



CENTRAL BANK OF SAMOA



**MONETARY POLICY STATEMENT
FOR THE FINANCIAL YEAR 2007/2008**

**APIA
September 2007**

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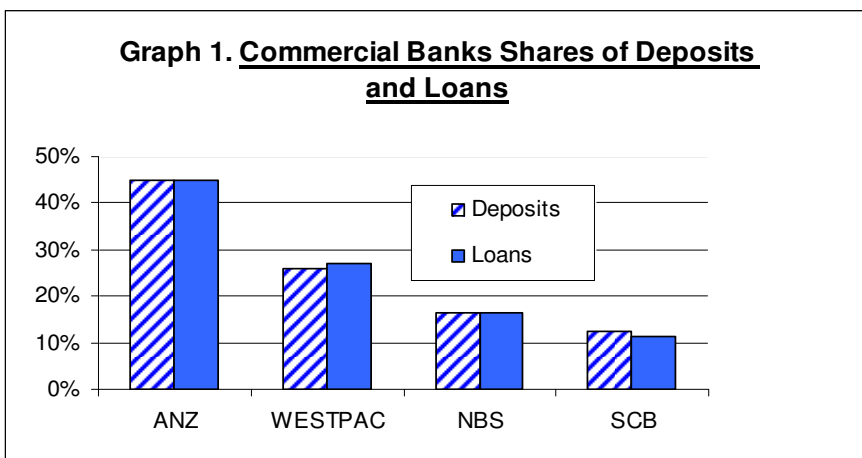
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1. INTRODUCTION

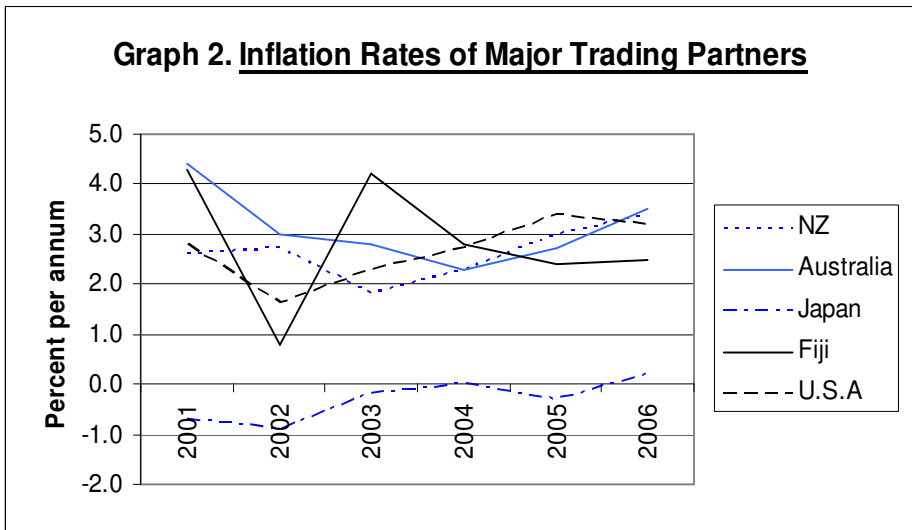
In line with Government's emphasis on transparency and accountability, Monetary Policy Statements (MPS) serve as the main vehicle to communicate and explain to the public the main monetary policy objectives and targets that would be pursued by the Central Bank in the year ahead. As well, these Statements 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.

The existing monetary policy framework was first introduced with the commencement of financial sector liberalization in January 1998. Under this framework, monetary policy decisions are implemented via open market operations through the issuance and trading of Central Bank Securities. By and large, monetary policy decisions are channelled through the commercial banks since they play a dominant role in the financial system. Commercial banks are the only institutions authorised to accept deposits from the public and extend credit from those deposits. In addition, they account for the largest share (over 60 percent at end June 2007) of financial institutions' loans to the private sector. (See Graph 1.)



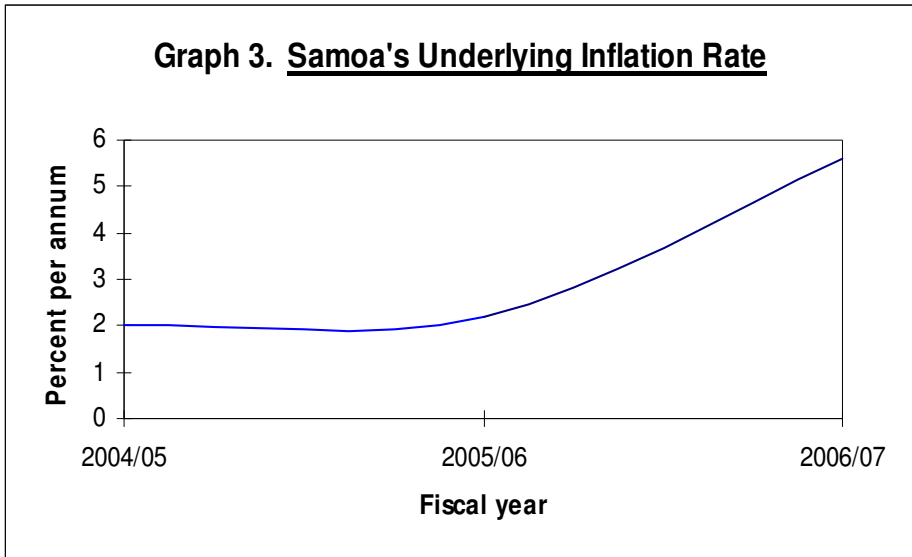
However, given that the Samoan economy is small, the lopsided structure of the financial system with one bank dominating the deposits and the lending market (as shown by the above graph), and the relatively large size of the public sector, open market operations type of monetary instruments in Samoa need to be supplemented with *moral suasion* to make monetary policy more effective.

The Central Bank has defined price stability as an inflation rate consistent with those of Samoa's main trading partners. The rates of inflation for Samoa's main trading partners currently average around 3.0 percent per annum and this is the target that the Central Bank normally aims to achieve in the long term. (See Graph 2.)



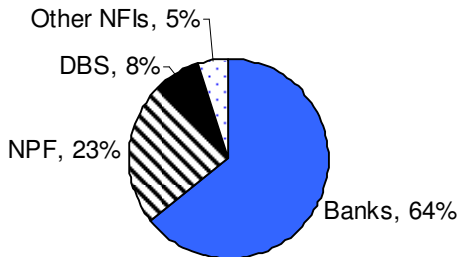
Aiming to be consistent with inflationary trends for trading partner countries reflects the need to maintain the international competitiveness of Samoa's industries, particularly those that are export oriented. However, there are times when changes to prices are beyond the realms of monetary policy, indeed beyond the control of the Central Bank. This was the case in recent years where the sharp and continually increasing international price of crude oil combined with the adverse effects of natural disasters, such as cyclone Heta in January 2004, to drive up the

prices of petroleum products and local food. During such periods, attention is focused more on the underlying or core inflation rate. The underlying CPI is a relatively new measure, with a time series compiled and published for the last three years. (See Graph 3.)



Since 1998, the main intermediate target has been money supply M2. However, targeting M2 has become increasingly difficult because of the ongoing developments in the domestic financial system with the consequent instability in the technical relationships between the monetary aggregates and target variables as well as uncertainty surrounding the timing of expenditures related to large public sector financial flows. Government financial flows in particular are relatively large and therefore have a substantial impact on the monetary system, the financial sector and the economy. With the share of the banks in the credit market continuing to grow relative to that of the non-banks, more attention has been given to targeting the growth of bank credit to the private sector in recent years. (See Graph 4.)

Graph 4. Financial System Credit to Private Sector



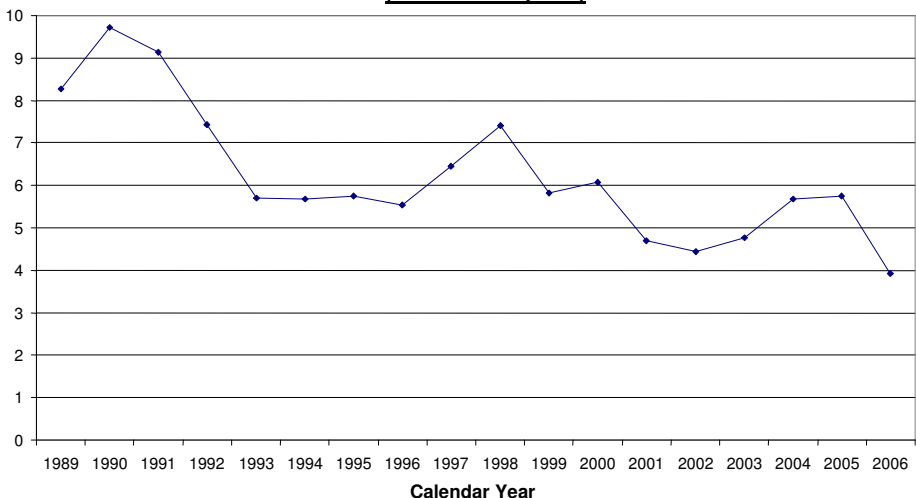
In addition, although they have not been targeted specifically because of technical constraints (particularly the absence of sufficient historical time series), the limited data available seem to confirm that monetary policy would be more effectively implemented by focusing on interest rates rather than on monetary aggregates. Whereas the limited access to credit was the main constraint facing the private sector at the time financial liberalization was introduced in 1998, the expansion and continuing changes to the structure of the financial system and further financial deepening have made interest rates increasingly important in the community's decision making process.

