



### Strong economic recovery projected for 2021

The World Bank Group (WBG) in June 2021 projects the global economy to rebound by 5.6% in 2021, following the 3.5% contraction in 2020. This upward growth projection for 2021 stems from a sharp recovery in major economies, particularly the US, driven by sizeable fiscal support. The US is expected to expand by 6.8% in 2021, underpinned by higher personal income and consumption spending. Meanwhile, the Australian Bureau of Statistics reported that the Australian economy increased by 1.8% in the March quarter of 2021 with an annual rate of 1.1%. Higher export prices, investments, and consumption spending drove this increase. The New Zealand economy also grew by 1.6% in the first quarter of 2021, supported by higher growth in the services and manufacturing sectors, however, it declined by 2.3% annually.

### Slight improvement in domestic economic activities

The primary sector growth was mostly positive in May 2021. Total agricultural exports increased over the month by 79.0 tonnes (11.9%), driven by higher exports of cassava and taro. This coincides with slight rise in agricultural exports proceeds by \$0.3 million (162.6%). Annually, both agricultural exports volumes and proceeds fell by 2,567.3 tonnes (20.0%) and \$1.5 million (18.6%) respectively, stemming from lower exports of squash. Total marine exports also rose over the month by 0.2 metric tons (0.1%), largely owing to an increase in the export of shark meat. Additionally, local marine production also rose over the month by 0.7 metric tons (5.7%), mainly due to the increase in octopus and finfish production. However, the marine exports proceed in the same period dropped by \$0.1 million (22.3%). Over the year to May 2021, total marine exports volumes and proceeds decreased by 842.1 metric tons (38.5%) and \$4.3 million (48.2%).

The secondary sector showed mixed outcomes during the month. Loans extended to the secondary sector slowed during the month, particularly lending to the manufacturing and utility sectors. However, lending to the construction sector increased over the month by \$0.4 million (2.0%). In May 2021, three new manufacturing businesses were registered. A new classroom building for the Tonga Police was completed under Pacific Resilience Project (PREP) as part of the TC Gita recovery program. Electricity consumption and production fell by 0.1 million kilowatts (1.3%) and 0.1 million kilowatts (1.8%), respectively, despite the increase in total electricity consumers rose by 60 consumers (0.2%).

Meanwhile, the service sector improved somewhat in the month. Total container registrations rose by 154 containers over the month, driven by higher private and business containers. This coincided with the monthly increase in import payments. A report by the Ministry of Trade and

Economic Development (MTED) showed 49 new businesses were registered during the month, where over half of them are in the service industry. Vehicle registrations increased in May by 4 vehicles (1.5%) and annually by 248 vehicles (8.3%). This indicates a more active trading sector. International arrival passengers increased over the month by 220 passengers (814.8%) due to a repatriation flight from New Zealand, whilst travel receipts declined by \$0.5 million (26.0%). Annually, international arrival passengers and travel receipts both declined by 87,979 passengers (97.5%) and \$96.0 million (81.9%) respectively.

### Job advertisements increased

The Reserve Bank's survey showed a rise in the job vacancies advertised in May by 15 vacancies. The majority of these job vacancies were for public administration. Annually, advertised job vacancies fell by 227 vacancies (51.8%).

### Annual headline inflation continues to rise in May

Table 1: Inflation Rates

Prices	Monthly		Annual	
	May-21	Apr-21	May-21	May-20
Headline Inflation (%)	-0.2	0.3	4.7	0.1
Domestic prices	-1.0	-0.3	1.4	-0.1
Imported prices	0.4	0.8	7.3	0.2

Source: Statistics Department

The monthly inflation for May 2021 declined for the first time since October 2020 by 0.2%. This was driven

Table 2: Average annual prices of selected items

Items (\$ per kg)	Unit	Annual		
		May-21	May-20	Change
<b>Domestic</b>				
Octopus	1kg	\$18.05	\$13.57	\$4.48
Tuna	1kg	\$19.50	\$15.64	\$3.86
Yams - early	1kg	\$7.87	\$4.21	\$3.66
Cockles (to'o)	1kg	\$6.26	\$5.08	\$1.18
<b>Imported</b>				
Pall Mall	1 box	\$23.00	\$19.43	\$3.57
Turkey tails	1 kg	\$11.66	\$8.91	\$2.75
Apples	1 kg	\$6.54	\$5.37	\$1.17

Source: Statistics Department

largely by lower prices for local items, mainly food. However, imported prices slightly picked up due to the rise in fuel prices, clothing & footwear and food items.

