



ANNUAL REPORT

2022 - 2023

NATIONAL RESERVE BANK OF TONGA

Honourable Tiofilusi Tiueti
Ministry of Finance
St. George Building
Nuku'alofa

Subj. **Annual Report for the Year Ended 30 June 2023**

It is with privilege and responsibility that I submit to you the Annual Report of the National Reserve Bank of Tonga for the year 2023, in accordance with Section 54(1)(b) of the National Reserve Bank of Tonga (NRBT) Act.

The Annual Report covers NRBT operations for the year ended 30 June 2023 including the balance sheet, income statement, and the statement of cash flows from the Audited 2023 Annual Financial Statement. Following the double disasters in 2022 of the COVID-19 and HTHH volcano eruption, the Bank confronted the challenges where it has the capacity to return business to normal as a testament to the dedication and hard work of all the staff and the Board of Directors who remain steadfast in upholding our responsibilities and contributing to the economic prosperity and well-being of our people.

Thank you for your support and guidance as we work together to achieve our shared vision for the financial well-being of all the people of Tonga here and abroad.

Sincerely,

A handwritten signature in black ink, consisting of a series of fluid, overlapping loops and a trailing line that ends in a small dot.

Tatafu Moeaki
Governor
August 2023.

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1. FUNCTIONS & OBJECTIVES

The National Reserve Bank of Tonga (Amendment) Act, 2014, Section 4 sets out the principal objectives of the Bank. It states:

Objectives of the Bank

- (1) *The principal objectives of the Bank shall be to maintain internal and external monetary stability.*
- (2) *Without prejudice to its principal objective, the Bank shall -*
 - (a) *promote financial stability; and*
 - (b) *promote a sound and efficient financial system*
- (3) *Subject to subsections (1) and (2), the Bank shall conduct its activities in a manner that supports macroeconomic stability and economic growth.*

Maintaining internal monetary stability is pursued by the Reserve Bank through promoting low and stable inflation over the medium term. The Reserve Bank's reference inflation rate is to be maintained below 5%.

Maintenance of external monetary stability is pursued through maintaining an adequate amount of foreign currencies (foreign reserves) to meet the country's foreign currency demands to pay for imports and other obligations. As such, the Reserve Bank's monetary policies aim to ensure that Tonga always has foreign reserve holdings of at least three to four months of import cover.

The National Reserve Bank Act, Section 4A also sets out the Reserve Bank's functions:

"The principal functions of the Bank shall be, to:

- (a) *issue currency;*
- (b) *formulate and implement monetary policy;*
- (c) *prescribe the regime for the determination of the external value of the Tongan currency in consultation with the Minister;*
- (d) *determine the foreign exchange rate and implement foreign exchange policy;*

- (e) *determine and implement financial stability policy, and oversee the maintenance of the stability of the financial system as a whole;*
- (f) *regulate as required the supply, availability and international exchange of money;*
- (g) *exclusively hold and manage the external reserves of the Kingdom;*
- (h) *provide advisory services to the Minister on banking and monetary matters;*
- (i) *be the principal banker, fiscal agent and depository of the Government;*
- (j) *undertake banking business, in Tonga or elsewhere, subject to the provisions of this Act;*
- (k) *regulate and supervise financial institutions, including non-bank financial institutions;*
- (l) *oversee and promote the efficient, sound and safe functioning of the payment system;*
- (m) *collect and produce statistics;*
- (n) *cooperate with and participate in international councils and organisations, including public international financial institutions, and cooperate with domestic and foreign public entities, concerning matters related to its objectives and functions;*
- (o) *regulate and supervise capital markets in Tonga; and*
- (p) *to manage and promote financial inclusion initiatives and related activities; and*
- (q) *carry out any other function or any ancillary activities incidental to the exercise of its functions under this Act or any other Act.*

Details on how the Reserve Bank applied its functions to meet its objectives are outlined in this report and other publications.

2. FOREWORD



The Reserve Bank's unwavering commitment to prudent monetary policies is proudly reflected on financial year 2023¹ as a year of resounding success in maintaining price and financial stability. Our financial performance in 2023 reveals commendable growth in various aspects, underscored by increasing our investable assets, increasing longer term maturity and changing composition of currency proved effective during the year. Our daily management of the exchange rate was assessed appropriate by the IMF as the independent international agency.

Our approach was underpinned by the development of a renewed 5-year strategy to start from the second half of 2023 and reviewing the principal Act to improve prudent economic management, and promote transparent communication and collaborative partnerships. Consequently, the Reserve Bank can chart stronger financial opportunities and a course of prosperity that benefits every individual and upholds the honour of Tonga's economic legacy. We maintained a steadfast commitment to open communication and transparency through dialogue with the four (4) banks and the Association of Banks in Tonga (ABT), a roundtable with the two retirement funds, seventeen foreign exchange dealers, money lenders, and other financial institutions. We collected and analysed data, and published updates on economic indicators, policy decisions, and future projections to assist predictability and enable the public, businesses the Government and stakeholders to make informed choices. This, in turn, promoted stability in financial markets and nurtured an atmosphere of trust in the financial sector.

The financial performance recording \$20.4 million net profit in 2023 reveals commendable growth in various aspects of NRBT underscored by prudent financial management and effective policies.

Our ability to navigate through economic challenges and capitalize on opportunities reflects the strengthened leadership of the Reserve Bank with stronger business acumens.

We partnered closely with the Ministry of Finance and Government bodies, financial institutions, Pacific central banks and Governors, International Monetary Fund (IMF), Alliance for Financial Inclusion (AFI) and international organizations to ensure a unified response to economic challenges. By coordinating efforts and sharing insights, we enhanced the effectiveness of our policies and achieved results that exceeded expectations.

The Reserve Bank's achievements translated into tangible improvements in the lives of every Tongan

citizen here and abroad who remit money from time to time to their relatives. Families enjoyed shielded purchasing power from reduced inflation, entrepreneurs found a conducive environment for business expansion with annual credit growth of over 8% driven by businesses.

With an eye towards the future, we commit to ensuring financial stability remains resolute, and that our successes in 2023 continue to resonate in the next year and onwards for the betterment of the Kingdom and its people.

A stylized black ink signature of Tatafu Moeaki.

(Tatafu Moeaki)
Governor

¹ From 1st July 2022 to 30th June 2023

3. BOARD OF DIRECTORS



Leadership

The Board is composed of Directors tasked with critical decision-making roles for the Reserve Bank. It includes Lord Sevele as the Chairman, four (4) other non-executive Directors, the Secretary for Finance, and the Governor. During the year, the Board saw changes in its composition. Two directors, including the former Governor, resigned, and Director Chapman and Director Fusimalohi were welcomed as new directors. Additionally, the new Governor assumed office for a five-year term.

Overall, the Board played a multifaceted role in FY 2023 promoting financial stability, price stability, shaping Tonga's economic landscape, and contributing to the well-being of the Kingdom's citizens. The Directors bear responsibility for the Reserve Bank's accountabilities, monetary policies, currencies supply, stability of the financial system, investment of the foreign reserves, and ensuring our pegged exchange rate stays relevant for macroeconomic stability, noting the value of the Tongan pa'anga as measured by the nominal effective exchange rate (NEER) strengthened over the year. This encompasses continuous assessment of the Reserve Bank's performance in fulfilling its functions and resource

utilisation. The Board guides the Governor to ensure not only the Reserve Bank's efficient and effective management but also its compliance with the NRBT Act and related statutes.

Tonga's economy has successfully rebounded in FY 2022-23 after consecutive contractions in the last two years. The Reserve Bank estimates growth at 2.4% for FY 2022-23 and forecasts the economy will further grow by 2.6% in FY 2023-24. Recovery from the double shock in 2022 is ongoing but several supply side constraints remain which are hampering a faster recovery, while also adding to the inflationary pressure. As custodians of the nation's financial well-being, the Reserve Bank's strategic measures led by an untiring Board of Directors have yielded a harmonious balance between economic growth and the challenges of containing the persistent core inflation in order to foster an environment of prosperity for all Tongans.

Headline inflation has eased from its peak of 14% in September 2022 to 7.4% in June 2023 and down to 4.8% in July 2023 in line with our forecast to be below the 5% reference rate for the first time since May 2021. Although imported inflation has eased to 3.0% in June 2023,

domestic inflation has surprised on the upside and has remained relatively high at 8.8%. By exercising keen judgment and foresight, we ensured that the Tongan economy remained robust and resilient, where we have the capacity shielding our population from the fluctuations that can sometimes disrupt their daily lives.

The economic rebound and maintenance of price stability while the foreign assets of the Reserve Bank trended higher, indicates the effective management of foreign reserves, increased economic stability and prudent monetary policies led by the Board. The Reserve Bank has also implemented 8 of the 10 recommendations from the IMF 2021 Safeguards Assessment, enhancing its independent oversight and governance of its responsibilities.

As part of rebuilding transparency and accountability, the Board Audit Committee was re-established during the year. As mandated, the Board shall convene a minimum of 10 meetings annually. However, throughout the year, the Board and the Board Audit Committee held a total of 33 and 18 meetings respectively, contributing to the scaled up strategic guidance, policy formulation, and financial and operational monitoring of the Reserve Bank.

Significant accomplishments transpired during the year, including the endorsement of the Domestic Electronic Payment System (DEPS) launched in July 2022, recovery of operations post COVID-19 and HTHH reconstruction, enhanced banking supervision, diligent scrutiny of prudential requirements breaches and more proactive economic management of the monetary aspects of the Tongan economy. The Directors also processed the final designs the new Bank Note series

which include new polymer notes endorsed by the Government and approved by the Privy Council to issue in 2024. The Board also authorised special operations to count, reissue, or destroy the 4-year backlog of currency notes to maintain appropriate currency supply and currency integrity.

The Board of Directors reviewed and approved the Reserve Bank's financial statements every month. Pursuant to its function under section 54(4) of the NRBT Act, the Statement of Assets and Liabilities is submitted to the Minister of Finance and the Prime Minister's Office, to be published in Government Gazette Notice. In FY 2023, the foreign currency assets reached a substantial value of \$940.9 million, demonstrating a significant increase from the \$878.2 million recorded in FY 2022. This growth is evidence of the Reserve Bank's effective management of the foreign reserves and prudent monetary policies as the economy continues to recover. The substantial increase in net profit available for distribution from \$0.5 million in 2022 to \$20.4 million in 2023 signifies a remarkable financial performance.

Lastly, the Directors played a pivotal role in shaping the Reserve Bank's future endeavors. This includes the endorsement of the NRBT FY 2024 Annual Budget, organisational changes, as well as a comprehensive review of the Reserve Bank's Strategic Plan. In the pipeline, efforts are underway to complete the review of the NRBT Act as well as enhance organisational efficiency, scheduled for the second half of 2023. The Board's collective efforts and informed decision-making continue to steer the Reserve Bank to be more successful in achieving its mission and vision.