Samoa is a small open economy with total merchandise trade alone representing around 60 percent of nominal GDP. In the event, it is very important that Samoa maintains a sufficient level of international reserves to withstand large 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. This target level of international reserves was set principally as a buffer that would be adequate enough to sustain the

economy whilst it tries to recover from a major external shock in the future.

With global warming intensifying, Samoa is now regularly subjected to natural calamities particularly cyclone devastations. As experienced in the first week of February 1990, Cyclone Ofa struck the country causing tremendous damage to public as well as private sector infrastructure. Less than a year later in December 1991, Cyclone Val struck with even more devastating force. Virtually all sectors of the economy were adversely affected directly or indirectly. Consequently, the level of international reserves, which have been piling up reaching a high of 11.4 months just before Cyclone Ofa struck Samoa in 1990, tumbled down to 8.6 months cover twelve months later, and further down to 5.9 months twelve months after Cyclone Val. (See Graph 5.)

**Graph 5. GROSS OFFICIAL INTERNATIONAL RESERVES
(Months of Imports)**



Historical events and trends supported the setting of the target for international reserves at 4 months imports cover. After declining in the period after the major cyclones of the early 1990s, the level of reserves hovered between 5 and 6 months of imports cover in the four years to 1996. Thereafter, reserves started to build up again reaching 8.3 months

in July 1998. However, the liberalization of the financial system in 1998 and further relaxation of foreign exchange control regulations saw the level of reserves tumbling down subsequently to 7.0 months in December 1998, 5.9 months in December 1999 and to 4.9 months in May 2001. After May 2001, reserves hovered between 4 and 5 months up to September 2003, rising gently to between 5 and 6 months up to December 2005 before it finally rested between 3 and 4 months in 2006. For much of 2006, therefore, the minimum international reserves target of 4 months import cover was allowed to be breached with the understanding that it would improve once the large construction projects start to wind down and with the large one-off overseas payments out of the way.

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) and real effective exchange rate (REER) of the Tala, the Central Bank aims to avoid a real appreciation of the Tala since it can adversely affect the international competitiveness of export oriented industries.

2. EXECUTIVE SUMMARY

In 2006/07, most of the major economies around the world operated under contractionary macroeconomic policies to ward off a build up of inflationary pressures. Despite the continuing rise in international oil prices, the world output grew 5.5 percent in real terms while the world inflation rate registered at 2.0 percent. Real growth was led by the booming giant economies of China and India as well as in the Euro-area, USA and Japan.

In fiscal year 2007/08, the World economic expansion is expected to continue although the real rate of growth, at 5.2 percent, would be slightly less than in 2006/07. Growth will continue to be driven by China, India, USA, Euro-area and Japan. The NZ and Australian economies are expected to remain solid in 2007/08 with rising inflation being their main concerns. Overall, oil price volatility still remains a key short term risk to global economic expansion.

On the domestic front, the reduction of the banks Statutory Reserve Deposit Ratio in October 2006, a rise in base interest rates of the commercial banks in the March 2007 quarter, large inflows of foreign direct investments and improved financial position of the Government saw liquidity conditions, which tightened significantly in the first half of the financial year 2006/07, bounce back substantially in the second half to a level that was comfortably higher than at the end of 2005/06. Consequently, combined bank credit to the private sector and public institutions as well as money supply rose sharply.

In the event, estimates showed that the local economy grew 3.1 percent in real terms in 2006/07, compliments of the ongoing construction of buildings, grounds and facilities for the 2007 South Pacific Games, continuation of Government's infrastructural developments, huge investment and aggressive competition in telecommunications infrastructure, the completion of the Development Bank of Samoa headquarter, further expansion in the commerce sector, rise in tourism

and export earnings and the second installment of the approved salaries and wages increase for the public sector.

On the external side, the balance of payments recorded a larger than expected overall surplus which outweighed a dramatic surge in imports , pushing up official international reserves to a level equivalent to slightly above the target of 4.0 months of imports.

On the other hand, domestic prices remained a pressing concern in 2006/07, as the approved increase in the VAGST and excise taxes, international oil price rises, the second installment in public servants' salaries and wages adjustment, a shortfall in agricultural food supplies to the Fugalei Market and growth in aggregate demand pushed up the headline and underlying inflation rates to above the 3.0 percent target rate.

In fiscal year 2007/08, the Samoan economy is expected to grow at much the same rate as in the last financial year. Growth will be driven by a continuation of large infrastructure projects, the construction of a number of very large buildings including the multi-million Tala buildings for the Ministry of Education, further tourism growth which in part reflect the hosting of the South Pacific Games in August 2007, redirection of tourists from the troubled spots around the Pacific, improved exports performance, and higher agriculture production.

The balance of payments is forecast to record an overall surplus of around \$10 million in 2007/08. The main contributors to this outcome are the expected strong growth in tourism revenues, a recovery in private remittances and improvement in export earnings.

For tourism, the South Pacific Games is projected to generate substantial foreign exchange earnings for the country.

The latest figures suggest that inflation is going to continue to trend higher in the first half of 2007/08, with the annual headline inflation rate likely to reach a high of 6.2 percent in December 2007 and the underlying inflation rate peaking earlier at 7.2 percent in September

2007. Thereafter, both measures of inflation are expected to decline with the headline rate slowing down to 5.1 percent in June 2008 and the underlying rate falling to 5.3 percent.








Given the outlook for the economy in fiscal year 2007/08, the Central Bank Board has decided for monetary policy to remain tightened, in order to safeguard international reserves and contain inflationary pressures. This monetary policy stance shall be reviewed mid term in February 2008 or earlier if necessary. (See Table 1.)

Table 1
Selected Domestic Economic Indicators

Fiscal year to end June	2004/05	2005/06	2006/07	2007/08 Forecast
	(Percentage change over the previous year)			
Real sector				
Nominal GDP	10.8	8.3	7.2	6.3
Real GDP	5.7	2.3	3.1	2.7
Prices				
Headline Consumer Price Index (annual average)	7.8	3.2	4.9	5.1
Underlying Consumer Price Index (annual average)		2.2	5.6	5.3
Implicit GDP Deflator (annual average)	4.6	5.8	4.0	3.5
Monetary aggregates				
Net foreign assets (annual average)	12.5	-2.3	-3.7	4.4
Government's net monetary position (end of period)	22.9	-10.9	12.7	-0.1
Bank credit to private sector				
Annual average	12.2	21.6	22.0	19.9
End period	6.8	28.3	16.5	20.1
Money Supply, M2				
Annual average	10.8	14.0	13.1	13.1
End period	15.0	13.0	8.7	16.8
Exchange rate				
Nominal Exchange Rate	0.48	0.11	0.76	na
Real Exchange Rate	5.72	-1.49	2.10	na
International reserves				
Gross International Official Reserves (Tala million)	228.23	179.34	207.24	217.76
Gross International Official Reserves (Months of imports)	5.9	3.9	4.1	4.1
Weighted average interest rates		(End of period, percent p.a.)		
CBS 14 days Securities	2.22	-	4.30	4.30 (1)
CBS 28 days Securities	3.20	-	5.65	5.33 (1)
CBS 56 days Securities	4.23	-	6.00	5.00 (1)
CBS 91 days Securities	4.92	-	6.00	-
CBS 182 days Securities	-	-	-	-
CBS 365 days Securities	-	-	-	-
CBS Securities overall weighted average yield (annual average)	3.5	1.9	4.9	4.6 (1)
Commercial bank deposits	4.3	4.8	6.5	6.4 (1)
Commercial bank credit	11.0	11.5	12.8	12.8 (1)
Commercial bank interest rate spread	6.7	6.7	6.2	6.4 (1)
Source: Central Bank of Samoa				
(1) Interest rate as at end July 2007				

3. WORLD ECONOMY

Continuing its above-trend growth, the world economy registered real economic growth of 5.5 percent in 2006/2007 and it is expected to decline slightly to 5.2 percent over the period 2007/08 period. World inflation on the other hand was registered at 2.3 percent in 2006 and is expected to decline to 2.1 percent over 2007/08 period. (See Table 2.)

