



Global economic recovery slows a little than expected

The International Monetary Fund (IMF) in its October 2021 World Economic Outlook (WEO) revised its 2021 global growth projection downwards to 5.9% from 6.0% in the July WEO. The downward revision reflects the spread of the Delta variant and the heightened uncertainty stemming from the threat of new variants, which has affected both advanced and low-income economies. In particular, the growth projection for the US economy was lowered to 6.0% from the previous forecast of 7.0%. Meanwhile, the Australian Bureau of Statistics recorded a 6.8% increase in the number of dwellings approved during August 2021 and unemployment rate for New Zealand has fallen to 4% from 5.3% a year ago as reported by the Reserve Bank of New Zealand. Nonetheless, both Australia and New Zealand expect a slowdown in economic activities in the September quarter due to the recent Delta outbreak and prolonged lockdowns.

Some domestic economic activities in August 2021

The primary sector picked up in August 2021, particularly the agricultural sector. Total agricultural export volumes rose over the month by 27.9 tonnes (3.9%), driven by higher exports of root crops such as yam and taro. Additionally, the onset of the squash harvest season saw squash exports picking up during the month. Agricultural export proceeds also rose over the month by \$0.4 million. Over the year to August 2021, total agricultural export volumes fell by 3,043.0 tonnes (22.6%), largely reflecting last year's unfavourable squash harvest. This also coincides with the fall in the annual agricultural export proceeds by \$0.8 million (10.6%).

Activities in the secondary sector generally slowed over the month. Loans extended to the manufacturing, utility, and mining and quarrying sectors increased over the month whilst lending to the construction sector fell by \$0.5 million (2.5%). However, activities in the construction sector continued during the month such as projects for WASH facilities for Government schools that were commissioned and hundreds of vulnerable homes repaired after cyclones Gita and Harold. The utility sector was supported by Water Supply Improvements in Niuafou'u. Electricity prices remained at 80.71 seniti per kilowatt in August 2021 but electricity production and consumption slowed by 0.4 million kilowatts (6.3%) and 0.4 million kilowatts (6.6%) respectively. Electricity consumers, however, increased by 37 consumers (0.1%). Annually, electricity production and consumption increased by 2.3 million kilowatts (3.3%) and 3.2 million kilowatts (4.8%) respectively. Electricity consumers rose by 741 consumers (3.0%) annually.

The tertiary sector showed mixed outcomes in August 2021. Total container registrations substantially increased over the month by 430 containers (86.3%) due to both higher business and private containers. This reflects the arrival of rerouted shipments from previous months. Import payments (excluding oil), however, decreased by \$1.0

million (2.6%). Over the year to August 2021, container registrations increased by 190 containers (1.7%), primarily owing to higher business container registrations of 1,804 containers (26.8%). As international air travel remained largely stagnant, the arrival of passengers and travel receipts both dropped during the month by 138 passengers (90.8%) and \$0.1 million (5.7%) respectively. Annually, arriving passengers fell by 55,619 passengers (95.3%) and travel receipts dropped by \$62.9 million (75.5%). Vehicle registrations increased in August 2021 by 5 vehicles (1.7%) and 159 vehicles (5.3%) annually.

Slight fall in job advertisements

The Reserve Bank's survey showed 21 job vacancies advertised during the month, which is largely similar to the 22 vacancies reported in the previous month. Majority of these vacancies are in public administration. Annually, advertised job vacancies decreased by 124 vacancies (34.2%).

