



GOVERNMENT OF TONGA

BUDGET STATEMENT 2014/2015

“Partnership” :
Government and People
together building the
economy and society

Ministry of Finance and National Planning

Nuku'alofa, May, 2014



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1 FOREWORD

This Budget, like all work of Government, is founded on our national motto: **“God and Tonga are my inheritance”**. This is supported by the Government’s theme **“The Partnership – Government and People Together Building the Economy and Society”**. The Budget theme builds on this: **“Improved Government Delivery and Accountability for better Results for the people of Tonga through Partnership”**.

This is the fourth and last budget of the current administration. It builds on the earlier budgets and initiatives that government has been pursuing for nearly four years as guided by the Tonga Strategic Development Framework (TSDf). These budgets have helped to maintain fiscal stability while driving improvements in government performance.

This budget will only serve the current administration for less than six months. Government wishes to hand over a strong, forward looking and responsible budget to the next administration which leaves sufficient space for the new administration to carry on for the remaining half of the financial year so that conditions can continue to improve for our people.

The budget focuses its priorities on maintaining and strengthening Government’s reform commitments. Core to our future success is improving sustainable growth to improve employment and income for our people and so that government revenues can be improved to help finance the level and quality of public services expected following our recent political reforms.

We know that we have a small and dispersed economy. While competition helps to improve quality and lower prices for consumers, this must take place within an overall commitment from the various economic agents to work in partnership. We are committed to further strengthening the private public sector partnership through initiatives such as the Sector Growth Committees. We are directing large parts of our capital funding – provided by the partnership with our development partners – to improve key infrastructure including energy, transport and communications. We are seeking to further improve the business enabling environment so that necessary government regulations and revenue collection are more efficient and effective and provide only the minimum necessary burden on business. The earlier initiative of providing soft loans and some grants to key economic sectors will be expanded to provide a significant increase in soft loan to business. This will be managed for Government by Tonga Development Bank, who has the required skills for such a large expansion in lending. We will continue to support the capacity of our people to take on higher levels jobs provided by the overseas worker schemes in our overseas partner countries.

We know that growth, as measured by GDP, is only an approximate indicator of improvements in the wellbeing of our people. We seek to avoid conditions where the more vulnerable and less endowed groups in our society are left behind. Government cannot afford the welfare systems of our large neighbors; even they are finding the costs to be a burden and that if not designed with care they can undermine commitment to hard work and economic growth. But Government does wish to ensure a well designed, caring and responsible support to those in need. Government is expanding support to the elderly lowering the starting point for aged welfare payments from 75 years to 70 years. With the support of a number of our development partners, new policies are being designed and piloted, working in close partnership with communities and non-government organizations that focus on the needs of the most vulnerable groups. These include babies born into poor families and people with serious disabilities (both mental and physical) which limit their capacity to be active members of society.

The delivering of these growth and social support initiatives also require an efficient, effective and affordable public service able to deliver what it is responsible for working in close partnerships with organization across Tonga and beyond. This budget continues support for key reform initiatives to help ministries to improve their management and delivery. These include improving accountability and transparency, such as conversion of the Commissioner for Public Relations Office to cover the functions of Ombudsman and Anti-Corruption. Other reforms underway including public financial management reform, improved corporate plans linked to ministry budgets, strengthen staff performance management system with job descriptions aligned to ministry outputs, and improve the monitoring and evaluation of our progress at all levels. Sound and good governance are essential for building public confidence in government and creating the trust needed for building good partnerships.

Despite our limited financial circumstances and other constraints, this budget focuses on improving performance, growth, and wellbeing, while ensuring sound fiscal conditions; these conditions are in turn an essential requirement for our policies and priorities to be successful. The opportunities for new prudent borrowing, resulting from progress in lowering our level of debt distress, are being taken with care. They focus on saving costs, driving growth, and addressing the urgent need to help our people in Ha'apai whose islands were devastated by cyclone Ian. This highlights the cross-cutting commitment of Government to address improved disaster management and the longer term threats from climate change and environmental degradation. The combining of these functions into a new Ministry will help to improve focus.

The Budget also lays the foundations for the important traditional events associated with the Coronation of our King due early in the 2015/16 fiscal year. As the last Kingdom in the Pacific, this event celebrates and reconfirms our unique position among the countries of the Pacific; it reconfirms our ties and links as a people. Another important event, due in 2019, is the Pacific Games. The budget provides funding for the Pacific Games Committee to effectively plan and seek funding for this important event so that we can effectively showcase our Kingdom in recognition of sports as of a priority area for development.

We face many challenges and some opportunities resulting from increased globalization and climate change. To respond effectively to the challenges and make the most of the opportunities we must also be willing to change. But we must strive to change for the better, not let ourselves be marginalized in a rapidly changing world. We must learn to keep what is good and effective from our past, while being willing to change those things that hold us back and limit us from improving our performance. This is true whether we work in the government service or private sector. We must hold on to our inheritance while we learn to apply it in new and innovative ways. We want to continue to be Tongans, but Tongans who can thrive in the 21st Century. The upcoming elections, which are also funded in this budget, are an important symbol of our political reform and maturing as a people.

I wish to extend a special thanks to all of our development partners for their ongoing support to Tonga. This goes beyond just development assistance, it includes provision of ideas, advice and moral support. It is the foundation of sound partnership as set out in our collective commitments to improved development effectiveness. I also wish to thank our people, in their many roles as workers, business people, consumers, members of churches and community groups, across the Kingdom and beyond our shores, and call on them to continue to work in partnership with Government as we drive for sustainable growth, with a caring and responsible society.

My last, but not least, thanks go to the members of the Legislative Assembly for the detailed work that is needed to review this Budget Estimates and Statement, along with the Ministry Corporate Plans. Their commitment to reviewing this work, and helping to ensure that it truly address the aspirations for our people, is part of the partnership that grows from our new and more open political system.

May we all continue to work in responsible partnership, respecting each other, while being willing to challenge and fine tune our efforts. It is only through honest and open debate, delivered with sensitivity and respect, that we can drive the improvements in performance that our people expect and deserve. Let us work together to show that we truly build on "God and Tonga are my inheritance".

God Bless Tonga

Faka'apa'apa atu



'Aisake Valu Eke
Minister for Finance and National Planning

2 INTRODUCTION

Improving the way government operates is key to a more efficient, effective and affordable public service needed to deliver government policies and services while ensuring fiscal stability. Major reforms are under way. These relate to economic and social policy analysis, national and corporate planning and budgeting, staff performance and management, improved governance and transparency as well as other technical areas. The Budget Statement is a key component of this reform process. Government continues to improve it and make it more results focused along with the results based approach, being integrated into the planning, budget and project processes.

Under this approach, the budget **funds** the **inputs** and **activities** that produce the corporate plan **outputs**¹ that government delivers, which, along with the efforts of everyone else in Tonga and beyond, help us to achieve the **outcomes** we desire. Following this results-based approach is demanding, but it will help us to better manage our limited resources and deliver the mandate given by the electorate.

This is the fourth and last Budget Statement of the current Government. It starts with a Foreword from the Minister setting out the areas of importance covered by this budget. The introduction follows in Section 2, setting out the structure of the Statement.

A revised diagram of the Vision and Objectives of the Tonga Strategic Development Framework is provided in Section 3, as a reminder of the guiding role provided by this document and the link to the Kingdom's founding motto. Section 4, then summaries the priority areas for this budget and provides the Budget Estimates at a Glance.

The background conditions and challenges in the economic, social sectors and communities, under which the budget was designed, are summarized in Section 5 (with supporting details in Annex I). These identify progress with the **outcomes** that are supported by the **outputs** of government and others. Based on these conditions, Section 6.1 sets out the key **outputs/activities** that government intends to pursue in the budget, grouped by the budget priority areas. These will support improved services to further drive progress towards the Outcomes in the TSDF, and our national Vision for improved wellbeing for the people of Tonga.

Section 6.2, supported by the details in Annex II, forecasts the domestic revenue and external development assistance that can reasonably be expected. Taking into account these estimated sources of funding, and the need for prudent fiscal management and limited borrowing, the Statement outlines the allocation of funding to ministries for their **outputs** to support the policies and initiatives that government intends to pursue from Section 6.1.

After the two annexes, which support Sections 5.0 and 6.2, detailed tables are provided in the annexes for those readers interested in delving more deeply into the numbers behind the analysis.

¹ Outputs are within our capacity to deliver and support our desired outcomes which lie beyond our capacity to directly deliver.

3 TONGA STRATEGIC DEVELOPMENT FRAMEWORK



Government of Tonga

KINGDOM OF TONGA MOTTO: “God and Tonga are my Inheritance”

A profound statement by King George Tupou 1 that sealed the True foundation of identity and heritage for his people, by proclaiming boldly God, as the Salvation, and Source of protector and provider of the Kingdom of Tonga

THE NATIONAL DEVELOPMENT VISION 2010-2014

“To develop and promote a just, equitable and progressive society in which the people of Tonga enjoy good health, peace, harmony, and prosperity, in meeting their aspirations in life”.

Achieve
through

Outcome Objectives

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Strong inclusive communities	Dynamic public and private sector partnership	Appropriate well planned and maintained infrastructure	Sound education standards	Appropriately skilled workforce	Improved health of the people	Cultural awareness, environmental sustainability	Better governance	Safe, secure and stable society

support

Enabling Themes

- A.** Continuing progress to a more efficient and effective government by focusing on its core functions; improving coordination, service delivery and optimizing use of resources
- B.** Improving the macro-economic environment and fiscal management, including effective revenue services to ensure a level playing field and that service to the people can be appropriately funded
- C.** Ensuring Public Enterprises are sustainable and accountable, and where appropriate moved into the private sector
- D.** Ensuring a more coordinated whole of government approach in our partnership with development partners

4 BUDGET ESTIMATES AT A GLANCE

The Tonga Strategic Development Framework (TSDF) remains the guiding document, while recognizing that it will be reviewed and updated during the 2014/15 Budget year for the new administration.

Drawing on the TSDF, the **Budget 2014/2015** is focused on the following four key areas:

1. **Supporting growth** through focused interventions to build targeted productive sectors and relax binding constraints to business which include provision of infrastructure and the development of national human resources
2. **Community development** for all people with additional focus on *protecting vulnerable groups*
3. **Maintaining macroeconomic (monetary and fiscal) stability**, including sound management of government debt, while making prudent use of the renewed capacity for limited borrowing
4. **Improved governance and Public Administration**, with better accountability, budgeting, and delivery of public services

In addressing these priorities, government recognizes the critical need to address longer term issues such as climate change and increase vulnerabilities to disasters. This is in particularly highlighted by the immediate need to help the people of Ha'apai to recover from the destruction wrought by cyclone Ian.

In line with the theme of Partnership, which runs through all of government policy and the theme of this budget, Government will seek to enhance mutual partnership within the public service, with key partners in Tonga, overseas Tongans, our development partners, and our neighbors in the region and beyond.

The Total Appropriation in the budget is **\$302.7 million**. When in-kind support is included, the total budget is **\$483.7 million**. **Table 1** shows how these funds are divided by the nine outcomes of the TSDF.

Table 1: Total Budget Government and Aid for each Outcome Objectives (TOP\$ m)

Outcome Objectives		Government (Local and Budget Support)	Projects			Total Budget
			Donor Cash	Donor In-kind	Total Donor	
1	Strong inclusive communities	7.70	2.80	4.82	7.62	15.32
2	Dynamic public and private sector partnership	99.20	6.25	3.40	9.65	108.85
3	Appropriate, well planned and maintained infrastructure	9.80	35.00	114.21	149.20	159.00
4	Sound education standards	34.00	7.63	6.78	14.41	48.41
5	Appropriately skilled workforce	5.00	0.42	0.02	0.44	5.44
6	Improved health of the people	26.20	5.10	3.74	8.83	35.03
7	Cultural awareness, environmental sustainability,	4.80	3.69	33.37	37.06	41.86
8	Better governance	23.10	3.62	5.98	9.65	32.71
9	Safe, Secure and stable society	25.50	2.89	8.67	11.56	37.06
Grand Total		235.30	67.40	180.99	248.38	483.70

Source: Ministry of Finance and National Planning

Table 2: Key Economic and Fiscal Indicators

	2012/13	2013/14	2014/15
Real GDP Growth	0.3%	1.8%	3.0%
Nominal GDP¹ in \$ million	806.9	829.5	854.4
(AS % of GDP)			
Total Domestic Revenue	18.9%	19.0%	19.7%
Total Budget Support	2.4%	4.1%	4.4%
Total Project Aid Funding (cash)	4.1%	5.0%	7.9%
Total Project Aid Funding (in-kind)	7.9%	8.3%	21.2%
Total Expenditure²	22.1%	23.4%	27.5%
Total Public Debt	46.2%	44.3%	46.8%
Debt Servicing	2.5%	2.4%	2.5%

¹1% inflation for 2013/14; 0% inflation assumed for 14/15

²GFS definition

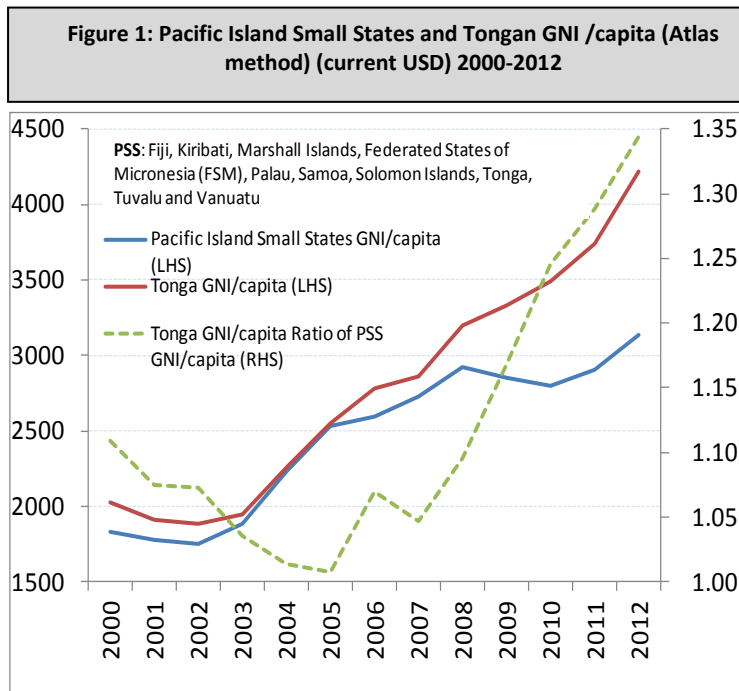
Source: Ministry of Finance and National Planning

5 ECONOMIC AND SOCIAL OUTCOMES AND OUTLOOK

5.1 Growth in Tonga compared to the region

Following the setbacks of the strikes and riots in 2005 and 2006, Tonga's GDP from calendar 2008 to 2012 has grown at 2.2 percent per annum compared to only 1.4 percent for our fellow Pacific Island Small States.

Because Tonga's population is barely growing, while some of our neighbors have population growth of 1-2 percent, a per capita measure is more helpful. Gross National Income (GNI) also gives a better measure of the actual income going to Tongans. **Figure 1** shows that since 2005 Tonga's GNI per capita has grown considerably faster than the average for the region, increasing from about the same as the average to 35 percent greater.

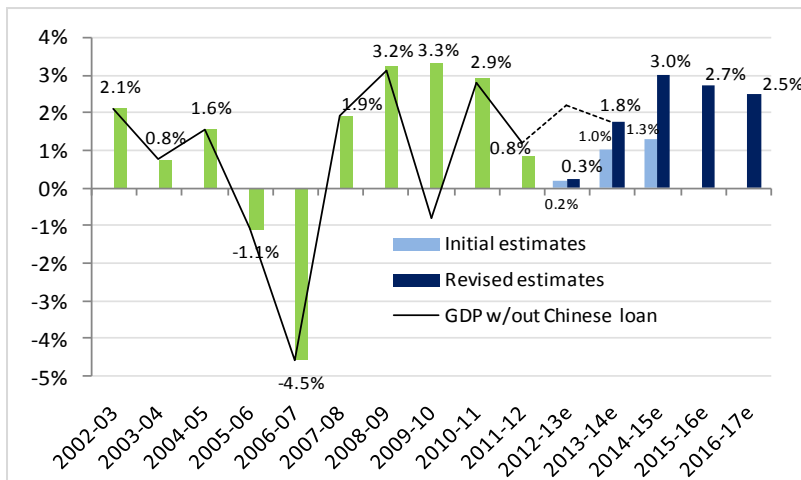


Source: World Bank Data

Tonga also ranks first among Pacific developing member countries that were included in the United Nations Development Programme's 2012 Human Development Report, with a Human Development Index of 0.710 (95th out of 186 countries) compared to the average for Asia Pacific Region of 0.683. Since June 2013, Tonga has moved from low to upper middle income bracket.

5.2 GDP Growth and Outlook

**Figure 2: Real GDP Growth with and with-out EXIM China Bank Loan
2002/03 to 2016/17**



Sources: Tonga Statistics Department and MoFNP estimates

As always anticipated, total growth slowed significantly with the completion of the EXIM Bank funded construction loans which boosted growth between 2008/09 and 2010/11 as shown on Figure 2.

Despite the end of this significant boost, the present estimate is that growth did not turn negative for 2012/13, as was always a possibility. Growth without the impact of the construction expenditure has continued at nearly 2 percent despite the very low growth of only 0.3 percent in 2012/13.

The estimated nominal GDP for 2012/13 was \$806.9 million, giving GDP per capita of T\$7,792 placing Tonga now in the upper middle income group of countries for the first time.

Growth is forecasted to strengthen sharply over the next few years; driven largely by the post-cyclone reconstruction efforts as well as continued strength in other sectors. Government seeks to maintain these higher growth rates, with a target average growth of 2.5 percent per annum. This will require continued commitment and partnership between Government, businesses and the people to achieve given our continued challenges and vulnerability.

Table 3 shows the actual estimates for real GDP growth for the three major sectors to 2011/12; with provisional estimates for 2012/13 and forecasts for the next two years.

Table 3: GDP Main Components (real growth rates)

Real Growth Rates (%)	08/09	09/10	10/11	11/12	12/13e	13/14e	14/15e
Primary Sector (17%)*	-1.4	0.5	2.0	0.5	3.7	0.2	1.3
Secondary Sector (19%)*	12.9	11.6	5.5	1.2	-4.9	4.0	7.8
Tertiary Sector (54%)*	0.8	1.0	1.8	0.5	0.3	1.4	2.0
GDP**	3.2	3.3	2.9	0.8	0.3	1.8	3.0

e-preliminary estimates

**contribution to GDP.*

***The 10 percent balance accounts for net tax and subsidies.*

Sources: Tonga Bureau of Statistics, Ministry of Finance and National Planning

Primary Sector growth averaged 0.4 percent over the past four years up to 2011/12. It however picked up strongly in 2012/13 at 3.7 percent. It is expected to slow significantly in 2013/14 before picking up again in 2014/15.

Agriculture (14 percent of GDP) grew strongly in 2011/12 and 2012/13 with sharp recovery in agricultural exports, but a sharp fall in squash exports is likely to cut growth in 2013/14. Remaining non-squash commodity exports (including vanilla, coconuts, kava) are expected to continue to expand. Growth should recover in 2014/15 with pick up in squash and other exports.

Forestry (1 percent of GDP): growth fluctuates considerably from year to year. The collapse in sandalwood exports created large contractions in 2011/12 and 2012/13. Slow growth is anticipated in the next few years.

Fisheries (2 percent of GDP): this sector also fluctuates a lot being sensitive to changes in a few products. Overfishing of sea cucumber created negative growth in 2011/12 before it jumped 18 percent in 2012/13 with expansion in seaweed and tuna. A fall off in tuna, snapper and seaweed production in 2013/14 will again push growth negative. Despite large fluctuations year to year, fisheries and marine related exports are starting to recover.

Secondary Sector (19 percent GDP): after strong growth from 2008/09 to 2010/11, growth fell significantly, and turned negative by 4.9 percent in 2012/13. Strong recovery is anticipated going forward. Changes in levels of construction activity are the main contributors to these large changes in the secondary sector.

Construction (share in GDP has varied): with the end of the EXIM loan funded construction growth plunged nearly 10 percent in 2012/13. A sharp turnaround is anticipated in 2013/14 with growth over 6 percent doubling to 13 percent in 2014/15 with other large aid funded projects, including Ha'apai reconstruction, coming on stream.

Mining and Quarrying (1 percent of GDP): movements in this sector closely track movements in the construction sector, only with considerably greater fluctuations in growth rates. After falling 8 percent in 2012/13 it is expected to recover sharply over the next two years.

Electricity and Water Supply (3 percent of GDP): electricity sector growth in 2012/13 to 2014/15 is expected to rise from 1.5 to 2 percent with further expansion in access and production. Water sector is also estimated to grow steadily with expanding water supply systems, and increased demand from construction.

Manufacturing (6 percent GDP): growth is also subject to fluctuations in and out of positive territory with changes in the fortunes of larger individual business. The revival in beer production, saw-milling activities, expansion in coconut oil production, and construction related products should help to keep growth positive at 1 to 2 percent from 2012/13 to 2014/15.

