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14 November 2019

Monetary Policy Decision

The National Reserve Bank of Tonga's Board of Directors at its board meeting on the 11th November 2019, approved to maintain its current monetary policy measures outlined below. This is to encourage utilization of the excess liquidity in the banking system, through further lending in order to support economic growth and strengthen the monetary policy transmission mechanism.

- a. maintain the monetary policy rate at 0% (zero interest rate policy);
- b. maintain the minimum loans/deposit ratio of 80%;
- c. maintain the Statutory Reserve Deposit ratio at 10%, and
- d. maintain the inflation reference rate at 5%.

The Governor of the Reserve Bank, Sione Ngongo Kioa, indicated that domestic economic activities continued to vary in September 2019. Export of fish and marine products doubled over the month by 344.8 tons mainly driven by tuna exports. The agricultural sector showed a decline over the month reflected by a fall in agricultural proceeds of \$0.3 million (23.4%), however local supply of root crops and kava Tonga improved and is reflected in the lower prices. On the other hand, activities in the industry sector is slowing as reflected in the declined lending to the construction, mining & quarrying, manufacturing and utility sectors. Individual housing loans also declined in September, however rose over the year. The services sector showed mixed growth yet again, with declines in both international air arrivals and departures in September while container registrations increased. Vehicle registrations continued to decline.

The banking system continues to be sound supported by strong capital and adequate profits. The banks' total loans to deposit ratio slightly decreased from 79.0% to 78.6% over the month, reflecting loans decreasing more than the decrease in deposits. This still remains close to the 80% minimum loan to deposit ratio. However, the liquidity in the banking system remains relatively high indicating existing capacity is still available for further lending. The weighted average interest rate spread narrowed to 6.06% due to a decrease in weighted average lending rates coupled with an increase in weighted average deposit rates.

The official foreign reserves fell by \$0.9 million in September to \$490.8 million, (equivalent to 7.9 months of imports cover) due to a net outflow in foreign exchange deals with commercial banks to cater for customers' overseas payments during the month. Annually, foreign reserves rose by \$38.7 million due net inflows from budget support, project funds and remittances.

A monthly deflation was recorded for September 2019 of 0.1% and owing mostly to lower domestic prices of kava-Tonga and local food items such as root crops and vegetables. However, import prices rose over the month and was driven mostly by the increases in fuel prices and imported food items. Annual headline inflation returned in September 2019 by 0.4% compared to a 0.1% deflation in August 2019, and 5.5% inflation in September 2018. This was due to higher imported inflation offsetting the lower domestic prices.

The medium-term outlook on Tonga's economic performance remains positive, yet weather uncertainty and global uncertainties continue to pose a risk to this expectation. The level of foreign reserves is projected to remain at a comfortable level, and inflation is expected to remain below the reference rate of 5%. The banking system is anticipated to continue to remain sound.

Given the above developments and outlook, the current monetary policy stance is considered appropriate in the medium term. The Reserve Bank continues to adopt measures to encourage the utilization of the excess liquidity in the banking system to increase lending, support domestic economic activities, and strengthen the monetary policy transmission mechanism. Meanwhile, the Reserve Bank will continue to remain vigilant and closely monitor external and domestic developments and may change its monetary policy setting to support its monetary policy objectives.

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