Board of Directors

June 2023



LORD SEVELE 'O VAILAHI
Chairman
*Appointed as Director
on 25 February 2022*



MR. RICHARD PREMA
Deputy Chairman
*Appointed as Director
on 2 May 2003*



MRS. SIOSI LATU MAFI
Director
*Appointed as Director
on 13 December 2019*



MR. JOHN PAUL CHAPMAN
Director
*Appointed as Director
in September 2022*



MRS. VIKA FUSIMĀLOHI
Director
*Appointed as Director
in September 2022*



MRS. KILISITINA TUAIMEI'API
Director
*Appoint as Director in July 2022
as in her role of Secretary for Finance*

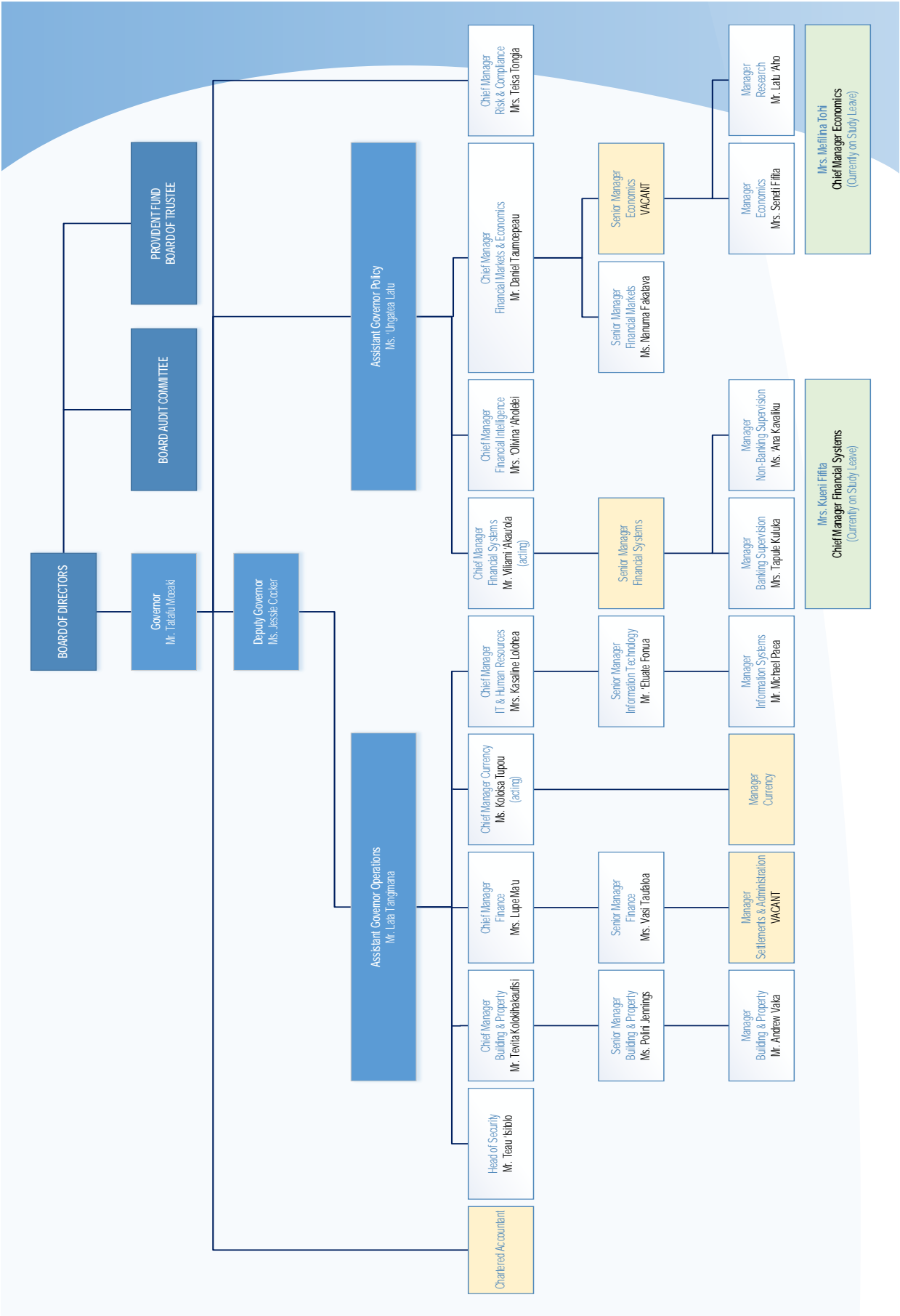


MR. TATAFU MOEAKI
Governor



MS. JESSIE COCKER
Deputy Governor

Figure 1:
Our Organizational Chart
June 2023



Our Executive Management



MR. TATAFU MOEAKI
Governor



MS. JESSIE COCKER
Deputy Governor



MS. 'UNGATEA LĀTŪ
Assistant Governor Policy



MR. LATA TANGIMANA
Assistant Governor Operations

4. HIGHLIGHTS OF THE YEAR

Price Stability:

Inflation dropped from all-time high of 14% (December '22) to **4.8%** in July 2023.



Foreign Reserves:

Foreign Reserves rose to **\$921.4 MILLION** with a 13 months' worth of imports



\$20.4 MILLION

Net Profit for Financial Year 2022/2023

FY 2021/22: \$0.5 MILLION

Financial Stability:

- The **SRD Ratio** was increased from 10% to 15%, setting aside a higher portion of liquid assets in the banks' SRD accounts.
- The **minimum requirements** for the loans to deposit ratio of 70% was revised to a **maximum/ceiling of 80% to 90%**, to be in line with international best practices.

Banknotes and coins:

Finalized 2024 New Series including Polymer Notes
Banknotes and coins in circulation down to **\$118.0 MILLION** in 2022/23



\$14.2 MILLION

Distribution to Government to support overall development

FY 2022: \$0.3 MILLION

Corporate Plan:

Board of Directors approved the FY 2022/23 Corporate Plan with **717** measurable targets.

69%
Corporate Plan
Achievement Rate



1 July 2022

Reserve Bank launched its **Domestic Electronic Payment System**



5. CORPORATE PLAN

The Board of Directors approved the Reserve Bank's Corporate Plan for 2022/23 with 717 measurable targets. The corporate plan was reviewed at the end of May 2023 and it showed that overall the Bank had achieved 69% of the 717 Corporate Plan targets for 2022/2023. Throughout the current year, executive management has been diligently engaged in shaping the path of NRBT for the future as it engaged a process to develop its comprehensive 5-year NRBT Strategy 2023 - 2028 on track for completion second half of 2023. Its operational efforts during the year focused on fulfilling its core mandates;

- a) *Fostering both price and financial stability. This has entailed careful monitoring of inflation, interest rates, and monetary policy, all of which contribute to sustaining an equilibrium that benefits businesses and individuals alike;*
- b) *Maintaining a stable economic environment within the nation in the face of evolving economic conditions and global uncertainties;*
- c) *Issuing and managing Tongan Pa'anga (TOP) exchange rate and the currency in circulation;*
- d) *Managing the country's foreign reserves, which are held to stabilize the exchange rate and ensure that the country can meet its international payment obligations;*
- e) *Overseeing and ensuring the efficiency and security of the payment systems;*
- f) *Collecting and analysing data and issuing economic publications for the public's informed economic decisions, while also facilitating access to financing for vulnerable businesses and households, to promote an inclusive and successful economic recovery and create a conducive atmosphere for sustainable development;*
- g) *Ensuring balanced and holistic financial management of the Reserve Bank's operations;*
- h) *Delivering its role as the Government's Banker; and*
- i) *Fostering International Relations.*

OUR VISION

To be an effective and dynamic central bank in promoting Tonga's economic prosperity.

OUR MISSION

To formulate and implement sound monetary policy that is conducive to economic prosperity; promote stable and efficient financial system, external stability and effective payment systems through professionalism and independence.

OUR VALUES

We will pursue our mission with the following values.

TEAM WORK

Working together for a more effective Bank

INTEGRITY

Being professional and exercising sound judgement

INNOVATION

Continually improving what we do

EXCELLENCE

Producing high-quality work

6. PRICE STABILITY



Monetary Policy Formulation

We conduct monetary policy using monetary instruments to promote price stability through low and stable inflation whilst maintaining sufficient level of foreign reserves. During the year, inflationary outturns were averaging 10.3%, remaining higher than the Reserve Bank's 5% reference rate since May 2021. These were mainly attributed to supply constraints since COVID-19 and the Russia Ukraine war in 2022, which outweighed the growing demand pressures from higher consumer spending funded by the increase in remittances and the Government's expansionary fiscal policy to support economic recovery.

As such, we changed the monetary policy stance in February 2023 to prioritise the fight against inflation to maintain price stability. Concurrently, the Reserve Bank continued to promote easier access to credit for those who are vulnerable and thereby assist with the economic recovery.

Monetary Policy Actions

Price Stability

We seek to manage price stability and adopted the following monetary policy measures:

- *Focus the exchange rate policy on cushioning the erosion of household and business purchasing power by:*
 - *reducing the exchange rate spread offered by authorised agents: USD/TOP from 220 to 170 basis points, AUD/TOP at 300 basis points, and NZD/TOP at 350 basis points;*

- *linking the exchange rate policy to developments in energy prices; and*
- *encouraging competition and level playing field for all authorised foreign exchange dealers on foreign exchange trade and lower costs to be passed on to customers.*
- *Increase the Statutory Reserve Deposit ratio to 15% from 10%.*
- *Offer deposit facilities for the Government and the retirement funds at the NRBT for targeted mopping of excess liquidity.*
- *Conduct effective communication of future course and actions to reduce inflation in the next 6 months.*
- *Maintain the inflation reference rate at 5%.*

Macro-economic Stability

To support the economic recovery and maintain macro-economic stability, the monetary policy stance also complemented the expansionary fiscal policy by:

- *Lifting the syndicate loan restrictions allowing banks and non-banks to share risks.*
- *Continuing to support developing financial instruments to build medium-term growth through targeted credit easing for:*
 - *(i) vulnerable growth sectors identified with disproportionate access to finance: agriculture, tourism, manufacturing, housing construction, education, and*
 - *(ii) Energy efficient and climate resilience financing such as investments in renewable energy. Increased financial instruments to support credit easing in consultation with the Ministry of Finance of the Government of Tonga.*
- *Enhancing collaboration between the Reserve Bank and Government to address high inflation.*

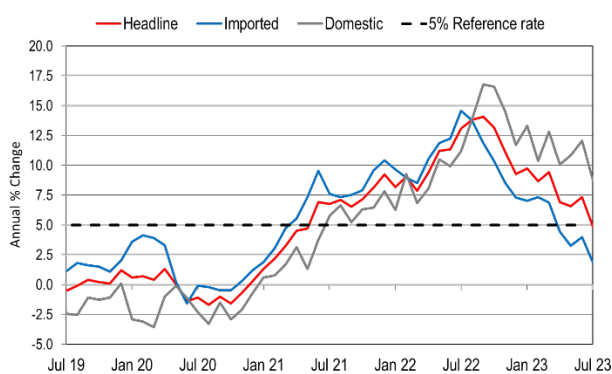
Monetary Policy Outcomes

The Board reviews updates on the implementation of the Monetary Policy Statement from February 2023. This included the effects on key indicators of monetary policy, such as liquidity, inflation, foreign reserves, and interest rates.

