



# NATIONAL RESERVE BANK OF TONGA

## MONTHLY ECONOMIC UPDATE

Vol. 9

No. 10

Month Ended: October 2022

### Inflation in major trading partners continue to increase

The United States inflation increased by 7.7% over the year to October 2022 primarily driven by gasoline and food prices. Food prices in New Zealand rose by 10.1% in the year to October 2022, as reported by the New Zealand Statistics, driven by meat, poultry and fish prices. Reserve Bank Australia raised the cash rate target again in October to 2.60%.

### Domestic performances improved in October

The primary sector performance were more upbeat in October 2022. Harvesting seasons for squash and watermelons drove the 136.7% (718.0 tonnes) increase in the total agricultural exports. In addition, higher exports of cassava and kava Tonga also contributed to the monthly rise. The marine exports also increased in the same month by 101.5 metric tons (869.3%), stemming from higher tuna exports. This reflects the gradual return of foreign fishing vessels to Tonga, and the increasing capacity available for airfreight exports. Aquarium exports also rose by 4.4%, further supporting the fisheries sector. In year ended-terms, both agricultural and marine exports are still lower by 19.7% (2,023.3 tonnes), and 47.7% (707.4 metric tons), respectively, due to the impacts of the HTHH disaster and the border lockdowns.

Indicators in the industrial sector continued to show positive outcomes. The construction sector benefitted from the implementation of donor-funded projects including the Queen Salote Wharf Upgrade, and the new Tonga Police Workshop. Private projects such as the new Tonga High School sports complex also contributes to the sector's growth. Banks' lending to construction businesses rose by 0.4% (\$0.1 million) over the month, with more loan commitments for individual housing and construction projects. Additionally, provision of asphalt distributor trucks for road works by Japan Government will further support the infrastructure projects. The utility sector performance may be improved further by the progressive transitions to renewable energy, with the commissioning of Tonga's first large scale Battery Energy Storage System in October.

The service sector is also more active with higher travel and domestic trading activities. Travel receipts rose by 6.3% (\$0.5 million) coinciding with the arrival of several cruise ships in October. Container registrations also rose by 68.3% (493 containers) from both businesses and private containers, as businesses stock up for the Christmas season. Vehicle registrations also increased by 29.6%.

### Lower job vacancies advertised

The Reserve Bank's job survey recorded a 30.9% (34 job vacancies) decline in the number of job vacancies advertised during the month. Majority of the advertised vacancies were in the public administrations, and transport & communications sector. The job vacancies advertised over the year, still rose by 409 job vacancies (133.7%). New

Zealand also announced an additional 3000 places for the Regional Seasonal Employer Scheme (RSE), which may attract more participants in the labour mobility schemes, putting pressure on domestic labour supply.

### Inflation declined over the month

Inflation declined in October 2022 by 0.5%, owing to decreases in both imported and local prices. The

Table 1: Inflation Rates

Prices	Monthly		Annual	
	Oct-22	Sep-22	Oct-22	Oct-21
Headline Inflation (%)	-0.5	0.3	12.9	7.2
Domestic prices	0.0	2.3	16.2	6.3
Imported prices	-0.8	-1.3	10.4	7.8
Core inflation - ex. energy and imported food (%)	-0.1	2.5	12.1	3.2

Source: Tonga Statistics Department

monthly fall in domestic prices was driven by lower prices of local food items such as root crops, sea food, and vegetables. Harvesting season of various agricultural products has eased the pressure on the domestic food prices. At the same time, lower imported prices were from food items, fuels, liquefied petroleum gas, and clothing & footwear. The decline in the fuel prices moves in line with the declining global oil prices, in addition to Government subsidies on fuel which was extended until mid-October.

The headline inflation rose by 12.9% over the year, driven by higher domestic and imported prices. The domestic inflation contributed 7.0% to the headline, mostly from higher prices of food items, electricity, local transport services, takeaway food, communication related services, and labour cost. The Government also extended its subsidy on electricity consumption, which helps in protecting poor and vulnerable households against the higher energy prices. Imported inflation contributed 5.9% to the headline, driven by higher prices of fuels, food items, construction materials, goods for personal care, alcoholic beverages, and liquefied petroleum gas.

