



### Global economic growth revised upwards for 2021

In its April 2021 World Economic Outlook (WEO), the IMF anticipates a stronger recovery in 2021 by 6.0%. This is an upward revision from 5.5% projected in the January 2021 WEO update. This revision reflects positive impacts of substantial fiscal support in major economies and confidence stemming from the vaccine rollout. Economic growth in the US is expected to recover by 6.4% in 2021 from -3.5% in 2020. Meanwhile, the unemployment rate in Australia continues to fall since October 2020 to 5.8% in February 2021, indicating an improvement in the labor market. Similarly, the Reserve Bank of New Zealand in its February 2021 Monetary Policy Statement, reported that resilience in the labour market has been better than expected, falling to less than 5.0% by the end of 2020, reflecting the recovery of economic activities.

### General slowdown for domestic economic activity

The primary sector showed mixed growth in February 2021. Total agricultural exports rose during the month by 147.8 tonnes (42.8%) due to more yams and cassava exports. This coincided with a monthly increase in agricultural export proceeds by \$0.3 million (52.1%). However, agricultural exports over the year fell by 2,384.2 tonnes (19.3%) and proceeds by \$0.8 million (9.9%). Additionally, marine export volumes dropped by 117.6 tonnes (69%) over the month and 1,035.1 tonnes (44.9%) annually. However, the marine export proceeds recorded a slight increase over the month, but fell annually by \$5.7 million (57.5%).

Loans to the secondary sector show mixed movements, however, the construction sector showed dynamic activities within the industry. Lending to the construction sector increased by \$0.8 million (3.7%) over the month. However, lending to the utility and manufacturing sectors over the month both fell by \$0.1 million (45.4%) and \$0.2 million (1.6%), respectively. Despite the decline in lending to those respective sectors, part of the Nuku'alofa Network Upgrade Project of the Tonga Power Ltd was completed in February 2021, as well as an Upgraded water supply system for Hihifo funded by Japan under Grant Assistance for Grassroots Human Security Projects (GGP). A new warehouse for NEMO<sup>1</sup> funded by Australia and new classrooms for Holonga co-funded through World Bank's Pacific Resilience Program (PREP), and the Australian Government were also successfully commissioned during the month.

The services sector continued to slow down in February 2021. Container registrations dropped during the month by 332 containers (37.7%) as both business and private container registrations fell by 207 containers (36%) and 125 containers (40.2%), respectively. This is the normal monthly trend for February as in past years. International arrivals declined by 17 passengers (7.1%), thus reflecting a slight decrease in the travel receipts over the month. Annual

international arrivals and travel receipts dropped by 104,381 passengers (95.3%) and \$107.8 million (79.8%) respectively. International departures for February 2021 increased by 209 passengers (100.5%) due to the seasonal workers scheme in Australia and the departure of university students to Fiji. Annual international departures dropped by 105,334 passengers (95%).

### Employment opportunities

The Reserve Bank's survey showed an increase in vacancies over the month by 14 job vacancies (87.5%) and mostly for public administration. Ministry of Infrastructure had the most vacancies advertising for 8 roles. In addition, Tonga's first Labour Mobility Policy was launched during the month to ensure an effective labour mobility program and engagement, thus promoting more job opportunities for the unemployed and unskilled labor force.

### Higher headline inflation in February 2021

**Table 1: Inflation Rates**

Prices	Monthly		Annual	
	Feb-21	Jan-21	Feb-21	Feb-20
Headline Inflation (%)	1.1	0.7	2.1	0.8
Domestic prices	0.9	0.8	0.9	-3.1
Imported prices	1.3	0.7	3.1	4.1

Source: Statistics Department

Over the month, both the imported and local prices rose, driving higher inflation. Higher imported prices largely drove the monthly inflation and attributed to the increase in transportation items, reflecting the increase in global oil prices coupled with higher freight rates, food, and maintenance & repair items. Meanwhile, the rise in local items was significantly driven by higher food prices, specifically for vegetables and some root crops which is a similar pattern observed in February of previous years.

Table 2: Average annual prices of selected items

Items (\$ per kg)	Unit	Feb-21	Annual	
			Feb-20	Change
<b>Domestic</b>				
Tomatoes	1kg	\$19.87	\$15.23	\$4.64
Octopus	1kg	\$23.81	\$19.71	\$4.10
Capsicum	1 kg	\$19.96	\$17.46	\$2.50
Eggs	1 tray	\$17.97	\$16.08	\$1.89
<b>Imported</b>				
Pall Mall	1kg	\$23.00	\$19.29	\$3.71
Turkey tails	1 kg	\$10.88	\$9.39	\$1.49
Apples	1 kg	\$6.46	\$5.37	\$1.09

Source: Statistics Department

Annual headline inflation rose by 2.1% and is the highest since February 2019. Higher food prices, tobacco & alcoholic beverages, and clothing & footwear drove the rise in imported items. However, higher prices for local items resulted from higher food prices, tobacco, and clothing & footwear. Inflation is expected to gradually rise in the near future.