Inflation

We implemented financial measures to cool down inflation from its peak of 14% in September 2022. It was 7.4% in June 2023 before easing further to 4.8% in July 2023 in line with our projections. The Reserve Bank stands ready to tighten its monetary policy stance further if the high domestic inflation persists.

FIGURE 3:
INFLATION
Annual



Source: Tonga Statistics Department; National Reserve Bank of Tonga

Foreign Reserves

External stability was maintained during the year through an adequate level of foreign currencies (foreign reserves) exceeding the country's foreign currency demands to pay for imports and other obligations. The Foreign Reserves increased to T\$921.4 million equivalent to 13.0 months of imports, which is well above our required foreign reserve holdings of 3-4 months of import cover, and above the IMF's optimal level of 7.3 months of import cover.

Economic Analysis and Research

We conduct research and analysis of Tonga's macro-economic position and performance, which informs the formulation of monetary policy. This is through collection and analysis of data and information, preparation of forecasts, and production and dissemination of economic publications. Liaisons with international agencies such as the International Monetary Fund, and domestic stakeholders in the private sector and the Association of Banks were also conducted.

We produced 28 financial and economic publications during the year including:

1. *February 2023 Monetary Policy Statement,*
2. *Two (2) Quarterly Bulletins,*
3. *Thirteen (13) Monthly Monetary Policy Data sheets,*
4. *Twelve (12) monthly updates on the performance of the economy and analyses of important indicators of the economy such as the Overseas Exchange Transaction, remittances and inflation.*

The publications are also posted on the Reserve Bank's website for the general public's consumption. Some of the current publications such as the Quarterly Bulletins and monthly reports are being restructured to better suit the stakeholders' needs.

Additionally, the Economics department disseminate data and reports on a regular basis to the Board of Directors of the Reserve Bank, the International Monetary Fund, the Tonga Department of Statistics, the Asian Development Bank, World Bank Group and other others who request from time to time. Much focus was on the persistently high inflation, which peaked in September 2022 at 14% remaining above the NRBT's 5% reference rate, therefore regular analyses and reports on inflation trends and sources were submitted to the Board.

Furthermore, liaison meetings with the general public and private sector were carried out to better inform the analysis of economic data and information. The department also conducts and provides analysis on special research topics as needed and required by its various stakeholders.

In enhancing the quality of reports collected, 4 training of banks and foreign exchange dealers on the OET reporting requirements were undertaken during the year. Administrative penalties for wrong and late reporting was put on hold until August 2022, in light of the impact of COVID-19 and recovery from the natural disasters in early 2022.

Technical assistance and missions received from development partners during the year helped to enhance the department's capacity. The IMF's Forecasting and

Policy Analysis system (FPAS) mission assisted in strengthening the forecasting capability of the department, through enhanced macro-econometric analysis and now casting models for GDP and inflation. The IMF PFTAC also provided training on GDP expenditure measurement and forecasting and macroeconomic program.

Economic Advice to stakeholders

We work to improve evidence-based analysis, liaised, collaborated with, and provided policy advice to various arms of the Government during joint meetings with them such as the Macroeconomic Technical Committee to enhance the coordination of fiscal and monetary policies, the Trade Development Committee to implement Tonga's trade policies, and with the Tourism sector.

Inputs were provided for the Ministry of Finance's budget statement for 2023/24. Dialogue with the Ministry of Finance, Ministry of Revenue & Customs, and the Ministry of Trade and Economic Development helped in identifying sources of inflation and developing relevant measures to support reducing inflation. This included subsidies for electricity prices and exploring ways to further reduce consumption taxes or freight charges.

The Economics Department also produced and conducted presentations to external stakeholders on current economic and financial conditions, the Government and the private sector economic summits amongst others. This includes updates to development partners during the Joint Policy Reform Matrix (JPRM) missions, and other bilateral missions providing budget support to the Government.

7. FINANCIAL STABILITY

We license and supervise both banks and non-bank financial institutions to ensure they are managing risks prudently, and thereby safeguard the stability of the financial system. The Reserve Bank's supervisory function is implemented through offsite collection and analysis of reports and other relevant information, and onsite visits to verify compliance with the prudential requirements.

Prudential Regulation

Ongoing update of the prudential requirements as outlined in the prudential standards issued by the Reserve Bank is critical for aligning with international standards. The Pacific Financial Technical Assistance Centre (PFTAC) continued to assist with reviewing of the current regulatory framework for banks and non-bank financial institutions to ensure ongoing compliance with the Basel framework and best practices. We developed new prudential banking standards for operational risk management and business continuity management, and interest rate risk management. Two new prudential standards were also developed for non-bank credit institutions (microfinance institution, moneylenders, credit unions) on governance and risk management, and other key prudential requirements. The implementation of the new prudential statements will be preceded by an impact study. PFTAC has also provided training on conducting of prudential standards impact study. The draft Prudential Standards will be finalized in the next financial year.

The measures adopted in the February 2023 MPS also supported strengthening of the resilience of the banks. The increase in the SRD ratio from 10% to 15% set aside a higher portion of liquid assets in the banks' SRD accounts. The minimum requirement for the loans to deposit ratio of 70% was revised to a maximum/ceiling of 80% to 90%, to be in line with international best practices. Concurrently, banks' liquidity management became more active following the initiation of mopping of the retirement funds' deposits to the Reserve Bank as well as the increase in the SRD ration took effect. Nonetheless, close monitoring of the impact of the MPS on financial stability remains important.

The restriction on banks' syndicated lending with a non-bank financial institution was lifted to increase banks'

capacity to finance larger-scale projects with risks being shared among syndicate partner financial institutions.

The Reserve Bank engaged with the ADB Pacific Private Sector Development Initiative (PSDI) and the World Bank to review the existing draft Pension Fund Bill and Insurance Bill respectively to address the stakeholders' comments from the 2021 consultations. This work will continue to the 2024 financial year for further consultation and finalization of the respective Bills to be passed by Parliament.

The PSDI has also offered its assistance to conduct a feasibility study on the possibility of establishing a Credit Registry to enhance the credit environment and better monitor the business and household indebtedness in the economy. The mission report is being finalized.

Prudential Supervision

We regulate and supervise the financial system as it continues to recover from the impact of the global pandemic and the 2022 natural disasters and new financing opportunities emerged, therefore the supervisory work continued to focus on ensuring the financial system remained sound.

With elevated vulnerability of risks to financial stability, enhanced supervision of banks continued. Stress testing and analysis of the impact of potential shocks to the financial system was conducted to identify early warning signals that would require supervisory actions.

Bilateral meetings with the banks, as well as with banks' external and internal auditors, and meetings with the Association of Banks in Tonga (ABT), continued during the year to ensure the Reserve Bank is kept abreast of the banks' strategies in light of the market developments, and consult on new policies, while ensuring compliance with prudential requirements.

Targeted onsite examination of banks were conducted as needed to address any concerns arising from offsite supervision that required immediate actions. As part of the PFTAC's regional cybersecurity program to upskill the supervisors in this new area of supervision, an onsite visit to examine cyber risk management in one of the banks was conducted. This is the first cybersecurity-focused onsite examination, and was joined by participants from the central banks of Samoa and Fiji. The scope included

verification of compliance with the Prudential Banking Standard 15 on Cyber Risk.

The supervision of foreign exchange dealers (FEDs) continued to focus on ensuring FEDs' compliance with all legal and regulatory requirements. This is important in supporting FEDs' case against de-risking practices by banks. The result of the 2022 annual compliance checks is being implemented. This includes a notice of revocation of licence issued to two FEDs as a last recourse to enforcing compliance. Training was conducted for the FEDs on the revised Exchange Control Directive and other supervisory issues identified in the reports to the Reserve Bank and outcomes of spot checks.



Figure 4: PETAC Technical Assistance

Cybersecurity experts, as part of the PETAC's regional cybersecurity program, conducting a workshop with the Banks Supervision Department, in preparation for the cybersecurity-focused onsite examination

We also licensed moneylenders during the year. As of the end of June 2023, the Reserve Bank has licensed 87 moneylenders (8 with license Type A, 37 with license Type B, and 42 for License Type C). Training was conducted for moneylenders on the Money Lender Act's requirements and license conditions, including the reporting requirements. The reporting template is being finalized for issue in 2023/24.

The supervision of the sole licensed microfinance institution focused on collection of reports and analysis of the microfinance institution's performance and operations.

Ensuring financial customers' interests continue to be adequately protected was also crucial.

- *The Reserve Bank published the commercial banks' fees & charges and interest rates on its website for the first time in October 2022 to assist financial consumers make informed decisions. This document will be updated at least bi-annually to ensure that the public is able to make well-informed financial decisions based on up-to-date information.*
- *The Financial System department also received and processed one complaint from one of the licensed financial institutions' customers during the year. Three complaints have been resolved, of which one was from FY 2021/22, and one is still being processed. The majority of the complaints were from customers of moneylenders due to overcharging of interest rates.*

In managing the unclaimed monies paid to the Reserve Bank by the commercial banks, unclaimed accounts totaling \$699,632.2 were published to allow customers to place their claims for their funds before they are forfeited to the Government. During the year, an amount of \$276,500.5 was forfeited to the Government's account pursuant to sections 94 (7) & (8) of the Banking Act 2020.

AML/CFT Supervision

On behalf of the Government working side by side with the Office of the Attorney General (AGO), we take on the responsibility for the anti-money laundering/counter-terrorism financing (AML/CFT) supervision of banks and non-bank financial institutions to support the efforts of our internal financial intelligence. Combating money laundering and terrorism financing mitigates risks to the sound management of financial institutions and in turn the stability of the financial system. An AML/CFT onsite examination of one bank was conducted in November 2022. This AML/CFT supervision capacity will continue to be built with the training of staff and refinements to the supervisory framework and regulations.

8. FINANCIAL INTELLIGENCE

Intelligence Analysis and Dissemination

We constantly assess and analyse suspicious transaction reports (STRs) and other financial transaction reports that the Financial Intelligence Department (FID) receives from reporting entities and other agencies in Tonga.

