



# NATIONAL RESERVE BANK OF TONGA

## MONTHLY ECONOMIC REVIEW

Vol. 4

No. 10

Month Ended: October 2017

Global economic conditions varied over October. The Federal Reserve of the United States noted that economic activity expanded at a solid pace due to growth in the manufacturing sector and commercial construction. The Reserve Bank of Australia reported that retail sales in the country had been weak in the September quarter reflecting lower consumption growth. However, retail price inflation was low due to competitive pressures in the retail sector, particularly prices for volatile items such as fruit and vegetables. The Reserve Bank of New Zealand reported low house price inflation reinforced by new government policies on housing.

Domestic activity remained positive over the month of October with mixed partial indicators. This was supported by strong performance in the agricultural exports which rose by 2,360 tonnes mainly due to the squash season. On-going construction activities continued to boost performance in the secondary sector, which coincided with a 1.1% growth in individual housing loans. Electricity consumption also rose by 0.61 million kWh. On the other hand, economic activities in the tertiary sector slowed. Total air arrivals declined by 1,421 passengers (15.0%), in line with a \$1.6 million decrease in travel receipts. In addition, total number of container registrations decreased by 68 (6.2%), attributed to lower number of private containers. However, vehicle registrations slightly rose by 18 vehicles mostly on taxis and rentals reflected the preparation for the Christmas season. This contributed to growth in the transport sector and expected to have flow-on-effects for the distribution sector through oil consumption. The float parade for the Mate Ma'a Tonga's team and campaigning for the Rugby League World Cup and election contributed to this growth.

As a partial indicator of employment, the total number of job advertisements fell over October 2017 by 2 vacancies and over the year by 133 vacancies.

The headline inflation for October is yet to be released by the Statistics Department. However, the Reserve Bank expects the annual headline inflation rate to increase further in October 2017 by 6.2% after a 5.8% rise in September 2017. This anticipated high inflation rate is due to higher expectations of prices of food, transportation, alcohol, electricity and kava-Tonga.

In October 2017, the Tongan Pa'anga appreciated against the NZD. This resulted in a slight increase in

	Monthly			Annual	
	Oct-17	Sep-17	% Growth	Oct-16	% Growth
Nominal Effective Exchange Rate Index	91.7	91.5	0.2	90.8	1.1
Real Effective Exchange Rate Index	105.6	105.7	0.0	100.1	5.5

Sources: NRBT

Nominal Effective Exchange Rate (NEER) index over the month and year. Real Effective Exchange Rate (REER) index on the other hand, slightly fell over the month and rose over the year. This reflected Tonga's higher headline inflation rate relative to its trading partners, which may impact the international competitiveness of the Tongan exports of goods and services.

	Monthly			Annual		
	Oct-17	Sep-17	% Growth	Oct-17	Oct-16	% Growth
<b>OET Receipts (TOP \$ million)</b>	<b>69.7</b>	<b>58.8</b>	<b>18.6</b>	<b>766.4</b>	<b>683.9</b>	<b>12.1</b>
Export receipt	3.4	1.0	249.2	24.9	19.1	30.4
Travel receipts	10.0	11.6	-13.8	116.5	87.6	33.0
Private transfers	23.1	23.0	0.3	274.9	238.7	15.2
Others	33.2	23.2	43.4	350.1	338.5	3.4
<b>OET Payments (TOP \$ million)</b>	<b>54.9</b>	<b>67.4</b>	<b>-18.5</b>	<b>666.0</b>	<b>598.3</b>	<b>11.3</b>
Import payments	31.2	33.8	-7.7	381.3	338.5	12.6
Services payments	11.0	13.5	-18.8	142.0	131.5	8.0
Primary income payments	4.0	6.6	-39.3	35.7	24.0	48.8
Others	8.7	13.4	-35.1	107.0	104.3	2.6

Total Overseas Exchange Transaction (OET) receipts rose by 18.6% to \$69.7 million in October 2017. Higher receipts for both telecommunication services and grants to non-profit organization during the month largely contributed to the trend. In year ended terms, total OET receipts also rose by 12.1% to \$766.4 million driven by higher inflows of private remittance and travel receipts. Total OET payments however fell by 18.5% to \$54.9 million over the month due to return of funds to head office in the previous month. Over the year, total OET payments rose by 11.3% to \$666.0 million, particularly payments for imports of wholesale & retail goods. The overall OET balance for October 2017 recorded a surplus of \$10.5 million. This contributed to the increase in the official foreign reserves to \$413.6 million, equivalent to 7.5 months<sup>1</sup> of import cover, which is above the Reserve Bank's minimum range of 3-4 months.

