I. GOVERNOR'S FORWARD

The twelve months to December 2003 was a challenging time for the Reserve Bank of Vanuatu (RBV). During this time I was appointed in April as the sixth Governor of the RBV. The RBV faced many challenges especially with regard to changes in the international economic conditions that impact on the earnings of the Bank and international requirements to increase banking supervision standards; liquidity issues in the banking system; and the RBV's financing of the Government's deficits via the overdraft facility which impacted on the monetary policy adopted by the Bank. The RBV faced these challenges well.

In 2003 we can see that it is an interesting year for the Vanuatu economy. It recorded a positive growth after two previous years of economic downturn. This growth was mostly attributable to the improvements in the agricultural and tourism sectors. The improvements in the agricultural sector was attributable to a number of factors, mainly, a growing involvement of the private sector in cocoa and copra industries, an increase in world prices for cocoa and coconut oil and good weather conditions.

Annual inflation in 2003 was 3.5 percent in the third quarter and declined to 2.9 percent at the close of 2003. This was below the 4 percent maximum comfort threshold set by the RBV. This pleasing result was largely achieved by sound monetary and exchange rate policies pursued by the RBV.

In May 2003, the Vanuatu Commodities Marketing Board (VCMB) became a regulator and the exports of primary commodities were now left to the private sector to undertake. This means that the foreign exchange receipts that were coming from the VCMB through the RBV stopped and is now channeled through the market. This development has affected the level of official foreign exchange reserves at the RBV. Official foreign reserves declined and as a result the Bank tightened its foreign exchange guideline. With this measure the official reserves was stabilised at 4.4 months of import cover. The RBV viewed this import cover as relatively stable, as it is above its 4 months threshold.

Monetary policy stance remained unchanged as the discount rate continued to be at 6.5 percent. This was mainly attributable to the fragile nature of economic growth and official reserves, and untenable monetary conditions resulting mainly from Government borrowings to RBV to finance its deficits. This Monetary policy stance is reviewed twice a year and in 2003 was undertaken in June and November and was approved by the Board of Directors.

With the passage of the International Banking Act, the RBV took on responsibility for the supervision of Vanuatu's offshore banks in addition to its supervisory responsibility for Vanuatu's domestic banks. Prudential guidelines and statistical returns were developed for offshore banks and, with the new legislation existing licensees were required to apply for a license under the International Banking Act. Staff assessed applications from 11 applicants and nine licenses were issued by 31 December 2003. The RBV is now also responsible for the supervision of the Vanuatu National Provident Fund and discussions have commenced with the Fund on the implementation of the new supervisory arrangements. The Bank also continued its normal range of supervisory activities and during 2003 undertook on-site inspections to review domestic banks' anti-money laundering policies and procedures.

On the financial performance of the RBV, I am pleased to report an operating profit of VT36.6 million in 2003. The performance is a reflection of a number of factors such as extremely low levels of global interest rates during the year, as over 70 percent of the reserves are invested offshore and the continuing expansion of the activities of the RBV. The RBV will provide VT38.4 million to the Government, which constitutes 90 percent of profit to be transferred to Government and a transfer from revaluation reserve of VT5.4 million, as required by the RBV Act.

Shortly after taking office, the RBV Board and Management were committed to see policy reviews at the RBV. As a result, a manual was developed and adopted. This was accompanied with other policies focusing on the areas of training, security, loan and housing. In addition to these, a Banks budget was formulated and a currency review was undertaken. Both were undertaken for the first time. These policies and reviews were subsequently approved by the RBV's Board of Directors.

As part of the RBV's objective to improve transparency, an official website was launched for the first time during the year. This website contains information on the role and activities of the RBV and will be useful for the public, bankers, investors and students who are interested to know about the RBV and its role in the economy.

The above achievements will carry on to 2004. The Bank will continue to focus its objectives on maintaining a stable financial environment, ensuring a sufficient foreign reserves and a strong financial system. To attain these objectives effectively and efficiently in 2004, a strategic plan will be developed which will also contained the RBV's vision and mission statements and also a review of the RBV will be undertaken which will see a major internal re-organisation of the Bank and a revamped role of the management and Board.

I would like to take this opportunity to thank the Board of Directors for their support and guidance through out the year. Finally, I would also like to extend my deep appreciation to the management and staff for their continual support and effort during the year.

Odo Tevi
Governor and Chairman of the Board

II. THE YEAR IN BRIEF

NO.	BRIEF OUTLINE OF MONETARY CONDITIONS AND POLICY DURING 2003	EFFECTIVE DATE
1.	Vanuatu Commodities Marketing Board, or VCMB, began issuing licenses for private individuals to trade in cocoa and copra, the main export commodities and the principal source of official foreign reserves of the RBV. The decision by the Government had an impact on the level of official foreign reserves throughout 2003.	January 2003
2.	The Vanuatu's Council of Ministers agreed for Vanuatu's commitment to the OECD Harmful Tax competition Initiative which includes requests that: • Vanuatu must be removed from OECD's blacklist of non-compliant countries; • All OECD member states must not apply defensive measures against Vanuatu; • Vanuatu must be compensated for its lost revenue as a result of its commitment to OECD; • The sovereignty of Vanuatu must always be recognized and upheld while negotiating with OECD; • Vanuatu must participate in global forums to express its views on issues that are of importance to its economy and people; • Help must be given when requested to enable Vanuatu to make necessary changes to its laws.	April 2003
3.	The term of Mr. Andrew Kausiama, Governor of the Reserve Bank of Vanuatu ended in April 2003. Mr. Andrew Kausiama served as Governor of the Bank for the period of five years. During this period, he successfully steered the Bank through a number of challenges and was instrumental in the Bank's adoption of more market oriented monetary control. Mr. Kausiama is succeeded by Mr. Odo Tevi a former Principal Economist with the Ministry of Finance. Mr. Tevi holds a Master Degree in Economics and Development Studies from Sussex University, UK.	April 2003
4.	Revocation of Licence Regulation order No. 16 of 2003 came into effect, requiring the Reserve Bank not to revoke a licence unless a licensee that has made or makes a request under paragraph 11(1)(d) of the International Banking Act No.4 of 2002 to provide satisfactory evidence of all of the following to the Reserve Bank: • The licensee has repaid all deposits of money to	May 2003

depositors;
- The licensee has discharged all liabilities to creditors;
- The licensee has made arrangements to transfer or transferred all assets held or administered by it on behalf of other persons to those persons or other persons;
- The licensee has ceased to carry on all forms of international banking business from Vanuatu.

Until a licensee complies with the above, the Reserve Bank must not decide whether or not to revoke a license. This regulation applies not only to a licensee that makes request under paragraph 11(1)(d) of the International Banking Act No.4 of 2002 on or after the commencement of this Regulation but also applies to a licensee that made a request before this Regulation commenced.

5. The Board of Directors of the Reserve Bank of Vanuatu in its meeting in June approved the Monetary Policy stance of the Bank. The Board decided to maintain the official interest rate at 6.5 percent. June 2003

6. The enforcement of the Debit Tax became effective on 1st July 2003. Debit tax is a tax charged on any debit transaction (withdrawal of money) from any commercial banks. The new tax system was based on an Australian tax system. July 2003

7. The launching of the Reserve Bank of Vanuatu website. The website (http://www.rbv.gov.vu), aims to facilitate the accessibility of information in relation to the Bank's main activities. August 2003

8. The Reserve Bank of Vanuatu introduced International Bank Prudential Guideline 11 – **Physical Presence of Licensees and Employees in Vanuatu**. Under the International Banking Act No 4 of 2002, international banks are required to maintain a physical presence and have management in Vanuatu. The Guideline provides an interpretation of the requirements of Section 20 of the Act. The guideline can be found on the Bank's website. September 2003

9. The Bank undertook a review of its currency operations. Mr. John Howard, a former General Manager of the Reserve Bank of Vanuatu, was hired by the Bank to carry out the review. The Term of Reference (TOR), as approved by the Board, focused on appraising the daily currency operations including working relationship with banks, current denominations of both notes and coins in terms of production costs, monetary value, life and public acceptance. October 2003

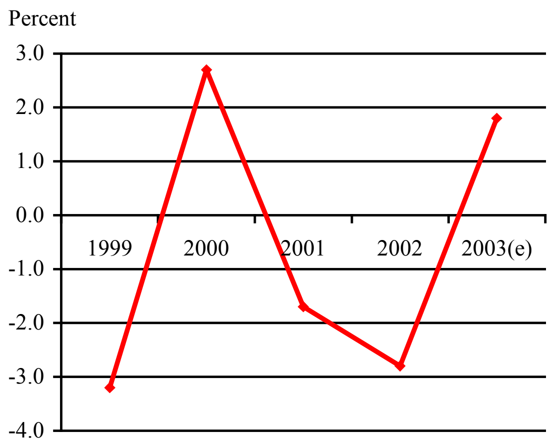
An assessment of the currency security features taking into account the counterfeiting experience was also included and other topics covered in the review scope were the human resource capacity and development of numismatic currency.

10.	The Board of Directors of the Bank met and approved the Monetary Policy stance of the Bank. The official interest rate was maintained unchanged at 6.5 percent.	November 2003
11.	The Reserve Bank of Vanuatu authorized Vianka Bank Limited to operate as an international bank under the provisions of the International banking Act. No. 4 of 2002. Vianka Bank is the first international bank licensed under the new arrangements and its license is effective from January 1 2004. Vianka Bank Limited was previously licensed to operate as an international bank under the Banking Act [CAP 63]. With the introduction of new legislation and supervisory arrangements, all offshore banks were required to re-apply for a license under the international Banking Act in August 2003. Vianka Bank was one of ten banks to re-apply for a license under the new arrangements and the bank's senior management worked closely with staff of the Reserve Bank during the assessment of the application.	December 2003
12.	Bank Supervision Policy Guideline 3 – Supervision of the Adequacy of Liquidity of Banks – requires domestic banks to meet a minimum Liquid Asset Requirement (LAR). The purpose of the LAR is that each bank holds a stock of cashable, undoubted assets, which, with the Reserve Bank's approval can be quickly converted into cash in extreme circumstances. Such stock is additional to the liquid assets which each bank needs for management of its day-to-day liquidity needs. Banks are expected to meet the LAR at all times. The Reserve Bank is thinking of reviewing the LAR ratio in the future.	December 2003

III. MONETARY POLICY FORMULATION

The monetary objectives of the Reserve Bank are price stability and the maintenance of adequate level of reserves to meet Vanuatu's external obligations. The Reserve Bank considers an annual growth rate of inflation above 4 percent as the maximum threshold and 4 months of import cover as the minimum comfort level.