Tertiary Sector (54 percent GDP): in part due to its large size the rates of growth in this sector have been relatively stable, averaging out greater movements in the sub-sectors.

Wholesale and retail (10 percent to GDP): growth slowed to 0.3 percent in 2011/12 and 0.7 percent in 2012/13. A pick up is anticipated over 2013/14 and 2014/15 with general growth in the economy and pick up in remittances.

Hotels and Restaurants (3percent to GDP): experienced growth of 1.8 percent in 2012/13, in line with a slight improvement in tourism. A slight decline of 0.5 percent is anticipated in 2013/14 related to weak visitor numbers and uncertainty in the domestic airline industry. A pick up to 3 percent for 2014/15 is anticipated, associated with solving issues with the domestic airline, increased activity by the new Tourism Authority and the Coronation.

Transport and communication (6 percent to GDP) grew 1 percent in 2012/13 picking up to 3 percent in 2013/14 and 2014/15 driven by rapid increase in use of the fiber optic cable, growth in sea and air travel, in part related to Ha'apai reconstruction, solving of domestic airline uncertainty, and increased vehicle registration.

Financial intermediation (5 percent GDP): after contracting for some time, growth is expected at 4 percent in 2013/14 with strengthening of the bank and non-bank sectors and expanding lending, the opening of the newly introduced Pacific International Commercial Bank and anticipated expansion of Tonga Development Bank Services.

Public Administration and Services (12 percent of GDP): growth is expected at 1 percent in 2013/14 and 1.5 percent in 2014/15 up from 0.6percent in 2012/13, driven in part by 5 percent increase in civil servants' wages and salaries. Scope for future growth will depend on maintaining fiscal stability and availability of budget support.

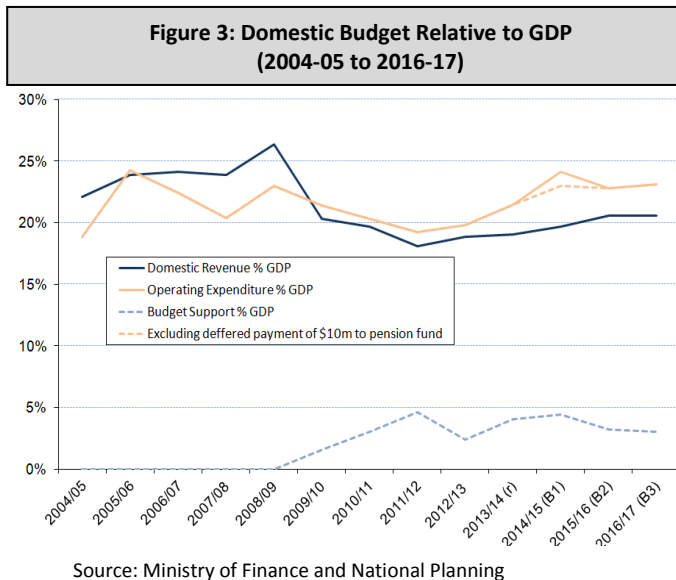
Ownership of dwellings (9 percent of GDP): growth is expected to decline by 0.4percent in 2013/14 mainly driven by damages done to housings in Ha'apai but expected to slightly pick up in 2014/15 after post reconstruction efforts.

Education, health and social work excluding public health and education, included in public administration (3 percent GDP): growth for non-government education in 2013/14 at 1 percent compared to 2 percent in the previous year. Non-government health and social work sector is expected to continue growing in future years with growth role for community organizations.

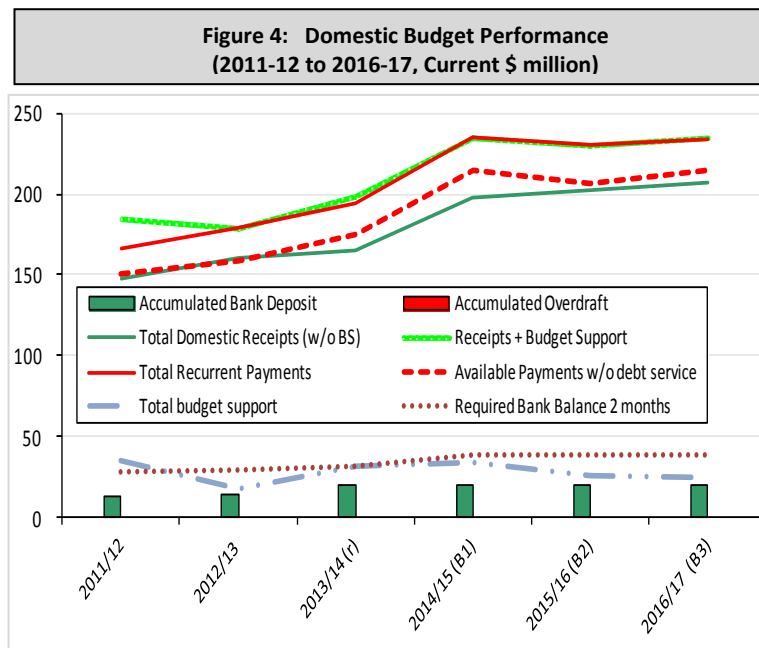
Recreation, cultural and sporting activities and other small sectors: expected to remain slightly positive with general economic growth.

5.3 Fiscal and Debt Outcomes

Focusing on the local or “recurrent budget”, the gap between domestic revenue and operating expenditure (the cost of running the public service) has continued to widen over the last few years (see Table 6 in section 6.2). This gap continues to be met by budget support which has been running around 2.5 to 3.5 percent of GDP. Over the MTBF revenue to GDP is expected to recover gradually to just over 20 percent GDP. Operating expenditure will jump in 2014/15 to 24.1 percent of GDP due to costs such as the COLA carrying forward, and the paying off of \$10 million of the transfer value Government owes to the retirement fund. Without this transfer value, the increase in operating expenditure to GDP would only be to 23.0 percent. Over the next two years the level is forecast at about 23 percent of GDP. These trends are shown in **Figure 3**.



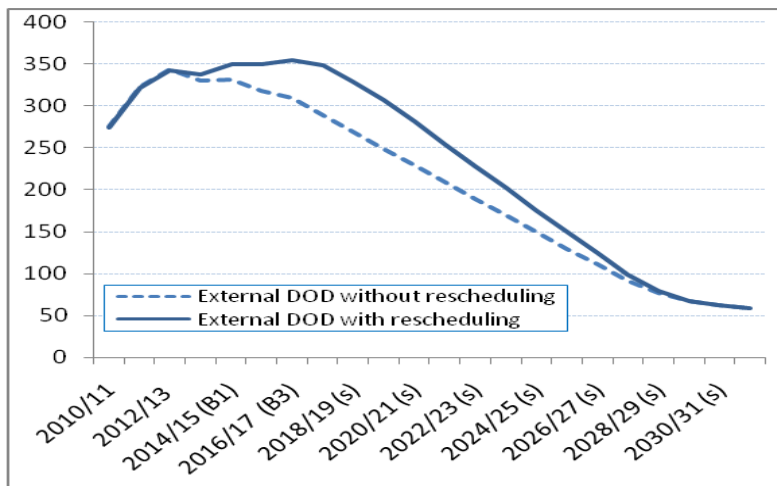
The 2013/14 is anticipated to generate a cash surplus (“recurrent budget”) of \$5 million resulting from the deferral of the EXIM Bank loan repayments. Following the deterioration in cash balances prior to 2010/11 the 2013/14 Recurrent Budget generated a small cash surplus of \$0.9 million bringing the consolidated fund balance up to \$14.5 million retaining a level equal to one month of total payments (still below the objective of two months cover). This was accomplished by moderating expenditure to compensate for a short fall in budget support which only reached \$19.2 million down from over \$37 million in the preceding year.



2012/13 delivered a small cash surplus of about \$1 million. Compared to a planned balanced cash budget, 2013/14 is expected to generate a cash surplus of about \$5 million; though this would be a deficit without the deferral of the EXIM Bank loan repayments for five years. This will raise consolidated fund to \$19.7 million or about 1.2 months cover of payments, still well below the target two months. A balanced cash budget is projected for each of the three years in the MTBF leaving cash balances close to \$20 million. These trends are shown in **Figure 4**.

Staff costs have stabilized at about 53.5 percent of operating expenditure, and are projected at a similar level over the MTBF. As a percentage of domestic revenue, however, it has increased from 45 percent in 2008/09 to over 65 percent. This reflects the failure of domestic revenue to

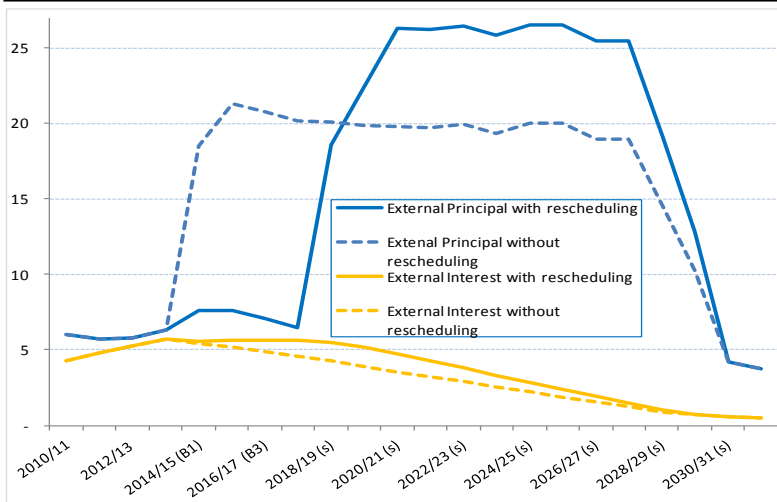
Figure 5 : External Disbursed outstanding debt (DOD) with and without rescheduling of Exim Bank Loan Repayments



Source: Ministry of Finance and National Planning

budget support from 100 percent grant to 50 percent grant and 50 percent loan. This provides some room for prudent debt financing. This will focus on domestic borrowing to support direct cost savings and economic growth. New external borrowing will focus on budget support and reconstruction of Ha'apai.

Figure 6: External Disbursed outstanding debt (DOD) with and without rescheduling of Exim Bank Loan Repayments



Source: Ministry of Finance and National Planning

public debt at 30 June 2014 is estimated at \$368.2m (44 percent of GDP); with total external debt, of \$338.7m (40 percent of GDP) or which nearly two thirds is owed to EXIM Bank. Total Domestic debt, of \$29.5 million (3 percent of GDP) consists only of Government bonds on issue with 56 percent held by financial institutions and over 24 percent by retirement funds. This is proposed to increase to \$ 49.5 million during 2014/15.

keep up with operating costs, and the increased dependence on budget support, both to cover the gap between domestic revenue and operational expenditure, as well as debt repayments and other costs. Over the MTBF this ratio is projected to decline slightly.

Recent improvement in economic and public management conditions resulted in IMF upgrading Tonga from high debt distress to medium. This raises a number of key debt ceilings, as well as changing World Bank and ADB project and

The debt data includes the impact of this new borrowing along with the recent rescheduling of the two large EXIM Bank loans, with first repayments now delayed by five years, starting in 2018/19 with a significant rise in external debt service estimated at over \$12 million. **Figure 5** shows the forecast outstanding external debt with and without the deferred EXIM bank, while **Figure 6** shows the two options Total

public debt at 30 June 2014 is estimated at \$368.2m (44

Total debt service for the year ended 30 June 2014, is estimated at \$19.5m, comprising of external \$12.0m (62 percent) and domestic \$7.5m (38 percent). This is equivalent to about 2 percent of GDP and nearly 12 percent of domestic recurrent revenue.

Total on-lent debt, at 30 June 2014, due to Government from various public and other enterprises is estimated at \$62.6 million (7 percent of GDP and 18 percent of total external loans). Most of these loans relate to on lending of the EXIM Bank loans for rebuilding of the Nuku'alofa business district. Total on lent debt service, at 30 June 2014, is \$1.57 million; most of these companies are having difficulties with their repayments; some have still to sign their loan agreements with Government.

5.4 Foreign Reserves and Balance of Payments Outcomes²

Gross official foreign reserves were \$281.1 million as at the end of February 2014, up 6.8 percent this financial year. This is equivalent to a record 9.4 months of import cover, well above the 3 month target. The level is anticipated to continue to increase over the next year.

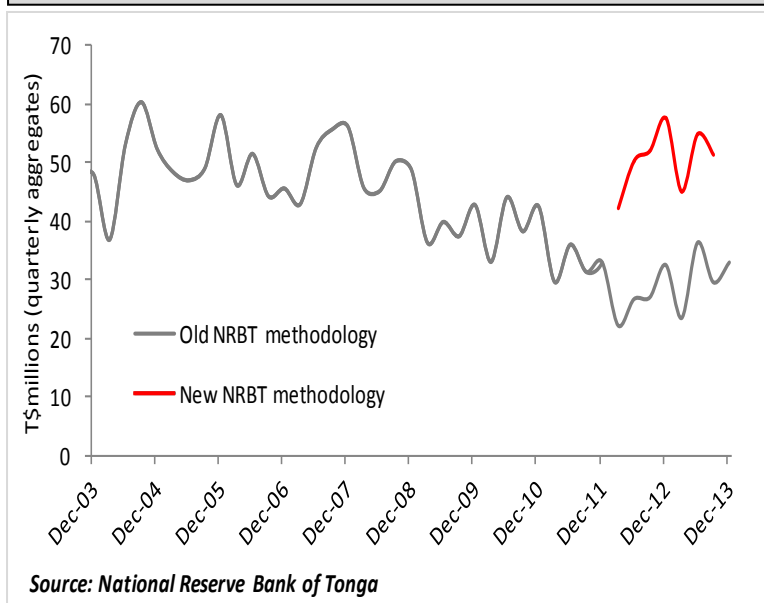
Imports, (adjusted overseas exchange transactions - OET), have been little changed so far this financial year with major components broadly stable also, with a slight increase in payments for oil and construction materials being offset by a fall in payments for retail goods.

Exports (OET adjusted) receipts have picked up a little and are now at high levels by recent standards. The increase comes from the continuing overall rise in agricultural exports. A slight depreciation of Tonga's trade-weighted index over the past two years has supported export growth also.

Remittances, NRBT has been able to adjust the remittances data to take account of recent changes to the way OET transactions are recorded by foreign exchange companies (this is explained in Annex 1). This nearly doubles the estimation of cash remittances back to pre-GFC levels, over \$200 million per annum. **Figure 7** shows the new and old series (on a quarterly basis) with a slight pickup in the last year. This improvement is consistent with developments in other similar countries. As a share of Tonga's most recent official measure of gross national disposable income (for financial year 2012), remittances are 21 percent.

The NRBT has also made some very rough estimates of in-kind remittances – those that were never captured. Over the year to December 2012, these are estimated at some \$85 million per annum pushing total remittances up to nearly 30 percent of disposable income.

Figure 7: Cash Remittances, New and Old Series – Quarterly aggregates



² Source of data for this section is the NRBT.

Balance of foreign exchange transactions, which is the closest to a full balance of payments available, was in surplus over the year to February 2014, wider than the surplus recorded over financial year 2013. The widening reflected a lower current account deficit and a higher capital account surplus.

5.5 Monetary Outcomes³

Consumer prices rose over the 12 months to February 2014 by 4.7 percent. The increase was the fastest since September 2011 but below the NRBT reference range of 6 to 8 percent. Prices of imported goods rose by 3.2 percent, despite world oil prices being little changed in pa'anga terms. Much of the imported inflation was driven by increased costs of goods imported from NZ. Domestic prices rose 6.8 percent over the past year; driven by increased domestic food prices. The rate of the core inflation, which excludes food and energy prices, increased by 5.6 percent over the year to February. Inflation is project to be around 2.5 percent in June, before falling to 0 percent at the end of 2014.

Interest rates have fallen by between 36 and 71 basis points since the end of the last financial year. The weighted average rate on all bank loans has fallen by more, because the composition of lending has shifted towards lower-risk lending products. Lending rates are now low by the standards of the past decade. Deposit rates are little changed. NRBT sees little room for lending rates to fall much further despite increased competition in banking services.

Total bank lending balances grew by 8.9 percent over the year to February 2014; the fastest in five years. Including loans extended by the Retirement Fund Board (RFB), South Pacific Business Development (SPBD) and Government of Tonga (both for building reconstruction and other), lending would have grown by 10.9 percent over the year. The growth was all to households with a continued, but slower, decline to businesses. Some of the lending to households may be of a commercial nature. NRBT anticipates a further growth in lending of 10 percent over the current year and 2015 which will support the anticipated improvements in GDP growth.

Broad money balances grew by 5.2 percent over the year to February. The components of broad money have, however, grown at very different speeds. The fastest growth has been recorded for the components that earn the lowest interest and are most suited for transactional purposes, consistent with the NRBT's expectations for faster economic growth this year. Term deposits balances have contracted markedly.

5.6 Social, Community Poverty and Vulnerability Outcomes

Millennium Development Goals (MDGs) Acceleration Framework (MAF): The MAF focuses on Goal 6C (health), the goal that is most off track, associated with an epidemic in non-communicable diseases, falling life expectancy and rising death rates. The state of NDCs is a national crisis. It is understood that MDG Goal 1 (Poverty) and MDG Goal 3 (Gender Equality and Empower Women) will also be considered in the framework of achieving Goal 6C

Health: Government continues to provide most of the **health services** in the country though there are gradually more private clinics being established. Adult mortality has risen and life expectancy fallen over the last 10 years, in spite of a sustained low, under-five mortality. The NCD crisis is resulting in an increased number of people dying in mid-life. Between the period 2001-2004 and 2005-09, life expectancy for males dropped from 69 to 65 years and for females from 72 to 69 years. The major focus of MAF is to address this crisis

³ Source of data for this section is the NRBT apart for inflation data from Statistics Bureau.

Education: Tonga's literacy rate was reported at 98.2 percent, higher than the literacy rate for the Asia Pacific of 94.7 percent - however, there are other indications that suggest the rate may not be this high beyond basic literacy. For the population aged between 5 to 14 years primary school enrollment is 94.4 percent. For the population aged 15 and older 74.6 percent have secondary education. Based on the 2011 Census, the percentage of population with vocational/professional/TVET training was 9.6 percent and with tertiary education 16.1 percent.

Labor Force Participation: several measures of unemployment are calculated by the Census: 1.6 percent for those who did not work but were looking for and available for work; 6.5 percent if discouraged workers are included; and 33.2 percent if subsistence workers are included. Tongans on overseas employment schemes increased from 833 in 2010 to 2,772 in 2013. Most workers are in the New Zealand Recognized Seasonal Workers (RSE), covering horticulture and viticulture industries. The largest percentage increase relates to the Australian Seasonal Workers Program (SWP) which has a more attractive minimum wage for fruit picking.

Demography: the population is estimated at 103,219, June 2012; roughly five times the population in 1901. Average annual growth is 0.2 percent from 101,911 (2006 Census) to 103,036 (2011 Census). A total fertility of about 3.8 (down from 4.2 in 2006), is offset by the continued net out migration from the Kingdom of negative 20 per 1000. 73 percent of the population is resident on Tongatapu, with a steady net migration from the four outer island groups to Tongatapu. This has been associated with an annual growth in urban population of 0.5 percent and rural population on Tongatapu of 0.2 percent. These movements reflect the common experience of most countries as they develop.

Parliament Constituency's Report, 2013, focuses on the problems for people remaining in the outer islands and how to address them. Government is seeking ways to address these through various means including health and education facilities, maintenance of roads, subsidies for utilities (electricity & water), as well as community and environmental development projects. The strengthening of district plans under Ministry of Internal Affairs will help to address these in a more coordinated manner. Other constituency requests are addressed through relevant section of the statement.

Multi-dimensional measures of Poverty: no new income poverty data is available, however, GDP and GNI per capita has continued to grow. Tonga ranks well compared to other countries in terms of the multi-variable measure of poverty/well-being, the Human Development Index (HDI), as shown in Table 4.

Table 4 : Tonga's Relative Human Development Index (HDI) indicators for 2012

Country	HDI Value	HDI Rank	Life Expectancy at birth	Expected years of schooling	Mean Years of schooling	GNI per capita (PPP US\$)
Tonga ³	0.71	95	72.5	13.7	10.3	4,153
Federated States of Micronesia	0.645	117	69.2	11.4	8.8	3,352
Solomon Islands	0.53	143	68.2	9.3	4.5	2,172
East Asia and the Pacific	0.683	-	72.7	11.8	7.2	6,874
Medium HDI	0.64	-	69.9	11.4	6.3	5,428

³Life expectancy for Tonga based on UN total population estimates which are slightly higher than Government recent average estimates on 65 for male, 69 for females
Source: United Nation Development Programme (UNDP)

Social assistance payments: the aged pension as requested by many constituencies is being extended for eligible elderly from those 75 years and older, to those 70 and older. Approximately 2,161 women and 1,812 men are eligible.

Poverty Reduction Pilot Social Protection of the Vulnerable: the first such services by Government of Tonga have been operating for two years. Aged care services have been extended to 151 clients, compared to a potential eligible number across the country of 609 (10 percent of the total elderly over 65 years). The early intervention (0-3 year olds) services are covering 55 babies, compared to a potential eligible number of 82 babies born each year (nearly 1 percent of all births). The plan is to gradually extend both of these schemes to the whole country.

