Monthly Economic Review

For January 2015

Global developments over the month of January provided mixed settings for domestic growth. Unemployment rate in the U.S. rose 0.1 percentage points to 5.7% and in Australia by 0.3 percentage points to 6.4%. The Australian and New Zealand dollar also fell on the back of a strengthening US dollar. However, imports, particularly food items became cheaper and helped keep inflation low. Global oil price also fell below USD$50 a barrel to its lowest level since March 2009.

The domestic economy took a downturn over the month of January. However, this reflects more the seasonality of economic activities rather than signalling a weakening economy. The primary sector contracted in line with declines in agricultural and fisheries activities. Agricultural exports volume declined by 29.8% partly due to bad weather but also because of seasonality of crops. Banking data showed proceeds for agricultural products declined by 82.8%. Proceeds for fisheries also declined by 23.3%. The services sector also weakened indicating a decline in consumption over the month. Container registrations declined by 57.3%, after reaching its highest level on record in the previous month during the festive season, driving a contraction in the distribution sector. Activities in the hotels and restaurants sector slowed down in line with international air arrivals decreasing by 24.5%. However, tourism activities received a boost from the unexpected arrival of 3 cruiseships redirected from neighbouring countries due to weather conditions in the region. The cruiseship arrivals together with further declines in domestic fuel prices buoyed the transport sector while vehicle registrations recorded a decline of 22.5%.

Moderating the declines in economic activities, the financial sector improved driven by a rise in domestic credit. Increases in individual housing lending and business lending to construction and manufacturing companies also supported the expansion of the secondary sector. Moreover, liaison with construction companies indicated that more houses were released for reconstruction over the month under the Ha’apai project. Additionally, the education sector was revitalised with the commencement of the school year during the month.

Coinciding with the start of the school year, Clothing & Footwear prices increased by 5.1% over the month seemingly due to high demand for uniform and sandals. Food prices also contributed to the rise in CPI over the month. The recent drought affected domestic food supply, leading to higher domestic Food prices, whereas the rising food prices in New Zealand contributed to the higher imported prices but were softened somewhat by the depreciating New Zealand dollar over the month. Furthermore, Imported Tobacco prices rose by 9.0% after being stable since February 2013.

In year ended terms, headline inflation eased to 0.1% mainly due to spillover effects from the lower global oil prices offsetting the rises in Food prices. Imported Tobacco prices also increased over the year by 8.8%, which is the largest increase since June 2011.

Economics Department | National Reserve Bank of Tonga
Release date: 11th March 2015

Over January, both the NEER and the REER rose by 1.1% and 3.1% respectively. This largely reflects the general appreciation of the Tongan pa'anga against the currencies of its major trading partners. In year ended terms, however, the NEER rose slightly, whilst the REER fell by 1.6%.

The balance of the official overseas exchange transactions was a $6.4 million deficit in January compared with a surplus of $25.8 million in December. The turnaround resulted from higher net outflows in the current account. Import payments rose by 45.3%, with more payments made for the import of oil and wholesale/retail goods. Export receipts fell by 73.6%, after peaking at $2.6million last month mostly due to the decline of agricultural proceeds. Travel receipts and remittances fell by 35.8% and 33.1% respectively, with the end of the Christmas season having contributed to the decline. Foreign reserves at the end of January fell by 2.2% to T$287.2 million, sufficient to cover 9.9 months of imports.

The decline in foreign reserves more than offset a rise in domestic credit which led to Broad Money falling by 1.7% or T$6.5 million to T$380.8m. The decline in currency in circulation and total domestic demand deposits support the fall in broad money.

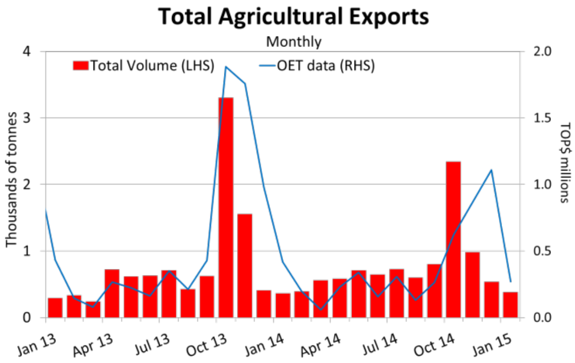
Banking system liquidity rose by 1.7% (T$2.7 million) to T$156.4 million over the month. In year ended terms, banking system liquidity also rose by 13.2%.

Bank lending rose over the month mainly due to an increase in lending to public enterprises and household lending. Lending from the managed funds facilitated by Tonga Development Bank recorded more than 20 new approved loans totaled to more than $0.9 million. The new loans were largely under the Education sector in preparation for the new school year. Total outstanding balance as at January 2015 reached more than $2.0 million. In year ended terms, domestic credit grew by 7.7%. Total lending including loans extended by non-banks increased only by 5.2%, reflecting the wind down of Government on-lending.

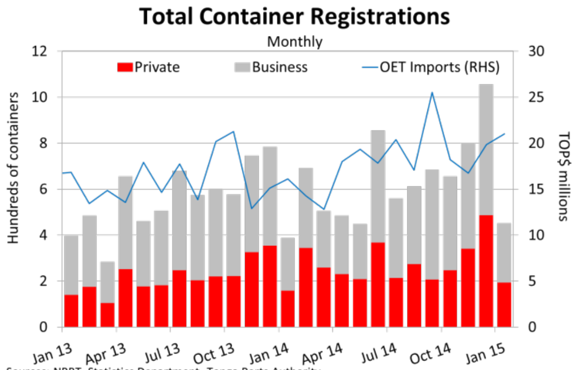
Weighted average interest rate spread narrowed further over the month to 6.33% due to a fall in weighted lending rates while weighted deposit rates increased slightly. A rise in lower interest rates lending particularly the 7.2% increase in loans to public enterprises contributed to the lower weighted lending rates, while increases in the volume of long term deposits and savings resulted in the increase in weighted average deposit rates.

