Monthly Economic Review

For February 2015

Global developments continue to support domestic economic activities. Over the month of February, unemployment rate in the U.S. and Australia have improved to 5.5% and 6.3% from 5.7% and 6.4% respectively. The U.S. dollar strengthened against the Australian and the New Zealand dollar on improvements in the U.S. economy. Global oil price was around USD$60 a barrel up from USD$49.10 in the previous month, though 45.1% lower than it was a year ago. The falling energy prices have lowered headline inflation globally.

The domestic economy bounced back in February after a downturn in the previous month. The primary sector rebounded with a 12.4% rise in agricultural exports volumes due to the commencement of yam and breadfruit harvest season. Banking data also showed proceeds for agricultural products increased by 65.8%. Fisheries receipts also more than trippled over the month indicating a lively sector.

The distribution sector remained strong over the month as the volume of private container registrations increased by 9.3% while business containers remained constant. This was supported by lower prices over the month contributed to higher purchasing power. International air arrivals declined by 34.1% affecting activities in the hotels and restaurants sector. A further decline in cruiseship arrivals also affected tourism activities following an unexpected lift in the sector from redirected ships in the previous month. The transport sector continues to benefit from the low global oil price as local fuel prices continued to fall during the month. Vehicle import payments increased by 7.8% over the month which indicates a rise in future consumption. However, new vehicle registrations declined by 27.8% over the month.

Headline inflation decreased by 0.7% over February. This was caused largely by the declining global oil prices which affected both domestic and imported prices. The largest decline was in Domestic power & fuel prices. Prices for the Household Operation, Housing and Transportation components were all affected by the lowered energy prices. However, despite lower food prices in New Zealand and a monthly average depreciation of the New Zealand dollar against the Tongan pa'anga, imported food prices rose over the month suggesting prices being driven by high demand and low supply.

Over the year, inflation was -1.1% being the first deflation rate since May 2013. This was largely driven by lower Domestic fuel & energy prices following the decline in global oil prices. In contrast, Imported prices increased by 0.1%, largely driven by rises in food prices.

On a trade-weighted basis, both the nominal effective exchange rate (NEER) and the real effective exchange rate (REER) depreciated by 0.6% and 1.5% respectively over the month of February. This largely reflects the weakening of the Tongan pa'anga against the New Zealand dollar in month-ended terms. Furthermore, both the NEER and the REER fell by 0.1% and 3.1% respectively over the year to February 2015.

Economics Department | National Reserve Bank of Tonga
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The balance of the official overseas exchange transactions was a $5.8 million deficit in February compared with a deficit of $6.4 million in January. The improvement was due to an increase in the current account. Import payments fell by 16.8% reflecting fewer payments for fuel imports and wholesale & retail goods. Export receipts doubled over the month to $1.5 million driven by a significant increase in marine exports. The monthly average depreciation of the Tongan pa'anga against the U.S. dollar supports the higher export earnings. Travel receipts and payments fell by $0.1 million and $2.7 million respectively. This is consistent with declines in both international arrivals and departures following the end of the holiday season. Similarly remittances fell by 7.9% over the month to $16.2 million. Foreign reserves at the end of February therefore fell by 2.0% to $281.3 million, sufficient to cover 8.6 months of imports.

Broad Money fell by 0.3% (T$1.2 million) over February due to a decline in net foreign assets more than offsetting an increase in net domestic assets. The decline in total domestic demand deposits and currency in circulation support the fall in broad money. Banking system liquidity fell by 4.2% to T$149.9 million over the month. In year ended terms, banking system liquidity rose by 4.8%.

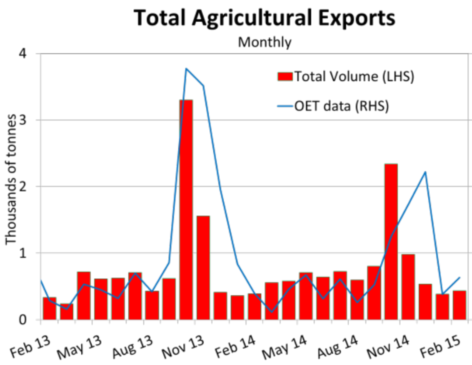
Bank lending rose by 1.7% ($4.9 million) over the month. This was driven by a 2.9% increase in lending to households, mainly housing loans. Personal loans and business lending slightly increased. Lending from the managed funds during the month recorded more than 25 new approved loans.

In year ended terms, total bank lending grew by 9.4%. This was a result of a 12.3% and a 7.0% increase in household and business lending respectively. Including loans extended by non-banks, total lending only increased by 6.8%, reflecting lower on-lent loans by the government over the year.

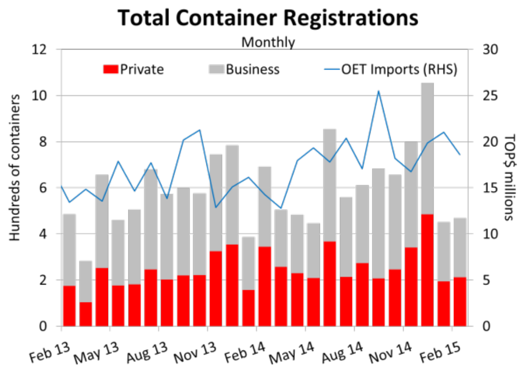
Weighted average interest rate spread widened over the month to 6.51% by 0.18 percentage points due to an increase in weighted lending rates outweighing a rise in the weighted deposit rates. An increase in interest rates on loans to businesses contributed to the higher weighted lending rates, whilst increases in the volume of savings and long term deposits resulted in higher weighted average deposit rates.