In addition, the program will also consider the provision of a national welfare grant to benefit the targeted vulnerable group (disable) based on an acceptable national registry in partnership with a recognized national body in relation disabilities.

6 GOVERNMENT BUDGET: FUNDING THE OUTPUTS

6.1 Priority Focus for Budget

The Government is focusing on boosting longer term more inclusive growth working in partnership with all the people, development partners and others to build a stronger economy with more jobs and increased incomes, in the face of ongoing economic uncertainty in the world. Government also seeks to improve governance and accountability as part of the political reform and a central requirement for the delivery of government's policies. The TSDF remains the guiding strategic document, while recognizing that it will be reviewed and updated during the 2014/15 Budget year. The four areas of key focus for the budget, drawing on the TSDF and the Budget theme, are:

1. **Supporting growth** through focused interventions to build targeted productive sectors and relax binding constraints to business which include provision of infrastructure and the development of national human resources
2. **Community development** for all people with additional focus on **protecting vulnerable groups**
3. **Maintaining macroeconomic (monetary and fiscal) stability**, including sound management of government debt, while making prudent use of the renewed capacity for limited borrowing
4. **Improved governance and Public Administration**, with better accountability, budgeting, and delivery of public services

Even within these four core areas all expenditure is not equal. Careful testing of proposals in the corporate plans, both for recurrent operations and maintenance, and for new aid funded projects, have been required. In addressing these priorities, government recognizes the critical need to address longer term issues such as climate change and increase vulnerabilities to disasters. This is particularly highlighted by the immediate need to help the people of Ha'apai to recover from the destruction wrought by cyclone Ian.

In line with the theme of Partnership, which runs through all of government policy and the theme of this budget, the following broad principles guide all sections:

Broad principles for Enhanced Mutual Partnership:

- ✓ Public Service clearly working as an apolitical servant of the people, in line with the high expectations following political reform
- ✓ improving collaboration and partnership for better performance:
 - within government between all ministries and agencies, in particular the core agencies so that they provide consistent advice and systems to line ministries
 - with the people of Tonga, in their many roles as producers, consumers, students, members of non-government, church and other organizations, to better identify and prioritize their many legitimate needs
 - with all development partners, to ensure good relationships as set out in the many internal agreements on improved aid and development effectiveness
- ✓ being a responsible member of the Pacific and international community by effective and constructive participation in regional and international forums, supporting peace keeping and other initiatives

6.1.1 Supporting Growth

Given the important role of GDP growth to increase incomes, generate revenue for Government and allow the improvements in government delivery of its outputs, a growth target has been established of at least 2.5 percent per annum⁴. During the period of the MTBF this is anticipated to be realistic.

This needs to be broad based and sustainable in order to achieve tangible benefits as Government is keen to ensure improved services to the people of Tonga while ensuring they get better value from the use of public resources raised from this higher growth. Job creation must be across the country, especially for youths, with increased income earning opportunities across our communities. Increased government revenue is required, but it must be collected fairly and efficiently limiting negative impacts on incentives for working and generating businesses.

To accomplish this, Government will provide its contribution to this national high level outcome through:

- ✓ seeking to maintain political stability while respecting the rights of all Tongans enshrined in the Constitution
- ✓ continuing efforts to improve effective partnerships with the private sector and others
- ✓ facilitating macroeconomic stability through effective monetary and fiscal policy, while directing improved expenditure towards:
 - enhancing the business and regulatory environment
 - providing enabling infrastructure
 - supporting the development of entrepreneurial, business skills and national human resources
 - supporting debate on those social and cultural norms which may limit businesses development, and seeking responses appropriate to conditions in Tonga
 - fostering a public service that delivers more efficient, effective and affordable services and so places less burden on tax payers.

6.1.2 Public investment

The following principles will be followed:

- ✓ use NIIP 2 and NIIP2+ (which will expand NIIP2 to include social and administration related infrastructure) to guide all capital investment based on identified government priorities and assessment of viability
- ✓ better management and implementation of development aid funded capital investments, showing all Government related expenditure, taking note of limiting maintenance cost, building in climate change protection, and protecting the natural and social environment
- ✓ encouraging private/public partnerships (PPP), build operate transfer (BOT) cost sharing options for financing of priority infrastructure

⁴ The total growth rate in Tonga will tend to be lower than the growth rate for countries with more rapidly growing populations.

- ✓ implementation of TERM to improve affordability and efficiency of energy

Specific policies to be supported:

- managing an effective reconstruction for Ha'apai, and ensure all ministries take account of this in their respective budgets, including:
 - a house reconstruction for US\$13.8m (including US\$12 million sourced 50:50 grants loan) from the World Bank, US\$1.8 millions from the EU
 - public utility and school reconstruction for US\$10.2 million from ADB, including US\$4 million contribution by New Zealand
- investing in petroleum downstream supply through medium range tanker and storage to reduce transport costs from source
- pursuing new PPP opportunities such as for financing infrastructural development to include the extension of fibre optic from Tongatapu to the outer island (Vava'u and Ha'apai)
- increasing attention towards ensuring all capital investments by Government are sustainably budgeted for by taking full account of future operations and maintenance
- increasing private sector adherence to building standards and safety codes
- ensuring improved quality control of aid funded constructions, to ensure compliance with procurement and building codes
- supervising the construction of St George's Palace to ensure better standards than recent aid funded buildings, design that is appropriate to domestic needs, the inclusion of attractive public spaces, and overall attractive entry point for cruise ships
- effectively managing the relationship for the IDHL reconstruction and operation under PPP
- improving planning for the financing of the Pacific Games (PG) operations and facilities, including funding of the Pacific Games committee working on these plans
- increasing investment in the countries EEZ claims on the Minerva Reef
- support the transport sector safety

6.1.3 Improve private sector sustainable growth

The following principles will be followed:

- ✓ enhancing the enabling business environment across all areas of government to address those key constraints (access and cost of credit) to growth, within Government influence
- ✓ addressing the cost disadvantages of priority productive sector (agriculture, fisheries, tourism & manufacturing) to help them be more competitive
- ✓ working with the people to encourage better health and education for a more productive work force, in particular addressing the NCD epidemic
- ✓ supporting funding for Tonga Tourism Authority (TTA) to build and improve Tonga's regional tourism market share and sustain increase tourism receipts
- ✓ seeking options for more cost effective access to overseas education by Tongan students through appropriate channels such as PACER Plus negotiations or Government to Government bilateral arrangements

Table 5: Terms and Conditions for Concessional Loans

Funds	Amount	Interest Rate	Repayment Period	Max Loan
Agriculture Marketing Fund (AMF)				
	\$1 million	1%	3 months	100K
Funds Objective: To boost exporter's confidence by providing a facility to allow the early payment to primary producers for their exports.				
Fisheries Development and Export Fund (FDEF)				
	\$300,000	1%	6 months	30K
Fund Objective: Assist fishermen, vessel owner and exporters to generate increased exports, income and employment in the fisheries sector				
Tourism Fund				
	\$500,000	1%	2 years	50K
Fund Objectives:				
<ul style="list-style-type: none"> • To promote the development of new tourism products and events • To improve the quality of small-medium accommodations • To develop a clean and beautiful tourist environment • To support and encourage community participation in development of heritage sites • To promote and encourage cooperation and coordination within the tourism sector 				
Manufacturing Fund				
	\$250,000	1%	2 years	50k
Fund Objectives:				
<ul style="list-style-type: none"> • To support export-ready manufacturers • To stimulate innovation • To promote the development of competitive value-added products • To promote and encourage cooperation and coordination in manufacturing sector 				
Student Loan Scheme				
	\$1 million	1%	4 years	15K
Fund Objectives:				
<ul style="list-style-type: none"> • To promote and enhance the academic and professional skills of Tongans that need to further their study abroad but cannot afford the costs, diploma level upwards • To support qualifications from an accredited institution 				
Economic Growth Facility (private sector expansion)				
	\$10 million	4%	5 years	depends on proposal
Fund Objective:				
<ul style="list-style-type: none"> • To encourage private sector expansion by supporting viable projects that will stimulate economic growth and benefit Tonga by topping up the existing funds or any other new economic activities 				
TOTAL LOAN FUNDS : \$13.05 MILLION				
Pure Grants : Handicrafts Funds				
	\$250,000			
Fund Objective				
<ul style="list-style-type: none"> • To increase demand and production of Tongan handicrafts, and apply existing conditions being used by MCTL 				

Source: Ministry of Finance and National Planning

Specific policies to be supported:

- establishing appropriate funds for marketing and other key needs (agriculture, tourism, manufacturing, fisheries), managed by TDB, based on concessional loans and grant assistance to handicraft marketing (see detail of terms and conditions in **Table 5**)
- ensuring coordinated, transparent and effective implementation of the marketing funds, and related initiatives (local and aid), that targets the intended beneficiaries
- ensuring TTA is performing and effectively implementing the Tonga Tourism Roadmap
- discussing with Australia and NZ options for a non-discretionary education fees for Tongan's (and other Pacific Islanders), lower than the high overseas student fees
- developing an appropriate student loan scheme, for higher overseas education to help with the cost of students education
- continuing partnership with the private sector through strengthened National and Sector Growth Committees resulting in identification of constraints and implementation of solutions
- ensuring appropriate transport safety and security arrangements for full compliance by all aircrafts (including MA60) and shipping
- continuing to pay insurance for the MA60 and the one new Y12 aircraft to help contain airfares to outer island
- establishing a multi-sector regulatory framework that provides clarity and support to domestic and foreign investors
- better utilizing overseas missions to provide services that help maintain links of Tongans overseas to Tonga (birth certificates, passports) and encourage foreign investment (business advice)

6.1.4 Community Development and Protecting Vulnerable Groups

The following principles will be followed:

- ✓ negotiating for a greater range of options for overseas employment schemes, encouraging higher income jobs, while taking note of the impact this may have on domestic growth
- ✓ ensuring that government policies work to maintain and strengthen the links with Tongans overseas, to ensure the continuation of family support links, and the increase the likelihood of them spending time in Tonga to help with community and business development
- ✓ supporting disadvantaged households from the impact of flooding and natural disasters through provision of appropriate infrastructures and safekeeping of affected areas
- ✓ raising financial literacy to improve small businesses and to protect people from exposure to excess financial charges
- ✓ developing clear policy based, and financially affordable, social protection schemes to support vulnerable groups such as the elderly and disabled

Specific policies to be supported:

- continuing to provide direct cash grant to the 17 electoral constituencies, to assist community development
- working with member of Parliament to ensure that projects and issues identified in the Constituencies report are integrated with district and other plan of Government to support their implementation
- continuing to work on improving local government, as part of the public service, and seeking options for developing existing office space and qualified staff for MPs, District and Town Officers in their constituencies to facilitate the economic and social development of the communities
- developing public awareness and understanding, with particular focus on women's groups, of the consequences of borrowing from 'loan sharks' and engaging in gambling such as Radio Bingo
- supporting the continued implementation of the MDG Acceleration Framework (MAF)
- extending the Social Welfare Scheme for the elderly over 75 years of age (which supports reduction in poverty and hardship and the maintenance of their welfare and dignity) to be extended to those aged between 70 and 74
- funding the continuation of the Tonga Social Services Support Pilot Scheme (\$250,000) and Social Protection of the Vulnerable (\$500,000) working with the NGOs on:
 - care services for the elderly
 - early intervention services to children with disabilities
 - job placement services for people with disabilities
- establishing a deputy CEO post in the Ministry of Internal Affairs to coordinate the social welfare programs
- finalizing the introduction of maintenance work in village communities that will be piloted by the World Bank by training the villagers to maintain roads
- supporting youth groups/community kava club to clean up the communities and Nuku'alofa, including the waterfront, in order to keep the environment clean and attractive for residents and visitors
- supporting community street lights
- subsidizing electricity tariff through electricity concession agreement

6.1.5 Maintaining Macroeconomic (Monetary and Fiscal) Stability

Both Government and the NRBT recognized the very limited options for expansionary monetary policy and domestically funded fiscal expansion in a small open economy. Prudent and coordinated decisions between both policies are critical. Imprudent policies can quickly generate a macroeconomic and fiscal crisis which would set progress back, in all areas, for many years. Macroeconomic stability will thus remain the corner stone of the collaboration between fiscal and monetary policy.

6.1.5.1 Monetary policy

The NRBT already is following as relax a monetary policy as prudence would allow. The banking system is still working off the high level of non-performing loans from the last attempt to boost lending beyond prudent levels. Bank lending to business continues to decline, though

less rapidly, while lending to households (which includes some commercial activity) is growing. Monetary policy will work to mitigate against a future building up in the level of non-performing loans while encouraging lending for commercially viable investments.

The roles of monetary policy include:

- ✓ ensuring sound financial institutions (encourage strong and viable banking)
- ✓ maintaining adequate foreign reserves (at least 3 months cover of imports)
- ✓ protecting external balance (balance of payments and currency convertibility)
- ✓ supporting price stability (low inflation)
- ✓ facilitating growth of the domestic economy.

Specific policies to be supported:

- increasing competition with the opening of a new bank, (Pacific International Commercial Bank), while ensuring all banks continue to follow prudent lending rules
- continuing negotiations for sale of 40 percent of Tonga Development Bank (TDB) shares, however, as these negotiations are still ongoing no estimation has been included for this revenue in the budget, if successful, the revenue from the sale will be used to build up the government's debt sinking fund; sale will be to an appropriate foreign investor who can provide additional funds, at low interest, to:
 - deepen the lending base of TDB
 - allow for lower interest on TDB loans
 - diversify risk
 - further develop and formalize the commercial side of TDB operations while maintaining its development banking role
- extending opportunities for micro finance that includes improved understanding by borrowers
- providing additional funds (from bond sale and government revenue) to extend TDB's capacity to lend on cheaper rates to priority economic activities (see **Table 5**)
- reviewing the NRB Act to seek options for strengthening the Reserve Bank's support to economic development while continuing to support monetary stability and the soundness and resilience of the financial sector

6.1.5.2 Fiscal policy

Government fiscal policy is its primary tool to improve income distribution through both its revenue and spending policies. Fiscal policy are designed to support macroeconomic stability, correct market failures and provide public goods with particular emphasis on inclusiveness, in particular elderly welfare, special needs of vulnerable groups and disabled, access to free and improved health care, and free basic primary education and subsidized postsecondary education.

As learnt over recent years, there is no scope for further fiscal expansion from large external loans. Fiscal expansion beyond the capacity of domestic revenue must be funded by increases in budget support and external aid, issuance of domestic bonds that mobilizes excess domestic

liquidity, with some prudent external borrowing for viable projects, on highly concessional terms. To improve the complementary between fiscal and monetary management, government also supports the reforms to the management of the NRBT Act mentioned under monetary policy.

Government remains committed to its fiscal consolidation strategy started two years ago, which includes ensuring better management of public finances and the return to a more sustainable position as the overarching determinant of fiscal policy. Government also take into account possible financial market pressures of its policies, and vulnerability to large external deficits, reliance on budget support and the need to protect cash reserves as part of its commitments. This consolidation is required to strengthen the long-term position of the budget and rebuild policy buffers against future external shocks.

The following principles will be followed:

- ✓ improving estimation of funding ceilings based on realistic assessments of revenue raising capacity, budget support and development assistance, and where appropriate prudent borrowing
- ✓ more careful assessing and managing of appropriate levels of public debt and cash reserves required to create fiscal space to respond to shocks and unforeseen events
- ✓ improving budget allocation across sectors by better analysis, prioritization and discussions to better align funding allocations to ministry corporate plans based on the TSDF and overall available funding
- ✓ improving quality of expenditure by ensuring commitments are properly costed and funded, restricting ad hoc funding additions during the year, improved financial management and reporting, linked to reporting on progress against corporate plan indicators

More detailed measures are covered under the Section on Improved Governance and Public Administration further down.

6.1.5.3 *Funding the Budget and revenue measures*

The following principles will be followed:

- ✓ seeking to ensure that the system of revenue collection is supportive of both the Government's ambition to support growth and to support a fair and equitable society, and to continuously review tax policy against these high level objectives
- ✓ continuing improvements to revenue collection to ensure that due taxes are collected and collecting arrears while seeking to limit unnecessary disruptions to businesses and consumers
- ✓ limiting erosion of the revenue base from exemptions by applying clear policy guidance rather than ad hoc decisions (taking account of target sectors, addressing structural disadvantages, improving performance of business, non-discretionary, fairness and transparency and protecting the revenue base)
- ✓ seeking predictable levels of budget support, to support sound budgeting
- ✓ two yearly reviewing of Government fees and fines to ensure they keep up with inflation, remain relevant, avoid charges that cost more to collect than they raise, encourage cost recovery for government services where appropriate, and are supportive to Government's wider growth and development strategies
- ✓ increasing the revenue base through increased non tax revenue sources, e.g. offshore companies

- ✓ improving returns from Government assets, consistent with the other responsibilities of such assets
- ✓ improving the use of development assistance, in collaboration with our development partners
- ✓ basing any borrowing requirements on principles of prudent debt management.

Specific policies to be supported:

- developing investment incentives and policy measures to support increased investment in agriculture and fisheries exports, tourism, commerce, manufacturing, and ICT, and include a M&E system to be sure that any incentives are having the required impact
- assessing optimum tax, non-tax levels compared to actual collection, and conditions in similar economies
- improving efficiency and returns from PE consistent with economic and social conditions and policies
- further exploring non tax revenue sources, in particular related to exploitation of marine sources and minerals by domestic based and international businesses
- providing regular payments to pay off the “transfer value” Government obligations to the Government employees’ Retirement Fund
- issuing of domestic bonds domestic bonds equivalent to \$26 million (\$10 million towards payment of transfer value; \$10 million to fund the economic loan funds managed by the TDB; \$6 million for role over of existing bonds coming due)
- fully implementing a new schedule of excise duties that support the health and well-being of the people by increasing duties on those food and drink that most increase the risk of developing non-communicable diseases.

6.1.5.4 Prudent debt management

The following principles will be followed:

- ✓ ensuring that the sustainable debt policy remains up to date and adhered to
- ✓ managing the currency composition of debt to avoid over exposure to any one currency, or one source of funding
- ✓ including all debt and lent out funds in the debt management system

Specific policies to be supported:

- targeting macro prudential policies including supervision of debt and repayments
- Debt swap to offset Government liabilities
- seeking options for establishing a debt sinking fund to cover future debt payments (including deferred China loan repayments to help avoid the difficulties when these deferred payments come due over a shorter period of time)
- updating and further developing the existing debt management policy to include comprehensive treatment of borrowing sources and purposes, modification to allow domestic bond issues for cost saving and productive issues, and highly concessional borrowing for high priorities, with no external commercial borrowing and purposes for.

6.1.6 Improved Governance and Public Administration

Good Governance is essential for establishing a stable rule based system under which people, communities, and business can go about their daily lives and engage in legitimate business and social activities in safety. Government takes seriously its responsible for the maintaining law and order, national security and open and transparent administration and legal system.

Government is committed to getting better results from the public service while recognizing the important contribution of Government employment to total formal sector employment. The need to fill critical professional staff positions remains essential. Public Enterprises reforms will also continue to ensure that they become more efficient, and less of a burden on Government finances, while delivering better services to their customers.

The main focus of the enhanced corporate planning and budgeting relates to undertaking more honest analysis of current situations and what level of outputs can be delivered. The Plans set out improvements to internal structures, systems, procedures and HR capacity. Plans and budgets must be consistent with each other and in balance. Not all improvements are about spending more money. Better management, more evidence based analysis and identification of solutions, and a general commitment to improved efficiency – rather than just being busy – are essential for improved performance by ministries and agencies.

The Draft Public and Financial Management (PFM) Reform Roadmap covers the improvements to the budget process and wider financial system. This Sector Plan will help guide the corporate plans of all concerned organizations. Gradual progress is being made on monitoring of performance and better staff management; this will continue.

6.1.6.1 *Improved budget allocation and usage of public funds for better service delivery*

The following principles will be followed:

- ✓ ensuring greater clarity of the mandate and scope of government responsibility with appropriate delegating of mandates to ministries and agencies, establishing greater focus on core functions of government
- ✓ allocating a greater share of resources and staffing to priority sectors, in particular infrastructure and economic sectors
- ✓ outsourcing of functions to more appropriate institutions where they can be done more efficiently and effectively, helping to promote private business and community involvement
- ✓ better resourcing of core outputs to avoid backlogs
- ✓ clear recording of asset and their management to protect the capital stock of government
- ✓ improving resources for maintenance so as to avoid large rehabilitation costs using development assistance which could be better spent on supporting economic growth and community development
- ✓ exploring collaboration with NGOs in the delivery of social services.
- ✓ ensuring that corporate plans cover all reforms programs and justifications for staff needs, as part of clearly linking corporate planning and budgeting supported by clear guidance and processes
- ✓ improving information and presentation of budget (domestic cash, cash and inkind inputs, Government Financial Statistics (GFS), Classification of the Functions of Government (COFOG) to enhance financial and economic analysis and planning

- ✓ improving understanding and commitment across Government for prudent budgets and avoiding large unbudgeted items, often only within months of the approval of the budget
- ✓ all proposed recruiting or creating of new posts must be fully justified in the CPs, and should in most cases be funded within the existing limits
- ✓ only considering salary revisions, if affordable to government, and
 - for public service upon recommendations from the appropriate authority
 - for those other institutions/ministries/agencies that are not under the Public Service Commission upon recommendations from the Remuneration Authority or relevant authority
- ✓ improving budgeting to limit transfers between programs, and avoid new priority expenditures being submitted to Cabinet, within the first six months of the budget period.