Inflation above the reference rate of 5% as projected

In August 2021, the monthly inflation increased by 0.2%, mainly owing to higher imported prices. Higher fuels and food prices were the key drivers of the increase in the imported prices over the month. Meanwhile, local prices declined by 0.2%, largely due to a fall in prices of food and kava.

| Prices | Monthly | | Annual | |
|------------------------|---------|--------|--------|--------|
| | Aug-21 | Jul-21 | Aug-21 | Aug-20 |
| Headline Inflation (%) | 0.2 | 0.3 | 7.0 | -1.6 |
| Domestic prices | -0.2 | 0.9 | 6.7 | -3.4 |
| Imported prices | 0.4 | -0.1 | 7.3 | -0.2 |

Source: Statistics Department

Higher imported and local prices both contributed to the 7.0% annual headline inflation. The higher imported prices were due to

| Items (\$ per kg) | Unit | Annual Change | | |
|-------------------|-------|---------------|---------|--------|
| | | Aug-21 | Aug-20 | Change |
| Domestic | | | | |
| Octopus | 1kg | \$18.45 | \$11.66 | \$6.79 |
| Capsicum | 1kg | \$15.30 | \$11.68 | \$3.62 |
| Tomatoes | 1kg | \$7.84 | \$5.23 | \$2.61 |
| Tuna | 1kg | \$19.50 | \$17.00 | \$2.50 |
| Imported | | | | |
| Turkey tails | 1kg | \$12.70 | \$9.21 | \$3.49 |
| Petrol | litre | \$2.98 | \$2.34 | \$0.64 |
| Diesel | litre | \$2.86 | \$2.37 | \$0.49 |

Source: Statistics Department

higher prices for fuels, gas and other fuels, and food items. The increase in prices of electricity, and food items contributed to the higher domestic prices over the year. Inflation is expected to remain above the 5% reference rate in the upcoming months. This is mainly driven by temporary inflationary pressure arising from disruptions to supply chains given the outbreak of new COVID-19 variants in our trading partners. Inflation is therefore expected to return below the 5% reference rate in early 2022.

Higher effective exchange rates

Table 3: Effective Exchange Rates

| | Monthly | | | Annual | |
|---------------------------------------|---------|--------|-----|--------|----------|
| | Aug-21 | Jul-21 | % | Aug-20 | % Growth |
| Nominal Effective Exchange Rate Index | 89.4 | 89.2 | 0.2 | 90.8 | -1.5 |
| Real Effective Exchange Rate Index | 107.4 | 107.2 | 0.2 | 104.1 | 3.2 |

Source: National Reserve Bank of Tonga



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The Nominal Effective Exchange Rate (NEER) slightly increased in August 2021 as most of Tonga's trading partners' currencies depreciated against the Tongan Pa'anga (TOP). Similarly, the Real Effective Exchange Rate (REER) index also slightly rose over the month.

In year-ended terms, the NEER fell as trading partners' currencies strengthened against the Tongan Pa'anga. However, the REER increased over the year in line with the higher inflation rate. This is indicative of a loss in Tonga's trade competitiveness in comparison to its trading partners.

Foreign reserves reached a new peak

Table 4: Foreign Reserves

| | Monthly | | | Annual | | |
|----------------------------------|---------|--------|---------|--------|--------|----------|
| | Aug-21 | Jul-21 | %Growth | Aug-20 | Aug-20 | % Growth |
| Foreign Reserves (\$ in million) | 751.7 | 704.8 | 6.7 | 556.1 | 35.2 | |
| Import Coverage (months) | 13.1 | 12.3 | 6.5 | 9.7 | 35.1 | |

Source: National Reserve Bank Tonga

Official foreign reserves rose significantly in August 2021 by \$46.9 million to a new record high of \$751.7 million, equivalent to 13.1 months of imports. This resulted largely from an increase in capital inflow and remittances. In year ended terms, foreign reserves increased substantially by \$195.6 million, underpinned by receipts of budget support, project funds, and remittances. Majority of the official foreign reserves are held in USD, AUD, and NZD.