### Major trading currencies strengthened against TOP

The Nominal Effective Exchange Rate (NEER) fell again in February 2021 as major trading currencies appreciated

<sup>1</sup> National Emergency Management Office



# NATIONAL RESERVE BANK OF TONGA

## MONTHLY ECONOMIC REVIEW

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against the Tongan Pa'anga (TOP). However, the Real Effective Exchange Rate (REER) index rose over the month, after 10 consecutive months of decline. This reflected Tonga's higher inflation.

Table 3: Effective Exchange Rates

	Monthly			Annual	
	Feb-21	Jan-21	%	Feb-20	% Growth
Nominal Effective Exchange Rate Index	85.6	85.7	-0.1	93.2	-8.2
Real Effective Exchange Rate Index	101.3	100.3	1.0	108.6	-6.7

Source: National Reserve Bank of Tonga

In year-end terms, both the NEER and REER declined, indicating an improvement in Tonga's trade competitiveness with trading partners, further supporting foreign currency receipts.

### Lower foreign reserves on official receipts

Table 4: Foreign Reserves

	Monthly			Annual	
	Feb-21	Jan-21	Growth	Feb-20	% Growth
Foreign Reserves (\$ in million)	692.4	705.3	-1.8	479.8	47.0
Import Coverage (months)	11.7	12.0	-2.5	7.4	58.3

Source: National Reserve Bank Tonga

The foreign reserves declined at the end of February 2021 by \$12.9 million, equivalent to 11.7 months of imports. The monthly movement was underpinned by increased business and government payments for goods and services. However, foreign reserves rose significantly in the year to February 2021 by \$212.5 million. This attributed mostly to receipts of budget support, official grants, and remittances. Foreign reserves are held mainly in USD, AUD, and NZD.

Table 5: Remittance Receipts

	Monthly			Annual		
	Feb-21	Jan-21	% Growth	Feb-21	Feb-20	% Growth
Remittance (\$ in million)	32.9	32.3	1.6	411.3	350.8	17.2

Source: National Reserve Bank Tonga

Remittances slightly rose in February 2021 by \$0.5 million. All categories increased over the month, mostly private transfer receipts, particularly AUD receipts. This was supported by receipts from seasonal workers in addition to the strong AUD. However, remittances continued to increase over the year, rising by \$60.5 million. This stemmed from higher private transfers and compensation of employees.

Table 6: Overseas Exchange Transactions

	Monthly			Annual		
	Feb-21	Jan-21	% Growth	Feb-21	Feb-20	% Growth
<b>Overall Balance</b>	<b>-12.9</b>	<b>29.7</b>	<b>-143.5</b>	<b>212.5</b>	<b>6.4</b>	<b>3232.2</b>
<b>Current Account</b>	<b>-14.9</b>	<b>18.2</b>	<b>-18.4</b>	<b>168.2</b>	<b>-3.9</b>	<b>4183.5</b>
Merchandise Trade	-39.0	-36.7	-6.3	-421.8	-406.2	-3.8
Services	-7.3	-2.1	-255.4	-17.0	32.4	-152.4
Income	3.0	3.4	-10.5	23.5	2.3	906.1
Transfers	28.5	53.7	-47.0	583.4	367.6	58.7
<b>Capital Account</b>	<b>4.7</b>	<b>3.5</b>	<b>35.8</b>	<b>44.2</b>	<b>31.6</b>	<b>40.2</b>
<b>Financial Account</b>	<b>-2.8</b>	<b>8.0</b>	<b>-134.4</b>	<b>0.1</b>	<b>-21.3</b>	<b>100.5</b>

Source: Banking Systems

Overall, Overseas Exchange Transactions (OET) recorded a deficit of \$12.9 million in February 2021, following a surplus in the previous month. This attributed to a decline in OET receipts, primarily from official transfers following the influx of budget support and donor funds in the previous months.

In the year to February 2021, the OET balance surplus rose substantially by \$206.2 million, underpinned by a higher current account surplus. This was supported by higher official transfer receipts. The capital account surplus also increased on the back of higher official and private capital receipts. The financial account improved over the year, driven mainly by lower interbank transfer payments.