Specific policies to be supported:

- identifying scope for Government to reduce cost of services including outsourcing management of Treasury services in 'Eua and Ha'apai following the positive experience in the Niuas
- clearing and avoiding backlogs which hold back economic activity and delivery of justice to the people on time, e.g. court cases under Justice; land registrations and record management under Lands
- reviewing mandate and outputs of ministries to focus on core services based on appropriate size of government (starting from large ministries) (Government has approved an additional ministry comprising of communications and information, climate change, environment, NEMO, meteorology and energy)
- streamlining Government agencies and their respective cost to Government including the establishment of Multi-sector regulatory body and remuneration authorities
- reviewing remuneration and increments and how they can better be linked to staff performance management system, and seek ways to improve overall management
- maintaining the 5% COLA effective as of 1st January 2014 and reviewing the option for future COLA that recognize the need to protect purchasing power of public servants wages within the capacity of government to pay
- identifying options for government wide procurement of common goods and services to reduce costs to government
- identifying opportunities for collaboration with NGOs in the delivery of services such as high school education in Ha'apai for all
- merging of the Government and national retirement fund administration
- submitting ministries' corporate plans together with the budget to Parliament for the first time in 2014
- strengthening the whole of Government corporate roles of central ministries
- introducing One Process Tool: integrated balanced corporate plan & MTBF, guided by the TSDF, helping to improve the planning, budgeting and reporting of ministries activities
- improving MFNP consultation with CEO Forum to improve cross government allocation and management of resources

- for the first time, submitting all CPs of ministries and agencies together with the Budget Estimates and Budget Statement to the Legislative Assembly

6.1.6.2 *Monitoring & evaluation of results*

The following principles will be followed:

- ✓ Integrating M&E of TSDF, sector/district plans, Corporate Plans & Budgets, projects to be integrated into all ministries management systems
- ✓ establishing stronger national M&E to
 - help strengthen capacity for accurate and timely data from all ministries, with a well established role for the Bureau of Statistics
 - improve monitoring and evaluation of performance at all levels, with honesty
 - improve evidence based policies and allocation of resources to priorities
- ✓ improving quality and alignment of Annual Reports (to LA as per the Public Service Commission Act) reporting on the results of corporate plans and budget to show links to improved performance both against outputs and outcomes
- ✓ improving Quarterly reporting for internal government management
- ✓ improving reporting of macro level progress for improved strategic and longer term planning

Specific policies to be supported:

- strengthening M&E capacity of ministries and agencies to inform plans and budgets with linkages to their corporate plans outcomes, output focusing on effectiveness, efficiency and affordability to Government
- establishing a new structure for the Annual Reports so that the reports are more consistent with the enhanced corporate plans (especially KPIs) and budgets, with improved quality and timeliness
- implementing the program to develop the capacity of the Statistics Bureau to gather better data and providing improved local funding for its operations
- designing an annual review of the performance of the public service results, and public servants performance

6.1.6.3 *Good governance & accountability*

The following principles will be followed:

- ✓ ensuring timely completion of public accounts and their submission to Audit, to enhance financial accountability
- ✓ ensuring effective interface between Government and the LA Public Accounts Committee
- ✓ timely reporting on project progress and acquittals of cash funding to development partners
- ✓ improving accountability for results performance across all levels of Government
- ✓ improving controls and checking to limit incentives and opportunities for corruption
- ✓ establishing more active commitment to public disclosure of fiscal position (e.g. tax spend, projected deficits, debt position)

Specific policies to be supported:

- completing the backlog of public accounts (last 2008/09)
- clearing backlog of aid acquittals to re-establish accountability with development partners
- strengthening and expanding Audit Department for more timely Audit reports including new ones like the development projects and performance audit
- converting the Public Relations Commission into providing an Ombudsman and an Anti-corruption function
- increasing enforcement and compliance with the Procurement Reform Strategy and Regulations
- ensuring closer alignment of actual expenditure with priorities established in the budget and corporate plans
- increasing funding of Ministry of Justice to enable clearance of backlog of court cases
- continuing assistance to Ministry of Lands with the clearance of backlog of land issues

6.2 Summary of 2014/2015 Budget Estimate funding the Outputs

This section provides a summary. Annex II provides a more detailed discussion of the various components of the budget including projects.

6.2.1 Overall Budget in GFS Format

This section provides an overview of the current estimate 2013/14 and new expenditure initiatives in the 2014/15 Budget. The details are provided in Annex 9.

This is the first year that government has changed from presenting the full budget from the GFS1986 to the GFS2001 format. This provides a more transparent presentation consistent with international norms.

The major impact of the move to adopt the more contemporary GFSM 2001 system of classifying fiscal transactions for economic analysis has been to

- move net lending “below the line” where they are recorded as an asset of the Government
- separate the government’s investment activity in nonfinancial assets (often described as capital expenditure; and
- incorporate all in-kind transactions for and on behalf of the Government.

The equivalent of the former budget balance in GFSM 2001 is the net borrowing requirement, the net of transactions in financial assets, (primarily cash and loans and equity injections) and liabilities (borrowing by Government). The **Table 6** shows estimated transactions for the budget and following financial year that give rise to its net lending requirements.

Table 6: Overall Fiscal Balance (Current/Capital \$ million)

	Actual 2012/13	Estimate 2013/14	Revised Estimate 2013/14	Estimate 2014/15	Projection 2015/16	Projection 2016/17
Revenue	251.9	350.9	302.3	437.0	406.6	405.8
Tax and non-tax revenue	152.3	157.3	158.8	169.4	182.0	186.7
Grants						
Current	52.7	114.0	116.0	116.2	112.5	98.9
Capital	46.9	79.6	27.6	151.4	112.1	120.2
Expense	203.0	257.8	265.7	294.7	262.2	269.3
Gross Operating Balance	48.9	93.1	36.6	142.3	144.4	136.5
Net Acquisition of Non Financial Assets	56.6	79.1	28.0	156.0	134.6	130.6
Net Lending/Borrowing Requirement	- 7.7	14.0	8.6	- 13.7	9.8	5.9
Net Acquisition of Financial Assests & Liabilities (Financing)	- 7.7	14.0	8.6	- 13.7	9.8	5.9

Source: Ministry of Finance and National Planning

Reflecting the need to finance an urgently needed ongoing scheme to promote new initiatives in strengthen the private sector, and to address long outstanding arrears in relation to the government’s contribution to the retirement benefits scheme, the government will undertake new domestic bond borrowings in 2014/15 the first such borrowings for quite some time. This is

possible due to the progress in improve the finances and the reclassification of Tonga as only medium debt distressed as discussed in Section 5. The increase in borrowing by the Government in 2014/15 will of course be partly offset in the net financing component of the Government's accounts by a financial asset that represents the extent of net loans made through the revolving funds financed from the bond issue.

The estimated net borrowings necessary in 2014/15 is \$13.8 million. After that one off injection into the economy to address some critical priority needs the Government is expecting to return to more normal government fiscal position and finish the year with strengthened overall cash balances as well as a significant reduction in its net debt position (which includes changed in cash balances and ownership of assets in addition to changes in gross debt).

The fiscal indicators for 2014/15 imply that the fiscal outlook of the Government remains relatively tight and will be so in the short to medium term. The challenge for the Government is to sustain this fiscal stance of reducing its net debt over the longer term to help strengthen and build the private sector and therefore its revenue base in light of emerging pressures associated with the ageing population and continuing increases in competing demand for quality services from the public such as health and education.

In the face of those challenges, the Government's aggregate net borrowing requirement is expected to decline from its peak in 2014/15, by about \$23.6 million in 2015/16, from a net borrowing of 13.8 million to a net lending of 9.8 million; reaching \$5.9 million in 2016/17. The increase in the net borrowing requirement in 2014/15 reflects in a large part the impact of Government's new policy initiatives in the economic, social, and public sectors, through the establishment of the agricultural, fisheries, tourism and manufacturing fund concessional loan schemes to stimulate targeted sectors in the private sector, assistance to the education of Tonga's young leaders through a scheme to provide low interest loans to assist financing the costs of tertiary education, and the payment of long outstanding arrears in relation to retirement benefit contributions of Government of Tonga staff. The revolving nature of those loan schemes mean this will be a one off injection to assist these sectors with future low interest loans to be financed through the repayment of earlier loans.

From 2014/15, Government is also borrowing, on highly concessional terms, for World Bank and ADB budget support. In addition the project support from World Bank to fund urgent reconstruction of housing damaged in Ha'apai from cyclone Ian. The move towards splitting the assistance between grants and loans reflects Tonga's elevation from high to medium debt distress status consistent with the rules governing those banks' activities. As a result this sort of assistance moves from 100 percent grant to 50 percent grant, 50 percent concessional loan. It is, in part a reflection of the comparative strength of the Tongan economy and a judgment about how well the Government has been able to impose constraints on its fiscal activity over recent years.

Total revenue and cash grants (covering both projects and budget support) will increase by \$134.6 million compared with the 2013/14 estimated outturn of \$302.3 million. This increase is overwhelmingly driven by an increase in donor grants of \$124 million (which include current grants of \$116.2 million and capital grants of \$151.4 million) and an increase of \$10.5 million in tax and non- tax revenues. Grant receipts during 2013/14, are due to fall short of the budget estimate by \$50 million. In 2014/2015 projected grant from donors is \$267.6 million.

Preliminary data indicates that Government is projected a total GFS borrowing requirement of \$7.7 million for 2012/13 largely financed by a rundown of total cash balances (which include government funds, special funds and development fund) and the drawdown of the final tranche of the Chinese EXIM Bank loan. The estimated result for 2013/2014 is a negative net borrowing requirement of \$8.6 million reflecting the tight fiscal policies constraining expenditures by ministries and improvement in tax revenue collections. With donor grant assistance offsetting the

expenditures of those grants, this improvement in the budget result will allow total cash reserves to be rebuilt. Total expenditure is estimated to increase during 2013/14, and that increase is largely financed by donor assistance, including budget support from Tonga's donor partners.

The other notable feature of the 2013/14 estimated outturn data has been the deferment of principal repayments on the China EXIM loan. This repayment has been deferred for further five years.

6.2.1.1 Government Domestic or "Recurrent Budget"

The Budget Statement is presented on a GFS basis to meet international standards. Up until last year, the Statement used the 1986 format. This year is the first time to use the 2001 format. However, a key interest of Government is the total funds under its direct control provided from domestic revenue, borrowing and budget support. Before the introduction of the integrated budget this was referred to as the Recurrent Budget. This treats loan draw downs and repayments differently to the GFS. Repayment of debt is treated as "expenditure" and drawdown of loans as "revenue", while in the GFS2001 these are recorded as net lending or borrowing. Total Government controlled expenditure and revenue is thus better called payments and receipts to avoid confusion with the terms under the GFS.

The total Budget Revenue (Receipts) consists of (i) Domestic receipts that make up domestic revenue (taxes, charges, fees etc), transfers from other funds and sale of bonds, plus funding from revolving funds; and (ii) Budget Support. In section 5.3 and 8.4 the analysis on staff ratios and revenue to GDP, used "Domestic Revenue" as this shows what taxes etc government can raise to fund the budget.

Total Budget Expenditure (Payments) consists of (i) operating expenditure (the cost of running ministries); and (ii) other payments which include purchase of assets and equity, and repayment of debt. In section 5.3 and 8.4 the measure of expenditure used in the charts are "operating expenditure" as that is what is needed to keep the public service operations running. Staff costs are an important part of this.

This **Table 7** shows the significant contribution of budget support relative to domestic revenue. The share of staff costs compared to operating expenditure can also be seen (these are shown in charts in sections 5.3 and 8.4). The small cash surplus in 2012/13 and estimated larger surplus in 2013/14 (arising from deferral of the EXIM Bank loan repayments) will contribute to government cash balances. The balanced cash budgets (zero deficit) for the three years of the budget, will leave government cash balances in the government fund constant.

Table 7: Government "Recurrent Budget" Key Components

	2012/13 (p)	2013/14 Budget	2013/14 (r)	2014/15 (B1)	2015/16 (B2)	2016/17 (B3)
Budget Revenue (Total Recurrent Receipts)	179.57	198.80	198.88	235.33	225.30	229.26
Total Domestic Receipts	160.33	163.14	165.28	197.63	197.30	201.96
<i>Domestic Revenue (1)</i>	152.16	156.49	157.95	167.91	180.57	185.22
<i>Transfers and Bond Receipts (2)</i>	8.17	6.65	7.33	17.30	7.27	7.27
<i>Revolving Fund Receipts (3)</i>	-	-	-	12.42	9.47	9.47
Budget Support (4)	19.24	35.65	33.60	37.70	28.00	27.30
Budget Expenditure (Total Recurrent Payments)	178.62	198.80	193.70	235.32	225.30	229.26
<i>Operating Expenditure (5)</i>	160.01	177.02	177.84	206.15	200.31	208.15
Established & Unestablished Staff (6)	92.71	98.95	101.67	111.24	115.85	117.51
Purchase of Goods and Services (7)	23.90	22.59	23.41	27.68	26.83	32.88
Other operating expenditure (8)	43.40	55.48	52.76	67.23	57.63	57.76
<i>Other Expenditure/Payments (9)</i>	18.61	21.78	15.86	29.17	24.99	21.11
Cash Deficit/Surplus	0.95	0.00	5.18	0.00	0.00	0.00

Source: Ministry of Finance and National Planning

- (1) includes all taxes, fees & licences, entrepreneurial and property income (all Standard Categories for revenue 00 to 06) includes all transfer between funds and receipts from the sale of bonds, both new and roll over (standard category 07)
- (2) Transfer and bond receipts.
- (3) receipts to revolving funds, both for Government special activities, and private sector initiatives
- (4) budget support, both grant and loan (standard category 08)
- (5) all costs associated with the operations of the public service, including special government activity revolving funds.
- (6) includes established and un-established staff costs (category 10 & 11)
- (7) purchase of goods and services (category 14)
- (8) includes travel & communications (cat 12), maintenance & operations (cat 13), operations grants & transfers (cat 15), development duties expenditure (cat 16), debt management (part of cat 17 interest payments only), contingency fund (cat 18), pensions & gratuity (cat 19)
- (9) includes purchase of assets (cat 20), equity payments (cat 21), expenditure on private sector initiatives revolving fund (cat 22); debt management (part of cat 17 excluding interest payments)

Estimated payments during 2012/13 were slightly lower than their original budget estimate. Receipts in 2012/13 were substantially short of the original estimate, primarily caused by a lower than anticipated inflow of budget support from the World Bank and non-receipt from the European Union. Total Government payments are expected to increase by \$22.0 million, or 12.4 percent, during 2013/14. With new donor-funded initiatives planned. Government is committed to a balanced cash budget in the Government during 2013/14 and for the next three years.

7 CONCLUSION

The Government, in its last year of administration, is set to continue with the implementation of its development vision and objectives stipulated under its Tonga Strategic Development Framework (TSDF) with the theme to foster the partnership with people and all relevant key stakeholders to build the economy and society. In reflecting the past three and half years of the current administration, we agree that it was not a smooth journey as we encounter some challenges on the way and up to a stage tough decisions had to be made. With the utmost guidance and help of the Almighty God, the continuous commitment and persistent to go on, Government has been able to face and withstand these challenges and has achieved a lot in implementing its vision and development agenda. This has been indicated by positive results in most indicators of the Millennium Development Goals (MDGs) some of the key economic sectors of the economy. To name a few to highlight some of these key achievements include:

- **Infrastructure development:** In the construction sector, identified as the driving factor for GDP growth. The major development projects included the submarine fibre optic cable for better, faster and cheaper communication, the reconstruction response to the devastation from Niuatoputapu tsunami and cyclone Ian in the Ha'apai group, through the reconstruction of housing and strengthening of other sectors, the completion of the new hospital, the airport and runway development, more efficient energy sector through the implementation of renewable (solar plant) energy sources, water and waste improvement, wharf and airline development.
- **Private Sector development:** Government's investment in the economic sectors reflect positive improvement from a low base on agricultural exports, tourism receipts and earning, positive income earning from handicrafts, potential development initiatives in fisheries and manufacturing, continuous effort of Government to improve regulatory environment for private sector and business development including a more efficient and good governance SOEs.
- **Community development:** the investment in the development of sports, labor mobility scheme and the formal existence of social benefit scheme and the ADB/Japan piloting project in providing the day care services for the elderly and children with disabilities.
- **Tonga graduates from high risk debt distress to moderate level:** were due to the recognition of all the current work in reforms that Government is undertaking. The prudent debt and fiscal management and consolidation help to maintain macroeconomic stability.
- **Tonga graduates from lower-middle to upper-middle income status:** is also reflected in our GNI per capita continuing to grow faster than that of our neighbours

Going forward, Government will continue to build on the good momentum and progress of its reform initiatives. This includes the ongoing restructuring and reform to create a stronger public service. The continuous effort for each line ministries to adopt the enhanced corporate planning and budgeting, within a medium term budget framework, aiming for line ministries to deliver focus outputs and an efficient and effective allocation and utilization of Government resources to meet its objectives.

There remain key significant challenges such as the debt level which still requires to carefully manage, the public wage bill crowding the ministries recurrent budget, and the dependence on budget support in the next 3-5 years. In response, the Budget emphasize the national commitment of investing in the productive sectors of the economy to further revitalize growth, review and rationalize the public sector; and the Government recognition of increasing number of elderly people in our society who are disadvantaged or vulnerable and who need special care and attention.

We trust that this Budget will help to build and develop Tonga to a much higher standard with the good spirit of partnership amongst all key stakeholders.

8 ANNEX I: ECONOMIC AND SOCIAL DEVELOPMENT OUTCOMES AND OUTLOOK

8.1 Global and Regional Development

8.1.1 Global Highlights

According to recent updates from the International Monetary Fund January 2014 *World Economic Outlook (WEO)*, global growth strengthened during the second half of 2013 and is anticipated to grow at an annual growth of 3.7 percent in 2013/14 – revised from a broadly unchanged 3.6 percent in the previous *October 2013 WEO*.

The **United States** is expected to grow 2.8 percent in 2013/14 up from 1.9 percent in 2012/13 – mainly carried by final domestic demand supported in part by a reduction in the fiscal drag as a result of the recent budget agreement.

The **Euro Area** is turning the corner from recession to recovery as growth is projected to strengthen to 1 percent in 2013/14, but the recovery will be uneven as the pick-up will generally be more modest in economies under stress, despite some upward revisions including Spain. High debt, both public and private, and financial fragmentation will hold back domestic demand, while exports should further contribute to growth.

In **Japan**, growth is now expected to slow more gradually than what was anticipated in the October 2013 WEO projections, however temporary fiscal stimulus should partly offset the drag from the consumption tax increase in early 2014 and result in a broadly unchanged annual growth of 1.7 percent.

Growth in **China** rebounded in the second half of 2013, largely due to acceleration in investment. This surge is expected however to be temporary, in part because of policy measures aimed at slowing credit growth and raising the cost of capital.

Figure 8 : Real GDP Growth (annual)

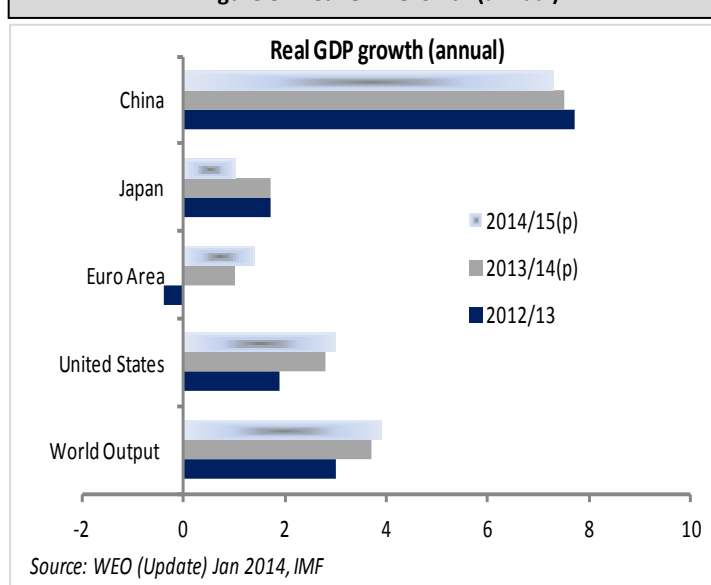
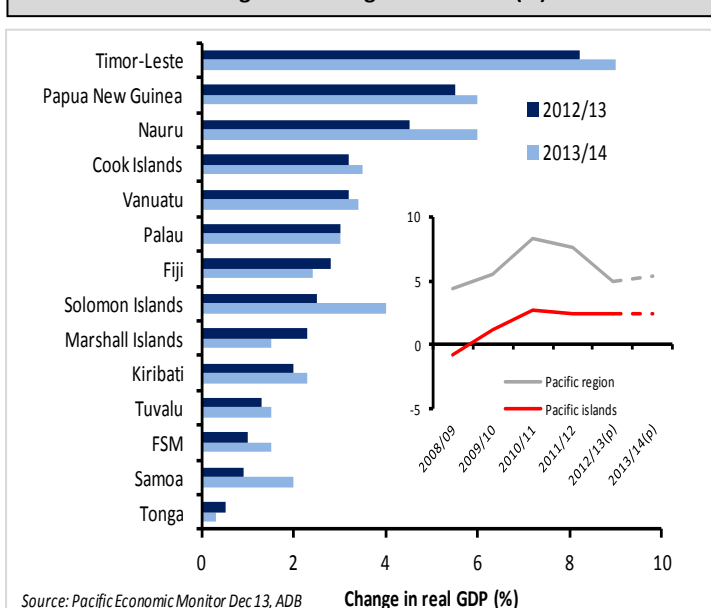


Figure 9: Change in Real GDP (%)



8.1.2 Regional Highlights

According to the ADB's GDP growth estimates, since 2010/11 the Pacific Islands'⁵ overall growth has appeared to have remained steady and is anticipated to grow 2.5 percent in 2013/14. Tonga however was one of six Pacific island countries anticipated to still grow well below that average.

