



## MONTHLY ECONOMIC REVIEW

Vol. 4

No. 4

Month Ended: April 2017

As reported by the International Monetary Fund (IMF) in its April 2017 World Economic Outlook (WEO) report, global growth for 2017 is expected to increase by 3.5% an upward revision from the previous projection of 3.4%. The US is anticipated to be the main driver of growth amongst advanced economies with an upward revised GDP growth of 2.3% for 2017 (from 2.2%). However, recent statistics reported by the US Bureau of Economic Analysis reflect a slowdown in economic growth due to a sharp decline in consumer spending as well as business investments. Tonga's remaining major trading partners Australia and New Zealand experienced a slight slowdown in economic growth. More specifically, Australia noted an improvement in the unemployment rate yet experienced slow growth in mining activities. New Zealand recorded a fall in agricultural output and weak manufacturing growth.

Domestically, economic activities reflected slow growth during the month. Primary sector activities in April 2017 were slightly similar to March 2017, the total volume of agricultural exports declined by 45.6 tonnes (7.8%) largely due to a 66.0 tonnes (22.6%) decline in cassava exports. According to the Reserve Bank's liaison program, the domestic agricultural and fish markets were similar to the previous month with no significant trend. Activities in the construction sector continued to lift performance in the secondary sector, supported by an increase in housing loans by \$2.0 million over the month and also rise in the number of electricity consumers by 45 customers.

Growth in the tertiary sector was quite sluggish during the month. This was reflected in a slight decline in the total number of container registrations by 16 containers (1.8%) over the month. Lower registrations of business containers outweighed a rise in private containers, indicating a strong informal distribution sector. This was consistent with the \$11.2 million decline in import payments in April particularly payments for wholesale and retail goods. There were no cruise ships arriving during the month, resulting in a decline in international arrivals by 1,459 passengers. However, total visitors increased by 1,293 passengers and may have supported the tourism industry. Vehicle registrations slightly rose by 17 vehicles (5.9%).

The total number of job advertisements increased by 4 vacancies over April 2017 however fell over the year by 9 vacancies, led by recruitment intentions in the services sector. This indicated a rising demand for labour in Tonga and may assist in reducing the unemployment rate.

Headline inflation increased over the month by 0.3% driven by the prices of local food and electricity. Domestic inflation rose by 0.9% at the end of April due to the seasonality of local food and increased prices of electricity. However, imported prices decreased by 0.2% due to a decrease in prices of food, and fuel which outweighed the increase in prices of kerosene, and liquid petroleum gas.

Prices	Monthly		Annual	
	Apr-17	Mar-17	Apr-17	Mar-17
Headline Inflation (%)	0.3	0.4	9.5	9.4
Domestic prices	0.9	0.1	5.7	4.9
Imported prices	-0.2	0.6	12.7	13.2

Source: Statistics Department

Despite the relatively low increase over the month, annual headline inflation rose by 9.5%. This was due to imported prices being at a very low level in April 2016, which declined by 6.5%. However, in April 2017 imported prices rose by 12.7% contributing 6.9 percentage points to the annual headline inflation. All imported food categories rose except for imported fruits and vegetables, led by a 23.2% increase in prices of meat, fish & poultry due mainly to a 37% and 27% increase in the price of mutton flaps and chicken pieces respectively. This was followed by the prices of other food components which increased by 15.6%, for items such as sugar and flour. The prices of these imported food continued to reflect the excise taxes and custom duties imposed on various imported food in July 2016. Similarly, the price of Winfield blue tobacco increased by 32.5%. Additionally, the increase in world oil prices drove the price of fuel higher by 23.6%, followed by an 8.5% increase in the prices of kerosene and liquid petroleum gas. Similarly, the domestic annual inflation rate rose by 5.7% largely due to the rise in electricity price, continued short supply of kava-Tonga, and volatile local food prices. The price of electricity rose by 22.7% whilst the price of kava-Tonga increased by 55.5% over the year, followed by a 3.5% rise in the prices of local food.

