



NATIONAL RESERVE BANK OF TONGA

MONTHLY ECONOMIC REVIEW

Vol. 6

No. 6

Month Ended: June 2019

Global growth remains subdued

Global growth forecast for 2019 was further downgraded by 0.1 percentage point to 3.2% according to the IMF's July World Economic Outlook (WEO), compared to a 3.3% in released in its April 2019 WEO. This downgrade is attributed to the escalated United States-China trade war, prospect US sanctions threatening global technology supply, Brexit-related uncertainty, and geopolitical tensions. Although global growth is forecasted to pick-up to 3.5% in 2020, it is also 0.1 percentage point lower than the previous forecast in the April WEO. Consequently, slower growth was observed amongst Tonga's major trading partners such as New Zealand and Australia for June 2019. New Zealand Treasury reported that weak business confidence and global uncertainties continued to weigh on GDP growth prospects. The Reserve Bank of Australia lowered the cash rate by 25 basis points to a record low of 1.0% early in July, reiterating the same reason for the cut in June, which is to support employment growth and progress toward the medium-term inflation target. Economic growth for the first half of 2019 was lower than expected as household consumption declined, and the level of housing credit remained low.

Sector performances continue to be mixed

Activities in the primary sector were mixed in June 2019. The total volume of agricultural exports decreased by 206.1 tonnes due to lower exports of squash and cassava. This coincided with a \$0.2 million decline in agricultural export proceeds following an offseason squash shipment on the previous month. Over the year, agricultural export volumes also declined by 30.7%. Fish exports, however, more than doubled over the month by 215.6 tonnes, mostly for exports of tuna. Exports of aquarium products, on the other hand, dropped by 59.5% weighing on the proceeds for marine exports, which slightly declined by 9.7%. Over the year, total marine export volumes rose coinciding with the 42.6% rise in proceeds.

Construction works was slow during the month, reflecting the decline in lending to the secondary sector. However, the road improvement project continued to support the mining & quarrying sector. Electricity consumers increased steadily throughout the year, as a consequence of the increase in new houses constructed and reflects the increase in housing loans over the years. Upcoming infrastructure projects earmarked for this fiscal year will further contribute to the growth of the industry sector.

Performance of the tertiary sector was mostly favourable. Container registrations rose by 270 containers over the month as both business and private containers increased by 238 and 32, respectively. Private consumption and trade are expected to thrive in June with activities relating to the annual church conference of the Free Wesleyan Church, preparations for His Majesty's 60th Birthday, and

the Heilala Festival. Visitors attending these annual events increased international air arrivals by 6.5%, further contributing to the tourism, transport, and communications sectors.

Available employment opportunities

Another 40 vacancies were advertised in June close to the 41 vacancies in May and mostly for public administration. Despite the Government's initiative to tighten the wage bill, the on-going vacancies advertised suggest labour migration either to the private sector or overseas. Liaison with businesses indicates labour shortages in the local market due to the impact of the increase in Tongans participating in the New Zealand and Australia seasonal workers schemes. Labour shortages may continue as Australia and New Zealand expand the seasonal workers scheme to other sectors.

Slow headline inflation in June

Table 1: Inflation Rates

Prices	Monthly		Annual	
	Jun-19	May-19	Jun-19	May-19
Headline Inflation (%)	0.2	0.8	1.8	1.6
Domestic prices	-0.3	-0.2	1.7	1.5
Imported prices	0.6	1.7	1.9	1.7

Source: Statistics Department

The monthly inflation rate further slowed in June to 0.2% compared with a higher 0.8% inflation in the previous month. A 0.3% decline in domestic prices was driven by a substantial fall in the price of Kava-Tonga and domestic food prices over the month by 4.1% and 0.4%, respectively. The price of Kava-Tonga declined to an average price of \$115.00 per kilogram whilst lower food prices were noted for eggs and vegetables such as tomatoes and head cabbages. This was however outweighed by a 0.6% increase in imported prices driven by a rise in the prices of imported meats such as chicken pieces, turkey tails, and mutton flaps.

