



COVID-19 severe impacts on the global economy

The IMF in its April 2020 World Economic Outlook indicated that global growth is expected to fall to -3.0% for 2020 projecting it to be the worst recession since the great depression and exceeding the 2009 Global Financial Crisis recession. This largely stems from the impacts of the COVID-19 pandemic affecting the tourism, trade, international travels, and other sectors of economies around the world. The US Bureau of Economic Analysis reported in January 2020 that the economy grew by 2.3% in 2019 driven mainly by lower import bills, but expects slower growth for 2020 amid the COVID-19 outbreak. The Reserve Bank of Australia reported in February 2020 that annual growth of 2.0% is projected for 2019 but expects the aftermath of the recent bushfires and COVID-19 to weigh down on GDP growth in the near-term due to the disruptions on exports, manufacturing, and other economic activities. Meanwhile, Westpac NZ in its February 2020 economic overview revised economic growth for New Zealand downwards to 0.1% from 0.7% for the first quarter of 2020 taking into account the impacts of COVID-19 on business activities. The severity of the COVID-19 pandemic continues to pose a risk on the global growth outlook for 2020.

Weaker domestic performance

The volume of agricultural exports rose in February 2020 by 245.4 tonnes (71.9%) due to higher exports of root crops, mostly cassava and taro. Receipts of export proceeds for agricultural changed little over the month while marine proceeds increased by \$0.2 million (38.8%), supporting growth in the primary sector. Partial data indicates a slowdown in the industry sector as both electricity consumption and production declined by 13.2% and 3.9% in February. Meanwhile, the number of electricity consumers slightly rose coinciding with the \$1.1 million (0.6%) rise in lending for individual housing.

On the other hand, the services sector is already showing signs of impacts from COVID-19. Travel restrictions, health risks and additional security measures has discouraged travelers from travelling overseas. While February is a slow month for tourists in Tonga, the hotels and accommodation businesses reported that occupancy rates in February were lower than the usual. The Government diverted few of the cruise ships that was scheduled to arrive in Tonga during February raising concerns from the Tourism sector. International arrivals reported for the month dropped significantly by 5,416 passengers (46.1%) reflected in the decline in travel receipts by \$1.2 million (11.1%). Trade also slowed down with container registrations dropping yet again by 247 registrations (29.5%). Both private and business containers fell respectively by 78 (24.7%) and 169 (32.4%) registrations. Vehicle registrations also decreased by 22 registrations (8.9%). Consequently, payments for imports of wholesale & retail goods, oil and motor vehicles also declined in February. As the country shifts its focus to securing the health of its people, the economy is expected to undergo significant losses in the process.

Temporary unemployment expected

The Reserve Bank survey shows a rise in vacancies being advertised in February 2020 by 15 job vacancies (34.9%) mostly for public administrations. However, the private sector, specifically the tourism sector, has indicated laying off of some of their employees due to reduced activity. They expect to face more dire situations should Government enforce more security measures such as Border or National lockdowns in the coming months.

Low inflation maintained in February

Table 1: Inflation Rates

Prices	Monthly		Annual	
	Feb-20	Jan-20	Feb-20	Feb-19
Headline Inflation (%)	0.3	-0.3	0.8	3.2
Domestic prices	0.7	-0.6	-3.1	8.5
Imported prices	0.0	0.0	4.1	-1.0

Source: Statistics Department

Headline inflation rose by 0.3% over the month as domestic prices increased by 0.7% while imported prices remained stable during the month. Higher domestic prices were solely driven

Table 2a: 'Monthly average prices of selected domestic items'

Items (\$ per kg)	Unit	Monthly		
		Feb-20	Jan-20	Change
Tomatoes	1kg	\$15.23	\$5.83	\$9.40
Capsicum	1kg	\$17.46	\$10.42	\$7.04
H/Cabbage	1kg	\$5.57	\$3.00	\$2.57
Talo - Futuna	1kg	\$1.35	\$1.25	\$0.10
Sausages	1kg	\$8.40	\$8.33	\$0.07
Carrots	1kg	\$2.45	\$2.43	\$0.02

Source: Statistics Department

by the 2.5% increase for local food prices which contributed 0.4% to the monthly movement. More specifically, prices for local vegetables drove the monthly rise. Meanwhile, imported prices changed little over the month.

Annual inflation for February was at 0.8% compared to 0.6% in January 2020 and 3.2% in February 2019. Higher import prices is attributed to higher prices for food, transport and alcoholic beverages.

