NATIONAL RESERVE BANK OF TONGA

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OFFICIAL PRESS RELEASE

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Monetary Policy Decision

The National Reserve Bank of Tonga's Board of Directors at its first board meeting for the year, on the 31st of March 2021, 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 to growth sectors and to support the economy from the impacts of COVID-19.

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%.
d. Maintain the inflation reference rate at 5%.
e. Monitor the commercial banks' liquidity and adjust the SRD ratio if needed.
f. Monitoring the commercial banks' capital reserves and adjust further when required.
g. Ease the exchange control requirements when required.
h. Continue to issue Government Bonds.
i. Maintain clear channels of effective communications with the financial institutions for adequate preparedness.
j. Continue to be transparent and raise awareness of its monetary policy decisions through press releases to the public.
k. Closely monitor the impacts of the pandemic in the financial system for early detection of any signs of vulnerability.
l. Continue to ensure both commercial banks and non-bank financial institutions adheres to all Government declarations regarding COVID-19 in the workplace while delivering essential financial services to the public.

The Governor of the Reserve Bank, Sione Ngongo Kioa, shared that there was generally a domestic slowdown in January 2021. The primary sector reported a decline in total agricultural exports largely driven by the decrease in export of root crops such as cassava, taro, yam, and squash. Agricultural export proceeds also declined during January 2021 aligning with decline in volume of exports. Lending to the construction sector decreased coinciding with the decline in import payments for construction materials whilst growth in the services sector dropped further in January 2021. The total container registrations declined significantly as a result of both lower business and private container registrations indicating a slowdown in trading activities following the festive season.

Inflation increased by 0.7% in January 2021 due to higher imported and domestic prices (particularly fuel and food items). The annual inflation rate for January 2021 rose by 1.3%. This was due to both higher imported and domestic prices. Particularly, an increase in prices for food, tobacco and alcoholic beverages (imported prices) whilst higher prices for food, tobacco, and clothing & footwear drove domestic prices higher.

Official foreign reserves rose in January 2021 by $29.7 million to $705.3 million and equivalent to 12.0 months of imports. This was due to receipt of a government loan from the IMF Rapid Credit Facility. Funds related to COVID-19 and TC Harold were also received. Similarly, foreign reserves increased significantly in the year to January 2021 by $222.4 million. This was largely a result of budget support, official grants, and remittances.

The total banking system maintained its soundness supported by strong capital and excess liquidity. The banks' total lending slightly fell in the month whilst the level of deposits continued to rise. Consequently, the loans to deposit ratio was lower in January 2021, it fell to 67.8% from 68.6% last month and below the 80% minimum. The consistent decline of this ratio continues despite the excess liquidity in the system. The weighted average interest rate spread increased over the month by 1.0 basis points and declined by 32.8 basis points in the year to January 2021 to 5.709%.

The Reserve Bank's latest GDP forecast depicts a worse-than-expected outcome for 2019/20 and 2020/21 fiscal years. However, even with the revised forecasts, the level of foreign reserves is still expected to be above the 3 months minimum threshold of import cover, while inflation is to remain below the 5% reference rate. The banking system is still sound supported by high liquidity and capital positions. Meanwhile, the Reserve Bank continues to be vigilant in closely monitoring its economic and financial indicators and stands ready to adjust its monetary policy settings if needed to maintain internal and external stability and support macroeconomic growth.

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