Table 2: Items contributing to annual domestic inflation

Items (\$ per kg)	Monthly			Annual	
	Jun-19	May-19	Change	Jun-18	Change
Octopus	\$20.25	\$17.64	\$2.61	\$14.87	\$5.38
Yams-late	\$4.42	\$2.58	\$1.84	\$2.22	\$2.20
Tuna	\$17.00	\$16.49	\$0.51	\$15.00	\$2.00
Tomatoes	\$10.37	\$14.68	-\$4.31	\$8.42	\$1.95
Cockles (to'o)	\$6.86	\$5.21	\$1.65	\$5.23	\$1.63
stringed fish (mixed)	\$9.00	\$9.00	\$0.00	\$8.00	\$1.00
Eggs	\$17.67	\$19.63	-\$1.96	\$16.90	\$0.77
Cassava	\$1.28	\$1.12	\$0.16	\$0.70	\$0.58
Kava	\$115.00	\$121.25	-\$6.25	\$150.00	-\$35.00

Source: Statistics Department

The annual headline inflation was 1.8% in June, compared to 3.0% in the same period last year. Both imported and domestic prices rose over the year by 1.9% and 1.7%, respectively. Imported inflation contributed 1.0% to the annual headline inflation due to higher prices of imported food, tobacco, alcohol, maintenance & repair of the dwellings and fuel. Domestic inflation contributed 0.8% to the annual headline inflation as higher prices were noted for food, tobacco and restaurant services.



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Major trading currencies strengthened against the TOP

Table 3: Exchange Rates

	Monthly			Annual	
	Jun-19	May-19	% Growth	Jun-18	% Growth
Nominal Effective Exchange Rate Index	91.8	92.4	-0.6	90.9	1.0
Real Effective Exchange Rate Index	106.3	106.8	-0.5	105.3	0.9

Source: National Reserve Bank of Tonga

The Nominal Effective Exchange Rate (NEER) index declined in June 2019 due to an appreciation of the NZD, AUD, FJD, JPY & EUR against the TOP. The Real Effective Exchange Rate (REER) also decreased during the month as Tonga's inflation rate is lower compared to some of its major trading partners. Annually, both the REER and NEER rose, which may impact the international competitiveness of exported goods and services.

Table 4: Bilateral Exchange Rates

	Jun-19	May-19	Jun-18
USD/TOP	0.4394	0.4353	0.4397
AUD/TOP	0.6274	0.6300	0.5985
NZD/TOP	0.6559	0.6689	0.6515
FJD/TOP	0.9437	0.9445	0.9211
JPY/TOP	47.3388	47.6849	48.6418
GBP/TOP	0.3467	0.3451	0.3365
EUR/TOP	0.3864	0.3909	0.3805
CNY/TOP	3.0218	3.0044	2.9139

Source: National Reserve Bank of Tonga

Higher overall balance due to official transfer receipts

Table 5: Foreign Reserves

	Monthly			Annual	
	Jun-19	May-19	% Growth	Jun-18	% Growth
Foreign Reserves (\$ in million)	484.3	468.3	3.4	468.7	3.3
Import Coverage (months)	8.1	7.9		8.0	

Source: National Reserve Bank Tonga

Official foreign reserves rose by \$16.0 million in June 2019 to \$484.3 million, equivalent to 8.1 months of imports cover, as expected funds for budgetary support were received prior to the closing of the fiscal year.

Table 6: Overseas Exchange Transactions
Overseas Exchange Transactions

	Monthly			Annual		
	Jun-19	May-19	% Growth	Jun-19	Jun-18	% Growth
Overall Balance	16.0	4.1	290.5	15.6	60.9	-74.4
Current Account	8.6	5.1	69.6	-13.9	21.0	-166.3
Merchandise Trade	-35.5	-36.3	-2.4	-424.4	-386.1	9.9
Services	4.0	0.3	1190.4	32.2	32.3	-0.2
Income	-16.0	2.5	-734.9	-2.4	-7.7	-68.3
Transfers	56.1	38.6	45.5	380.7	382.5	-0.5
Capital Account	9.1	4.7	93.7	42.1	40.6	3.7
Financial Account	-1.7	-5.7	-70.1	-12.6	-0.7	1646.6

Source: Banking Systems

The overall Overseas Exchange Transactions (OET) balance edged higher in June 2019, as a result of the receipt of budget support and government projects, totaling to \$40.4 million. Other receipts such as interbank receipts and services for construction and telecommunication also rose. These outweighed the decline in receipts from private transfers, travel, and exports. At the same time, payments for investments abroad of \$11.2 million and dividends of \$6.8 million contributed to the increase in total payments.

