

Banking Sector Developments

August 2016

Release date: 08 February 2017

	Aug 16	Jul 16	Jun 16	May 16
Deposit rate (%)*	2.219	2.217	2.27	2.22
Lending rate (%)*	7.90	7.92	7.879	7.877
Total Deposits (T\$m)	481.9	462.6	468.3	453.7
Total lending (T\$m) ^	355.2	351.9	352.3	348.7
New commitments (T\$m)	12.8	11.2	10.5	11.3
Broad Money (T\$m)	491.0	478.0	470.5	460.5

*Weighted Average calculated as a function of interest rate and volume of deposits and loans

^This series shows total lending from the banking sector only.

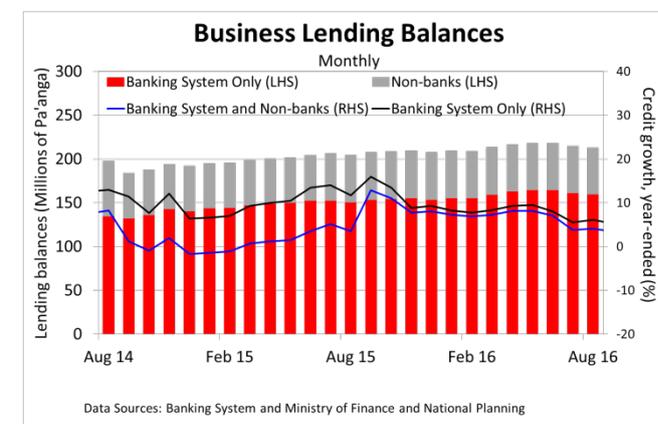
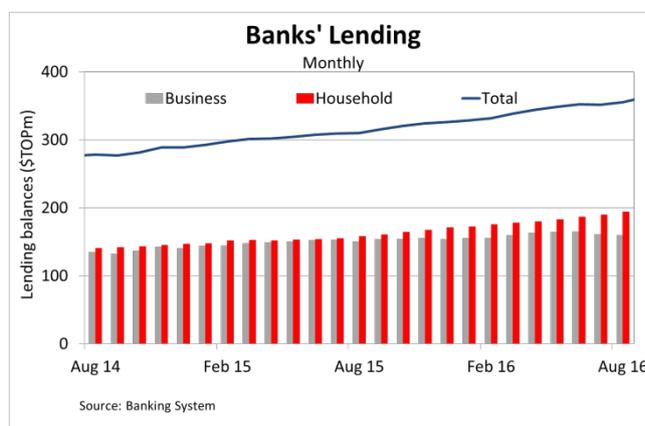
Household loans steered strong credit growth

Lending

A pick-up in total bank's lending by \$3.3 million (1.0%) has taken lending to \$355.2 million in August 2016, much higher than \$0.9 million (0.3%) growth in August 2015. This stemmed from an increase in lending to households, offsetting a decline in business loans. In year ended terms, both lending to households and businesses contributed to a marked increase of \$45.2 million (14.6%) in total bank lending with household loans contributing the most. Lending by the non-bank financial institutions also increased over the year by \$12.5 million (11.0%) to \$126.3 million. This was driven by higher loans to households which outweighed a decline in business lending.

Business lending

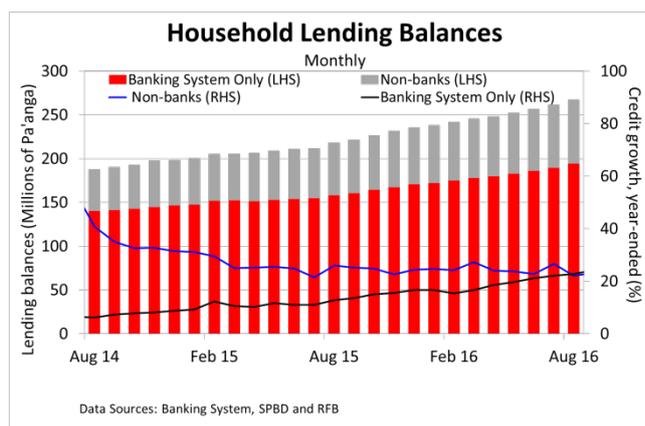
Over the month, banks' lending to businesses continued to decline by \$1.6 million (1.0%) to \$159.6 million. This was due mainly to a decrease in lending to the mining & quarrying, trade, manufacturing sectors as well as a decrease in loans to public enterprises. The write-off of a



