



CENTRAL BANK OF SAMOA

MONETARY POLICY STATEMENT FOR THE FINANCIAL YEAR 2018/2019



APIA
NOVEMBER 2018

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1. INTRODUCTION

The ultimate goal of Monetary Policy Statements (MPS) is to effectively communicate the Central Bank of Samoa's (CBS) monetary policy stance and promote its accountability through public awareness. The main objectives of the monetary policy and its corresponding targets are set out in its main legislation, the CBS Act 2015. This Statement is also aligned with the Central Bank of Samoa's Corporate Plan (CBSCP) and the latest Government's Strategy for the Development of Samoa. The primary aim of the Central Bank's monetary policy is to achieve and maintain price stability as well as fostering and maintaining a stable financial system in order to achieve a sustainable real economic growth and a comfortable level of international reserves. Monetary policy decisions are conducted through open market operations (OMO) through the issuance and trading of CBS Securities (CBSS) to achieve these objectives.

The CBS quantifies Samoa's targeted inflation rate to its major trading partners' at an annual average inflation rate of 3.0 percent in order to pursue and achieve price stability. This naturally determines the target that the CBS seeks to maintain each year although price volatilities that are usually created by external shocks beyond CBS monetary policy control. Past years' experiences reveals that persistent sharp hikes in international prices such as crude oil and imported food prices had exerted significant pressures on the domestic prices of petroleum and food items. During such periods, focus was mainly on the underlying (core) inflation rate.

Another major aim of the CBS is to nurture and maintain a stable financial system by promoting the regulation and supervision of commercial banks and non-bank financial institutions like the Samoa National Provident Fund, Development Bank of Samoa, Unit Trust of Samoa as well as money transfer operators, foreign

exchange dealers and insurance companies. This will ensure an efficient operation of the financial market amidst a sound and effective infrastructure.

Samoa is a small open economy with total merchandise trade representing about 60 percent of nominal gross domestic product (GDP). Total earnings from exports of goods accounts roughly for one tenth of total import payments every year. It is crucial therefore that Samoa maintains a sufficient level of international reserves in order to withstand the many unanticipated economic shocks (both natural and man-made). CBS, under prevailing circumstances targets a level of gross official international reserves to no less than 4.0 months of imports of goods, sufficient to maintain Samoa's long term international reserves viability.

The main objective of the CBS's policy on Exchange Rate (ER) is to ensure that export-oriented industries remain competitive in overseas markets whilst 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 its international competitiveness through its export sector.

2. EXECUTIVE SUMMARY

2.1 World Economy

The initial IMF World Economic Outlook (WEO) in October 2018 projected a 3.7 percent growth in global economic activity for 2018/19, downgraded from a 3.8 percent forecast in its July publication. This latest updated economic growth estimates mainly reflect downside risks, which has escalated the level of uncertainty across the globe and curbed the strong economic performances in the last half of 2017/2018. These included escalating trade tensions between the United States of America and China as the two major economies imposed import tariffs on each other's products, the

weak economic releases in some advanced economies, weaker outlook for some key emerging market and developing economies, geopolitical tensions and rising oil prices.

2.2 Domestic Economy

The Samoan economy slowed further in 2017/18, in line with CBS forecasts reflecting the complete closure of Yazaki Samoa Limited as well as reductions in output for the 'Fishing', 'Agriculture' and 'Financial services' sectors.

On the monetary side, commercial bank's average liquidity continued to improve during the course of the year in light of strong external inflows while commercial bank interest rates were more or less stable.

On the fiscal side, the Government expenditure was kept in control in line with fiscal consolidation objectives but still prioritizing key sectors such as Education, Health and Infrastructure.

Looking at prices, both the headline and underlying CPI were on the rise given increases in both imported (hike in imported fuel prices) and domestic prices (increase in local food following Cyclone Gita). (See Table 1.)

Table 1						
Selected Domestic Economic Indicators						
Fiscal year to end June	2014/15	2015/16	2016/17	2017/18	Forecast 2018/19	
(Percentage change over the previous year)						
Real sector						
Nominal GDP	4.4	5.5	1.3	6.1	6.0	
Real GDP	1.7	7.2	2.7	0.7	3.7	
Prices (February 2018=100)						
Headline Consumer Price Index (ann ave)	1.9	0.1	1.3	3.7	3.5	
Underlying Consumer Price Index (ann ave)	0.6	-3.7	1.5	3.7	3.3	
Implicit GDP Deflator (annual average)	2.7	-1.7	-1.4	5.4	2.3	
Monetary aggregates						
Net foreign assets (annual average)	-42.4	3.1	-14.9	97.7	18.7	
Government's net monetary position (end of period)	14.9	14.8	28.4	15.3	-13.4	
Bank credit to private sector						
Annual average	13.5	10.6	13.9	2.2	6.6	
End period	17.6	13.0	8.7	-0.7	7.8	
Money Supply, M2						
Annual average	8.0	7.6	6.6	12.8	5.3	
End period	0.6	7.1	7.8	16.5	-0.3	
Exchange rate (March 2016=100)						
Nominal Exchange Rate (annual average)	-0.18	-0.03	0.16	-0.02	na	
Real Exchange Rate (annual average)	0.52	-1.24	-0.36	1.64	na	
International reserves						
Gross International Official Reserves (Tala million)	335.77	283.04	312.79	422.74	436.37	
Gross International Official Reserves (Months of imports)	5.1	4.3	4.8	6.1	6.1	
Weighted average interest rates						
	(End of period, percent p.a.)					
CBS 14 days Securities	0.13	0.13	0.13	0.13	na	(1)
CBS 28 days Securities	0.16	0.16	0.16	0.16	na	(1)
CBS 56 days Securities	0.18	0.18	0.18	0.18	na	(1)
CBS 91 days Securities	0.41	0.41	0.41	0.41	na	(1)
CBS 182 days Securities						
CBS 365 days Securities						
	(period average, p.a.)					
CBS Securities overall weighted avg yield (ann avg)	0.15	0.16	0.14	0.16	na	(1)
Commercial bank deposits	3.02	2.58	2.45	2.75	na	(1)
Commercial bank credit	10.45	10.02	8.82	8.86	na	(1)
Commercial bank interest rate spread	7.43	7.44	6.37	6.11	na	(1)
Source: Central Bank of Samoa						
(1) Interest rate as at end August 2018						
na - not available						

The external sector recorded a record surplus of 109.8 million in the balance of payments for the whole of 2017/18 reflecting large Government and private sector inflows as well as strong growth in remittances and visitor earnings. As a result, gross foreign reserves leapt to \$422.6 million or equivalent to 6.1 months of imports from 4.8 months in the previous year.

