



NATIONAL RESERVE BANK OF TONGA

MONTHLY ECONOMIC REVIEW

Vol. 7

No. 4

Month Ended: April 2020

Global remittances expected to decline significantly

In April 2020, the World Bank Group reported that global remittances is projected to fall by 20% in 2020. This projection is reported as the largest decline in the past 20 years and is largely attributed to the anticipated impacts of the COVID-19 pandemic. Furthermore, remittances to low and middle-income countries alone are projected to decline by 19.7% in 2020. In the US, the Bureau of Labor Statistics shared that the unemployment rate for April 2020 recorded the highest increase in the US rising to 14.7% (from 4.4% in the previous month) driven significantly by the COVID-19 outbreak. Meanwhile, in Australia, the recent bush fires coupled with the COVID-19 lockdown contributed to the contraction in the economy by 0.3% in the March 2020 quarter as reported by the Australian Bureau of Statistics. Similarly, the New Zealand economy as shared by Westpac NZ in its May 2020 Economic Overview is projected to drop by 6.3% in 2020.

TC Harold worsens domestic performances

While COVID-19 already threatens to reduce domestic activities, the arrival of Tropical Cyclone (TC) Harold in April further amplified the downturn. TC Harold (Category 4) brought very strong winds and a massive storm surge, causing severe damages to businesses, household dwellings, agriculture and public infrastructures across Tongatapu and 'Eua.

Primary production slowed down in April, with agricultural export volumes falling by 215.7 tonnes (28.7%) due to lower exports of taro and cassava. The proceeds for marine exports also declined by \$0.5 million (81.2%) over the month whilst the proceeds for agricultural exports rose by \$0.1 million (22.9%). Over the year to April, the volume of agricultural exports surpassed the volume of the previous year by 3,902.6 tonnes (44.4%) reflecting a much better harvesting season.

Damages from TC Harold may cause further delays to construction projects, while lending continues to decline. The utility sector also faced some disruptions in distribution from the cyclone. Meanwhile, electricity benefits from the low oil prices resulting in lower electricity tariffs starting in April.

As expected, the national lockdown and closing of Tonga's borders for COVID-19 brought tourism activities to a standstill in April. With no international arrivals, hotels and resorts receive very minimal activities. Night clubs and entertainment businesses were also ordered to close down during the national lockdown. The majority of the private sector reduced their operations during the month as efforts were made to comply with curfews and social distancing requirements. Container registrations rose by 215 registrations (32.1%), solely driven by higher business containers indicating that the wholesale and retail distributions are taking initiatives to replenish and build-up

stock for any expected shortages in supply. Unfortunately, TC Harold destroyed resorts along the western coast of Tongatapu and some in 'Eua worsening the situation for the tourism sector. The damages to the 'Eua wharf will also affect local trade and transport.

Tight labour market conditions

The impacts of the COVID-19 lockdown coupled with the damages of TC Harold has resulted in many businesses laying off staff whilst others have reduced working hours in April 2020. The impact is much more evident in the tourism sector. Consequently, the total number of job advertisements continued to decline in April 2020 by 12 vacancies (52.2%) mostly for public administration but rose throughout the year by 18 job vacancies (4.1%).

Annual headline inflation rises in April

Table 1: Inflation Rates

Prices	Monthly		Annual	
	Apr-20	Mar-20	Apr-20	Apr-19
Headline Inflation (%)	-0.8	0.2	1.3	0.2
Domestic prices	-1.7	0.2	-1.1	-0.1
Imported prices	-0.1	0.2	3.2	0.3

Source: Statistics Department

Inflation fell by 0.8% over the month as both the domestic and imported prices decreased by 1.7% and 0.1% respectively. Lower local prices were largely driven by the

8.6% fall in electricity, gas & other fuel prices, followed by food items and tobacco at 1.2% and 2.6% respectively. Imported prices also decreased over the month solely driven by lower prices for transportation items.