### Broad money fell further

Table 7: Broad Money

	Monthly			Annual	
	Feb-21	Jan-21	% Growth	Feb-20	% Growth
Broad money (\$ in million)	703.4	706.9	-0.5	590.1	19.2
Net Foreign Asset	722.0	735.1	-1.8	494.9	45.9
Net Domestic Asset	-17.6	-27.3	-35.4	95.7	-118.4

Source: Banking System, National Reserve Bank of Tonga

Broad money declined further by \$3.5 million (0.5%) in February 2021, solely driven by lower net foreign assets. The foreign reserves decreased as a result of higher payments made for imports and services during the month. This was partly offset by the increase in net domestic assets from the lower government deposits made in the month. However, over the year, broad money rose significantly by \$113.3 million (19.2%), underpinned by the higher foreign reserves.

### Liquidity in the financial system declined

Table 8: Reserve money

	Monthly			Annual	
	Feb-21	Jan-21	% Growth	Feb-20	% Growth
Reserve money (\$ in million)	421.2	424.9	-0.9	297.9	41.4

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the financial system decreased over the month of February 2021, by \$3.7 million (0.9%), however, it rose over the year by \$123.3 million (41.4%) to \$421.2 million. Both the currency in circulation and the commercial banks' ESA (Exchange Settlement Account) fell over the month and offset the slight increase in the Required reserves. The lower commercial banks' ESA coincided with the higher net purchase of foreign exchange from the Reserve bank to cater for the major payments during the month, mainly for oil and other imports.

Over the year, liquidity rose with the bank's ESA rising the most, coinciding with the commercial banks' increased deposits to the Reserve Bank vault. Currency in circulation followed, in line with the festivities during the year such as the churches annual donations and Christmas and New Year festivities. Required reserves also increased, corresponding to the rise in total deposits.



### Credit growth continues to decline

Table 9: Total Lending

Lending	Monthly			Annual	
	Feb-21	Jan-21	% Growth	Feb-20	% Growth
Total Lending (\$ in million)	492.2	494.5	-0.5	499.7	-1.5
Business lending	234.0	236.4	-1.00	237.8	-1.6
Household lending	258.2	258.1	0.03	261.9	-1.4
Other lending	0.0	0.0	0.0	0.0	0.0

Source: Banking System, National Reserve Bank of Tonga

In February 2021, the banks' total lending declined again and for the third consecutive month, by \$2.3 million (0.5%). Lending to public enterprises and businesses in the wholesale & retail distribution, agriculture, and transport sectors decreased, as well as households' vehicle, and other personal loans. Similarly, the bank's total lending decreased annually by \$7.5 million (1.5%), mainly on lower loans offered to public enterprises and businesses such as manufacturing, professional & other services, and utilities sectors, and to households for other personal loans.

In February 2021, the banks' total deposits fell by \$7.7 million (3.4%) to \$703.1 million, solely driven by lower demand deposits mainly by government, public enterprises, and churches. The decline in total deposits outweighed the decline in total lending which resulted in a higher loans to deposit ratio of 68.2% in February 2021, an increase from 67.8% last month, but still below the 80% minimum.

### Weighted average interest rate spread narrowed

Table 10: Weighted Average Interest Rates

Interest Rates	Monthly			Annual	
	Feb-21	Jan-21	Growth	Feb-20	Growth
Weighted Average Banks Deposit Rate (%)	2.002	1.972	3.0	2.040	-3.8
Weighted Average Banks Lending Rate (%)	7.694	7.681	1.34	8.015	-32.0
Weighted Average Interest Rate Spread (%)	5.693	5.709	-1.6	5.975	-28.2

Source: Banking System, National Reserve Bank of Tonga

The weighted average interest rate spread narrowed by 1.6 basis points in February 2021. The weighted average deposit rate increased and offset the rise in weighted average lending rates. The higher weighted average deposit interest rates stemmed mostly from higher demand and savings deposit rates, outweighing the lower time deposit rates over the month. The increase in the weighted average lending interest rates is attributed to higher housing loan rates, and supported by higher rates on loans to the construction and fisheries sectors.

In year ended terms, the weighted average interest rate spread also narrowed by 28.2 basis points to 5.693%. This resulted mainly from lower weighted average lending interest rates on loans to households for other personal loans, public enterprises, and businesses in the mining & quarrying, construction, and utility sectors. Similarly, deposit interest rates declined also for savings and term deposit rates.

### Outlook

Domestic economic growth is anticipated to remain subdued. However, the Reserve Bank's monetary policy stance remains accommodative. The Reserve Bank will continue to monitor emerging risks prompted by uncertainties surrounding the COVID-19 pandemic, which may impact economic growth and potentially impair financial stability. The Reserve Bank remains vigilant in its regulatory and supervisory roles to ensure that financial stability is maintained whilst working to mitigate the economic downturn and support recovery.