large private business loan contributed to the monthly decline. However, total bank lending to businesses over the year increased by \$9.1 million (6.1%) largely led by higher loans to the tourism, construction, manufacturing, agricultural and trade sectors. The continuous support by government through its Government Development loan facility contributed to the annual growth. With the inclusion of government on-lent loans, annual business lending increased by \$8.4 million (4.1%), reflecting a decline in government on-lent loans driven by repayments during the year.

Household lending

Banks' lending to households continued to be the main contributor to both the monthly and annual growth in total bank lending. The ongoing competition among banks and continued high demand for loans due to more capacity for households to borrow may have boosted the growth in household lending over the month to a new record of \$194.3 million, increasing by \$4.8 million (2.5%). This has been the highest monthly growth in the year 2016 and much higher than the \$3.2 million (2%) growth in the same period last year. Housing loans increased over the month by \$5.0 million (3.7%) which offset a slight decrease in vehicle and other personal loans of \$0.04 million (5.1%) and \$0.1 million (0.2%) respectively. The growth in housing loans was also supported by a 1.3 basis points fall in the weighted average lending rate for housing loans over the month.



Annually, banks' lending to households also rose by \$36.1 million (22.8%). All lending categories increased, with housing loans rising by \$32.6 million (31.2%) followed by an increase in other personal loans of \$3.2 million (6.0%). This is due mainly to a number of possible reasons including more capacity for households to borrow as well as the different events taking place during the year such as annual church conferences and donations. The decrease in housing and other personal lending rates over the year by 44.3 and 4.9 basis points respectively, also supported the annual growth. Lending from non-bank financial institutions to households also increased over the year by \$13.2 million (22.2%), reflecting higher other personal loans. The introduction of home improvement loans by the Retirement Fund Board in July 2016 for its members also contributed to the monthly and annual growth.

Other lending

Other loans from banks rose over the month and over the year by \$0.1 million (8.3%) and \$0.02 million (2.0%) respectively, due mainly to lending activities within the non-profit institutions sector.

Non-performing loans

Banks' total non-performing loans continued to decline over the month by \$1.4 million (7.4%) to \$17.0 million, representing 4.8% of total loans. Both non-performing business and household loans declined over the month, with non-performing business loans decreasing the most by \$1.3 million

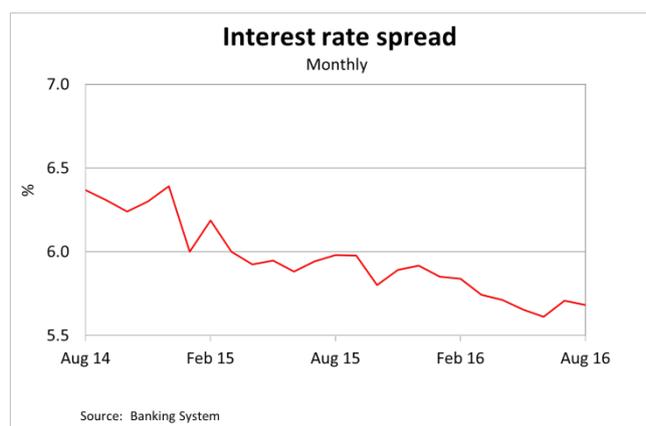
(12.0%). This was due mainly to the write-off of one major non-performing private business loan. Over the year, total non-performing loans fell by \$10.1 million (37.2%), resulting from a decline in non-performing business loans mainly from the mining & quarrying, tourism and trade sectors.