Annual headline inflation for April 2020 was 1.3% which is higher than the 0.4% in March 2020 and 0.2% in April 2019. Imported prices increased by 3.2% over the year to April 2020 attributed to higher food prices

Table 2b: 'Average annual prices of selected items'

Items (\$ per kg)	Unit	Annual		
		Apr-20	Apr-19	Change
Domestic				
Kava	1kg	\$70.00	\$121.25	-\$51.25
Octopus	1kg	\$14.20	\$17.20	-\$3.00
Eggs	1 tray	\$16.84	\$18.29	-\$1.45
Imported				
Mutton flaps	1kg	\$17.69	\$15.46	\$2.23
Chicken pieces	1kg	\$3.51	\$2.89	\$0.62
Sugar	1kg	\$1.88	\$1.77	\$0.11

Source: Statistics Department

(7.2%), electricity, gas & other fuels (13.5%), and clothing & footwear (4.1%). Imported food prices were higher for mutton flaps, chicken pieces, and sugar. Domestic prices fell by 1.1% in the year to April 2020, partially offsetting higher imported prices. This owed mostly to lower prices for kava Tonga (-36.2%) and electricity, gas & other fuels (-8.6%).



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Major trading currencies weakened against the TOP

Table 3: Effective Exchange Rates

	Apr-20	Monthly Mar-20	% Growth	Annual Apr-19	% Growth
Nominal Effective Exchange Rate Index	94.7	94.9	-0.2	91.6	3.3
Real Effective Exchange Rate Index	111.2	110.8	0.4	106.5	4.4

Source: National Reserve Bank of Tonga

In April 2020, the Nominal Effective Exchange Rate (NEER) slightly decreased due to the appreciation of AUD against the TOP. However, the Real Effective Exchange Rate (REER) index increased over the month.

Over the year, both the NEER and REER increased which may imply a loss in Tonga's international trade competitiveness.

Higher foreign reserves on official receipts

Table 5: Foreign Reserves

	Apr-20	Monthly Mar-20	% Growth	Annual Apr-19	% Growth
Foreign Reserves (\$ in million)	475.1	457.5	3.9	464.2	2.3
Import Coverage (months)	6.9	6.8		7.8	

Source: National Reserve Bank Tonga

The official foreign reserves rose by \$17.7 million over the month and by \$10.9 million in the year to April 2020. The increase was mainly due to the inflow of budget support, grants, and additional funds from donor partners to assist Tonga's preparations for COVID-19.

Table 6: Overseas Exchange Transactions
Overseas Exchange Transactions

	Apr-20	Monthly Mar-20	% Growth	Annual Apr-20	Annual Apr-19	% Growth
Overall Balance	17.7	-22.4	178.9	10.9	18.3	-40.6
Current Account	24.4	-2.1	1259.4	32.1	-4.6	805.0
Merchandise Trade	-29.9	-32.4	7.8	-402.4	-423.8	5.1
Services	-2.3	6.7	-135.0	31.0	22.4	38.4
Income	-2.0	-5.6	64.3	-6.6	8.2	-179.7
Transfers	58.6	29.3	100.2	410.1	388.7	5.5
Capital Account	1.0	2.1	-54.3	29.8	34.4	-13.5
Financial Account	-7.7	-22.4	65.8	-51.0	-11.5	-342.4

Source: Banking Systems

Overall, the Overseas Exchange Transactions (OET) balance recorded a surplus in April 2020 from the inflow of official receipts. Hence, the current account balance increased recording a \$24.4 million surplus. This outweighed a lower surplus in the capital account from a decline in capital receipts. The financial account deficit declined due to lower payments on investment and interbank transfers during the month.

Annually, the overall OET balance surplus was lower attributed mainly to the financial account deficit. Higher payments over the year were for offshore investments. The capital account surplus also declined as private capital receipts fell over the year. However, the current account recorded a surplus compared to a deficit in the previous year. This was owed to lower payments for imports and

services whilst travel receipts and private transfer receipts increased.

Domestic assets lowered broad money

Table 7: Broad Money

	Apr-20	Monthly Mar-20	% Growth	Annual Apr-19	% Growth
Broad money (\$ in million)	581.6	596.4	-2.5	585.9	-0.7
Net Foreign Asset	503.3	485.3	3.7	482.6	4.3
Net Domestic Asset	79.0	111.7	-29.3	103.8	-23.9

Source: Banking System, National Reserve Bank of Tonga

Lower credit to the government and private sectors over the month lowered the net domestic assets and consequently the broad money, despite the increase in net foreign assets. The increase in foreign reserves from the receipts of budgetary support and grants for COVID-19 assistance contributed to the higher net foreign assets.