	Monthly			Annual	
	Apr-17	Mar-17	% Growth	Apr-16	% Growth
Nominal Effective Exchange Rate Index	90.7	91.4	-0.8	91.3	-0.6
Real Effective Exchange Rate Index	104.7	105.3	-0.6	97.8	7.0

Source: NRB

In April 2017, the United States Dollar (USD), Chinese Yuan (CNY), Japanese Yen (JPY), Euro Dollar (EUR), British Pound (GBP) and Fijian Dollar (FJD) appreciated against the Tongan Pa'anga (TOP) while the Australian Dollar (AUD) and New Zealand Dollar (NZD) depreciated against the TOP. As a result, both the Nominal Effective



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Exchange Rate (NEER) index and the Real Effective Exchange Rate (REER) index slightly decreased over the month. In annual terms, the NEER index continued to fall while the REER index rose. The rise in the REER index reflected Tonga's higher headline inflation rate relative to its trading partners, which may impact the international competitiveness of the Tongan exports of goods and services.

	Monthly			Annual	
	Apr-17	Mar-17	% Growth	Apr-17	% Growth
<b>OET Receipts (TOP \$ million)</b>	<b>53.7</b>	<b>49.4</b>	<b>8.6</b>	<b>735.8</b>	<b>18.3</b>
Export receipt	1.5	1.6	-10.7	23.1	53.1
Travel receipts	7.1	7.1	0.0	102.5	25.1
Private transfers	20.1	21.2	-4.9	256.8	15.9
Others	25.0	19.6	27.8	353.3	72.6
<b>OET Payments (TOP \$ million)</b>	<b>45.6</b>	<b>59.0</b>	<b>-22.8</b>	<b>619.3</b>	<b>11.8</b>
Import payments	25.9	37.2	-30.2	356.1	13.9
Services payments	10.2	11.9	-14.9	143.4	22.2
Primary Income payments	0.7	1.5	-56.6	20.9	26.4
Others	8.8	8.4	4.7	98.8	-7.9

Source: Banking System

Total OET receipts rose over the month of April 2017, by 8.6% to \$53.7 million. This was mainly driven by the rise in commercial banks' interbank transfers. Official transfer receipts also rose underpinned by receipts of official grants by the Government for technical assistance and other current expenditures. In year ended terms, total OET receipts rose by 18.3% which was largely owing to the higher inflows of private remittances and official grant receipts. The celebrations and annual events during the year supported the annual growth in remittances. Majority of the annual remittance receipts were in USD and AUD which was supported by the depreciation of the TOP against these currencies. This coincided with the positive economic growth in these countries.

Total OET payments decreased over the month of April 2017 by 22.8% to \$45.6 million due mainly to lower import payments. Services, primary income and transfer payments also decreased. Lower payments for oil and wholesale & retail goods drove the decline in imports. This was consistent with the decline in container registrations over the month. Total OET payments however rose over the year by 11.8%, which was mainly driven by higher imports payments particularly payments for wholesale and retail goods.

The overall OET balance for April 2017 was therefore a surplus of \$5.7 million. This contributed to the rise in the official foreign reserves to \$371.7 million in April 2017,

<sup>1</sup> Method of calculation changed in February 2017 to include both imports of goods & services (previous method used imports of goods only)

	Monthly			Annual	
	Apr-17	Mar-17	% Growth	Apr-16	% Growth
Foreign Reserves (\$ in million)	371.7	366.0	1.5	322.9	15.1
Import Coverage (months)	6.8	6.7		6.7	

Source: Banking System, Statistics Department

equivalent to 6.8 months<sup>1</sup> of imports cover, which is still above the Reserve Bank's minimum range of 3-4 months.

Broad money (money supply) increased over April, due to rises in both net foreign and net domestic assets. The rise in the foreign reserves contributed to the increase in net foreign assets whilst the higher cash withdrawals by the commercial banks from the Reserve Bank vault during the month drove the increase in net domestic assets. This was to cater for the replenishment of cash holdings of the commercial banks in the outer islands and the foreign exchange dealers. Over the year, broad money also rose driven solely by an increase in net foreign assets. Higher foreign reserves continued to be the underlying reason for the annual growth.