3. REVIEW OF 2017/2018

3.1 WORLD ECONOMY

The International Monetary Fund (IMF), in its *October 2018 World Economic Outlook*, downgraded the global economic growth projection for the short term as mounting headwinds in recent months weighed heavily across the board. Compared to an earlier 3.8 percent projection in April and July, the global economy is now expected to remain at a 3.7 percent growth rate in 2018/2019. This reflected an estimated slowdown in the advanced economies from 2.35 percent in the previous year to 2.25 percent, as well as a steady growth of 4.7 percent in the emerging market and developing economies.

The IMF's downward revision for 2018/2019 comes after a string of downside risks in recent months which has escalated the level of uncertainty across the globe and curbed the strong economic performances in the last half of 2017/2018. These included escalating trade tensions between the United States of America and China as the two major economies imposed import tariffs on each other's products, the weak economic releases in some advanced economies, weaker outlook for some key emerging market and developing economies, geopolitical tensions and rising oil prices.

With higher commodity prices, inflationary pressures built up in 2017/2018, pushing world inflation to an estimated 3.25 percent. It is projected that with the continued rise in oil prices and depreciation in some currencies in 2018/2019, the world inflation rate will increase to 3.52 percent.

As a result, monetary policies in most economies remained highly accommodative in 2017/2018. Central banks across the globe opted to maintain their interest rates close to zero levels in 2017/2018 to provide ongoing monetary stimulus to support their economies.

These monetary policies, however, are projected to diverge among the advanced economies. In particular, the Bank of England (BOE) delivered one 25 basis points hike during the year from 0.25 percent to 0.50 percent. The US Federal Reserve Bank also delivered a total of three rate hikes during 2017/2018, resulting in a target range of 1.75 percent to 2.00 percent in the Funds rate at end June 2018 compared to 1.00 percent to 1.25 percent at end June 2017. The Reserve Bank of Australia and the Reserve Bank of New Zealand maintained their policy rates at 1.50 percent and 1.75 percent respectively. It is anticipated that most of the central banks will maintain their policy interest rates at current levels, with the exception of the US Federal Reserve, which is expected to continue its tightening cycle with three more rate hikes in the Fund Rate of between 2.75 percent and 3.00 percent by the year end 2018/2019.

The foreign exchange markets in 2017/2018 continued to be driven by the deviating economic fundamentals across the globe, commodity price movements and speculation, with the markets also reacting to the start of the trade row between the US and China in January 2018. As a result, the major currencies in Samoa's Tala currency basket, namely the Australian, New Zealand and the Euro dollars, weakened against the United States dollar (USD). Subsequently, the Samoan Tala appreciated against the three currencies but depreciated against the USD. The same factors are expected to influence the currency movements in 2018/2019 with the escalating trade dispute between the top two major economies and rising oil prices to feature more prominently. (See Table 2.)

Table 2
Selected World Economic Indicators

Fiscal year to end June	2014/2015	2015/2016	2016/17	2017/18	2018/19 Forecast
Real growth rate	3.55	3.40	3.50	3.70	3.70 (1)
Inflation rate	3.00	2.80	3.00	3.25	3.52 (1)
Official international interest rates					
US Federal Reserve	0 - 0.25	0.25 - 0.50	1.00 - 1.25	1.75 - 2.00	2.75 - 3.00 (2)
Reserve Bank of Australia	2.00	1.75	1.50	1.50	1.50 (2)
Reserve Bank of New Zealand	3.00	2.25	1.75	1.75	1.75 (2)
Bank of England	0.50	0.50	0.25	0.50	0.75 (2)
European Central Bank	0.05	0.00	0.00	0.00	0.00 (2)
People's Bank of China	4.85	4.35	4.35	4.35	4.35 (2)

Source: IMF and reserve banks' publications and information releases.

(1) IMF World Economic Outlook Database (IMF Website)

(2) Westpac Market Outlook 05/10/2018

3.2 DOMESTIC ECONOMY

3.2.1 Policy Developments

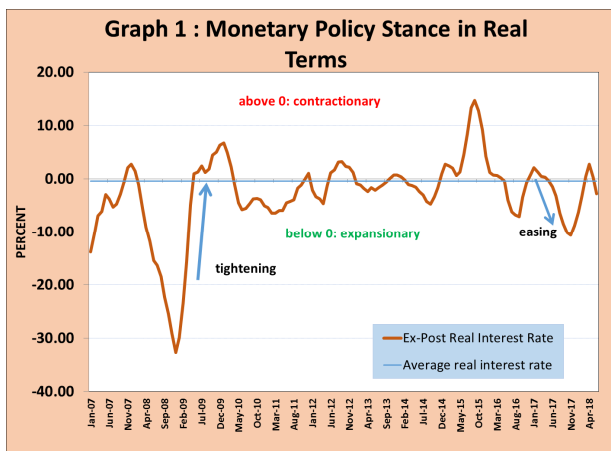
3.2.1.1 Macroeconomic Policy Settings

In line with its medium term target of the Budget deficit to be within 3.5 percent of GDP, the Government continued its fiscal consolidation stance in 2017/18. In actual fact, the budget deficit for the past two years were below 1 percent of GDP signalling the intent of Government to effectively reduce unnecessary spending and create fiscal buffers in the face of more frequent natural disasters. This was broadly achieved by prioritising its expenditure on critically important sectors such as health, education and infrastructure while consolidating its external debt levels and ramping up its revenue collection measures.

With fiscal policy mainly in neutral in terms of total expenditure, monetary policy continued to remain accommodative in order to

achieve economic growth while ensuring low inflation and stable financial system.