Headline inflation continued to rise in year-ended terms, nearing the 5.0% reference rate at 4.7%. This attributes to the significant rise in imported prices, specifically for fuel prices, food items and tobacco. The recovery in the global oil market, coupled with additional costs and delays in shipments due to COVID-19 quarantine requirements, may contribute to higher import prices. Meanwhile, local prices also rose, attributed to higher prices for tobacco and food items. Inflation is projected to continue rising in the near future above the NRBT's reference rate of 5%, driven by rising fuel prices and local food items. Nevertheless, inflation is expected to moderate and fall back below the reference range by the last quarter of 2021.



### Major trading currencies weakened against TOP

Table 3: Effective Exchange Rates

	Monthly			Annual	
	May-21	Apr-21	%	May-20	% Growth
Nominal Effective Exchange Rate Index	88.3	87.2	1.2	94.8	-6.9
Real Effective Exchange Rate Index	105.5	104.5	0.9	110.3	-4.4

Source: National Reserve Bank of Tonga

The Nominal Effective Exchange Rate (NEER) increased in May 2021. Most of Tonga's major trading currencies depreciated against the Tongan Pa'anga (TOP) over the month. Similarly, the Real Effective Exchange Rate (REER) index also increased over the month.

Both the NEER and REER continued to decline in year-end terms, indicating an improvement in Tonga's trade competitiveness with trading partners, further supporting foreign currency receipts.

### Foreign reserves rebounded in May

Table 4: Foreign Reserves

	Monthly			Annual	
	May-21	Apr-21	Growth	May-20	% Growth
Foreign Reserves (\$ in million)	689.5	679.7	1.5	489.6	38.8
Import Coverage (months)	12	11.9	0.8	8.2	46.3

Source: National Reserve Bank Tonga

Official foreign reserves rose over the month of May 2021 by \$9.9 million to \$689.5 million, equivalent to 12.0 months of imports. This was attributed mostly to receipts of donor funds to support Tonga's recovery from COVID-19. In year ended terms, foreign reserves still increased significantly by \$199.9 million from receipts of budget support, official grants, external debt and remittances. Foreign reserves are held mainly in USD, AUD, and NZD.

Table 5: Remittance Receipts

	Monthly			Annual		%
	May-21	Apr-21	% Growth	May-21	May-20	
Remittance (\$ in million)	42.8	42.5	0.8	455.4	345.8	31.7

Source: National Reserve Bank Tonga

Remittances remained at very high levels, increasing slightly by \$0.3 million in May 2021. This stemmed from higher private transfer receipts (particularly NZD), and private capital receipts. These private transfer receipts are mostly family support, gifts, and contributions for annual church conferences. Domestic activities such as the family month and High school fundraising activities were the main drivers of the higher remittances. Annually, remittances continued to increase by \$109.6 million over the year. This was mainly underpinned by higher private transfers and the compensation of employees.

Overseas Exchange Transactions (OET) recorded an overall surplus of \$9.9 million in May 2021 compared to the \$6.0 million deficit in April 2021. This resulted from increases in all of the accounts, particularly the higher transfer receipts from official grants.

Table 6: Overseas Exchange Transactions

	Monthly			Annual		
	May-21	Apr-21	% Growth	May-21	May-20	% Growth
Overall Balance	9.9	-6.0	264.8	199.9	21.3	838.1
Current Account	15.9	7.1	124.4	154.9	32.2	381.4
Merchandise Trade	-40.9	-35.6	-14.9	-449.4	-398.5	-12.8
Services	-2.7	-1.3	-101.4	-25.9	26.5	-197.7
Income	3.5	4.4	-19.7	34.4	-1.6	2246.6
Transfers	56.0	39.6	41.2	595.8	405.7	46.9
Capital Account	1.9	0.5	286.0	42.5	27.0	57.5
Financial Account	-8.0	-13.6	41.4	2.5	-37.8	106.7

Source: Banking Systems

In the year to May 2021, the receipts of official grants, budget support, external debt, and higher remittance receipts drove the significant increase in the OET balance surplus by \$178.6 million.

