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**Reserve Bank's February 2024 Monetary Policy Keeps Watchful Eye
on Domestic Inflationary Pressures**

The National Reserve Bank of Tonga (NRBT) has released its Monetary Policy Statement (MPS) for February 2024 following its approval by the Board of Directors.

Despite fluctuations exceeding the 5% reference rate in January 2024, headline inflation has eased to 3.6% in February 2024. Governor Moeaki stated that “while recent improvements are noted, NRBT remains vigilant regarding domestic inflation risks. Economic growth forecasts for FY 2024 have been revised downward, although foreign reserves remain at comfortable levels. The February 2024 Monetary Policy Statement (MPS) will keep a watchful eye on domestic inflation and its focus will be twofold: firstly, to uphold macroeconomic stability by keeping inflation below the 5% reference rate, with closer collaboration with the government on targeted reforms to alleviate Tonga's high cost structure; and secondly, to implement measures ensuring financial stability and fostering access to financing for underserved and climate change-vulnerable sectors.”

The lower inflation in February 2024 was mainly driven by lower energy prices and improved local food prices. Annual average inflation decreased to 6.4% in December 2023 from 10.9% percent in December 2022. Inflation is expected to continue to remain below the reference rate in 2024, but this is highly vulnerable to the volatility in local food prices associated with Tonga's high susceptibility to natural disasters, extreme weather events, labour market mismatches, the current rising energy prices, and other external shocks.

Tonga's economic growth projected for the FY 2024 is 2.2%, a downward revision from the 2.6% forecasted in the August 2023 MPS due to lower than expected production in both the primary and secondary sectors. However, this reflects the need for financial sector support to stimulate private sector growth. This is also compounded by tight labour market stemming from skill mismatches and labour force migration hindering economic activities and contributing to domestic inflationary pressures.

Foreign reserves remains robust exceeding the 7.5 months of import cover standing at \$891.4 million by February 2024, equivalent to 11.4 months of import cover.

The banking system is supportive of economic growth, with annual credit growth of 6.4% in January 2024. However, an increase in non-performing loans to 12.1% of total loans in December 2023 from 6.0% 12 months before is monitored closely as part of the economic recovery. Enhanced supervision of banks and non-bank financial institutions on-going to moderate financial stability risks. Overall, the banking system remains sound with adequate capital and ample liquidity to absorb any shock to the system. The NRBT will continue to closely monitor both global and domestic economic developments and align its monetary policy as needed.

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