Chart 1. Real GDP

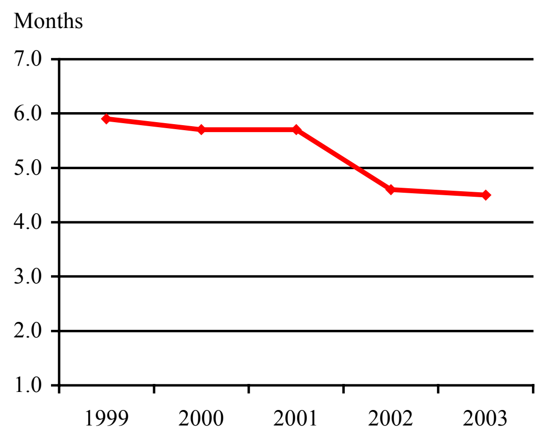


At the start of 2003, monetary policy was conducted against a backdrop of global and economic weaknesses. The Reserve Bank had anticipated weak economic growth following two years of sub-par growth and inflation of about 2.5 percent. As it turned out, the estimate of GDP at the end of the year improved to 1.8 percent and actual annual inflation turned out to be 2.9 percent.

Against this initial weakening, official reserves fell to 4.4 months of import cover at the beginning of 2003. The situation was compounded by the Government decision to award exports of the country's important commodities, copra and cocoa, to private undertakings from the Vanuatu Commodities Marketing Board (VCMB). As a result, the Reserve Bank of Vanuatu tightened its foreign exchange guideline on the minimum dealing amount of U.S. Dollars 250,000 per importer imposed in 2001, and sought to either spread out the payment of foreign exchange that meet the requirement, and/or to only meet part of the request.

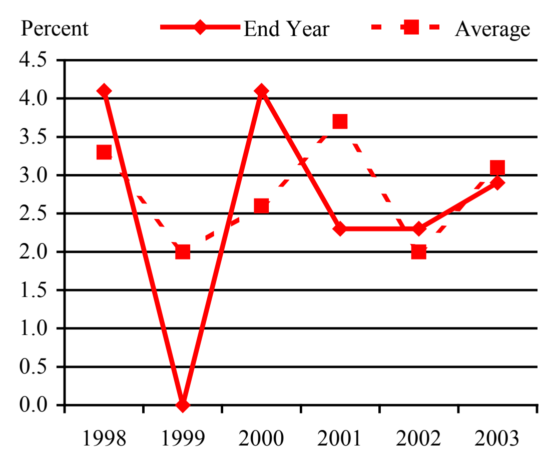
The RBV continued to meet fully the Government's foreign exchange requirements to meet external debt obligations and other Government foreign exchange transactions. As a result of this tightening, official reserves rose to 4.5 months of import cover at the end of the year. In addition, the level of official reserves began to stabilize towards the latter half of 2003 and the Bank's crisis indicator, depicting the ratio of official reserves to Broad Money, showed some improvements in December 2003.

Chart 2: Official Reserves in Months of Import Cover



The economy began to strengthen in the second half of 2003 however, monetary development continued to be untenable. While overall money growth and net credit to the Government showed deceleration, there was a large deterioration in the net position of the Government with the central bank, leading to pressures on liquidity and interest rates through out 2003. Excess liquidity declined to low levels towards the end of 2003 reflecting a number of factors including liquidity destruction on behalf of the government, seasonal movements and liquidity management of banks, which exerted pressure on bank lending rates. As a result open market operation activities were lower in 2003 in line with the decline of the settlement balances of commercial banks at the Reserve Bank.

Chart 3: Inflation



The policy rate of the RBV was left unchanged at 6.5 percent at the close of the year after a review undertaken in June and November, in view of the fragile nature of growth and official reserves, and untenable monetary conditions. Although annual inflation rose to 3.5 percent in the third quarter it decelerated to 2.9 percent at the close of 2003, well below the 4.0 percent maximum comfort threshold of the RBV.

The Bank continued to advise the Government on the need to persist with improving fiscal policy.

III.1 ECONOMIC OVERVIEW

Economic activity in 2003 recovered from previous years of economic contraction. However, growth has concentrated mainly in the agricultural sector but may extend to the services sector from current and anticipated improvements in the tourism sector. In reflection of this sudden upswing, a number of upward growth revisions were made mostly in the second half of 2003, from initially negative growth at the beginning, to growth estimate of 1.8 percent towards the end of the year.

While Broad Money (M4) contracted by 0.8 percent over the year, the current account deficit of the balance of payments also deteriorated, a development that conformed to the rise in Narrow Money rather than Broad Money growth. Movements in the latter can be driven by activities of the finance centre. In line with this external development, a fiscal deficit, currently estimated to be around 1.8 percent of projected GDP, emerged in 2003 and financed by domestic borrowing, principally through central bank borrowing, roll-over of maturing government securities and decline in government deposits. This development is not reflected in the banking system's net credit to the Government. On the contrary, the government's net lending position with banks improved substantially, but the improvement reflected the maturing of VNPF related government securities held by banks and the shift of government security holdings from the banking system to the captive market. The Government position with the Reserve Bank however deteriorated significantly, a development that exerted pressure on both liquidity creation and the stance of monetary policy throughout 2003.

Broadly however, macroeconomic stability was maintained and at the end of December 2003, official international reserves amounted to 4.5 months of import cover.

III. 2 WORLD ECONOMIC DEVELOPMENTS

The year 2003 saw a marked strengthening of world economic recovery from the recession in 2001 with much of the improvement taking place in the second half of the year. Led by the United States and China, practically most of the major economies including the Euro zone, Japan and other Asian countries experienced pick up in economic activities compared to 2002.

The improvement was driven by accommodative monetary and fiscal policies, especially in the United States over the past years. Furthermore, the improving financial environment and mounting business and consumer confidence are applying positive weight to global growth.

Table 1: World Economic Indicators

	2001	2002	2003 f
World Output	2.4	3.0	3.2
Advanced countries	1.0	1.8	1.8
Developing countries	4.1	4.6	5.0
US	0.3	2.4	2.6
Australia	2.6	4.4	2.6
New Zealand	2.7	3.6	3.0
World Trade (Volume)	0.1	3.2	2.9
Imports (Advan Count)	-1.0	2.2	2.8
Exports (Devel Count)	-0.8	2.2	1.6
Commod. Prices (USD)			
Oil	-14.0	2.8	14.2
Non-fuel	-4.0	0.6	5.0

f forecast
Source: World Economic Outlook, IMF Sept 2003.

Since a recession in 2001, economic recovery in the US became prominent in the second half of 2003. Real GDP grew at an annual rate of 8.2 percent in the third quarter, boosted by a surge in consumer spending and business fixed investment. Fourth quarter GDP data grew at a year-on-year rate of 4.0 percent. Although this is roughly half of the preceding quarter's growth, it showed that the US economic recovery has gathered significant momentum. Recent estimates by the IMF indicate further output expansion of 3.9 percent in 2004.

The Euro area witnessed a mild turnaround in the second half of 2003, following three quarters of economic decline. Third quarter GDP rose from last year by 0.3 percent, underpinned by external demand whereas domestic demand remained weak due to frail household consumption and declining investment spending. The outlook remains positive with exports likely to be boosted by stronger economic growths in trading partner countries, especially the US and China. However, the recent sharp appreciation of the Euro against the US dollar has led to concerns about its dampening effect on growth prospects. The IMF has forecast economic growth in the Euro area during 2004 to increase to 1.9 percent.

The Japanese economy continued successive growths over the past six to seven months, albeit a slow pace annual rate of 1.8 percent in the third quarter, sourced mainly from rising exports. Advanced estimates revealed an annual growth rate of 6.4 percent in the fourth quarter of 2003, the fastest growth in more than 13 years. Rising external demand as well as stronger than expected domestic demand, resulting from increasing consumer and business spending, were driving the economy in the fourth quarter.

In Australia, economic activity picked up in the second half of 2003 and continued momentum into the fourth quarter in line with global economic recovery. High consumer spending and consumer confidence fuelled by rising employment, higher wages, surging house prices and a stronger stock market and increased borrowing have been the drivers of growth in 2003. The outlook for the economy appears good with the drought now over and improvement in international economic conditions will gradually improve the country's export earnings.

In New Zealand, the economy grew at an annual rate of 3.2 percent in 2003. Sturdy domestic demand was the main factor behind the strength of the economy. On the other hand, net exports remained weak and has been a drag on economic growth. Nevertheless, reflecting the strength of the economy, unemployment declined by 4.4 percent.

World inflation continues to remain at historical low level. The IMF, in its September 2003 World Economic Outlook, projected the advanced countries' inflation at below 2.0 percent and developing countries at around 5.0 percent.

The effect of world economic developments on the Vanuatu economy were:

(i) the strengthening of world economic growth had positive impact on the domestic economic recovery. World economic recovery and strengthening consumer and business sentiments led to rising world demand and contributed to improved world prices for commodities relevant for Vanuatu's exports, in particular world copra prices;

(ii) Subdue world inflationary pressures assisted in keeping the pressure on domestic inflation from high import prices low despite the level of world petroleum prices and sharp movements in exchange rates of major trading partner currencies;

(iii) the sharp appreciation of the Australian and New Zealand dollars led to some improvement in tourism and export competitiveness although this came at some cost to domestic inflation towards end-2003. The overall effect of exchange rate movements on domestic inflation in 2003 was kept low because of the high share of US dollar in imports and the relatively high depreciation of the currency against the Vatu.

III.3 DOMESTIC ACTIVITY

The Research Department is responsible for advice on policy formulation and analysis of domestic and external conditions and disseminates the information through the Bank's various publications, policy statements and policy advice in accordance with the Act of the Reserve Bank of Vanuatu.