Net credit to government continues to increase by about 8% over February due to lower government deposits. Official receipts rose by 25% during the month while the official payments abroad doubled.

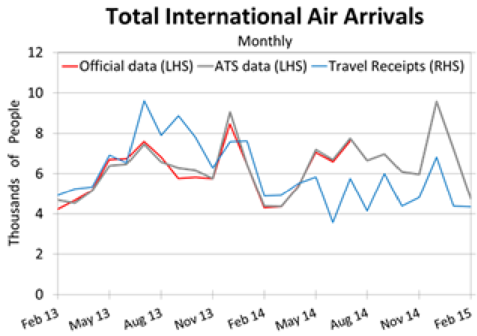
In summary, the domestic economy bounced back after a downturn in the previous month. Deflation was expected as global oil prices continued to remain low. This lower prices in turn supported economic activity over the month. Foreign reserves are anticipated to remain comfortably above the NRBT's minimum range of 3-4 months of imports. Credit growth is still on the rise and bank liquidity remains high. Given these developments, the existing monetary policy setting is therefore considered appropriate. The NRBT is mindful of the impact of a continued deflation and will continue to closely monitor the country's economic developments and financial conditions to adjust the monetary policy stance for macroeconomic stability and economic growth.



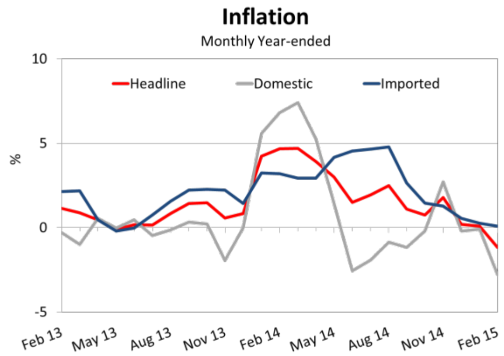
Source: NRBT; Ministry of Agriculture, Forestry, Food and Fisheries



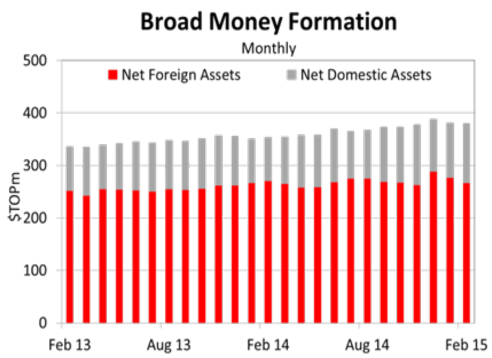
Sources: NRBT, Statistics Department, Tonga Ports Authority



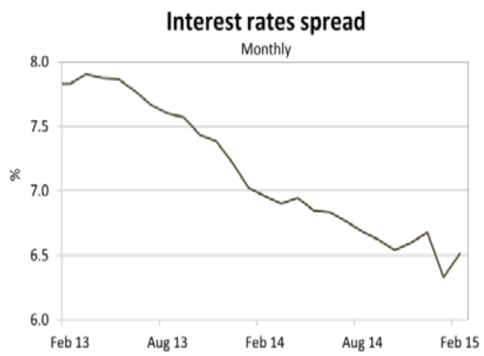
Sources: Department of Statistics; Air Terminal Services; Banking System



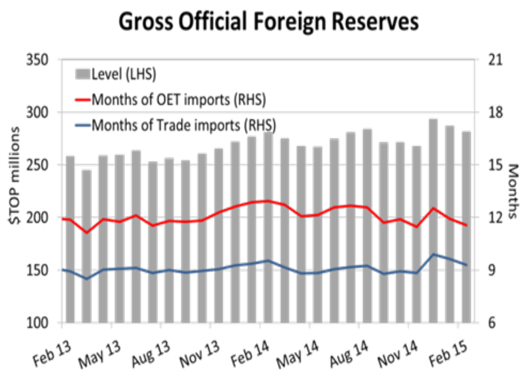
Source: Tonga Department of Statistics; NRBT



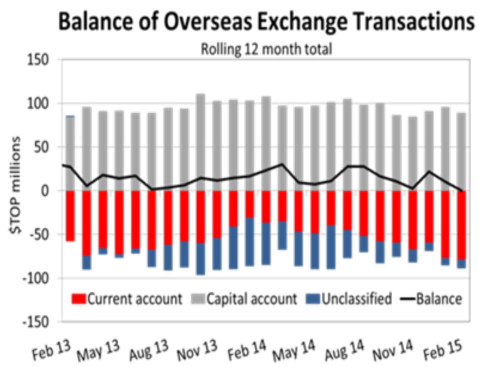
Sources: NRBT, Banking System



Source: Banking systems; NRBT



Sources: Banking system; Foreign exchange dealers; NRBT



Sources: Banking system; Foreign exchange dealers; NRBT