Table 2				
Selected World Economic Indicators				
Fiscal year to end June	2004/05	2005/06	2006/07	2007/08 Forecast
	(Percent)			
Real growth rate	4.7	4.9	5.5	5.2
Inflation rate	1.9	2.3	2.0	2.1
Official international interest rates,	(End of period, percent pa.)			
US Federal Reserve	3.25	5.25	5.25	5.25  (1)
Reserve Bank of Australia	5.50	5.75	6.25	6.50  (1)
Reserve Bank of New Zealand	6.75	7.25	8.01	8.25  (2)
Bank of Japan	0.10	0.10	0.50	0.50  (3)
Bank of England	4.75	4.50	5.50	5.75  (4)
European Central Bank	2.00	2.75	4.00	4.00  (5)
Reserve Bank of Fiji Notes, 91 days	1.75	2.25	4.25	4.25  (6)
Source: IMF and reserve banks' publications and information releases.				
(1) Interest rate as at 07th August 2007				
(2) Interest rate as at 13th September 2007				
(3) Interest rate as at 23rd August 2007				
(4) Interest rate as at 02nd August 2007				
(5) Interest rate as at 06th September 2007				
(6) Interest rate as at July 2007				

Increases in real economic growth noted around the world caused great concern about inflation risks, thus the macroeconomic policy setting was generally contractionary. This has been true for two of the key players of the world economy: the Euro area and Japan, while the USA was on hold. The markets project that given the pick-up in economic strength in the Euro area and Japan, they will remain on a tightening cycle while the slowdown in the world's largest economy, that of the

USA will see it remain on hold but with prolonged emphasis on upside risks to the domestic inflation outlook. On the exchange rate front, the US dollar was generally weighed down against most of the major currencies. This is expected to continue more so as yield differentials continue to disadvantage the US dollar.

The world economy is forecasted by the latest updates to the IMF World Economic Outlook (WEO April 2007) to continue its expansion into 2007/08 at 5.2 percent with world inflation expected to remain close to 2.0 percent. The economic expansion is envisaged to be driven by strong growth in China and India with projected growth rates of 11.2 and 9.0 percent respectively while the key players of the world economy, the United States, Euro area and Japan are expected to take a back seat to this global economic expansion with forecasted growth rates of 2.0, 2.6 and 2.6 percent respectively.

The overall decline in oil prices since the start of the latter half of 2006 had provided welcome relief to the global economy by supporting household spending power and alleviating inflation concerns. But then oil prices rebounded in early 2007 and currently remain on the high side. Overall, oil price volatility still remains a key short term risk to the global economic expansion. The outlook is for oil prices to remain both high and volatile. Spikes toward US\$75 per barrel cannot be ruled out but a further slowdown in US economic growth could see oil prices retreat to around an average of US\$64 per barrel in 2007 and around US\$69 per barrel in 2008.

And now a look at our two closest trading partners: New Zealand and Australia.

New Zealand

After experiencing subdued growth in the third quarter 2006, the New Zealand economy rebounded on a strong pick-up in domestic demand growth - buoyed by lower petrol prices, renewed strength in the housing market and continued favourable labour market conditions. Real GDP

grew 0.8 percent in the December quarter, up from 0.3 percent growth in the September quarter 2006. This strong growth trend continued into 2007 as GDP increased further by 1.0 percent in the first quarter, taking annual average growth to 1.7 percent. A significant recovery in exports growth, particularly in dairy and metal/machinery/equipment, contributed much to growth and the reduction of the annual current account deficit to 8.5 percent of GDP in the March year 2007, from 9.0 percent in the December quarter. The easing of oil prices seen in the latter half of 2006 saw the decline in the annual CPI from 4.0 percent in June 2006 to 2.5 percent in the March quarter 2007.

Growth in upcoming quarters is expected to be within 0.5 – 0.75 percent and annual average growth is forecasted to be around 2.7 percent in 2007/08. The annual CPI is expected to be around 2.6 percent in 2007 as medium-term inflationary pressures are expected to persist. The RBNZ is also expected to maintain its tight stance until a sustained period of slow growth alleviates these pressures and should see annual inflation around 1.8 percent in 2008. Exports are expected to remain under pressure given the high exchange rate, which has been sustained by USD weakness and interest rate differentials supporting the carry trade. The annual current account deficit is forecasted to be around 8.6 percent of GDP over 2007/08. Consumer confidence has fallen over 2007, suggesting the expected easing will occur while Business sentiment has improved only slightly with fewer businesses expecting conditions to deteriorate. Westpac Australia forecasts unemployment to be around 3.3 – 3.4 percent over the 2007/08 period.

Australia

Growth in Australia continued to be driven mainly by domestic demand. Consumer confidence has remained relatively robust, thus consumer spending picking up in late 2006 and continuing into 2007, supported by growth in employment, rising household wealth and a high level of consumer confidence. GDP grew 2.8 percent in the year to December quarter 2006. The easing of oil/fuel, food and import prices in 2006 saw the underlying CPI at 2.9 percent in the year to December 2006,

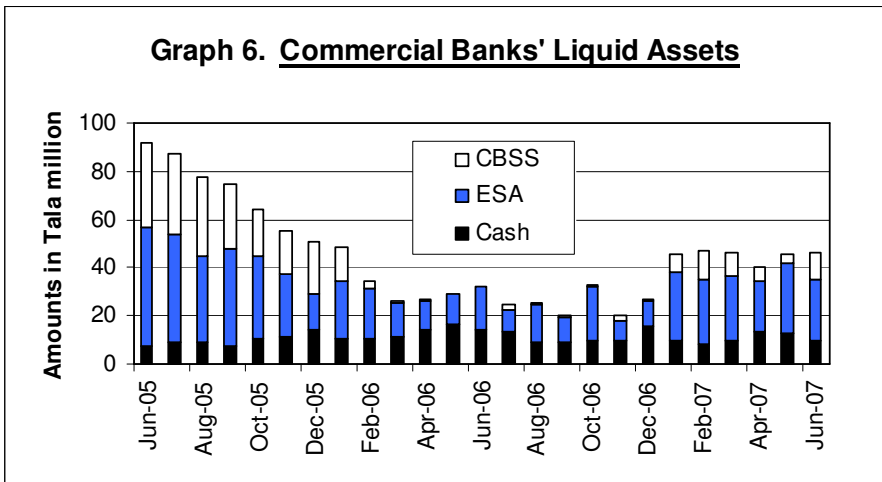
and recently at 2.4 percent in March. Unemployment was at 4.8 percent in December and has fallen to 4.5 percent in March. The current account deficit stood at around 5.5 percent of GDP. In the foreign exchange market, the AUD continued to appreciate on strong domestic data and rising commodity prices.

The growth momentum has continued into 2007. Output growth has picked up, accompanied by falling unemployment and continued strength in incomes, which have been supported by extremely high commodity prices and lower petrol prices. As GDP is forecast to grow around 4.5 percent over 2007/08 and growth will remain strong in the period ahead, this suggests operations close to full employment. Thus, ongoing pressures in the labour market and high levels of capacity utilization are expected to remain with annual CPI inflation forecasted to be around 2.8 percent over 2007/08. This will also see the RBA maintaining its mild tightening stance until mid-2008. The Unemployment rate is expected to be around 4.2 percent and the current account deficit is forecasted to be around 5.7 percent of GDP in the period 2007/08.

4. DOMESTIC ECONOMY IN 2006/07

4.1 Policy Developments

Pressure on the financial system which started to build up in the fiscal year 2005/2006 continued well into fiscal year 2006/2007. Consequently, with fiscal policy continuing on an expansionary path, as Government gave priority to Samoa's preparations for hosting the 2007 South Pacific Games, monetary policy remained tightened throughout 2006/07. Intense competition, particularly in the banking system, combined with record growth in credit to the public and private sectors to squeeze commercial bank liquidity extremely tight. (See Graph 6.)

