

Banking Sector Developments October 2016

Release date: 24 March 2017

	Oct 16	Sep 16	Aug 16	Jul 16
Deposit rate (%)*	2.213	2.233	2.208	2.226
Lending rate (%)*	7.89	7.88	7.90	7.92
Total Deposits (T\$m)	496.8	491.2	481.9	462.6
Total lending (T\$m) ^	368.2	362.7	355.2	351.9
New commitments (T\$m)	13.1	12.4	12.8	11.2
Broad Money (T\$m)	501.2	496.2	491.0	478.0

*Weighted Average calculated as a function of interest rate and volume of deposits and loans

^This series shows total lending from the banking sector only.

Deposit rate has been revised from Jul 16 to current month

Both lending and deposits rise over October

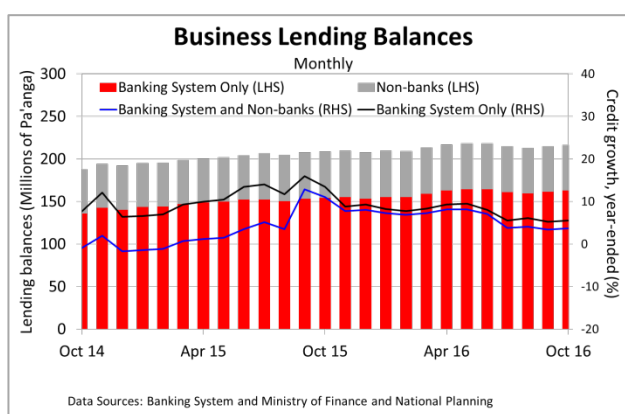
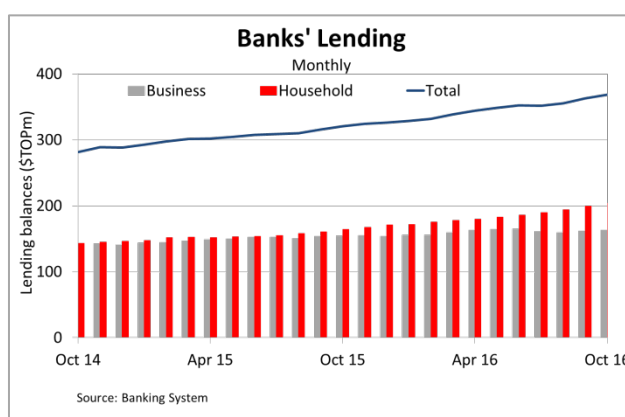
Lending

Lending by banks rose to \$368.2 million over the month. This \$5.5 million (1.5%) increase is lower than the \$7.5 million (2.1%) growth over September 2016. Over the year to October 2016, total bank lending increased by \$47.9 million (15.0%). This was contributed by more business and household loans.

Lending activities in the non-bank financial institutions also rose over the year by \$13.9 million (11.9%) to \$129.9 million. This was driven by higher household loans offsetting a decrease in government on-lent loans.

Business lending

Banks' lending to businesses rose over October 2016 by \$1.4 million (0.9%) to \$163.1 million. Loans to the agricultural, construction, and manufacturing sectors increased by \$0.3 million (3.4%), \$0.3 million (3.6%), and \$0.2 million (1.3%) respectively. This included the construction of a new hotel in Sopu. Over the year, lending to businesses increased by \$8.6



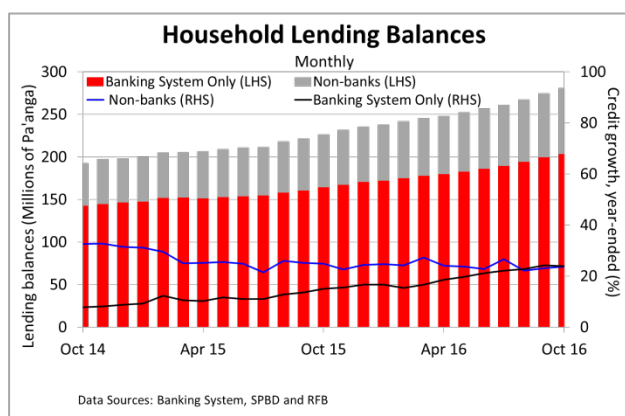
million (5.5%) due mainly to a rise in lending to the tourism sector of \$6.1 million (60.5%) and the manufacturing sector of \$2.8 million (21.8%). Government's continuous support through its Government Development Loans facility contributed to the monthly and annual growth. With the inclusion of government on-lent loans, the annual growth in business lending was lower, increasing by \$7.7 million (3.7%), reflecting the loan repayments made over the year.

Household lending

Banks' lending to households rose over the month by \$4.1 million (2.1%) to new high record of \$203.8 million. This is higher than the \$3.7 million (2.3%) monthly growth in October 2015. All household lending categories increased over the month, with housing loans contributing the most with a rise of \$4.0 million (2.9%).

Annually, banks' lending to households increased by \$39.4 million (24.0%). Housing loans rose the most by \$36.1 million (32.9%) followed by an increase of \$2.9 million (5.4%) in other personal loans.