One of Tonga's major trading partners, **Australian economy**⁶, from 3.7 percent growth in 2011/12 to a projected 2.5 percent in 2012/13, due to external (modest economic growth in China) and domestic (fiscal consolidation and subdued private consumption growth) factors. Inflation was trending higher due to increased housing, health, and education prices. The unemployment rate reached 5.8 percent in December 2013 and is approaching 2009 highs. The lower value of the Australian dollar, low interest rates, and improving business and consumer confidence, are seen as supporting economic growth in the country in the near term.

Tonga's major trading partner, New Zealand economy was seen to grow by 2.7 percent, on the average, in 2012/13 and 2013/14, supported by higher private consumption and earthquake- related construction activity. In an effort to cool down rising house prices and inflation pressures, the Reserve Bank of New Zealand implemented mortgage lending restrictions and signalled that the policy rate may start to rise next year. This policy move and a strong currency would likely put a dent on growth. Unemployment, especially among the Pacific labour force, remained stubbornly high

Figure 10: Australia Economics Indicators

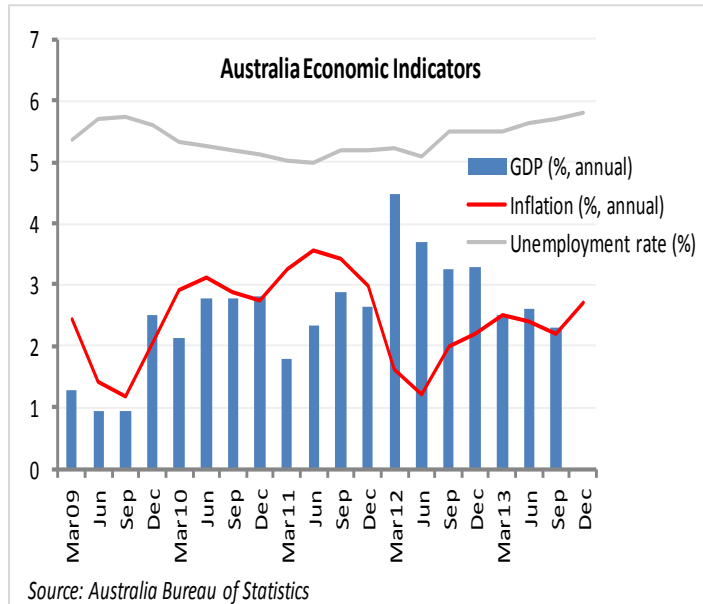
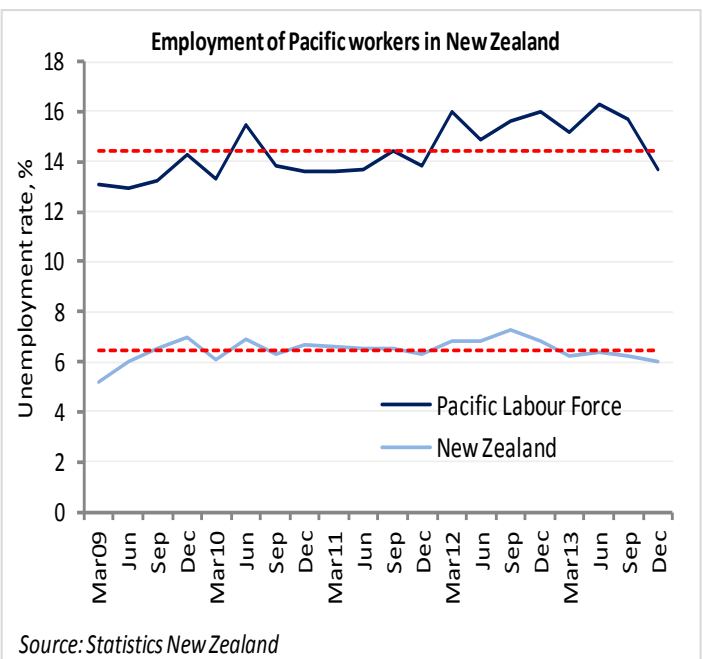


Figure 11: Employment of Pacific Workers in NZ



⁵ excluding PNG and Timor-Leste

⁶ Source: Pacific Economic Monitor Dec 2013 Issue, Asian Development Bank (ADB)

relative to the general New Zealand unemployment rate (6 percent); however it reached 13.7 percent in December 2013 – a slight improvement being just below the past four years average (*red dotted line*) of 14 percent per quarter

Tourist departures from Australia and New Zealand to major Pacific destinations⁷ have continued to grow over the past five years; but fairly steady from New Zealand and Australia has recently slowed, recording almost no growth in 2012/13 year-on-year – supposedly associated with the slow moderate growth in both countries mentioned earlier. However, recent data for the first half of 2013/14 have already started to show positive signs i.e. NZ tourists already with 66 percent and Australia with 56 percent of total last year's numbers. Tonga however, gets only 7 and 3 percent of these total departures on average per annum from New Zealand and Australia respectively, relative to other major Pacific destinations – Fiji being dominant with around 40 and 70 percent of total departures per annum.

Cash recorded remittances slightly picked up in 2012/13 for both the main recipients in the Pacific (Tonga and Samoa), in particular in Tonga as it grew by 5 percent. The 2012/13 pick-up for Tonga was followed by more than a 50 percent increase number of seasonal workers working in New Zealand after an almost 30 percent decline in the previous year. Recent data for the first half of 2013/14, cash recorded remittances showed a pick-up already year-on-year up by 5 percent. More details on revisions to Tongan remittance data is provided in section 8.5.

Merchandise exports to Australia from the Pacific fell by 13.4 percent (y-o-y) in January–August 2013. Papua New Guinea (PNG) continued to account for about 90 percent of total Pacific exports

Figure 12: Tourists Departures to Major Pacific Destinations

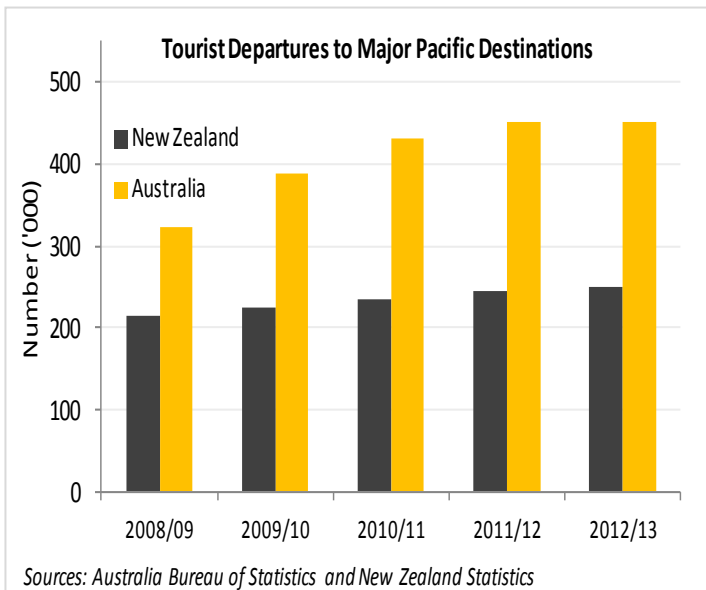
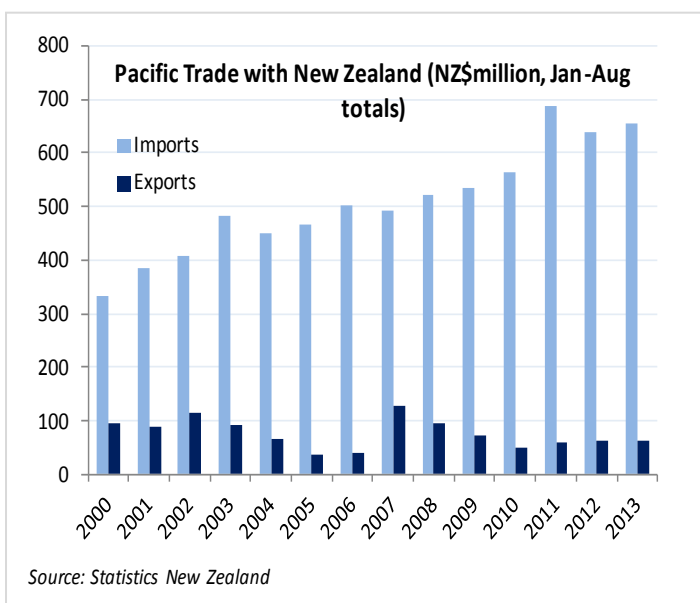


Figure 13: Pacific Trade with NZ



⁷ includes only the Cook Islands, Fiji, Samoa, Tonga and Vanuatu

to the country, but slower economic growth in Australia and lower international prices depressed the value of PNG's petroleum exports. Growth in Pacific imports from Australia was flat during the first 8 months of 2013 compared with a year ago. Thus, the Pacific's balance of trade with respect to Australia worsened from a surplus of AUD\$307 million in January–August 2012 to a deficit of A\$32 million in the same period of 2013.

Pacific exports to New Zealand increased by 1.9 percent in January–August 2013 compared with the same period in 2012. A sharp mid-year rise in phosphate exports from Nauru more than offset declines in food exports from Fiji and PNG. With Pacific imports from New Zealand (excluding transhipped goods) rising by 2.5 percent (y-o-y) in the first 8 months of 2013, the region's trade deficit relative to New Zealand widened to NZ\$592 million from NZ\$577 million during the comparable period in 2012.

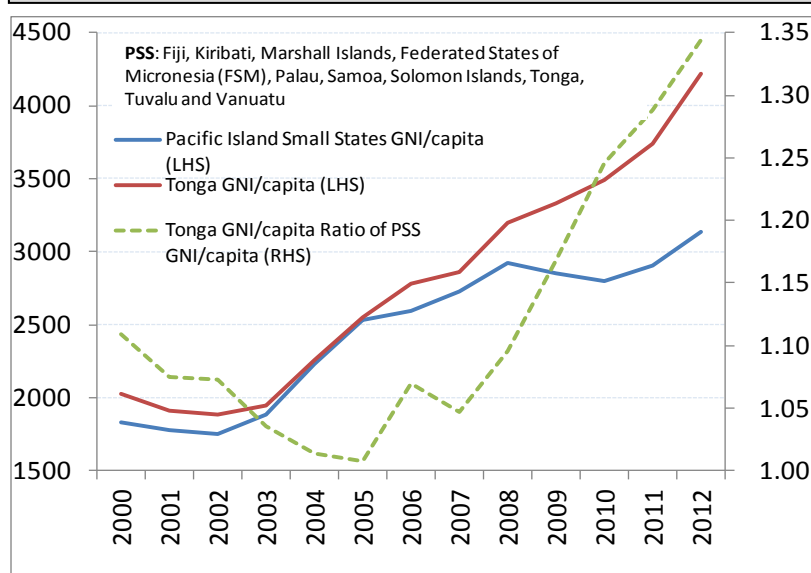
Fuel prices increased to a 16-month high in September 2013. Average fuel prices for the first 9 months of the year, however, are still 2.0 percent lower than in the same period last year. Food prices in January–September 2013 were 7 percent lower (y-o-y), and average prices of coconut oil and timber also suffered declines. Weakening commodity prices are expected to persist until next year, with expectations of more favourable supply conditions including some degree of stability in the Middle East.

8.1.3 Growth in Tonga compared to the region

The disruptions from the 2006 riots, and the recent slowdown resulting from the end of the loan induced stimulus, along with demands for improving standards of living, have resulted in concerns about Tonga's relative economic performance. Increasing engagement with Asia, has resulted in unfavorable comparisons between their performance and that of Tonga. In reality, however, these are not reasonable comparisons. Tonga is a disbursed archipelago of islands in the middle of the Pacific with a small population and limited

resources. The better comparison is with our neighboring Pacific Island Small States⁸ who face similar conditions to us. **Table 7** shows the growth rate for Tonga compared to the group of PISS. Over the full 30 years for which data is available, Tonga has grown at the same rate as the average for all PISS. Looking at 10 year periods, if it had not been for the significant growth set back from the 2006 riots, Tonga would have grown as well, or better, than the average for each of the 10

Figure 14: Pacific Island Small States and Tongan GNI /capita (Atlas method) (current USD) 2000-2012



Source: World Bank Data

⁸ Fiji, Kiribati, Marshall Islands, Federated States of Micronesia, Palau, Samoa, Solomon Islands, Tonga, Tuvalu, and Vanuatu.

year periods. For the period 2008-2012, Tonga as grown at 2.2 percent well ahead of the 1.4 percent average.

Table 8: Average Percentage Growth Rate Real GDP, Various Time Periods for Tonga and Pacific Island Small States

Period	1982-2012	1982-1991	1992-2001	2002-2011	2008-2012
Pacific Islands Small States	2.0	1.3	2.6	1.8	1.4
Tonga	1.9	2.3	2.6	1.4*	2.2

* for 2002-11 if Tonga growth for 2006 was 0 percent not -4 percent its period average would be 1.8

Source: World Bank Data

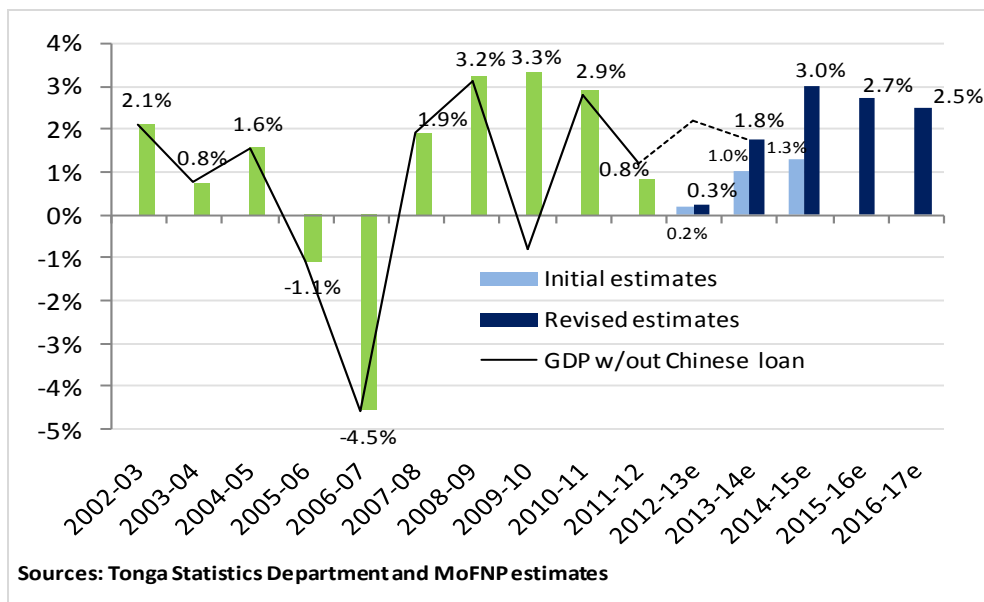
GDP growth rates, however, do not take into account the rate of population growth. Over most of this period Tonga's population has growth very slowly. For example, some countries in the Pacific would have to grow GDP by 2 percent per annum just to keep their average income per person constant. For Tonga, GDP would only need to grow by about a quarter percent per annum. Over the same 30 years Tonga's GDP per capita has improved from 40 percent of the average to some 130 percent of the average; showing, despite some fluctuations, a steady improvement. GNI per capita is also a useful comparison as it captures income earned from overseas which is becoming more important in Tonga. After falls in the first few years, GNI/capita recovered. From 2007, Tonga GNI/capita has raced ahead of the regions average, pushing Tonga from a level similar to the regions average, to 35percent above the average.

As shown in Section 8.8, Tonga ranks first among Pacific developing member countries that were included in the United Nations Development Programme's 2012 Human Development Report. Tonga has a Human Development Index of 0.710 (95th out of 186 countries) compared to the average for Asia Pacific Region of 0.683. The estimated nominal GDP for 2012/13 was \$806.9 million, giving GDP per capita of T\$7,792 placing Tonga now in the upper middle income group of countries for the first time.

While this additional information help to put Tonga's performance into a better light, Government remains committed to work with the people of Tonga to find new and innovative ways to continue to expand incomes and opportunities while better supporting vulnerable groups.

8.2 Recent Economic and Social Outcomes and Outlook for Tonga

Figure 15 : Real GDP Growth with and with-out EXIM China Bank Loan 2002/03 to 2016/17



The economy has recorded strong average growth rate of 3.2percent in three consecutive years (beginning in 2008/09), due in part to reconstruction of the Nuku'alofa central business district, large Chinese loan funded construction and other donor-funded aid projects.

As always anticipated, total growth slowed significantly with the completion of the China funded construction loans. Despite the end of this significant boost, the present estimate is that growth did not turn negative as was always a possibility. The estimated level of nominal GDP for 2012/13 was \$806.9 million, with GDP per capita standing at T\$7,792.

The objective of the loan funded construction was to raise growth faster than it would have been without this expenditure. This is what happened, during the years of the construction stimulus as shown in **Figure 15**: Real GDP growth including the loan funded expenditure was consistently above growth excluding the loan funded expenditure. Now that the loan funding has ended, the two growth rates have switch (as expected) before returning to the same rate in 2013/14.

Overall growth is forecast to strengthen sharply over the next few years; driven largely by the post-cyclone reconstruction efforts as well as continued strength in other sectors. Government wishes to maintain these more favorable growth rates, however, the country continues to face significant economic and social challenges from its vulnerability and cost disadvantages as a small multi-island economy far away from markets. Tonga is also challenged by its vulnerability to natural disasters ranked second most vulnerable in the Pacific. The devastation by Cyclone Ian to the Ha'apai Group of Islands is the most recent example of this. Reconstruction will cost some 10 percent of annual GDP. The associated increase in aid expenditure will, given the way GDP is estimated, result in a boost to growth.

These are some of the reasons why Government, under the new political chapter, is determined to respond to these challenges with a more efficient and effective public service to deliver better results, and by fostering stronger partnership with the private sector, development partners and the many stakeholders that can contribute.

8.3 GDP Sector Outcomes

Table 9 shows the actual estimates for real GDP growth for the three major sectors over to 2011/12. The figures for the other three years are based on provisional estimates. Given the poverty of data and the many unknown variables it is not possible to provide meaningful estimates beyond 2014/15. For the two outer years of the medium term budget framework 2015/16 and 2016/17 the trend for GDP growth is a return to the target 2.5 percent (see **Figure 15**).

Table 9: GDP Main Components (real growth rates)

	08/09	09/10	10/11	11/12	12/13e	13/14e	14/15e
Primary Sector (17%)*	-1.4	0.5	2.0	0.5	3.7	0.2	1.3
Secondary Sector (19%)*	12.9	11.6	5.5	1.2	-4.9	4.0	7.8
Tertiary Sector (54%)*	0.8	1.0	1.8	0.5	0.3	1.4	2.0
GDP**	3.2	3.3	2.9	0.8	0.3	1.8	3.0

e-preliminary estimates

**contribution to GDP.*

*** The 10 percent balance accounts for net tax and subsidies*

Sources: Tonga Bureau of Statistics, Ministry of Finance and National Planning

8.3.1 Primary Sector

Table 10: Primary Sector's Real GDP Growth (%)

	08/09	09/10	10/11	11/12	12/13e	13/14e	14/15e
Agriculture	1.3	-1.9	-0.3	3.5	2.2	0.4	1.2
Fisheries	-17.1	19.3	4.2	-9.6	17.9	-1.0	2.0
Forestry	3.0	-9.0	72.4	-25.7	-17.3	0.3	0.3
Primary Sector	-1.4	0.5	2.0	0.5	3.7	0.2	1.3

e-preliminary estimates

Sources: Tonga Bureau of Statistics and Ministry of Finance and National Planning

The primary sector includes agriculture, forestry and fisheries, which remains an important source of livelihood for the Tongan people in terms of providing food security, distribution of wealth and act as a social safety net during times of hardship. The primary sector accounts for around 17 percent of GDP.