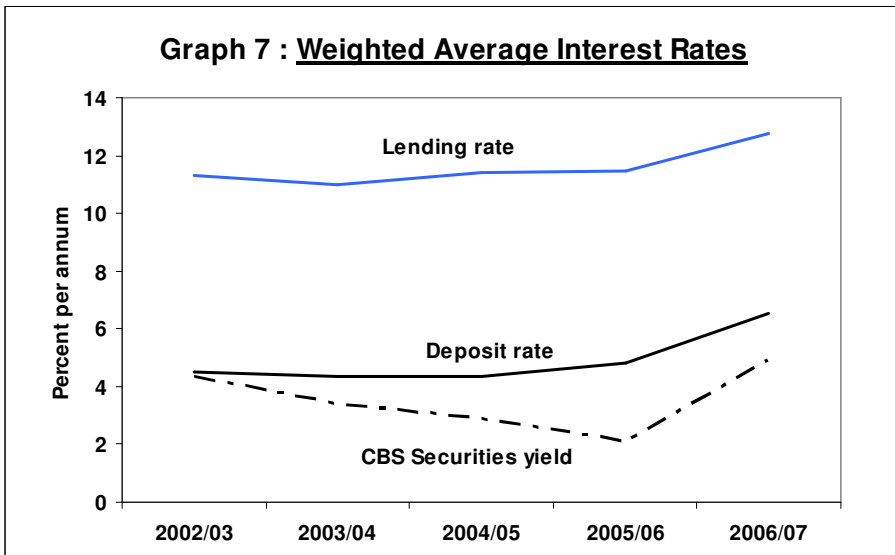


- *CBSS – CBS Securities*
- *ESA - Exchange Settlement Accounts*

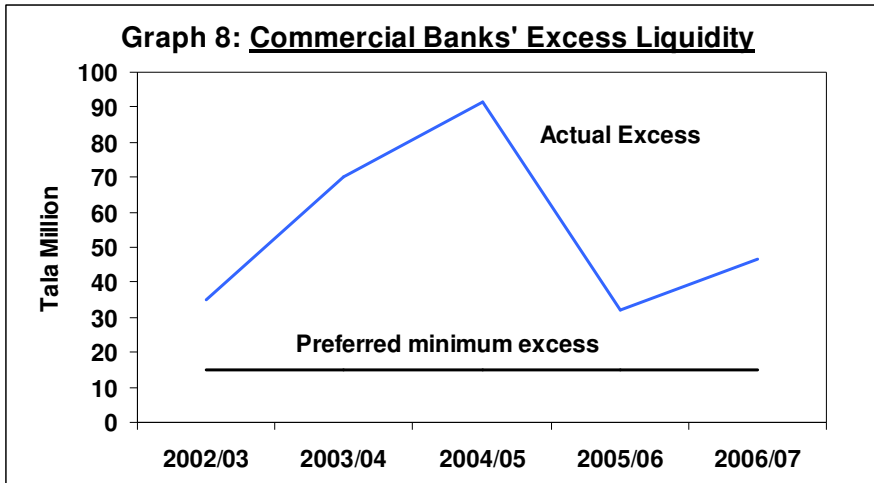
From over \$90 million at the end of fiscal year 2004/05, total commercial bank liquidity subsided steadily reaching a low of \$26 million in March 2006 and improving temporarily to \$30 million at the end of 2005/06. In the first six months of 2006/07, commercial bank liquidity declined to an average level of \$25 million, dropping to as low as \$20 million each in September and November 2006, before

recovering to an average of \$45 million in the six months to end June 2007.

Despite the very strong demand for credit which gave rise to strong credit growth, intense competition to maintain market shares saw interest rates rising only marginally in the period to end December 2006. (See Graph 7.)



The marginal rises in the overall weighted average deposit and lending rates, which reflected the acceptance of deposits and granting of loans at the higher ends of the prevailing interest rate spectrum, was insufficient to attract and sustain a high enough level of deposits or to dampen the demand for credit. As banks clambered to hold on to their shares of the banking services market, base interest rates remained unchanged, prolonging the tight liquidity situation. In the event, the liquidity situation deteriorated in the first half of 2006/07. (See Graph 8.)



So much so that in October 2006, the Statutory Reserve Deposit was reduced from 4.8 percent to 3.5 percent as a financial stability preservation measure to prop up the overall liquidity position of the banking system which had plunged to a dangerously low level at the end of September 2006.

With open market type of operations becoming ineffective in restraining the growth of credit, “moral suasion” and increased transparency became critically important tools in the Central Bank’s efforts to manage and steer monetary conditions in the preferred direction. Consultations with the banks, media publications and public presentations became more regular and bolder.

At the beginning of the second half of 2006/07, liquidity pressure and moral suasion eventually succeeded in driving the commercial banks to increase their base interest rates, starting with Westpac in January 2007, then ANZ and NBS in February and SCB in March. (See Table 3.) The base interest rates on deposits were raised between 50 and 100 basis points while those on loans were increased between 100 and 300 basis points. Almost immediately, and combined with an inflow of funds from abroad, these increases in base interest rates resulted in improving

the banking system's liquidity position substantially. Credit growth also started to slow down.

Table 3.
Commercial Bank's Base Interest Rates

	LENDING RATES		DEPOSIT RATES							
	OLD	NEW	OLD				NEW			
			1-2 mths	3-5 mths	6-11 mths	12 mths & over	1-2 mths	3-5 mths	6-11 mths	12 mths & over
WESTPAC (1)			3.75	5.25	5.75	6.25	4.25	5.75	7.00	7.50
Prime Lending	10.75	11.75								
General Finance	12.50	13.50								
Housing Loan	12.75	13.75								
Consumer Finance	15.50	16.50								
ANZ (2)	10.75	11.75	3.25	5.10	6.50	7.50	3.25	5.75	7.25	7.75
NBS (3)	10.00	12.00	3.75	5.25	6.00	7.00	4.00	5.75	7.00	7.50
SCB (4)			4.00	5.25	7.00	7.50	4.50	6.00	7.50	8.00
Motor Vehicle	12.00	14.00								
General Finance	12.00	13.50								
Housing Loan	12.00	13.50								
Small Loans	12.00	15.00								

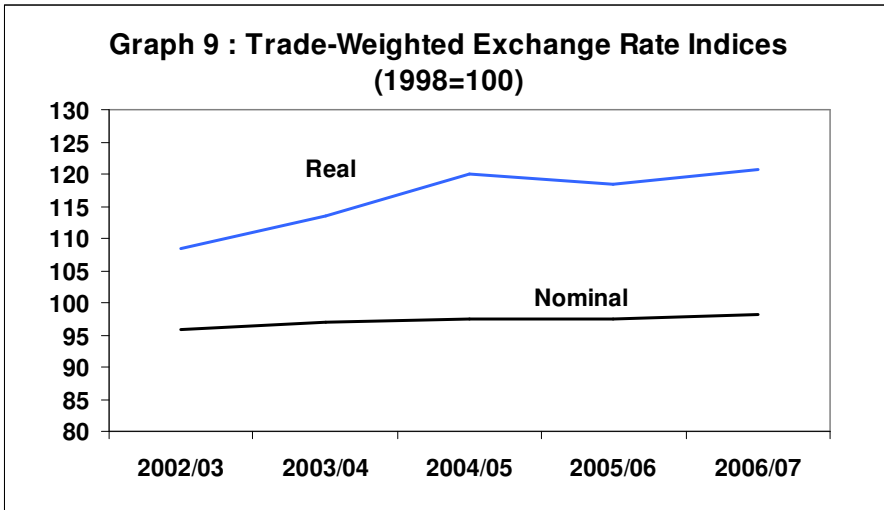
(1) Revised and effective on 22 January 2007

(2) Revised and effective on the 1st week of February 2007

(3) Revised and effective on 26 February 2007

(4) Revised and effective on 1st March 2007

In fiscal year 2006/07, the nominal effective exchange rate (NEER) of the Tala appreciated 0.76 percent on an annual average basis against the currencies in its exchange rate basket. Although this nominal appreciation helped to soften the impact of imported inflation during the year, it was not sufficient to outweigh other domestic inflationary pressures such as the increased VAGST and aggregate demand growth. Consequently, the Tala appreciated 2.12 percent in real effective terms (REER) reflecting the higher inflation rate in Samoa compared to those of our major trading partners. (See Graph 9 below.)



4.2. Macro-economic performance

4.2.1 *Real sector*

National accounts figures for the March and June quarters of 2007 are not yet available. Nevertheless, estimates showed that, for the fiscal year 2006/07 as a whole, real GDP grew 3.1 percent, which was up from 2.3 percent in 2005/06.

The key factors that drove the economy in 2006/07 were the expansionary fiscal policy, which was largely focused on the completion of sporting facilities for the 2007 South Pacific Games, the continuation of Government's infrastructural developments, the completion of the DBS Headquarter, construction of other public sector buildings and further strengthening in tourism activities. Growth was led by buoyant activities in the "commerce" sector, the largest sector of the economy, "transport and communications", "construction", "electricity and water" and "hotels and restaurants" sectors. (See Table 4.)

