30 June 2013

Government of Tonga
Annual Public Debt Bulletin

Prepared by

Debt Management Section

Ministry of Finance & National Planning

Authorised for release by

Minister for Finance & National Planning

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Acronyms and Abbreviations

ADB	Asian Development Bank
APDB	Annual Public Debt Bulletin
ATF	Average Time to Refixing
ATM	Average Time to Maturity
AUD	Australian Dollar
BOC	Bank of China
CBD	Central Business District
CNY	Chinese Yuan Renminbi
ComSec	Commonwealth Secretariat
CPIA	Country Policy and Institutional Assessment
CS-DRMS	ComSec Debt Recording and Management Section
DMS	Debt Management Section
DSA	Debt Sustainability Analysis/Assessment
DOD	Disbursed Outstanding Debt
EGS	Exports of Goods and Services
EIB	European Investment Bank
EUR	Euro
EXIM	Export–Import Bank of China
FC	Foreign Currency
FI	Financial Institution
FY	Financial Year
GDP	Gross Domestic Product
GFS	Government Finance Statistics
GoT	Government of Tonga
GBP	Great British Pounds
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
JPY	Japanese Yen
LIC	Low Income Countries
MoFNP	Ministry of Finance and National Planning
MTDS	Medium Term Debt Strategy
NRBT	National Reserve Bank of Tonga
NPV	Net Present Value
PFMA	Public Finance Management Act
PRC	People Republic of China
RFB	Retirement Fund Board
SDR	Special Drawing Rights
TA	Technical Assistance
TCC	Tonga Communication Corporation
TDB	Tonga Development Bank
TDS	Total Debt Service
TDDS	Total Domestic Debt Service
TEDS	Total External Debt Service
TOP	Tongan Pa'anga
TPD	Total Public Debt
TPL	Tonga Power Limited
TSDF	Tonga Strategic Development Framework
USD	United States Dollar
WB	World Bank
WBOT	Westpac Bank of Tonga

Acknowledgements

This is the second Annual Public Debt Bulletin (APDB) as based on an Outline recommended by Commonwealth Secretariat (ComSec) in line with international reporting requirements of Public Debt Statistics Guide issued by (International Monetary Fund) IMF and affiliated associations.

The key role played by the Debt Management Section (DMS) for co-ordinating production of this important report is acknowledged also the other contributors of data from the Economic and Budget divisions of Ministry of Finance and National Planning (MoFNP), also related divisions of the National Reserve Bank of Tonga (NRBT).

Milestones that have been achieved in the implementation of debt management reforms during the last year are referred in Section 2.3. under Reforms.

Foreword

The Government of Tonga (GoT) recognises the importance of prudent debt management in the medium term and for better reporting of its debt portfolio for informed decision making.

In order to improve this, the MoFNP has been working closely with development partners such as the ComSec and the World Bank (WB).

As part of its effort to disseminate information on the public debt position, regular quarterly debt reporting is provided to Cabinet and other institutions as required including information available on the Ministry's website.

This APDB is a comprehensive format which reports annually on the state of public debt management over the last few years with reference to current reforms in this area and also includes projections of both debt stock and debt service in the future years.

GoT primary objective of the debt management policy is to maintain sovereign debt within levels that are sustainable over time. This requires regular monitoring of debt levels against commonly accepted debt targets or thresholds established by multilateral institutions while also ensuring that any financing requirements are met at low cost with a minimum degree of risk in the medium term. This general objective and approach is also reflected in the Tonga Strategic Development Framework (TSDF) of 2011-2014 and the MoFNP's Corporate Plan.

Public debt continues to be a priority issue for GoT and it is imperative to ensure debt sustainability in the medium term especially with the significant rise in external debt service as projected from FY 2013/14. The Budget theme of FY 2013/14 "Continuing to Create Opportunities by Building on Inclusive Sustainable Growth", reflects the belief that the next five years will continue to be challenging reflecting the uncertain global economic conditions, but that with continued prudence we can still encourage inclusive sustainable growth while ensuring fiscal stability.

Further to improvement of the Country Policy and Institutional Assessment (CPIA) rating from 'Weak' to 'Medium' by the WB, Tonga has been recently upgraded by the IMF from a high risk of debt distress to a moderate level. This review provides a significant increase in the prior debt sustainability thresholds in the medium term. However, GoT will be cautious of the debt position and the ‘no new borrowing’ policy to continue until such time that it may be feasible.

In priority efforts by MoFNP to minimise major risks in GoT’s external debt (estimated at 92%), proposals include to reduce the significant portion of debt from People’s Republic of China (PRC) as denominated in Chinese Yuan Renminbi (CNY at 66.6%) also the high level of debt from Asian Development Bank (ADB) and International Development Agency of World Bank (IDA) as denominated in Special Drawing Rights (SDR at 33.2%) and for a more balanced composition of public debt including development of the domestic debt market (estimated at 8%).

A Medium Term Debt Strategy (MTDS) for GoT over FY 2013/14 to 2015/16 has been developed by DMS of MoFNP which refers to some options that are considered as practical for GoT to explore during the next three years and for review annually in line with progress of macro and fiscal developments. This policy to be submitted to Cabinet for endorsement and implementation by the MoFNP as part of its medium term fiscal consolidation.

With this upgrade it also means reduced grant financing of 100%, whereby future requirements from the WB and ADB will be considered on a 50:50 grant/loan mix and MoFNP is liaising with these donors to confirm date for implementation of this policy in the future. As this will have an impact on budget support assistance in the medium term and limited options for GoT to finance its various obligations.

In conclusion, I wish to take this opportunity to express my continued appreciation to all the stakeholders participating in the on-going public debt management reforms. It remains a challenging time for GoT to improve the debt burden and other fiscal vulnerabilities while maintaining sustainability and stability also to strengthen the relations with external and domestic financiers including the development partners collaborating with Tonga.

Hon. Lisiate ‘Aloveita ‘Akolo

Minister for Finance & National Planning

Executive Summary

- **The total disbursed outstanding debt** (DOD) of loans by Government as at 30th June 2013 in nominal value at millions of Pa'anga's over the 5 year period, is shown below:

Loans	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
External	202.4	228.8	274.9	322.6	**343.1**	**20.5**	**140.7**
Domestic	22.5	29.5	29.5	29.5	**29.5**	**-**	**7.0**
Total Public Debt	**224.9**	**258.3**	**304.4**	**352.1**	**372.6**	**20.5**	**147.7**
Guarantees	9.5	14.0	12.1	7.8	**0.1**	**-7.7**	**-9.4**
On-lent	22.3	23.0	40.8	63.9	**64.1**	**0.2**	**41.8**
Total Contingent Debt	**256.7**	**295.3**	**357.3**	**423.8**	**436.8**	**13.0**	**180.1**

- **Total public debt** was estimated at $372.6m *(44.6% of GDP)*, with External debt at $343.1m *(41.0%)* and Domestic debt at $29.5m *(3.6%).* During the 5 year period, there was a huge increase in external debt ($140.7m) mainly due to loan disbursements from EXIM for CBD and Roads and appreciation of the CNY currency.
- **Main external debt creditors** are**:** EXIM at $221.0m *(64%*), and ADB at $64.3m *(19%)*. During the 5 year period, there was an increase of $170.4m in the DOD to EXIM as result of appreciation in the CNY currency. The total disbursement was made for Roads Improvement Project estimated at $8.7m.
- **Domestic debt** comprises of bond issues, with the majority of holdings by Financial Institutions (FI) at $17.3m *(59%)* and Retirement Fund Board (RFB) at $6.6m *(23%)*. During the 5 year period, there was an increase of $7.0m mainly due to new bond issues.
- The **main external loan currency denomination** is the CNY at $228.4m *(67%)* and the SDR at $114.0m *(33%)*. During the 5 year period, there was a significant increase in CNY composition of $170.4m *(54%)*, due to the major loan disbursements from EXIM.
- **Total External DOD** in **net present value (NPV)** by 30 June 2013 is estimated at $346.7m (*41% of GDP)* at current FC/TOP rates. For the next 2 years and with reference to debt sustainability targets below, most of the indicators will not be breached (includes fluctuations[1]).

[1] Nominal GDP, Exports & Remittances decrease by 2%, Revenue decrease by 1%,& FC rates increase by 5%

Debt Sustainability Indicators	IMF-GoT Target %	FY 2013 %	FY 2014 %	FY 2015 %
NPV of debt as:				
% of GDP	**40**	41	41	36
% of exports & remittances	***150***	129	132	121
% of budget revenue	**250**	215	214	192
Total Debt Service as:				
% of exports & remittances	**20**	8	11	13
% of budget revenue	**20**	13	18	20

- **External DOD to GDP will continue to exceed the recommended level in the medium term** and the main Creditor and Currency composition will remain as EXIM and CNY currency. This results in high risk and exposure to volatility of exchange rates especially with strengthening of the CNY.
- **External debt service** is estimated to significantly increase to $20m *(at around 2% of GDP and 11% of expenditure)* from FY 2013/14 but will remain within the recommended targets. This is mainly due to commencement of the principal loan repayments to EXIM for CBD and Roads, until loan maturity in FY 2029/30.
- **To maintain debt sustainability in future**, it is vital that our current level of economic activity prospects improve together with prudent public debt management through priority implementation of MTDS, in order to mitigate the vulnerability to shocks.

1. Introduction

The *APDB as at 30 June 2013* presents the major public debt management activities between July 2012 and June 2013 including review of historical data over the last 5 fiscal years and with projections over the next 10 fiscal years or so. It reports key data and ratios on the public debt portfolio (stocks and flows) and how these have changed over the course of the year. Looking forward, the Bulletin will discuss the GoT's MTDS and priority action for debt reduction programs, fiscal consolidation, estimations for GDP growth, projections of fiscal deficits and other macroeconomic developments.

SECTION 2: Addresses the framework for Public Debt Management Operations

SECTION 3: Covers the following recent developments:

- recent macroeconomic and fiscal trends,
- the borrowing program during the past year,
- domestic debt issuance,
- external debt borrowing,
- a comparison of the planned vs actual borrowing, and
- developments in the secondary market

SECTION 4: An overview of the public debt portfolio and discusses some risk indicators

SECTION 5: Position of Contingent Liabilities

- loans on-lent
- loan guarantees

SECTION 6: Discusses issues relating to debt sustainability

SECTION 7: Conclusion and way forward for debt management

2. Framework for Debt Management Operations

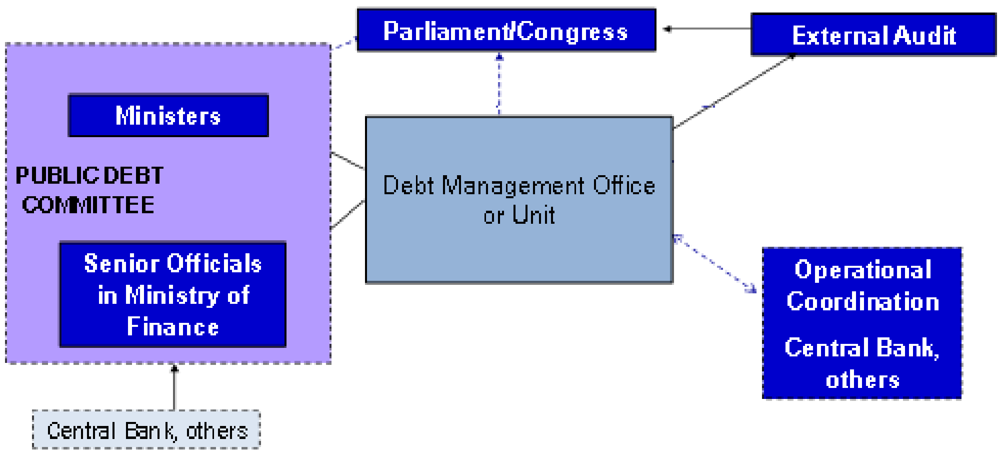
The PFMA 2002 specifies that the Minister of Finance is responsible for economic, fiscal and financial management by Government, Part V, provides the basic legal framework for Government's borrowings, loans and guarantees.