1 REAL SECTOR DEVELOPMENT

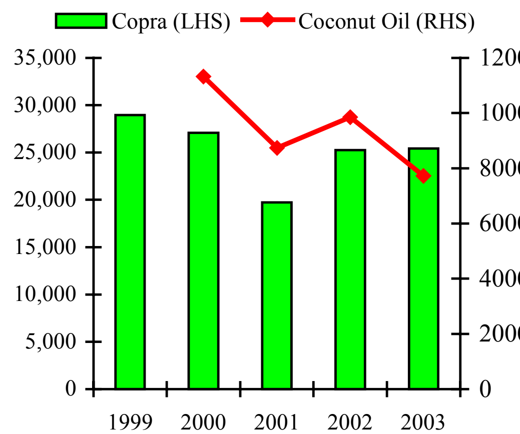
1.1 Output and Production

The current estimate, with partial indicators to December, indicates that the economy grew in real terms by 1.8 percent in 2003 compared to a negative growth of –2.8 percent in 2002. A complete assessment of GDP growth in 2003 is yet to be finalised. While this is considered a conservative estimate, business perception of economic activity was not as upbeat for most of 2003.

The growth was largely driven by improvements in the agriculture sector and property land development, although much of the increase in economic activity occurred in the second half of the year. Developments in the latter partly reflect current real estate development in neighbouring Australia and New Zealand.

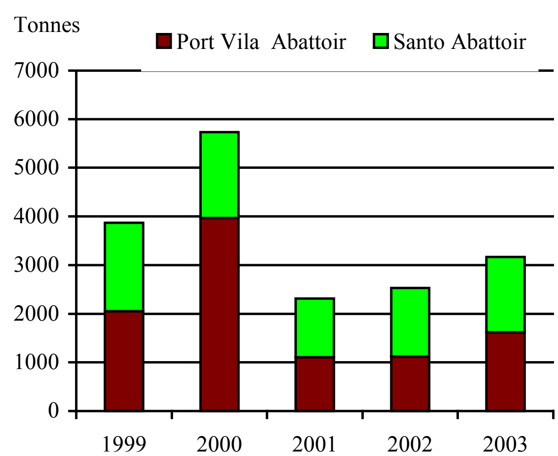
Growth in the agricultural sector of 8.7 percent, had much to do with greater private sector involvement in the trade of copra and cocoa, general improvement in the world prices for cocoa and coconut oil, the development of new markets for organic beef and favourable weather conditions that allowed the increased harvest of logs for harvesting. The improvement in the Agriculture Sector reflects improved copra, cocoa, beef and timber production. Copra production improved slightly by 0.6 percent from the 2002, although it was lower in the first half than the same period in 2002, while processed coconut oil exports fell to lower levels. World copra prices rose substantially towards the end of 2003.

Chart 4: Copra and Coconut Oils Exports (tonnes)



Cocoa production rose by a substantial 32.7 percent from 2002. The sector was affected by past cyclones and showed supply response to private initiatives in the purchase of organic cocoa from farmers.

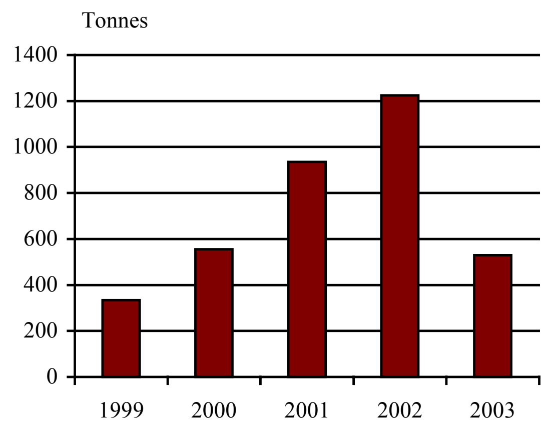
Chart 5: Beef Production



Beef production rose by 25.1 percent, boosted by the opening of the Australian organic beef market. The depreciation of Vatu against the Australian dollar was an added factor for this particular market.

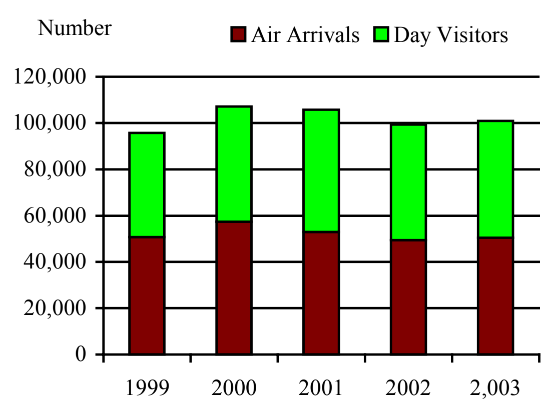
The kava sector in 2003 had encountered a less than average output, primarily due to subdued markets in Europe and the United States of America. Kava exports fell by 50 percent from the level of 2002. Export prices also declined by approximately 10 percent.

Chart 6: Kava Production for Exports



The services sector was estimated to have improved by 0.6 percent in 2003. Within the services sector, there was a 1.3 percent increase in the level of visitor arrivals to 100,830, from 99,488 in 2002.

Chart 7: Visitor Arrivals



The increase in the second half followed seasonal trends and the sharp depreciation of the Vatu against the Australian Dollar during that period. Cruise ship arrivals also rose towards the end of 2003 due to an additional cruise ship in November.

The current estimates show that the industry sector continues to under perform and has been stagnant for a long period.

1.2 Inflation

The annual rate of inflation rose to 2.9 percent from 2.3 percent in 2002. Inflation was largely affected by import duty increases in food items and the appreciation of the Australian dollar.

The effect of the exchange rate on the general price level depends to some extent on the share of goods and services imported from Vanuatu's trading partners. On this basis, despite the effect of the appreciation of the Australian dollar on the price of important food items such as rice, the price effect of the exchange rate was contained somewhat by the high share of the US dollar in imports and the relatively high depreciation of the currency against the Vatu.

Most items in the CPI basket remained almost static from the previous year in reflection of sluggishness in the economy. Increases in import duties were placed on certain items covered by the Melanesian Spearhead Group trade agreement such as canned beef.

2 FISCAL OPERATIONS

The central government balanced budget amounted to VT7,231.1 million in 2003 but preliminary indications point to a deficit of VT624 million, equivalent to 1.8 percent of estimated GDP. This level is lower than the 2002 deficit in both absolute terms (VT 1328.1 million), and relative to GDP (4.0%).

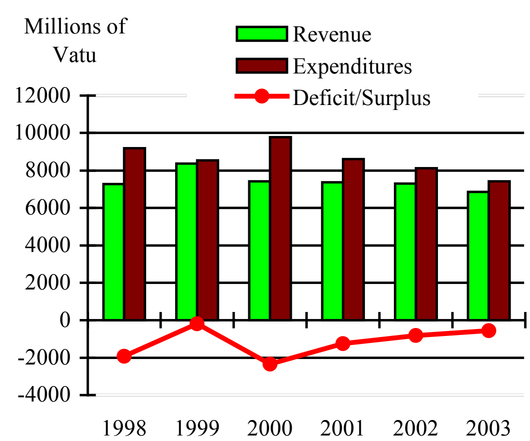
The new revenue measures in the light of this development reflect continuing tight fiscal expenditure management controls and the introduction of the Debit Tax on bank transactions and increase in excise. The introduction of the Debit Tax was undertaken in the middle of 2003 and took the place of another tax and its impact on revenue was therefore minimal.

Table 2: Fiscal Operations of the Central Government (millions of vatu).

	2002	Budget 2003	2003 Prelim
Receipts			
VAT	2242.5	2295.1	2356.8
I. Duties	2276.1	2524.5	2283.5
B. Licenses	141.4	140.8	124.6
Turnover	117.0	116.9	97.9
Excise	85.7	461.0	322.7
Other taxes	912.6	946.2	839.1
Non tax	682.9	723.7	655.7
Grants	727.9	550.0	381.4
Total	**7082.1**	**7758.2**	**7058.3**
Expenditure			
Goods	5834.2	5752.2	5683.0
Salary	3929.2	4077.9	4072.3
Interest	318.6	308.2	352.6
Subsidies	1003.9	1131.0	1118.0
Assets	73.0	39.6	85.8
NR Transfers	458.3	0.0	0.0
Development	722.1	375.0	442.8
Total	**8410.2**	**7606.1**	**7682.3**
Def/Surplus	**-1328.1**	**152.1**	**-624.0**
Financing			
T. Rev. & Grts	7082.1	7758.2	7058.3
T. Exp. & NL	8410.2	7606.1	7682.3
Def/Surplus	**-1328.1**	**152.1**	**-624.0**
Ext. Finance	0.0	0.0	0.0
Dom. Finance	1328.1	0.0	624.0
T. Finance	**1328.1**	**0.0**	**624.0**

Recurrent revenue collected for the 12 months accounts for 92.3 percent from the budget. This shortfall occurred mainly due to a general decline in tax and non-tax revenue.

Chart 8: Government Expenditures and Revenue.



There was a general decrease in total expenditures of VT715.1 million (8.8 percent) as compared to the same period of 2002. This decline is due principally to decreases of 2.0 percent in good and services, 21.1 percent in subsidies and transfers and 20.3 percent in development expenditure. However, there was an increase of 15.3 percent in interest payments on both domestic and external debts.

2.1 Financing

The initial estimate of the budget deficit of 1.8 percent of estimated GDP was financed by domestic borrowing, mostly from the central bank and the captive market and decline in government deposits at the central bank.

Domestic borrowing took the form of rollover of maturing long-term government securities. Of the total amount of VT1,284.2 million that matured in 2003, only VT 248.1 million were retired and the rest were rolled-over.