Table 4
Real Gross Domestic Product by Industry

(At 2002 prices, amounts in Tala Million)

During the period	2004/05	2005/06	2006/07	2007/08
	Actual	Actual	Estimated	Forecast
Agriculture	70.8	71.3	66.3	67.6
Fishing	51.0	47.2	49.1	49.8
Food & Beverage manufacturing	32.6	32.6	29.7	31.2
Other Manufacturing	105.3	89.4	90.9	89.9
Construction	79.2	85.4	89.4	92.3
Electricity and water	43.7	45.9	46.8	47.7
Commerce	188.4	196.0	205.9	210.6
Hotels, restaurants	26.0	28.5	30.4	33.1
Transport, Communication	126.0	127.9	132.1	136.7
Public administration	82.2	98.4	102.0	105.8
Finance and business service	92.8	98.3	106.2	110.7
Less: Enterprise share of FISIM (1)	-11.9	-12.2	-12.4	-12.7
Ownership of dwellings	34.9	35.6	36.3	37.1
Personal and other service	53.9	53.5	55.7	56.7
Total	974.9	997.6	1028.6	1056.5
Annual percent change	5.7	2.3	3.1	2.7
Implicit GDP deflator	113.0	119.5	124.3	128.6
Annual percent change	4.6	5.8	4.0	3.5
Source: Ministry of Finance				
(1) FISIM : Financial Intermediary Services Imputed				

The “commerce” sector, which tends to follow developments in other sectors of the economy, as well as the “electricity and water” sector, have both been robust in recent years, recording growth rates of 5.1 percent and 2.0 percent respectively in 2006/07. In the second half of 2006/07, the fishing industry rebounded as the five year growth cycle of fish stocks reached maturity stage providing the opportunity for the local fishing fleet to increase the size of their harvests. Consequently, estimates showed that there was a 4.1 percent real increase in the output of the fishing sector in 2006/07. The “construction” sector was estimated to have grown by 4.6 percent in real terms, compliments of the various large projects mentioned earlier. “Other Manufacturing” rose 1.7 percent in 2006/07 reflecting an improvement in the exports of

automotive wire harnesses to Australia, assisted by the strengthened Australian dollar. With the growth in tourism reaching new heights in the financial year under review, the output of the ‘Hotels & restaurants’ sector was estimated to have jumped 6.7 percent in real terms in 2006/07. The real output of the ‘Transport & Communications’ sector expanded 3.3 percent reflecting the substantial investments and increased competition in the cellular phone services market, combined with buoyant demand for transport services. The real value-added of the “Public Administration” sector grew 3.7 percent as Government spending for the 2007 SPG preparations intensified. The strong growth in credit saw the demand for banking services strengthening in 2006/07, driving up the real output of the “Finance & business services” sector by 8.1 percent.

On the downside, the output of the “Agriculture” sector declined 7.0 percent in 2006/2007. This saw the level of agricultural produce supplied to the Fugalei Market fall 8 percent. The availability of most staple food crops (particularly taro, banana, ta’amu and taro palagi) and some vegetables all declined in the fiscal year under review. As a result, the overall price index for the Market was 4 percent higher than in 2005/2006. Furthermore, the ‘Food and beverage manufacturing’ sector was estimated to have fallen 8.8 percent in 2006/07 reflecting a decline in beer production.

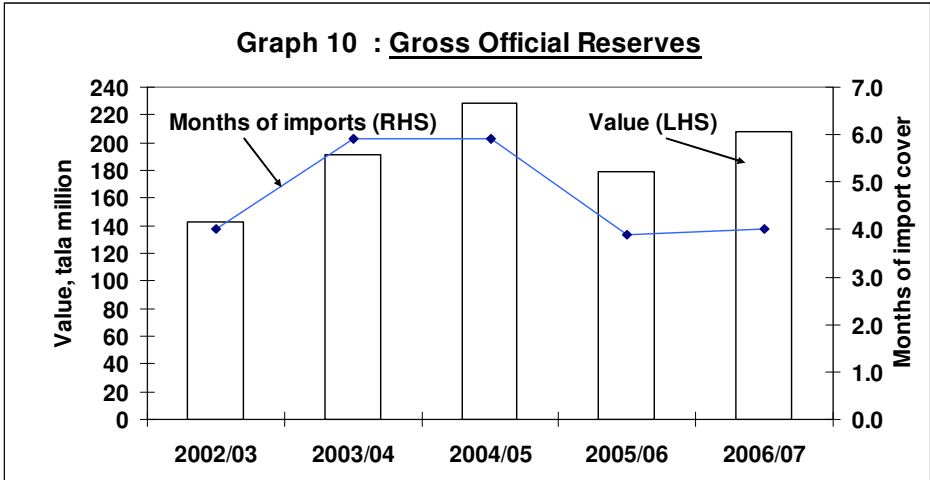
4.2.2 Balance of payments

As expected, the balance of payments recorded an overall surplus in 2006/07 of \$29 million. This surplus, which was much higher than anticipated, reflected increased tourism and export earnings, combined with the large inflows of foreign investments in the telecommunications sector. (See Table 5.)

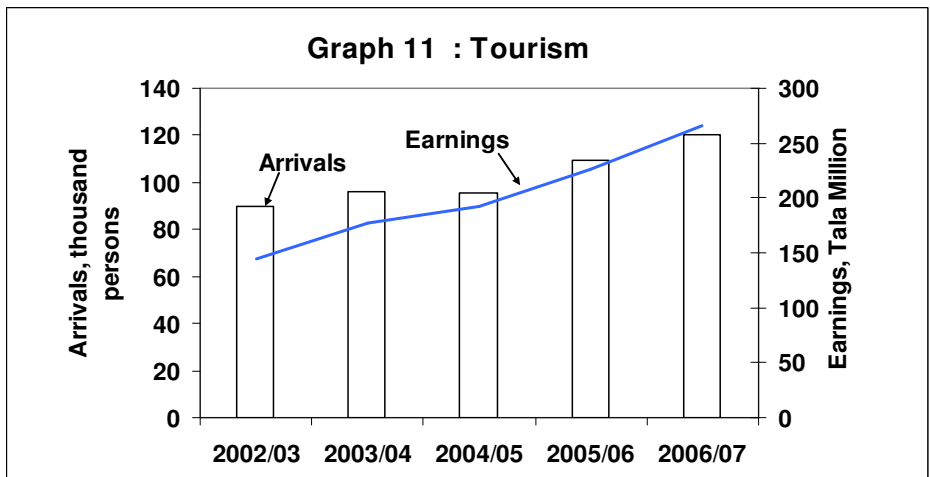
Table 5
Balance of Payments
(Amounts in Tala Million)

During the period	2004/05	2005/06	2006/07	2007/08
	Actual	Actual	Actual	Forecast
A. Current Account Balance	-61.9	-81.0	-125.6	-80.5
Merchandise Trade Balance	-429.8	-519.9	-585.5	-607.1
Exports	35.3	29.6	31.3	34.0
Imports	-465.0	-549.5	-616.7	-641.1
Services, net	160.2	178.4	234.7	263.3
Income, net	-61.9	-24.6	-26.3	-10.1
Current Transfers, net	269.5	285.1	251.5	273.4
Private transfers	241.9	280.9	246.8	265.7
Official transfers	27.6	4.2	4.7	7.7
B. Capital Account Balance	163.9	75.4	122.7	68.2
Official Grants	157.2	71.8	93.6	69.2
Other	6.7	3.6	29.1	-1.0
C. Financial Account Balance	-50.0	-27.4	25.0	22.2
Direct Investment	-8.1	0.5	51.6	11.9
Portfolio Investment	0.8	0.3	2.4	1.3
Other Investment	-42.8	-28.3	-29.1	9.1
D. Reserve Assets	-36.2	49.5	-28.5	-9.9
E. Net Errors & omissions	-15.7	-16.5	6.4	0.0
Source: Central Bank of Samoa				

The overall surplus was sufficient to offset a significant expansion in imports, thus maintaining the level of official reserves at 4.1 months of imports, which was slightly above the target of 4.0 months. (See Graph10.)

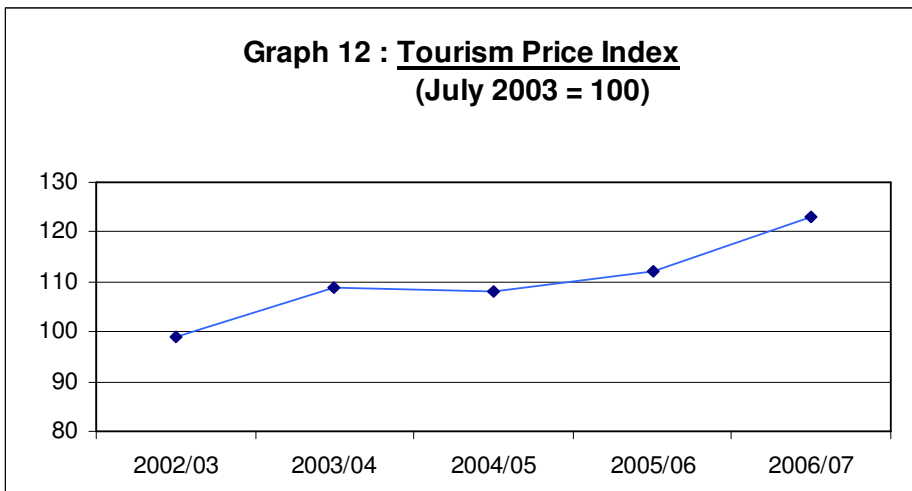


As expected, tourism activities grew strongly in 2006/07 with earnings rising 18 percent (\$40 million), compliments of a 10 percent growth in tourist arrivals and a 7 percent increase in average tourist expenditure. (See Graph 11.)