The DMS under the Treasury Division is primarily responsible for debt management duties on behalf of MoFNP and the mandated task of meeting the GoT's objective for public debt management as referred in the GoT's inaugural MTDS for 2013/14 – 2015/16 at June 2013 is:

> *That the GoT maintains sovereign debt within levels that are sustainable over time. This requires regular monitoring of debt levels against commonly accepted debt targets or thresholds established by multilateral institutions while also ensuring that any financing requirements are met at low cost with the minimum degree of risk in the medium term.*

This debt management objective is also reflected in the GoT's TSDF and also the MoFNP's Corporate Plan.

Figure 1: Typical Governance Structure



2.1 Legislative Arrangements

The PFMA, Part V, Sections 23 to 34 refers to the main provisions on Borrowings, Loans and Guarantees: Authority to borrow; Power to raise loans; Loans to GoT; Subsidiary Loan Agreements; Stocks, Bonds and Promissory Notes; Treasury Bills; Liability of GoT; Power to give Guarantees and Indemnities; Taking and release of security to GoT;

Expenditure for protection of public securities and Register of Loans and Guarantees.

The MoFNP is also considering review of the draft Policy Framework for GoT Guarantees and to also include the on-lent loans to public enterprises and other entities as arises.

2.2 Role of the Central Bank

The NRBT acts as registrar for Government's securities and fiscal agent for external and domestic loan payments.

2.3 Reforms

In reference to the past reforms these have been covered in the initial APDB of June 2012.

During the 1 year period (FY 2012/13), some of the main debt management activities carried out were:

(i) Quarterly reporting to Cabinet on the status of GoT's loan portfolio, with progress of the CBD and Roads loans including Debt Sustainability Analyses (DSA).

(ii) An Advisory Mission by ComSec on Domestic Debt Market Development from 16 to 27 July 2012, with recommendations and order of priority for work to be done and assistance by ComSec, as possible (refer Recommendations Table 1);

(iii) A Mission by World Bank on Public Debt Management Reform Plan from 29 November to 11 December 2012, with recommendations and order of priority for work to be done and assistance by WB, as possible (refer Recommendations Table 2);

(iv) Draft MTDS 2013/14-2015/16 completed in June 2013 and submitted to MoFNP management for final comments and tabling at Cabinet.

(v) Ongoing capacity building of staff by participation in donor funded trainings as related to debt policy issues, during September 2012 to June 2013.

3. Developments in the Past Year

3.1 Macroeconomic Developments

Table 1: Main Economic Variables *in TOP$m*

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
Gross Domestic Product	664.3	711.4	783.4	781.5	836.1	54.6	171.8
Fiscal Balance	-19.4	33.6	24.5	23.7	25.4	1.7	44.8
Current Account Balance	-97.8	-52.6	-69.8	-86.2	-74.5	11.7	23.3
Inflation (%)	5.6	1.7	6.0	3.4	0.9	-2.5	-4.7
Exports of Goods &Services	95.1	83.2	100.3	103.1	154.8	51.7	59.7
Debt Service	16.9	17.0	22.8	15.2	20.4	5.2	3.5
Expenditure	207.8	175.8	177.5	165.2	178.3	13.1	-29.5
Revenue	186.8	159.6	151.0	146.7	159.7	13.1	-27.1
Remittances	175.2	157.4	146.5	112.3	113.3	1.0	-61.9
Foreign Reserves	136.3	170.5	203.8	246.1	258.4	12.3	122.1

In reference to the GoT's Budget Statement of 2013-14 and its theme of "Continuing to Create Opportunities by Building on Inclusive Sustainable Growth". This focuses on consolidating and building on priority policy and program areas that were implemented in 2012/13 and have the potential for further development. The theme reflects the belief that the next five years will continue to be challenging reflecting the uncertain global economic conditions, but that with continued prudence we can still encourage inclusive sustainable growth while ensuring fiscal stability

The following information refers to the key macroeconomic developments and impact on borrowing.

The economy has recorded a strong average growth rate of 2.6% for 4 consecutive years, due in large part to reconstruction of the Nuku'alofa central business district and road development from the large Chinese loan funded construction and other donor-funded aid projects.

With the end of the loan drawdown, total growth is slowing, though the underlying growth rate, without the loan expenditure, remains stronger. Overall growth is forecast to gradually strengthen over the next few years; however, it will not be possible to repeat the large boost from the heavy borrowing, which has left the country with a large debt overhang. The nature of the growth now taking place is also better balanced and more wide spread than the construction boom lead growth which was focused in Nuku'alofa, with much of the value added produced by foreign workers and company who were based in Tonga long enough to be included in GDP estimates.

The macroeconomic environment which includes low level of inflation, adequate level of liquidity and funding available for lending at reasonable interest rates will help to shape economic growth, fiscal operations and by extension the level of debt that the GoT will contract to fund its activities.

3.2 The Borrowing Programme

Tonga's Debt Sustainability position has been recently upgraded by IMF-WB DSA of 2013, from a high risk of debt distress to a moderate level. As further to recent improvement of the Country Policy and Institutional Assessment (CPIA) rating by WB from weak to medium.

However, in line with the current "No New Loan Policy", this is maintained by GoT as part of the priority actions under the MTDS. With close monitoring and for any ease in future of borrowing to be at concessional terms and for debt levels to remain within the recommended targets.

The annual borrowing by GoT during FY 2012/13 is approved by Legislative Assembly in July 2012 as part of the Budget estimates. This includes projections of remaining external loan disbursements from PRC (EXIM) for the Roads project at $8.7m (the initial approval for these 2 loans were made in prior fiscal years), and roll-over for financing of maturing bonds ($7.5m).

Financing for roll-over of the maturing bonds remained within the statutory limit of $15.0m as stated in PFMA Section 25(1). Section 31(1)(b) also refers that the total level of guarantees outstanding at $0.15m, is well below the limit for 5 percent of GoT fund appropriated.

There were no other borrowings taken.

3.2.1 Fiscal Outcome

GoT's fiscal position[2] declined with the global slowdown and fall in remittances putting downward pressure on GoT receipts which fell 14% between FYs 2010/11 and 2011/12. Without budget support, GoT would have had to cut expenditure by a further 15% or more in real terms; however, with budget support it was possible to rebuild cash balances from a crisis level of $1.9m in FY 2009/19 to a healthy $33.7m in FY 2011/12. This is the desired level of about 2 months' payments, which is considered prudent.

[2] This section is focusing on GoT receipts (basically revenue plus repaid on-lent loans) and payments (basically expenditure plus repayment of GoT debt). Receipts and payments matter for GoT's overall cash balance, while revenue and payments matter for the GFS accounts.

Even with vigilance, there remain however, serious structural issues that GoT continues to struggle with. The most serious include the high proportion of the budget that goes on staff costs, and the large increase in debt repayments. This limits the scope for expanding into new initiatives.

Table 2: Fiscal Outcome *in TOP$m*

Item	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
1. Total Receipts	186.8	159.6	151.0	146.6	159.7	13.1	-27.1
2. Total Expenditure	207.8	175.8	177.5	165.2	178.3	13.1	-29.5
3. Gross Fiscal Deficit/Surplus	-21.0	-16.2	-26.5	-18.5	-18.6	37.1	2.4
As a % of GDP	**3.2**	**2.3**	**3.4**	**2.4**	**2.2**	**-0.2**	**-1.0**
4. Financing of Fiscal Deficit							
(a) Local Currency Financing							
(i) Bonds	7.0	6.6	10.4	3.0	7.5	4.5	0.5
(b) Foreign Currency Financing							
(i) Loans	43.0	41.4	67.6	47.5	8.7	-38.8	-34.3

3.2.2 Government Borrowing

In this section, the Bulletin will discuss the GoT's borrowing target and borrowing strategy for the year under review (FY 2012/13). External debt accounts for 92% and domestic debt accounts for 8%. Loans sourced externally are mainly on a concessional basis at an average of 35 years and 1.63% interest per annum, mainly from the EXIM and ADB. Domestic debt comprises of public bonds issued on a more commercial basis at an average of 5 years and 4.93% interest per annum.

Table 3: Government Borrowing *in TOP$m*

Total Net Borrowing	**FY 2013 Original**	**FY 2013 Actual**	**change**
Domestic	7.5	7.5	-
External	5.1	8.7	3.6
Total	**12.6**	**16.2**	**3.6**
Gross Borrowing by Instrument			
Bonds	29.5	29.5	-
Loans	316.7	343.1	26.4
Total	**346.2**	**372.6**	**26.4**

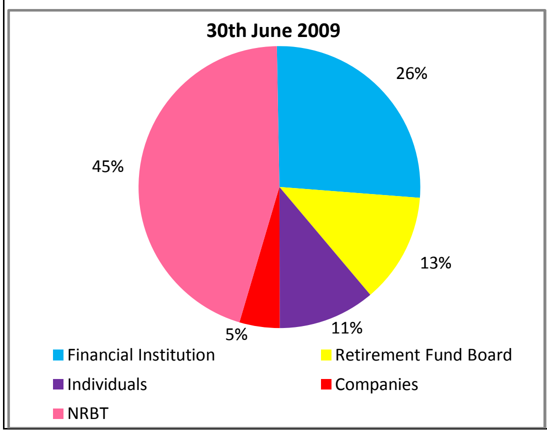
On net basis, a total borrowing was estimated at $16.2m in 2013. Of this total, $8.7m and $7.5m to be raised from external and domestic sources, respectively. However, total net borrowings exceeded the original target by $3.6m due to the fluctuation of FC/TOP rates as used in the original external estimates and the actual position as at 30 June 2013.

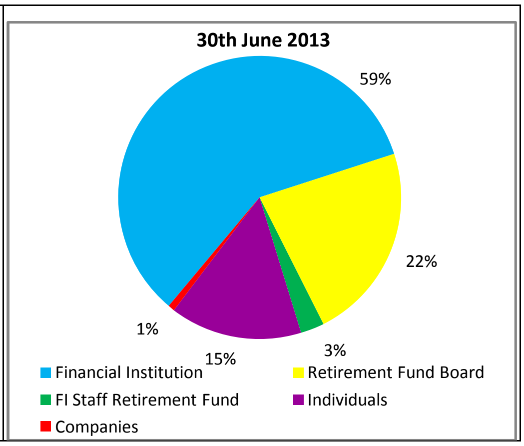
3.2.3 Domestic Debt Issuance

From FY 2009 to FY 2013, domestic debt has increased by 31.1% to current level of $29.5m. As result of the global financial crisis, a couple of bond issues of $8.0m were required during FY 2009/10 for budget support. During FY 2010/11, a 3-6 month Treasury Bill of $7.0m was also issued to support GoT's operations and it was settled by June 2011 once the budget support funds was received from donors.

GoT's bonds are mainly issued on a roll-over basis with exception of any redemptions or new issues. FI's now account for the majority of holdings at $17.3m with RFB at $6.6m and Individuals at $4.4m. Since amendment of NRBT Act in 2007, they no longer have any holdings of GoT's securities.

Figure 1: Holdings of Domestic Debt





3.2.4 External Debt Borrowing

The grant element specifies the level of concessionality of external loans taken form bilateral or multilateral creditors. In countries such as Tonga with higher debt vulnerabilities, the concessionality threshold or minimum grant element as recommended by the IMF and WB should be at minimum average of 32%.

At such level, it implies that loans will have a longer grace and maturity period with lower interest rates. Concessionality of GoT's external loans over the last 5 year period is shown below:

Table 4: Average Terms of New Loans

	FY 2009	FY 2013
Maturity (Years)	20.0	20.0
Grace Period (Years)	5.0	5.0
Interest Rate (%)	2.0	2.0
Grant Element (%)	57.5	55.6

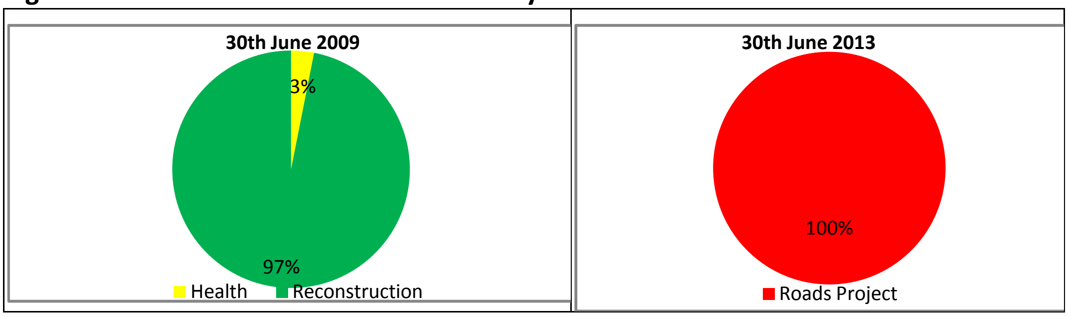
3.2.5 Disbursement of External Loans

The following Table shows the position of total external loan disbursements over the 5 year period. There has been a significant change in disbursements of major projects, as shown in the Charts.