	Monthly			Annual	
	Oct-17	Sep-17	% Growth	Oct-16	% Growth
Foreign Reserves (\$ in million)	413.6	403.0	2.6	367.0	12.7
Import Coverage (months)	7.5	7.3		7.0	

Sources: NRBT

Broad money (money supply) rose over October, due to a significant rise in net foreign assets (official foreign reserves) outweighing the decline in net domestic assets (fall in credit to private sector). Annually, broad money

<sup>1</sup> Method of calculation changed in February 2017 to include both imports of goods & services (previous method used imports of goods only)



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increased driven yet again by significant rise in the foreign reserves.

Money	Monthly			Annual	
	Oct-17	Sep-17	% Growth	Oct-16	% Growth
Money Supply (\$ in million)	553.6	549.7	0.7	501.2	10.5
Net Foreign Asset	433.1	419.0	3.4	375.0	15.5
Net Domestic Asset	120.7	131.0	-7.9	126.4	-4.5

Source: Banking System, NRBT

Liquidity in the banking system (reserve money) increased over October to \$292.0 million. This was driven significantly by an increase in deposits by the commercial banks to the Reserve Bank vault. The banks' total loans to deposit ratio fell to 72.0% in October from 75.1% last month. This reflected a \$14.4 million (2.6%) increase in total deposits outweighing the decline in total lending of \$7.0 million (1.7%). This ratio continues to remain below the 80% loan to deposit ratio target which indicates excess liquidity in the banking system remains and that there is capacity for further lending by banks.

The reclassification of the Government Development Loans in October resulted in a decline in the reported total banks' lending to \$410.0 million. This reclassification impacted the level of business loans reported, however, banks' lending continue to grow. Over the year, total banks' lending continued to increase due to more lending to both businesses and households. This rise stemmed from higher lending to households mainly housing loans. Additionally, business loans also contributed to the annual rise as a result of more lending to the wholesale & retail, manufacturing, and transport sectors. This continued to support the domestic economic activities evident throughout the year.

Lending	Monthly			Annual	
	Oct-17	Sep-17	% Growth	Oct-16	% Growth
Total Lending (\$ in million)	410.0	417.0	-1.7	368.2	11.3
Business lending	172.6	180.8	-4.5	163.1	5.8
Household lending	236.4	235.1	0.6	203.8	16.0
Other lending	1.0	1.1	-7.6	1.3	-22.6

Source: Banking System, NRBT

The weighted average interest rate spread widened over October and over the year to 5.816%. The monthly increase resulted from a rise in the weighted average lending rate outweighing a decline in the weighted

average deposit rate. The weighted average lending rate rose due to higher rates for housing, vehicle, and other personal loans. Furthermore, higher lending rates also applied mainly to loans for the manufacturing, agriculture, and construction sectors. The weighted average deposit rate declined due to a decline in term deposit rates whilst demand and saving deposit rates increased. Annually, the weighted average interest rate spread widened due to higher lending rates outweighing lower deposit rates. However, these rates remained relatively favourable as stable credit growth for households and businesses maintained its momentum.

Interest Rates	Monthly			Annual	
	Oct-17	Sep-17	Growth (bps)	Oct-16	Growth (bps)
Weighted Average Banks Deposit Rate (%)	2.160	2.186	-2.6	2.180	-2.0
Weighted Average Banks Lending Rate (%)	7.975	7.851	12.4	7.893	8.2
Weighted Average Interest Rate Spread (%)	5.816	5.665	15.1	5.713	10.3

Source: Banking System, NRBT

Net credit to Government decreased over the month by \$11.5 million, driven by a rise in government deposits. Similarly, net credit to Government fell over the year by \$50.7 million due to receipts of budgetary support funds and improved government revenue collection.

The Reserve Bank's outlook for strong domestic economic activity remains in the medium term. The level of foreign reserves is also expected to remain at comfortable levels supported by expected higher receipts of remittances and foreign aid. This will be partially offset by the projected rise in imports. Upward inflationary pressure remains in the near term, however it is expected to fall below the Reserve Bank's inflation reference rate of 5% per annum in 2017/18. In light of the above developments and that the banking system remained sound, the Reserve Bank Board maintained its current monetary policy measures. The Reserve Bank will remain vigilant and continue to closely monitor developments in the domestic and global economy for early signs of vulnerability or overheating of the economy. Furthermore, the Reserve Bank will continue to update its monetary policy setting to maintain internal and external monetary stability and to promote a sound and efficient financial system, in order to support macroeconomic stability and economic growth.