

### High uncertainty dampens outlook for Global growth

US-China tariffs war still remains a major concern for global growth, in addition to the likely no-deal Brexit in the Euro Area. The United States recorded a 2.0% GDP growth in the second quarter of 2019, due to positive private consumption and higher government spending which was partly offset by the drop in private inventory investment, exports, and investments in housing. Growth in Australia for the second quarter of 2019 grew by 0.5% and by 1.4% over the year attributed mainly to robust public sector spending and subdued growth in household spending outweighing a decline in housing investment. New Zealand experienced mixed growth over the month of July as labour income continued to grow whilst consumer spending weakened. The Reserve Bank of New Zealand also reduced the Official Cash Rate (OCR) in early August by 50 basis points to 1%.

### July festivities support domestic activities

Tonga presented their best local produce, catches, and crafts during the Royal Agricultural, Fisheries and Tourism Show in July 2019, where the emphasis was on 'Smarter Agriculture' for climate change. Agricultural exports rose by 154.7 tonnes (30.1%) to 668.9 tonnes in July, particularly for taro, yams, cassava, and coconuts. Agricultural harvests are showing signs of recovery after TC Gita, but not yet up to the levels before the cyclone. Proceeds from agricultural exports increased by \$0.34 million (78.7%), and credit to the agricultural sector also rose by \$0.30 million (2.7%). Farming equipment such as tractors, disc plows, and funds for construction of fishing vessels were donated to the Government to assist with the development of the agriculture and fishing sector. The Pathway to Sustainable Oceans project was also launched in July to strengthen and develop selected sustainable fisheries activities.

The secondary sector continued to show positive activities in July. Individual housing loans and manufacturing loans increased over the month by \$0.8 million (0.4%) and \$0.2 million (1.2%) respectively. Additionally, new commitment loans for the construction sector also increased by \$1.8 million, indicating future prospective investments in construction services. Tonga's first wind farm was switched on in Niutoua which creates renewable energy, as part of Tonga energy road map (TERM) project. Meanwhile, the road development project continues benefitting the manufacturing, mining and quarrying sectors.

The tertiary sector performances were mostly favourable during the month. The Heilala Week Festival and the King's 60<sup>th</sup> Birthday Celebration attracted many visitors to

Tonga in July, evident in the 12.8% (1,305 passengers) increase in international air arrivals. The number of international flights recorded also rose by 28.3% (26 flights). Tonga's domestic airline now operates international flight routes to Samoa and currently Fiji. Vehicle registrations increased by 32.7% (81 vehicles) while container registrations decreased by 30.7% (403 containers) as both business and private containers registrations declined.

### Employment interest from Education

There were 39 vacancies advertised in July compared to 40 in the previous month, according to the NRBT employment survey. More than half of these vacancies were for teaching positions at the Ministry of Education and Training for vocational/technical studies. With the competitive rates offered by the seasonal working schemes overseas, the local employers are either competing to retain their current staff or are looking for new staff to replace those who have left. This will continue to lower the unemployment rate in Tonga.

### First deflation since 2016

Table 1: Inflation Rates

Prices	Monthly		Annual	
	Jul-19	Jun-19	Jul-19	Jun-19
<b>Headline Inflation (%)</b>	<b>0.2</b>	<b>0.2</b>	<b>-0.5</b>	<b>1.8</b>
Domestic prices	0.2	-0.3	-2.4	1.7
Imported prices	0.2	0.6	1.1	1.9

Source: Statistics Department

The Statistics Department reported 0.2% inflation for the month of July. Both domestic and imported prices rose by 0.2% respectively. Prices of local food such as fruits and vegetables, fish and seafood drove the higher domestic prices. The major events and celebrations held during the months of June and July may have led to higher demand for local food, thus contributing to the higher prices. For import prices, the lower fuel prices in July were offset by the rise in prices of imported meat, footwear, and household items.

Annually, July recorded the first deflation of 0.5% since May 2016 (-1.0%). This was driven by lower domestic prices (-2.4%) for Kava and some local root crops, fruits and vegetables relative to the same month last year, as outlined in Table 2 below. This reflects favourable supply of food and kava in the local markets in July, compared to the shortages in the same month last year, following the cyclone. Prices of local telephone and telefax services also declined over the year, as well as utility prices. However, imported inflation rose by 1.1% over the year. Prices of all groups rose except for petroleum, personal care services, and medical products.