TABLE 1: REPORTS RECEIVED

Types of reports filed	2019/20	2020/21	2021/22	2022/23
Suspicious Transaction Reports (STRs)	39	21	22	23
Currency Transaction Reports (CTRs)	12,944	18,096	10,969	17,790
Border Currency Reports (BCRs)	63	2	2	1
TOTAL	13,046	18,119	10,993	17,814

Source: Financial Intelligence Department, National Reserve Bank of Tonga

TABLE 2: REQUEST FOR INVESTIGATIVE ASSISTANCE

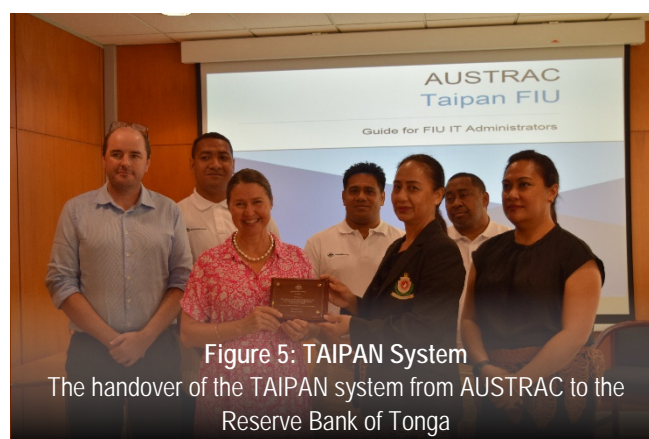
Request Report(s)	2019/20	2020/21	2021/22	2022/23
Number(s) of Request for Investigative Assistance	28	18	19	27

Source: Financial Intelligence Department, National Reserve Bank of Tonga

During the year, we received 17,814 reports consisting of STRs, CTRs, and BCRs.

- 23 STRs were received during the year, of which 2 reports were disseminated to law enforcement agencies (Tonga Police and Ministry of Revenue & Customs) for further investigations.
- The STRs were mostly related to unusual transactions especially with the use of third parties, and large or rapid movement of funds.
- 17,790 CTRs were received during the year, majority of which were funds moving into the financial system for business purposes. These information provide critical information for the analysis of the STRs.

The AUSTRAC successfully installed the Taipan system in September 2022, which helped to strengthen the analysis and information management system of the FID.



We responded to 27 requests for information from law enforcement agencies, such as Tonga Police, the Ministry of Revenue & Customs and the Attorney General's Office, in relation to subjects that are under investigation for possible predicate offences.

Due Diligence

During the year, we conducted background checks on 146 individuals and entities. We also responded to several surveys from the Reserve Bank's correspondent banks, in relation to its AML/CFT policy and procedures.

TABLE 3: REQUESTS FOR BACKGROUND CHECKS

Background Checks	2019/20	2020/21	2021/22	2022/23
Number of Customer of Interests/Business of Interests	250	145	138	146

Source: Financial Intelligence Department, National Reserve Bank of Tonga

Supervision of Reporting Entities

Compliance Reviews

We oversee Financial Institutions operating in Tonga and engaged the assistance of the Department of Internal Affairs, New Zealand in the development of our supervision strategy for Designated Non-Financial Businesses and Professions (DNFBPs). This assistance will guide the FID in terms of the outreach approaches to these entities as well as the frequency and intensity of supervisory activities required for them. Fundamental to the effective supervision of these entities are the necessary legislations to be in place as well as qualified personnel to carry out the supervision tasks, both of which are currently in progress for completion in the next few months.

Coordination and Engagement

Working Group on Serious Financial Crimes

We are the Co-chair and Secretariat of the Working Group as the technical arm of the Cabinet Committee on Serious Financial Crimes. The Working Group continued to focus on addressing the APG Mutual Evaluation's recommendations therefore discussions included:

- *Stakeholder contributions to the review of Tonga's MLPC Act and Regulations, with the assistance of the International Monetary Fund. The draft Bill is currently being revised for finalisation in the team's next mission to Tonga in August 2023.*
- *Review of Tonga's National Risk Assessment and Policy*
- *Tonga's Follow Up Report (FUR) to the APG due in October 2022*

These discussions resulted in an update report provided to the Cabinet Committee on progress made by the Working Group, in terms of the concerns identified in Tonga's Mutual Evaluation, as well as recommended actions to bring the necessary legislations in line with the recommendations of the ME report.

Going forward, the Working Group will coordinate the preparation of a Strategic Implementation Plan for addressing the MER recommendations, with the assistance of APG before the end of 2023.

International cooperation is being enhanced with the signing of a Memorandum of Understanding with the Macao China Financial Intelligence Unit for information sharing. A similar arrangement with AUSTRAC is currently being processed. The Reserve Bank is also a member of the Pacific Financial Intelligence Community (PFIC) which provides support on developing strategies for combating regional money laundering and terrorist financing threats.

In May 2023, we conducted training for staff of the Ministry of Revenue & Customs' Revenue Department. This training relates to handling of information exchanged in tax-related investigations to combat financial crimes. We also provided similar trainings to Police through the Attorney General's Office.

9. PAYMENT SYSTEMS & ACCESS TO FINANCE

We regulate and supervise the Payment Systems which involves the daily settlement of interbank obligations arising from the conduct of Exchange Settlement Accounts (ESA), the National Reserve Bank of Tonga's own trading activities, and undertaking of banking business and depository for the Government. In modernising Tonga's payment and settlement system, the Domestic Electronic Payment system (DEPS) was fully functional since July 2022, where transactions between banks are settled in real-time.

Domestic Electronic Payment System

We manage and update DEPS live on a daily basis from terminals located at each of the Commercial Banks. For security purposes the DEPS is available to participants (4 commercial banks and NRBT) from 8:30am to 4:00pm daily, with the availability of an extension for late settlements by banks being approved on request. All interbank transactions and cheque clearance are physically exchanged by the banks daily and then processed through the DEPS. Commercial banks can view the balance of their ESA daily at any time to manage their liquidity. All payments and receipts are settled on a highly secured platform. Since July 2022, commercial banks arrange between themselves a time suitable to physically exchange and clear their cheques daily. A cheque can be cleared within 2 business days when verified by the originating bank into DEPS. In addition, the banks also avail opportunity for customers to fund their account before a cheque is presented for settlement.

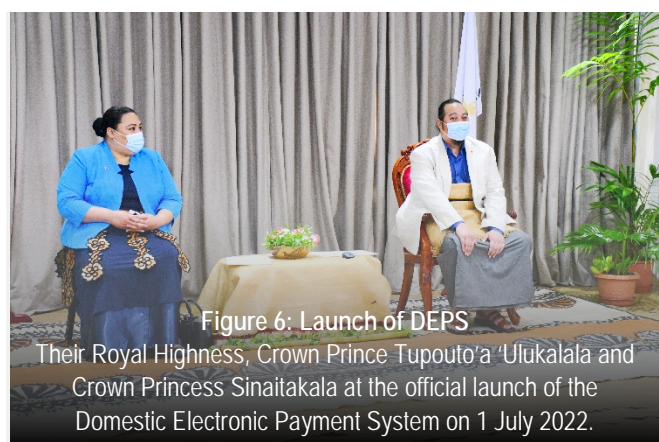


Figure 6: Launch of DEPS

Their Royal Highness, Crown Prince Tupouto'a 'Ulukalala and Crown Princess Sinaitakala at the official launch of the Domestic Electronic Payment System on 1 July 2022.

Interbank Daily Cheques Clearance

A total of 98,266 cheques were presented for clearance at the Reserve Bank during the financial year 2022/2023,

120,113 cheques in 2021/2022, 139,404 cheques in 2020/2021, and 145,821 cheques in 2019/2020. The 19.15% decrease from 2021/2022 in the number of cheques presented for clearance was driven by the broader usage of electronic transfer payments such as internet banking and EFTPOS machines. The clearance of cheques continued, and all participants were committed to settle their dues on time.

Cross Border Payments

We manage cross border payments for the Government and its counterparts overseas. The offshore payments on behalf of both Government and commercial banks were successfully conducted. Cross border payments via SWIFT are closely managed with the enforcement of strict controls administered by the IT department to mitigate any operational risks or financial loss. Internal controls through the reconciliation of the account balances to ensure safety and security of the Reserve Bank's assets overseas continued to be undertaken. The SWIFT system has been migrated from the current system to the ISO20022 on the 20th March 2023 and will co-exist until November 2025. The Settlement staff worked closely with our Correspondent Banks to validate the new swift messages and also to confirm that we are aligned with the Cross Boarder Payment and Reporting Plus (CBPR+) Standard. The Settlement staff continued to attend virtual meetings on the ISO20022 and continuous training has been conducted with operators to familiarize themselves with the new message format. NRBT is expecting to go-live by July 2023.

Access to Financial Services

An inclusive payment system, coupled with enhanced access to finance, forms the infrastructure that catalyzes economic growth by facilitating seamless low cost transactions, empowering businesses, and enabling individuals to participate more actively in economic activities. We promote financial inclusion initiatives to increase access to financial services and thereby support inclusive economic growth and poverty reduction efforts. We collect and analyse reports on access to financial services while engaging with relevant national and international stakeholders in supporting the financial inclusion initiatives. The national financial inclusion strategy to guide this work is being finalized, with the implementation of the financial inclusion

initiatives being supported by the Alliance for Financial Inclusion and other stakeholders.

Access points and usage of financial services

Tonga has seen increased access to financial services with the labour mobility schemes' expansion and linkage of foreign exchange dealers' (FEDs) remittance products to bank accounts particularly during the COVID-19

period and recovery from the HTHH disaster. The total number of cash in and cash out access points rose by 3% over the year to December 2022. This was driven by an increase in the number of branches (8%), number of agents (by 4%) and number of EFTPOS terminals (by 2%). The increase reflected the entrance of new FEDs into the market as well as the expansion of the services of FEDs and non-bank lenders.

TABLE 4: SUMMARY OF FINANCIAL INSTITUTIONS' ACCESS POINTS

Access Points	Dec '22	Dec '21	Year ended – Dec '22	
			Volume	Change (%)
Branches	68	63	5.0	8%
Agents	350	337	13.0	4%
EFTPOS	387	381	6.0	2%
ATMs	25	26	-1.0	-4%
TOTAL	830.0	807.0	23.0	3%

Source: Banks & Non-Bank Financial Institutions

In terms of constituency, Vava'u 15, Tongatapu 1 and Tongatapu 4 recorded the highest increase in the total number of access points mainly due to the rise in the number of EFTPOS as well as the number of agents in these constituencies. According to the banks, the increase in the number of EFTPOS over the year was mainly due to the installation of new EFTPOS terminals in some of the stores. Some EFTPOS machines and access points were deactivated due to the few number of transactions, perhaps indicating lower levels of financial and economic activity. On the other hand, the higher number of agents was driven mainly by Foreign Exchange Dealers and the microfinance institution (South Pacific Business Development). This reflects the expansion of their financial services to the outer islands especially to 'Eua, Vava'u and Niuafo'ou and Niuatoputapu and the demand for financial services from overseas seasonal workers and remittances. This is part of the Foreign Exchange Dealers' financial services outreach programme to the outer islands. The increase in branches also reflected the entrance of new Foreign Exchange Dealers.

