



### COVID-19 crisis further scales down global growth

The IMF in its June 2020 World Economic Outlook has further revised global growth downwards to a -4.9% growth projected for 2020 (compared to a -3.0% growth forecasted in April 2020). This largely stems from the intensifying impacts and disruptions of the COVID-19 pandemic consequently resulting in the contraction of global trade, subdued consumption spending, and weaker investment opportunities across economies. In the US, the Federal Reserve in June 2020 has continued to maintain its federal fund's rate at the target range of 0 – 0.25%. This is to stimulate growth by supporting the credit flow to businesses and households to strengthen investment activities. However, the Reserve Bank of Australia in its May 2020 Monetary Policy Statement projects a contraction in the Australian economy by around 10% over the first half of 2020. This aligns with expected higher unemployment rates and the slow recovery of economic activities. Meanwhile, the Statistics New Zealand (NZ) in June 2020 shared that the NZ economy recorded the highest drop in economic growth (since 1991) by -1.6% in the first quarter of 2020. This largely stems from the impacts of the COVID-19 restrictions affecting the service industries, construction, and household consumption.

### Sluggish domestic activities

Domestic activities for May have been slow as the country still maintains its COVID-19 restrictions. The Government has gradually eased up the restrictions on curfews and

mass gatherings over the month, allowing businesses such as Bars and Night Clubs to open for a few hours. Additionally, the Government has also started transferring funds to some of the businesses that have applied for the Economic Stimulus Package. The usual celebrations in May for White Sunday, Mother's Day, and Father's Day were kept to a minimum given the current State of Emergency for the global pandemic.

The primary sector shows positive growth despite the COVID-19 restrictions. The volume of agricultural exports increased by 312.2 tonnes (58.3%) during the month mainly driven by a rise in exports of cassava and taro. Over the year to May, the volume of agricultural exports was higher by 3,781.3 tonnes (41.9%) reflecting better harvests and recovery in this sector. The Ministry of Fisheries also took initiatives to support local fishing companies by buying some of their catch and selling it to the public at a cheaper price. Export proceeds rose over the month by \$0.3 million due to higher marine export proceeds.

Lending to construction businesses and individual housing rose by \$0.9 million (7.4%) and \$0.8 million (0.4%) respectively in May. The Road Improvement project continues to support the mining and quarrying sector, although businesses are reporting slower activities. The

damages from Cyclone Harold to the electricity lines have been restored and the Network upgrade project continues.

The tourism industry bears the brunt of the border lockdown, leaving hotels and resorts empty. Reduced mobility is also reflected in domestic transport. Restaurants and Catering businesses are facing weak demand as many booked functions and events get canceled. The total number of container registrations decreased by 89 registrations (10.1%) over the month owing to a decline in business containers for wholesale and retail businesses. Meanwhile, private containers slightly rose as they benefit from import duty exemptions as part of the government's relief package for the pandemic and TC Harold.

### Employee support, part of the Economic Stimulus package

Business owners were also requested to apply for Employee Support from the Government's Economic Stimulus package on behalf of their employees that were lay-off due to the impacts from COVID-19. Successful applications were allocated a one-off payment of \$535 pa'anga per employee. Job advertisements survey shows that vacancies being advertised are mostly for public administration, while very few vacancies are for the private sector.

### Lower inflation in May

Table 1: Inflation Rates

Prices	Monthly		Annual	
	May-20	Apr-20	May-20	May-19
Headline Inflation (%)	-0.4	-0.8	0.1	1.6
Domestic prices	0.7	-1.7	-0.1	1.5
Imported prices	-1.2	-0.1	0.2	1.7

Source: Statistics Department

Inflation fell by 0.4% over the month as imported prices declined by 1.2% outweighing the 0.7% increase in local prices. Lower imported prices were significantly driven by the 9.8% decline in the costs of transportation items particularly fuel which is consistent with the declining global oil prices. Domestic retail petrol prices recorded at the lowest level since 2016 of 187.58 seniti per litre. However, higher domestic prices are attributed to the increase in tobacco and food items both rising by 1.1% and 2.7% respectively.