Deposits

Total bank deposits rose over the month by \$19.3 million (4.2%) to \$481.9 million. This was driven by a rise in all categories with time deposits recording the highest growth of \$8.1 million (4.6%), reflected higher time deposits of businesses. In year ended terms, total deposits rose by \$68.1 million (16.4%) driven by a rise in all categories with demand deposits rising the most.

Interest rate spread

The weighted average deposit rate changed a little in August while the weighted average lending rate fell by 2.13 basis points due to lower interest rates on housing and business loans. The weighted average interest rate spread therefore slightly narrowed to 5.68% from 5.71% last month. Over the year, the weighted average interest rate spread narrowed by 30 basis points, due mainly to a fall in the weighted average lending rate outweighing a decline in the weighted average deposit rate.



Broad money

Broad money reached another record high of \$491.0 million in August 2016, a rise of \$13.0 million (2.7%) from the previous month. This was largely attributed to a \$9.6 million (9.2%) rise in net domestic assets which was contributed by the growth in net domestic credit over the month. In addition, net foreign assets rose by \$3.6 million (1.0%) as holdings by banks with foreign banks increased due mainly to a large receipt of funds for foreign investment during the month. In year ended terms, broad money grew significantly by \$66.9 million (15.8%) as a result of a marked increase in net foreign assets by \$75.5 million (25.0%) outweighing a \$9.0 million (7.3%) fall in net domestic assets. The receipt of the Government's budget support funds and remittances during the year largely contributed to the higher foreign reserves and corresponded to the rise in net foreign assets.

Liquidity

The liquidity (reserve money)¹ in the banking system increased by \$1.7 million (0.6%) in August 2016 to \$267.2 million, due mainly to an increase in the banks' deposits to the NRBT vault. Meanwhile excess liquidity in the banking system remains as the banks' total loans to deposit ratio decreased to 73.7% in August from 76.1% last month, which is below the 80% minimum loan to

¹ Liquidity (reserve money) in the banking system is a sum of currency in circulation, exchange settlement account balances, and required reserve deposits.

deposit ratio target that was effective on 1st July 2016 to be achieved by December 2016. Over the year, banking system liquidity rose by \$20.9 million (8.5%) due mainly to a \$15.1 million (9.0%) rise in banks' deposits to the NRBT vault.

Outlook

The National Reserve Bank of Tonga in its February 2016 Monetary Policy Statement (MPS) estimated credit growth of about 11% in 2016/17. This forecast will be revised again and will be published in the August 2016 MPS. The NRBT's forecast is in line with the IMF Article IV's projected growth of 10.8% for 2016/17. The banks' prospects for credit growth remains positive and the NRBT's projection is supported by improving economic conditions, as well as annual and one-off events taking place during the year.

The NRBT forecasts the annual growth in broad money to rise by 10%, coinciding with the IMF's estimated growth projection of 9% for June 2017, which is supported by the anticipated increase in lending and foreign reserves.

The banks' loan to deposit ratio of 80% - 90% is anticipated to be achieved progressively over 18 months. This measure is to encourage the utilization of the excess liquidity in the banking system to increase lending, in order to support economic growth. At the same time, the NRBT is exploring alternative monetary policy and macro prudential tools to strengthen the policy transmission mechanism, and at the same time ensure financial stability is maintained. The NRBT will closely monitor the country's economic and fiscal developments and financial conditions to maintain internal and external monetary stability, and promote a sound and efficient financial system to support macroeconomic stability and economic growth.

