



Global fiscal support critical amidst COVID-19 crisis

The IMF reported in its January 2021 Fiscal Monitor Update highlights that global fiscal support amounting to \$14 trillion played a significant role in mitigating the downside effects of the COVID-19 pandemic. The US Bureau of Economic Analysis reported that personal income in the US rose by 10.0% in January 2021. The Government's social benefits rose as part of its COVID-19 response program largely drove this rise. Meanwhile, Australia's economic growth is projected to rebound by 3.5% in 2021 from -2.0% growth in 2020 as more business activities resume. The Reserve Bank of New Zealand, in its February 2021 Monetary Policy Statement, anticipates a 2.4% contraction in economic growth over the year to March 2021, as business investments remain subdued together with projected higher unemployment.

Primary sector slowing down

The primary sector performance slowed down in January 2021. Total agricultural exports decreased by 654.6 tonnes (65.5%) over the month, driven mainly by the decline in exports of root crops such as cassava, taro, yam, and fruit products, particularly squash. It also declined over the year by 2,012.4 tonnes (16.7%). Agricultural export proceeds fell by \$0.3 million (32.2%) in January 2021 and annually by \$1.5 million (18.1%). However, marine export proceeds slightly rose by \$0.01 million (1.3%) over the month. Still, they declined over the year to January 2021 by \$5.2 million (53.0%).

The industry sector recorded mixed growths in January 2021. Lending for the utility sector increased by \$0.2 million over the month. However, lending to the construction sector decreased by \$0.3 million (1.4%), coinciding with the decline in import payments for construction materials which fell by \$1.6 million (39.9%). A multi-donor project in the outer islands to rehabilitate the electricity network, provide solar power infrastructure and energy storage by the Outer Islands Renewable Energy Project (OIREP) and other donors will significantly assist with economic developments in rural areas and contribute to sectoral growth.

The services sector continued to weaken in January 2021. The additional quarantine measures in both overseas and local ports resulted in a significant drop in total container registrations over the month by 248 registrations (22.0%). The decrease in both business and private container registrations contributed to this decline, indicating a slowdown in the wholesale and retail trade activities following the festive season. January international arrivals declined by 48 passengers and by 97,357 passengers (89.6%) over the year, reflecting the international border closures' continued impact. This coincides with an annual decline of \$101.4 million in travel receipts. Vehicle registrations declined by 42 registrations over the month. Meanwhile, the Government continues its efforts to stimulate the economy and provide relief for those affected

by the pandemic supported by additional funds from development partners.

Some vacancies in public administration

The Reserve Bank's survey showed a slight increase in vacancies over the month by 4 job vacancies (45.5%) and mostly for public administration, particularly for Government. However, job vacancies continued to decline in over the year to January 2021 by 275 vacancies (54.9%). The COVID-19 pandemic is expected to continue restricting employment opportunities.

Annual headline inflation continues to rise

Inflation increased in January and was attributed to the rise in both local and imported prices. The increase in domestic prices was significantly driven by food items, particularly for vegetables and root crops, largely reflecting the seasonality

Table 1: Inflation Rates

Prices	Monthly		Annual	
	Jan-21	Dec-20	Jan-21	Jan-20
Headline Inflation (%)	0.7	1.3	1.3	0.6
Domestic prices	0.8	2.1	0.7	-2.9
Imported prices	0.7	0.6	1.8	3.6

Source: Statistics Department

of these food items, coupled with the impact of unfavourable weather conditions. However, imported prices rose due to higher fuel prices and food items. Demand for oil in the global market recovered coupled with the higher freight rates, contributed to higher fuel prices for the month, whilst rising food prices in trading partner countries led to higher prices for imported food items.

Over the year to January 2021, inflation rose by 1.3%, the highest on record since April 2020. Rising food prices, clothing & footwear and alcoholic beverages drove the increase in imported items, while increased local prices were due to higher food items, tobacco and clothing & footwear. This trend in prices is expected to continue. Hence, inflation may continue to trend upward in the near future closer to the NRBT 5% reference rate.