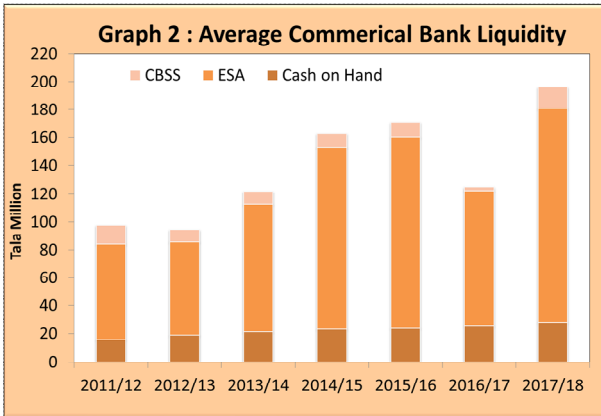
In fact, looking at the conduct of monetary policy since the onset of the global financial crisis (GFC) in 2008, the Central Bank of Samoa has pursued an accommodative or easing monetary policy stance all throughout the past ten years given the many challenges the economy has gone through starting from the GFC, the 2009 tsunami, 2012 Cyclone Evans, 2nd round effects of the GFC, closure of Yazaki and Cyclone Gita in 2018. However, as illustrated in the graph below, despite the easing stance adopted by the CBS, there are periods where monetary policy were in fact, tightening or contractionary due to periods where the hikes in the headline inflation rate managed to offset the low official interest rates levels, which are currently just above 0 percent. This is represented on the graph by the areas where ex-Post Real Interest rate line is above 0, which mostly occurred in 2009, early 2012 and around 2014 and 2015. (See Graph 1.)



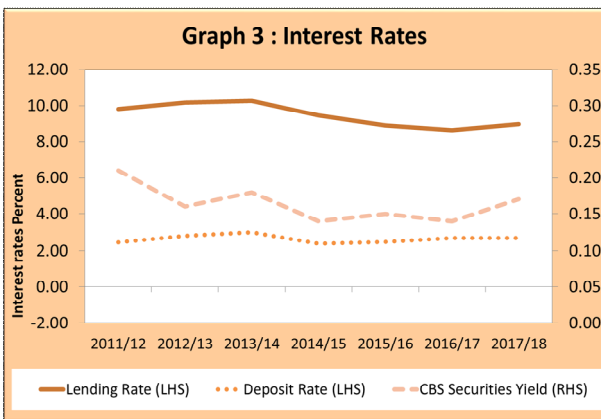
3.2.1.2 Monetary Conditions

Liquidity conditions in the financial system continued to improve further during the year with average commercial banks' excess

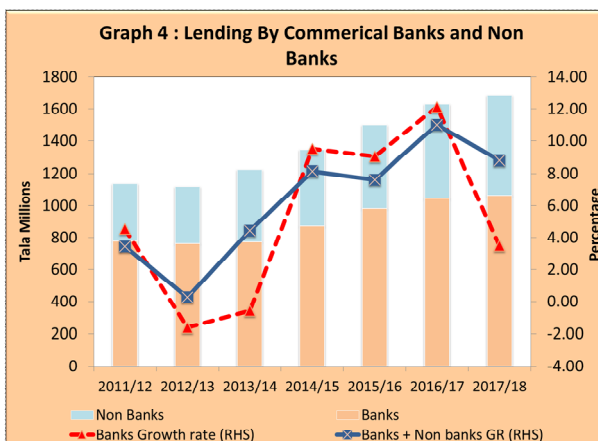
reserves increasing by 56.9 percent to \$196.24 million in 2017/18 from \$125.1 million last year. (See Graph 2.)



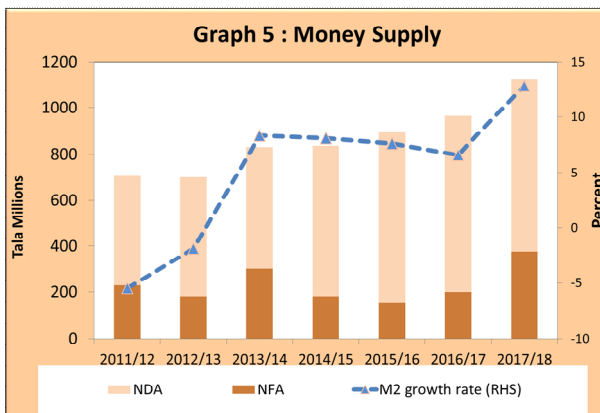
On the whole, CBS’ official interest rate remained low despite a slight increase to 0.17 percent at end June 2018 from 0.14 percent last year in line with its loosening policy stance. Likewise, the commercial banks’ average lending rates rose by 33 basis points to 8.98 percent at end June 2018, from 8.65 percent at end June 2017. However, commercial banks’ deposit rates were unchanged at 2.70 percent from last year. (See Graph 3.)



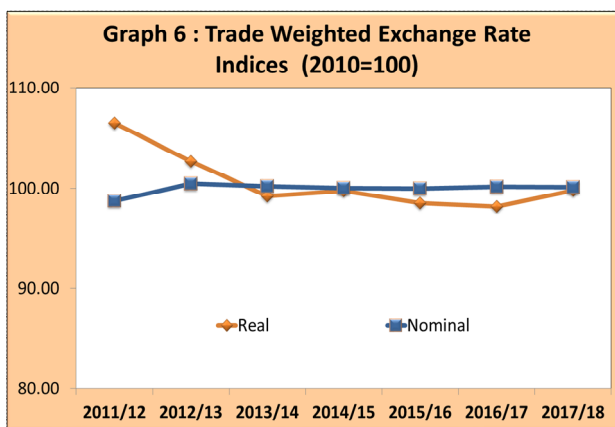
Due to slightly higher lending rates, commercial banks' credit to the private sector and public institutions rose by 1.7 percent to \$1,064.74 million on a point to point basis. But on an annual average basis, the growth rate of commercial bank lending grew by 3.5 percent in 2017/18, slowing down significantly from 12.1 percent in 2016/17. Similarly, total financial system credit, which combines the lending of the four commercial banks with those for the non-bank financial institutions like the Samoa National Provident Fund and Development Bank of Samoa, amounted to \$1,683.1 million, recording an annual growth rate of 5.4 percent at end June 2018 compared to 11.7 percent at end June 2017. (See Graph 4.)



