

**OFFICIAL PRESS RELEASE****6 October 2020****Monetary Policy Decision**

The National Reserve Bank of Tonga's Board of Directors at its board meeting on the 30th of September 2020, approved to maintain its current monetary policy measures outlined below. This is to encourage utilization of the excess liquidity in the banking system, through further lending to growth sectors and to support the economy from the impacts of COVID-19.

- a. Maintain the monetary policy rate at 0% (zero interest rate policy).
- b. Maintain the minimum loans/deposit ratio of 80%.
- c. Maintain the Statutory Reserve Deposit ratio at 10%.
- d. Maintain the inflation reference rate at 5%.
- e. Monitor the commercial banks' liquidity and adjust the SRD ratio if needed.
- f. Monitoring the commercial banks' capital reserves and adjust further when required.
- g. Ease the exchange control requirements when required.
- h. Continue to issue Government Bonds.
- i. Maintain clear channels of effective communications with the financial institutions for adequate preparedness.
- j. Continue to be transparent and raise awareness of its monetary policy decisions through press releases to the public.
- k. Closely monitor the impacts of the pandemic in the financial system for early detection of any signs of vulnerability.
- l. Continue to ensure both commercial banks and non-bank financial institutions adheres to all Government declarations regarding COVID-19 in the workplace while delivering essential financial services to the public.

The Governor of the Reserve Bank, Sione Ngongo Kioa, reported that domestic activities for July 2020 was generally slow without the normal annual festivities. Cancellation of the Heilala Week Festival and the Royal Agricultural Show contributes to dampening aggregate demand. For the primary sector, total volume of agricultural exports decreased during the month, although still higher than July of the previous year. Households show resilience and consistent preparation in anticipation of a shortage in food supply particularly imported products by engaging more in backyard farming and home gardening. Reconstruction and rehabilitation projects from recent cyclones supported the industry sector with the completion of various projects such building schools, private households, and office premises. The first repatriation flight provided some activity for accommodation providers that were used as a quarantine facility, however it is still not sufficient to counteract the standstill in tourism. Container and vehicle registrations have picked up during the month indicating some positive trading activities, however these levels are still relatively lower compared to the previous year.

Inflation rose in July 2020 with a monthly movement of 0.5% driven solely by higher imported prices whilst domestic prices declined. Annual inflation for July 2020, however, declined by 1.1%, which is slightly higher than the deflation rate of 1.4% last month but lower than deflation rate of 0.5% in July 2019. Import prices fell due to lower global oil and food prices. Meanwhile, domestic prices declined due to lower prices for electricity and Kava Tonga.

In July 2020, the official foreign reserves rose to a new record high of \$555.9 million, noting an increase of \$12.1 million in the month, and an increase of \$63.0 million in the year. This owes to inflow of remittances and project grants from development partners. Tonga's remittance picked up strongly in July 2020 defying expectations of a decline from the impact of COVID-19. Majority of the remittance receipts are family support and monetary gifts, which will assist in cushioning some of the fallouts in domestic activities.

The total banking system still maintains its soundness supported by strong capital and adequate profits. The banks' total loans to deposit ratio declined to 76.8% from 77.9% last month as loans declined while deposits rose. The shrinking of this ratio continues despite excess liquidity existing in the system and a rise in money supply. Meanwhile, lending remains subdued as demand is considerably lower. The weighted average interest rate spread declined both over the month and year to July 2020 by 0.1 and 43.3 basis points respectively to 5.674%. This stems from declines in both lending and deposit rates.

Given the above developments, the Reserve Bank continues to review its GDP forecasts and projects a moderate downturn in future economic growth. Foreign reserves is still expected to be well above the 3 months minimum threshold of import cover, while inflation is also expected to remain below the 5% reference rate. The banking system is still sound supported by high liquidity. Meanwhile, the Reserve Bank continues to be vigilant in closely monitoring its economic and financial

indicators and stands ready to adjust its monetary policy settings if needed to maintain internal and external stability and support macroeconomic growth.

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