Table 5: Disbursement of External Loans *in TOP$m*

DETAILS	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
Disbursed Outstanding Debt	202.4	228.8	274.9	322.6	343.1	20.5	140.7
Disbursements	42.9	41.4	67.6	47.5	8.7	-38.8	-34.2
Principal Repayments	4.7	4.6	6.0	5.7	5.8	0.1	1.1
Net Flows On Debt	38.2	36.8	61.6	41.8	2.9	-38.9	-35.3
Interest Payments	3.6	3.8	4.3	4.8	5.3	0.5	1.7
Net Transfers On Debt	34.6	33.0	57.3	37.0	-2.4	-39.4	-37.0
Total Debt Service	**8.3**	**8.4**	**10.3**	**10.5**	**11.1**	**0.6**	**2.8**

Figure 2: Disbursement of External Loans by Use of Funds



3.2.6 Developments in the Secondary Market

As at 30 June 2013, there was still a high level of liquidity in the banking system and market interest rates were lower then prior years. Prior to amendment of the NRBT Act in 2007 to repeal Section 49 in the Principal Act that NRBT may hold GoT bonds, NRBT held the majority of holdings in GoT's bonds and the Financial Institutions now account for the main bond holders.

The NRBT is registrar of Government's securities and a public tender of bonds available is made in the local media and NRBT website. There is no auction system used and NRBT also makes direct contact with the main bond holders to confirm interest for investment.

There is a need to develop the domestic market and particularly the issue of GoT's securities according to best market practices. In line with the main findings and based on some of the recommendations by the ComSec and WB missions during 2012 that the MTDS considers some practical strategies to be explored by GoT during the next 3 years. Other recommendations on development of debt management as made by experts as a way forward will be considered by MoFNP with request to these donors for further technical assistance (TA).

4. Public Debt Portfolio

Gross external debt, at any time, is the outstanding amount of those actual and current, not contingent liabilities that require payment of principal and/or interest by the debtor at some point in the future; and that is owed to non-residents by residents of an economy.

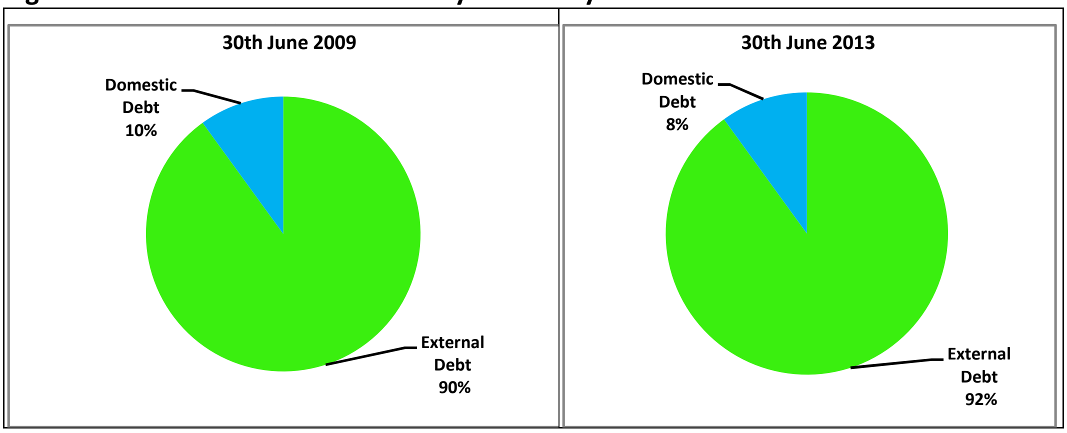
Gross public sector debt increased by 5.8% between 2012 and 2013, continuing the upward trend since 2008, as result of the external debt position.

Table 6: Main Debt Indicators *in TOP$m*

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
Gross central govt debt	**224.9**	**258.3**	**304.4**	**352.1**	**372.6**	**20.5**	**147.7**
Debt-to-GDP (%)	33.9	36.3	38.9	45.1	44.6	-0.5	10.7
External Debt	**202.4**	**228.8**	**274.9**	**322.6**	**343.1**	**20.5**	**140.7**
External debt-to-GDP (%)	30.5	32.2	35.1	41.3	41.0	-0.3	10.5
External debt-to-EGS (%)	237.0	260.9	302.4	375.1	221.7	-153.4	-15.3
External debt-to-Reserves (%)	148.5	134.2	134.9	131.1	132.8	1.7	-15.7
Domestic Debt	**22.5**	**29.5**	**29.5**	**29.5**	**29.5**	**-**	**7.0**
Domestic debt to GDP (%)	3.4	4.1	3.8	3.8	3.5	-0.3	0.1

As at 30th June 2013, the external debt stock increased to $343.1m, which is equivalent to 41% of GDP at 92% of total debt. By contrast, domestic debt remained constant at T$29.5m and only makes up 4% of GDP at 8% of total debt (Figure 4).

Figure 3: Central Government Debt by Residency of Creditor



External debt continues to account for the majority of total public sector debt. Access to financing from external sources is readily available especially from PRC, and the increase of 4% during the 5 year period (June 2009 to June 2013) is due to further drawdown of the two major infrastructure loans from EXIM for the CBD and Roads projects.

The breakdown of GoT debt by instrument type is referred below.

Table 7: Debt by Instrument Type *in TOP$m*

Gross debt by instrument type	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
Loans	202.4	228.8	274.9	322.6	343.1	20.5	140.7
Securities	22.5	29.5	29.5	29.5	29.5	-	7.0
Arrears	-	-	-	-		-	-

Other essential items on status of the public debt portfolio are:

Figure 4: Total Public Debt to Nominal GDP % (TOPm), FY 2008/09 – 2012/13

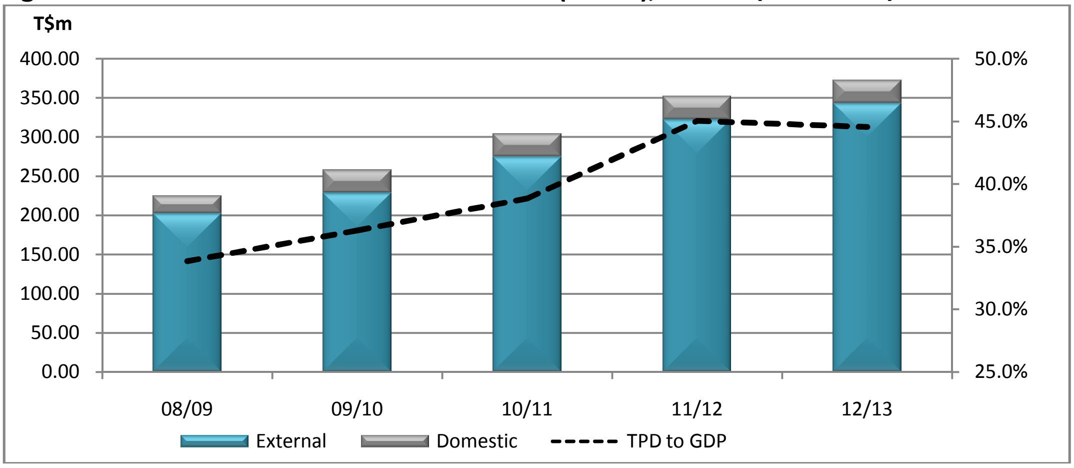


Figure 5: Total Public Debt service in ratio to Revenue and Expenditure, FY 2008/09 – FY 2012/13

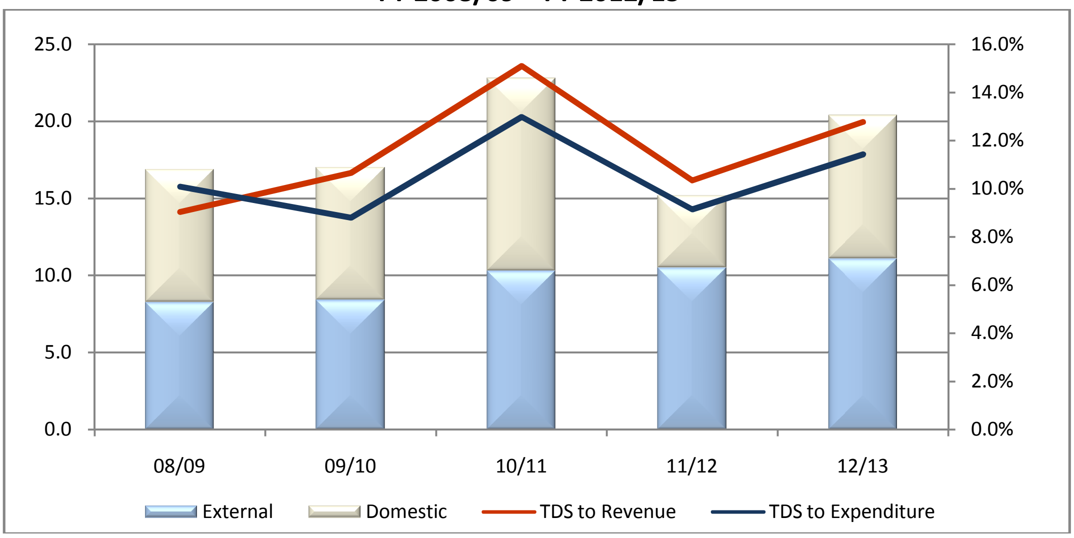


Figure 6: Instrument

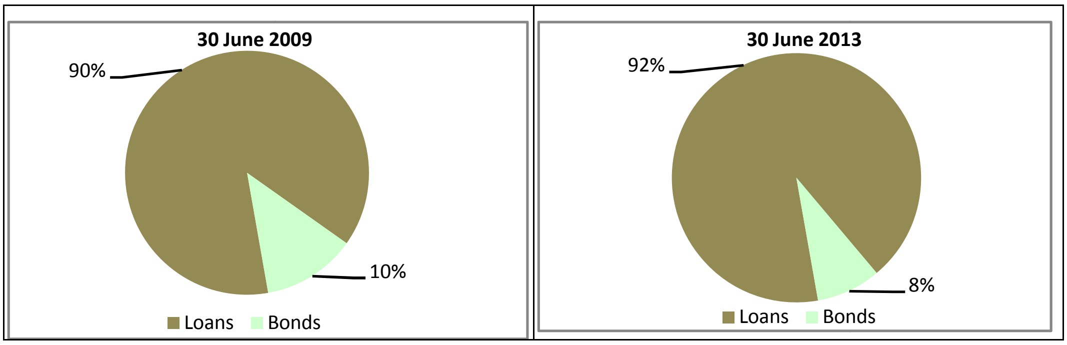
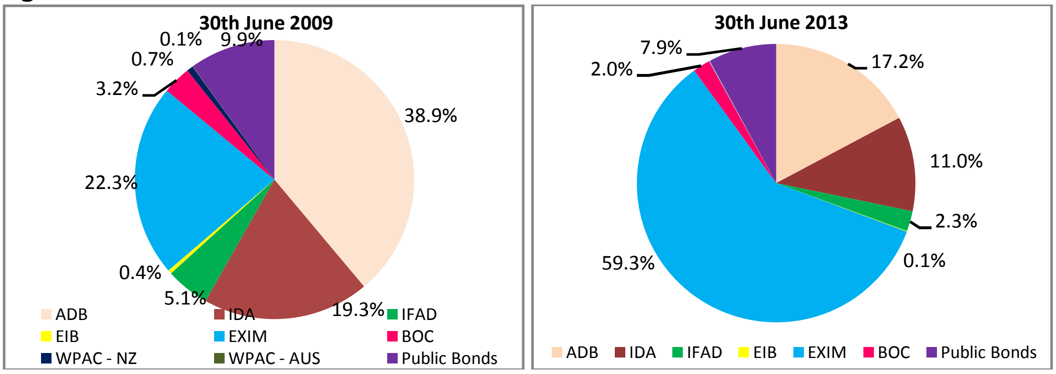