Average growth rate for the primary sector in the past four years up to 2011/12 recorded 0.4 percent per annum. It however picked up strongly in 2012/13 at 3.7 percent on the back of strong performance from the agriculture and fisheries sector (while forestry continued to declined due to end of high sandalwood exports).

Despite a weak marginal growth of 0.2 percent estimated for 2013/14, it is growing from a strong base in the previous year. This is mainly driven by a slower growth in the agricultural sector from its strong performance in 2012/13 –driven in large part by the decline in squash exports which contribute over 30 percent to total real agricultural export earnings. This was mainly due to one of the main squash exporter pulling out of the industry; however levels could have dropped further had it not been for the support of the Government's Agriculture Marketing Fund (AMF). The expected decline in the exports of some main fish commodities including tuna and seaweed, are also suppressing activity in fisheries. These items mainly drove growth in the previous year. However, the primary sector's growth is expected to slowly pick up in 2014/15 and future years

mainly attributed to performances in squash, vanilla and yams in the agriculture sector; fisheries exports to pick up due to support provided from Government's new initiative of a fisheries exporting fund scheme.

Some key initiatives in the sector in 2013/14 and onwards include the continued Government's \$1 million AMF, the Australia funded Pacific Horticultural Agricultural Marketing Access (PHAMA) project's support for farmers including supplies of newly designed retail packaging for exports of frozen produce; the expected design and implementation of the Agriculture and Fisheries' sector plans plus other management plans aimed at conserving high-value fisheries species, re-planting programmes for sandalwood and coconuts and other on-going donor funded projects and activities that help maintain and fuel growth in the primary sector.

8.3.1.1 Agriculture Sector

Agriculture remains a largely informal sector in the Tongan economy, and therefore, the total contribution to the economy remains difficult to quantify. Latest GDP estimate indicates that the agriculture sector contributes some 14 percent to total GDP⁹. The agriculture sector is expected to continue experiencing positive growth of 0.4 percent in 2013/14 and 1.2 percent in 2014/15 compared to a stronger performance of 2.2 percent in 2012/13.

Export of agricultural produce has shown some pick up since 2009/10 and reached slightly above \$10 million and close to 10,000 tonnes of exports in 2012/13. However this still remains below the average of 18,000 tonnes worth \$15 million per year which occurred in the early 2000s.

Real growth for the agriculture sector still managed to stay positive despite a 12 percent decline y-o-y in squash exports¹⁰ in 2013/14 i.e. down from 4,330 tonnes, see **Figure 17**. This decline was due to the pulling out of the

Figure 16: Agricultural Exports 2008/09 – 2012/13

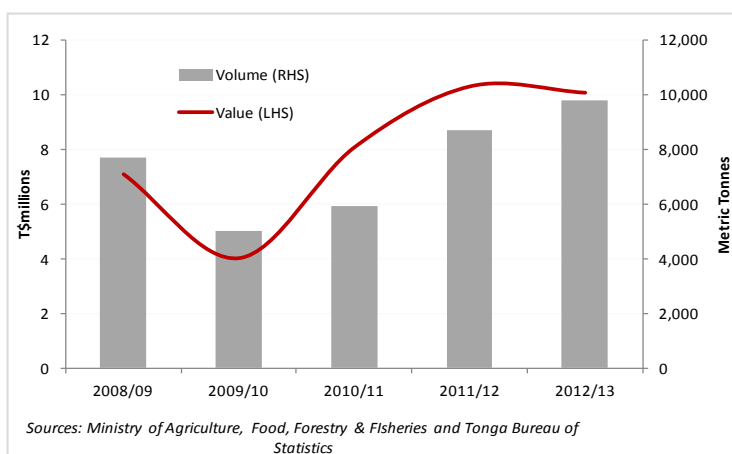
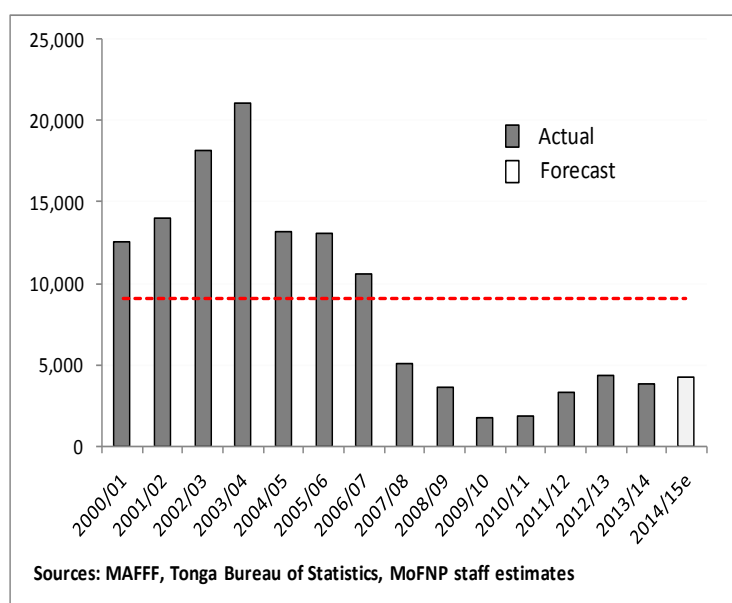


Figure 17 : Squash Exports 2000/01 to 2014/15 (tonnes)



⁹ GDP at market price

¹⁰ Squash exports account for more than 40 percent of total agricultural exports in real terms

largest squash exporter. However, if it was not for the support of the Tongan Government's Agriculture Marketing Fund¹¹ (AMF), squash exports could have further worsened to a 70 percent decline. On the upside however, remaining non-squash commodity exports are expected to continue to expand, holding up growth towards the end of 2013/14, at 2 percent. Major drivers include vanilla - picking up after a two consecutive years decline, yams in the first half of 2013/14 have more than doubled the past five years' average (200 tonnes), and watermelons reached an all-time high of 220 tonnes – strongest first six months performance in the past decade. Other agricultural exports continue to show strong growth from high bases last year such as coconuts (+9 percent) and kava (+6 percent). In addition, domestic production¹² (worth around 90 percent¹³ of total agricultural production) continues to experience minimal increases¹⁴.

In 2014/15, the outlook continues to remain positive for the agriculture sector as major crops such as squash is expected to pick-up in terms of volume by around 10 percent - this is more than 30 percent the past 5 years average of around 3,000 tonnes per annum. However, this still remains well below the long run average of 9,000 tonnes¹⁵ of squash exports per annum (see red dotted line in **Figure 17**). Total root crops production is also expected to slightly increase from an already high base, partly supported by the AMF initiative and exports of vanilla, kava and others are expected to maintain positive growth in coming years.

However challenges still remain for the agriculture sector, main ones include:

- ❖ increasing production costs
- ❖ quality control issues
- ❖ the need to strengthen capacity building and better communication across all stakeholders
- ❖ large size of arable land¹⁶ still remain idle, due to limited access
- ❖ insufficient and weak quality records of agricultural data to help better support policy decisions

Limited critical infrastructures to appropriately conduct essential services and improve productivity and production also remain a constraint, including:

- ❖ limited fumigation chamber space
- ❖ agro processing
- ❖ quarantine facilities
- ❖ poor agricultural roads
- ❖ irrigation facilities
- ❖ farm machineries
- ❖ research and post-harvest facilities

¹¹ Government's initiative to support farmers export their agricultural produce

¹² Includes both agricultural sales at the Talamahu market and roadside market sales

¹³ Both including market and non-marketed agricultural production

¹⁴ This is based on statistical adjustments and anecdotal information due to the difficulty in estimating domestic production with the available data. Growth is assumed to go hand-in-hand with population growth (0.25%)

¹⁵ Average for 2000/01 – 2013/14

¹⁶ Arable land (2011) is around 22% of total land in Tonga

In addition, there remains a pressing need for further strengthening of coordination and partnership efforts among all key stakeholders playing important roles in developing the agriculture sector.

Despite these challenges faced by the agriculture sector, the Tongan Government, its development partners and the private sector continue looking into ways of addressing them. Some key sector priorities that the Agriculture Sector Growth Committee has identified include: import substitution development (focusing on livestock research development, post-harvest storage and packing facilities), the continued provision of the AMF to help increase exports, conducting of the Agriculture Census to gather sufficient data for more evidence based policy decisions and the formulation of the proposed National Agriculture Sector Plan. In addition, key activities will continue under the Pacific Horticultural and Agricultural Market Access (PHAMA) project aiming at further developing the market access and pathways for Tonga agricultural commodities towards formal markets in New Zealand and Australia. Lack of proper packaging limits Tonga's competitiveness in key markets and thus has withheld Tongan exporters from exporting to formal and established markets such as supermarkets and formal retail points in major market destinations such as New Zealand, Australia and the US. Under the PHAMA project, carton boxes have been recently provided in which some exporting companies have started using to package their products for overseas markets – this is a major step to help improve quality and thus add value for the development of the sector in the long run.

8.3.1.2 Forestry Sector

The availability of data for proper monitoring and evaluation of the forestry sector remains a challenge. It often does not go into sufficient detail to identify forestry sector activities. However, recent estimates suggest the forestry sector contributes around less than 1 percent to GDP, mainly dominated by sandalwood production. The other main contributor is the work of Tonga Timber Ltd a government public enterprise (PE).

Real growth of the forestry sector dropped in the last 2 years mainly due to significant declines in exports of sandalwood after being heavily exploited. Growth is expected to however remain broadly unchanged in the next two years, but with some marginal growth in local firewood production¹⁷.

In terms of locally manufacturing forestry products, key challenges include access to finance for capital expenditures to run full capacity production, weak public-private partnership and the need to urgently accelerate re-planting of current tree resources to ensure sustainable production in future years. But despite these challenges, potential opportunities lie ahead for the forestry sector including, increases in product lines, biomass generation from waste, capacity building with implementation of training programmes, using coconut for timber particularly as it can serve demand for affordable housing and it can also be treated locally to add value. In addition for future growth, are completed activities, with assistance from SPC, that have assisted forestry sector development including: a completed draft regulation for sandalwood, mobilized mahogany tree seeds in Tonga, established agro-forestry demonstration area to facilitate mainstreaming of forestry into the agriculture curriculum and Tongan nationals successfully being trained in seed technology – these may help produce long term positive results in terms of agro-biodiversity being conserved, developed, promoted and utilized. In addition, with assistance from the FAO, the development of the floriculture industry continues to assist farmers and women village groups for income generation and food security in Tonga.

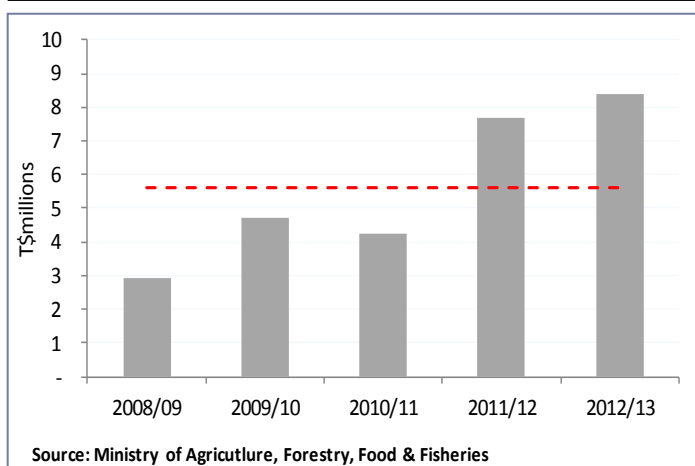
¹⁷ Assuming growth in local firewood production to be in line with population growth

8.3.1.3 Fisheries Sector

The fisheries sector's long run average contribution is around 4 percent to GDP¹⁸ however this has declined to around 2 percent in 2012/13. It is anticipated that the fisheries sector will experience a negative growth of 1 percent in 2013/14 compared to a strong growth in the previous year. This is largely due to anticipated declines in major fisheries exports i.e. tuna fell by more than half year-on-year to around 120 tonnes in line with an anticipated decline in the number of tuna foreign fishing vessels (24 to 6), while snapper declined from 48 tonnes last year but managed to stay just above the average of its corresponding periods in the past 5 years (35 tonnes). Seaweed exports plunged, even in its peak period (July-Dec) down to 33 tonnes from 293 tonnes exported last year. In addition, some low volume but very high-valued fisheries products that boosted last year's growth significantly dropped in the first half of 2013/14 year-on-year, for instance, live hard coral and shark fins exports – probably related to restrictions by the Chinese Government on the use of shark fins soup at formal occasions.

Total fisheries exports' value is worth almost \$6 million on average per annum (see red dotted line in **Figure 18**), in which the recent 2 years were above this average, deviating by around over \$2 million. This was mainly due to the peak periods of sea-cucumber and other marine exports. Over exploitation of sea-cucumber is likely to result in further contraction in catches.

Figure 18: Fisheries Exports 2008/09 – 2012/13



The main challenges which largely hinder the development of the fisheries sector include inadequate infrastructure, limited cargo space available for fisheries exports, lack of value added activities for fish exports, high freight costs, access to finance, high costs of production, poor sustainable management of fish resources, the need to enforce fisheries regulations with proper due diligence and the concern of protecting local fishing companies from foreign vessels fishing in local waters. In addition, subjective information suggests that a significant amount of fisheries exports

is sourced from Ha'apai. And due to the cyclone impact, it was reported around \$1 million worth of damage (mainly on to fishing boats, outboard motors and all fishing equipment) – this may add on to the negative impact on fisheries growth in 2013/14. This may recover to above average in future years should these damages be fixed.

Despite these challenges, a pick-up in growth by 2 percent is projected for 2014/15, mainly attributed to possible increases from fish exports as a result of support being provided to local fishermen under Government's new initiative, the fisheries export fund scheme (worth around T\$300,000). In addition, future positive growth may also be supported by the exemption of consumption tax (CT) charged on fisheries related imports which should help decrease cost of production, the implementation of aquaculture projects i.e. pearl farming and sea cucumber hatchery, increasing number of interested communities in the Special Management Area (SMA) program and further improvement of Monitoring, Control and Surveillance (MCS) activities and

¹⁸ Long run average from 1994-95 to 2011-12

coverage which can help increase observer opportunities not only for improvement of fisheries data but to also provide employment for locals.

8.3.2 Secondary Sector

Table 11: Secondary Sector's Real GDP Growth (%)

	08/09	09/10	10/11	11/12	12/13e	13/14e	14/15e
Construction	35.0	21.7	6.1	1.2	-9.7	6.2	13.0
Mining and Quarrying	16.8	137.5	3.2	37.9	-8.0	5.0	9.0
Electricity and Water supply	-4.6	-3.5	2.9	-1.1	1.5	1.6	2.0
Manufacturing	-0.2	-1.7	5.9	-2.7	0.9	1.5	2.0
Secondary Sector	12.9	11.6	5.5	1.2	-4.9	4.0	7.8

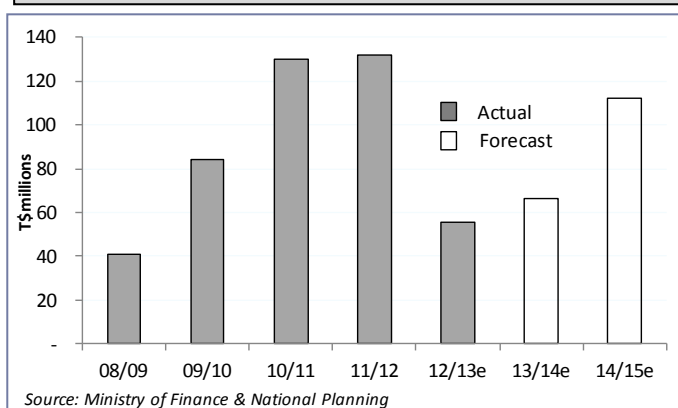
e-preliminary estimates

Sources: Statistics Department and Ministry of Finance and National Planning

The secondary sector contributes some 19 percent to total GDP. In association with the end of the construction lead boom, and the associated boom in quarrying activity, growth in this sector will be 3.7 percent in 2013/14 compared to the rapid growth in recent years. The main drive behind the secondary sector successes in recent years came from the reconstruction of Nuku'alofa CBD area and the rehabilitation of roads around Tonga. Looking forward, growth is again anticipated to pick up along with the new construction projects coming on line. Growth in the other sub-sectors is anticipated to remain relatively subdued as shown in **Table 11**.

8.3.2.1 Construction

Figure 19: Public Construction Projects 2008/09 – 2014/15



Growth in construction, and thus the size of its contribution to GDP, has varied quite a bit over recent years due to the large Chinese loan funded reconstruction of the Central Business District - Nuku'alofa and the national road constructions, which have been a major driver of GDP's strong growth particularly in 2008/09 and 2009/10. The ending of these projects (as had always been anticipated) was then associated with a slow-down in the construction sector's growth, down to a negative growth of 9.7 percent in

2012/13. Growth is anticipated, however, to recover in the following two years, particularly in 2014/15 where the post-cyclone reconstruction will mostly take place.

The recovery in growth for future years (see **Figure 19**) is anticipated to also be supported by other key public construction projects increasing through the pipe line, including the upgrading of the main international airport – Fua'amotu under the World Bank funded Pacific Aviation Investment Project (PAIP), energy projects including the phases 2 and 3 of the Tonga Village Network Upgrade (TVNU) project, road constructions under the Transport Sector Consolidation Project (TSCP) and the St Georges Palace Government office building. Private sector construction around Nuku'alofa remains active.

8.3.2.2 *Mining and Quarrying*

This sector is small contributing only 1 percent to GDP. Most activity is in quarrying where changes in activity have correlated with construction as aggregate is used for blocks and the large amounts of concrete and road works. The 8 percent negative growth in 2012/13, following the end of major road work projects, is likely to be followed by slow growth in the following years, closely associated with the key projects mentioned under the construction sector development. This growth may be supported by the re-opening of the recent privatized 'Ahononou Quarry'¹⁹, in 2014/15, after being closed for seven years. This is the only source of high quality aggregate in Tongatapu. There are a number of opportunities for the use of this aggregate including the resealing of the runway at Fua'amotu Airport which is now due for rehabilitation, as well as repair of a number of roads around the island. It is possible that this quarry could deliver up to 19,000m³ per annum of crushed aggregate for various projects. The establishment of the Road Maintenance Fund, funded through the fuel levy and vehicle licensing fees, should be a continued source of funds to generate demand for the output of this Quarry

8.3.2.3 *Electricity and Water Supply*

Electricity and Water supply account for a relatively small 3 percent of GDP but provide vital services to both the productive activities and peoples consumption needs. There are some difficulties in the measure of activity in this sector, since improvements in efficiency of distribution, which mean there is less wastage from leaks, may still be associated with increased consumption.

Growth in the electricity sector is expected to continue to be positive in 2013/14 from the previous year i.e. electricity production is expected to increase by 2 percent and consumption up by 3 percent year-on-year in 2013/14. And despite an increase in the average electricity price i.e. up by 6 percent in the first half of 2013/14 year-on-year to 0.93 seniti/ kilowatt associated with a 2 percent increase in diesel prices, the solar farm energy projects have helped maintain electricity prices below \$1 pa'anga per kilowatt up to date. Two large solar farm projects have been completed and are currently operating with a total size of 1.5MWh, meeting 6 percent of total power generation (4 percent in Tongatapu and 2 percent in Vava'u) and saving up to a total 740,000 litres of diesel imports (or worth \$1.3 million) per annum. Other energy projects, although their impact will take time to show much significance, are reaching to outer islands in terms of improved accessibility, clean and safe supplies should not be overlooked. Water sector is estimated to continue positive growth in 2013/14 due to on-going and increasing water supply installation/ upgrading projects across Tonga, in addition to more anticipated water consumption resulting from revival in building and road construction projects.

Through the Tonga Energy Road Map (TERM), projects are already on the ground to enhance Tonga's energy supply, reduce cost and improve efficiency of energy usage. This includes solar plants for Tongatapu, Vava'u, Ha'apai, 'Eua and the Niua, alternative options for the management of the fuel farm and supply of fuel, phases 2 and 3 of the Tonga Village Network Upgrade project and improving options for micro energy generation. Government continues to provide recurrent funding for streetlight maintenance and operations. There are also community solar power projects in operation in the outer islands.

¹⁹ This Quarry has been an important source of aggregate for the construction of sealed roads throughout Tongatapu, including the road between the Queen Salote Port and the Fua'amotu Airport. The current runway at the Fua'amotu airport was also sealed using this same material about 20 years ago.