Many of the increased tourist arrivals were holiday makers and those visiting friends and relatives. There were also many who were here for the numerous regional sporting activities such as the international and

regional championships for weightlifting, archery, athletics and amateur boxing. The increase was facilitated by increased number of flights to the country, a reduction in airfares, the diversion of tourists from troubled neighbouring countries and success of overseas tourism promotions in attracting tourists to the country. The rise in average tourist expenditure, as shown by the surge in the Tourism Price Index (TPI), largely reflected the increases in the prices of products and services consumed by tourists such as hotel accommodation, car rentals and transportation, consequent to the increase in the VAGST and excise taxes in 2006/07. (See Graph 12.)



There was a slight increase in earnings from the export of automotive wire harnesses. On the other hand, private remittances fell 11 percent (\$35 million) to \$271 million in 2006/07 reflecting lower receipts by Churches (down 47 percent or \$35 million) and households (down 9 percent or \$18 million). Nevertheless, family remittances continued to account for the bulk of private remittances (65 percent) followed by remittances received by Churches (14.3 percent). Most of the private remittances came from NZ (29 percent) followed by USA (27 percent) and Australia (20 percent). A large portion of private remittances are still being received in the form of foreign banknotes (15 percent).

The total value of exports recovered to \$31 million in 2006/07, on account of a 10 percent rebound in fish export revenues (particularly in the latter half of the fiscal year under review), combined with increased earnings from nonu products (up 20 percent), coconut cream (up 8 percent), beer (up 1 percent) and re-exports (up 3 percent). (See Table 6.)

During the period	2004/05	2005/06	2006/07	2007/08 Forecast
Domestic Exports	34.99	29.53	28.39	31.10
Fish	13.65	12.68	16.88	18.61
Nonu Products	7.90	8.19	4.07	4.90
(Nonu Juice)	(6.08)	(7.25)	(3.18)	(4.00)
(Nonu Fruits)	(1.82)	(0.94)	(0.89)	(0.90)
Beer	4.60	4.34	3.18	3.21
Coconut cream	2.53	2.26	2.16	2.34
Taro	1.27	0.67	0.66	0.66
Coconuts	0.53	0.31	0.38	0.38
Soft drinks	0.24	0.22	0.34	0.24
Coconut oil	1.20	0.00	0.10	0.10
Others	3.07	0.86	0.62	0.66
Re-exports	0.20	0.09	2.86	2.95
Total	35.19	29.62	31.25	34.05

On the other hand, the strong growth of the economy saw total imports rise 12 percent (or \$67 million) to \$617 million in 2006/07, with increases recorded for all major categories of imports. Non petroleum private sector imports went up 6 percent (up \$28 million) due to a 5 percent increase in volume and a 1 percent rise in average import prices. Similarly, a rise of \$21 million was registered for Government imports which was largely due to an increase in the volume of Government imports. In addition, a 17 percent increase in petroleum imports (up \$18 million) was entirely accounted for by an expansion in the volume of

petroleum imports. In US dollar terms, the international price of oil rose 2.1 percent in 2006/07 but was offset by a 2.1 percent appreciation of the Tala against the US dollar leaving the imported price of oil unchanged in Tala terms.

While actual figures are not yet available, provisional Government Budget figures showed that capital transfers rose \$22 million to \$93.5 million in 2006/07. This amount excluded the counterpart entry for a loan of \$35 million from China that was written off by the Chinese Government as part of its assistance package to countries in the Pacific.

Within the financial account of the balance of payments, direct investment in Samoa rose to \$57 million in 2006/07 reflecting the inflow of funds for the establishment of a new mobile phone company in September 2006 as well as reinvested earnings by foreign owned enterprises, particularly the two foreign owned commercial banks. The foreign exchange assets of the commercial banks, which are not part of the country's official international reserves holdings, fell by \$3.6 million. Their foreign exchange liabilities also went down \$5.4 million. Repayments of official foreign debt dropped substantially mainly reflecting, as mentioned earlier, Samoa's debt to China of \$35 million that was written-off by that country.

4.2.3 Prices

A combination of significant domestic and external factors contributed to the outcome for inflation in 2006/07. In October 2006, the VAGST rate was increased by 250 percentage points to 15.0 percent while the excise tax on alcohol and Pocket Edition tobacco was increased by 10 percent in July 2006 and for Pall Mall Cigarettes in February 2007. In February 2007, a surcharge was imposed on electricity consumption. Furthermore, the presence of strong demand pressure associated with the growing domestic economy pushed up consumer prices in the fiscal year under review. In addition to those factors, the supplies of the local agricultural food items to the Fugalei Market fell in 2006/07. The overall volume of agricultural produce supplied to the Fugalei Market

decreased 8 percent in the twelve months to end June 2007. As a result, the overall price index for the Market was 4 percent higher than in 2005/2006.

Although overseas inflation was moderate, the relentless appreciation of the currencies of two of Samoa's major trading partners, New Zealand and Australia, particularly in the latter months of 2006/2007 drove up the prices of imported items. During the fiscal year under review, international oil prices rose further but were partially offset by an appreciation in the value of the Samoan Tala against the US dollar. All those factors combined to push up the annual headline and underlying inflation rates steadily throughout 2006/2007. The annual headline inflation rate, in particular, rose to 4.9 percent at end June 2007 from 3.2 percent at the end June 2006, 190 percentage points above the long term annual inflation target of 3.0 percent. (See Graph 13 and Table 7.)

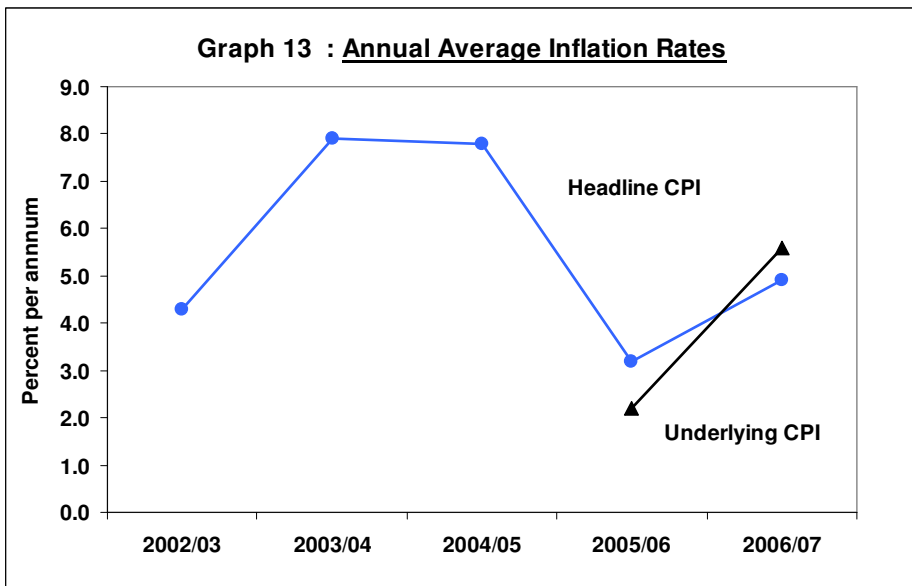


Table 7
Consumer Price Index
(March 2004 = 100)

Fiscal year to end June	2004/05	2005/06	2006/07	2007/08 Forecast
A. Headline Inflation				
(12 months average percent change)				
Description				
All Groups	7.8	3.2	4.9	5.1
Food	10.8	2.1	6.4	7.0
Clothing and Footwear	-6.3	-7.3	-3.3	-5.7
Housing and Household Operations	3.9	6.2	2.6	4.2
Transport and Communication	3.8	10.0	-1.1	2.7
Alcohol and Tobacco	-0.1	1.2	11.1	6.6
Miscellaneous	0.7	0.4	3.2	0.5
Import Component	3.6	3.5	6.0	5.1
Local Component	10.1	3.1	3.9	5.1
B. Underlying Inflation (1)				
	year on year end percent change		12 months average percent change	
Description				
All Groups	-0.4	2.2	5.6	5.3
Food	-0.7	3.0	6.5	6.6
Clothing and Footwear	-8.1	-7.3	-3.3	-5.7
Housing and Household Operations	3.1	1.5	0.5	2.5
Transport and Communication	0.9	1.4	7.1	6.2
Miscellaneous	1.3	0.9	6.6	1.1
Import Component	-1.5	1.9	5.8	5.4
Local Component	3.1	3.0	4.9	4.7
Source: Statistical Services Division, Ministry of Finance				
(1) The historical series for this new index started in August 2003.				

The acceleration of the inflation rate in the period under review reflected average increases in all groups of the headline CPI (except the “Clothing and Footwear” and the “Transport and communication” sectors, with the latter reflecting falling international oil prices, which dipped to USD\$57.22 per barrel on 12 October 2006). Contributing mainly to the increase in the twelve months of 2006/2007 were expansions of 430 points and 990 points respectively in the “Food” and “Alcohol and Tobacco” sub-indices. This saw the overall local and import components of the CPI rise 3.9 percent and 6.0 percent respectively in the period under review.