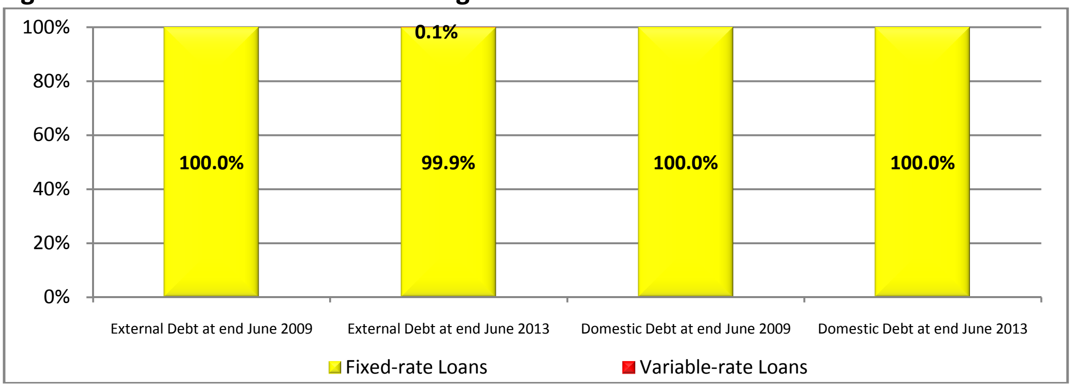
Figure 7: Creditor



4.1 Portfolio Risks

The basic risk measures include:

Figure 8: Share of fixed rate to floating rate debt



As the majority of GoT's external and domestic borrowing is on a fixed interest basis, there is currently minimal interest rate risk and this is expected to apply during the next 3 years.

Short term debt is defined as instruments of less than 1 year on original maturity plus long-term instruments with a remaining maturity of less than 1 year.

Figure 9: Share debt maturing within 1 year

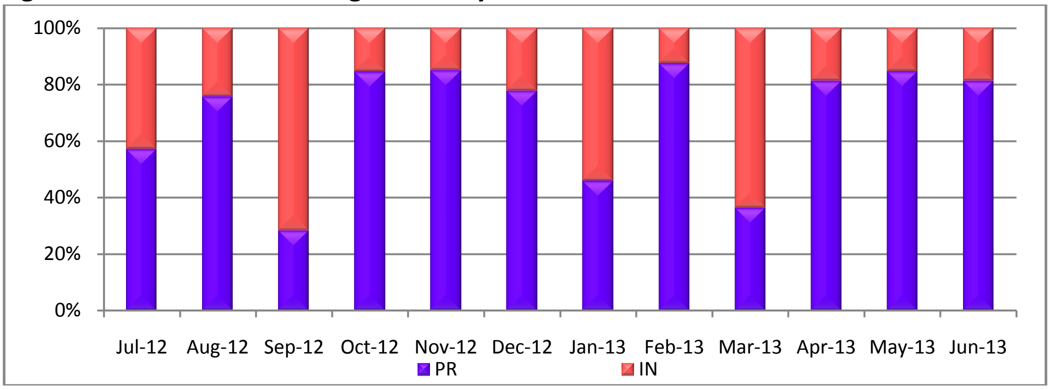


Table 8: Average time to interest rate re-fixing (external debt)

Years	Fixed	Variable	ATF
1 - 2	0.2	-	0.0
3 - 5	4.3	-	0.1
5 - 10	2.5	0.4	0.1
10 - 15	150.6	-	5.8
+15	185.1	-	8.6
TOTAL	**342.7**	**0.4**	**14.6**

Figure 10: Share of foreign currency to domestic currency debt

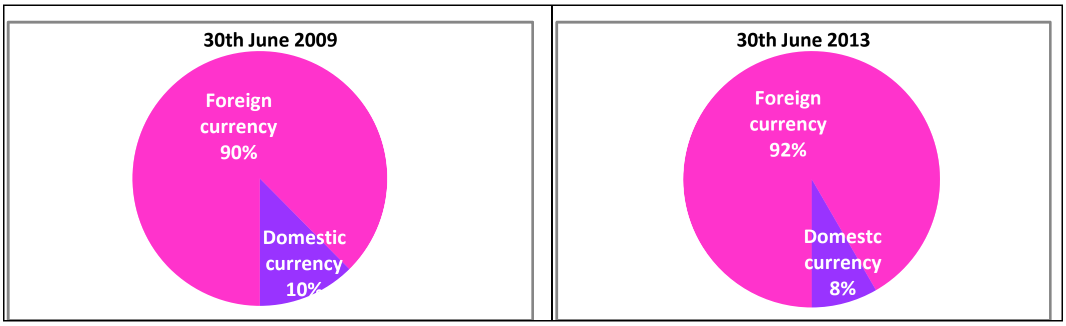


Figure 11: Currency composition

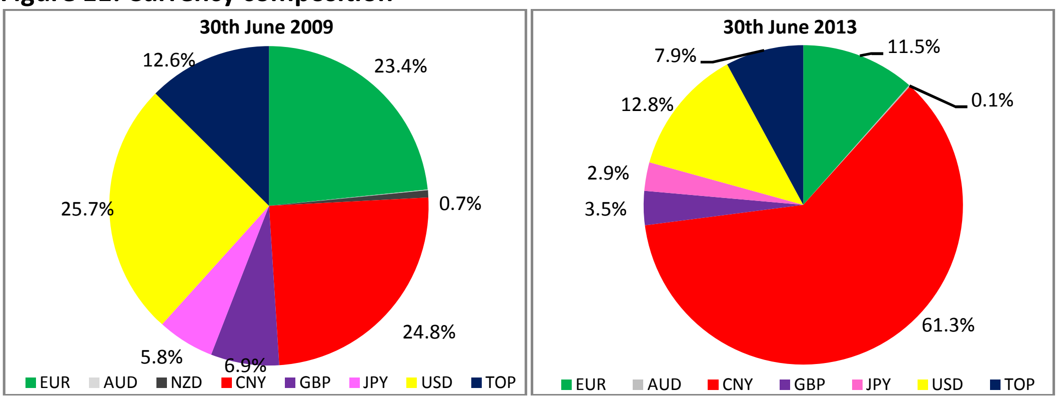


Figure 12: Volatility of Foreign Exchange Rates to Tongan Pa'anga

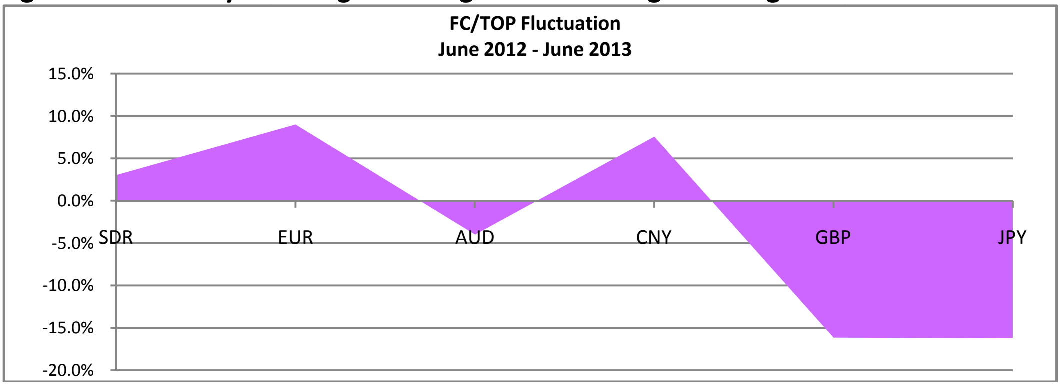
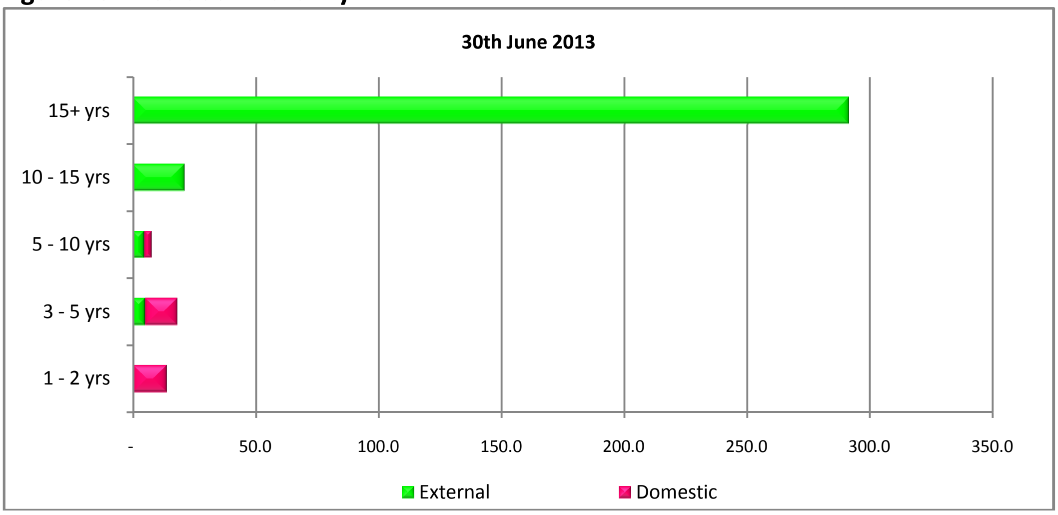


Table 9: Average maturity of the debt (external debt)

Years	Redemption	ATM
1 - 2	0.2	0.0
3 - 5	4.3	0.1
5 - 10	2.9	0.1
10 - 15	150.6	5.5
+15	185.1	8.1
TOTAL	**343.1**	**13.7**

At the end of 2013 the proportion of external debt with maturity of 10 to 15 years was 43.9% of external debt while 53.9% of external debt had more than 15 years maturity with repayments in the distant future. Domestic debt of 42.8% will mature in 1 - 2 years.

Figure 13: Residual Maturity



4.2 Domestic Central Government Debt

As shown in Table 10, GoT's domestic debt stock grew by $7.0m over the review period from $22.5m to $29.5m.

Table 10: Domestic Debt by Instrument and Holder *in TOP$m*

Instrument	FY 2009 $m	FY 2009 %	FY 2013 $m	FY 2013 %	5 yr change
Total Stock of Deposit Debt (A+B)	**22.5**	**100.0**	**29.5**	**100.0**	**7.0**
A. Government Securities	21.5	95.6	29.5	100.0	8.0
Bonds	21.5	95.6	29.5	100.0	7.0
Financial Institutions	5.7	25.3	17.3	58.9	11.6
Retirement Fund Board	2.7	12.0	6.6	22.4	3.9
Other	13.1	58.2	5.6	18.7	-7.5
B. Other Government Debt					
Other	1.0	4.4	-	-	-1.0

4.2.1 Domestic Debt by Instrument

As at FY end 2013, Bonds account for 100% of the securities issued. Bonds are the main type of instrument issued on a 5 yearly duration and issue of 3-6 month Treasury Bills which were settled during FY 2010/11.

4.2.2 Domestic Debt by Holder

GoT financed the deficit during this review period mainly by budget support funding from international donor agencies. Bonds that matured during the fiscal year were rolled over as financing for payments and hence a nil effect. During last 5 years, FI's remain the largest holder of GoT debt, with holdings by non-bank sources decreasing from $16.8m to $12.2m, while those of commercial banks increased from $5.7m to $17.3m.

Table 11: Domestic Debt by Funding Source in TOP$m

Holder	FY 2009 Amount	FY 2009 %	FY 2013 Amount	FY 2013 %	5 yr change
Banks of which:					
Commercial Bank	5.7	25.3	17.3	58.9	11.6
Non Banks of which:					
Other Non Bank Sources	16.8	74.7	12.2	41.1	-4.6
Total	**22.5**	**100.0**	**29.5**	**100.0**	**7.0**

The increase of outstanding bonds during the 5 year period resulted in more holdings by FI, RFB and Individuals, and less holdings by the Companies and Others. FI's continued to hold the majority (59%) of bonds, followed by RFB (23%) and Individuals (15%).