Net credit to government improved by about $3 million to -$57 million mainly due to lower government deposits. This is also much higher compared to January of last year. However, official overseas exchange transactions recorded a surplus of around $0.8 million over the month.

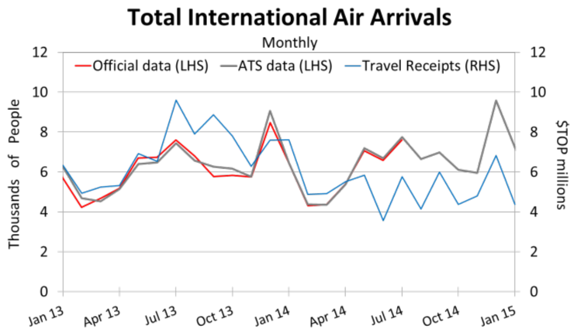
In summary, the NRBT expects the domestic economy to rebound in the near term. Inflation is within acceptable levels as global oil prices continue to fall. Foreign reserves are anticipated to remain comfortably above the NRBT's minimum range of 3-4 months of imports. Credit growth is still on the rise and bank liquidity is at its highest level. Given these developments, the existing monetary policy setting is therefore considered appropriate. The NRBT 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.



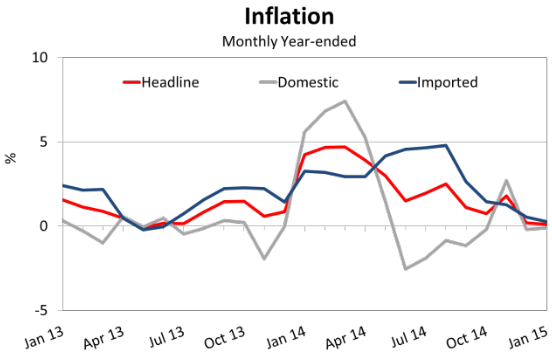
Source: NRBT; Ministry of Agriculture, Forestry, Food and Fisheries



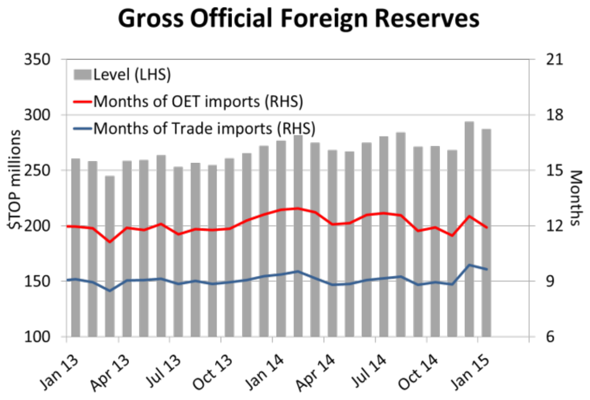
Sources: NRBT, Statistics Department, Tonga Ports Authority



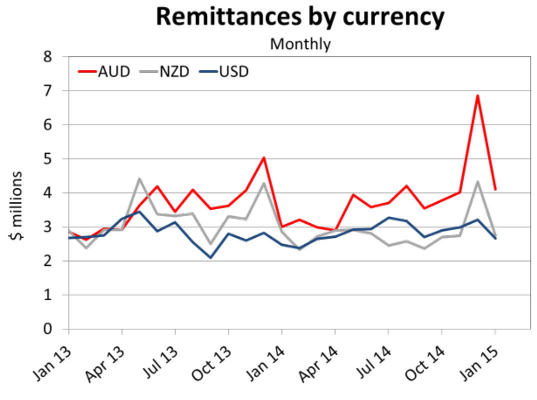
Sources: Department of Statistics; Air Terminal Services; Banking System



Source: Tonga Department of Statistics; NRBT



Sources: banking system; foreign exchange dealers; NRBT



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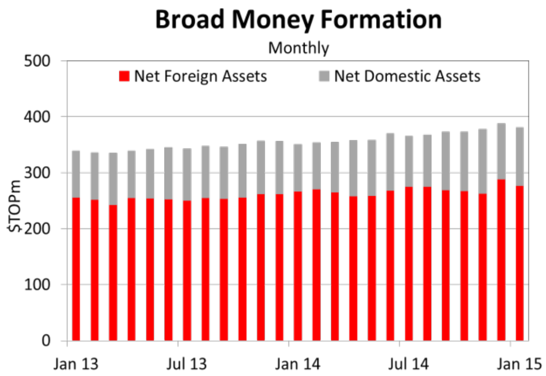
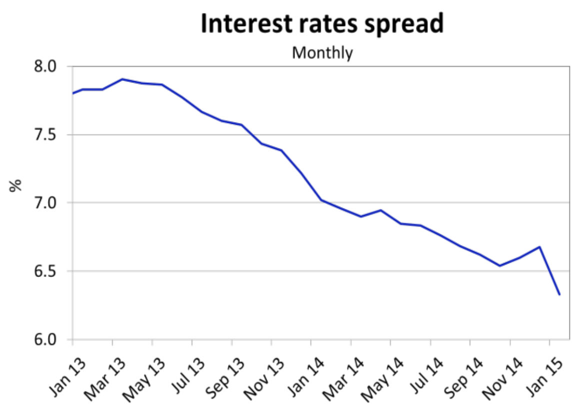


Sources: NRBT, Banking System



Source: Banking systems; NRBT.