And, after extracting the influence of volatile price movements from the CPI, the underlying inflation rate increased to 5.6 percent at end June 2007, an acceleration of 340 percentage points from 2.2 percent at the end of the 2005/06 fiscal year.

5. DOMESTIC ECONOMIC OUTLOOK FOR 2007/08

5.1 Government Budget

The approved Government Budget for 2007/08 is again an expansionary one although the projected overall deficit is slightly lower than the Budget for fiscal year 2006/07. In Government Financial Statistics format (GFS), an overall budget deficit of \$14 million is expected in 2007/08, \$2 million lower than in the previous fiscal year. (See Table 8.)

During the period	2004/05 Actual	2005/06 Actual	2006/07 Budget	2007/08 Budget
Total Revenue and Grants	524.4	387.1	461.5	500.1
Total Revenue	283.0	315.3	363.0	423.1
Tax	242.2	273.1	317.9	358.7
Non-tax	40.9	42.2	45.2	64.5
External Grants	241.4	71.8	98.5	76.9
Total Expenditure	521.4	391.7	477.6	514.0
Current Expenditure	236.6	281.9	325.1	401.5
Development Expenditure	263.8	86.1	131.7	108.2
Net Lending (1)	21.0	23.7	20.7	4.4
Overall Surplus / Deficit (-)	3.1	-4.6	-16.1	-14.0
Financing	-3.1	4.6	16.1	14.0
External Financing	15.8	6.2	17.8	17.7
Disbursements	27.6	19.2	33.3	31.2
Amortisation	11.8	13.0	15.5	13.5
Domestic Financing	-18.9	-1.6	-1.7	-3.7
Monetary system	-19.0	-11.0	0.0	0.0
Other	0.1	-12.6	-1.7	-3.7

Source: Ministry of Finance

A significant part of the Budget for 2007/08 is for the completion of sporting facilities and operational expenditures for the hosting of the August 2007 South Pacific Games (SPG). It also contains the third and final installment of the approved increase in public sector salaries and wages. Aside from the preparations for the SPG, Government continues to accord priority to the “Education” and “Health” sectors as well as to upgrade the country’s roading and telecommunications infrastructure.

In 2007/08, therefore, total expenditure of \$478 million is projected to increase 8 percent from the level in 2006/07. On the revenue side, there are no new measures planned. However, Government intends to introduce improved procedures and processes to raise the efficiency of its revenue collections. This should see total tax and non-tax revenues increase 17 percent to \$423 million, more than offsetting a 22 percent fall in external grants from abroad.

The overall budget deficit is expected to be financed entirely by an increase in external soft term loans. This should allow Government to generate a cash surplus vis-à-vis the domestic financial system, thereby assisting in strengthening the liquidity position of the financial system.

5.2 Real sector

In the Government Budget for 2007/08, the “Agriculture” sector has been brought under the spot light with the sector receiving significant investment by Government. Emphasis has been placed on supporting agro-processing research to produce new and improved products for export. Investment in another heat treatment plant is in the pipeline aimed at helping manufacturers and exporters of agricultural based products satisfy overseas quarantine requirements. Agriculture production is expected to improve in 2007/08 with real output forecast to recover by 1.9 percent.

On the fishing industry, the Fisheries Division of the Ministry of Agriculture and fish exporters expect a good year for the “fishing” sector as fish stocks reach their normal five year maturity cycle.

Therefore, real output of the fishing industry is expected to improve 1.3 percent in 2007/08.

For “Food and beverages” manufacturing, demand is expected to pick up with the SPG where more tourists and the celebratory atmosphere of the games is anticipated to generate increased demand for beverages, particularly beer and water which are the largest products in the sector. This sector is therefore projected to grow 5.0 percent in 2007/08.

The output for “Other manufacturing” is expected to fall 1 percent in 2007/08 as Yazaki Samoa Ltd faces intensified competition from South East Asian companies vying for a bigger share of the Australian automotive wire harness market.

After the highs associated with preparations for the SPG, the growth of the “construction” sector is expected to cool down from a growth of 4.6 percent in 2006/07 to 3.2 percent in 2007/08. A number of major multi-million Tala building projects are scheduled to begin in 2007/08. One of them is the new Ministry of Education building at Malifa which is already under way. Other major projects include the office block for members of Parliament and the new Courthouse at Mulinuu, the Flea Market Building at Savalalo and the Ministry of Works new building at Sogi.

It is expected that the demand for electricity and water would increase following the expected growth in other key sectors of the economy. The real output of “electricity and water” is therefore projected to expand by 2.0 percent in 2007/08.

The real output of the “commerce” sector, which depends largely on developments in other economic sectors has been expanding steadily over the years, with a growth of 2.3 percent expected in 2007/08.

“Tourism”, which is now the key to sustaining Samoa’s economic growth, has grown significantly in the past four years and is expected to expand further in 2007/08. The SPG games will no doubt spur a one-off

surge in tourist arrivals in fiscal year 2007/08. Combined with continued overseas promotions, cheap airfares, regular flights and trouble in other neighbouring countries, this should see the real output for the tourism sector expand by 8.8 percent in 2007/08.

“Transport and Communications” is projected to strengthen by 3.5 percent as competition in cellular telephone services intensify. On the basis of the expected increase in Government expenditure, the output of the “Public Administration” sector is anticipated to expand 3.7 percent in real terms. Following the growth in other economic sectors, the contribution of the “Finance and business” sector is expected to expand further by 4.2 percent in 2007/08, a lower rise compared to the last fiscal year as credit demand is expected to moderate somewhat after record increases in the last two financial years.

All in all, the Samoan economy is expected to grow by 2.7 percent in real terms in 2007/08.

5.3 Balance of payments

In contrast to substantial international payment outflows in the past two fiscal years, which were largely associated with the restructuring of the national airline, there are no major one-off overseas payments expected in 2007/08 except for a relatively small payment for the early return of an aircraft for Polynesian Airlines. A favourable outlook is therefore expected for the balance of payments in 2007/08.

On foreign trade, total export proceeds for 2007/2008 are projected to improve by close to 10 percent to \$34 million. The improvement is expected to come from a recovery in exports of fish, nonu products, and coconut cream. Nonu exporters have reported that other countries are now going in to nonu production, increasing competition in this relatively new export commodity. However, the local nonu industry aims to remain competitive by focusing more on producing high quality nonu products. Efforts are being made by the local nonu producers to get Samoa’s product certified as an organic product under National

Association for Sustainable Agriculture, Australia (NASAA). This will significantly improve the prospects for exporting nonu products to lucrative quality markets in Europe and in Asia. For coconut cream, the closure of the coconut oil mill and desiccated coconut factory should make more raw materials available for coconut cream production and exports. Beer exports are not expected to deviate much from their level in 2006/07 despite reports that its main market – American Samoa- is looking at measures that would result in dramatically increasing its selling price in the US Territory. International trade experts in Samoa, however, suggest that with the USA being a signatory to the World Trade Organisation (WTO), the US Territory's proposal is unlikely to be approved by the USA Government since it would contravene WTO rules.

For imports, both the volume and average price level of imports are expected to increase in 2007/08. With the economy expected to grow further in 2007/08, the volume of imports is expected to increase 4 percent with the import unit value edging up 2.0 percent. As a result, the total value of imports is expected to grow 6 percent to \$641 million. The increase is expected to come mostly from rises in private sector imports and petroleum imports.

The expected expansion in tourism activities is expected to push travel credit up by 14 percent to \$298 million. This projection includes an estimate for tourism revenue inflows related to the August 2007 SPG. Export processing is projected to slip 1 percent while private remittances are expected to rebound by 9 percent on the expectation that the low level of remittances for charitable organisations will recover in 2007/08. Capital project grants figures were taken from the Government Budget figures for 2007/08. These are valued at \$69 million while current official transfers amount to \$8 million. Foreign Direct Investment (FDI) in Samoa is expected to increase by \$18 million due to expected inflows of investments by foreign hotel companies, combined with anticipated reinvested earnings in FDI companies. On the financial account, commercial banks' foreign assets, which are not part of the country's official international reserves, are expected to

increase by \$5 million. In the event, the balance of payments is expected to record an overall surplus of a little over \$10 million in 2007/2008 following a surplus of \$28.5 million in the last fiscal year. The overall surplus should be sufficient to meet the expected rise in imports, thereby maintaining the official foreign reserves level at the equivalent of 4.1 months of imports cover, the same level as in the 2006/07 fiscal year.

5.4 Prices

In 2006/07, inflation was largely driven by increases in the prices of imported goods and services. In 2007/08, the prices of local goods and services are projected to play catch up to the rises in the prices of imported goods and services. As a result, both the headline and underlying inflation rates are expected to remain above the long term annual inflation rate target of 3.0 percent in 2007/08.