Declines in housing and other household lending rates over the year by 30.1 and 10.8 basis points respectively supported the annual growth. This further coincided with a \$1.3 million (90.0%) increase in construction import payments. Additionally, lending from non-bank financial institutions to households increased by \$14.8 million (23.8%), reflecting higher personal loans over the year. The introduction of home improvement loans by the Retirement Fund Board in July 2016 for its members also contributed to the annual growth.



Other lending

Other loans by the banks declined over the month and over the year by \$0.05 million (4.1%) and \$0.05 million (3.4%) respectively. This was mainly a result of a decrease in lending activities within the non-profit institutions sector.

Non-performing loans

Banks' total non-performing loans decreased over the month by \$0.3 million (1.9%) to \$17.1 million, representing 4.6% of total loans. Non-performing business loans drove the monthly fall with a \$0.4 million (2.1%) decline offsetting the slight rise in the non-performing household loans of \$0.1 million (3.0%). On an annual basis, non-performing loans decreased by \$7.3 million (30.0%). This was caused mainly by non-performing business loans which fell by \$2.4 million (12.4%). Manufacturing and tourism sectors contributed largely to the annual decline in non-performing business loans.

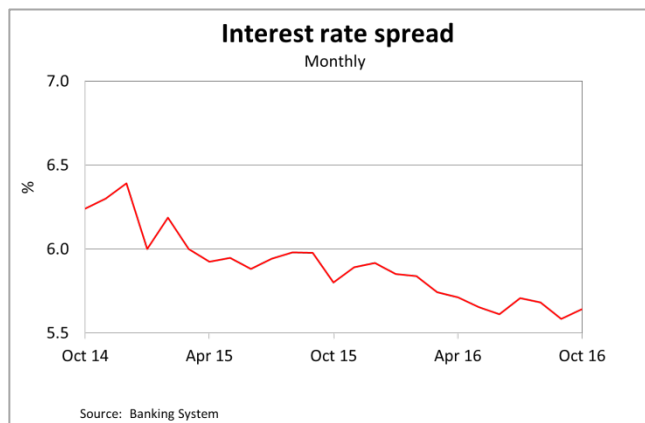
Deposits

Over the month, total bank deposits increased by \$5.6 million (1.1%) to a new high record of \$496.8 million, despite a fall in banks' deposit rates by 4.5 basis points. Demand deposits and savings deposits drove the increase in deposits over the month, rising by \$8.4 million (4.1%) and \$0.9

million (1.0%) respectively. This offset the decline in time deposits of \$3.7 million (1.9%). In year ended terms, total deposits rose by \$75.8 million (18.0%) as a result of an increase in all categories with demand deposits contributing the most.

Interest rate spread

The weighted average deposit rate decreased by 7.4 basis points to 2.21% over October 2016 due mainly to the narrowing of savings deposit rates. The weighted average lending rate however increased by 1.3 basis points driven by an increase in business lending rates. Accordingly, the weighted average interest rate spread widened to 5.68% from 5.65% last month.



Over the year, the weighted average interest rate spread narrowed by 12.0 basis points. This was due mainly to a fall in the weighted average lending rate outpacing the decline in the weighted average deposit rate.

Broad money

Broad money reached another record high of \$501.2 million in October 2016, a rise of \$5.0 million (1.0%) from the previous month. This was caused by increases in net domestic assets and net foreign assets of \$3.0 million (2.4%) and \$2.2 million (0.6%) respectively. Higher foreign reserves drove the rise in net foreign assets whilst the increase in private sector domestic credit caused growth in net domestic assets. Over the year, broad money rose significantly by \$72.5 million (16.9%) as a result of a substantial increase in net foreign assets by \$71.7 million (23.7%). Additionally, net domestic assets increased by \$0.6 million (0.5%). The receipt of the Government's budget support funds during the year contributed to the higher foreign reserves and corresponded to the rise in net foreign assets.

Liquidity

The liquidity (reserve money)¹ in the banking system decreased slightly by \$0.5 million (0.2%) over the month to \$267.6 million which resulted from the banks' deposits to the NRBT vault declining in October 2016. The loans to deposit ratio slightly increased from 73.8% last month to 74.1% in October 2016 but remained below the 80% minimum loan to deposit ratio target that was effective on 1st July 2016, which indicated excess liquidity in the banking system remains. In year ended terms, the banking system liquidity rose by \$20.3 million (8.2%) as a result of a \$13.2 million (7.7%) rise in banks' deposits to the NRBT vault.

¹ Liquidity in the banking system (reserve money) is a sum of currency in circulation, exchange settlement account balances, and required reserve deposits.

Outlook

The National Reserve Bank of Tonga (NRBT) in its August 2016 Monetary Policy Statement (MPS) is forecasting credit growth to continue. NRBT estimated a growth of about 11.0% in 2016/17. The NRBT's forecast slightly surpassed the 2016 IMF Article IV's projected growth of 10.8% for 2016/17. The banks' prospects for credit growth remains positive and the NRBT's projection is supported by improving economic conditions, business confidence, and annual (one-off) events taking place during the year.