Table 2b: Annual average prices of selected items'

Items (\$ per kg)	Unit	Annual		
		Feb-20	Feb-19	Change
Domestic				
Kava	1kg	\$72.50	\$140.00	-\$67.50
Octopus	1kg	\$19.71	\$22.10	-\$2.39
Carrots	1kg	\$2.45	\$4.72	-\$2.27
Imported				
Mutton flaps	1kg	\$16.61	\$15.38	\$1.23
Chicken pieces	1kg	\$2.86	\$2.67	\$0.19
Sugar	1kg	\$1.79	\$1.65	\$0.14

Source: Statistics Department

Imported food prices were highest for sugar, mutton flaps, and chicken pieces. However, domestic prices fell by 3.1% over the year, partially offsetting the 4.1% rise in imported prices. Lower domestic prices were significant for kava Tonga followed by local food items.

Competitive exchange rates

Table 3: Effective Exchange Rates

	Monthly			Annual	
	Feb-20	Jan-20	% Growth	Feb-19	% Growth
Nominal Effective Exchange Rate Index	93.2	91.7	1.6	91.1	2.3
Real Effective Exchange Rate Index	108.8	106.4	2.2	107.3	1.3

Source: National Reserve Bank of Tonga



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Table 4: Bilateral Exchange Rates

	Feb-20	Jan-20	Feb-19
USD/TOP	0.4319	0.4354	0.4431
AUD/TOP	0.6453	0.6327	0.6183
NZD/TOP	0.6735	0.6576	0.6474
FJD/TOP	0.8972	0.8987	0.8992
JPY/TOP	47.4170	47.4876	48.8303
GBP/TOP	0.3318	0.3319	0.3397
EUR/TOP	0.3949	0.3911	0.3898
CNY/TOP	2.8096	2.8329	2.8829

Source: Banking Systems

In February 2020, the USD, JPY, GBP and FJD appreciated against the TOP which resulted in a higher Nominal Effective Exchange Rate (NEER) over the month and year. The Real Effective Exchange Rate (REER) index, also increased over the month and year indicating a loss in Tonga's international trade competitiveness.

The overall OET deficit declined due to lower payments

Table 5: Foreign Reserves

	Feb-20	Monthly Jan-20	% Growth	Annual Feb-19	% Growth
Foreign Reserves (\$ in million)	479.8	482.9	-0.6	473.5	1.3
Import Coverage (months)	7.4	7.5		7.9	

Source: National Reserve Bank Tonga

The official foreign reserves declined over the month by \$3.0 million to \$479.8 million, equivalent to 7.4 months of imports. However, the receipts of budget support, grants, and project funds from development partners pushed the foreign reserves higher by \$6.4 million over the year.

Table 6: Overseas Exchange Transactions
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	Monthly			Annual		
	Feb-20	Jan-20	% Growth	Feb-20	Feb-19	% Growth
Overall Balance	-3.0	-4.6	33.5	6.4	25.5	-75.0
Current Account	4.1	-8.5	148.0	-2.0	-9.6	78.9
Merchandise Trade	-30.1	-34.9	13.6	-406.2	-420.4	3.4
Services	4.4	4.9	-10.9	34.6	11.0	213.3
Income	1.5	-1.2	222.9	2.0	7.7	-73.3
Transfers	28.3	22.7	24.8	367.6	392.1	-6.3
Capital Account	1.6	2.0	-18.2	31.6	33.4	-5.4
Financial Account	-8.7	2.0	-547.5	-8.6	-4.4	-95.0

Source: Banking Systems

Lower total payments in February 2020 recorded a lower deficit in the overall Overseas Exchange Transactions (OET). The current account surplus was \$4.1 million compared to an \$8.5 million deficit last month. Payments from the current account fell by \$11.0 million led by imports and income payments, followed by services and transfers payments. Lower import payments were mostly for oil & wholesale & retail goods. The current account receipts rose over the month, mainly on official transfer receipts which are grants and budget support.

The lower capital account surplus stemmed from lower capital receipts as there were no capital payments made during the month. However, the financial account recorded a deficit in February 2020 compared to a surplus in January 2020 attributed mainly to interbank movements.

In the year ended terms, the overall OET balance surplus fell to \$6.4 million due mainly to a lower surplus and deficits in the capital and financial accounts, respectively. These were driven by lower private capital transfer receipts and higher payments for offshore investment. The current account deficit improved over the year, owing to lower

payments for imports and services whilst travel receipts and private transfer receipts increased.