### Higher net foreign assets and net domestic assets

Table 7: Broad Money

	Monthly			Annual	
	May-21	Apr-21	% Growth	May-20	% Growth
Broad money (\$ in million)	724.7	712.3	1.7	592.2	22.4
Net Foreign Asset	724.4	715.5	1.3	517.2	40.1
Net Domestic Asset	1.2	-2.3	-153.8	75.6	-98.4

Source: Banking System, National Reserve Bank of Tonga

Over the month and year to May 2021, broad money rose further to a new high level of \$724.7 million, by \$12.4 million (1.7%) and \$132.5 million (22.4%), respectively. The net foreign assets increased over the month and year, underpinned by higher foreign reserves from the receipts of official funds such as external loans, budget support, project development funds, and financial assistance for COVID-19. The higher net domestic assets also supported the monthly rise due to an increase in other liabilities. However, net domestic assets declined annually due to higher government deposits from budget support and donor funds.

### Liquidity in the financial system grows

Table 8: Reserve money

	Monthly			Annual	
	May-21	Apr-21	% Growth	May-20	% Growth
Reserve money (\$ in million)	457.3	447.0	2.3	286.7	59.5

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the financial system increased again over the month and year to May 2021, by \$10.3 million (2.3%) and \$170.6 million (59.5%), respectively, to a new high level of \$457.3 million. All the three categories of liquidity continued rising over the month and annually. The bank's ESA rose the most, coinciding with net sales of foreign currencies to the Reserve Bank, mostly receipts of remittances. Currency in circulation followed, in line with the festivities during the month and year, such as the churches annual donations, Easter and family Sundays', Christmas and New Year festivities, Kava Idol, and the Tonga High School Ex-Students' Fundraising. Required reserves also increased, corresponding to the rise in total deposits.



### Credit growth narrowed due to lower business lending

Table 9: Total Lending

Lending	Monthly			Annual	
	May-21	Apr-21	% Growth	May-20	% Growth
Total Lending (\$ in million)	486.6	488.1	-0.3	495.4	-1.8
Business lending	227.7	229.4	-0.8	236.4	-3.7
Household lending	258.5	258.2	0.1	259.0	-0.2
Other lending	0.4	0.4	-0.5	0.0	0.0

Source: Banking System, National Reserve Bank of Tonga

The banks' total lending declined again in May 2021, by \$1.5 million (0.3%) over the month and \$8.8 million (1.8%) annually. The decline is due to ongoing loan run-offs and repayments by public enterprises offset new loans to other private businesses. Lower lending to businesses in the manufacturing, wholesale & retail, and transport sectors contributed to the monthly fall. In contrast, decreasing loans offered to manufacturing, transport and agricultural sectors drove the annual decline. Household loans, however, increased over the month for all categories but declined over the year, mainly for other personal loans.

In May 2021, the banks' total deposits rose by \$9.5 million (1.3%) to \$730.9 million. Saving and time deposits increased over the month and offset the decline in demand deposits. The increase in total deposits and the reduction in total lending resulted in a lower loan to deposit ratio of 64.9% in May 2021, a fall from 66.0% last month and still below the 80% minimum.

### Weighted average interest rate spread slightly narrowed

Table 10: Weighted Average Interest Rates

Interest Rates	Monthly			Annual	
	May-21	Apr-21	Growth	May-20	Growth
Weighted Average Banks Deposit Rate (%)	1.997	1.978	1.8	2.121	-12.5
Weighted Average Banks Lending Rate (%)	7.728	7.711	1.70	7.814	-8.5
Weighted Average Interest Rate Spread (%)	5.732	5.733	-0.1	5.693	3.9

Source: Banking System, National Reserve Bank of Tonga

The weighted average interest rate spread marginally narrowed in May 2021 by 0.02 basis points due to the increase in weighted average deposit rates outweighing the rise in weighted average lending rates. Both the demand and savings deposits increased over the month and offset the declined time deposit rates. The higher lending rates over the month attributed to increased loan rates offered to businesses in the construction, agriculture, and fisheries sectors and households' other personal loan rates.

However, annually, the weighted average interest rates widened by 3.9 basis points to 5.7%. This time, the weighted average deposit rates declined more than the fall in weighted average lending rates. The lower weighted average deposit rates resulted from the fall in time and saving deposit rates offsetting the increased demand deposit rates. Similarly, lower lending rates on household other personal loans and loans to the construction, utilities, and agricultural sectors drove the decline in lending rates.

### Outlook

Domestic economic growth is anticipated to remain subdued. However, the Reserve Bank's monetary policy stance remains accommodative. The Reserve Bank will continue to monitor emerging risks prompted by uncertainties surrounding the COVID-19 pandemic, impacting economic growth and potentially impairing financial stability. The Reserve Bank remains vigilant in its regulatory and supervisory roles to ensure that financial stability is maintained while mitigating the economic downturn and support recovery.