Net foreign assets registered a record increase of 88.6 percent (\$176.6 million) primarily due to a sharp hike of 35.2 percent in Gross foreign reserves and a 44.2 percent decline in foreign liabilities. Despite a 2.3 percent decline in net domestic assets, total broad money supply (M2) grow by 16.5 percent or \$159.2 million on a point to point basis, or around 12.8 percent on an annual average basis, compared to 6.6 percent at end June 2017. (See Graph 5.)



The nominal effective exchange rate (NEER) of the Tala in 2017/18 depreciated marginally by 0.03 percent against the currencies in its exchange rate basket. However, the real effective exchange rate (REER) appreciated by 1.64 percent in the course of the year. (See Graph 6.)



3.3 MACROECONOMIC PERFORMANCE

3.3.1 Real Sector

Following strong growth in 2015/16, economic growth has since slowed down to 2.4 percent in real terms in 2016/17 and now to around 1.0 percent forecast for 2017/18. This slowdown is also

partly compounded by the closure of Yazaki manufacturing, the drop in fishing industry output, completion of the Leone Bridge and road widening project from Vailoa to Vaitele in 2016/17.

As mentioned above, the expected decline in growth to 1.0 percent is mostly attributed to a decline of 27.2 percent reduction in the 'Other Manufacturing' sector given Yazaki Samoa's exit. Likewise, the 'Fishing' sector contracted by 29.7 percent in light of a further decline in fish exports in 2017/18. The 'Financial services' sector decreased by 5.7 percent while the 'Agriculture' dropped by 1.5 percent.

On the other hand, the 'Commerce' sector improved by 3.3 percent while the 'Construction', 'Communications', 'Accommodations & restaurants' and 'Personal & other services' also dropped by 7.8 percent, 12.1 percent, 17.0 percent and 5.6 percent respectively. (See Table 3.)

Table 3
Real Gross Domestic Product by Industry
(At 2009 prices, amounts in Tala Million)

During the period	2014/15	2015/16	2016/17	2017/18	2018/19
	Actual	Actual	Actual	Actual	Forecast
Agriculture	130.3	122.3	144.0	135.1	146.0
Fishing	47.4	69.9	65.3	52.3	43.7
Food & Beverages manufacturi	56.5	63.6	67.0	67.8	70.2
Other manufacturing	100.8	103.4	110.6	75.9	87.8
Construction	180.6	202.8	180.2	200.2	204.9
Electricity and water	73.7	71.6	75.9	78.9	83.7
Commerce	538.5	574.4	613.2	634.8	649.9
Accommodations & Restaurant	28.3	39.1	39.6	45.1	48.8
Transport	75.0	91.7	88.6	84.0	93.3
Communication	75.7	81.7	71.5	80.0	83.8
Public administration	131.4	133.1	131.9	137.9	141.1
Financial services	65.3	68.4	73.1	66.5	76.2
Business services	55.6	50.6	51.8	56.9	56.3
Ownership of dwellings	95.1	95.7	96.3	96.9	97.5
Personal and other service	85.5	95.5	106.0	114.4	105.9
Less: Enterprise share of FISIM	-20.7	-21.7	-23.2	-21.1	-20.7
Total	1,718.9	1,842.1	1,891.9	1,905.6	1,977.0
Annual percent change	1.7%	7.2%	2.7%	0.7%	3.7%
Implicit GDP deflator	113.4	111.6	110.1	116.0	118.3
Annual percent change	2.7%	-1.6%	-1.3%	5.3%	2.2%

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

3.3.2 Balance of payments

For the second year in a row, the balance of payments (bop) recorded a record surplus of \$109.6 million in 2017/18 of which \$106.4 million were due to net transactions and the \$1.2 million net exchange rate valuations gain. This surplus was a combination of large inflows of Government funds, inward private sector investments and strong growth in tourism and remittances markets. (See Table 4.)

Table 4
Balance of Payments (1)
(Amounts in Tala Million)

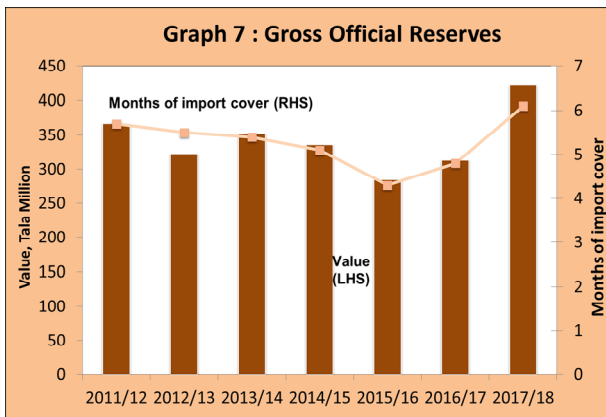
During the period	2014/15	2015/16	2016/17	2017/18	2018/19
	Actual	Actual	Actual	Actual	Forecast
A. Current Account Balance	-52.0	-93.0	-37.4	104.8	1.3
Balance on Trade in Goods	-714.8	-706.4	-686.1	-703.8	-745.4
Exports	67.7	96.5	96.3	94.3	117.6
Imports	782.5	802.9	782.5	798.1	-863.0
Balance on Trade in Services	308.2	316.9	360.1	400.8	351.1
Balance on Primary Income	-38.9	-48.5	-68.0	-74.5	-75.1
Balance on Secondary Income	393.5	344.9	356.7	482.3	470.7
Personal transfers	323.0	322.3	329.3	356.0	473.5
Other transfers	70.5	22.6	27.4	126.2	-2.8
B. Capital Account Balance	86.8	71.1	109.5	119.0	62.1
Capital Transfers	87.6	72.4	113.3	77.0	78.5
Other	-0.9	-1.3	-3.8	42.0	-16.5
C. Net Lending (+)/Net Borrowin	34.8	-21.9	72.1	126.3	63.3
D. Financial Account	-6.8	-82.2	39.2	111.1	98.4
<i>Net Lending (+)/Net Borrowing (-)</i>					
Direct Investment	9.1	24.3	24.2	0.3	0.3
Portfolio Investment	20.7	0.3	14.3	1.1	12.4
Other Investment	41.3	-19.1	-48.2	-51.2	38.9
Reserve Assets	61.6	-42.6	26.7	106.9	13.6
E. Net Errors & omissions	-41.6	-60.2	-32.9	-15.3	-35.1