The NRBT forecasts the annual growth in broad money to rise in June 2017 by 10% coinciding with the IMF's estimated growth of 9%. This is supported by the anticipated increase in lending and foreign reserves.

The banks' loan to deposit ratio of 80% - 90% is anticipated to be achieved progressively over 18 months. This measure is to encourage the utilization of the excess liquidity in the banking system to increase lending, in order to support economic growth. At the same time, the NRBT is exploring alternative monetary policy and macro prudential tools to strengthen the policy transmission mechanism, and at the same time ensure financial stability is maintained. The NRBT will closely monitor the country's economic and fiscal developments and financial conditions to maintain internal and external monetary stability, and promote a sound and efficient financial system to support macroeconomic stability and economic growth.

Table 1:

Consolidated Balance Sheet of Depository Corporations

	Level as at					Change over the last:	
	Oct-16 \$TOPm	Sep-16 \$TOPm	Aug-16 \$TOPm	Jul-16 \$TOPm	Oct-15 \$TOPm	1 month % growth	1 year % growth
Broad money liabilities	501.2	496.2	491.0	478.0	428.7	1.0	16.9
Currency in circulation	48.9	49.2	48.4	52.5	46.9	-0.6	4.3
Demand deposits	190.6	182.6	194.8	188.1	159.1	4.4	19.8
Savings and term deposits*	261.7	264.4	247.8	237.5	222.7	-1.0	17.5
<i>equals</i>							
Net foreign assets	375.0	372.8	377.9	374.3	303.3	0.6	23.7
<i>plus</i>							
Net domestic assets	126.5	123.4	113.4	103.9	125.8	2.5	0.5
Gross bank lending**	377.7	372.0	364.1	361.1	329.2	1.5	14.7
Public enterprises	41.7	41.4	40.0	40.4	46.2	0.9	-9.7
Private Sector	320.6	315.4	308.7	305.1	268.0	1.7	19.6
Other financial corporation	15.3	15.3	15.4	15.6	14.9	0.5	2.7
Other***	-251.2	-248.6	-250.7	-257.3	-203.3	1.1	23.5

* Also includes very minor amounts for securities other than shares.

** Differs slightly from standard measures of bank lending by amounts classified as accrued interest.

*** Includes mostly capital accounts of the banks and NRBT, and their net claims on the central government.

Sources: Banking system; NRBT

Table 2:

	Lending Balances							Shares of totals %
	Level as at					Change over the		
	Oct 16 TOPm	Sep 16 TOPm	Aug 16 TOPm	Jul 16 TOPm	Oct 15 TOPm	1 month %	1 year %	
Lending, banks	368.2	362.7	355.2	351.9	320.3	1.5	15.0	100.0
Household	203.8	199.7	194.3	189.5	164.4	2.1	24.0	55.4
Business*	163.1	161.7	159.6	161.2	154.5	0.9	5.5	44.3
Other	1.3	1.3	1.3	1.2	1.3	-4.1	-3.4	0.3
Lending, banks and other	498.1	490.6	481.6	476.8	436.4	1.5	14.2	100.0
Household	280.7	274.5	267.3	261.0	226.5	2.2	23.9	56.3
Business	216.2	214.8	212.9	214.6	208.5	0.7	3.7	43.4
Other	1.3	1.3	1.3	1.2	1.3	-4.1	-3.4	0.3
New comm'ts, banks	13.1	12.4	12.8	11.2	14.9	6.5	-11.5	N/A
Undrawn comm'ts, banks	13.3	14.6	17.6	18.7	20.6	-8.9	-35.3	N/A
Implied repay'ts, banks	8.9	7.9	10.5	9.0	10.9	12.8	-18.5	N/A

* Method for calculating these series was updated in August 2014, resulting in revisions to the full history of data

Sources: SPBD; RFB; MOFNP; Banking system

Table 3:

	Interest Rates							Share of loans/deposits %
	Level as at					Change over the last [^] :		
	Oct 16 %	Sep 16 %	Aug 16 %	Jul 16 %	Oct 15 %	1 month bps	1 year bps	
Deposits all	2.25	2.30	2.22	2.22	2.29	-4.52	-3.51	100
Demand	0.41	0.41	0.40	0.42	0.41	0.39	0.62	40
Savings	2.35	2.38	2.52	2.51	2.38	-2.73	-2.66	19
Term	4.04	4.05	3.92	3.93	4.09	-0.63	-4.56	40
Loans all	7.89	7.88	7.90	7.92	8.09	1.31	-19.43	100
Housing	8.09	8.08	8.08	8.09	8.39	0.24	-30.12	41.8
Other personal	11.02	10.98	11.00	10.96	11.13	3.26	-10.85	16.3
Business*	6.87	6.91	6.94	7.03	7.22	-4.44	-35.26	26.0
Other	6.54	6.64	6.54	6.25	6.44	-10.42	10.07	16.0

*Method for calculating these series was updated in August 2014, resulting in revision to the full history of data

[^]Due to rounding errors some data may not aggregate precisely

Sources: Banks; NRBT