Broad money declined

Table 7: Broad Money

	Monthly			Annual	
	Feb-20	Jan-20	% Growth	Feb-19	% Growth
Broad money (\$ in million)	590.1	592.5	-0.4	589.0	0.2
Net Foreign Asset	494.9	495.7	-0.2	492.6	0.5
Net Domestic Asset	95.7	97.3	-1.6	96.8	-1.1

Source: Banking System, National Reserve Bank of Tonga

Broad money fell over the month mainly on decreased domestic assets. This was due to higher lending to the public sector. Net foreign assets continued to fall as foreign reserves declined. Over the year, broad money rose due to higher net foreign assets as a result of the receipts of budgetary support and grants from development partners which drove the foreign reserves higher. This was partly offset by a decline in net domestic asset and attributed to higher government deposits.

Liquidity lowered over the month

Table 8: Reserve money

	Monthly			Annual	
	Feb-20	Jan-20	% Growth	Feb-19	% Growth
Reserve money (\$ in million)	297.9	301.3	-1.1	320.6	-7.1

Source: Banking System, National Reserve Bank of Tonga

The banking system remained sound over February 2020 although the liquidity in the banking system fell over the month and year to \$297.9 million. The monthly decline was due to lower deposits by the commercial banks to the Reserve Bank's vault. Yet, higher withdrawals from the Reserve Bank's vault by the commercial banks supported by lower required reserves and lower currency circulated contributed to the yearly decline.

Lower lending to businesses in February

Table 9: Total Lending

Lending	Monthly			Annual	
	Feb-20	Jan-20	% Growth	Feb-19	% Growth
Total Lending (\$ in million)	499.7	500.7	-0.2	483.7	3.3
Business lending	237.8	239.7	-0.8	222.6	6.9
Household lending	261.9	261.0	0.4	260.8	0.4
Other lending	0.0	0.0	0.0	0.3	-100.0

Source: Banking System, National Reserve Bank of Tonga

The banks' total lending declined by \$0.9 million over the month driven by lower business loans, while individual loans increased. The rise in individual lending were mostly for housing loans which was offset by a decrease in business loans for almost all sectors of the economy led by tourism, manufacturing, and construction. However, total lending rose over the year as both loans to business and individual increased. The annual trend resulted from lending to the agricultural, professional & other services, and transport sectors supported by individual housing loans.

Deposits also declined over the month more than the decline in loans, which led to a rise in the banks' total loans to deposit ratio from 81.1% in the previous month to 82.2% this month.



Weighted average interest rate spread narrowed

Table 10: Weighted Average Interest Rates

Interest Rates	Feb-20	Monthly		Annual	
		Jan-20	Growth (bps)	Feb-19	Growth (bps)
Weighted Average Banks Deposit Rate (%)	2.038	2.000	3.9	1.902	13.6
Weighted Average Banks Lending Rate (%)	8.015	8.033	-1.8	8.109	-9.4
Weighted Average Interest Rate Spread (%)	5.977	6.034	-5.7	6.207	-23.0

Source: Banking System, National Reserve Bank of Tonga

Over the month, the weighted average interest rate spread narrowed by 5.72 basis points due to lower weighted average lending rate, mainly business loans such as agriculture, tourism, and distribution sectors. This offsets the increase in saving, demand, and term deposit rates.

The weighted average interest rate spread also narrowed over the year largely attributed to a decline in weighted average lending rates which compared to the increase in weighted average deposit rates. The decrease in weighted average lending rates were mainly on business loans for the agriculture and tourism sectors. This was also supported by lower rates for individual loans. On the other hand, the weighted average deposit rates increased due to a rise in term deposit rates.

Outlook

While Tonga struggles with its preparations for COVID-19, TC Harold in April left major damages to households,

businesses and the infrastructure in 'Eua and the western side of Tongatapu. The Reserve Bank expects the economy to suffer a major set back by the end of 2019/20.

For the monetary indicators, the Reserve Bank projects the foreign reserves to remain at sufficient levels above the minimum of 3 months of import cover sustained by expected receipts of budget support. Inflation is forecasted to stay below the Reserve Bank's reference rate of 5% as global oil prices are expected to fall and partially offset the expected increases on other imported goods. Meanwhile, credit growth is projected to continue at a slower pace.

The Reserve Bank maintains its accommodative monetary policy stance for the near to medium term. Additional measures have been put in place to assist the Government and the commercial banks in their economic relief efforts through moratoriums and encouraging the utilization of the excess liquidity in the banking system to support economic activities and growth. The Reserve Bank remains vigilant by closely monitoring developments of COVID-19 in the domestic and global economies and stands ready to adjust its monetary policy setting to ensure financial and macroeconomic stability are maintained.