TABLE 5: SUMMARY OF FINANCIAL INSTITUTIONS' ACCESS POINTS (BY CONSTITUENCY)

Constituency	Dec '22					Dec '21				
	Total Access Points	Branches	Agents	EFTPOS	ATMs	Total Access Points	Branches	Agents	EFTPOS	ATMs
Tongatapu 1	59	1	19	36	3	55	1	20	32	2
Tongatapu 2	200	24	23	141	12	198	24	22	138	14
Tongatapu 3	42	1	12	28	1	42	1	12	28	1
Tongatapu 4	143	5	22	113	3	139	4	22	110	3
Tongatapu 5	32	2	22	8	0	33	2	23	8	0
Tongatapu 6	39	1	31	6	1	38	0	31	6	1
Tongatapu 7	48	1	38	8	1	52	1	38	12	1
Tongatapu 8	24	0	14	10	0	29	0	15	14	0
Tongatapu 9	38	4	24	9	1	35	4	24	6	1
Tongatapu 10	28	0	28	0	0	28	0	28	0	0

Constituency	Dec '22					Dec '21				
	Total Access Points	Branches	Agents	EFTPOS	ATMs	Total Access Points	Branches	Agents	EFTPOS	ATMs
'Eua 11	40	7	31	2	0	38	6	28	3	1
Ha'apai 12	25	7	15	2	1	25	7	14	3	1
Ha'apai 13	16	1	13	2	0	14	0	12	2	0
Vava'u 14	20	0	19	1	0	18	0	17	1	0
Vava'u 15	55	14	18	21	2	48	13	15	19	1
Vava'u 16	17	0	17	0	0	15	0	15	0	0
Ongo Niua 17	4	0	4	0	0	1	0	1	0	0
TOTAL	830	68	350	387	25	807	63	337	381	26

Source: Banks & Non-Bank Financial Institutions

The usage of financial services also increased with the rise in the total number of individual deposit accounts and loan accounts as the major contributors. The increase in new customer accounts reflected the opening of new bank accounts by Regional Seasonal Employment (RSE) workers as part of the RSE schemes' requirements, coupled with the availability of the service for remittances to be directly deposited to bank accounts. This enabled contactless access to remittance receipts via the ATMs or EFTPOS machines during the lockdown periods. Moreover, the increase in total individual loan accounts reflected the relief packages provided by financial institutions, particularly the microfinance institution to its members, in the aftermath of the January 2022 HTHH disaster.

Micro, Small and Medium Enterprises

The MSME sector's access to financial services increased with both the number of MSME loans and the MSMEs outstanding loans rising reflecting mainly

support for the recovery from the HTHH disaster as well as the COVID-19 lockdown. This indicates improvement in support to the MSME industry. Access to financing for MSMEs in the manufacturing and wholesale retail sectors improved which is in line with the recovery of the economy. MSMEs' outstanding loans rose by \$7.2 million (28.5%) to \$32.3 million over the year ended December 2022, mainly due to the increase in outstanding loans to other services, wholesale retail and manufacturing. Banks' increased lending to MSMEs were predominantly to the other services and wholesale retail sectors while non-banks' lending to MSMEs were mostly to the manufacturing sector.

Banks hold the bulk of the total MSMEs outstanding loans at 65%. The number of MSME borrowers in both banks and non-banks increased by 156 (6.7%) to 2,479 MSMEs owing to an increase in the number of MSMEs in the manufacturing, fishing, wholesale retail and construction sector.

TABLE 6: SUMMARY OF MSMEs LOAN (BY SECTOR)

Type of Sectors	Dec '22		Dec '21	
	Number of MSMEs	MSMEs Outstanding Balance (T\$m)	Number of MSMEs	MSMEs Outstanding Balance (T\$m)
Overall Total	2,479	32.3	2,323	25.1
Agriculture	909	6.4	1,021	10.0
Construction	19	1.9	10	0.5
Fisheries	114	2.2	88	0.9
Forestry	1.0	0.0	1	0.0

Type of Sectors	Dec '22		Dec '21	
	Number of MSMEs	MSMEs Outstanding Balance (T\$m)	Number of MSMEs	MSMEs Outstanding Balance (T\$m)
Manufacturing	1,168	10.7	938	9.0
Other Services	61	3.6	66	0.7
Tourism	52.0	2.3	55	1.7
Transport	21.0	0.7	28	0.4
Wholesale/Retail	134	4.5	116	1.9

Source: Banks & Non-Bank Financial Institutions

Financial products and services

Developing financial products and services that are affordable and relevant for the financial consumers' financing needs is important for striving for financial inclusion. We continued to support efforts to leverage on technology and other enablers in developing financial products that can be accessible and affordable, particularly for the vulnerable and productive sectors, while ensuring adequate protection of financial consumers. To help enhance access to financial services and reduce vulnerability to external shocks we supported new products, including digital financial services, parametric insurance, and credit scoring facility, to be piloted or rolled out by the banks with the assistance of development partners.

Financial Information

Financial information is published on the NRBT website to allow the comparison of the best exchange rate, lowest fees, and interest rates that are offered by the licensed banks and non-bank financial institutions. Furthermore, a financial calculator is also made available to allow customers to calculate and compare the Annual percentage rate (APR) on a loan. The APR includes all fees and charges as well as interest rates per annum and charged on a declining balance.

We are the Banker for Government

We are the Government Bank and continued to facilitate government payments and receipts both locally and overseas from its accounts at the Reserve Bank with no issue recorded in 2023.

TABLE 7: TOTAL VALUE OF GOVERNMENT PAYMENT – FY2023

Months	Overseas Payment (\$)	Local Payment (\$)	Government Bond (\$)
July 22	1,348,524.78	9,566,819.42	150,000.00
August 22	1,431,928.34	1,617,167.19	88,800.00
September 22	10,758,488.51	6,026,266.24	8,075.00
October 22	1,948,317.73	15,328,647.08	-
November 22	996,460.41	9,277,836.76	23,200.00
December 22	2,336,511.33	7,576,745.71	-
January 23	1,321,779.22	3,520,671.77	180,510.00
February 23	124,931.67	5,104,417.05	125,000.00
March 23	11,738,050.94	4,295,112.88	208,025.00
April 23	831,394.85	5,054,397.80	100,000.00
May 23	1,299,107.30	13,365,011.50	252,560.00
Jun 23	2,460,039.04	43,201,252.17	5,368,780.00

Months	Overseas Payment (\$)	Local Payment (\$)	Government Bond (\$)
TOTAL	36,595,534.12	123,934,345.57	6,504,950.00

Source: Banks & Non-Bank Financial Institutions

During the year, we continued to facilitate Government payments and receipts both locally and overseas from its accounts at the Reserve Bank. We continued to maintain a total of 39 number of Government accounts both in foreign currency and Tongan pa'anga, and provided financial statements daily and upon request.

Registrar of Government Securities & Policy Advice Support

As the registrar of Government securities, we conducted market preference surveys for bonds and provided advice to the Ministry of Finance. There are 17 Government bond series currently in circulation of which annual interest payments were processed and paid to holders while 3 matured and were rolled over during the financial year.

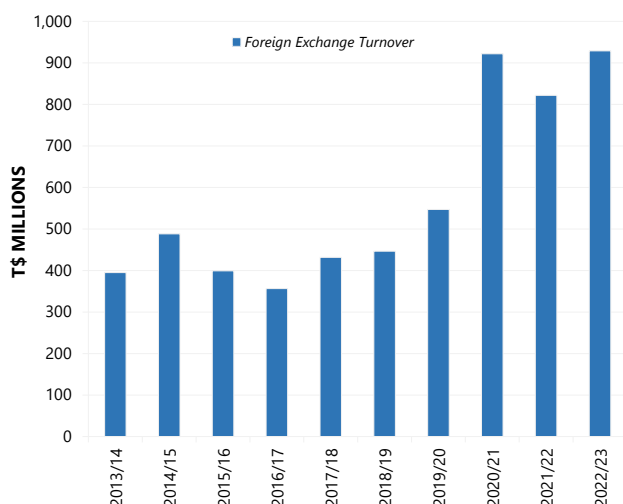
We also continued to provide weekly and monthly exchange rates to the Ministry of Finance and the Ministry of Revenue and Customs to assist with the ministries' functions. In addition, monthly exchange rates are provided to the Tonga Competent Authority at the Ministry of Trade and Economic Development for the setting of the domestic fuel prices.

10. FINANCIAL MARKET OPERATIONS

Foreign Reserves Management

Gross official foreign reserves was maintained well above the IMF's optimal level of 7.3 months of import cover. It peaked at a record high of T\$927.2 million during June 2023 before levelling at T\$921.4 million by the end of June 2023, equivalent to 13.0 months of import cover compared to T\$871.2 million (14.4 months of import cover) as at 30 June 2022. The significant increase in foreign reserves was attributed mainly to receipts of remittances, Government budget support, project funds, and other capital receipts, which outweighed the higher import payments during the year.

**FIGURE 7:
FOREIGN EXCHANGE TURNOVER**



Source: Commercial Banks' Exchange Rates

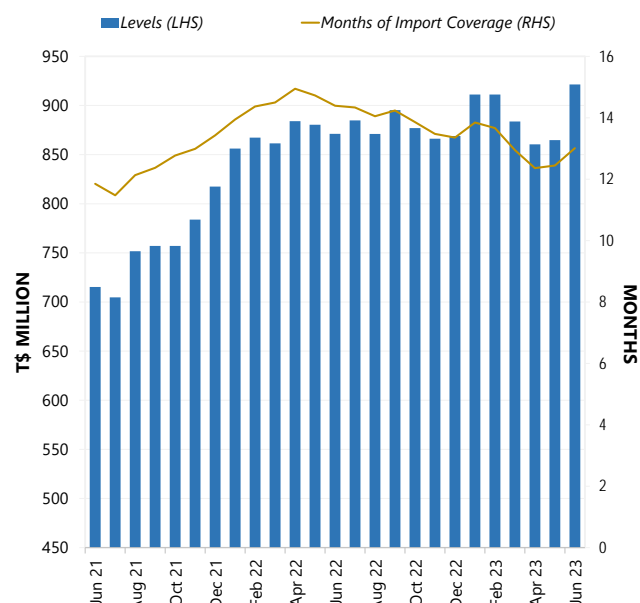
During the year, the Reserve Bank was a net purchaser in the spot foreign exchange markets. Foreign exchange purchases of T\$489.9 million exceeded sales of T\$439.0 million giving a total foreign exchange turnover for the year of T\$928.9 million. This is an increase from T\$821.3 million last year. The Reserve Bank also paid T\$1.2 million in foreign exchange levy tax from these transactions to the Ministry of Finance.

Our investment policy focused on maximizing income while maintaining safety, liquidity and the maintenance of overall value, which has proven to be challenging given the uncertainty and volatility in the global financial markets. The currency composition of the foreign reserves was mainly in US dollar, Australian dollar and New Zealand dollar.