Money	Monthly			Annual	
	Apr-17	Mar-17	% Growth	Apr-16	% Growth
Money Supply (\$ in million)	509.9	503.6	1.3	448.3	13.7
Net Foreign Asset	395.4	389.7	1.5	321.8	22.9
Net Domestic Asset	114.6	114.1	0.4	126.8	-9.7

Source: Banking System, NRBT

The banking system recorded a \$3.6 million (1.3%) increase in liquidity (reserve money)<sup>2</sup> over April. This resulted from higher cash withdrawals by the commercial banks from the Reserve Bank vault leading to a rise in the currency in circulation. Banks' total loans to deposit ratio dropped slightly to 74.5% in April from 75.5% in the previous month. This was due to higher deposits over the month which also coincided with the rise in foreign reserves. However, the loans to deposit ratio continued to remain below the 80% minimum loan to deposit ratio target which indicates excess liquidity in the banking system remains and that there is capacity for further lending by the banks.

Lending	Monthly			Annual	
	Apr-17	Mar-17	% Growth	Apr-16	% Growth
Total Lending (\$ in million)	391.9	391.2	0.2	344.0	13.9
Business lending	167.7	168.7	-0.6	162.9	3.0
Household lending	222.9	221.3	0.7	179.8	24.0
Other lending	1.3	1.2	10.8	1.2	3.2

Source: Banking System

Total banks' lending rose over the month and over the year to another record high of \$391.9 million. Lending to households was the only driver of the overall growth over

<sup>2</sup> Sum of currency in circulation, exchange settlement account balances, and required reserve deposits.



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April as a result of more loans being lent out for private housing constructions. Despite business loans declining over the month, it rose over the year. Lending to the manufacturing and agricultural sectors were the main contributors to the increase in annual business loans. This supported the yearly rise in agricultural exports volume and other domestic economic activities. Furthermore, the lower interest rates from the Government Development Loans have also supported the higher lending to these sectors. Loans to households also rose significantly over the year driven yet again by housing loans. Additionally, vehicle loans and other personal loans also contributed to the annual increase in household loans. Credit growth over the year to April was similar to the growth over the year to March, recording a \$47.9 million (13.9%) increase.

Interest Rates	Monthly			Annual	
	Apr-17	Mar-17	Growth (bps)	Apr-16	Growth (bps)
Weighted Average Banks Deposit Rate (%)	2.167	2.203	-3.6	2.255	-8.8
Weighted Average Banks Lending Rate (%)	7.856	7.845	1.1	7.968	-11.1
Weighted Average Interest Rate Spread (%)	5.689	5.642	4.7	5.712	-2.3

Source: Banking System, NRB

The weighted average interest rate spread widened to 5.689% in April. This was due to a decline in the weighted average deposit rate coupled with a minimal increase in the weighted average lending rate over the month. The weighted average deposit rate narrowed, driven by a fall in the demand and saving deposit rates. On an annual basis, the weighted average interest rate spread narrowed by 2.3 basis points. This resulted from a decline in weighted average lending rate outweighing a decline in the weighted average deposit rate. Lending rates for household loans and business loans namely the manufacturing, agricultural, and construction sectors fell

over the year to April. This supported the higher credit growth recorded over the month as well as over the year. Deposit rates for all deposit categories fell with demand deposit rates contributing the most to the annual decline.

Net credit to Government declined over the month and over the year by \$3.4 million and \$39.9 million respectively driven by a rise in government deposits. The receipts of the government grant funds during the month supported the higher deposits.

The Reserve Bank's outlook for strong domestic economic activity remains in the medium term. The level of foreign reserves is also expected to remain at comfortable levels supported by expected higher receipts of remittances and foreign aid and this will be partially offset by the projected rise in imports. Upward inflationary pressure remains in the near term due to the impact of the increase in custom duty and excise tax effective on 1<sup>st</sup> July 2016, however it is expected to fall below the Reserve Bank's inflation reference rate of 5% per annum in 2017/18. In light of the above developments and that the banking system remained sound, the Reserve Bank Board maintained its current accommodative monetary policy measures. The Reserve Bank will remain vigilant and continue to closely monitor early signs of vulnerability, developments in the domestic and global economy, and update its monetary policy setting to maintain internal and external monetary stability, and to promote a sound and efficient financial system in order to support macroeconomic stability and economic growth.