Table 12: Bonds by Holder *in TOP$m*

Holder	FY 2009		FY 2013		5 yr change
	$m	%	$m	%	
Financial Institutions	5.7	26.5	17.3	58.9	11.6
FI Staff Retirement Fund	-	-	0.8	2.7	0.8
Retirement Fund Board	2.7	12.6	6.6	22.6	3.9
Companies	1.0	4.7	0.2	0.8	-0.8
Individuals	2.4	11.2	4.4	15.1	2.0
Other	9.7	45.0	-	-	-9.7
Total	**21.5**	**100.0**	**29.5**	**100.0**	**7.0**

4.2.3 Domestic Debt by Tenor

GoT mainly issues bonds with a maturity of 3, 5 and 6 year and also Treasury Bills on a short-term basis, as required. The majority of outstanding bonds will mature in 3 – 4 years time.

Table 13: Bonds by Tenor *in TOP$m* (remaining maturity)

Security Type Bonds (Years)	FY 2009 Amount	Cum. Amount	Cum. %	FY 2013 Amount	Cum. Amount	Cum. %	5 yr Change
0 - 1 Years	3.1	3.1	14.4	6.0	6.0	20.3	2.9
1 - 2 Years	13.6	16.7	77.7	6.6	12.6	42.7	-7.0
3 – 4 Years	4.8	21.5	100.0	9.4	22.0	74.6	4.6
5 – 6 Years	-	-		7.5	29.5	100.0	
Total	**22.5**			**29.5**			**7.0**

4.2 External Central Government Debt

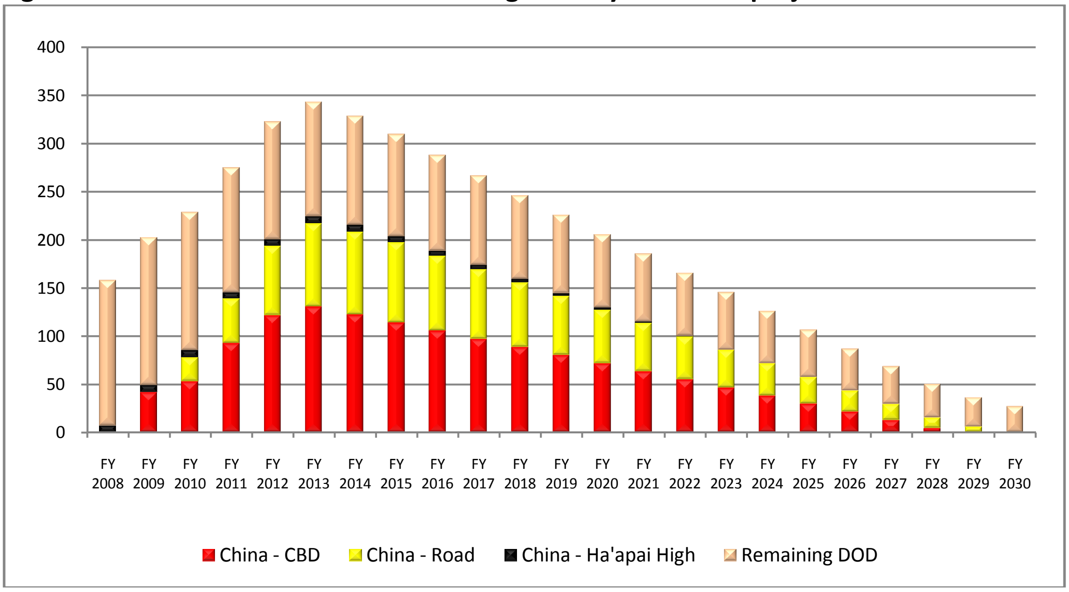
Table 15 shows that the stock of external debt increased from $202.4m (31% of GDP) at June 2009 to $343.2m (41% of GDP) at June 2013.

Worthy of note, is the fact that the debt service to exports ratio also significantly increased in 2009 to 2010 from 20% to 30% and gradually decreasing. This is mainly due to the higher rise of debt service for the loans to PRC compared to lower growth rate in exports in the prior years.

Table 14: Key External Debt Indicators *in TOP$m*

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
External Debt	202.4	228.8	274.9	322.6	343.1	20.5	140.7
Ratio of total external debt to GDP (%)	30.5	32.2	35.1	41.3	41.0	-0.3	10.5
Ratio of total debt service to exports (%)	20.4	30.1	25.1	17.9	13.2	-4.7	-7.2
Ratio of concessional debt to total debt (%)	45.6	42.5	42.8	43.8	43.6	-0.2	-2.0

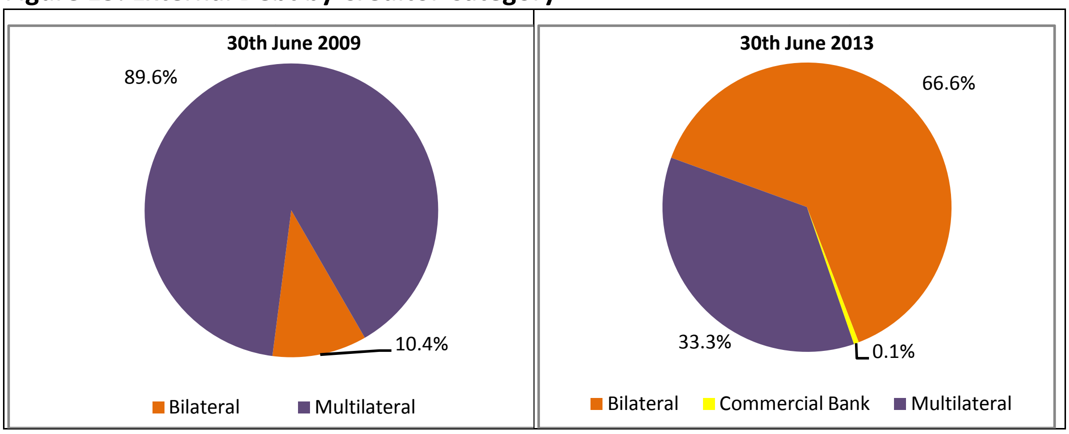
Figure 14: External Disbursed Outstanding Debt by main PRC project



4.3.1 External Debt by Creditor Category

At the end of June 2013, Tonga's external debt stock was dominated by debt owed to the bilateral creditors, accounting for 67% of the total debt stock. However in comparison to the position at the end of 2009, multilateral debt accounted for 90% of the total external debt stock.

Figure 15: External Debt by Creditor Category

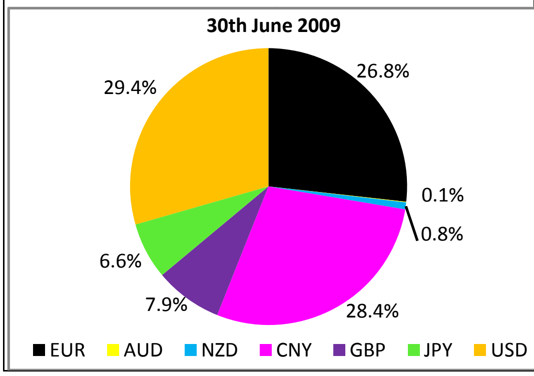


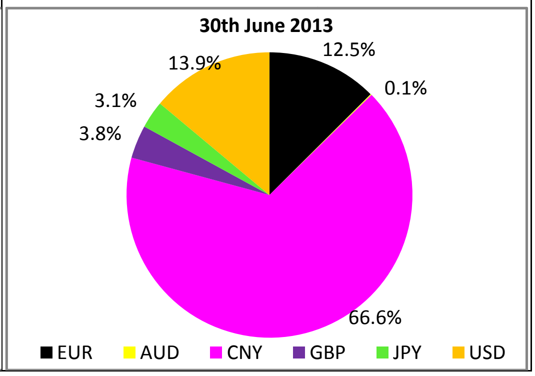
At end 2013, the major creditor was EXIM to whom Tonga's outstanding liability was $221.0m at 64.4% of external debt whilst ADB accounted for $64.3m at 18.7% and IDA of $41.0m at 11.9%.

4.3.2 External Debt by Currency

At the end of 2013, 66.6% of Tonga's external debt was denominated in CNY, SDR at 33.3% and AUD at 0.1%, as shown below.

Figure 16: External Debt by Currency

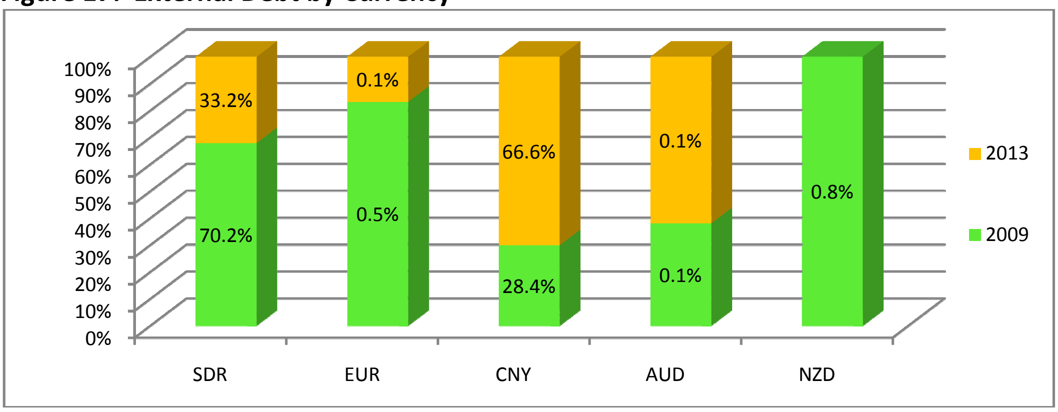




In reference to denomination of Tonga's foreign reserves there is a significant mismatch as the major currency component is the USD Dollar.

During the 5 year period, external debt was denominated in five currencies, mainly due to revaluation of all ADB loans to SDR from USD and new loans in AUD and NZD which was fully settled in September 2012. In particular, there has been a significant change in the CNY composition.

Figure 17: External Debt by Currency



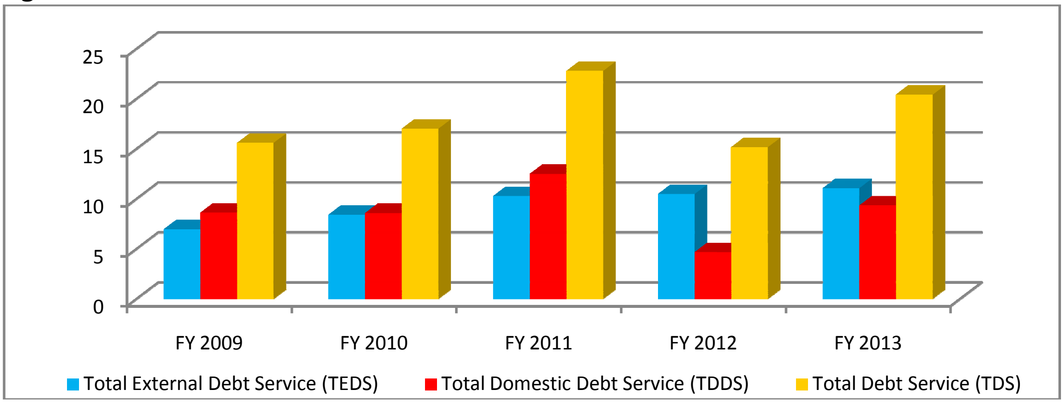
4.4 Total Public Debt Service

The structure of debt service changed over the 5 year period from June 2009 to June 2013. External debt service increased from 49% in 2009 to 54% in 2013, while domestic interest payments decreased from 51% in 2009 to 46% in 2013. Total debt service as a percentage of revenue saw an increase of 3.8 basis points, between 2009 to 2013 due to a decrease in revenue collection.