Our investment strategy continued to maintain the value of the foreign reserves, valued in Tongan pa'anga. As a hedge against currency fluctuations, the foreign reserves are invested in accordance with the weights of the currencies in the exchange rate basket (benchmark) that are used to calculate the rate of exchange of the Tongan pa'anga against other currencies. During the year, against a background of fluctuating exchange rates, the exchange rate policy decision was to strike a delicate balance between enhancing interest income on investment and safeguarding price stability, and maintaining the value of the foreign reserves. As a result, the deviation from the benchmark resulted in a revaluation loss.

Income on the investment of the foreign reserves increased by \$21.4 million from the previous year to an all-time high. This aligned with the record level of foreign reserves during the year. Higher interest rates in global markets due to prolonged aggressive tightening by the US, New Zealand and Australian central banks to combat inflationary concerns during the year also supported the growth in investment income.

**FIGURE 8:
GROSS OFFICIAL FOREIGN RESERVES
Monthly**



Source: Financial Markets | Economics Department

Foreign Exchange Control Operations

We manage the foreign exchange operations and processed 682 exchange control applications totaling

T\$395.2 million (of which 11.0% were classified as capital transactions) compared to 520 applications last year. The exchange control data and information on foreign currency payments by large customers are essential inputs to the Reserve Bank's forecast of foreign reserves, investment decisions and monetary policy decisions, while ensuring the payments are genuine transactions.

In addition, we reviewed and authorized 44 applications totaling T\$44.8 million for the removal of physical cash (both Tongan pa'anga and foreign currency notes totaling T\$10,000 and above) across the border, increasing from T\$2.4 million approved last year due to the border reopening.

In January 2023, we revised the Exchange Control Directive issued due to the high level of foreign reserves, the accommodative monetary policy stance, and feedback from banks and foreign exchange dealers. This resulted in the relaxation of some of the requirements, including an exemption list for highly compliant customers. Awareness Training on the Exchange Control Directive for all banks and foreign exchange dealers was undertaken.

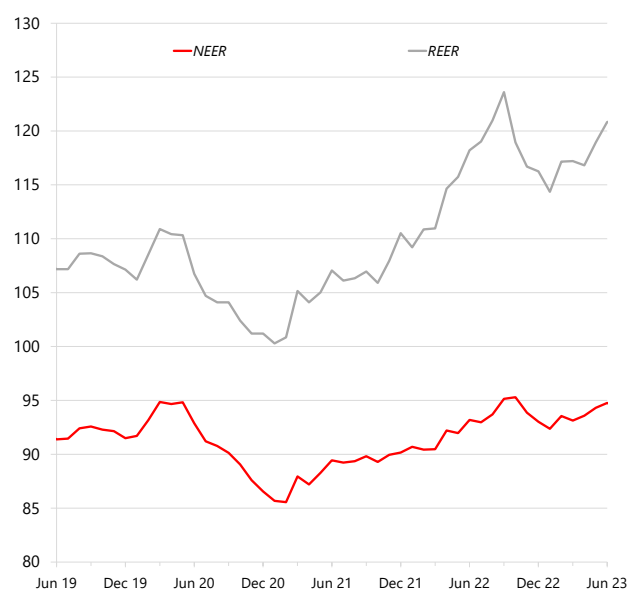
We also conducted regular spot checks and reviewed monthly reports received from banks and foreign exchange dealers and provided training to address any non-compliance.

Exchange Rate Management

The Reserve Bank determines the rate at which the Tongan pa'anga is exchanged for foreign currencies on a daily basis by reference to a weighted basket of currencies of Tonga's major partners in foreign trade and foreign receipts and payments. The exchange rates set on a daily basis generally form the basis of the commercial banks' publicly quoted foreign exchange dealing rates. During the year, the exchange rate policy was reviewed, including the review of the exchange rate basket and the assessment of the revaluation of the Tongan pa'anga. The IMF during its 2023 staff visit and Article IV mission assessed Tonga's exchange rate management framework as appropriate to promote stability.

The Reserve Bank monitored the movement of the rate of exchange of the pa'anga against other currencies to ensure that the country's balance of payments position and price stability are maintained at levels consistent with the achievement of macroeconomic stability.

FIGURE 9:
NOMINAL & REAL EFFECTIVE EXCHANGE RATES
Monthly



Source: National Reserve Bank of Tonga

Over the year ended June 2023, the Tongan pa'anga (TOP) generally strengthened against almost all of Tonga's trading partners' currencies except for the USD. The strength of the TOP as measured by the Nominal Effective Exchange Rate (NEER) increased by 1.7%. The TOP appreciated against the AUD and the NZD by 2.7% and 1.4% respectively while it weakened against the USD by 1.1%. The Real Effective Exchange Rate (REER) increased over the year by 0.9%. The annual increase is in line with the higher NEER as well as Tonga's higher inflation compared to its major trading partners, indicating a loss of competitiveness for Tongan goods on the global market.

As part the Reserve Bank's efforts to mitigate inflationary pressures, the limits on the exchange rate spreads on the telegraphic transfers were revised and approved in the February 2023 Monetary Policy Statement. The spread on US dollar transactions was reduced from 220 basis points to 170 basis points while the limits on AUD and NZD transactions remained the same at 300 bps and 350 bps respectively. Furthermore, these limits were imposed on foreign exchange dealers for the first time, which provides a level playing for all authorised dealers, including the commercial banks. The Reserve Bank will continue to monitor and ensure compliance of the exchange rate spreads of all authorized persons with the Reserve Bank's approved limits.

The Reserve Bank also continued to publish on the website, financial information, such as comparisons of financial institutions' daily and weekly exchange rates

and fees related to foreign exchange transactions, to assist the public with their financial decisions.

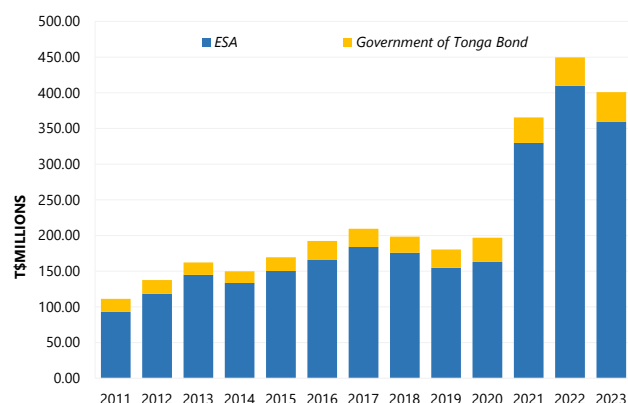
Implement Monetary Policy and Develop Tonga's Financial Market

The focus of the Reserve Bank's February 2023 Monetary Policy Statement was to better control the level of inflation. The statutory reserve deposits (SRD) rate was increased to 15% from 10%. The Financial Markets Department facilitated the establishment of new deposit facilities for the Government and the Retirement Funds to mop some of the high level of excess liquidity in the banking system, which had reached over \$350 million. A total of T\$41.3 million was mopped through the increase in SRD and a further T\$25 million was mopped from the retirement funds' deposits at the commercial banks.

The Reserve Bank will continue to explore ways to reduce the excess liquidity in the system to improve its monetary policy transmission mechanism. Due to the excess liquidity in the banking system, there was no activity in the inter-bank market. Similarly, there were no applications for repurchase agreements during the year.

The Reserve Bank is also exploring options to develop the domestic market operations to be more market-oriented.

**FIGURE 10:
BANKING SYSTEM LIQUIDITY**



Source: Financial Markets, National Reserve Bank of Tonga

11. FINANCIAL PERFORMANCE

The balance sheet, income statement, and the statement of cash flows from the Audited 2023 Annual Financial Statement² are provided in **Annex 1**. The notes to the audited financial statements providing a comprehensive overview of NRBT's financial performance and position are disclosed separately.

Foreign Currency Assets: The foreign currency assets have experienced a consistent upward trend over the past five years. Notably, in 2023, the foreign currency assets reached a substantial value of \$940.9 million, demonstrating a significant increase from the \$878.2 million recorded in 2022. **Local Currency Assets:** In contrast to the foreign currency assets, the local currency assets have displayed some fluctuations. The total assets have followed a consistently upward trajectory.

Foreign Currency Liabilities: The foreign currency liabilities have experienced an upward trend over the years, with a notable increase from \$103.5 million in 2022 to \$140.1 million in 2023. This escalation is attributed to the Government's interest-free loan from the IMF in the second half of 2022. **Local Currency Liabilities:** Local currency liabilities have also shown growth over the years, with \$790.2 million recorded in 2023. This steady increase from \$764.9 million in 2022 suggests increase in deposits contributed by the higher remittances and Government budget support. The total liabilities have risen consistently, reflecting the cumulative impact of both foreign currency and local currency liabilities. In 2023, the total liabilities reached \$930.3 million.

The net assets have witnessed fluctuations over the years, with a positive trend established until 2023. The subsequent decline from \$34.2 million in 2021 to \$32.8 million in 2023 reflects the ongoing revaluation loss in 2022 and 2023 and the payout to Government from the Revaluation Reserve in 2021. The substantial increase in financial performance and net profit during 2023 is the result of not only of higher interest rates, but a change in investment strategy that proved accurate and yielded better results.

The transfer of funds to the Government of Tonga from the net profit available for distribution has shown significant growth over the years, reaching \$14.3 million in 2023. This financial contribution can play a vital role in supporting the Government's initiatives, public services, and overall economic development.

TABLE 8: COMPARISON OF FINANCIAL RESULTS OVER THE YEARS

	2023	2022	2021	2020	2019
Foreign Currency Assets	940,998,055	878,165,991	719,707,467	553,063,047	495,905,776
Local Currency Assets	22,128,521	20,210,320	55,662,988	55,328,502	53,050,259
Total Assets	963,126,576	898,376,311	775,370,455	608,391,549	548,956,035
Foreign Currency Liabilities	140,094,098	103,511,006	70,125,399	94,115,730	73,516,881
Local Currency Liabilities	790,218,001	764,938,995	671,005,902	478,412,725	430,693,809
Total Liabilities	930,312,099	868,450,001	741,131,301	572,528,455	504,210,690
Net Assets	32,814,477	29,926,310	34,239,154	35,863,094	44,745,345
Net Profit available for distribution	20,387,379	529,534	200,050	4,273,964	6,000,600
Transfer to Government of Tonga	14,271,165	370,674	140,035	2,991,775	4,200,420

Source: Finance Department, National Reserve Bank of Tonga

² External audit for FY ended 30 June 2023 was conducted by KPMG Fiji.

12. RISK MANAGEMENT AND COMPLIANCE

We oversee risk management and promote a risk awareness culture against an updated risk management framework that has been integrated into all policy oriented and operational activities. The Risk Management Unit, under the Governor's Office, in collaboration with all departments identified, assessed, managed and monitored the many risks the Reserve Bank faces. Extensive use of Management Committees set up ensures that all risks, inherent and emerging, are considered and managed effectively.

Corporate Risk Governance

The Risk Management Committee approved in February 2023 the Risk Management Framework, Policy and Appetite for the Bank to implement and reviewed its application for amendments before it is presented to the Board for approval.