**Table 2: Items contributing to annual domestic deflation**

Items (\$ per kg)	Unit	Monthly			Annual	
		Jul-19	Jun-19	Change	Jul-18	Change
Kava	1 kg	\$115.00	\$115.00	\$0.00	\$150.00	-\$35.00
Lu	1 kg	\$3.65	\$3.40	\$0.25	\$9.41	-\$5.76
H/cabbage	1 kg	\$1.41	\$1.34	\$0.07	\$2.24	-\$0.83
Carrots	1 kg	\$3.88	\$4.45	-\$0.57	\$4.17	-\$0.29
Kumala	1 kg	\$2.12	\$2.03	\$0.09	\$2.36	-\$0.24
Talo-Futuna	1 kg	\$1.72	\$1.73	-\$0.01	\$1.89	-\$0.17
Sausages	1 kg	\$8.19	\$8.19	\$0.00	\$8.27	-\$0.08
Yams-late	1kg	\$2.70	\$2.57	\$0.13	\$2.76	-\$0.06
Cassava	1 kg	\$1.10	\$1.28	-\$0.18	\$1.08	\$0.02
Yams-early	1kg	\$4.92	\$4.42	\$0.50	\$4.84	\$0.08

Source: Statistics Department

### Competitive exchange rates

**Table 3: Effective Exchange Rates**

	Jul-19	Monthly		Annual	
		Jun-19	% Growth	Jul-18	% Growth
Nominal Effective Exchange Rate Index	91.9	91.8	0.1	91.1	0.9
Real Effective Exchange Rate Index	106.4	106.3	0.1	107.4	-0.9

Source: National Reserve Bank of Tonga

The Nominal Effective Exchange Rate (NEER) index marginally rose over the month as the NZD, AUD, JPY, GBP & EUR depreciated against the TOP. Additionally, the Real Effective Exchange Rate (REER) increased in July due to the monthly rise of Tonga's inflation. Annually, the NEER increased whilst the REER fell, which may impact the total inflow receipts and the international competitiveness of exports.

**Table 4: Bilateral Exchange Rates**

	Jul-19	Jun-19	Jul-18
USD/TOP	0.4363	0.4394	0.4416
AUD/TOP	0.6344	0.6274	0.5961
NZD/TOP	0.6594	0.6559	0.6471
FJD/TOP	0.9381	0.9437	0.9225
JPY/TOP	47.3669	47.3388	49.0286
GBP/TOP	0.3587	0.3467	0.3362
EUR/TOP	0.3910	0.3864	0.3771
CNY/TOP	3.0037	3.0218	3.0095

Source: National Reserve Bank of Tonga

### New high record for official foreign reserves

**Table 5: Foreign Reserves**

	Jul-19	Monthly		Annual	
		Jun-19	% Growth	Jul-18	% Growth
Foreign Reserves (\$ in million)	492.9	484.3	1.8	476.5	3.4
Import Coverage (months)	8.2	8.1		8.2	

Source: National Reserve Bank Tonga

Official foreign reserves continued to trend upward with a new record high of \$492.9 million in July 2019, equivalent to 8.2 months of imports cover. The monthly movement was attributed to net inflows from foreign exchange deals mostly for remittances receipts.

**Table 6: Overseas Exchange Transactions**

	Monthly			Annual		
	Jul-19	Jun-19	% Growth	Jul-19	Jul-18	% Growth
<b>Overall Balance</b>	<b>8.6</b>	<b>16.0</b>	<b>-46.2</b>	<b>16.4</b>	<b>67.6</b>	<b>-75.7</b>
<b>Current Account</b>	<b>0.4</b>	<b>19.8</b>	<b>-97.8</b>	<b>-3.1</b>	<b>14.8</b>	<b>-121.0</b>
Merchandise Trade	-33.9	-35.5	4.5	-421.6	-390.9	-7.8
Services	6.0	4.0	49.6	32.2	24.2	33.2
Income	1.2	-4.8	125.8	8.1	-4.6	274.5
Transfers	27.1	56.1	-51.7	378.1	386.2	-2.1
<b>Capital Account</b>	<b>0.2</b>	<b>9.1</b>	<b>-97.6</b>	<b>38.5</b>	<b>41.5</b>	<b>-7.4</b>
<b>Financial Account</b>	<b>8.0</b>	<b>-12.9</b>	<b>161.7</b>	<b>-18.9</b>	<b>11.2</b>	<b>-269.1</b>

Source: Banking Systems

The overall Overseas Exchange Transactions (OET) balance surplus lowered in July 2019 as both payments and receipts declined. Total receipts declined by 34.4% (\$34.6 million) following the high level of official transfer receipts in June 2019. Inflows to the capital and financial accounts also declined. These outweighed a rise in remittances & travel receipts and export proceeds. Similarly, payments declined by 21.5% (\$16.6 million) due to lower payments for investment offshore and dividends.