The core inflation (excluding energy and imported food items) was at 12.1% in October 2022, substantially higher than 3.2% in the previous year. This clearly indicates the susceptibility of local food supply to natural disasters, and broadening inflationary pressures on non-oil and non-food items.

### Major trading currencies appreciated against TOP

Table 2: Effective Exchange Rates

	Monthly			Annual	
	Nov-22	Sep-22	% Growth	Nov-21	% Growth
Nominal Effective Exchange Rate Index	94.9	96.8	-1.9	89.9	5.6
Real Effective Exchange Rate Index	119.9	122.9	-2.4	108.0	11.1

Source: National Reserve Bank of Tonga

The Nominal Effective Exchange Rate (NEER) declined over the month reflecting the general appreciation of the AUD, NZD, FJD, JPY, GBP and EUR against the TOP (month ended). Consequently, the Real Effective Exchange Rate (REER) also declined over the month.



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In year ended terms, the NEER increased as trading partners' currencies generally weakened against the TOP, except the USD. This may assist in partially offsetting some of the impacts of the higher imported inflation, particularly non-USD denominated imports. The REER also increased over the year in line with the higher NEER and Tonga's relatively higher inflation rate than its trading partner countries. This implies that Tongan exports is becoming more expensive thus impacting Tonga's trade competitiveness.

### Foreign reserves declined in October

Table 3: Foreign Reserves

	Monthly			Annual	
	Oct-22	Sep-22	%Growth	Oct-21	% Growth
Foreign Reserves (\$ in million)	877.0	895.3	-2.0	757.0	15.8
Import Coverage (months)	13.9	14.2	-2.3	12.8	8.9

Source: National Reserve Bank Tonga

Foreign reserves declined over the month of October 2022 by \$18.3 million to \$877.0 million, equivalent to 13.9 months of imports. This stemmed mostly from higher outflows for import payments. Annually, foreign reserves still increased markedly by \$119.9 million attributed to higher receipts of budget support, official grants, capital inflows, and remittances. The majority of the official foreign reserves are held in USD, NZD, and AUD.

Table 4: Remittance and Travel Receipts

	Monthly			Annual		
	Oct-22	Sep-22	% Growth	Oct-22	Oct-21	% Growth
Remittance (\$ in million)	41.0	43.7	-6.1	473.9	485.5	-2.4
Travel (\$ in million)	7.7	7.3	6.3	38.0	21.1	80.6

Source: National Reserve Bank Tonga

Total remittance receipts declined again over the month and year by \$2.6 million (6.1%), and \$11.6 million (2.4%), respectively. This was underpinned by the lower private transfers and compensation of employees. Rising cost of living and the economic slowdown in our source remitting countries may affect remittance inflows, coupled with the diversion of personal transfers to travel receipts.

### Broad money remain steady

Table 5: Broad Money

	Monthly			Annual	
	Oct-22	Sep-22	%	Oct-21	%
Broad money (\$ in million)	843.4	843.4	0.00	789.7	6.8
Net Foreign Asset	860.9	875.0	-1.6	743.1	15.9
Net Domestic Asset	-17.0	-31.2	45.5	47.5	-135.8

Source: Banking System, National Reserve Bank of Tonga

Broad money remained steady over the month, while increasing over the year by \$53.7 million (6.8%). Net domestic assets increased during the month, driven by higher net credit to central government from lower government deposits. Net foreign assets however, declined from the lower foreign reserves. Annually, net foreign assets increased, in line with movements in foreign

reserves, which more than offset the drop in net domestic assets.