Table 15: Public Debt Service *in TOP$m*

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
External Principal	4.7	4.6	6.0	5.7	5.8	0.1	1.1
External Interest	3.6	3.8	4.3	4.8	5.3	0.5	1.7
Total External debt service (TEDS)	**8.3**	**8.4**	**10.3**	**10.5**	**11.1**	**0.6**	**2.8**
TEDS as a % of total debt service (TDS)	49.1	49.4	45.2	69.1	54.4	-14.7	5.3
Domestic Principal	7.0	6.9	10.4	3.0	7.5	4.5	0.5
Domestic Interest	1.6	1.7	2.1	1.7	1.8	0.1	0.2
Total Domestic debt service (TDDS)	**8.6**	**8.6**	**12.5**	**4.7**	**9.3**	**4.6**	**0.7**
TDDS as a % of TDS	50.9	50.6	54.8	30.9	45.6	14.7	-5.3
Total debt service	**16.9**	**17.0**	**22.8**	**15.2**	**20.4**	**5.2**	**3.5**
Recurrent Revenue	186.8	159.6	151.0	146.7	159.7	13.0	-27.1
Export Earnings	95.1	83.2	100.2	103.1	154.8	51.7	59.7
Total debt service as % of revenue	9.0	10.7	15.1	10.4	12.8	2.4	3.8
Total external debt service as % of exports	8.7	10.5	10.3	10.2	7.1	-3.1	-1.6

Figure 18: Public Debt Service



4.4.1 External Debt Service by Creditor Category

Total external debt service increased significantly from $8.3m in 2009 to $11.1m in 2013. Principal repayments increased from $4.7m in to $5.8m in 2013 and the interest payments also increased from $3.6m to $5.3m in 2013. In the year ending 2013, a significant proportion of debt service was paid to multilateral creditors at 58% and to bilateral creditors at 52%, of the total debt service.

Table 16: External Debt Service by Creditor Category *in TOP$m*

Creditor Category	Payments	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 yr change	5 yr change
Bilateral	Principal	1.2	1.2	1.3	1.1	1.1	-	-0.1
	Interest	2.5	2.5	3.0	3.5	4.1	0.6	1.6
	Total	**3.7**	**3.7**	**4.2**	**4.6**	**5.2**	**0.6**	**1.5**
Commercial Bank	Principal	0.2	0.3	0.2	0.2	0.03	-0.17	-0.17
	Interest	-	0.0	0.1	0.1	0.02	-0.08	0.02
	Total	**0.2**	**0.3**	**0.3**	**0.3**	**0.05**	**-0.25**	**-0.15**
Multilateral	Principal	3.1	3.1	4.6	4.4	4.6	0.2	1.5
	Interest	1.4	1.4	1.2	1.2	1.2	-	-0.2
	Total	**4.5**	**4.5**	**5.8**	**5.6**	**5.8**	**0.2**	**1.3**
Grand Total	Principal	4.7	4.6	6.0	5.7	5.8	0.1	1.1
	Interest	3.6	3.9	4.3	4.8	5.3	0.5	1.7
	Total	**8.3**	**8.4**	**10.3**	**10.5**	**11.1**	**0.6**	**2.8**

4.4.2 Principal and Interest Payments

As shown in the following Chart, external debt service will double from FY 2013/14 and will remain over the medium term until maturity of loans from PRC (EXIM) for CBD and Roads projects.

Figure 19: External Debt Service by payment type

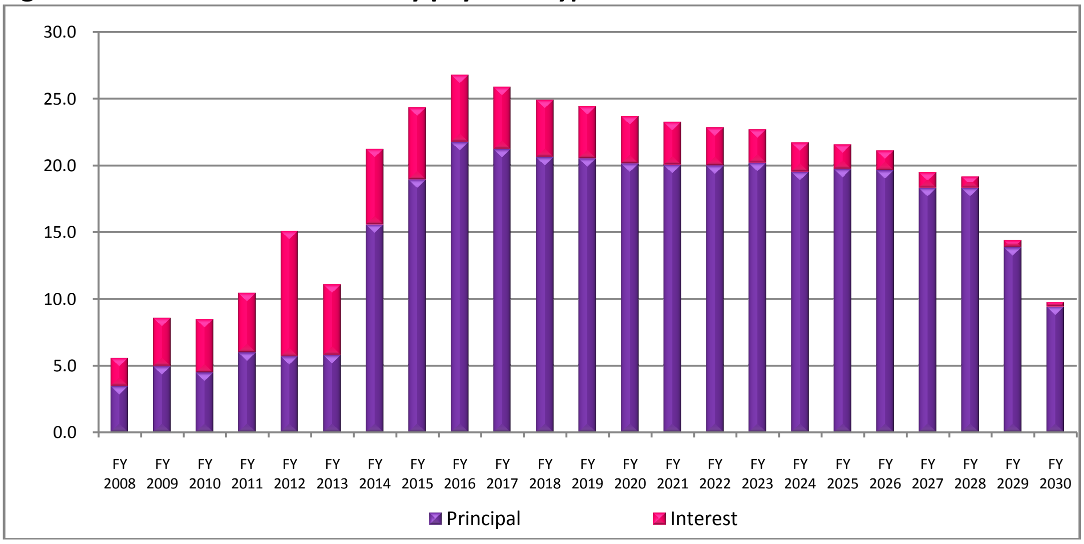
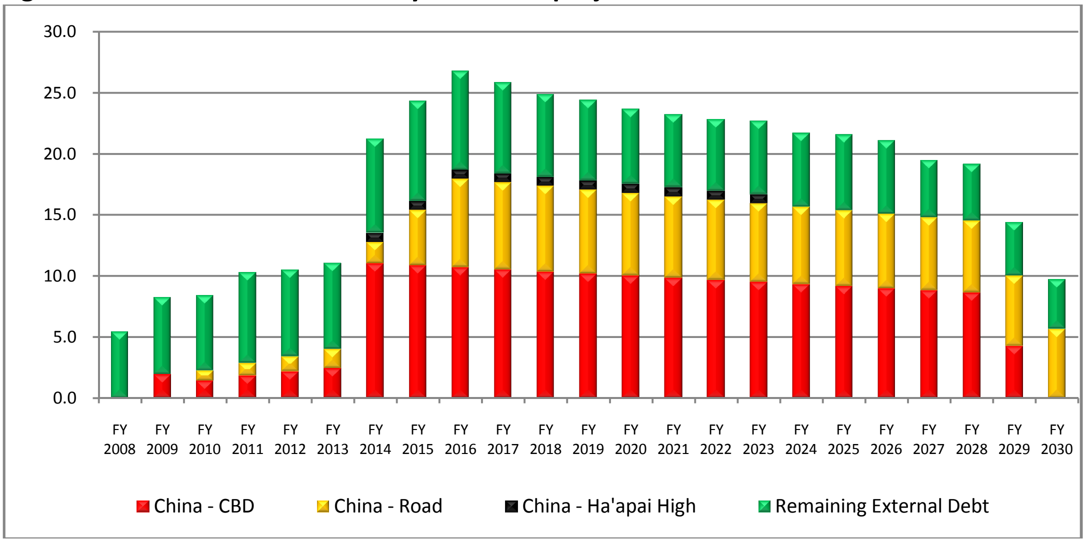


Figure 20: External Debt Service by main PRC project



4.4.3 Debt Service Schedule

The principal repayments for the Nuku'alofa CBD Reconstruction loan will begin in September 2013. The MoFNP in its efforts to minimise risks, and to reduce Tonga's high external debt servicing obligations, has filed requests with the Government of the PRC and the EXIM to convert some of the loans to development grants. These include (i) the Ha'apai High School loan (ii) the "Non on-lent" portion of Nuku'alofa CBD Reconstruction loan and (iii) the balance of the Janfull International Dateline Hotel loan. Alternatively, it has requested the Chinese authorities to consider deferment of the repayment of the principal of the Nuku'alofa CBD Reconstruction Loan for another period of 5 years, that is, to September 2018. Further discussion on decision from the PRC will be made during the GoT delegation to China in July 2013 led by the Prime Minister.

5. Contingent Liabilities

5.1 Loans On-lent

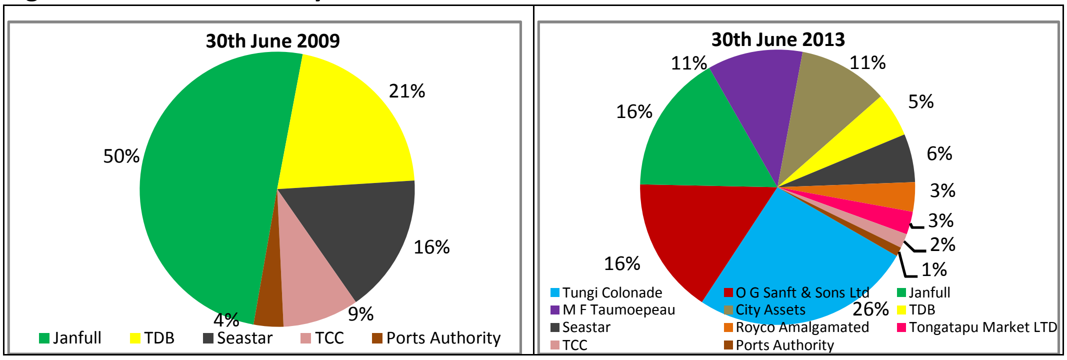
The following Table shows the outstanding balance due to Government from various public and other enterprises, and the repayment received during the reported periods.

Table 17: On-Lent Debt *in TOP$m*

Organisation	Loan Balance		5 yr Change
	FY 2009	FY 2013	
OG Sanft & Sons Ltd	-	10.2	-10.2
Janfull International Dateline Hotel	11.2	11.3	0.1
MF Taumoepeau & Sons Ltd	-	7.2	-7.2
Tonga Development Bank	4.7	2.8	-1.9
Seastar Fishing Co. Ltd.	3.6	3.6	-
Royco Amalgamated Co. Ltd.	-	2.2	2.2
Tongatapu Market Ltd.	-	1.8	1.8
Tonga Communications Corporation	2.0	0.9	-1.1
Ports Authority Tonga	0.8	0.7	-0.1
Tungi Colonnade Ltd.	-	16.6	16.6
City Assets Ltd.	-	6.8	6.8
Total	**22.3**	**64.1**	**41.8**

During the 5 year period, there has been a significant change in the outstanding balance of on-lent loans and the number of Borrowers. The rise is due to the on-lent loans for CBD project from EXIM, since June 2011.

Figure 21: On-lent Debt by Borrower



The total on-lent loan repayment as at 30 June 2013 is estimated at \$0.95m. The payments received were from TDB (59.3%), TCC (29.2%) and Royco Amalgamated Ltd. (11.5%).

5.2 Loan Guarantees

Publicly guaranteed debt includes local and external debt obligations of Tonga's public corporations and development banks, which are guaranteed by the Central Government. In providing these guarantees, the government commits to pay (if called upon to do so) out of public funds, such outstanding balances to satisfy the extent of its guarantee.

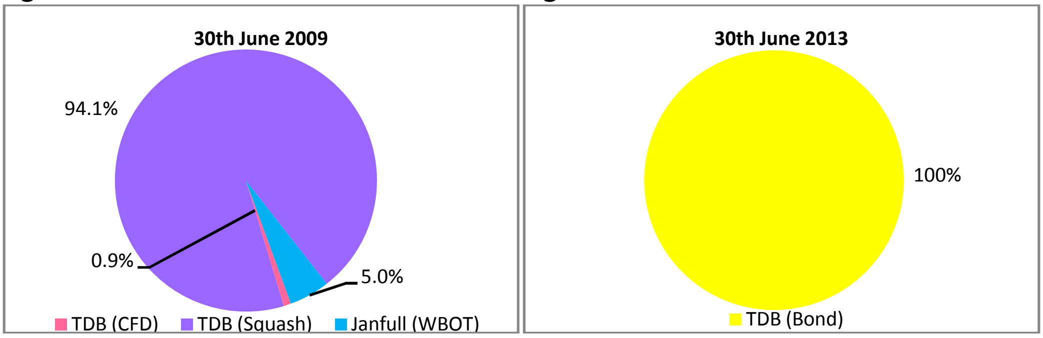
Section 31 of the PFMA 2002, states the conditions for guarantees or indemnities that may be given in a fiscal year.

As shown in the table below, during the year, the outstanding guaranteed debt decreased by \$7.7m to \$0.1m as at June 30, 2013. This position was result of cancellation for guarantee of the loans by Tonga Power Ltd. (TPL) and settlement of the loan guarantee for Janfull Hotel by GoT during the liquidation process. At present, the GoT is not paying on any defaulted guaranteed loans.