5.4.1 Headline CPI

5.4.1a Import component

The economy is yet to fully incorporate the impact of the increased VAGST and excise taxes and the appreciation of the New Zealand and Australian dollars against the Samoan Tala in the past twelve months. Consequently, imported inflation, as measured by the upward movement in the prices of imported goods and services, is expected to increase further in 2007/08, though at a lower pace than in 2006/07.

The import component of the CPI is, on average, expected to rise 5.1 percent in 2007/08, following a 6.0 percent increase in 2006/07. With economic fundamentals pointing to depreciation in the New Zealand dollar within the next twelve months, an easing of inflationary pressures in Samoa's major trading countries, particularly New Zealand and Australia, is expected to reduce pressure on the prices of imported commodities in 2007/08. On the other hand, the impact of the increase in the VAGST in October 2006 should become fully engrained into domestic inflation in the fiscal year under review. These factors,

together with increased demand as a result of projected economic growth and the third and last portion of the public sector's salary and wage increase would be the major factors behind the expected rise of the import component of the headline CPI in 2007/08.

Within the import component, the continued instability in the international oil markets is expected to drive up the "Transport and Communications" sub-index by 4.2 percent in the next twelve months, following a 6.2 percent rise in 2006/07. While oil price variability remains a major risk to the global economy, particularly as tensions persist in the major oil supplying countries in the Middle East and Africa, any fluctuation is not expected to be as severe as in the past two fiscal years. A slight increase is also anticipated for the "Alcohol and Tobacco" (by 2.7 percent) and "Miscellaneous" (by 1.5 percent) sub-indices in the year ahead, down from significant hikes in the previous fiscal year following the imposition of increased VAGST and excise taxes in 2006. On the other hand, the "Food" sub-index is projected to grow 7.0 percent (up from a 6.8 percent rise in 2006/07). The "Housing and Household Operations" sub-group is anticipated to edge up 1.6 percent as demand is expected to remain strong during the year ahead, particularly for building materials on the back of increased incomes.

5.4.1b Local component

The local component of the headline CPI is expected to increase 5.1 percent in 2007/08, up from 3.9 percent at the end of 2006/07. Mainly responsible for this upward assessment is demand pressure coming from the projected growth in the economy, the effects of the general salary increase for the public sector, the feed-through impact of the increase in the VAGST as well as a general upward adjustment in local prices as local goods suppliers try to catch up to the rises in the prices of imported consumer goods and services. Local food prices are projected to increase by about 7.0 percent in the twelve months to end June 2008 with demand pressures at the Fugalei Market expected to remain strong, partially offsetting the expected improvement in agricultural production. The local "Housing and Household Operations" sub-index, likewise, is

anticipated to rise 6.2 percent, driven mainly by the upward revision in electricity rates in 2006/07 as well as increased demand for building materials as construction activity remain buoyant throughout the next twelve months. Increased consumer demand will also exert pressure on prices for other commodities as reflected by a projected increase of 1.9 percent for the “Transport and Communication” sub-group.

5.4.1c Headline inflation rate

All in all, the annual headline inflation rate is projected to continue its upward trend from 4.9 percent at end June 2007, peaking at 6.4 percent in January 2008 before slowing down to 5.1 percent at end June 2008.

5.4.2 Underlying CPI

5.4.2a Import Component

In the twelve months to June 2008, the import component of the underlying CPI is anticipated to decelerate to 5.4 percent from 5.8 percent at end June 2007. The slight reduction reflects the downward pressure on imported inflation, which is expected to be assisted by a softening in the New Zealand and Australian currencies following the expected easing of inflationary pressures in those two countries. The higher VAGST imposed in October 2006 on all commodities is expected to become fully engrained throughout the economy in fiscal year 2007/08.

Mainly accountable for the expected slowing down of underlying inflation is a lower 1.5 percent increase in the average level of the “Miscellaneous” sub-group, which is down from a significant 9.6 percent increase in the previous fiscal year. Similarly, the “Clothing and Footwear” sub-group is expected to register a lower growth due to robust competition in the retail sector which is expected to be sustained by cheaper supplies from source countries in Asia. On the other hand, the “Food” sub-group is expected to accelerate further to 7.0 percent, from 6.8 percent at the end of the 2006/07 fiscal year reflecting the

strong demand conditions resulting from the expected growth in the economy as well as increased purchasing power supported by the last tranche of the increased general salary and wages of the public sector. Likewise, with the various substantial construction projects expected to start within the next twelve months, increased demand for building materials will put more pressure on the “Housing and Household Operations” sub-index as reflected by a projected 2.4 percent increase in 2007/08, in contrast to a 0.1 percent drop in the last fiscal year.

5.4.2b Local Component

The local component of the underlying inflation rate is expected to rise further in 2007/08 by 4.7 percent although it would be slightly lower than the 4.9 percent rise for 2006/07. The rise is based on a projected increase in local food prices, which is expected to expand 5.5 percent, just below the 5.6 percent growth in the last fiscal year. Similarly, the “Housing and Household Operations” sub-index is expected to rise 2.8 percent, lower than the 3.1 percent growth in 2006/07.

5.4.2c Underlying inflation rate

The combination of a higher wages growth and the projected real growth in the economy in the 2007/08 fiscal year is expected to generate strong demand pressures, pushing up underlying consumer prices in 2007/08. On an annual average basis, therefore, the underlying rate of inflation is projected to continue to trend upwards in the next few months, peaking at 7.2 percent in October 2007 before declining slowly to 5.3 percent at end June 2008.

6. MONETARY POLICY STANCE FOR 2007/08

In 2007/08, the Samoan economy is again forecast to grow strongly, driven by a continuation of large infrastructure projects, the construction of a number of very large buildings including the multi-million tala buildings for the Ministry of Education and office block for members of parliament. Further tourism growth is projected, which in part reflect the hosting of South Pacific Games in August 2007 and redirection of

tourists from the troubled spots around the Pacific. Agriculture production and the fish catch are anticipated to recover, increasing exports earnings in 2007/08. Remittances are also anticipated to recover. In the event, the balance of payments is forecast to record an overall surplus of a little over \$10 million. Despite imports growing further, the strength of foreign reserves is expected to hover around the same level of import cover as in 2006/07 of 4.1 months. This, however, is barely above the target level of 4.0 months which leaves very little room for relaxation of monetary policy settings.

On the other hand, prices are a great concern, with the latest figures suggesting that inflation will continue to trend higher in the first few months of the fiscal year. The annual headline inflation rate is likely to reach a high of 6.2 percent in December 2007 before it declines thereafter, slowing down to 5.1 percent in June 2008. The main inflationary factors in 2007/08 are the demand pressures that accompany the expected real economic growth, the third and last round of salary and wages increases for the public sector and the expected further rise in international oil prices. At 5.1 percent and 5.3 percent, the annual headline and underlying inflation rates respectively, exceed Government's long term annual inflation target of 3.0 percent.

Commercial bank liquidity recovered significantly in the last half of 2006/07 from its very low level in earlier months. However, in 2007/08, liquidity is again expected to come under pressure as the large projects that are in the pipeline commence. The banks' Statutory Reserve Deposit Ratio will therefore be kept at 3.5 percent in 2007/08.

Given the above outlook for the economy, monetary policy will remain tightened in fiscal year 2007/08, in order to safeguard international reserves and contain inflationary pressures. In 2007/08, therefore, bank credit to the private sector and money supply are projected to grow moderately. (See Table 9.)

Table 9
Monetary Survey
(Amounts in Tala million)

End of Period	2004/05	2005/06	2006/07	2007/08 Forecast
A. Determinants of Money Supply				
Net Foreign Assets	231.3	184.6	199.3	209.2
Net Domestic Assets	209.9	313.9	342.5	423.4
Government's Net Position	-100.3	-89.3	-100.5	-100.5
Bank credit to private sector	383.0	490.9	572.5	683.6
Bank credit to public institutions	10.3	28.5	31.6	31.6
Others, net	-83.1	-116.2	-161.1	-191.3
B. Money Supply (M2)				
Narrow Money	441.2	498.6	541.8	632.6
Currency Outside banks	132.8	145.2	151.0	183.2
Demand Deposits	30.7	37.0	42.4	46.1
Quasi-money	102.1	108.2	108.6	137.1
Savings deposits	308.4	353.4	390.8	449.4
Time deposits	55.8	64.3	71.2	82.1
Foreign Currency Deposits of Residents	239.5	269.4	309.9	351.5
Foreign Currency Deposits of Residents	13.1	19.7	9.7	15.8
Source: Central Bank of Samoa				

And, in line with this monetary policy stance, official interest rates – i.e. the interest rates on Central Bank Securities - will be maintained at their current levels with commercial bank base interest rates also expected to remain unchanged.

This monetary policy stance shall be reviewed in February 2008 or earlier if necessary.
