017 and 0.1 percent at end June 2016. This was due to an increase in imported inflation to 3.2 percent from 1.1 percent in the previous quarter, while domestic inflation slowed to -0.9 percent from 0.4 percent in the March 2017 quarter.

The underlying CPI likewise, increased by 0.2 percent from the previous quarter and was 0.7 percent higher when compared to the same quarter in 2016. On an annual average basis, the underlying inflation rate climbed up to 1.5 percent from 0.9 percent in the previous quarter and -3.7 percent in June 2016. (See Graph 8.)



III. PRUDENTIAL SUPERVISION

For the quarter ended 30 June 2017, the banking system reflected a remarkable growth in the level of total assets by 3.1 percent ($45.2 million) to $1,507.1 million as well as total liabilities which went up by 3.9 percent ($47.4 million) to $1,268.5 million. As compared to the previous twelve months, both total assets and liabilities recorded outstanding increases of 12.0 percent ($161.7 million) and 11.5 percent ($130.7 million).

The composition of the commercial banks assets consist mainly of loans and advances (net) of $1,054.1 million (69.9 percent of total assets), currency and deposits (including cash, reserves and deposits with banks) combined at $306.1 million (20.3 percent), nonfinancial assets of $105.1 million (7.0 percent), debt securities and other assets at $21.1 million (1.4 percent) and $20.8 million (1.4 percent) in that order.

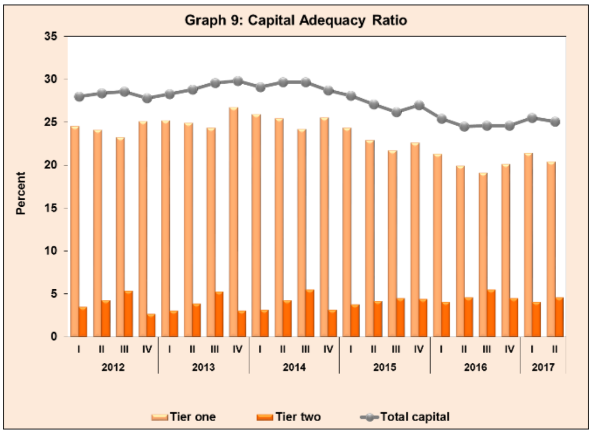
Total lending portfolio of $1,088.9 million remained at the same level over the previous quarter. On an annual comparison total loans and advances grew significantly by 6.7 percent ($68.8 million). The allocation of loans and advances by sectors during the quarter revealed a growth in loans to businesses.

Total deposit liabilities increased by $30.9 million (2.9 percent) over the past three months to $1,084.7 million. Likewise, annual comparison revealed an outstanding increase of $119.6 million (12.4 percent) due mainly to the growth in the level of domestic deposits. Time deposits ($543.7 million) represented 50.1 percent of total deposits, demand deposits ($404.7 million) accounted for 37.3 percent while savings deposits ($136.2 million) made up 12.6 percent of total deposit liabilities.

Contingent and off-balance sheet items of $150.9 million (10.0 percent of total assets), rose by $9.2 million (6.5 percent) over the quarter but dropped by $17.6 million (10.4 percent) as compared to the same period a year ago. The significant movement on annual comparison was caused mainly by decreases in unmatured foreign exchange contracts and unused credit commitments correspondingly.

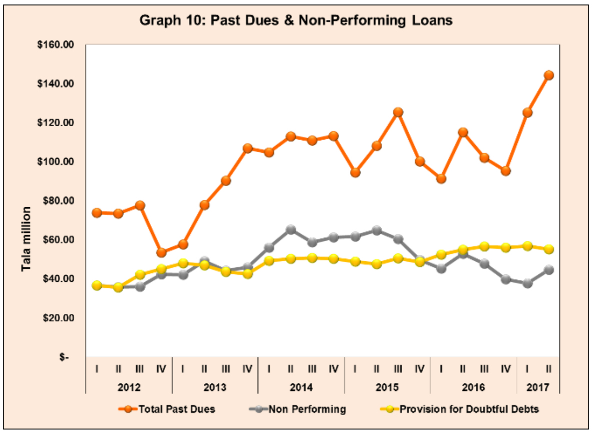
At $219.3 million, the capital adequacy ratio reduced minimally by 0.4 percent to 25.1 percent over March 2017, and continued to stay well above CBS minimum requirement of 15.0 percent.

Tier 1 capital ratio of 20.4 percent also continued to trend comfortably above the CBS minimum requirement of 7.5 percent. (See Graph 9).



The overall system liquidity level of $145.8 million improved tremendously by 22.3 percent ($26.6 million) over the previous quarter and represented 14.6 percent of total domestic deposit liabilities.

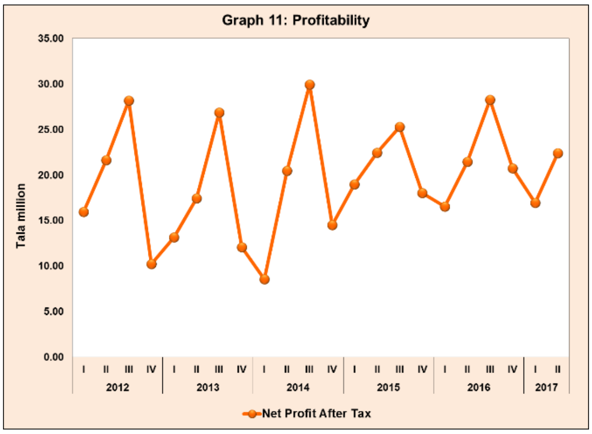
The overall level of non-performing loans (NPLs) of $44.8 million, went up by 18.9 percent ($7.1 million) over the previous quarter and dropped favorably by 15.5 percent ($8.2 million) over June 2016.



In relation thereto, total specific provisions of $34.8 million provided 77.7 percent coverage of non-performing loans. At the same level, total provision for bad and doubtful debts of $55.1 million accounted for 5.1 percent of total loans and advances and provided sufficient coverage for non-performing loans.

At a combined figure of $30.7 million, the banking system's pre tax profit level increased by 5.7 percent ($1.6 million) when compared to the same period a year earlier.

Total net profit after tax of $22.4 million, reflected a return on average networth and average assets of 25.9 percent and 4.2 percent respectively. (See Graph 11).



In terms of performance, the banking system efficiency level is reflected at 64.7 percent compared to 59.4 percent registered a year ago.

The combined foreign assets of the commercial banks amounted to $279.8 million as compared to total foreign liabilities of $250.6 million. At these levels, it showed a net long open position of $62.3 million or 28.4 percent of the banking system's total capital.