Chart 9: Net Claims on Government Versus Excess Liquidity

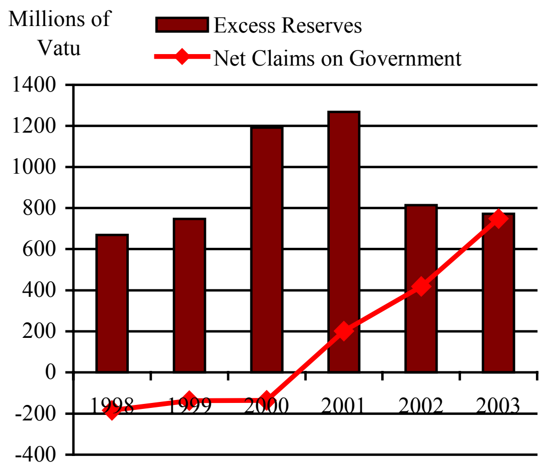
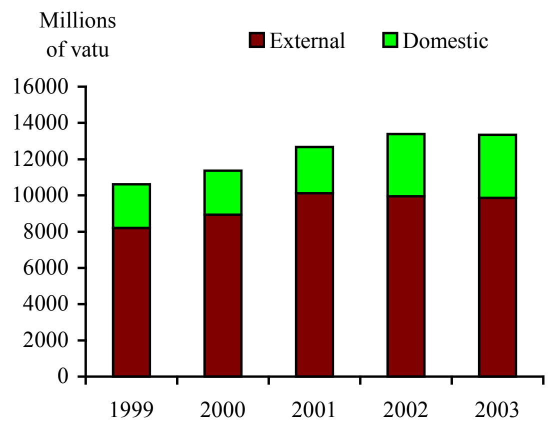


Chart 10: Public Debt



Government deposits at the Reserve Bank of Vanuatu fell by 25.7 percent to VT359.6 million, and the Government re-negotiated an advance facility for overnight borrowing at a daily ceiling of VT400 million. As a result, fiscal operations continued to contribute to liquidity creation in the system.

2.2 Outstanding Government Debt and Debt Servicing

The total outstanding public debt stood at approximately VT13.3 billion at end-2003, of which 26.1 percent comprised domestic debt. The level of outstanding public debt amounted to 38.9 percent of GDP in 2003.

Although this is low by international standards, the Government finances have experienced cash flow difficulties reflected by rise in its overdraft facility at the Reserve Bank of Vanuatu. In spite of this, the government has stayed within the legal limits of borrowings from the Reserve Bank and has always honoured its debt obligations.

3 MONETARY CONDITIONS

The role of monetary policy is to establish appropriate monetary conditions for price stability. During 2003, Broad money contracted by 0.8 percent as a result of liquidity outflows through the balance of payments and liquidity destruction on behalf of the government. These developments were reflected in declines in total net foreign assets and net credit to the government. These were offset by liquidity creation through private sector credit expansion.

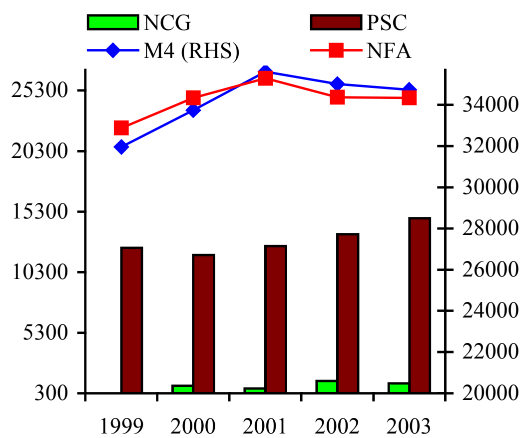
Monetary and credit expansion remained weak in the first half of 2003 reflecting weak domestic and international economic environment at that time. During the year Broad Money contracted but Narrow Money rose by 5.7 percent. Domestic credit slowed to 5.3 percent growth and private sector credit strengthened from the level of 2002 although the increase mostly took place in the second half of the year. Interest rate margins on commercial bank lending and deposit rates widened to 9.55 percent. The development reflected tight liquidity of some banks whereas interest rates on the RBV 91-day Notes decelerated towards end-2003.

3.1 Determinants of Money

3.1a Net Foreign Assets

Total net foreign assets decreased by 0.3 percent or VT65.3 million at the end of 2003. Commercial banks' NFA accounting for 81.0 percent of total NFA in 2003 was the driver behind movements in NFA. Movements in commercial bank's NFA follow the changes in resident deposits in foreign currencies and developments in the offshore finance center. During 2003, a number of offshore banks ceased operations and this probably could explain the decline.

Chart 11: Monetary Aggregates (Millions of Vatu)

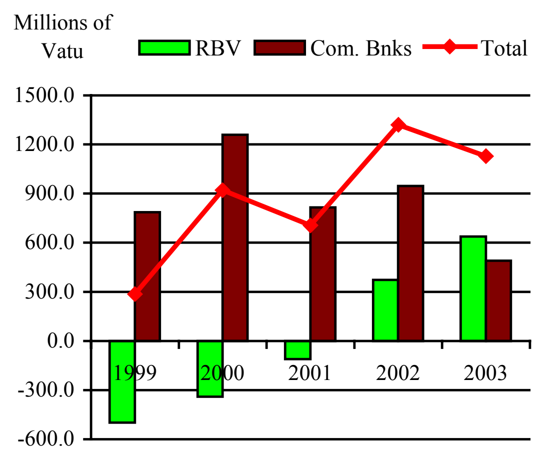


The NFA of the monetary authorities rose by 0.7 percent at the end of 2003 following a decline in 2002.

3.1b Domestic Credit

Growth in domestic credit slowed to 5.3 percent in 2003 from 11.9 percent in 2002. An expansion in private sector credit was slightly offset by falls in net claims on the government and claims on non-financial public enterprises (NFPE).

Chart 12: Net Claims on Government

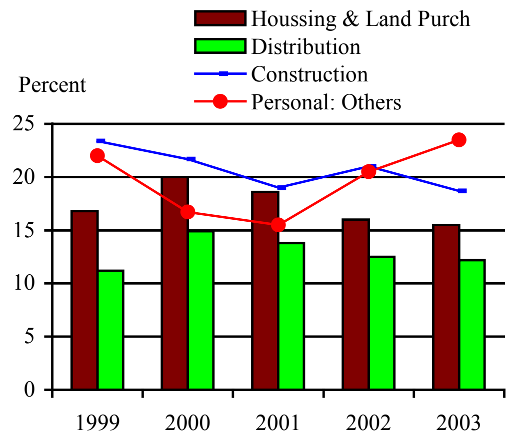


The government's net lending position with the banking system improved by 14.5 percent in 2003 following a deterioration of 87.2 percent in 2002. This is expressed in its net lending position with the commercial banks, which improved by 48.2 percent. Its position with the Reserve Bank, on the other hand, deteriorated by 71.2 percent. The decline in commercial banks' claims on the government is reflected in a decline in commercial banks' holdings of government securities because of shift of government borrowing from the commercial banks to the RBV and the captive market (Chart 12).

Claims on NFPE decreased by VT318 million or 95.2 percent in 2003, compared to an increase by 3.9 percent in 2002. The large decline reflected the repayment of VCMB's advances from the Reserve Bank in August 2003.

The year on year growth rate of private sector credit rose to 9.7 percent in 2003 from 7.9 percent in 2002.

Chart 13: Largest Sectoral Lending



3.1c Sectoral Distribution of Credit

During 2003, commercial banks increased lending activity to most sectors except for transport that declined by 0.1 percent, public utilities (97.5%), construction (1.0%) and professional and other services (4.5%). Of all the sectors that received expanded credit extension in 2003, agriculture and fisheries registered 9.4 percent, mining and manufacturing (107.1%), tourism (36.8%), entertainment (3.9%), financial institutions (37.7%), housing and land purchases (7.9%), distribution (8.5%), other personal loans (27.2%) and miscellaneous (20.7%). Personal loans accounted for the largest share of total lending in 2003 (Chart11).

3.2 Components of Money Supply

The contraction in total money supply was related to the fall in quasi money[1] whereas narrow money[2] continued to expand.

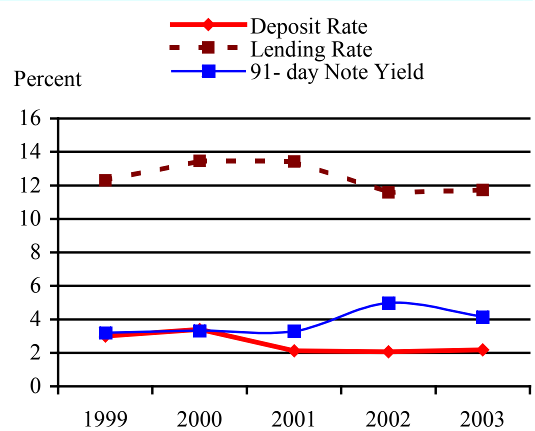
Narrow money expanded for the second successive year, adding VT651.8 million to reach VT12,176.3 million. This follows increases in currency with the public by 10.0 percent and demand deposit that expanded by 4.8 percent. The expansion in demand deposits was sourced from the foreign currency component that rose by 7.6 percent while demand deposits in Vatu expanded by 0.4 percent.

Quasi money contracted by 4.0 percent, following a decline of 15.0 percent in 2002. While Vatu-denominated quasi money continued to expand, successive declines in quasi money in foreign currency pushed total quasi money lower.

3.3 Interest Rates

The weighted average rate on fixed deposits rose from 4.13 percent in 2002 to 5.02 percent in 2003. Weighted average interest rate on all deposits followed the trend and increased by 0.11 basis points to reach 2.18 percent at the end of 2003.

Chart 14: Interest Rates



The overall weighted average rate on lending rose by 0.15 basis points to 11.73 percent at the end of 2003. The inter-bank lending rate was maintained at 5.50 percent.

[1] Quasi money comprises time and savings deposits in local and foreign currency
[2] Narrow money comprises currency outside banks and demand deposits.

3.3a Interest Rates Spread

As a result of the above developments the spread between weighted average deposit interest rates and lending rates widened by 0.04 basis points to reach 9.55 at the end of 2003.

The weighted average yield rate on the 91-days maturity and 28 days on RBV notes issued by the Reserve Bank at the end of 2003 was at 4.15 percent respectively. The average yield on the 63-days was at 4.16 percent.