Annual inflation for May 2020 was 0.1% which is lower than the 1.6% in May 2019 and

Table 2a: Monthly average prices of selected domestic items'

Items (\$ per kg)	Unit	Monthly		
		May-20	Apr-20	Change
Yams - early	1kg	\$4.21	\$3.42	\$0.79
Tuna	1kg	\$15.64	\$15.00	\$0.64
Eggs	1 tray	\$17.30	\$16.84	\$0.46
Kumala	1kg	\$1.40	\$1.18	\$0.22
Yams - late	1kg	\$2.94	\$2.86	\$0.08

Source: Statistics Department

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

Items (\$ per kg)	Unit	Annual		
		May-20	May-19	Change
<b>Domestic</b>				
Kava	1kg	\$70.00	\$121.25	-\$51.25
Octopus	1kg	\$13.57	\$17.64	-\$4.07
Eggs	1 tray	\$17.30	\$19.63	-\$2.33
<b>Imported</b>				
Mutton flaps	1kg	\$17.97	\$15.61	\$2.36
Sugar	1kg	\$1.95	\$1.78	\$0.17
Pall Mail	1box	\$19.43	\$19.29	\$0.14

Source: Statistics Department



slightly below 1.3% in April 2020. Imported prices increased by 0.2% over the year to May 2020 largely driven by higher food prices (6.1%), electricity, gas & other fuels (13.5%), and clothing & footwear (5.7%). This was partially offset by the lower prices for the operation of transport equipment (-20.3%). Imported food prices were higher for mutton flaps, sugar, and Pall Mall. Domestic prices fell by 0.1% in the year to May 2020, partially offsetting higher imported prices. This was continuously driven by lower prices for kava Tonga (-36.2%) and electricity, gas & other fuels (-8.6%).

### Major trading currencies weakened against the TOP

Table 3: Effective Exchange Rates

	Monthly			Annual	
	May-20	Apr-20	% Growth	May-19	% Growth
Nominal Effective Exchange Rate Index	94.8	94.7	0.1	92.0	3.0
Real Effective Exchange Rate Index	110.4	111.2	-0.7	107.7	2.5

Source: National Reserve Bank of Tonga

In May 2020, the Nominal Effective Exchange Rate (NEER) slightly increased due to the depreciation of the CNY, JPY, GBP, USD, and EUR against the TOP. However, the Real Effective Exchange Rate (REER) index declined over the month in line with lower inflation.

Table 4: Bilateral Exchange Rates

	May-20	Apr-20	May-19
USD/TOP	0.4334	0.4289	0.4368
AUD/TOP	0.6635	0.6798	0.6271
NZD/TOP	0.7108	0.7134	0.6644
FJD/TOP	0.9204	0.9237	0.8949
JPY/TOP	46.3420	46.0712	47.9934
GBP/TOP	0.3511	0.3445	0.3387
EUR/TOP	0.3966	0.3935	0.3894
CNY/TOP	2.8193	2.7905	2.8417

Source: Banking Systems

Over the year, both the NEER and REER increased which may imply a loss in Tonga's international trade competitiveness, however benefitting the remitters of foreign currency.

### Higher foreign reserves on official receipts

Table 5: Foreign Reserves

	Monthly			Annual	
	May-20	Apr-20	% Growth	May-19	% Growth
Foreign Reserves (\$ in million)	489.6	475.1	3.0	468.3	4.5
Import Coverage (months)	7.0	6.9	1.4	7.5	-6.7

Source: National Reserve Bank Tonga

The official foreign reserves recovered by \$14.5 million over the month and by \$21.3 million in the year to May 2020. The increase was mainly due to receipts of official funds as assistance for TC Harold and preparations for COVID-19.

Table 6: Overseas Exchange Transactions  
Overseas Exchange Transactions

	Monthly			Annual		
	May-20	Apr-20	% Growth	May-20	May-19	% Growth
<b>Overall Balance</b>	<b>14.5</b>	<b>17.7</b>	<b>-17.8</b>	<b>21.3</b>	<b>26.4</b>	<b>-19.2</b>
<b>Current Account</b>	<b>19.1</b>	<b>24.0</b>	<b>-20.5</b>	<b>45.7</b>	<b>6.0</b>	<b>666.2</b>
Merchandise Trade	-32.0	-30.2	-6.0	-398.4	-424.2	6.1
Services	14.5	-2.3	718.3	45.2	26.1	73.3
Income	2.5	-2.0	226.5	-6.6	10.2	-164.5
Transfers	34.1	58.6	-41.8	405.5	393.9	2.9
<b>Capital Account</b>	<b>1.9</b>	<b>1.0</b>	<b>97.9</b>	<b>-51.4</b>	<b>-16.0</b>	<b>-220.2</b>
<b>Financial Account</b>	<b>-6.4</b>	<b>-7.3</b>	<b>12.1</b>	<b>-82.1</b>	<b>-72.3</b>	<b>-13.6</b>

Source: Banking Systems

The Overseas Exchange Transactions (OET) balance recorded a lower surplus of \$14.5 million in May 2020

compared to a \$17.7 million surplus last month. This was mainly driven by the lower inflow of transfer receipts compared to that of last month and an increase in payments for imports. The current account balance thus recorded a lower surplus of \$19.1 million. This was followed by a higher surplus in the capital account from an increase in private capital receipts. The financial account deficit also improved slightly, due to higher receipts from other investments during the month.