8.3.2.4 *Manufacturing*

Manufacturing sector contributes around 6 percent to GDP, second to the construction sector as the largest contributor to the secondary sector. Government recognizes that manufacturing has limited room for growth due to the constraints imposed by small market size, lack of economies of scale, limited skills and capital. Some businesses, however, had been established. These nearly all cater for the domestic market, include food and beverages (bakery lines, beer, ice-cream, water and coffee); printing, furniture, construction materials, fiberglass, rain water tanks and local timber. A number of other areas, drawing more on traditional skills, include coconut oil, local handicrafts, including mats and tapa, carving, souvenirs, art designs which have high demand both domestically and internationally. A significant part of the trade in traditional goods, is associated with important life events, are part of the extended barter/monetary trade network between Tongans in Tonga and overseas. Some of the remittances may in fact be payments for the export of such goods. This also applies to food crops that are informally sent overseas by families.

Due to these limitations, future growth is anticipated to remain limited, but could be driven further with improvements in viable import substitution and specialized value added exports. There is some potential to contribute further to employment and growth through limited import substitution, and specialized exports utilizing agriculture and marine products, particular where value added is possible with small scale production.

Growth has fluctuated in and out of the positive territory over the last few years, however marginal positive growth is anticipated for 2013/14 and future years mainly due to new entrants into the local beer brewing industry and the increase in production of virgin coconut oil (VCO). Oxfam New Zealand is working with a local partner, the Tonga National Youth Congress (TNYC) to support rural communities in the whole of Tonga - providing locals with employment, skills and an opportunity to earn income. Currently 14 VCO sites operated by the end of 2012/13 and another 12 are expected in 2013/14. Government also initiated grant funds for the Manufacturing/ Handicrafts industry for communities in the form of Handicraft businesses and Tonga Made Products to help create job opportunities to generate income for families (43 percent of the fund has been released to 30 successful applications, the rest to be released before the end of 2013/14).

The saw-milling also showed positive growth due to high demand to supply electricity poles for the restoring and rebuilding of Ha'apai's electricity network. In 2014/15 and future years, growth in use of poles is expected to remain positive, again supported by continuing supplies of electricity poles required under the Tonga Village Network Upgrade (phases 2 and 3). The project aims to upgrade the power lines to every village on rural Tongatapu - that will add connections to more than 10,000 households.

Despite the improvement in manufacturing growth the influenced from the damage done in Ha'apai, from the cyclone will have a downward pressure on the total improvement in growth. Handicraft production has been disrupted following destruction of pandanus and root-crop inputs. World Bank estimates suggest handicraft production will be disrupted for approximately 12 months. Its pick up will be reflected in later years.

Government is also in the process of submitting to Cabinet, the Private Sector Strategy Plan Report done by the Commonwealth – to become the Manufacturing and Commerce's Sector Plan. This may help guide the sector's priorities and to maximize the contribution of manufacturing to Tonga's overall economic growth in the future.

8.3.3 Tertiary Sector

Table 12: Tertiary Sector's Real GDP Growth (%)

	08/09	09/10	10/11	11/12	12/13e	13/14e	14/15e
Wholesale and retail trade	4.3	-4.7	3.7	0.3	0.7	1.0	3.5
Hotels and restaurants	6.9	-4.4	3.3	-0.5	1.8	-0.5	3.0
Transport and communication	15.4	15.7	-2.9	0.5	1.0	3.0	3.0
Financial intermediation	-20.4	-2.7	2.9	-4.1	-5.3	4.0	2.0
Public administration and services	2.5	0.9	0.5	0.8	0.6	1.0	1.5
Ownership of dwellings	1.0	1.4	1.2	0.7	0.5	-0.4	0.4
Others* (8% of GDP)	3.6	1.9	3.9	4.5	2.3	2.4	3.0
Tertiary Sector	0.8	1.0	1.8	0.5	0.3	1.4	2.1

e-preliminary estimates

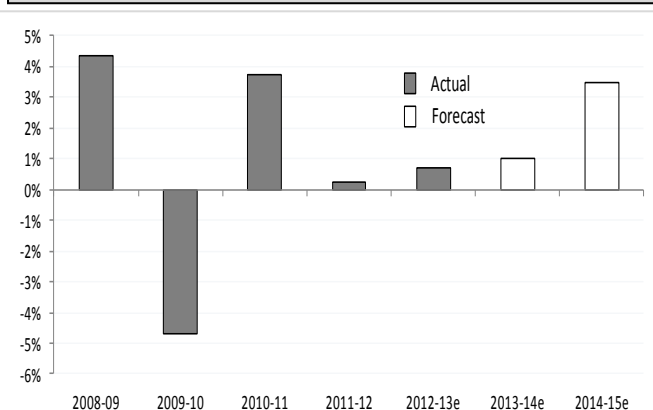
**includes small sub-sectors - real estate, private education & health, recreational and other community & personal services*

Source: Statistics Department and Ministry of Finance and National Planning

The Tertiary sector is by far the largest of the three broad sectors, accounting for more than half of GDP (54 percent). It contains several large sectors such as government administration, wholesale and retail trade, transport and communication, financial intermediation, as well as a variety of small items. These sectors include most of the activities associated with tourism, which is not a separate GDP sector, but covers sectors including transport, hotels and others.²⁰ In part due to its large size the rates of growth in the sector have been relatively stable, averaging out greater movements in the sub-sectors.

8.3.3.1 Wholesale and Retail Trade

Figure 20: Wholesale and Retail Trade Sector, real growth



Sources: Tonga Bureau of Statistics & MoFNP staff estimates

The wholesale and retail sector contributes around 10 percent to GDP. Around 46 percent of registered businesses are in the services sector and 45 percent are in the trade sector dominated by retail ventures which are identified, to be mostly owned by Chinese or by companies that include Chinese shareholders.

After a strong growth in 2010/11, growth slowed to 0.3 percent in 2011/12 before improving to 0.7 percent in 2012/13. It is anticipated to continue to grow at about 1 percent in 2013/14 associated with improving growth and

²⁰ Government plans to develop 'tourism GDP satellite accounts to help increase understanding of the impacts of this important business.

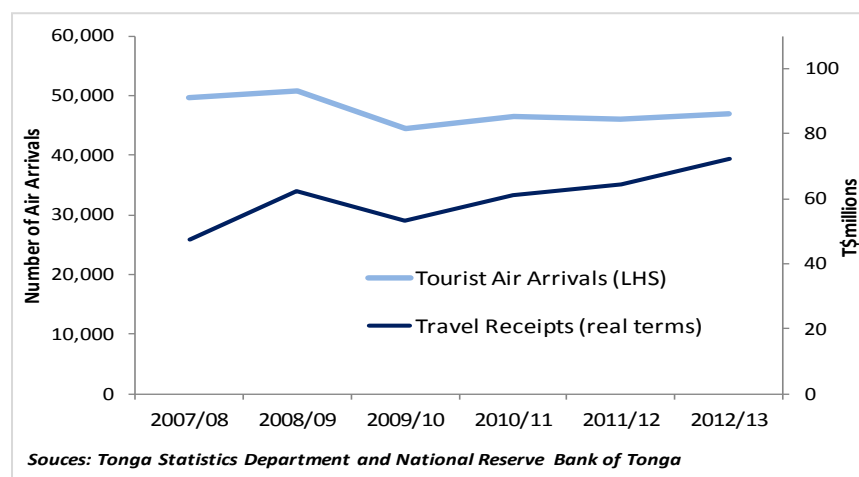
more in-kind remittances being directed in the form of goods through the retail sector. Challenge, however, remains in the growing importance of the informal sector of the wholesale and retail industry, due to in-kind “personal goods” being sold commercially at lower prices due to their non payments of duty and CT. This undermines tax revenue collection and established businesses’ performances. A number of (in particular newer) commercial establishments are also avoiding the payment of these taxes. The recently established Cabinet endorsed Commerce Sector Growth Committee (comprising of relevant private and public sector stakeholders) is intended to help identify and address these issues and challenges faced by the sector.

Pick-up in growth by around 3.5 percent in 2014/15 would largely stem from improving growth and anticipated business reforms – including the launching of the electronic business registry system (first in the Pacific) which will significantly reduce high costs associated with registering and establishing a business in Tonga, this may help encourage starting of new businesses. Tonga has been ranked 57 in 2014 by the World Bank (IFC) in Doing Business out of 189 countries in the world, up from 60 in 2013. Reviews to business and investment related regulations are also currently taking place aimed at improving the business and investment environment in Tonga (includes the Receivership Bill, Business Name Bill, Bankruptcy Bill and the Foreign Investment Act).

8.3.3.2 *Hotels and Restaurants*

The Hotels and Restaurants sector contributes around 3 percent to GDP. The sector experienced growth of 1.8 percent in 2012/13, which was in line with a slight improvement in

Figure 21: Tourism Receipts vs. Tourist Air Arrivals 2007/08 – 2012/13



tourist air arrivals by 2 percent and tourism receipts²¹ increased by 12 percent (real terms) up from the previous year (Figure 21). However, a slight decline of 0.5 percent is anticipated for the sector in 2013/14, mainly associated with a decline in number of tourist air arrivals: in the first half of 2013/14 air visitors declined by 20 percent compared

to corresponding peak period last year. This decline is likely to be partly due to the uncertainty in the domestic airline industry. Towards the end of 2013/14, performance is seen to be mixed i.e. based on the recent six months performance, travel receipts are likely to continue to increase while tourist air arrivals may end falling.

A number of major annual events take place in the second half of the year such as HM the King’s birthday together with the Free Wesleyan’s annual church conference to be held in Vava’u, and other annual church conferences in Tongatapu. These will hopefully help to keep visitor numbers up. Despite statistics for cruise ship tourist expenditures not being available, Tonga will

²¹ Note there is difficulty in distinguishing between tourism receipts and the remittances data, also tourism receipts are recorded from credit-card transactions which are still undergoing process to help distinguish spending by tourists and by locals using credit cards

pursue stronger developments for the cruise industry; there may be potential opportunities for more positive growth in future years.

Key challenges however still remain for the potential hotels and restaurants sector. These include the need to upgrade existing tourism products specifically tourism accommodations, tourist sites, and equipments for tour operators and tourism events, developments of new tourism culturally related products to target both cruise ship and air arrivals, capacity building and the stalling of New Zealand's funding for tourism developments.

But despite these challenges, a pick-up in growth is anticipated for future years, as the recent establishment of the Tonga Tourism Authority and its implementation of its business plan driving marketing efforts, in line with Government's Tonga Tourism Roadmap, better guiding the developments of the Tonga's tourism sector. In addition, the reconstruction of the International Dateline Hotel as the flat ship hotel for Nuku'alofa, once an agreement between Government and an appropriate investor has been made, may also help attract potential tourists and contribute positively to the hotels and restaurants sector.

8.3.3.3 *Transport and Communication*

The transport and communication sector consists of air, land and sea transports and telecommunication services, overall contributing around 6 percent to GDP. The sector is projected to grow at 3 percent in 2013/14 compared to a marginal 0.5 percent in 2012/13.

Main driver for the sector's growth in 2013/14 is anticipated to be from the communications sub-sector, supported by the recently launched fiber optic cable system. With both telecommunication service providers signed up for the cable's services, competition tensed leading to more affordable prices for faster internet and higher bandwidth capacity. For instance, one of Digicel's internet package deals fell by more than 30 percent, down from \$26.93 per gigabyte, while TCC's fell by more than half from \$24.75 per gigabyte. In addition, positive spill-over effects included benefits to local government, health and education sectors. Such as, seven district offices in Tongatapu were enabled to connect to the internet building in access for a more integrated local government, and a 50 percent internet connection discount to all primary and secondary schools in Tonga²² and the Vaiola Hospital, under a special offer supported by government. This is anticipated to help schools increase access to resources available for enhancement of students' researches, and also hospitals to access video conferencing and training courses that require fast internet.

Total number of private households with no access to the internet fell by over 20 percent in 2011 down to around 9,000 (55 percent of total) compared to over 12,000 (73 percent of total) recorded in the last 2006 census.

The transportation sub-sector is expected to continue growth in 2013/14 reflecting various activities in the domestic and international shipping services, air and road transportation. In terms of road transportation, there was a strong performance in the number of newly registered vehicles in the first half of 2013/14, over 40 percent higher than the past 5 years' average of more than 600 vehicles. Observations of on-line purchases of Japanese vehicles at relatively lower prices to local car dealers', suggest it may have contributed to this strong performance. Growth is also anticipated to improve from the road upgrading and maintenance activities carried out under the Transport Sector Consolidation Project (TSCP) funded by the World Bank and Australian Aid i.e. total of 171km of roads was maintained or rehabilitated in 2012/13. In addition, the government

²² Those registered with the Ministry of Education and Training (MET)

recently initiated a sustainable funding mechanism for the Road Maintenance Fund which will assist in maintaining roads in the future.

Growth in the domestic shipping services is expected to remain positive from the previous year (2012/13), but stronger in the second half of 2013/14 mainly supported by the introduction of a newly acquired cargo vessel – the Niuvākai. This may help improve Tonga's bulk cargo transportation to nearby Pacific islands including New Zealand. In addition, growth of the domestic shipping services will also gain from the urgent demand for transportation of aid equipment and materials to the Ha'apai group. Positive growth is also expected for international shipping services as cruise ships now seen potentially increasing in importance for the tourism industry.

In terms of air transportation, the withdrawal of Chatham Airlines in early March 2013 raised some uncertainty in the domestic as well as in the international tourist market over the status of the domestic airline industry in Tonga. This in addition to a stall in the availability of New Zealand aid funds aimed at developing Tonga's tourism industry, may have contributed to the 20 percent decline in the number of air visitor arrivals for the first half of 2013/14; usually this is the peak period²³. An overall decline in total air travel is possible this year. Air visitors particularly ones visiting friends and relatives (VFRs), due to the King's birthday and the annual Church's conference, may at recent levels. It is recognized that restoring confidence to the industry requires the assurance of all travelling customers that the new domestic airline is safe and reliable. The new domestic airline, 'Real Tonga', has therefore been subjected to the normal regulatory due diligence to ensure safe, more affordable, frequent and undisrupted flights for all the travelling public including tourists to the Kingdom. Anticipated positive growth for 2014/15 air visitors include the Royal Coronation and outer years include positive impacts after the upgrading of the current international airport under the aviation project (PAIP) and Tonga's hosting of the South Pacific Games.

8.3.3.4 Financial Intermediation

The financial intermediation sector contributes around 5 percent to GDP and growth is expected to be at 4 percent in 2013/14 compared to a negative growth of 5.3 percent in the previous year. The deterioration in 2012/13 was mainly due to ongoing tighter lending conditions by the banks creating financial difficulties for the private sector. However, a pick-up in 2013/14 and future years is to be expected consistent with an anticipated improvement in general economic conditions. This mainly includes competition from the newly introduced Pacific International Commercial Bank and an anticipated expansion of Tonga Development Bank Services. In addition, a temporary moratorium on principal and interest payments for loans in cyclone-affected Ha'apai introduced to assist impacted borrowers. The NRBT will continue to encourage lending through its monthly liaison with the banks.

8.3.3.5 Public Administration and Services

The Public Administration and Services sector contributes around 12 percent of GDP, making it the largest component of the Tertiary Sector. Growth is expected to be at 1 percent in 2013/14 and 1.5 percent in 2014/15 compared to 0.6 percent in 2012/13, mainly maintained by the budget supports expected to sustain expenditure. A 5 percent increase in civil servants' wages and

²³ Usually more than half of total air visitor arrivals fly in during the July-Dec period mainly due to Tongan families returning for Christmas holidays, visitors mainly from Australia and New Zealand leaving their winter seasons to take advantage of Tonga's warm weather for their holidays and also during this period sperm whales visit the Tongan warm waters for their breeding season and whale watching related activities peak

salaries also contributed to this growth. Future growth is expected to broadly lie between 0 and 2 percent consistent with government's key priority in maintaining sustainable fiscal consolidation for the current Medium Term Budget Framework (MTBF) to ensure that the Government is able to meet its current as well as future spending and debt commitments.

The public sector reform programs continue towards strengthening delivery, and ensuring better governance and accountability. These include Public Financial Management and Staff Performance Management reforms, the establishment of the Anti-Corruption Commission, strengthening of the Audit Department, increasing enforcement and compliance with the Procurement Reform Strategy & Regulations. Reforms in the public service are complemented by Public Enterprises reforms aimed at ensuring they continue to become more efficient and less of a burden to government finances while delivering better services to their customers.

8.3.3.6 *Ownership of dwellings*

Ownership of dwellings is about 9 percent of GDP. Growth is expected to decline by 0.4 percent in 2013/14 mainly driven by damages done to housings in Ha'apai but expected to slightly pick up in 2014/15 after post reconstruction efforts.

8.3.3.7 *Education, Health and Social Work*

The education, health and social work sector - excluding public health and education, included in public administration above - contributes around 3 percent to GDP. It is estimated that the growth rate for non-government education in 2013/14 will be at 1.0 percent compared to 2 percent in the previous year. Continuous support from Government and donors to non-government schools helps maintain growth in the sector, focusing on building capacity, human resources and upgrading of existing school facilities. The non-government health and social work sector is expected to continue growing in future years, mainly supported by the continuous work and support from the Mango Tree Center, the Alonga Center, the 'Ofa Tui he 'Amanaki organization, Tonga's Women and Children Crisis Center and others including private clinics. These services will remain vital to counter disability and health related services at all levels for Tonga. The expansion in social welfare to the elderly and disabled will help support growth in the social services sectors.

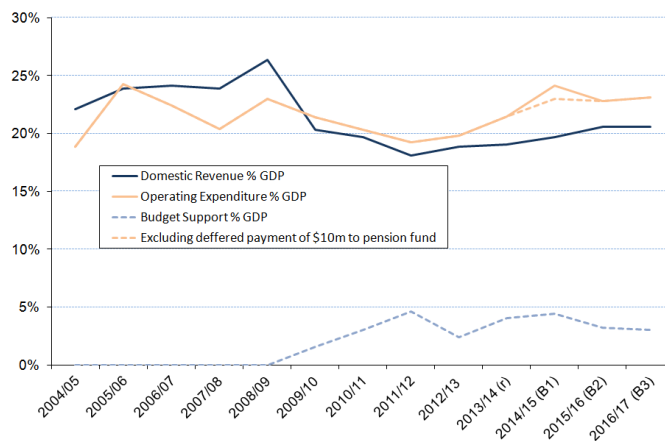
8.3.3.8 *Recreation, Cultural and Sporting Activities*

The recreation, cultural and sporting activities sector contributes around 1 percent to GDP, making it the smallest contributing sector to the Tertiary sector and growth is expected to remain positive reflecting special occasions such as the King's birthday in 2013/14 and the Royal Coronation coming up in 2014/15.

8.4 Fiscal and Debt Outcomes

8.4.1 Domestic Fiscal Position

Figure 22: Domestic Budget Relative to GDP (2004-05 to 2016-17)



Source: Ministry of Finance and National Planning

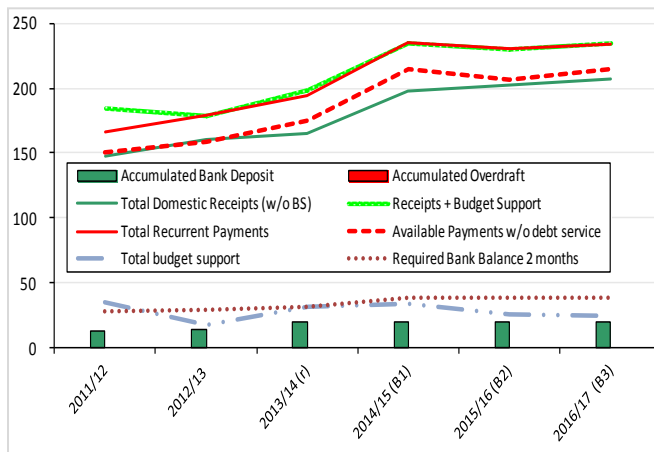
From 2001/01 until mid-decade domestic revenue (excluding receipts

from bonds and other funds) was a larger share of GDP (averaging some 22-24 percent) than operating expenditure - the cost of running the public service. Following the GFC domestic revenue fell below 20 percent of GDP, falling short of operating expenditure which has continued to rise. The increasing gap has been covered by budget support which has been running around 2.5 to 3.5 percent of GDP. This support has help avoid the need to cut priority government services. Over the MTBF revenue to GDP is expected to

recover gradually to just over 20 percent GDP. Operating expenditure will jump in 2014/15 to 24.1 percent of GDP due to costs such as the COLA carrying forward, and the paying off of \$10 million of the transfer value government owes to the retirement fund. Without this transfer value the increase in operating expenditure to GDP would only be to 23.0 percent. Over the next two years to level is forecasted at about 23 percent of GDP. These trends are shown in **Figure 22**.

Following the deterioration in cash balances prior to 2010/11 the 2012/13 Recurrent Budget generated a small cash surplus of \$0.9 million bringing the consolidated fund balance up to \$14.5 million retaining a level equal to one month of total payments (still below the objective of two months cover). This was accomplished by moderating expenditure to compensate for a short fall in budget support which only reached \$19.2 million down from over \$37 million in the preceding year.