Chart 14, portrayed that interest rate on the 91-day note yield was gradually declining as from the previous year as liquidity is more evenly distributed in the banking system. Weighted average interest rates on deposit and lending rates depicted almost a steady trend from the preceding year.

3.4 Reserve Money

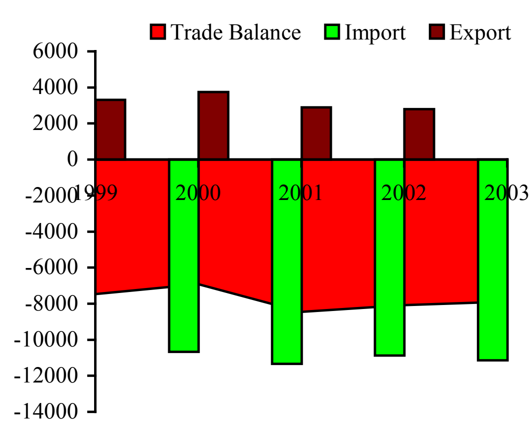
Reserve money[3] recorded an annual growth of 7.8 percent to VT4,828.6 million at the end of 2003. This was driven by an increase in SRD by 7.8 percent. Currency in circulation and excess reserves both recorded annual declines of 7.3 percent and 5.5 percent, respectively. The decrease in excess reserves could be explained by foreign exchange outflows through the balance of payments and increase in private sector credit extension.

4 EXTERNAL CONDITIONS AND INTERNATIONAL INVESTMENT POSITION

One of the main functions of the Reserve Bank is to maintain monetary stability expressed in terms of low inflation and external balance of payments viability. In terms of the latter the Reserve Bank aims to ensure that official reserves are always above four months of import cover. Largely because of economic weaknesses, the level of reserves declined from around 4.6 months of import cover in December 2002 to 4.4 months of import cover in February 2003. Pressure on reserves led the Reserve Bank to tighten its guideline on foreign exchange transactions stipulating a minimum of US$250,000 per importer. As a result official reserves began to stabilize in the third quarter of 2003. Since then there has been pressure on commercial banks foreign exchange due to the development of a trading arrangement in foreign exchange and season factors. The Reserve Bank continues to monitor developments and will take necessary measures where appropriate.

Within the balance of payments, the merchandise trade imbalance, amounting to VT7,886 million, improved by 2.6 percent compared to year 2002. Over the past five years the imbalance improved to VT6,921 million in 2000 but has deteriorated somewhat since then.

Chart 15: Trade balance

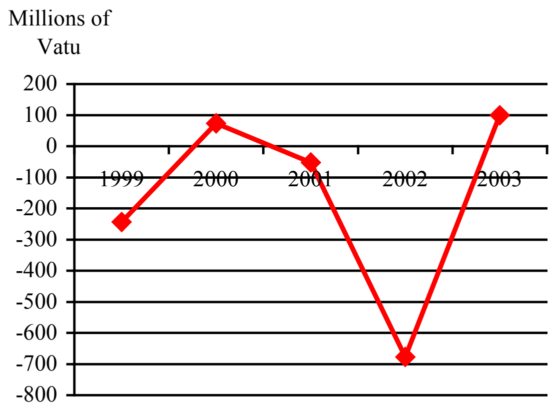


The current account recorded a large shortfall equivalent to 11 percent of estimated GDP, which was partly financed by the capital and financial account. In the current transfers account, official inflows

[3] Reserve money consists of currency in circulation, statutory reserve deposit (SRD) and excess reserves

dropped, caused by lower official grants from donors during the year.

Chart 16: Overall Balance of Payments



The overall external balance of payments turned into a surplus in 2003 compared to a large deficit in 2002. Net reserves (minus IMF positions) rose to VT4339 million at end-December 2003, which is equivalent to 4.5 months of import cover.

4.2 International Investment Position

The Bank has, for the first time, produced a comprehensive International Investment Position (IIP) for Vanuatu.

Table 3: Reconciliation Statement 2003

	Openin Position	Trans-action	Recon-Ciliation	Closing Levels
Net IIP	-721	-4793	-1417	-6931
Assets	62537	-7429	964	56074
Liabilities	63258	-2635	2381	63004

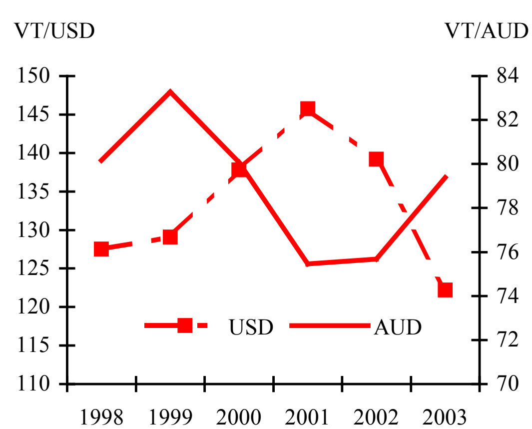
The IIP shows that Vanuatu's investment abroad (assets) was more that offset by foreign investment in Vanuatu (liabilities) resulting in a negative net international investment position (assets less liabilities). The net indebtedness position increased in 2002 and 2003. The numbers presented above reinforced the description given about the Financial Account, namely that assets and liabilities increased in 2002, only to fall in 2003, by 10.3 percent and 0.4 percent, respectively. The above position for Vanuatu during 2003 stemmed from other investment category. Other investment assets that recorded large decreases were currency and deposits (10.0%) and other tradable securities (59.0%). In liabilities, currency and deposits and loans both dropped dramatically in 2003.

5 EXCHANGE RATE MOVEMENTS

The Reserve Bank's exchange rate policy is aimed at maintaining a stable exchange rate of the Vatu. The currency is pegged to an undisclosed transaction weighted (trade and tourism receipts) basket of currencies from Vanuatu's major trading partners. Continued confidence in the exchange rate requires sound monetary policy.

During 2003 the Australian dollar appreciated in parallel with the Euro against the Vatu whilst over the same period the Vatu appreciated sharply against the US dollar.

Chart 17: Exchange rate



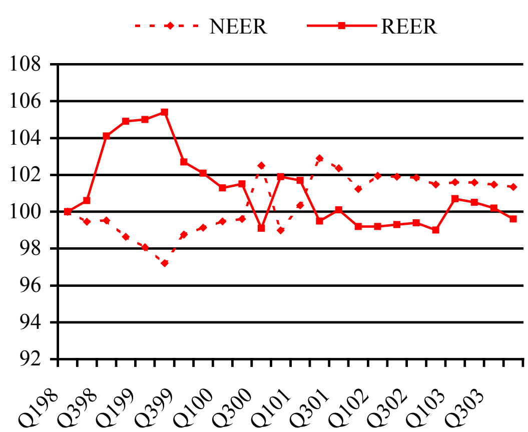
By end period comparisons, the Vatu appreciated against the US dollar (19.1 %), Pound Sterling (7.41%), Japanese yen

(7.63%) while it depreciated against the Australian dollar (10.17%), New Zealand dollar (4.30%) and Euro (0.46%).

5.1 Nominal & Real Effective Exchange rate.

The Nominal Effective Exchange Rate (NEER) has shown some improvement, indicating an improvement in competitiveness of the nominal exchange rate of the Vatu (at the end of the second quarter of 2003 the NEER had a value of 98.5). The improved competitiveness is due to the recent nominal appreciation of the Australian and New Zealand dollars and the Euro against the Vatu.

Chart 18: Vanuatu NEER and REER



The Real Effective Exchange Rate (REER) followed an upward trend at the end of the first quarter 2003 (the REER had a value of 103.2), which indicates that Vanuatu had a less favorable price performance compared to its main trading partners. From the development of the NEER in the same period the conclusion can be drawn that Vanuatu's external position improved. However, corrected for price difference, the competitive position of Vanuatu deteriorated but improved somewhat towards end-2003.
The REER was deflated on the basis of the Consumer Price Index (CPI).

6 OTHER ACTIVITIES OF THE RESEARCH DEPARTMENT

During December 2003, the Department organised a seminar for the Director Generals/Directors of Government Departments and First Political Advisors in the different Government Ministries. In this seminar, staff made presentations on the role of the Reserve Bank, developments in government finance and the effect of government finance on liquidity and its implication for monetary policy.

In the second half of 2003 and early 2004 a major effort was made to improve Balance Of Payment (BOP) statistics of Vanuatu. The review was undertaken with the assistance of an IMF consultant, Mr Geoff Robertson.

IV. MONETARY POLICY IMPLEMENTATION AND RESERVE MANAGEMENT

To achieve appropriate levels of monetary conditions the Reserve Bank implements monetary policy so as to achieve monetary stability in the domestic economy.

There was no change in the monetary policy indicator rate of the Bank during 2003 following its reduction from 7.0 percent to 6.50 percent on 01 May 2001.

The Reserve Bank uses a range of monetary policy tools to implement monetary policy. The principle instrument of the Bank has been open market operations, via auctions of the Reserve Bank of Vanuatu Notes (RBV Notes) to influence reserve money. Secondly, the Bank has in place a rediscount and repurchasing agreement facility for secured overnight borrowing from the Bank at a discount rate. This rate also serves as an indicator or official interest rate for the Bank's monetary policy stance. Thirdly, the Reserve Bank requires commercial banks to maintain Reserve Requirement of 10% of Vatu deposit liabilities and half of demand deposits in foreign currency. Fourthly, it maintains a portfolio of foreign exchange reserves, which enables it to buy and sell foreign exchange to support the exchange rate peg. The local currency is pegged to an undisclosed basket of currency.

1 Open Market Operations

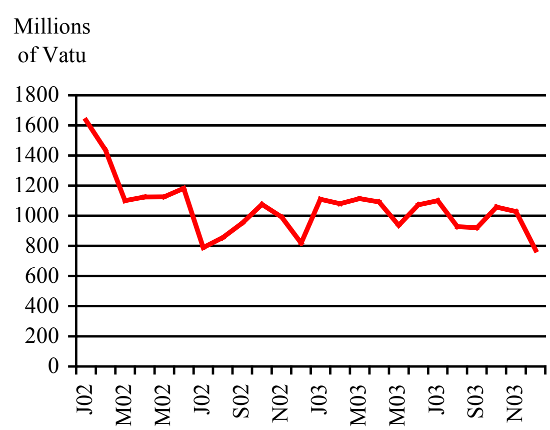
The Reserve Bank of Vanuatu operates an open market operation in the market for base money to absorb (inject) liquidity from (into) the banking system. Reserve Bank Notes are traded regularly in various maturities. The scale of operation is based on the outcome of the Bank's Reserve Money Program.