Liquidity declined in April

Table 8: Reserve money

	Apr-20	Monthly Mar-20	% Growth	Annual Apr-19	% Growth
Reserve money (\$ in million)	280.6	292.6	-4.1	305.9	-8.3

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the banking system continued to decline both over the month and year to April 2020 by \$12.1 million (4.1%) and \$25.3 million (8.3%) respectively. This was mainly driven by the decline in the exchange settlement accounts on higher deposits drawdown to cater for outgoing payments and government transfers for import payments and other COVID-19 preparations. It also included withdrawals by the commercial banks for business payments imports and services during the month.

Banks' total lending declined

Table 9: Total Lending

Lending	Apr-20	Monthly Mar-20	% Growth	Annual Apr-19	% Growth
Total Lending (\$ in million)	494.4	499.7	-1.1	484.3	2.1
Business lending	258.7	262.1	-1.3	258.9	-0.1
Household lending	235.7	237.5	-0.8	225.1	4.7
Other lending	0.0	0.0	0.0	0.3	-100.0

Source: Banking System, National Reserve Bank of Tonga

The banks' total lending fell by \$5.3 million (1.1%) over the month due to lower loans for both businesses and individuals. The decline in business lending were in majority of all sectors except for construction and transport which rose over the month. Household lending also fell mainly for housing and other personal loans.

Nonetheless, total lending rose during the year mainly driven by an increase in loans to businesses such as lending to the professional & other services, agricultural, and communication sectors. Loans to individuals fell as lower personal loans outweighed the rise in housing loans in the year to April 2020.

The banks' total loans to deposit ratio increased from 81.0% to 81.3% over the month as loans declined more than the decline in deposits.



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Interest rate spread narrowed

Table 10: Weighted Average Interest Rates

Interest Rates	Apr-20	Monthly Mar-20	Annual Growth (bps)	
			Apr-19	
Weighted Average Banks Deposit Rate (%)	2.115	2.025	9.1	1.954 16.2
Weighted Average Banks Lending Rate (%)	7.950	7.968	-1.8	8.111 -16.1
Weighted Average Interest Rate Spread (%)	5.835	5.943	-10.9	6.157 -32.3

Source: Banking System, National Reserve Bank of Tonga

The weighted average interest rate spread narrowed both over the month and in the year to April 2020 by 10.86 basis points and 32.27 basis points respectively. The monthly decline was due to a fall in the weighted average lending rate coupled with the increase in weighted average deposit rates. Lower average lending rates is attributed to business loans for the tourism, trade, and construction sectors. However, the average deposit rates increased resulting mainly from a rise in the savings deposit rate.

In year ended terms, the weighted average interest rate spread narrowed attributing to a decline in weighted average lending rates coupled with the increase in weighted average deposit rates. The decrease in weighted average lending rates was mainly on individual housing loans and business loans for the mining & quarrying, tourism, and construction sectors. Meanwhile, the weighted average

deposit rates increased due to a rise in savings, and term deposit rates.

Outlook

In light of the above developments, the impact of TC Harold, and the border remains closed until mid-June, the Reserve Bank is projecting an economic downturn for Tonga in 2019/20. This may continue to 2020/21 depending on the duration of the COVID-19 pandemic.

On the outlook for June 2020, foreign reserves is expected to remain at sufficient levels above the minimum of 3 months of import cover, sustained by the inflow of budget support and other relief funds from donor partners. Inflation is forecasted to gradually pick up yet remain below the Reserve Bank's reference rate of 5%. The banking system is still expected to remain sound with a slowdown in credit growth.

Monetary policy stance remains accommodative in support of domestic activities, macroeconomic growth, and mitigating the impacts of COVID-19 on the economy. The Reserve Bank remains vigilant by closely monitoring the financial and economic indicators for any sign of vulnerability and stands ready to adjust its monetary policy setting if required.