(1) Based on Balance of Payments Manual 6 format

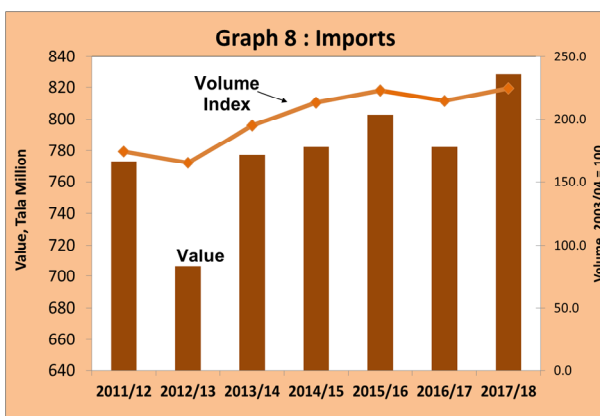
Source: *Central Bank of Samoa*

The current account improved significantly, recording a surplus of \$51.2 million compared to a deficit of \$37.4 million in 2016/17. This surplus was due to sharp gains in the Balance of Trade in 'Services' and Secondary Income net despite increases in balance on Trade of Goods and Primary Income deficits. The increase in the Trade in Goods deficit reflected a strong hike in import payments while the increase in the Trade in Services surplus was due largely to the

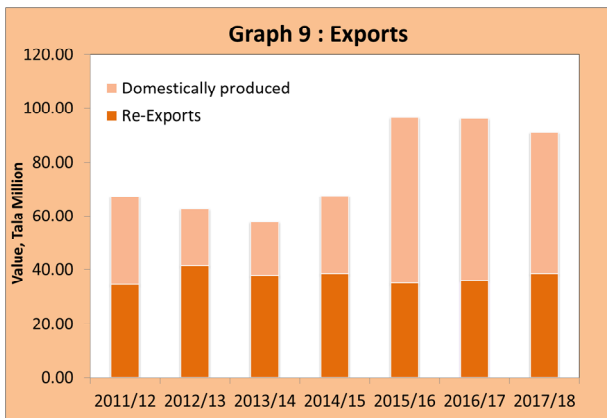
sharp improvement in Travel (visitor) receipt services. As a result, gross foreign reserves rose to \$422.6 million in 2017/18 or equivalent to 6.1 months of imports, up from 4.8 months in 2016/17. (See Graph 7.)



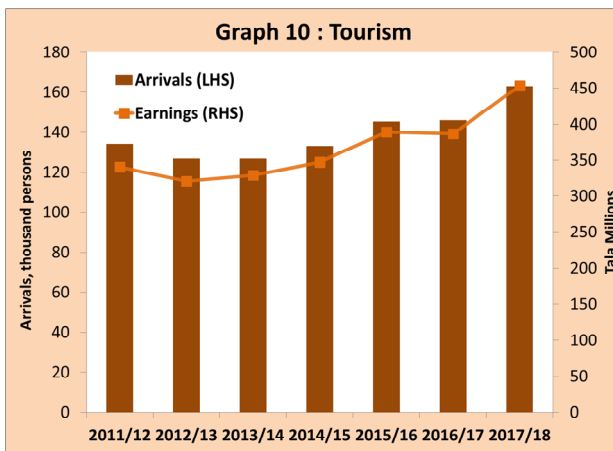
Total import payments rebounded by 5.9 percent (or \$46.3 million) to \$828.8 million in 2017/18, due to expansions of 6.8 percent and 21.1 percent respectively in other private sector imports and petroleum imports although government imports fell by 19.2 percent. (See Graph 8.)



On the other hand, exports decreased by 5.2 percent largely resulting from a 12.2 percent drop in domestically produced exports despite a 6.5 percent hike in re-exports during the year. As a result, the Balance in Trade of Goods deficit widened by 6.1 percent. (See Graph 9.)



Visitor earnings (Travel, credit) leapt by 18.5 percent to \$453.6 million in 2017/18 due to a 11.7 percent hike in the number of visitors coupled with a 6.8 percent increase in the average visitor spending. (See Graph 10.)



Similarly, balance on secondary income net (remittances) shot up by 25.2 percent to \$446.5 million, mainly due to a sharp pickup in funds for non-profit institutions serving households (churches) and for individuals and households.

3.3.3 Prices

The annual headline inflation rate grew to 3.7 percent at end June 2018 from 1.3 percent at end June 2017 as both local and imported inflation increased over the year. On the domestic side, the inflationary pressures created by the aftermath of Cyclone Gita in February 2018 saw local agricultural commodity average prices increase more than twofold. Similarly, the world price of crude oil as well as other commodity prices like imported food, registered strong hikes during the year, which contributed to the further increase in imported inflation in 2017/18. Similarly, the core or underlying inflation rate rose from 1.5 percent at end June 2017 to around 3.7 percent at end June 2018 due to the hike in its imported component especially crude oil and food items. (See Graph 11 and Table 5.)

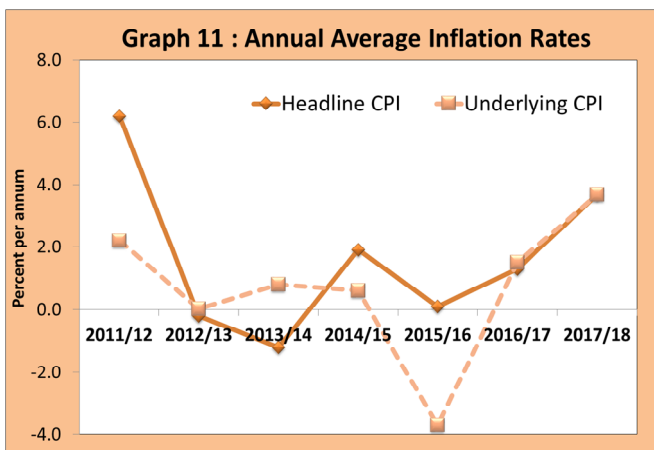


Table 5
Consumer Price Index
(February 2016 = 100)

Fiscal year to end June	2014/15	2015/16	2016/17	2017/18	2018/19
	Actual	Actual	Actual	Actual	Forecast
A. Headline Inflation					
12 months average percent change					
Description					
All Groups	1.9	0.1	1.3	3.7	3.4
Food and Non-Alcoholic Beverages	2.6	3.5	3.2	7.2	5.1
Import Component	-0.8	-6.8	3.2	5.2	5.0
Local Component	4.0	5.0	-0.9	2.1	1.8
B. Underlying Inflation (1)					
12 months average percent change					
Description					
All Groups	0.6	-3.7	1.5	3.7	3.0
Food and Non-Alcoholic Beverages	0.5	-1.9	3.3	5.6	5.0
Import Component	0.4	-5.4	2.3	5.0	4.4
Local Component	1.2	1.5	-0.2	0.7	0.9
Source: Samoa Bureau of Statistics (formerly Statistical Services Division, Ministry of Finance)					
(1) The historical series for this new index started in August 2003.					