Table 4: Reserve Bank of Vanuatu Notes (VT Million)

	2002	2003
Number of Issues	31	17
Flotation	2720	1300
Tenders	3340	2100
Allotments	2465	2065
Outstanding	330	100

At the end of 2003, total RBV Notes outstanding stood at VT100 million. This represented a net annual decline of VT230 million from the preceding year. During 2003, the bank floated a total of VT1,950 million in of RBV Notes of which VT1,250 million were allotted.

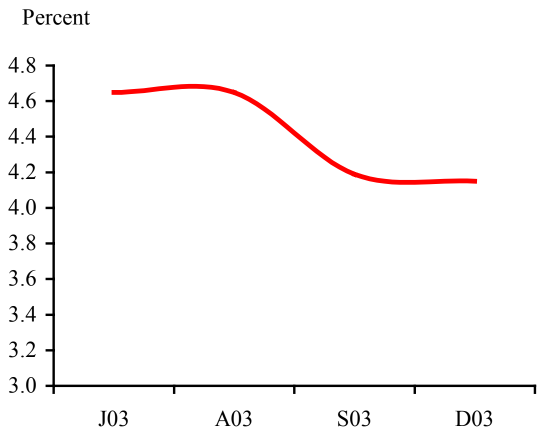
Chart 19: Excess Reserves



During the year the Bank introduced the 63-days Notes in the market in addition to the 28-days and 91-days. The 182-days and 119-days Notes were not issued in 2003.

Compared to 2002, open market operation activities were significantly lower in 2003 in line with the general decline in the settlement balances of commercial banks held with the Reserve Bank.

Chart 20: 91-days RBV Notes Yield



2 Rediscount and Repurchase Agreement Facilities.

These facilities allow the Bank to provide short-term liquidity to commercial banks by discounting Government securities and RBV Notes. Towards the end of 2003, some of the banks were faced with shortage in market liquidity partly due to seasonal demand and the banks own liquidity management. In view of this, banks resorted to the RBV's overnight discount window toward the end of the year in December but this ended when the Bank's Liquid Asset Ratio was reduced from 15 percent to 12 percent and when it was explained to the banks that their daily balance can go below the requirement without incurring penalty. However, for the most of 2003, there was ample liquidity in the system. The interest rate charged on borrowing through these facilities remained unchanged from last year at 6.50 percent. As noted this is also the policy rate of the Reserve Bank.

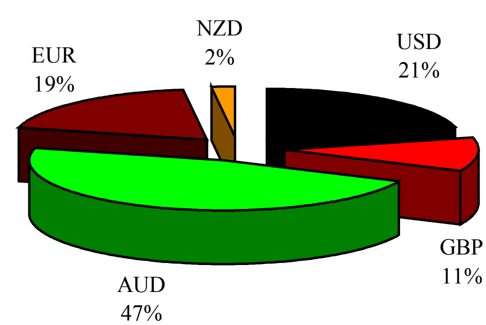
3 Reserve Requirements

Section 33 of the RBV Act states that the Bank may prescribe the maintenance of special reserves to be maintained by each financial institution. Reserve requirements were first introduced in 1988, primarily for prudential reasons when banks are required to maintain reserves equivalent to 10 percent of vatu deposit liabilities with the Reserve Bank. During April 1999, the Bank included half of demand deposit in foreign currency in its calculation of Reserve Requirement. Commercial banks meet reserve requirements on a daily averaging basis. By daily averaging, commercial banks are allowed to go below their reserve requirements at any time given they meet the Reserve Requirement on average during the holding period. Throughout 2003, there has not been any change in the Reserve Requirement ratio.

4 External Reserves Management

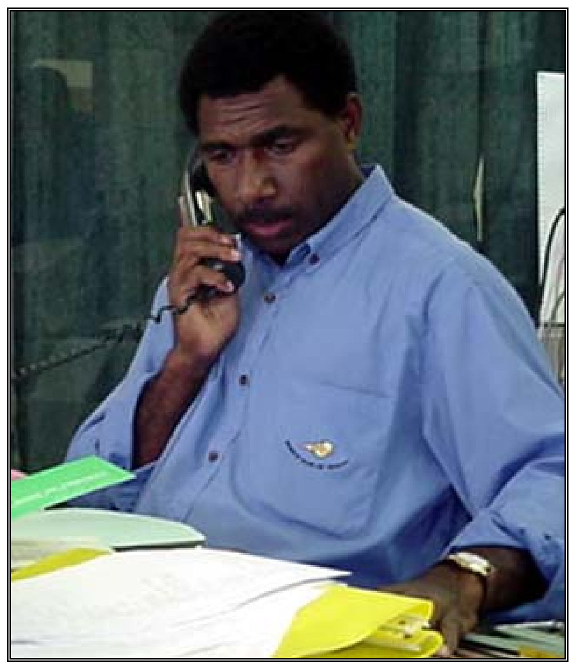
The Bank is charged under the Act with maintaining a reserve of external assets. In exercising this responsibility, the Bank continues to ensure that reserves are managed prudently within the parameters of safety and profit maximization.

Chart 21: Composition of Foreign Reserves



In 2003, total reserves of the Bank including the IMF positions are valued at VT4,901 million a slight increase over the previous year's figure of VT4,857 million. The year saw the role of VCMB, (a major earner of foreign exchange for the Bank) as an exporter being changed to regulator thus drying up a prime source of foreign reserves for the Bank.

Over the year, net sales of foreign exchange totaled VT981 million while purchases were recorded at VT923 million. While commercial banks grabbed the lion's share of 81 percent of the Bank's total of sales of foreign exchange, no reciprocal deal is recorded from them on purchases. The government and EEC were the main sources of foreign exchange purchases for the Bank recording a 47.3 percent and 40.8 percent respectively while purchases from were VCMB were down to 7.5 percent compared to 42 percent in 2002.



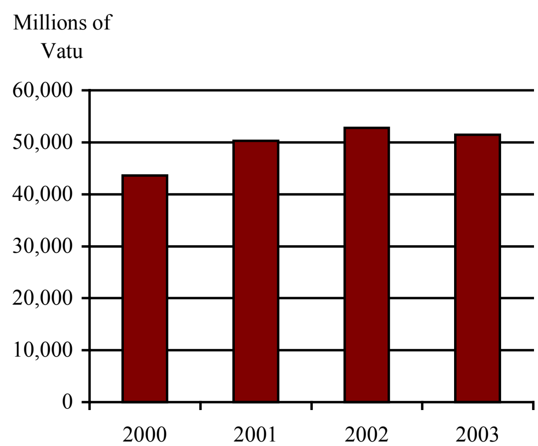
Due to the narrow source of foreign exchange earnings and to ensure that the level of reserves remains in compliance with its Act, the Bank issued and maintained throughout most of the year 2003, guidelines to manage its foreign exchange transactions.

The Bank employed two portfolio managers to assist in managing the foreign investments. The portfolio comprised mainly bonds and other securities as determined by availability and conditions of the international market. The remaining balance is managed by the Bank to settle government foreign debt service payments and to finance balance of payments transactions during the year. The currency distributions of the foreign reserves at the year-end are shown in chart 20.

V. BANKING SUPERVISION

The Reserve Bank of Vanuatu through its Bank Supervision Department continues to monitor and assess the performance of banks through the collection of information, the conduct of on-site inspections and meeting with bank's senior management. The Bank also has regular discussions with the banks to better understand their operations and to discuss issues where the Reserve Bank has some concerns.

Chart 22: Industry's Total Assets



In 2003 the Reserve Bank of Vanuatu supervised four domestic banks, namely, ANZ Bank (Vanuatu) Ltd, Westpac Bank Vanuatu, National Bank of Vanuatu and European Bank Limited. In addition this year, with the enactment of the International Banking Act No.4 of 2002, the Reserve Bank also assumed supervisory responsibility for offshore banks from the Vanuatu Financial Services Commission.

1 Balance Sheet

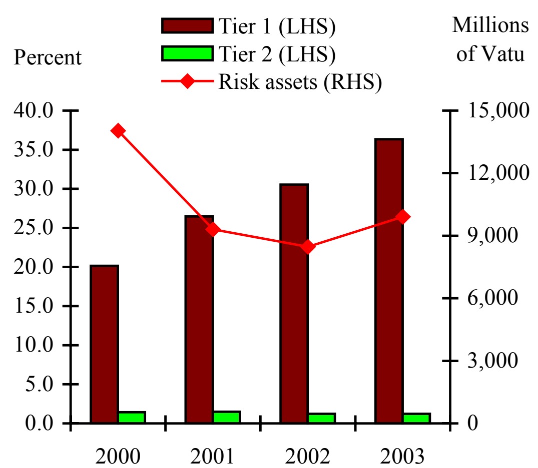
Total domestic banks' assets declined marginally by 2.5 percent to VT51.5 billion over the year to December 2003. The drop can be attributed to a decrease in banks' total foreign assets over the period.

Foreign assets represent more than 60 per cent (VT32.1 billion) of total assets. On the liabilities side, total deposits represent 63.9 percent or VT32.9 billion of total liabilities of which VT21.1 billion are foreign currency deposits.

2 Capital Adequacy

In the domestic banking industry, the bank's capital position as at 31 December 2003 stood at VT3.7 billion, up 38.3 percent from 2002. The increase in capital resources can be attributed to growth in retained earnings.