Table 1:

Consolidated Balance Sheet of Depository Corporations							
	Level as at					Change over the last:	
	Aug-16 \$TOPm	Jul-16 \$TOPm	Jun-16 \$TOPm	May-16 \$TOPm	Aug-15 \$TOPm	1 month % growth	1 year % growth
Broad money liabilities	491.0	478.0	470.5	460.5	424.2	2.7	15.8
Currency in circulation	48.4	52.5	48.5	48.7	46.7	-7.8	3.7
Demand deposits	194.8	188.1	181.4	171.3	158.6	3.6	22.8
Savings and term deposits*	247.8	237.5	240.7	240.5	218.8	4.3	13.2
<i>equals</i>							
Net foreign assets	377.9	374.3	362.5	334.0	302.4	1.0	25.0
<i>plus</i>							
Net domestic assets	113.4	103.9	108.3	126.8	122.4	9.2	-7.3
Gross bank lending**	364.1	361.1	361.5	357.6	318.5	0.8	14.3
Public enterprises	40.0	40.4	46.1	45.8	46.0	-1.1	-13.0
Private Sector	308.7	305.1	299.7	296.1	257.9	1.2	19.7
Other financial corporation	15.4	15.6	15.7	15.7	14.6	-0.9	5.7
Other***	-250.7	-257.3	-253.2	-230.8	-196.1	-2.6	27.9

* Also includes very minor amounts for securities other than shares.

** Differs slightly from standard measures of bank lending by amounts classified as accrued interest.

*** Includes mostly capital accounts of the banks and NRBT, and their net claims on the central government.

Sources: Banking system; NRBT

Table 2:

	Lending Balances							Shares of totals %
	Level as at					Change over the		
	Aug 16 TOPm	Jul 16 TOPm	Jun 16 TOPm	May 16 TOPm	Aug 15 TOPm	1 month %	1 year %	
Lending, banks	355.2	351.9	352.3	348.7	310.0	1.0	14.6	100.0
Household	194.3	189.5	186.3	183.1	158.2	2.5	22.8	54.7
Business*	159.6	161.2	164.7	164.4	150.5	-1.0	6.1	44.9
Other	1.3	1.2	1.2	1.2	1.3	8.3	2.0	0.4
Lending, banks and other	481.6	476.8	476.2	471.6	423.8	1.0	13.6	100.0
Household	267.3	261.0	256.6	252.4	218.0	2.4	22.6	55.5
Business	212.9	214.6	218.3	218.1	204.5	-0.8	4.1	44.2
Other	1.3	1.2	1.2	1.2	1.3	8.3	2.0	0.4
New comm'ts, banks	12.8	11.2	10.5	11.3	10.5	14.4	22.0	N/A
Undrawn comm'ts, banks	17.6	18.7	16.1	18.6	20.6	-5.9	-14.7	N/A
Implied repay'ts, banks	10.5	9.0	9.3	8.4	16.6	17.3	-36.5	N/A

* Method for calculating these series was updated in August 2014, resulting in revisions to the full history of data

Sources: SPBD; RFB; MOFNP; Banking system

Table 3:

	Interest Rates							Share of loans/deposits %
	Level as at					Change over the last [^] :		
	Aug 16 %	Jul 16 %	Jun 16 %	May 16 %	Aug 15 %	1 month bps	1 year bps	
Deposits all	2.219	2.217	2.27	2.22	2.28	0.20	-6.26	100
Demand	0.40	0.42	0.52	0.41	0.36	-1.47	3.95	41
Savings	2.52	2.51	2.51	2.46	2.45	0.79	7.49	19
Term	3.92	3.93	3.98	3.86	4.07	-1.48	-15.69	40
Loans all	7.90	7.92	7.88	7.88	8.26	-2.13	-35.87	100
Housing	8.08	8.09	8.09	8.06	8.52	-1.31	-44.33	40.7
Other personal	11.00	10.96	10.95	10.91	11.41	4.16	-41.06	16.3
Business*	6.94	7.03	6.97	7.05	7.38	-9.04	-44.45	26.8
Other	6.54	6.25	6.25	6.25	6.25	28.58	28.58	16.2

*Method for calculating these series was updated in August 2014, resulting in revision to the full history of data

[^]Due to rounding errors some data may not aggregate precisely

Sources: Banks; NRBT