Annually, the overall OET balance surplus was lower due mainly to the financial account deficit. This reflected higher payments over the year for offshore investments and external debt. The capital account surplus also declined as private capital receipts fell over the year. However, the current account recorded a higher surplus compared to the previous year. This was due to lower payments for imports and services while official and private transfer receipts increased.

### Broad money expanded

Table 7: Broad Money

	Monthly			Annual	
	May-20	Apr-20	% Growth	May-19	% Growth
Broad money (\$ in million)	592.2	581.6	1.8	584.8	1.3
Net Foreign Asset	517.2	503.3	2.8	488.8	5.8
Net Domestic Asset	75.7	79.0	-4.1	96.4	-21.5

Source: Banking System, National Reserve Bank of Tonga

Broad money rose over the month and year to May 2020 by \$10.6 million (1.8%) and \$7.4 million (1.3%) respectively. These movements were driven mostly by the increase in net foreign assets particularly foreign reserves. Net domestic assets, on the other hand, declined due to higher government deposits, and credit to private sectors over the month. Lower net domestic credit over the year was attributed to the rise in government net deposits with the Reserve Bank.

### Higher currency in circulation

Table 8: Reserve money

	Monthly			Annual	
	May-20	Apr-20	% Growth	May-19	% Growth
Reserve money (\$ in million)	286.7	280.6	2.2	311.0	-7.8

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the banking system increased in May 2020 by \$6.1 million (2.2%) solely driven by higher currency in circulation to cater for the family month of May. This was partially outweighed by a decline in the banks' ESA. In the year to May 2020, liquidity declined by \$24.3 million (7.8%) as the higher currency in circulation was offset by a decline in banks' ESA.

### Lending to the private sector increases

Table 9: Total Lending

Lending	Monthly			Annual	
	May-20	Apr-20	% Growth	May-19	% Growth
Total Lending (\$ in million)	495.4	494.4	0.2	487.3	1.7
Business lending	236.4	235.7	0.3	227.9	3.7
Household lending	259.0	258.7	0.1	259.1	0.0
Other lending	0.0	0.0	0.0	0.3	-100.0

Source: Banking System, National Reserve Bank of Tonga



# NATIONAL RESERVE BANK OF TONGA

## MONTHLY ECONOMIC REVIEW

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The banks' lending rose over the month by \$1.1 million (0.2%) for both businesses and individuals. Higher lending was for businesses in the construction, wholesale & retail, and agricultural sectors. This was also supported by the increase in housing loans made by households.

Over the year, the total lending increased by \$8.1 million (1.7%) which was largely underpinned by higher business loans such as lending to professional & other services, agricultural sectors, and public enterprises. Lending to individuals remained relatively stable over the year as the rise in housing loans was offset by the decline in other personal loans.

The banks' total loans to deposit ratio declined from 81.3% to 80.5% over the month, reflecting a higher increase in deposits compared to that of loans.

### Interest rate spread continued to narrow

Table 10: Weighted Average Interest Rates

Interest Rates	May-20	Monthly		Annual	
		Apr-20	Growth	May-19	Growth
Weighted Average Banks Deposit Rate (%)	2.119	2.115	0.3	1.956	16.3
Weighted Average Banks Lending Rate (%)	7.814	7.946	-13.3	8.044	-23.0
Weighted Average Interest Rate Spread (%)	5.695	5.831	-13.6	6.088	-39.3

Source: Banking System, National Reserve Bank of Tonga

The weighted average interest rate spread narrowed over the month by 13.57 basis points to 5.70%. This was a result of the continuous decline in weighted average lending rates coupled with the slight rise in weighted average deposit rates. Lower lending rates were mainly for the wholesale & retail, constructions, fisheries, and professional services sector. Households' housing and other personal lending rates also decreased. The slight increase in deposit rates was due to the rise in the volume of savings deposits despite the declining deposit rates offered.

Annually, the weighted average interest rates spread narrowed by 39.30 basis points due to a decline in the weighted average lending rates whilst the weighted average deposit rates rose. Lower lending rates were mostly for business loans particularly for the mining & quarrying, tourism, and professional & other services sectors as well as households' housing and personal loans. Higher deposit rates were for savings and demand deposit rates.

### Outlook

In light of the above developments, the impact of TC Harold, and the border remaining closed until September 2020, the Reserve Bank still projects an economic downturn in 2019/20. This is likely to continue on to 2020/21 depending on the duration of the COVID-19 pandemic.

On the outlook for the near term, 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. New taxes and duties for the new fiscal year 2020/21, global shocks, and heightened uncertainties from COVID-19 are risks to the outlook.

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 vulnerability in the financial system and stands ready to adjust its monetary policy setting if required.