Table 18: Publicly Guaranteed Debt *in TOP$m*

Organisation	Year Loan Contracted	Obligation Guaranteed	Creditor Country	Loan Balance		5 yr Change
				FY 2009	FY 2013	
Janfull (WBOT)	2007	Renovation Project	Tonga	0.48	-	-0.48
TDB (Bond)	2011	Bond Issue	Tonga	-	0.15	0.15
TDB (CFD)	1995	Development Project	Tonga	0.08	-	-0.08
TDB (IDH)	2003	Development Project	Tonga	-	-	-
TPL (WBOT)	2010	TPL Term Loan	Tonga	-	-	-
TDB (Squash)	2004	Development Project	Tonga	8.96	-	-8.96
Total				**9.52**	**0.15**	**-9.37**

Figure 22: Guaranteed Disbursed Outstanding Debt



As at 30 June 2013, there were no guaranteed loan payment arrears.

6. Debt Sustainability

6.1 Debt Sustainability Analysis

As advised by the recent IMF-WB DSA Report of 2013, that Tonga's rating has been changed from a high to moderate risk of debt distress based on the joint institutions low-income country (LIC) DSA. This change is mainly due to the improvement of the Country Policy and Institutional Assessment (CPIA) rating from 'Weak' to 'Medium' by the World Bank last year. Although the relevant indicators of external and public debt and debt service show a similar path for debt dynamics as last year's DSA, the upgrade of the CPIA rating for Tonga significantly increases the thresholds of these indicators.

Notwithstanding the upgrade of the DSA rating, risks remain significant, and a cautious approach is recommended towards new non-concessional loans. With the scheduled repayments for CBD and Roads loans from the EXIM, the debt service burden is expected to rise sharply from FY 2013/14 estimated at 1.2% of GDP ($10.2m), substantially draining the GoT's cash balance. The GoT's balance sheet is also exposed to a currency risk, with a huge portion of the outstanding external debt denominated in CNY. A declining path of external public debt is critically dependent on steadfast implementation of medium-term fiscal consolidation and for advancement of the economy, as outlined in the TSDF.

Over the last 5 years (FY 2008/09-2012/13), the Charts below shows the debt sustainability position of the GoT's debt portfolio (excludes fluctuations). Since FY 2007/08 when disbursements began for the EXIM loans, there has been a significant rise in the NPV of External Debt ratio where the threshold was breached in the last five years. The TDS ratios have shown a fluctuating trend but have remained well below the thresholds.

Figure 23:NPV of External Debt as % of GDP

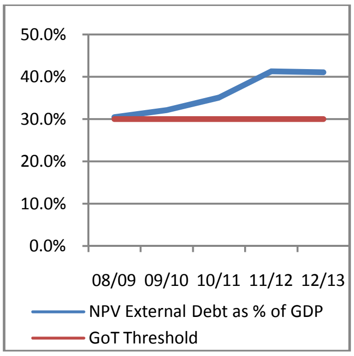


Figure 24:NPV of External Debt as % of Exp & Remittances

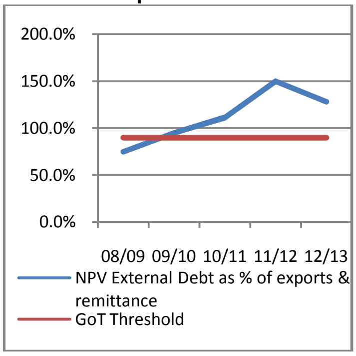


Figure 25:NPV of External Debt as % of Revenue

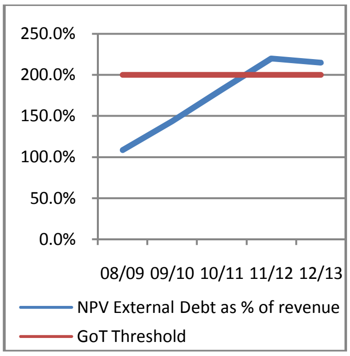


Figure 26:TDS as % of Exports & Remittances

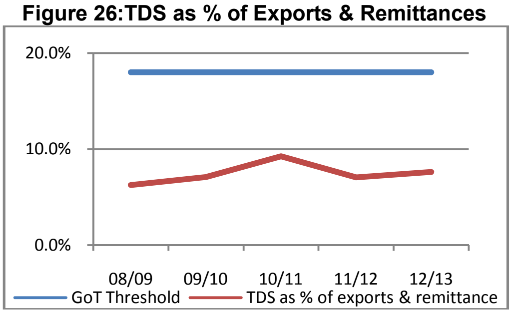
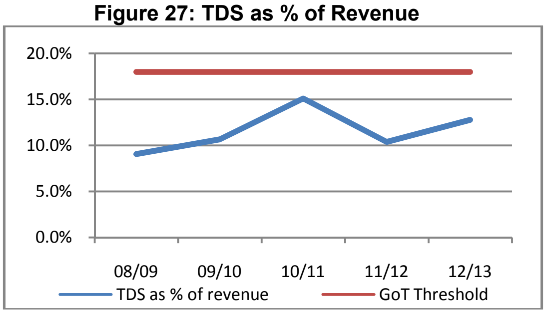


Figure 27: TDS as % of Revenue



Looking forward over the next 3 years, the debt sustainability position will change as result of the revised thresholds and assuming no new borrowing, that most of the indicators will not be breached (includes fluctuations[3]). However, cautious monitoring by MoFNP of GoT's debt sustainability level is required and especially on any ease for future external borrowing and to coincide with improvement in our current level of economic activity and prudent public debt management, in order to mitigate the vulnerability to shocks.

Table 19: GoT Debt Sustainability Position, FY 2013/14-2015/16

Particulars	IMF-GoT threshold	13/14	14/15	15/16
NPV External debt as:				
% of GDP	40	40.8	36.2	27.9
% of revenue	250	213.8	191.7	171.9
% of exports (& remittances)	150	132.0	120.8	108.8
Debt Service as:				
% of revenue	20	18.4	19.8	20.5
% of exports (& remittances)	20	11.4	12.5	13.0

[3] Nominal GDP, Exports & Remittances decrease by 2%, Revenue decrease by 1%,& FC rates increase by 5%

7. Conclusion and Way Forward

As at 30 June 2013, Government's **external debt** in nominal value is estimated at ***41% of GDP***, which **exceeds** the **IMF target** of **30%** and at the **Government target** of **40%.** With the projected position including future disbursements on both the Reconstruction and Roads projects, most of these ratios are expected to further exceed the recommended thresholds going forward *(as shown in the NPV graphs above)*.

The current Government external debt sustainability position remains vulnerable and concerted efforts need to be explored in the short to medium term in order to minimise the risks as going forward.

Further to Cabinet approval in February 2013 for the MoFNP to formalise the MTDS by June 2013 and to continue exploring practical options for mitigating of risks to GoT's external portfolio.

Ongoing efforts have been made by the MoFNP which includes strict adherence to the 'no new borrowing' policy in the medium term even with the revised debt sustainability thresholds, to follow up debt relief requests made to People's Republic of China, in-country missions by the Commonwealth Secretariat and World Bank on development of debt management, discussion with Westpac, ANZ and the National Reserve Bank of Tonga on options for hedging of GoT's external debt service.

A MTDS for 2013/14-2015/16 has been completed in June 2013 and to be endorsed by Cabinet as guidance to GoT for implementation during the next three years.

In view of the GoT's debt management objectives, the main principles that have applied in the MTDS are to:

- Maintain the 'no new borrowing' policy in place since June 2011 and for easing later when the external debt position is sustainable also to ensure that the debt level is maintained within the recommended targets;
- Reduce the external debt outstanding to the People's Republic of China (PRC) and the foreign exchange risk associated with the CNY also the high portion of external debt from the ADB and IDA denominated in SDR;
- Have a more balanced composition between external and domestic debt including development of the Government Securities Market.

Six strategies have been identified as practical for GoT to implement, as below:

1. To request for debt to development swap of a portion of external debt from PRC;
2. To reschedule the main loans from EXIM Bank China;
3. To refinance external debt portion from PRC with domestic debt;
4. To convert all external debt denominated in CNY and SDR to USD;
5. To lengthen bond maturity from 6 years up to 10 years;
6. To refinance external debt portion from PRC with concessional loans from ADB and IDA (under the revised 50:50 loan and grant financing).

Given that some of these strategies are beyond the direct control of DMS, that the MoFNP will be work in close liaison with the NRBT including TA from ComSec and WB as per recommendations of Missions during 2012 and for bilateral discussions with the GoT's main external creditors of EXIM and the ADB on scope for the related proposals.

Details of these strategies can be referred in the MTDS document which will be available on the MoFNP's website once it is approved by Cabinet.

8. Recommendations

Table 1. Summary of ComSec Mission recommendations specific to certain segments of the GSM

MONEY MARKET DEVELOPMENT			
The liquidity in the banking system to be kept on balance over a period of time.	MoFNP and NRBT	MT[4]	L
Recent amendment to NRBT ACT 2007 to be reviewed to enable NRBT to conduct open market operations using outright transactions as well repos transactions in Government securities	MoFNP and NRBT	ST	H
Central Bank and market repo to be introduced	NRBT	MT	H
Short term Treasury Bills to be used for funding temporary cash mismatches of Government in place of overdraft facility from a commercial bank at the commercial rate of interest.	MoFNP and NRBT	MT	M
NRBT to compile and disseminate money market transactions to market at a regular interval.	NRBT	LT	L
PRIMARY MARKET			
Adopt issuance policy based on Commercial Paper (CP) type issuances	MoFNP and NRBT	ST	H
Consult market actively before announcement of tenor, target issuance amounts and pricing.	MoFNP and NRBT	ST	H
Place a limit for issuance for each maturity year to contain refinancing risk	MoFNP	MT	M
Adopt and publish guidelines for issuance of Treasury Bills and Bonds	MoFNP and NRBT	MT	M
Shift to auction process at later stage	MoFNP	LT	M
Improve effectiveness of Cash Management by improving forecasting of cash balance, establishing a link between forecasted cash position and primary issuance and adoption of a comprehensive Treasury Single Account	MoFNP	ST	M
INVESTORS BASE AND SECONDARY MARKET			
Initiate an investor education program	MoFNP	MT	M
Undertake feasibility study for undertaking issuance of 'diaspora bonds' on a regular basis	MoFNP and NRBT	MT	M
Reinstate the authority to the NRBT to acquire and own Government securities	MoFNP and NRBT	ST	H
Set up legal framework for Insurance business	MoFNP	MT	H
MARKET INFRASTRUCTURE			
Introduce system of dematerialisation of securities and phase out physical form of holding securities.	NRBT and MoFNP	ST	H
Introduce a DvP based settlement of securities using DvP I mode	NRBT	MT	H
Facilitate introduction of a simple system for execution of sale and purchase of securities by buyers and sellers	NRBT	MT	H

[4] MT: Medium-Term, ST: Short-Term, L: Low, M: Medium, H: High

Table 2: Summary of WB Mission recommendations

Issues/ Project Components	Actions/Lead entity	Timing	Budget (external assistance)	Expected Output and/or Outcomes of the Actions
Developing Debt Management Strategy				
The current draft of a debt management strategy misses key components and its analytical foundation is rather weak. The focus has been on DSA and not on debt management issues. The current document does not explicitly endorses a preferred strategy	Revise the current draft of the debt management strategy to include: 1. Objectives and scope 2. Macro framework 3. Cost-risk characteristics of public debt portfolio 4. Sources of financing and analysis of alternative strategies 5. Strategy for domestic market development	**Priority Level: I** Start in 1Q 2013, duration 6 months	Internal	A debt management strategy document closer in line with best practice Formal and public debt management document Better coordination with NRBT
Strengthening Risk Management Framework				
On ***external borrowing***, there has been a concentration of borrowing from few external creditors and DMS has not been involved in any loan negotiation. There is no formal policies and procedures for external borrowing; therefore, it has allowed different institutions to be involved in loan negotiations	1. Develop a procedures manual for staff and institutions, including legal advisors, for loan contracting; include the whole public investment program into the medium-term budget to define the total financing needs, and develop the corresponding borrowing plan; 2. Analyze and evaluate existing and potential sources of financing to choose the most beneficial terms and conditions for the government in line with the objectives established in the medium-term debt strategy	**Priority level: II** Start 2Q 2013, duration 4 months	**Internal**	Procedures manual for loan contracting will be in effect. Public Investment Program will be integrated into the medium-term budget with more clear estimates for funding needs and more realistic projections for the borrowing plan. Analysis of potential sources of funding as well their most beneficial terms will be carried out leading to improved debt management
On guarantees, on-lending, and derivatives, there are no policies and operational guidelines regulating the government's approval and issuance of on-lending and guarantees. There is a need to develop risk assessment and well as creating institutional framework to collect "treasury receivables". The PPPs projects have already started but there is no institutional framework and capacity at the MoFNP to manage them.	1. Finalize the "Policy Framework for Government Guarantees" and review the Public Finance Management Act (2002), to see from the legal viewpoint if additional changes are necessary; 2. Develop capacity within the MoFNP to carry out financial and capacity-to repay-analysis; 3. Build a simple "decision to issue guarantees/on-lending" matrix and develop capacity at DMS to collect treasury receivables; 4. Develop an institutional framework to evaluate, analyze, and report on PPPs	**Priority level: I** **Start 1Q 2013, duration 12 months**	**Internal US$40,000**	A government framework document to provide guarantee and on-lending will be approved and in place. Procedures to issue guarantees and on-lending will be in effect together with improved analytical capacity in the decision process. The MoFNP, through the DMS will start monitoring and collecting "treasury receivables". An institutional framework (units in charge, procedures, criteria, etc.) to evaluate, analyze and report on government involvement in PPPs will be in effect.

