



### IMF projects steeper slowdown for global economy

Global economic growth has been downgraded to 3.2% in 2022, and 2.7% in 2023, according to the International Monetary Fund (IMF) World Economic Outlook (WEO) update in October 2022. Similarly, the Asia Pacific Region's growth is also projected to decelerate to 4.0% and 4.3% in 2022 and 2023, respectively, following a strong rebound of 6.5% in 2021. The main factors shaping the outlook are the tightening of financial conditions, the War in Ukraine, and stalling growth in major advanced economies. The United States recorded annual growth of 2.6% in GDP in the third quarter of 2022, primarily reflecting increases in export and business investment. Australia's annual inflation rate reached 7.3% in the third quarter of 2022, the highest since 1990 in accordance to the Australia Bureau of Statistics. New Zealand's annual inflation rate also increased to 7.2% reported by the New Zealand Statistics. Inflation in both countries were mainly driven by new dwelling construction, automotive fuel and food prices. However, Australia and New Zealand's unemployment rate remained low at 3.5% and 3.3%, respectively in September 2022.

### Tonga upgrade to Green Alert level

Primary sector performance remains weak in September 2022. Total agricultural exports decreased over the month by 64.9 tonnes (11.0%), although proceeds rose by \$0.6 million (158.5%). This owes to lower export volumes of cassava and yams. However, squash and watermelon seasons are starting and are expected to support exports over the coming months. The annual agricultural export volumes also declined by 999.5 tonnes (10.3%), mainly driven by lower exports of root crops reflecting the lockdowns in the first half of the year and unfavourable weather conditions. On the other hand, agricultural export proceeds increased by \$1.0 million (14.4%) over the year. Marine exports also decreased substantially over the month by 77.4 metric tonnes (86.9%), as fewer shipping vessels are operating. Aquarium exports also declined by 39.6% (5,695 pieces) over the month. Annually, both marine and aquarium exports declined by 53.0% (781.0 metric tonnes) and 23.6% (34,757 pieces) respectively.

More construction projects being rolled out continue to support the industry sector. These include 286 new house constructions underway for the Hunga Tonga Hunga Ha'apai (HTHH) displaced households, and the NZ\$5.2 million Pacific Leadership Centre. Lending to the construction sector and housing loans grew by 10.4% and 0.2%, respectively in September reflecting increasing investments in this sector with positive spillovers to manufacturing and quarrying. Electricity consumption will also increase in line with the pick-up in economic activities. Labour rates for construction work and imports of construction materials are increasing, coinciding with the higher demand.

Stronger performances in the tertiary sector was underpinned by the ceasing of the State of Emergency, and

the full re-opening of the borders during the month. Tonga's upgrade to green alert level has boosted consumer and investor confidence supporting the economy's recovery. Total passenger arrivals increased significantly by 1,018 passengers (30.3%), while travel receipts increased by \$2.5 million (53.3%) due to increasing number of international flights arriving. Wholesale and retail import payment rose over the month by \$3.5 million (12.4%) indicating active domestic trade and consumption.

### Strong labor demand continued

The Reserve Bank's job survey showed an increase of 46.7% (35 vacancies) in the number of job vacancies advertised during the month. Annually, the number of job vacancies advertised rose substantially by 375.5% (416 vacancies). More labour demand were from the transport, utility, accommodation and food services, and trade industries. This aligns with the gradual recovery within respective industry as the lockdown restrictions fade away. Additionally, more labour demand for seasonal workers are coming in.

### Domestic inflation accelerated in September

Inflation rose by 0.3% over the month mainly fuelled by increasing domestic prices, while the imported prices

Table 1: Inflation Rates

Prices	Monthly		Annual	
	Sep-22	Aug-22	Sep-22	Sep-21
Headline inflation (%)	0.3	0.9	14.0	6.5
Domestic prices	2.3	2.2	16.7	5.3
Imported prices	-1.3	-0.2	11.9	7.5
Core Inflation - ex. energy and imported food (%)	2.4	2.1	12.7	2.3

Source: Tonga Statistics Department

recorded its second consecutive monthly decline in September 2022. Local food items, transport services, takeaway food, and doctor visit fees were the drivers of domestic prices over the month. Meanwhile, the lower global oil prices coupled with the Government subsidy on fuel, reduced pressure on imported inflation.

Annually, headline inflation reached a new high of 14.0% in September 2022, as imported inflation remains persistent while domestic inflation is becoming more pronounced. Domestic prices contributed 7.3% to the headline, mostly stemming from local food items, electricity, local transport services, takeaway food, labor cost, and doctor visit fees. At the same time, imported prices contributed 6.7% to the headline, largely due to increase in prices of fuels, imported food items, construction materials, and goods for personal care.

Core inflation (ex. energy and imported food) also rose by 12.7% in the year to September 2022, owing to the rising prices of local food and the broadening price pressures.



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### Effective exchange rates appreciated

Table 2: Effective Exchange Rates

	Monthly			Annual	
	Sep-22	Aug-22	% Growth	Sep-21	% Growth
Nominal Effective Exchange Rate Index	96.5	94.8	1.9	89.8	7.5
Real Effective Exchange Rate Index	123.6	121.0	2.2	107.0	15.6

Source: National Reserve Bank of Tonga

The Nominal Effective Exchange Rate (NEER) and the Real Effective Exchange Rate (REER) rose over the month and year to September 2022. The increasing NEER was due to a general weakening of the major trading currencies against the TOP, except for the USD and EUR. The rising REER is indicative of Tonga's higher inflation rates relative to its major trading partners. This suggests a loss in Tonga's trade competitiveness.