Annually, the OET balance surplus lowered due to higher outflows from the current and financial accounts. Higher payments were noted for goods & services, offshore investment, and interbank transfers. These outflows outpaced the rise in receipts from travel, remittance, and earned income.

### Broad money declined on lower net domestic assets

**Table 7: Broad Money**

	Monthly			Annual	
	Jul-19	Jun-19	% Growth	Jul-18	% Growth
Broad money (\$ in million)	598.1	600.1	-0.3	605.6	-1.2
Net Foreign Asset	510.0	506.3	0.7	497.5	2.5
Net Domestic Asset	88.6	94.2	-6.0	108.4	-18.3

Source: Banking System, National Reserve Bank of Tonga

Lower government deposits over the month and higher credit to private sectors over the year, lowered the net domestic assets as well as broad money, despite the increase in net foreign assets. The increase in foreign reserves from the receipts of budgetary support, grants, and remittances contributed to the higher net foreign assets.

### Liquidity rose in July

**Table 8: Reserve money**

	Monthly			Annual	
	Jul-19	Jun-19	% Growth	Jul-18	% Growth
Reserve money (\$ in million)	309.0	302.2	2.2	332.3	-7.0

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the banking system rose over the month by \$6.8 million (2.2%), however, declined over the year by \$23.4 million (7.0%) respectively to \$309.0 million. The monthly rise was due mainly to higher exchange settlement accounts on the increase in deposits from the commercial banks to the Reserve bank vault, supported by the slight rise in required reserves. The banks' total loans to deposit ratio edged up slightly from 77.9% to 78.4% over the month, reflecting loans increasing at a faster pace than the increase in deposits.

### Credit growth rebounds to a new high level

**Table 9: Total Lending**

Lending	Monthly			Annual	
	Jul-19	Jun-19	% Growth	Jul-18	% Growth
Total Lending (\$ in million)	491.1	486.2	1.0	452.9	8.4
Business lending	231.7	226.9	2.1	203.9	13.7
Household lending	259.2	258.9	0.1	249.4	3.9
Other lending	0.2	0.4	-46.2	0.8	-73.4

Source: Banking System, National Reserve Bank of Tonga

Following a decline in June, the total banks' lending grew to a new high level of \$491.1 million in July 2019. This was due mainly to higher lending to businesses mostly for state-owned enterprises, professional & other services, agriculture, and manufacturing sectors. Housing loans by households also marginally increased over the month. Over the year, total lending increased by \$38.2 million (8.4%) which is again underpinned by higher credit to businesses and households.

### Weighted average interest rate spread narrowed

Table 10: Weighted Average Interest Rates

Interest Rates	Monthly			Annual	
	Jul-19	Jun-19	Growth (bps)	Jul-18	Growth (bps)
Weighted Average Banks Deposit Rate (%)	1.925	1.939	-1.4	2.019	-9.3
Weighted Average Banks Lending Rate (%)	8.012	8.029	-1.8	8.062	-5.0
Weighted Average Interest Rate Spread (%)	6.086	6.090	-0.4	6.043	4.3

Source: Banking System, National Reserve Bank of Tonga

The weighted average interest rate spread narrowed over the month by 0.4 basis points to 6.09%. This was a result of the decrease in weighted average lending outweighing the decline in weighted average deposit rates. The decreased lending rates were mainly for businesses such as fisheries, professional & other services, and tourism sectors as well as household housing loans. Both demand

and time deposits rates declined and offset the rise in saving deposit rates.

The weighted average interest rate spread, however widened over the year, by 4.3 basis points. This time the weighted average deposit rates decreased more than the decline in weighted average lending rates. Again, both demand and time deposit rates fell and outweighed the increase in saving deposit rates, whereas decreased lending rates offered to businesses such as fisheries, tourism, construction, and agricultural sectors, and household housing loans contributed to the decline in weighted average lending rates.

### Outlook

The Reserve Bank still expects domestic economic activity to remain positive in the medium term. Foreign reserves is at comfortable levels above the minimum of three months of imports cover, and inflation is below the Reserve Bank's reference rate of 5%. The Reserve Bank considers its current accommodative monetary policy stance to still be appropriate at this time. Nevertheless, the Reserve Bank continues to closely monitor developments in the domestic and global economies and stands ready to adjust its monetary policies, to ensure financial and macroeconomic stability are maintained.