Table 2: Average annual prices of selected items

Items (\$ per kg)	Unit	Jan-21	Jan-20	Annual
				Change
Domestic				
Octopus	1kg	\$29.13	\$22.24	\$6.89
Tomatoes	1kg	\$8.79	\$5.83	\$2.96
Eggs	1 tray	\$18.97	\$16.08	\$2.89
Stringed fish (mixed)	1kg	\$10.00	\$9.00	\$1.00
Imported				
Pall Mall	1kg	\$23.14	\$19.29	\$3.85
Mutton Flaps	1 kg	\$17.50	\$16.44	\$1.06
Turkey tails	1 kg	\$10.34	\$9.36	\$0.98

Source: Statistics Department

Effective exchange rates declined further

Table 3: Effective Exchange Rates

	Monthly			Annual	
	Jan-21	Dec-20	%	Jan-20	% Growth
Nominal Effective Exchange Rate Index	85.7	86.5	-1.0	91.7	-6.5
Real Effective Exchange Rate Index	98.1	99.7	-1.6	106.2	-7.6

Source: National Reserve Bank of Tonga

The Nominal Effective Exchange Rate (NEER) fell again in January 2021 as major trading currencies appreciated against the Tongan Pa'anga (TOP) except for the USD. The Real Effective Exchange Rate (REER) index also fell in line



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with Tonga's low inflation rates relative to its major trading partners.

In year ended terms, both the NEER and REER declined, indicating an improvement in Tonga's trade competitiveness with trading partners, supporting export proceeds and remittance receipts.

New government loan pushes foreign reserves higher

Table 4: Foreign Reserves

	Monthly			Annual	
	Jan-21	Dec-20	% Growth	Jan-21	% Growth
Foreign Reserves (\$ in million)	705.3	675.6	4.4	482.9	39.9
Import Coverage (months)	12.0	11.7	2.6	7.4	62.4

Source: National Reserve Bank Tonga

The foreign reserves rose in January 2021 by \$29.7 million to \$705.3 million and equivalent to 12.0 months of imports. This was mainly attributed to the receipt of a government loan from the IMF. Funds related to COVID-19 and TC Harold were also received and contributed to the monthly rise. Similarly, foreign reserves increased significantly in the year to January 2021 by \$222.4 million. This was driven largely by receipts of budget support, official grants, and remittances. The foreign reserves are held mostly in USD, AUD, and NZD.

Table 5: Remittance Receipts

	Monthly			Annual		
	Jan-21	Dec-20	% Growth	Jan-21	Jan-20	% Growth
Remittance (\$ in million)	32.3	43.8	-26.2	403.2	350.3	15.1

Source: National Reserve Bank Tonga

Remittances fell in January 2021 by \$11.5m to \$32.3 million following the high month of remittances received in December. All categories declined over the month, mostly private transfer receipts, particularly NZD and AUD receipts. However, remittances continued to rise over the year, increasing to \$403.2 million in January 2021. This stemmed from higher private transfers and compensation of employees.

Table 6: Overseas Exchange Transactions

	Monthly			Annual		
	Jan-21	Dec-20	% Growth	Jan-21	Jan-20	% Growth
Overall Balance	29.7	85.3	-65.2	222.4	3.9	5567.5
Current Account	18.2	75.5	-124.2	185.0	-18.4	906.8
Merchandise Trade	-36.7	-36.7	-0.1	-412.8	-410.4	-0.6
Services	-2.1	-4.3	52.0	-7.5	27.9	-126.9
Income	3.4	3.1	7.0	22.0	2.3	860.5
Transfers	53.7	113.4	-52.7	583.3	361.8	61.2
Capital Account	3.5	4.1	-15.9	41.1	31.3	31.6
Financial Account	8.0	5.7	-40.4	-3.7	-9.0	59.0

Source: Banking Systems

Overall, Overseas Exchange Transactions (OET) recorded a lower surplus of \$29.7 million in January 2021, compared to the \$85.3 million surplus in the previous month. This resulted from a substantial decline in OET receipts, primarily from official transfers following the influx of budget support from the World Bank in the last month.