Table 2 Con't: Summary of WB Mission recommendations

Issues/ Project Components	Actions/Lead entity	Timing	Budget (external assistance)	Expected Output and/or Outcomes of the Actions
On operational risk management; tasks and functions in the middle office (analytical and a framework for risk analysis) are not currently guided by a set of procedures and loans' documents should be better protected against fire and natural disasters. Preparing a business continuity plan will help to reduce operational risk management.	1. Formalize debt service payment procedures; 2. Design and approve middle office procedures; 3. Design and approve a business continuity plan.	**Priority Level: II** **Start 2Q** 2013, duration 8 months	**Internal**	Formal debt service procedures will be in place. Middle office functions will be guided by clear procedures. Business continuity plan will in effect together with a detailed plan for identifying/ managing operational risk Reduced operational risk
Improving Coordination with Macroeconomic Policies				
1. Undertake sensitivity analysis of the projections to changes in macroeconomic and financial market projections; 2. Make better use of existing committees (e.g., those involving technical staff from the Budget, Macro, Policy and Planning, and the NRBT) to jointly carryout the DSA and discuss the results and implications for their respective policy operations; 3. Develop capacity (training) to generate medium term forecasts within the MoFNP and, within DMS, to undertake scenario analysis to provide debt and debt service projections under alternative macroeconomic scenarios	**Priority Level: III** Start 3Q 2013, duration 8 months	Internal US$40,000	Improved budgeting and more information about risks to the budget forecast leading to more certainty about potential budget impacts from the debt	
1. Prepare a MoU between the MoFNP and the NRBT; 2. Revamp The Cash Flow Committee and Debt Management Committee, by updating the ToRs. 3. Establish in the legislation explicit legal limits on the government borrowing from the NRBT	**Start 2Q 2013, duration 12 months Action No. 3, start3Q2013, needs new law (preparation, discussion, approval), 18 months.**	Internal	A formal agreement (Memorandum of Understanding) between the MoFNP and NRBT will be in place. Responsibilities will be clear and accountable. Coordination to implement debt management and monetary policies will be improved	

Table 2 Con't: Summary of WB Mission recommendations

Issues/ Project Components	**Actions/Lead entity**	**Timing**	**Budget (external assistance)**	**Expected Output and/or Outcomes of the Actions**
1. Establish a working group led by MoFNP and including the DMS, NRBT, and market participants with a focus on improving the primary market for government securities and identifying constraints to market development; 2. Request technical assistance and capacity building programs on domestic market development for government securities;	**Start 1Q 2013, duration 36 months**	Internal US$50,000	Constraints to market development will be identified and well as measures to ameliorate them. A program to foster domestic market development will be prepared Coordination between MoFNP and NRBT will be improved	

9. Statistical Annex

Table 1: Summary Debt Tables

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 YR Change %	5 YR Change %
Total Public Debt (USDm)	**111.7**	**132.3**	**180.0**	**200.8**	**204.4**	**1.8%**	**83.0%**
Total Public Debt (TOPm)	224.9	258.3	304.4	352.1	372.6	5.8%	65.7%
External Debt	202.4	228.8	274.9	322.6	343.1	6.4%	69.5%
Domestic Debt	22.5	29.5	29.5	29.5	29.5	-	31.1%
Total Public Debt to GDP (%)	**33.9%**	**36.3%**	**38.9%**	**45.1%**	**44.6%**	**-1.1%**	**31.6%**
External Debt to GDP	30.5%	32.2%	35.1%	41.3%	41.0%	-0.7%	34.4%
Domestic Debt to GDP	2.9%	3.8%	3.8%	3.8%	3.6%	-5.3%	24.1%
Total Debt Service (TOPm)	**16.9**	**17.0**	**22.8**	**15.2**	**20.4**	**34.2%**	**20.7%**
Principal	11.7	11.5	16.4	8.7	13.3	52.9%	13.7%
Interest	5.2	5.6	6.5	6.5	7.1	9.2%	36.5%
External	8.3	8.4	10.3	10.5	11.1	5.7%	33.7%
External Debt by Creditor category (TOPm)	**202.4**	**228.8**	**274.9**	**322.6**	**343.1**	**6.4%**	**69.5%**
Multilateral	144.4	134.7	122	115.5	114.3	-1.0%	-20.8%
Bilateral	58.0	92.5	150.9	205.3	228.4	11.3%	293.8%
Commercial	-	1.6	2.0	1.8	0.4	-77.8%	100.0%
Debt Composition by Instrument Type (TOPm)	**224.9**	**258.3**	**304.4**	**352.1**	**372.6**	**5.8%**	**65.7%**
Loans	202.4	228.8	274.9	322.6	343.1	6.4%	69.5%
Bonds	22.5	29.5	29.5	29.5	29.5	-	31.1%
Foreign Currency Risk (%)							
% of debt in Chinese Yuan	28.7%	40.4%	54.9%	63.6%	66.6%	4.7%	132.1%
% of debt in SDR	70.9%	58.5%	44.2%	35.7%	33.5%	-6.2%	-52.8%
% of debt in other currencies	0.5%	1.0%	0.9%	0.7%	0.6%	-14.3%	20.0%
Interest Rate Risk (%)							
% of debt at floating rate	0.0%	0.7%	0.7%	0.6%	0.1%	-83.3%	100.0%
% of debt at fixed rate	100.0%	99.3%	99.3%	99.4%	99.9%	0.5%	-0.1%
Roll-over Risk (Yrs)							
Average term to maturity - domestic (years)	5.0	4.6	4.6	4.7	4.7	-	-6.0%
Average term to maturity - external (years)	36.2	35.6	34.8	34.8	34.8	-	-3.9%
Fiscal Indicators (%)							
Total Debt Service to Expenditure	8.1%	9.7%	12.8%	9.2%	11.4%	23.9%	40.7%
Total Debt Service to Revenue	9.0%	10.7%	15.1%	10.4%	12.8%	23.1%	42.2%
Interest cost to Expenditure	2.5%	3.2%	3.7%	3.9%	4.0%	2.6%	60.0%
Vulnerability Indicators (%)							
Reserves to External Debt	67.3%	74.5%	74.1%	76.3%	75.3%	-1.3%	11.9%
External Debt Service to Exports & Remittances	3.1%	3.5%	4.2%	4.9%	4.1%	-16.3%	32.3%

Main Economic Variables (TOPm)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	1 YR Change %	5 YR Change %
Gross Domestic Product	664.3	711.4	783.4	781.5	836.1	7.0%	25.9%
Exports of Goods & Services	95.1	83.2	100.2	103.1	154.8	50.1%	62.8%
Remittances	175.2	157.4	146.5	112.3	113.3	-35.3%	-35.3%
Expenditure	207.8	175.8	177.5	165.2	178.3	7.9%	-14.2%
Revenue	186.8	159.6	151.0	146.7	159.7	8.9%	-14.5%
Foreign Reserve	136.3	170.5	203.8	246.1	258.4	5.0%	89.6%
Exchange Rate USD/TOP	2.0134	1.9518	1.6914	1.7535	1.8232	4.0%	-9.4%

Sources: MoFNP, NRBT and IMF Staff Report for 2013 Article IV Consultation

Table 2: Total Public Disbursed Outstanding Debt (TOPm), FY 2007/08 – 2029/30

	China CBD	China Roads	China Ha'apai High	Remaining External Debt	Domestic Debt	Total
FY 2008	-	-	6.7	151.2	22.5	180.4
FY 2009	41.5	-	7.3	153.5	29.5	224.9
FY 2010	52.7	25.0	7.1	144.0	29.5	258.3
FY 2011	92.5	46.0	6.5	129.9	29.5	304.4
FY 2012	121.3	72.0	6.8	122.5	29.5	352.1
FY 2013	130.5	86.3	7.4	119.0	29.5	372.6
FY 2014	122.0	86.3	6.7	113.6	29.5	357.1
FY 2015	113.6	83.5	5.9	106.7	29.5	338.4
FY 2016	105.2	77.9	5.2	99.7	29.5	316.9
FY 2017	96.8	72.4	4.4	93.2	29.5	295.9
FY 2018	88.4	66.8	3.7	87.3	29.5	275.5
FY 2019	80.0	61.2	3.0	81.6	29.5	255.2
FY 2020	71.5	55.7	2.2	76.2	29.5	235.1
FY 2021	63.1	50.1	1.5	70.9	29.5	215.1
FY 2022	54.7	44.5	0.7	65.7	29.5	195.2
FY 2023	46.3	39.0	-	60.2	29.5	175.0
FY 2024	37.9	33.4	-	54.7	29.5	155.5
FY 2025	29.5	27.8	-	49.0	29.5	135.8
FY 2026	21.0	22.3	-	43.4	29.5	116.2
FY 2027	12.6	16.7	-	39.1	29.5	97.9
FY 2028	4.2	11.1	-	34.8	29.5	79.6
FY 2029	-	5.6	-	30.7	29.5	65.8
FY 2030	-	-	-	26.9	29.5	56.4

Source: MoFNP

Table 3: Total Public Debt Service (TOPm), FY 2007/08 – FY 2029/30

	China CBD	China Roads	China Ha'apai High	Remaining External	Domestic Debt Service	Total
FY 2008	-	-	-	5.4	8.1	13.5
FY 2009	1.9	-	-	6.4	8.6	16.9
FY 2010	1.4	0.9	-	6.2	8.6	17.1
FY 2011	1.8	1.0	-	7.4	12.5	22.7
FY 2012	2.2	1.2	-	7.1	4.7	15.2
FY 2013	2.4	1.6	-	7.0	9.3	20.3
FY 2014	11.0	1.7	0.7	7.7	7.4	28.5
FY 2015	10.8	4.5	0.7	8.2	8.0	32.0
FY 2016	10.7	7.2	0.7	8.1	7.8	34.4
FY 2017	10.5	7.1	0.7	7.5	4.4	30.0
FY 2018	10.3	7.0	0.7	6.8	6.4	31.0
FY 2019	10.2	6.9	0.7	6.6	3.9	28.1
FY 2020	10.0	6.8	0.7	6.1	7.4	31.2
FY 2021	9.8	6.7	0.7	6.0	8.0	31.3
FY 2022	9.7	6.6	0.7	5.9	7.8	30.7
FY 2023	9.5	6.4	0.7	6.0	4.4	27.0
FY 2024	9.3	6.3	-	6.0	6.4	27.9
FY 2025	9.1	6.2	-	6.2	3.9	25.5
FY 2026	9.0	6.1	-	6.0	7.4	27.6
FY 2027	8.8	6.0	-	4.7	8.0	26.6
FY 2028	8.6	5.9	-	4.6	7.8	25.9
FY 2029	4.3	5.8	-		4.4	18.1
FY 2030	-	5.6	-		6.4	16.2

Source: MoFNP