### Liquidity in the financial system declined

Table 6: Reserve money

	Monthly			Annual	
	Oct-22	Sep-22	%	Oct-21	%
Reserve money (\$ in million)	603.3	611.6	-1.4	534.3	12.9

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the financial system decreased again in October by \$8.3 million (1.4%), but still increased annually by \$69.0 million (12.9%). The Exchange Settlement Account (ESA) decreased the most over the month, attributed to lower deposits to the Reserve Bank vault. Currency in circulation and Statutory Reserve Deposits (SRD) also fell supporting the monthly decline. Annually, the ESA, currency in circulation, and SRD all rose.

### Credit growth declined

Table 7: Total Lending

Lending	Monthly			Annual	
	Oct-22	Sep-22	Growth	Oct-21	Growth
Total Lending (\$ in million)	478.8	482.3	-0.7	476.7	0.4
Business lending	221.3	225.9	-2.0	218.6	1.2
Household lending	255.1	254.0	0.4	257.8	-1.1
Other lending	2.4	2.4	-0.8	0.3	801.9

Source: Banking System, National Reserve Bank of Tonga

The banks' total lending fell over the month by \$3.5 million (0.7%). While new loans particularly from the Government Development Loan (GDL) scheme were extended in October, the exit of some of the Public Enterprise loans from the banking system was the main driver of the decline.

However, over the year, the annual credit growth was still positive rising by \$2.1 million (0.4%). This was driven mostly by more loans issued to businesses in retail distribution, construction, and agricultural sector, together with individual vehicles loans.

The banks' total deposits increased by \$6.1 million (0.7%) and \$74.0 million (9.2%) respectively, over the month and year to October 2022, to a total of \$862.6 million. The monthly rise was driven mostly by higher deposits from private businesses and the retirement funds. Similarly, higher deposits from private businesses and the non-profit organisations led the annual rise. Relative to the weaker lending growth, the loans-to-deposit ratio fell to 54.3%, compared to 55.1% last month and 59.1% last year.

### Widening weighted average interest rate spread

Table 8: Weighted Average Interest Rates

Interest Rates	Monthly			Annual	
	Oct-22	Sep-22	(bps)	Oct-21	(bps)
Weighted Average Banks Deposit Rate (%)	1.631	1.656	-2.5	1.837	-20.6
Weighted Average Banks Lending Rate (%)	8.209	7.878	33.0	7.845	36.4
Weighted Average Interest Rate Spread (%)	6.578	6.223	3.0	6.008	57.0

Source: Banking System, National Reserve Bank of Tonga

Over the month and year to October 2022, the weighted average interest rate spread widened further to 6.58%. The



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weighted average lending rate increased over the month, mostly from lending to businesses in the agricultural, distribution, and transport sectors, and also for household housing loans. The lower volume of loans over the month may have also contributed to the higher weighted average lending rate. On the other hand, the weighted average deposit rate fell reflecting the growing deposit volumes.

Annually, lending rates offered to businesses in the agricultural, construction and distribution sectors increased, as well as the loan rates issued to households for vehicle and housing loans. Rising deposit volumes over the year continued to put pressure on the weighted average deposit rates.

### Outlook

The economic indicators continue to be inline with the NRBTs expectations that the Tongan economy is to gradually recover in FY2022/23, supported by the reconstruction from the HTHH disaster, the implementation of development projects, and the re-opening of the international borders. Global economic growth has

weakened while inflation remains elevated. This has triggered aggressive monetary policy tightening in many advanced economies resulting in volatile exchange rate markets. The high inflation in our overseas trading partners and volatile exchange rates have passed through to Tonga's inflation. However, headline inflation is forecasted to cool off in the last quarter of 2022 then gradually ease towards the reference rate in 2023. This is based on the expectation that global oil prices will continue on its downward path, global supply demand mismatches phase out, freight rates decline, and domestic food supply recovers. Imports are projected to strengthen in line with the economic recovery, while remittance receipts and inflows from donor funds returns to pre-pandemic levels. Meanwhile, foreign reserves levels will still remain comfortable above the minimum 3 months of imports cover, supported by inflows of budget support and donor funds. The financial system remains stable with ample liquidity available as credit growth improves. Banks are also well capitalized to absorb further deteriorating asset quality from rising non-performing loans.