4. OUTLOOK FOR 2018/19

4.1 WORLD ECONOMY

While the global economy is expected to continue with its positive economic growth and recovery, recent developments have highlighted less robust activities and uneven expansion than earlier anticipated. The initial IMF World Economic Outlook (WEO) in July 2018 projected a 3.80 percent rebound in global economic activity for 2018/2019. The latest economic growth estimates, however, point to a downward revision to 3.70 percent following elevated downside risks and a less harmonised global expansion. In particular:

- The emerging market and developing economies are projected to grow slower than expected to 4.70 percent compared to the July expectation for a 5.00 percent expansion. This is largely attributed to downward revisions in the emerging and developing European countries, the Middle East, Sub-Saharan Africa as well as Latin America and the Caribbean. China's economy is also expected to slow further as weak external demand growth and the negative effect of recent tariff actions may add more pressure as financial deleveraging efforts continue.
- A 2.25 percent estimated growth for advanced economies, slightly down from the 2.30 percent estimates in July 2018. This lower than expected expansion mainly highlights the weak dynamics out of the European Area and the United Kingdom economies. The continued Brexit negotiations, political uncertainties and debt fears in some of the major European countries will likely strain consumer and business sentiments, while a pullback in global demand will also impact on waning industrial production in the region.

Of Samoa's main trading partner countries:

- The US economy is expected to grow strongly from 2.55 percent in 2017/2018 to 2.70 percent in 2018/2019 as the effects of the fiscal stimulus and a healthy labour market provide for buoyant activity. This is a downward revision from an earlier growth of 2.80 percent for 2018/2019 reflecting the dampening effects from the now full on trade war with China which may impact adversely on consumer spending and business investment, as well as effects from the continued increase in interest rates and inflation.
- According to the Reserve Bank of Australia's recent outlook, the Australian economy is expected to expand just above 3.0 percent, with solid growth anticipated from non-mining business investments, consumption spending and exports (particularly in liquefied natural gas products). However, the uncertainties around China's economic slowdown may also have a bearing on the Australian economy, given their close trading relations.
- The growth of the New Zealand economy, according to the Reserve Bank of New Zealand, is expected to lift in 2019, supported by both fiscal and monetary stimulus as well as higher net exports. Downside risks, however, are also high with the uncertainty from the full extent of the cattle disease (*Mycoplasma bovis*) on the agriculture sector as well as the impact of the international trade tensions, particularly on business confidence given China is also a close trading partner for the Kiwi economy.

Given the current global economic conditions, most monetary authorities have indicated a continued accommodative easing of monetary policies during 2018/2019. The exception to this trend are the US Federal Reserve Bank and the Bank of England, with both central banks already hiking their policy interest rates by 25 basis point each in the September quarter, and the US to continue further in the months ahead. (See Table 2.)

4.2 DOMESTIC ECONOMY

4.2.1 Government Budget

The 2018/19 budget theme is 'The Right Path', which entails that Government be fiscally responsible and disciplined, making the right balance between the current needs of the country and building for the future. The main thrust of the Budget is to focus on improving revenue collection especially on tax compliance while maintaining its investment in education and health of its people. The medium term fiscal budget deficit target remains at its ceiling of 3.5 percent of GDP was achieved in 2017/18 and Government is looking to further reduce that ratio in the coming years. (See Table 6 and Graph 12.)