Table 5: Remittance Receipts

| | Monthly | | | Annual | | |
|----------------------------|---------|--------|----------|--------|--------|----------|
| | Aug-21 | Jul-21 | % Growth | Aug-21 | Aug-20 | % Growth |
| Remittance (\$ in million) | 43.2 | 41.9 | 3.3 | 472.2 | 359.8 | 31.2 |

Source: National Reserve Bank Tonga

Remittance receipts increased over the month by \$1.3 million (3.3%) supported by higher family support, compensation of employees and private capital transfer receipts offsetting the slight decline in social benefits. In the year to August 2021, remittances continued to increase firmly by \$112.4 million. This was attributed to higher private transfers and compensation of employees mostly from seasonal workers.

Table 6: Overseas Exchange Transactions

| | Monthly | | | Annual | | |
|-------------------|---------|--------|----------|--------|--------|----------|
| | Aug-21 | Jul-21 | % Growth | Aug-21 | Aug-20 | % Growth |
| Overall Balance | 47.0 | -10.5 | 547.5 | 195.6 | 64.3 | 204.3 |
| Current Account | -1.7 | -9.2 | 81.8 | 118.2 | 61.2 | 93.2 |
| Merchandise Trade | -39.1 | -46.6 | -16.1 | -472.0 | -397.4 | -18.8 |
| Services | -6.7 | -4.7 | -43.4 | -35.6 | 10.2 | -449.1 |
| Income | 3.9 | 3.7 | 4.4 | 25.4 | 7.8 | 223.9 |
| Transfers | 40.3 | 38.4 | 4.9 | 600.4 | 440.6 | 36.3 |
| Capital Account | 1.4 | 0.6 | 131.8 | 40.6 | 23.1 | 76.0 |
| Financial Account | -1.9 | 1.1 | -269.9 | 36.8 | -20.0 | 284.5 |

Source: Banking Systems

Overall, Overseas Exchange Transactions (OET) recorded an overall balance surplus of \$47.0 million in August 2021 compared to a \$10.5 million deficit in July 2021. This was attributed to increases in all of the accounts, particularly the lower current account deficit as the merchandise trade deficit improved over the month.

Annually, the OET balance surplus still expanded firmly by \$131.3 million supported by higher official grants, budget support and remittance receipts.

Broad money rose

Table 7: Broad Money

| | Monthly | | | Annual | |
|-----------------------------|---------|--------|----------|--------|----------|
| | Aug-21 | Jul-21 | % Growth | Aug-20 | % Growth |
| Broad money (\$ in million) | 779.2 | 769.7 | 1.2 | 624.7 | 24.7 |
| Net Foreign Asset | 742.4 | 740.2 | 0.3 | 582.4 | 27.5 |
| Net Domestic Asset | 37.3 | 30.3 | 23.2 | 42.9 | -13.0 |

Source: Banking System, National Reserve Bank of Tonga

Broad money rose further over the month and year to August 2021, by \$9.5 million (1.2%) and \$154.5 million (24.7%) respectively. The net domestic assets increased as lower government deposits contributed to higher net credit from central government. The net foreign assets rose driven mostly by the higher foreign reserves. Annually, the net foreign assets increased again and offset the decline in net domestic assets. Higher net foreign assets corresponded to the rising foreign reserves whilst the lower net domestic assets reflected lower credit to public enterprises and higher government deposits.

Liquidity in the financial system rose

Table 8: Reserve money

| | Monthly | | | Annual | |
|-------------------------------|---------|--------|----------|--------|----------|
| | Aug-21 | Jul-21 | % Growth | Aug-20 | % Growth |
| Reserve money (\$ in million) | 515.0 | 504.0 | 2.2 | 336.3 | 53.1 |

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the financial system increased over the month and year to August 2021, by \$11.0 million (2.2%) and \$178.7 million (53.1%) respectively. The monthly rise was solely driven by higher commercial banks' Exchange Settlement Accounts (ESA) due mainly to net deposits to the Reserve Bank vault offsetting the net purchases of foreign currency from the Reserve Bank. Annually, all categories rose with the commercial banks' ESA increasing the most due to higher government deposits. Currency in circulation also increased in line with the festivities during the year, such as the churches annual donations, Easter, family month of May, Christmas and New Year festivities, Kava Idol, and the Tonga High School Ex-Students' Fundraising. Required reserves also increased, corresponding to the rise in total deposits.