In year ended terms, 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, income, and official receipts.

Broad money expanded

Table 7: Broad Money

	Monthly			Annual	
	Jun-19	May-19	% Growth	Jun-18	% Growth
Broad money (\$ in million)	600.1	584.8	2.6	575.4	4.3
Net Foreign Asset	506.3	488.8	3.6	485.3	4.3
Net Domestic Asset	94.2	96.4	-2.3	90.3	4.4

Source: Banking System, National Reserve Bank of Tonga

Net foreign assets hiked in response to the rising foreign reserves in June, thus further expanding Broad Money. Meanwhile, net domestic assets declined over the month, due mainly to higher government deposits, although it increased over the year, mainly on higher credit to the private sector.

Liquidity declined in June

Table 8: Reserve money

	Monthly			Annual	
	Jun-19	May-19	% Growth	Jun-18	% Growth
Reserve money (\$ in million)	302.2	311.0	-2.8	317.7	-4.9

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the banking system fell over the month and year by \$8.8 million (2.8%) and \$15.5 million (4.9%) respectively to \$302.2 million. These were mostly driven by the decline in the exchange settlement accounts mainly on withdrawals for investments abroad, and to cater for the June festivities. The required reserves also fell supporting the monthly decline. The banks' total loans to deposit ratio fell from 78.7% to 77.9% over the month, reflecting declining loans against increasing deposits.

Credit remained high despite the slight decline

Table 9: Total Lending

Lending	Monthly			Annual	
	Jun-19	May-19	% Growth	Jun-18	% Growth
Total Lending (\$ in million)	486.3	487.3	-0.2	447.3	8.7
Business lending	226.9	227.9	-0.4	199.9	13.5
Household lending	257.7	257.8	-0.1	247.7	4.0
Other lending	0.4	0.3	34.1	0.9	-52.6

Source: Banking System, National Reserve Bank of Tonga

The total banks' lending slightly fell by 0.2% over the month yet increased over the year to \$486.3 million. The partial write off of non-performing business loan in the construction and tourism sector led the monthly movements. The decline in lending to the agricultural and fisheries sectors, and households also contributed to the monthly fall in lending. However, the expansion of lending to both businesses (transport, professional & other services & distribution) and household (housing and other personal loan) drove the 8.7% annual growth. This is lower than the previously anticipated 13% annual growth and is mainly due to delays and cancellation of some projects, coupled with few debts written off. However, the excess liquidity in the banking system remains and there is still available capacity for further lending.



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Weighted average interest rate spread widened

Table 10: Weighted Average Interest Rates

Interest Rates	Monthly			Annual	
	Jun-19	May-19	Growth (bps)	Jun-18	Growth (bps)
Weighted Average Banks Deposit Rate (%)	1.939	1.956	-1.7	2.042	-10.3
Weighted Average Banks Lending Rate (%)	8.029	8.044	-1.5	8.026	0.4
Weighted Average Interest Rate Spread (%)	6.090	6.088	0.2	5.983	10.7

Source: Banking System, National Reserve Bank of Tonga

The weighted average interest rate spread widened over the month and year to 6.09%, by 0.2 basis points and 10.9 basis points, respectively. The monthly rise was largely driven by the decline in weighted average deposit rates outweighing the decrease in weighted average lending rates. Demand deposit rates decreased, offsetting the increase in saving and time deposit rates, whereas lower lending rates were mainly for the construction, tourism and agricultural sectors.

The annual rise was a result of the 10.3 basis points

decrease in weighted average deposit rates coupled with the 0.4 basis points rise in weighted average lending rates. Both demand and time deposit rates decreased and outweighed the increase in savings deposit rates, while the increase in lending rates were mainly for the manufacturing, distribution and utility sectors.

Outlook

The Reserve Bank expects domestic economic activity to remain positive in the medium term. Furthermore, foreign reserves is also expected to remain at comfortable levels, while inflation will continue to remain below the Reserve Bank's inflation reference rate of 5% per annum throughout 2019. The Reserve Bank will maintain its monetary policy stance, continue to closely monitor developments in the domestic and global economies, and make adjustments to its policies, to ensure financial and macroeconomic stability are maintained.