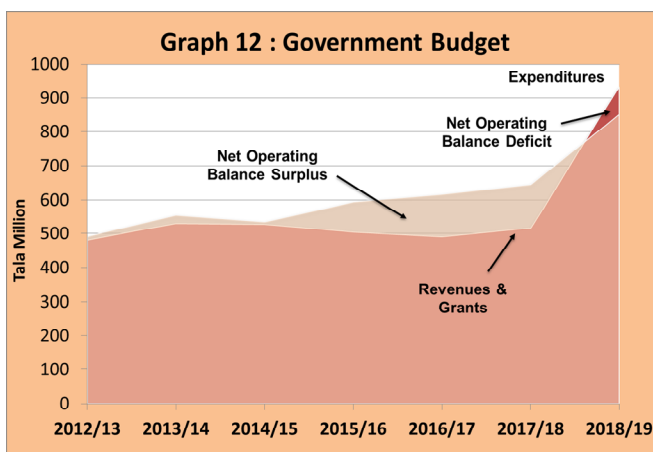


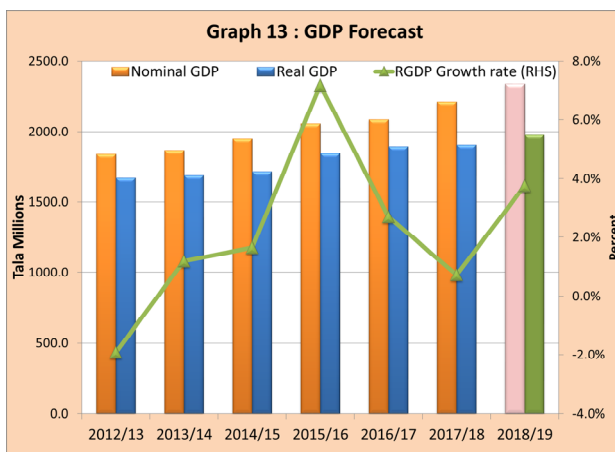
Table 6					
Financial Operations of Government (1) (Amounts in Tala Million)					
During the period	2014/15 Actual	2015/16 Actual	2016/17 Actual	2017/18 Actual	2018/19 Budget
Revenues	534.4	595.6	617.4	645.4	849.5
Taxes	442.0	497.6	517.5	525.8	626.3
Grants	41.2	45.4	40.8	61.1	223.2
Other Revenues	51.2	52.6	59.1	58.4	n/a
Expenses	526.7	503.9	490.5	515.5	932.9
Compensation of employees	154.6	163.5	170.0	194.4	n/a
Use of goods and services	151.7	120.3	112.7	141.9	n/a
Interest	17.9	18.4	17.2	17.3	n/a
Subsidies	17.8	15.1	10.2	5.1	n/a
Grants	165.2	163.6	158.8	135.5	n/a
Social benefits	17.6	17.9	18.1	18.6	n/a
Other expenses	1.8	5.1	3.5	2.6	n/a
Net Operating Balance	7.7	91.7	126.9	129.9	-83.4
BUDGET DEFICIT					
TRANSACTIONS IN					
NONFINANCIAL ASSETS:	83.3	100.1	149.5	128.4	n/a
Net Acquisition of Nonfinancial Assets					
Net lending / borrowing	-75.7	-8.4	-22.5	1.5	-12.9
Net acquisition of financial ass	-35.2	-9.3	-29.3	19.3	n/a
Domestic	-35.2	-9.3	-29.3	19.3	n/a
Net incurrence of liabilities	40.4	-0.8	-6.8	17.8	n/a
Domestic	-4.9	-9.9	-9.5	-9.8	n/a
Foreign	45.3	9.1	2.8	27.6	n/a
<i>(1) GFS Manual 2001 format</i>					
Source: Samoa Bureau of Statistics and Ministry of Finance					

4.2.2 Real Sector

The Samoan economy is expected to improve further by 3.7 percent in 2018/19, up from 0.7 percent recorded for 2017/18. This forecast

recovery reflects current strong growth in remittances and visitor receipts coupled with several large government construction projects and preparations for the Pacific Games in 2019.

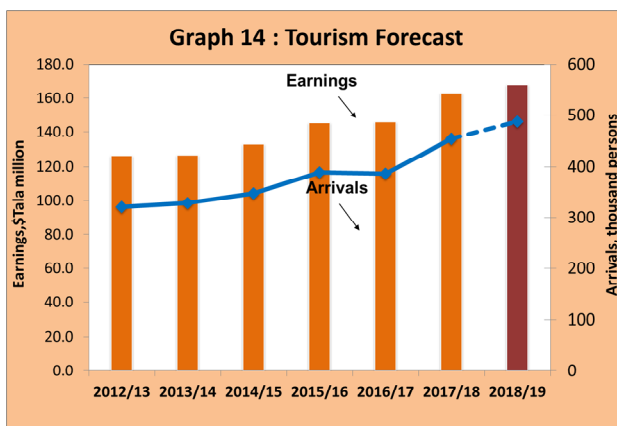
In particular, there are strong growth expected for sectors such as ‘Commerce’ (up 2.6 percent), ‘Construction’ (up 5.5 percent), ‘Transport’ (up 3.5 percent), ‘Financial Services’ (up 10.5 percent), ‘Other Manufacturing’ (up 9.0 percent) and ‘Agriculture’ (up 3.0 percent), in light of various public and private sector projects. Government projects include the construction of the new Prison at Tanumalala, extension of the Vaisigano Bridge, continuation of the airport upgrade, Apia Waterfront developments, road widening project from Saina to Faleolo as well as upgrade of Pacific Games facilities. The spillover effects on consumer demand are expected to boost sectors such as, ‘Finance services’ (up 2.1 percent), ‘Business services’ (up 3.0 percent) and ‘Agriculture’ (up 2.0 percent) amongst many others. (See Graph 13.)

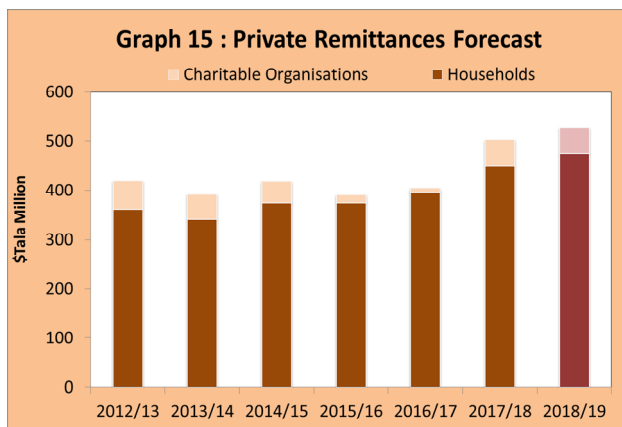


4.2.3 Balance of Payments

For the FY 2018/19, the balance of payments is expected to post a much smaller overall surplus of \$13.6 million from last year’s record surplus of \$109.8 million. This net inflow of foreign reserves is

mainly underpinned by smaller expected surplus in the current account of \$23.8 million from \$41.2 million in the previous year. The lower surplus in the current account reflects expected increase in capital inflows from both private sector investments into Samoa and government grants, as well as increase in foreign investments by our financial institutions abroad. The deficit in the balance in trade in goods is expected to expand slightly by 1 percent while the surplus on the Trade in Services is expected to decline also by 1 percent. The drop in the latter is despite an expected hike in **visitor earnings (travel credit)** by 7.5 percent in line with increased airlines seat capacity and frequency of flights to Samoa together with cheaper airfares. **Remittances** are expected to grow further by 5.1 percent in line with strong growth experienced in 2017/18. (See Graph 14 and Graph 15.) **Total exports** are expected to rebound by 5.4 percent due to modest increases in domestic export products such as fish, coconut oil, beer, taro and nonu juice. Also, **imports** are estimated to growth further by 4.1 percent to \$863.0 million due to an expected hike in private sector and petroleum imports as global commodity prices are forecast to increase in the next 12 months as the global economy grows. As a result, gross foreign reserves are forecast to increase to around \$436.2 million at end June 2019 or equivalent to 6.1 months of imports.