Credit growth remains subdued

Table 9: Total Lending

| Lending | Monthly | | | Annual | |
|-------------------------------|---------|--------|----------|--------|----------|
| | Aug-21 | Jul-21 | % Growth | Aug-20 | % Growth |
| Total Lending (\$ in million) | 478.8 | 481.6 | -0.6 | 487.6 | -1.8 |
| Business lending | 221.6 | 223.2 | -0.7 | 229.0 | -3.2 |
| Household lending | 256.9 | 258.1 | -0.4 | 258.7 | -0.7 |
| Other lending | 0.3 | 0.4 | -24.4 | 0.0 | 0.0 |

Source: Banking System, National Reserve Bank of Tonga

Over the month and year to August 2021, the banks' total lending declined by \$2.8 million (0.6%) and \$8.8 million (1.8%). Both declines are attributed to loan repayments made by public enterprises which outweighed the few lending opportunities offered to other private businesses. Lower lending to businesses in the distribution, professional & other services, and constructions sectors as well as



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household housing loans also supported the monthly fall. Similarly, lower loans offered to businesses within the manufacturing, professional & other services, and agricultural sectors contributed to the annual decline coupled with the decline in all types of household loans.

In August 2021, the banks' total deposits increased by \$7.7 million (1.0%) as saving and demand deposits increased over the month. The increase in total deposits together with the decline in total lending resulted in a lower loan to deposit ratio of 58.9% in August 2021 compared to 59.8% last month. This remains below the 80% minimum.

Weighted average interest rate spread widened

Table 10: Weighted Average Interest Rates

| Interest Rates | Aug-21 | Monthly Jul-21 | Growth | Annual | |
|---|--------|-------------------|--------|--------|--------|
| | | | | Aug-20 | Growth |
| Weighted Average Banks Deposit Rate (%) | 1.868 | 1.884 | -1.5 | 2.134 | -26.5 |
| Weighted Average Banks Lending Rate (%) | 7.764 | 7.752 | 1.25 | 7.783 | -1.8 |
| Weighted Average Interest Rate Spread (%) | 5.896 | 5.868 | 2.8 | 5.649 | 24.7 |

Source: Banking System, National Reserve Bank of Tonga

The weighted average interest rate spread widened over the month and year to August 2021, by 2.8 basis points and 24.7 basis points respectively to 5.90%. Over the month, the decline in the weighted average deposit rates coupled with the rise in the weighted average lending rates contributed to the wider weighted average interest rate spread. The lower weighted average deposit rates resulted mainly from lower demand and saving deposit rates. However, higher lending rates over the month was offered mainly to businesses within the fisheries, agriculture, and

transport sectors as well as household vehicles and other personal loans.

Over the year, the higher weighted average interest rate spread is due mainly to the decline in the weighted average deposit rates, outpacing the fall in the weighted average lending rates. Higher deposit volume contributed to the lower weighted average deposit rates. All deposit rates fell, whilst lending rates for businesses in the utilities, constructions, and agricultural sectors also declined. Lower lending rates for other personal loans led the annual decline for loans extended to households.

Outlook

While the evolution of COVID-19 continues to impact economic development, both globally and domestically, the Reserve Bank still expects foreign reserves to remain at comfortable levels above the minimum of 3 months of import cover. Inflation is forecasted to remain above the Reserve Bank's reference rate of 5% in 2021 yet expected to fall below 5% in January 2022. The banking system is still expected to remain sound despite the slowdown in credit growth. The current monetary policy stance remains accommodative but the Reserve Bank will continue to monitor emerging risks prompted by uncertainties surrounding the COVID-19 pandemic, impacting economic growth, and potentially impairing financial stability. The Reserve Bank remains vigilant in its regulatory and supervisory roles to ensure that financial stability is maintained while supporting economic recovery.