Chart 23: Industry's Capital Adequacy

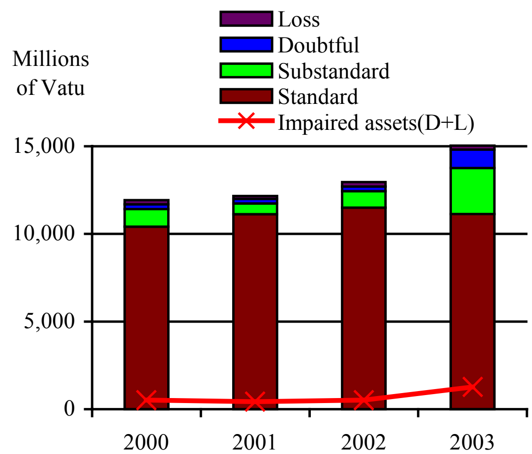


The Banks' risk weighted assets total VT9.9 billion, up 16.9 percent over 2002. The industry's capital adequacy ratio was 37.6 percent.

3 Impaired Assets

Banks continue to maintain high quality loans in their books with standard loans accounting for 75 percent of total loan portfolio of VT15 billion. However, as depicted in the graph below, the industry's level of impaired assets has risen significantly from last year by 150.6 percent to VT1.3 billion or around 34.1 percent of the consolidated industry capital.

Chart 24: Industry's Asset Quality



The deterioration in assets quality from 2002 was due to downgrading of some large facilities over the year. However, banks remain confident that workout strategies that they have in place should see these exposures return to performing status or be repaid. It is also positive to note that the level of exposures, classified as loss, has not deteriorated over the year.

4 Liquid Asset Requirement (LAR)

During the last quarter of 2003 the industry experienced increased pressure on liquidity, which pressured interest rates upward, so banks commenced rationing loan funds. The Reserve Bank after reviewing the situation reduced the LAR from 15% to 12%. The revised arrangements will come into effect from January 2004.

5 International Banks Licensing Arrangements

With the enactment of the International Banking Act No 4 of 2002 (the "Act"), the Bank assumed supervisory responsibility for the international (offshore) banking sector from the Vanuatu Financial Services Commission. At the commencement of the Act there were 34 licensed international banks. The number of offshore banks fell to 24 as a number of licensees requested the revocation of their licenses upon commencement of the new Act.

In terms of the Act, those licensees that wished to continue to operate after 31 December 2003 were required to submit an application to the Bank by 1 August 2003. Those licensees that failed to re-apply were required to make arrangements to exit the market and advise the Bank of their plans. Applications were received from 11 international banks. Applications were reviewed with the Bank focusing on the following key areas:

- Details on beneficial owners including financial capacity to provide additional capital resources;
- Fitness and propriety of owners, directors and managers;
- Business plan; and
- Risk management systems, including anti-money laundering, credit risk, liquidity risk and operational risk.

During the assessment process the Bank met with owners and management of some of the international banks and sought clarification/additional information on aspects of the applications. The Bank granted nine licenses while one applicant failed to respond to requests for additional information and its application was refused. One applicant, decided to withdraw its application, as it was not able to meet the licensing requirements.

The consolidated assets of the offshore banks declined significantly from Vt1.4 billion in the first quarter of 2003 to Vt395 million in the fourth quarter of 2003. The decline in assets of offshore banks over the year was mainly due to a number of banks exiting the market. Loans and advances continue to contribute more than 70 per cent (Vt285.3 million) of the sector's total assets while deposits represents 74.8 per cent of the banks' total liabilities.

6 Prudential Guidelines

Over the year, the Bank released 11 prudential guidelines that apply to the operations of international banks. The guidelines cover capital adequacy, large lending limits, customer due diligence, fit and proper criteria and physical presence requirements in Vanuatu. The guidelines are consistent with international standards.

7 On-site visit program – Anti-Money Laundering (AML)

During 2003, Bank Supervision Department staff undertook on-site AML visits to the domestic banks. These visits are in addition to usual supervisory visits conducted on domestic banks. During the visits interviews are conducted with bank staff, deposit/account opening files reviewed and transaction information reviewed to ensure consistency with the bank's own internal policies, the Bank's prudential guideline (Policy 9 – Customer Due Diligence) and the requirements of the Financial Transactions Reporting Act.

On the whole, the visits revealed that banks have taken steps to improve AML controls. This is partially in response to our requirements and also increased market pressure from overseas banks following the attacks of September 11 and the enactment of the USA Patriot Act, and in response to tighter requirements being set by international standard setters, such as Financial Actions Task Force.

8 Supervision of the Vanuatu National Provident Fund (VNPF)

During the year, the Minister of Finance and Economic Management authorized the Bank to conduct supervisory oversight of the VNPF. Following the Minister's recommendation, the Council of Ministers approved the supervision of VNPF and in December 2003 an Order was signed to give power to the Bank to supervise the VNPF.

The Bank's approach to supervision of VNPF will involve on-site and off-site supervision. The on-site supervision will be conducted through prudential consultations and inspections and the off-site supervision through the analysis of statistical data that will be collected from the Fund. As supervisor the Bank will not be hindering the operations of the Fund as mandated under the VNPF Act and the Fund will continue to carry out its essential functions as it has done since its inception in 1986.

It is intended that the Bank will meet with the VNPF early in 2004 to discuss the new supervisory arrangements.

9 Association of Financial Supervisors of Pacific Countries

In November 2003, the Bank's Deputy Governor was elected as Chair of the Association of Financial Supervisors of Pacific Countries for a term of two years. The Association is to meet in Vanuatu in 2004.

VI. BANKING AND CURRENCY OPERATIONS

1 ASSET AND PROFITS

The year 2003, saw the continuing downward trend in the Bank's net operating profit and posting an all time low of VT36.6 million for the year compared to VT57.4 million in 2002. Although official reserves are slightly higher than the previous year, interest rates in international markets, especially the USD dollar, were at their lowest level resulting in an 8.1 percent decline on total interest received on foreign investments. Interest income on domestic government bonds and secured lending increased by 7.3 percent and 12.6 percent respectively. While expenditures continue to increase over the previous year due to increase in staff members and other costs, the year registered the first payment of VT11.0 million towards the provision for gratuity and recognition of long service for staff members who have served the Bank for more than 10 years as provided for in the RBV Staff Guideline. The Bank spent VT3.0 million for undertaking a review of the Bank's currency operations.

2 BANKING

2.1 Currency Operations

The total value of Vatu notes and coins issued by the Bank peaked in an all time high at VT2,559.5 as at the end of 2003 representing an increase of 12.6 percent from 2002. This increase in currency issued figures may be interpreted as a result of the Bank refining its cash operations with commercial banks in August allowing them to effectively manage their cash operations and hold larger cash reserves to cater for their daily cash operations. Of the total currency issued, VT1,000 continued to be the most preferred denomination although its percentage share of total notes issued decreased to 47.9 percent from 48.5 percent in 2002 followed by the VT5,000 with a 42.7 percent share compared to 41.6 percent in the previous year. The VT500 and VT200 followed in that order. Although the Bank stopped printing the VT100 bill in 1999, the value of the denomination still in circulation make up the last 1 percent of total notes issued. The VT100 continued to dominate the coins issue comprising a total share of 56.8 percent as compared to 56.4 percent in 2002 followed by VT20 (15.7%), VT10 (10.6%), VT 50 (9%), VT 5 (4.3%), VT 2 (21.%) and VT1 (1.5%).

The Bank continues to perform its fundamental role as the sole issuer of the country's currency, ensuring sufficient stock is available and maintaining the quality of the notes and coins. In 2003 a total of 2,464,454 were examined, 224,401 notes less than total notes examined last year. Of the total notes examined, 17.3 percent were rejected as unfit for reissue. As can be seen from Table 1, more than half of the lower denominations of VT500 and VT200 that were deposited for examination during the year were rejected as unfit for reissue and all VT100 notes were cancelled for destruction.

Table 5: Notes Examination

Notes	Number Examined	Fit for Reissue	Unfit for Reissue	Rejection Rate
5,000	422,925	400,302	22,623	5%
1,000	1,747,989	1,507,076	240,913	14%
500	135,194	56,432	78,762	58%
200	157,751	74,892	82,859	53%
100	595	0	595	100%
Total	**2,464,454**	**2,038,702**	**425,752**	**17.3%**

In October 2003, the Bank hired a consultant and former General Manager, Mr John Howard to undertake a review of the Bank's Currency operations. The Term of Reference as approved by the Board focused on appraisal of daily currency operations including working relationship with banks, current denominations of both notes and coins in terms of production costs, monetary value, life and public acceptance.

An assessment of the currency security features taking into account the counterfeiting experience was also included and other topics covered in the review scope were the human resource capacity and development of numismatic currency.

2.1a Counter Operations

The Bank continued to provide customer banking services to the government, commercial banks and the VCMB as provided for under the RBV Act.

During 2003, the total counter transactions increased by 5.5 percent over the previous year and are reflected by 8.5 percent increase in withdrawals 2.4 percent increase in deposits.

Table 6: Cash Counter Transactions

Period (Year)	Withdrawals	Deposits	Totals
2000	4,145	4,136	8,281
2001	4,098	3,980	8,078
2002	3,902	3,873	7,775
2003	4,235	3,965	8,200

2.2 Anti Counterfeit Measures

Since the Bank started issuing its own currency Vatu in 1982, this year 2003 marked the first experience of sophisticated currency counterfeiting. Whereas previous counterfeiting were done on normal copier with results being easily spotted, the recent counterfeits were believed to have been scanned and printed on colour printers which made it very difficult to identify at a first glance. Counterfeits confiscated were of the two highest note denominations of VT5,000 and VT1,000. The Bank through the commercial banks and the media alerted and advised the public to be vigilant. The matter has been reported to the Police for further action.

2.3 Payment System

The total number of cheques and payment orders presented through the clearinghouse in 2003 decreased by 71,798 from 2002. Likewise, the total value of cheques cleared in the clearinghouse also declined (see table).