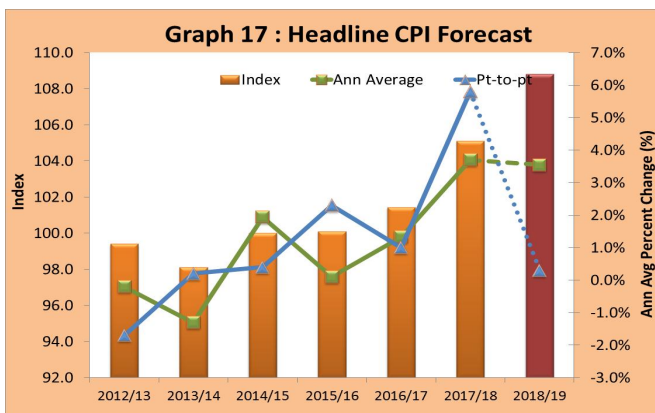
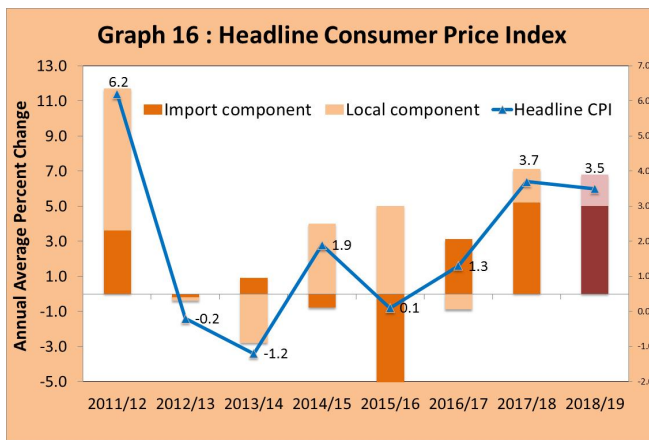
4.2.4 Prices

Inflationary pressures remain elevated in the first few months of 2018/19 as the aftermath of Cyclone Gita is still being felt on local agricultural prices although it is on the decline. Also, global commodity prices on the whole are picking up especially international oil prices around the world.

4.2.4.1 Headline Inflation

Local agricultural production and supply is expected to pick up to its pre-cyclone levels in 2018/19 especially for crops such as taro, coconut, banana and most vegetable items. However, downside risks of another devastating cyclone as well as the threat of the US-China trade war remains a threat to inflation forecasts.

As a result, **imported inflation** is expected to drop to 5.0 percent from 5.2 percent as various imported prices like clothing and household items are expected to drop during the year. Similarly, **domestic inflation** is expected to decrease to 1.8 percent in 2018/19 as elevated prices from the cyclone gradually starts to return to normal levels. As a result, **the annual average headline inflation** is forecast to decline to 3.5 percent from 3.7 percent in the previous fiscal year. (See Graph 16 and Graph 17.)



4.2.4.2 Underlying Inflation

The underlying inflation rate is also expected to weaken in line with drop in imported inflation, falling to 3.3 percent by end June 2019 from 3.7 percent last year.

4.2.5 Monetary Aggregates

Looking at the outlook of the monetary system, commercial banks' credit to the private sector and public institutions is expected to hasten to around 4.1 percent at end June 2019, up from 3.5 percent in 2017/18. On the other hand, the annual growth rate of M2 is

expected to slow to around 3.7 percent at end June 2019 from 12.8 percent at end June 2018 as net foreign assets is expected to return to normal levels from substantially high levels in 2017/18. (See Table 7.)

Table 7						
Monetary Survey						
(Amounts in Tala million)						
End of Period	2013/14	2014/15	2015/16	2016/17	2017/18	Forecast 2018/19
A. Determinants of Money Supply						
Net Foreign Assets	301.2	180.5	150.2	199.3	375.8	256.8
Net Domestic Assets	530.4	655.7	745.0	766.0	748.6	864.6
Net Credit to Non-financial Public Sector	-101.1	-79.7	-96.3	-156.5	-185.1	-158.9
Credit to private sector	734.2	827.2	940.0	1,022.2	1,014.6	1,093.3
Net Credit to Non-monetary Financial Instit	87.6	109.8	110.8	113.2	135.2	135.4
Others, net	12.8	25.7	33.9	21.9	43.9	57.4
B. Money Supply (M2)						
Narrow Money	831.6	836.2	895.3	965.2	1,124.4	1,121.5
Currency Outside banks	380.2	356.2	394.2	405.5	499.3	487.7
Transferable Deposits	46.2	49.5	61.4	67.0	75.2	76.6
Demand Deposits	334.0	306.8	332.8	338.5	424.1	411.0
Foreign Currency Deposits of Residents	217.4	250.3	275.8	270.8	353.4	337.5
Quasi-money	116.6	56.4	57.0	67.6	70.7	73.5
Other Deposits	451.4	480.0	501.1	559.7	625.1	633.8
Savings Deposits	451.4	480.0	501.1	559.7	625.1	633.8
Time Deposits	106.5	122.0	129.5	132.7	139.9	152.0
Time Deposits	344.9	357.9	371.5	427.0	485.2	481.8
Source: Central Bank of Samoa						

5. MONETARY POLICY STANCE FOR 2018/2019

To recap, headline inflation is expected to ease slightly in 2018/19 to around 3.5 percent from 4.6 percent at end September 2018 and 3.7 percent at end June 2018. Real GDP growth is expected to recover by 3.7 percent in light of current strong growth in remittances and visitor receipts as well as ongoing construction projects like the Apia Waterfront, Vaisigano bridge, road widening project to Faleolo and other planned works mentioned earlier. Foreign reserves are expected to remain high at 6.1 months of imports and foreign exchange earnings from exports of goods, tourism and remittances are forecast to growth further in 2018/19.

However, there are downside risks to these forecasts and outlook, with early meteorological forecasts expecting around 3 possible cyclones or strong winds that could affect the country.

Given the current hike in headline inflation rate is expected to be temporary and it will come back down to its medium term target of 3.0 percent, the primary objective of ensuring and maintaining price stability is expected to be maintained in 2018/19 while the economy is expected to rebound. The Central Bank of Samoa will continue to pursue an easing or loosening monetary policy stance in 2018/19 to foster economic growth (its third main objective) while at the same time ensure the soundness of its financial system through prudential and financial supervision compliance.

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