Incident Reporting is part of the Risk Management Framework of the Reserve Bank to document events that occur and that may adversely affect the achievement of the Reserve Bank's mandate as outlined in the NRBT Act. There were twenty-six incidents reported during the year. Majority of the incidents were Operational and Financial Risk related incidents, however they were Risk Rated low and are manageable. Some incidents were caused by external factors, which was beyond the Reserve Bank's control, however the resilient controls embedded in the processes were very effective leading to proactive alerts to Management. We continue to ensure that incidents are identified, reported and are timely and effectively resolved.

Where required, the relevant processes or internal controls are reviewed to ensure that any risk arising are mitigated. Furthermore, during the year, the Risk Management Unit conducted random spot checks of the Foreign Reserves Management processes according to the approved Reserve Management Policy. Overall compliance were confirmed.

Management is responsible for consistently implementing and maintaining mitigations for risks arising within their respective department. The structured process throughout the Reserve Bank and the relevant policies, processes and system are sufficient to manage the anticipated risks.

Internal Audit

A strong, independent and objective internal audit function is a key part of the Reserve Bank's overall commitment to good corporate governance practice. In response to the IMF Safeguard Assessment recommendation, the Reserve Bank is outsourcing its

internal audit function with the invitation to tender distributed in May 2023. A chartered accountant to also serve as Internal Auditor proceeded to recruitment before the end of June 2023. This is mainly to focus on high risk areas, such as currency operation, foreign reserves management and information technology.

Delegation of Authority

All Reserve Bank activities and expenditure must be authorised in accordance with the respective delegations, policies and procedures. The Risk Management Unit reviewed and updated the Delegation of Authority that was approved by the Board.

Complaints Management

We tasked the Risk Management Unit with registering complaints from external parties, stakeholders or the general public, in relation to the performance of the Reserve Bank's services and/or functions, as well as the services of the financial institutions that are licensed by the Reserve Bank. During the year, there were three complaints lodged with the Reserve Bank against the licensed financial institutions which was referred to the Financial Systems department. There were no complaints against the Reserve Bank regarding its services and/or functions.

Business Continuity and Disaster Recovery Management

The continuity of critical business functions before, during and after a disruptive event is a key area of focus for us. The Reserve Bank continues to refine its Business Continuity and Disaster Recovery Plan during these unprecedented times of National State of Emergency.

IMF Safeguards Assessment

The Reserve Bank continued to address the IMF's 2021 Safeguards Assessment report's recommendations. The key areas highlighted in the report were mainly on the 5 pillars underpinning good governance. This includes External Audit Function, Legal Function, Reporting Function, Internal Audit Function and Internal Control

Function. The Reserve Bank has completed addressing 8 of the recommendations while 2 are still work in progress. Some of the recommendations require the assistance of a technical expert to guide the implementation, and the IMF has agreed to provide the necessary technical assistance. Other highlighted issues are still work in progress, as Management is drafting

policies to strengthen its operations through strengthening the internal control.

As the Reserve Bank continues to keep the IMF apprised on the progress, the Board and Management continued to ensure that the Reserve Bank adopts international best practice on its operations.

13. CURRENCY MANAGEMENT

We are responsible for regulating the issue of currency in the Kingdom of Tonga and maintaining an adequate supply of quality banknotes and coins in circulation to meet the public's currency needs. To maintain its clean currency policy, the Reserve Bank redeems from the banks any banknotes or coins that are mutilated or no longer fit for circulation and destroys them accordingly.

On the 30 June 2023, the face value of currency in circulation, both new and re-issuable in the old King George Tupou V design and new King Tupou VI design, totaled \$118.0 million. This was a decline of 14.5% over the past year due to removal of the COVID-19 pandemic restrictions, which waned demand for banknotes.



The value of banknotes in circulation for the FY 2023 fell by 15.3% to \$112.3 million. The \$10 banknote denomination recorded the largest decline of 24.8% to \$4.9 million, mainly due to increased usage of EFTPOS for small merchant purchases. The \$50 remained the most popular bank-note for the previous 5 years and recorded the highest volume of notes in circulation.

The value of coins in circulation increased by 6.6% to \$5.6 million as at end of June 2023. The 20 seniti registered the highest growth of 7.0% to \$1.1 million while the 10 seniti accounted for the highest volume of coins in circulation at \$8.8 million pieces. High usage of the 20 seniti and large volume of 10 seniti in circulation are both attributed to demand from retail shops.

The Reserve Bank focuses on maintaining an adequate supply of quality banknotes and coins to accommodate public demand and facilitate the commercial banks' banking operations. In FY 2023, \$119.5 million of notes and coins was issued to commercial banks, 10.8% less than the previous year. The commercial banks returned \$138.4 million worth of notes to the Reserve Bank to be processed. Of this, \$131.3 million was deemed fit for reissue while \$7.0 million was deemed unfit and destroyed.

A 4-year backlog of notes for destruction warranted a special currency operation starting in March 2023 which recounted and destroyed a total of \$127.4 million by 30th June 2023. Nine (9) staff were engaged to assist this project and is considered a successful initiative. As at 30 June 2023, more than 90% of the 618 parcels marked for destruction were finally shredded. We also considered the use of more advanced technology in the area of currency management.

TABLE 9: CURRENCY IN CIRCULATION

Tongan Pa'anga	2018/19	2019/20	2020/21	2021/22	2022/23
Banknotes (\$millions)	86.5	88.2	111	132.7	112.3
Coins (\$millions)	4.1	4.4	4.8	5.3	5.7
TOTAL	90.6	92.6	115.8	138.0	118.0

Source: Currency Department, National Reserve Bank of Tonga

Counterfeit Bank Notes

Ensuring the integrity of the national currency remained a top priority for the Currency Department in 2023. Efforts to combat counterfeit currency were advanced through a combination of collaboration, and public awareness campaigns. During the year, a total of 26 confirmed counterfeit notes received by the Reserve Bank was six times more than the previous year. Of the total number of counterfeits received 50% of the value was \$20 pa'anga and 35% was \$50 pa'anga.

Numismatic Currency

During the year, numismatic coins were issued to collectors throughout the world under agreements between the Reserve Bank and various producers for the production and marketing of coins in various denominations. Collectibles banknotes were also sold to local and overseas clients of previous and current banknotes series. The income from the sale of numismatic currency fell by 53% to \$0.03m compared to the previous year. Slow sales was attributed to the pandemic.

New Bank Note Project

We continued to work with De La Rue on the design concept for the new family of bank notes for Tonga that was approved by Privy Council. The new bank note design concept reflects Tonga's national identity, manufactured from the latest materials for durability, and integrating the modern security features to thwart counterfeit, to ensure Tonga's bank notes is a secure document.

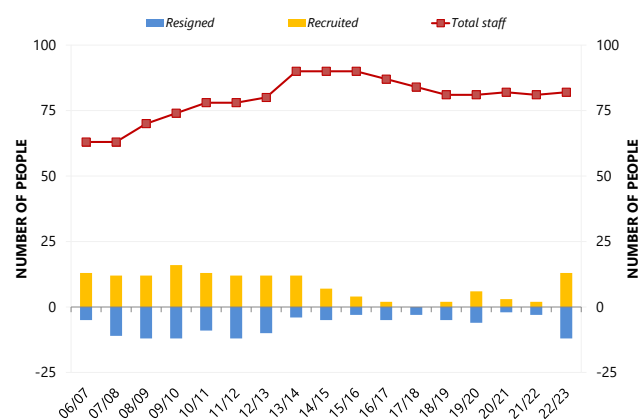
14. CORPORATE SERVICES

Staffing

We support the wellbeing of our staff through the Human Resources (HR) Department providing a range of services to the Reserve Bank as a whole. This entails facilitating services to maintain staff productivity, such as annual performance appraisal reviews, recruitment and selection of a professional team, enhanced staff training and development, review of job descriptions and promotion of a healthy organization. The Department also maintained compliance with all legal, statutory and Reserve Bank organizational policies.

At the end of June 2023, the Reserve Bank maintained a total staff of 82 employees, 22% on fixed-term contracts, 66% permanent employees, 2% were new recruits and 10% daily paid staff. The Reserve Bank also supported staff engagement in further studies via part-time correspondence study and overseas full-time professional study. Of the 82 staff, 54% are women, and 46% are men. The staff turnover in FY 2023 increased to 15% from 4% in FY 2021/22 where 12 employees exited the Reserve Bank due to various reasons.

FIGURE 12:
NRBT STAFF NUMBERS



Source: National Reserve Bank of Tonga

We increased activities outlined in the corporate plan and recruited 13 employees in 2023 financial year with 4 permanent staff, 1 contract staff and 8 daily paid staff. This is to strengthen staff capacity in the Security, Finance, Currency and Governor's Office. With 82 employees onboard, the Reserve Bank continued to facilitate and deliver its core responsibilities to achieve its objectives and strategic priorities.

Staff Training and Development

We encourage staff's participation at overseas professional training, which increased in 2023 due to the re-opening of international borders. This is in addition to the online and virtual training conducted throughout the year. We provide financial support for staff undertaking part-time correspondence studies at the University of the South Pacific, Tonga. In January 2023, 3 employees were supported to be on full-time professional studies in Australia. The Reserve Bank also acknowledge the ongoing support of the Australian Scholarship Award Program for the opportunity granted to the Reserve Bank staff to enable tertiary studies in Australia.

Organizational Health and Safety

We continue to encourage a healthy work environment by supporting staff to participate in corporate netball tournaments, regular health checks, encourage group exercise and various health activities. We believe that a healthy employee improves self-confidence, health, staff productivity, and overall morale.

Human Resource Information System

In modernizing the Reserve Bank's operation, we invested in a Human Resource Information System (HRIS) to automate the HR processes and enable staff to apply for leave electronically via the system as well as strengthen staff learning through the Learning Management System (LMS) and also automate the Staff Performance Management System (PMS). In February 2023, the Reserve Bank engaged ELMO HR as its HRIS and the implementation of the system is currently underway to be completed in the next financial year. ELMO HR will also be integrated with Payroll and the Accounting.

System Information Technology

Our Information Technology (IT) Department is developing and maintaining a resilient network infrastructure that support the ongoing operations of the Reserve Bank. Our technology environment comprises of specialized systems, software applications and three (3) highly available network infrastructure.

In 2023, we focused on the provision of technology services to support the our response to the pandemic, including the implementation of the Domestic Electronic Payment System (DEPS), ongoing development of

Cybersecurity initiatives, and the review of existing system and software.

Technical Support - Domestic Electronic Payment System

We completed the development of the Domestic Electronic Payment System and was officially launched on 1st July 2022, marking the completion of the development and testing phase. We deployed and connected the DEPS from commercial banks in July 2022. Our IT department provided technical support to the clients and ongoing monitoring of the DEPS payment system. A network monitoring system was installed in April 2023 to provide real-time monitoring of the DEPS infrastructure and network.