In the year to January 2021, the OET balance surplus rose significantly by \$218.5 million on the back of a higher

current account surplus. Higher official transfer receipts supported this. The capital account surplus also increased due to rises in both official and private capital receipts. The financial account deficit also narrowed over the year due mainly to lower interbank transfer payments.

Broad money slightly fell

Table 7: Broad Money

	Monthly			Annual	
	Jan-21	Dec-20	% Growth	Jan-20	% Growth
Broad money (\$ in million)	706.9	707.5	-0.1	592.5	19.3
Net Foreign Asset	735.5	705.9	4.2	495.7	48.4
Net Domestic Asset	-27.4	2.4	-1220.4	97.2	-128.2

Source: Banking System, National Reserve Bank of Tonga

The decline in net domestic assets from higher government deposits offset the higher net foreign assets from the receipts of government loans and grants. This lowered broad money over the month by \$0.6 million (0.1%). However, over the year, broad money rose by \$114.5 million (19.3%) mainly due to higher foreign reserves.

Liquidity in the financial system continues to expand

Table 8: Reserve money

	Monthly			Annual	
	Jan-21	Dec-20	% Growth	Jan-20	% Growth
Reserve money (\$ in million)	424.9	422.8	0.5	301.3	41.0

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the financial system increased further over the month of January 2021, by \$2.1 million (0.5%) and over the year by \$123.6 million (41.0%) to \$424.9 million. The commercial banks' ESA (Exchange Settlement Account) increased the most, coinciding with the commercial banks' increase in deposits to the Reserve Bank vault. Required reserves also increased, corresponding to the rise in total deposits. Currency in circulation, however, decreased over the month but rose annually.

Credit growth slightly decreases

Table 9: Total Lending

Lending	Monthly			Annual	
	Jan-21	Dec-20	% Growth	Jan-20	% Growth
Total Lending (\$ in million)	494.5	495.4	-0.2	500.7	-1.2
Business lending	236.4	236.3	0.05	239.7	-1.4
Household lending	258.1	259.1	-0.4	261.0	-1.1
Other lending	0.0	0.0	0.0	0.0	0.0

Source: Banking System, National Reserve Bank of Tonga

The banks' total lending slightly fell in the month and in the year to January 2021. All categories of household loans decreased over the month, notably on loans to businesses in the construction, manufacturing, and trade sectors. Similarly, loans offered to public enterprises, professional & other services, manufacturing, and utilities sectors declined over the year and loans for households' other personal loans.

In January 2021, the banks' total deposits hit \$703.9 million. The first time deposits rose above the \$700 million mark. This was due mainly to an increase of \$17.2 million (2.5%) in the month driven largely by churches' time deposits, public enterprises, and individuals' demand deposits. The



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decline in total lending coupled with higher deposits drove the loans to deposit ratio lower in January 2021 to 67.8% from 68.6% last month and below the 80% minimum.

Weighted average interest rate spread widens

Table 10: Weighted Average Interest Rates

Interest Rates	Monthly			Annual	
	Jan-21	Dec-20	Growth	Jan-20	Growth
Weighted Average Banks Deposit Rate (%)	1.972	1.982	-1.0	1.995	-2.3
Weighted Average Banks Lending Rate (%)	7.681	7.681	-0.05	8.033	-35.3
Weighted Average Interest Rate Spread (%)	5.709	5.699	1.0	6.038	-32.9

Source: Banking System, National Reserve Bank of Tonga

Both the weighted average deposit rate and the weighted average lending rate declined over the month. This widened the weighted average interest rate spread again in January 2021 by 1.0 basis points. All three categories of deposit interest rates decreased whilst weighted average lending rates declined slightly. The lower average lending interest rates stemmed mostly from lower interest rates on loans to the professional & other business services, agriculture, and households' vehicle loans.

In year ended terms, the weighted average interest rate spread narrowed by 32.8 basis points to 5.709%. This resulted mainly from lower weighted average lending interest rates on loans to households for other personal loans and businesses in the mining & quarrying, construction, and utility sectors. On the other hand, deposit interest rates slightly declined (term and savings).

Outlook

The expected downturn in domestic economic growth remains. Against this background, the Reserve Bank's monetary policy stance remains accommodative. Furthermore, the Reserve Bank continues 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.