### Foreign reserves increased in August

Table 3: Foreign Reserves

	Monthly			Annual	
	Sep-22	Aug-22	%Growth	Sep-21	% Growth
Foreign Reserves (\$ in million)	895.3	871.0	2.8	757.0	18.3
Import Coverage (months)	14.3	14.1	1.8	12.4	15.7

Source: National Reserve Bank Tonga

Foreign reserves increased by \$24.2 million in September, equivalent to 14.3 months of imports. This stemmed mostly from receipts of budget support and project funds from development partners. This was partially offset by outflows for imports and debt repayments. In year ended terms, foreign reserves still increased markedly by \$138.2 million attributed to higher receipts of budget support, official grants, capital inflows, and remittances. The majority of the official foreign reserves are held in USD, NZD, and AUD.

Table 4: Remittance Receipts

	Monthly			Annual		
	Sep-22	Aug-22	% Growth	Sep-22	Sep-21	% Growth
Remittance (\$ in million)	43.6	47.6	-8.3	476.6	480.3	-0.8

Source: National Reserve Bank Tonga

Total remittance receipts declined over the month and year by \$3.9 million (8.3%) and \$3.6 million (0.8%) respectively. This was mainly underpinned by lower private transfers. The resumption of international travels diverts part of the remittance inflows to travel receipts

### Broad money slightly decreased

Table 5: Broad Money

	Monthly			Annual	
	Sep-22	Aug-22	%	Sep-21	%
Broad money (\$ in million)	843.4	843.5	-0.01	783.8	7.6
Net Foreign Asset	875.0	846.8	3.3	745.7	17.3
Net Domestic Asset	-31.2	-3.1	-915.3	39.0	-180.0

Source: Banking System, National Reserve Bank of Tonga

Broad money slightly fell by 0.01% (\$0.1 million) in September 2022. However, it still rose over the year by

7.6% (\$59.6 million) in line with the increasing net foreign asset. Net domestic asset however, declined as government deposits increased from budget support and donor funds.

### Lower liquidity in the financial system

Table 6: Reserve money

	Monthly			Annual	
	Sep-22	Aug-22	%	Sep-21	%
Reserve money (\$ in million)	611.6	615.0	-0.6	530.2	15.4

Source: Banking System, National Reserve Bank of Tonga

Liquidity in the financial system decreased further in September 2022, by 0.6.% (\$3.4 million) as both currency in circulation and Statutory Reserve Deposits (SRD) fell and outweighed the increase in the Exchange Settlement Account (ESA). On the other hand, liquidity still expanded over the year resulting in excess liquidity remaining in the banking system.

### Credit growth slowly recovers

Table 7: Total Lending

Lending	Monthly			Annual	
	Sep-22	Aug-22	Growth	Sep-21	Growth
Total Lending (\$ in million)	482.3	479.5	0.6	476.2	1.3
Business lending	225.9	224.6	0.6	218.8	3.3
Household lending	254.0	252.5	0.6	257.1	-1.2
Other lending	2.4	2.5	-1.9	0.3	688.3

Source: Banking System, National Reserve Bank of Tonga

The banks' total lending (with GDL) grew over the month and year to September 2022, by 0.6% (\$2.8 million) and 1.3% (\$6.1 million) respectively. The monthly rise was driven by higher household loans for housing and other personal loans. Business lending also rose for construction, retail distribution, and professional and other business services.

During the year, business loans rose supporting the positive annual growth, whilst household loans declined. This is indicative of the economic recovery from HTHH and Covid-19.

The loans-to-deposit ratio rose from 54.7% last month to 55.1%, attributing to the decline in deposits, coupled with the higher lending.

### Weighted average interest rate spread widened again

Table 8: Weighted Average Interest Rates

Interest Rates	Monthly			Annual	
	Sep-22	Aug-22	(bps)	Sep-21	(bps)
Weighted Average Banks Deposit Rate (%)	1.656	1.641	1.5	1.839	-18.4
Weighted Average Banks Lending Rate (%)	7.878	7.765	11.4	7.807	7.2
Weighted Average Interest Rate Spread (%)	6.223	6.124	3.0	5.967	25.5

Source: Banking System, National Reserve Bank of Tonga

Over the month and year to September 2022, the weighted average interest rate spread widened to 6.22%. The weighted average lending rates rose at a faster pace than the rise in the weighted average deposit rates during the month. This was largely driven by the movements in the



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volume of loans and deposits, while minimal changes were seen in the nominal interest rates on deposits and loans.

Annually, the weighted average deposit rates declined, corresponding to the higher deposit volumes. Meanwhile, the weighted average lending interest rates increased stemming from higher lending rates offered to the constructions, utility, and fisheries sectors.

### Outlook

A moderate recovery of 3.4% is projected for the Tongan economy in FY2022/23 supported by the reconstruction

from the HTHH disaster, and the resumption of international travels. Inflation is expected to soon peak and then to slowly ease in 2023. Import outflows are anticipated to increase in line with the economic recovery, while remittance receipts and official transfers slow down to pre-pandemic growth rates. This will be absorbed by the strong level of foreign reserves. Credit growth is estimated to be stronger in the near term, however non-performing loans may also increase due to the withdrawal of loan moratoriums. Nevertheless, the excess liquidity in the banks are well capitalised to absorb any further shocks.