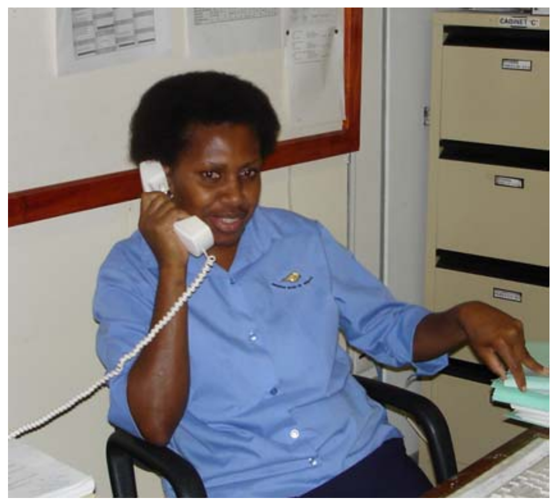
Table7: Operation of Clearinghouse

Period (Year)	No. of Effects	Value (MVT)
1999	370,352	34,224
2000	398,286	32,622
2001	378,016	34,995
2002	335,462	33,878
2003	263,664	28,230

VII. RELATIONS WITH INTERNATIONAL ORGANISATIONS

Vanuatu is a member of a number of international organizations. These include the International Monetary Fund (IMF), the World Bank and the Asian Development Bank. As in previous years, the Reserve Bank continues to benefit from Vanuatu's membership in the IMF, through the Fund's Technical Assistant Program.

Throughout 2003, the Fund continues to fund Mr. Andrew Milford's secondment with the Bank. Mr. Milford serves as an advisor to the Banking Supervision Department.



Mr. Ferdie Van de Walle, who used to be the General Advisor to the Bank, visited the Bank several times during 2003. The IMF also funds him.

Also, during 2003/2004, the IMF funded a Balance of Payment (BOP) consultant, Mr Geof Robertson, who visited the Bank twice in 2003 to review and improve the BOP statistics of the country.

VIII. INTERNAL MANAGEMENT

1 ADMINISTRATION

1.1 Appointment of Governor

Governor Odo Tevi's appointment came into effect on the 25th of April 2003. He succeeded Mr. Andrew Kausiama whose term as Governor expired on the 25th of April 2003. Governor Tevi holds a Masters in Economics from Sussex University in UK. His appointment was made by Prime Minister, on recommendation by the Minister of Finance, is for a period of five years.

1.2 The Board of Directors

The Board of Directors is responsible for the policy and the general affairs of the Bank. The Board made a number of major policy decisions in 2003. These included the approval of the budget for 2003, the financial statements for year ending 2002, the Terms of Reference (TOR) for the independent review of the Bank, the Bank policies, the currency review and the report on the review and the monetary policy stance of the Bank.

During 2003, the Board of Directors consisted of Odo Tevi who succeeded Andrew Kausiama as Governor and Chairman of the Board, Mr. Geordie Mackenzie-Reur and Mrs. Aniva Tarilongi. There was no appointment from the Ministry of Finance and Economic Management as stipulated in the Reserve Bank Act. The term of office for members do not exceed five years.

The Act requires that the Board meet not less than four times a year Board. There were a total of seven Board meetings in 2003.

1.3 Management Committee

The management committee is responsible for the implementation of policies approved by the Board of Directors. It meets on a regular basis and makes decisions concerning the internal management and daily administration of the Bank. The committee meets every week on Mondays. The committee is made up of the Governor who is also the chairman of the committee, Deputy Governor, Director of Research, Director of Operations and the Acting Director of Administration.

1.4 Official Representation overseas

During June 2003, the Governor attended the Banking and Financial Services Symposium and Governors' Symposium in England. After this, he proceeded to attend the BIS Annual General Meeting in Switzerland.

In July, Deputy Governor Peter Tari attended the Offshore Group of Banking Supervisors' meeting held in Mauritius.

In September 2003, the Governor accompanied the Minister of Finance to the Commonwealth Finance Ministers' meeting in Brunei and the International Monetary Fund (IMF) and World Bank Annual meeting that was held in Dubai.

During October, Governor Tevi attended the late Siwatibau's funeral at Christchurch in New Zealand.

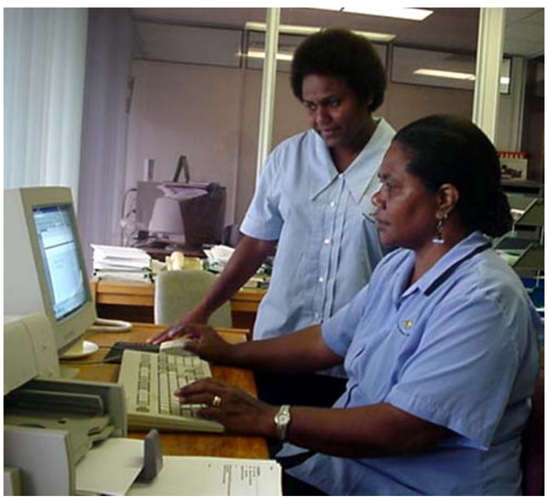
In November the Deputy Governor attended the annual meeting of AFSPC in Fiji. The Governor attended the South Pacific Central Bank Governors' meeting in Papua New Guinea during December 2003.

2 Legal Issues

During the year legal advice was sought and provided to the departments on different issues in relation to relevant legislations and policies affecting the operation of the Bank. The Bank's internal policies and guidelines were approved by the Labour Department pursuant to the Employment Act and they became operative on 19th August 2003.

3 Information Technology

The Information Technology Unit continues to maintain the Bank's Local Area Network and other computer systems.



The Bank has successfully migrated from a Novell Netware environment to a Windows 2000 platform. Windows 2000 group policies have been applied to various network settings to maintain and ensure a more controlled network environment.

Information Systems security was reviewed and enhanced. For example a corporate version of anti-virus software was introduced and provides the entire Bank with an online, real-time virus prevention method. IT Unit continues to seek better and effective methods of maintaining the Bank's network, information and data security procedures.

External email and the local Intranet continue to cater for information dissemination with counter parties and within the Bank respectively. The local Intranet is undergoing analysis and tests for a better content management system. This system will be a web based database management system accessible via a browser program to view and access information and to an extent process data.

The Bank's official Internet website was launched in 2003. It provides general and more specific information about the Bank to the public and is continuously being reviewed and updated. The website can be accessed on the following link: **www.rbv.gov.vu**

End-user applications and installations pertain to only approved Bank software. The IT Unit was involved in the development of certain in-house applications to automate various unit tasks. Various software and hardware installation and upgrades were also carried out.

4 Publications

The Bank has various mediums through which it informs the public about policies and its internal operations. As in previous years, the Bank has continued to keep the public informed about international and domestic economic developments through its Monthly Financial and Economic News Summary, the Quarterly Economic Review and Annual Reports

The 2001/2002 Annual Reports were issued in April and covered analysis of economic and financial developments in these two years, the operations and activities of the Bank and the audited financial reports for 2001 and 2002.

The Bank's various publications are posted in the Bank's website, launched in 2003.

5 Library

The Bank's library, which is under the supervision of the Research Department, continues to respond to the information need of the bank and enhance its service to the bank staff. It also maintains a complimentary listing of subscribers who receive the regular issues of the bank publications, namely, the annual report, quarterly economic review and the monthly financial and economic news summary.

The library holdings consist of a variety of publications that include IMF and World Bank publications, annual reports and quarterly bulletins from other Central Banks, government reports, journals and magazines on monetary, economics and financial issues.

As an important organ in the bank, the Library does not only provide information to the bank staff but also to students from nearby schools and tertiary institutions. The library also participated with other libraries within Port Vila during the ***Lire en Fete 2003/Reading Festival 2003*** organized by the French Embassy in Port Vila from the 13th to 18th October 2003.

6 Human Resources

The total number of staff of the Reserve Bank rose to 56 at the end of 2003 from 53 at the end of the preceding year. Of this total, 55 were Ni-Vanuatu and 1 an expatriate who is the advisor to the Banking Supervision Department. Two other expatriate advisors visited the Bank from time to time in 2003. All advisors served under the IMF technical assistant program. In 2003, two staff left the Bank of whom one resigned and the other was terminated. Also, during the year four new staff were recruited, three as security officers and one assistant banking supervisor.

The Director of the Research Department, Mr Simeon Athy, left the Bank at the end of July 2003 and moved on be the Director General in the Ministry of Finance and Economic Management. Following the departure of Mr Athy, Mr Michael Hililan was appointed Director of Research effective December 2003. Mr Hililan is also the Chief Economist of the Reserve Bank. He holds a masters degree in Economics from Bradford University in the UK.

7 Training and Development

During the year, the Board approved, along with other policies and guidelines, the training policy of the Bank. The Bank actively encourages staff training with the following broad objectives:

1. To help staff perform their duty assignment effectively;
2. To help develop an individual staff member to reach his/her potential, or further his/her future career prospect; and
3. To help ensure productivity among staff.

As in previous years, the Bank continued to support staff training and development throughout 2003.

Table 8: Staff Training in 2003		
Types of Training	**No. of Staff**	**No. of Courses**
Full Time Training	1	4
Part Time Training	5	3
Course/Attachment	8	7

The Bank supports a range of training that includes in-house training, full time training, part time studies and short courses/attachments with regional Central Banks and other approved institutions.

8 Other Activities

The Bank continues to offer chances for students to do holiday jobs with the Bank in 2003. During 2003, a total of 12 students were offered work experiences in the various departments of the Bank. Of this, 4 did holiday jobs during May and June and 8 during the Christmas holidays.

8.1 Staff Goodwill tour

During the Easter break between 17th April and 24th April 2003, 33 members of the RBV staff participated on a goodwill tour to the Reserve Bank of Fiji (RBF). As part of the exchange program, staff members of the two central banks participated in sporting and other social activities. Immediately, after the tour, 20 staff left for Vanuatu on the 20th April 2003, while the other 13 did attachment in various departments within RBF for another two days before leaving for Vanuatu on the 24th April 2003.

8.2 The RBV Staff and Social Welfare Association

In 2003, the RBV Social and RBV Welfare Committees merged and formed the RBV Staff and Social Welfare Association (RBVSSWA). The purpose of this Association is to look into staff welfare and organize social and outdoor activities for RBV staff. There is an executive committee tasked with the running of this association and consist of a Chairman, Vice Chairman, Secretary, Vice Secretary, Treasurer, Vice Treasurer and four other staff members representing all the Departments in the RBV.

9 Acknowledgments

The Board and the Governor of the Reserve Bank of Vanuatu wish to convey their gratitude for the continuous commitment of staff during 2003. This appreciation is also extended to the International Monetary Fund (IMF) for the advisors provided to the Bank under its technical assistant program.