Cybersecurity



Figure 13: Cybersecurity Incident Response

The Reserve Bank's Cyber Incident Response Team (CIRT) during their annual Cyber Incident Desktop exercise for 2022

Cybersecurity remains a key priority for us in 2023, with continued ongoing threat monitoring and detection of emergency security vulnerabilities in ensuring the security of the Reserve Bank's systems and information are maintained. This is supported by a program of activities to build cybersecurity awareness for all Reserve Bank staff, and cyber intelligence-sharing with the financial institutions, Government (Tonga Computer Emergency Response Team) and central banking communities. The Reserve Bank continued to comply with the SWIFT Customer Security Program (CSP) mandatory requirements through external independent attestation. The Cyber Incident Response Team (CIRT) completed the annual desktop exercise and testing the effectiveness of the Cyber Incident Response Plan (CIRP). The Reserve Bank will continue to work on the remaining SWIFT CSP advisory controls, including penetration testing and vulnerability assessment in the next financial year. The Reserve Bank was also very cautious on its internet connection capabilities during the period where one of the Internet Service Providers succumbed to a cyberattack during the year. Our

redundancy setup enables the Bank continue its internet-enabled operations while keeping a close eye on the cyber risks from the attack.

Technology Review and Delivery

To remain efficient and relevant, the Reserve Bank's technology was upgraded and updated on a regular basis. This includes annual replacement of desktop workstation with laptops and ongoing automation of patching and malware endpoint protection. The Reserve Bank also utilized cloud computing to enable virtual meetings and online trainings for staff. The IT staff continued to upskills through online courses and workshop.

The Reserve Bank continues to research for more ways of implementing technological advancement and innovate improvements into its operations, which will also support the Bank in achieving its Strategic Priorities.

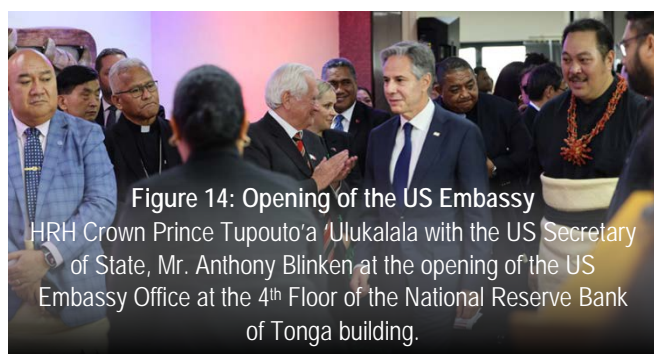
Major technology-related projects completed in FY 2023 included: the review of the SWIFT System, the implementation of the TAIPAN system for FID; the review of the Human Resource Information System (ELMO HR); and the review and replacement of the current Attaché Accounting Software with Accredo Software. The IT team conducted system review and will continue to support the projects' implementation.

Building & Property

Our Building & Property team continued to maintain the Reserve Bank's building, property, plant and equipment to uphold its standards and enhance a safe and secure working environment for the Bank's staff, tenants, visitors and stakeholders in 2023. We managed to successfully provide in-house repair and maintenance programs to ensure efficient operation of all systems. This involved carrying out refurbishment projects which include the following:

- (a). Completion of the NRBT plumbing system upgrade for the Embassy of Japan bathroom;
- (b). Completion of Phase two for the upgrade works towards the centralized air condition system and control;
- (c). Installation of temporary split air condition unit at the Embassy of Japan;

- (d). Upgrade the main water pump for the building's main water supply;
- (e). Review and renewal of the leased agreement for the World Bank for another five years;
- (f). Facilitating two new tenants' offices, the Embassy of the United States of America occupying the whole 4th Floor and the Tonga Australian Support Platform at Level 3 Suite 4.
- (g). Undertaking the NRBT Building Evaluation for insurance coverage.
- (h). Completion of the structural assessment of the building to ensure that it is structurally sound to withstand cyclones and earthquakes.
- (i). Review of the Tenants' rental rate and Tenancy agreements.



The Reserve Bank continued to engage Willis Tower NZ Ltd to manage its insurance programs and with the completion of the building evaluation in May, the market value of the Building increased to \$23.1 million and Plant and Contents at \$1.6 million.

General Administration

During 2023, we continued to provide support services to the other departments through responsibilities for procurement of goods and services, managing access to the building, physical and electronic keys registry as well as management of the transport services and office delivery. Records management, purchase orders, commitment records, and corporate communications systems management are services also provided by the Administration Unit. Throughout the year, these services were well managed and provided without any issues.

Security Unit

Our Security team continued to carry out its responsibilities of ensuring that the security and safety of the Reserve Bank's staff and premises are maintained at all times by providing effective 24-hour surveillance of the Reserve Bank building and compound. The Security Unit also monitors the movement of visitors in the Reserve Bank property to ensure proper approval have been granted to enter the property. One of the primary responsibilities of the Security Unit is to safeguard the Currency operations and consignments to mitigate the risks that may arise in these areas. At the end of the year, no security breach was observed and the safety and security of the Reserve Bank staff and building were maintained. Currency operations and consignments were also safeguarded well and no issue was reported.



15. ANNEX 1: AUDITED NRBT FINANCIAL STATEMENTS

<u>NATIONAL RESERVE BANK OF TONGA</u>		BALANCE SHEET AS AT 30 JUNE 2023	
	<u>2023</u>	<u>2022</u>	
	\$	\$	
ASSETS			
Foreign Currency Assets			
Short/Long Term Investments and Current Accounts	851,157,990	801,947,340	
Accrued Interest	19,610,321	7,033,412	
International Monetary Fund (IMF)			
- Reserve Tranche Position	10,889,205	10,749,556	
- Special Drawing Rights	59,340,539	58,435,683	
Local Currency Assets			
Cash on Hand	10,666	7,456	
Accrued Interest	52,586	-	
Other Assets	11,621,855	9,921,042	
Property, Plant and Equipment	10,443,414	10,281,822	
Total Assets	963,126,576	898,376,311	
LIABILITIES			
Foreign Currency Liabilities			
Accrued Interest	57,689	4,142	
Demand Deposits	77,275,079	41,550,419	
IMF Special Drawing Rights Allocation	62,761,330	61,956,445	
Local Currency Liabilities			
Payable to Government	14,271,165	370,674	
Demand Deposits	504,158,153	541,184,871	
Accrued Interest	167,528	15,456	
Other Liabilities	5,102,780	3,383,208	
Currency in Circulation	118,026,586	138,018,723	
Statutory Reserve Deposits	123,395,000	81,819,000	
Non-Bank Deposits	25,000,000	-	
Employee Provisions	96,789	147,063	
Total Liabilities	930,312,099	868,450,001	
NET ASSETS	32,814,477	29,926,310	
CAPITAL AND RESERVES			
Paid up Capital	5,000,000	5,000,000	
General Reserves	22,748,068	16,631,854	
Revaluation Reserve Account	5,066,409	8,294,456	
TOTAL CAPITAL AND RESERVES	\$32,814,477	\$29,926,310	

Income	<u>2023</u>	<u>2022</u>
	\$	\$
Interest Income	26,810,437	5,351,355
Other Income	3,581,734	3,060,776
Total Operating Income	30,392,171	8,412,131
Expenses		
Interest expense	1,889,625	153,036
Administration and other expenses	8,096,542	7,712,145
Allowance for impairment losses	18,625	17,416
Total Operating Expenses	10,004,792	7,882,597
Net profit available for distribution	20,387,379	529,534
Net losses arising from the translation of foreign currency balances to local currency	(3,228,047)	(4,471,704)
Other comprehensive losses for the period	(3,228,047)	(4,471,704)
Total comprehensive (loss)/income	\$17,159,332	(\$3,942,170)

	Paid up Capital \$	General Reserves \$	Revaluation Reserve Account \$	Retained Earnings \$	Total \$
Balance 30 June 2021	5,000,000	16,472,994	12,766,160	0	34,239,154
Net Profit				529,534	529,534
Net losses arising from the translation of foreign currency balances to Tongan currency	-	-	(4,471,704)	-	(4,471,704)
Transfer to General Reserves (as provided for under Section 8(1)(c) of the National Reserve Bank of Tonga (Amendment) Act 2014, and approved by the Minister of Finance	-	158,860	-	(158,860)	-
Balance Payable to Government of Tonga as required under Section 8(3) of the National Reserve Bank of Tonga (Amendment) Act 2014.	-	-	-	(370,674)	(370,674)
Balance 30 June 2022	5,000,000	16,631,854	8,294,456	0	29,926,310
Net Profit	-	-	-	20,387,379	20,387,379
Net losses arising from the translation of foreign currency balances to Tongan currency	-	-	(3,228,047)	-	(3,228,047)
Transfer to General Reserves (as provided for under Section 8(1)(c) of the National Reserve Bank of Tonga (Amendment) Act 2014, and approved by the Minister of Finance	-	6,116,214	-	(6,116,214)	-
Balance Payable to Government of Tonga as required under Section 8(3) of the National Reserve Bank of Tonga (Amendment) Act 2014.	-	-	-	(14,271,165)	(14,271,165)
Balance 30 June 2023	5,000,000	22,748,068	5,066,409	0	32,814,477

	2023 \$	2022 \$
CASH FLOWS FROM OPERATING ACTIVITIES		
Interest received	14,180,943	2,866,550
Rental income	1,762,652	593,808
Numismatic sales	37,654	80,565
Other income	2,684,798	2,394,391
Purchase of currency	(3,266,467)	(1,636,511)
Interest paid	(1,684,006)	(149,125)
Payments to suppliers and employees	(5,336,140)	(4,515,158)
Net cash inflow from operating activities	8,379,434	(365,480)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of fixed assets	(860,603)	(239,449)
Net movement in IMF accounts	(1,044,504)	(40,636,993)
Net movement in staff loans	263,111	(142,193)
Net movement in investible reserves	(50,044,821)	(133,881,396)
Net cash used in investing activities	(51,686,817)	(174,900,031)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net movement in currency in circulation	(19,992,137)	22,125,450
Net movement in demand deposits	(50,684,062)	79,896,275
Net movement in statutory deposits	41,576,000	13,936,000
Net movement in Government of Tonga account	49,382,004	3,986,823
Net movement in funds held for clearance	-	157,447
Net movement in IMF SDR Allocation	804,885	40,823,506
Profit repatriation to Government	(370,674)	-
Debt securities issued by the Bank	25,000,000	-
Net cash inflow from financing activities	45,716,016	160,925,501
NET INCREASE IN CASH	2,408,633	(14,340,010)
CASH AND CASH EQUIVALENT AT BEGINNING OF FINANCIAL YEAR	13,256,545	32,068,259
NET EFFECT OF CHANGE IN EXCHANGE RATE	(3,228,047)	(4,471,704)
CASH AND CASH EQUIVALENT AT END OF FINANCIAL YEAR	12,437,131	13,256,545