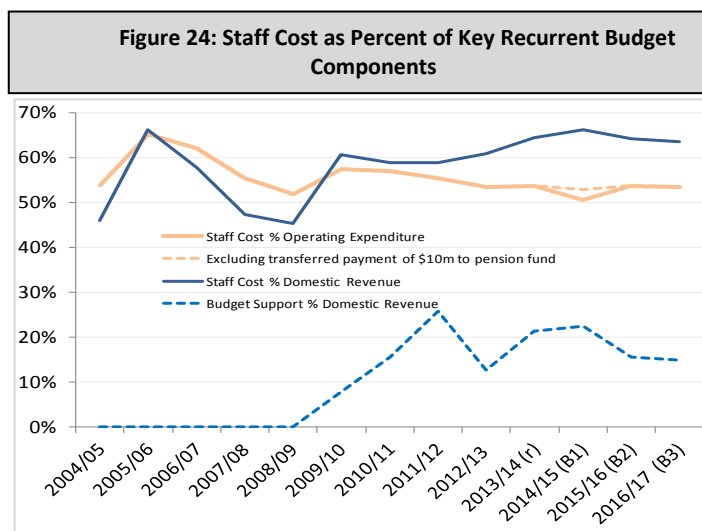
Figure 23: Domestic Budget Performance (2011-12 to 2016-17, Current \$ million)



Source: Ministry of Finance and National Planning

Compared to a planned balanced cash budget, 2013/14 is expected to generate cash surplus of about \$5 million. This results from the deferral of the EXIM Bank loan repayments for five years. This will raise consolidated fund to \$19.7 million or about 1.2 months cover of payments. Without this deferral, there would be a cash deficit of about \$4 million. No supplementary budget was thus required. Strong domestic revenue growth is anticipated with the growth in the economy. Budget support is only expected to fall off gradually, allowing operating expenditure to be maintained in real terms but fall off compared to GDP. A balanced cash budget is projected for each of the three years. This will

retain the cash balance at about one month cover of total payments. Government will strive to manage expenditure with care if there are any signs of lower than expected domestic revenue or shortfall in budget support. These trends are shown in **Figure 23**



Source: Ministry of Finance and National Planning

Government continues to seek ways of managing the costs of its operations. Staff costs are the single largest item and also particular sensitive given staff are humans and need to be treated with respect and dignity. Staff cost as a percent of Operating Expenditure, peaked in 2005/06, following the public service strikes and large salary increases. Since then they have trended down and been about 57 percent since 2012/13. Apart for a drop in 2014/15 (due to a jump in expenditure to repay the transfer value to the retirement fund). Without the payment to the pension fund, the ratio would have stayed at about 57 per cent

as it does over the MTBF. This is well above the target of 45 per cent.

On the other hand, since 2008/09 staff costs as a share of domestic revenue has increased from 45% to 65%. This is reflected by the failure of domestic revenue to keep up with operating costs, and the increased dependence on budget support, both to cover the gap between domestic revenue and operational expenditure, as well as debt repayments and other costs. Over the MTBF this ratio is projected to decline slightly. This is shown in **Figure 24**.

8.4.2 Public Debt Position

Government continues to recognize the importance of prudent debt management and of regular reporting for informed decision making. The Ministry of Finance and National Planning is working closely with development partners such as the Commonwealth Secretariat and the World Bank to strengthen debt management practices and to build local capacity both in technical areas of debt data and also related policy areas.

Government provides regular reporting on its debt position which is also available on the Ministry's website. The Budget Statement also provides an annual update, in this section which details the Government's debt position in June 2013 and also provides forecast levels for June 2014 and the medium term. The information covers external, domestic, on-lent, and guaranteed debt.

Given the revised debt sustainability ratios, since June 2013, Tonga is now improved from high to medium debt distress. This provides some room for prudent debt financing. However, this upgrade results in revised financing by the multi-lateral donors such as World Bank and Asian Development Bank from the prior 100% grant, to 50% grant and 50% loan component for projects and budget support.

The Government's fiscal position has also remained very tight with a heavy reliance on budget support from donors to supplement the recurrent budget deficit. Further, the Government has sought to reschedule its major repayment obligations due to the Export-Import (EXIM) Bank of China in People's Republic of China. In view of Government's draft Medium Term Debt Strategy, agreement has recently been made for rescheduling of these obligations with principal repayments for both EXIM Bank loans deferred for five years. This option will provide temporary

fiscal space but will cost Government more with the extra interest to be paid and higher principal installments once repayments start. Projected cost may also rise from escalation of the Chinese currency in the years to come against the pa'anga and other currencies.

With the current high external debt outstanding level, especially to China, and future proposed external financing, Government may continue to face difficulty in maintaining debt levels within the recommended levels. This is one of the reasons for Government's focus on promoting growth and improved revenue collection along with prudent public debt management, to help pay for future debt while mitigating against the vulnerability to shocks on the Government's debt portfolio. Government is also seeking to establish a debt sinking fund in which to place any revenue savings to help with future debt payments.

8.4.2.1 Total Public Debt

Total public debt at 30 June 2014 is estimated at \$368.2m (at 44 percent of GDP), a decrease of \$4.4m from June 2013 as shown in **Figure 25**. This is mainly due to a decrease in external debt by 0.53 percentage points of GDP, resulting from fluctuation of the borrowing currencies against the Pa'anga.

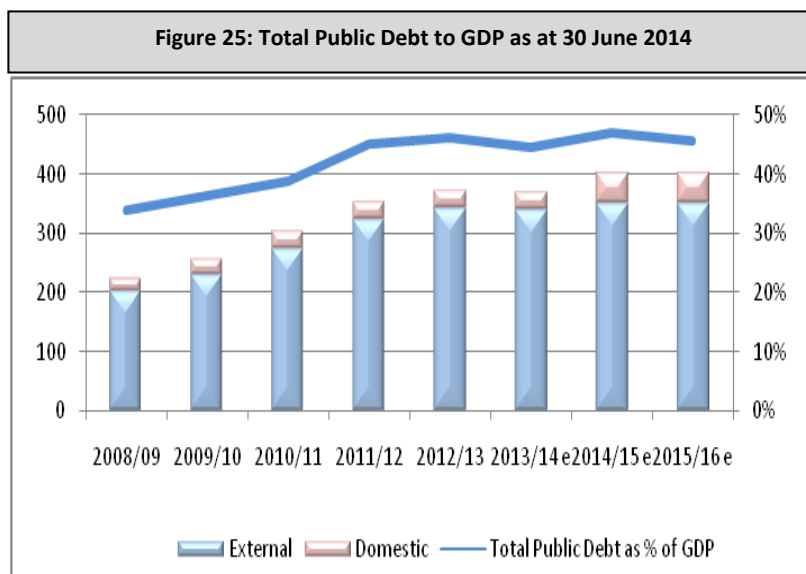
During FY 2013/14, total public disbursement is estimated at \$10.8m. This comprises of external loan disbursement for Budget support from World Bank in December 2013, the 50% loan component (\$4.8m); and domestic loan disbursement for bond rollover of maturing bonds (\$6.0m), as due during April 2014 (\$5.0m) and June 2014 (\$1.0m)

Total public debt from FY 2014/15 it is estimated to increase by 8.9 percent from June 2014 due to projected loan component of budget support from World Bank and Asian Development Bank, the loan component of the World Bank funded project for Ha'apai Housing Reconstruction (excludes future exchange rate fluctuations) and a new bond issue to be raised domestically to finance priority Government expenditures.

8.4.2.2 External Debt

Total external debt, at 30 June 2014, is shown in **Figure 26**, estimated at \$338.7m²⁴ (41 percent of GDP). Nearly two thirds of this is owed to EXIM Bank. The main change, since June 2013, was a decrease in the outstanding loan balance to People's Republic of China due to a depreciation of the Chinese Yuan Renminbi (CNY) against the pa'anga.

For details of the terms and conditions of the two major loans from China, the Nuku'alofa CBD Reconstruction project and Tonga National Road Improvement project and details of each project

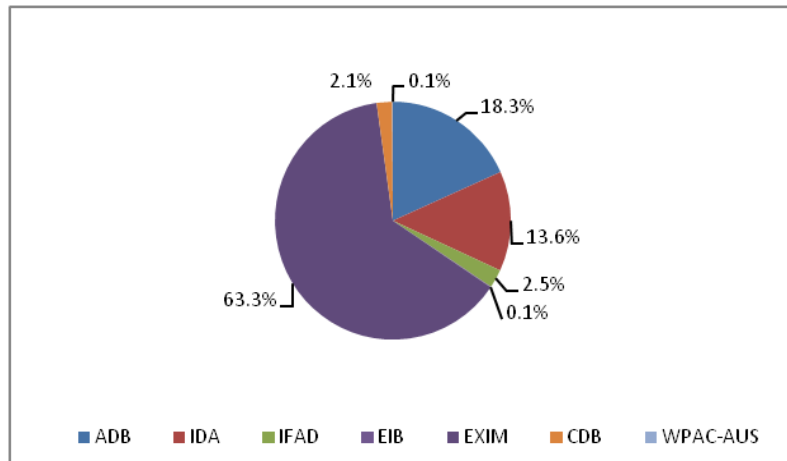


Source: Ministry of Finance and National Planning

²⁴ Excludes future movement of exchange rates from April 2014

fund allocation are provided in **Table 67** in the *Appendices*. Following long negotiations between Government and the Chinese authorities, EXIM Bank has agreed to defer repayment of principal for a period of five years. The first repayments are starting in 2018/19 with a significant rise in external debt service estimated at over \$12 million. **Figure 31** shows the long run impact of this deferment on external debt.

Figure 26- External Disbursed Outstanding Debt (DOD) by Creditor

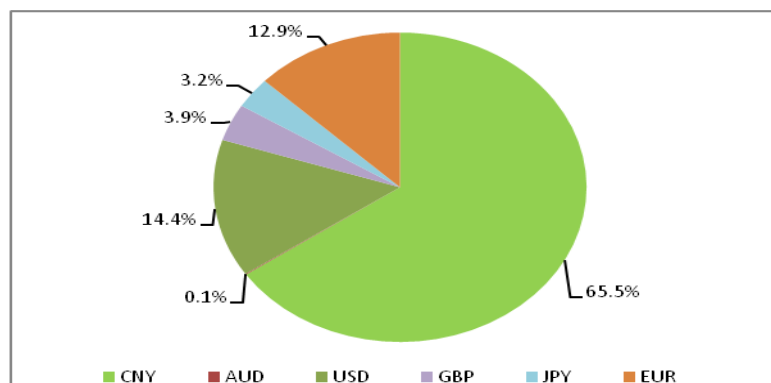


Source: Ministry of Finance and National Planning

8.4.2.2.1 Currency Denomination of External Debt

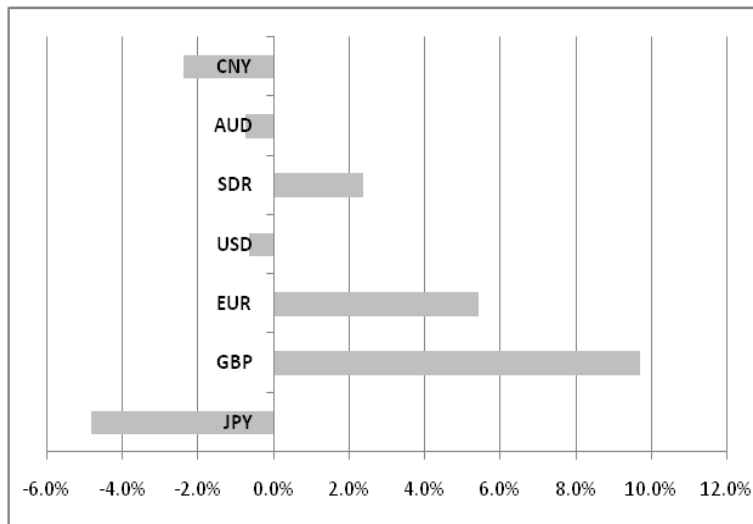
The main outstanding currency denomination of the external debt, as at 30 June 2014, as shown in **Figure 27** is estimated as (CNY) at \$221.7m (66%) and the Special Drawing Rights (SDR) and small currencies at \$116.4m (34%). During the last year, there was mainly a decrease in the CNY composition of \$6.7m (2.9%). The projected changes in value during June 2013 to June 2014 of the Pa'anga against the borrowing currencies (including SDR currency components) is shown in **Figure 28**.

Figure 27- External DOD by Currency as at 30 June 2014



Source: Ministry of Finance and National Planning

Figure 28: FC/TOP Exchange rate Trend, as at 30 June 2014

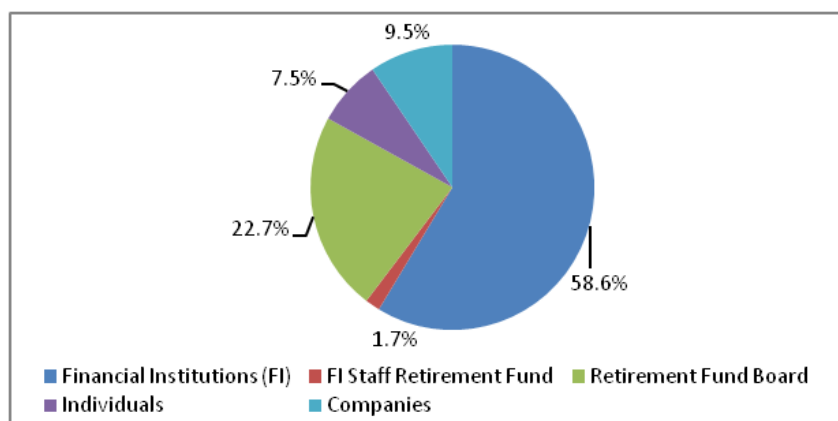


Source: Ministry of Finance and National Planning

8.4.2.3 Domestic Debt

Total Domestic debt, at 30 June 2014, is estimated at \$29.5m (3 percent of GDP); consisting only of Government bonds on issue. The shares held by different bond holders are shown in **Figure 29**, with Financial Institutions accounting for nearly 60 percent. Between June 2013 and June 2014, there has been a noted change in the bond holders, with an increase in holdings by Companies and decrease by Individuals of \$2.5m.

Figure 29 : Government Bond Holders (%) as at 30 June 2014



Source: Ministry of Finance and National Planning

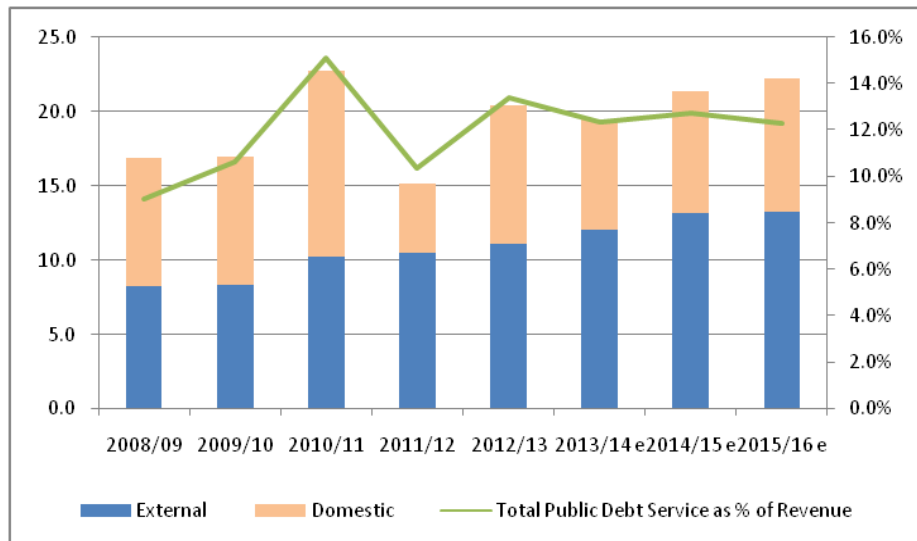
8.4.2.4 Debt Service

Total debt service (expenditure), for the year ended 30 June 2014, is estimated at \$19.5m, composing of external \$12.0m (62 percent) and domestic \$7.5m (38 percent). This is down from \$20.5m in June 2013, due mainly to lower payments due for bonds.

The total debt service is estimated as equivalent to 2 percent of GDP and in ratio to 12.3 percent of recurrent revenue and 10.3 percent of recurrent expenditure. The main repayment months for

external debt, are September (26 percent of total external debt service), and March (26 percent). For domestic loans the months are April (71 percent of total domestic debt service) and June (17 percent). There are no public debt payment arrears anticipated²⁵.

**Figure 30: Total Public Debt Service (TOPm) FY's 2008/09 - 2015/16
(including actual and projected)**



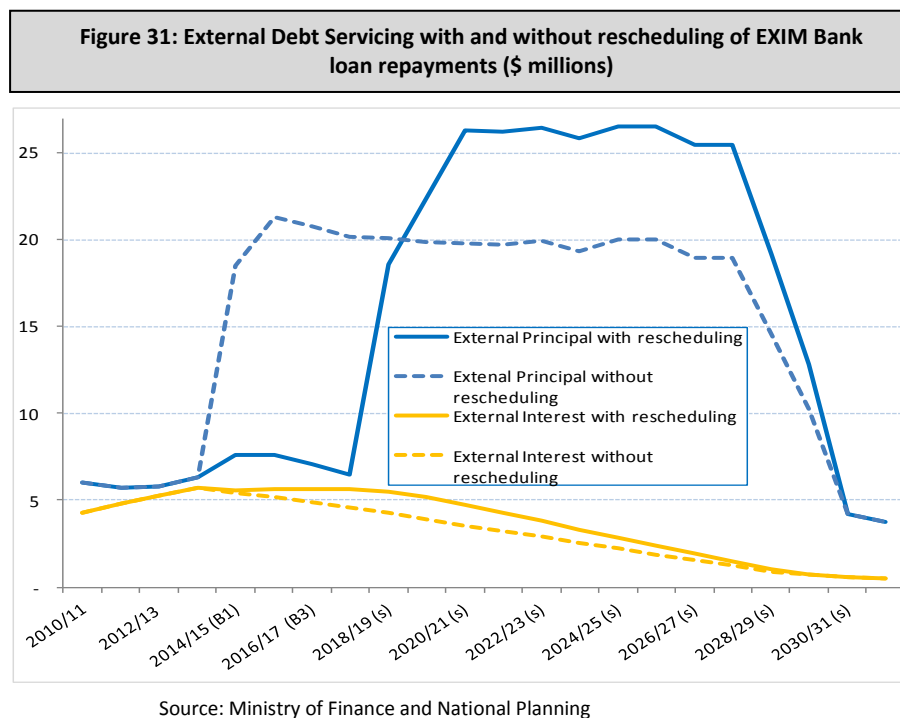
Source: Ministry of Finance & National Planning

With the deferral of the two EXIM Bank loan repayments, projected total public debt service increases by only \$1.1m due to the proposed Budget Support 50 percent loan component from WB and ADB. The deferred EXIM loan repayments will now start in 2018/19 with a significant rise in external debt service in 2018/19, estimated at over \$12.0m (further 1.4 percent of GDP); at a total of \$24.0m, .

Figure 30 shows the projected debt service, with external debt service based on the know new loans in the next few years, and the latest available exchange rates at hand and do not take into account any future appreciation of the borrowing currencies. The domestic debt service is based on current bond maturity (principal) and at weighted average (interest) of 4.93 percent on the total bonds on issue (\$29.45m), excludes any future domestic borrowings.

²⁵ Pending confirmation of Ha'apai High School loan reschedule with PRC

Figure 31 shows the change in external debt servicing resulting from the deferral of the principal payments by five years.



8.4.2.5 On-lent Debt

Total on-lent debt, at 30 June 2014, due to Government from various public and other enterprises is estimated at \$62.6m (7 percent of GDP and 18 percent of total external loans). The decrease of \$1.5m in the outstanding on-lent debt between June 2013 and June 2014 is mainly due to prepayment of the outstanding loan by TCC in August 2013.

The main sub-borrowers are shown in **Table 13**. OG Sanft Ltd.; MF Taumoepeau Ltd and Royco Amalgamated Co. Ltd are onlent from the EXIM Bank under Phase I of the Nuku'alofa CBD Reconstruction loan as signed in December 2010. Sub-borrowers of Phase II include Tungi Colonnade Ltd and City Assets Ltd have yet to sign with Government.

Total debt service from onlent loans (revenue), at 30 June 2014, is estimated at \$1.57m, for on-lent loan repayments from TDB, of \$0.42m (27 percent); TCC of \$0.92m (58 percent); Ports Authority Tonga of \$0.12m (8 percent) and Royco Amalgamated Co. Ltd. of \$0.11m (7 percent). The total on-lent loan payment arrears is estimated at T\$1.23m, for loan repayment due from OG Sanft at T\$0.69m (4 percent) and Taumoepeau at T\$0.54m (2 percent). Government is working with these companies to resolve the arrears.

Table 13 : On-lent Loan, as at 30 June 2014

Sub Borrowers	Jun-13 (\$m)	Jun-14 est. (\$m)
Tonga Development Bank	2.9	2.5
Tonga Communication Corporation	0.9	0.0
Seastar Star Fishing Co. Ltd	3.7	3.6
Janfull International Dateline Hotel Ltd**	11.3	11.1
Ports Authority Tonga*	0.7	0.6
Tongatapu Market Ltd	1.8	1.8
CBD Reconstruction Projects		
Phase I		
Royco Amalgamated Co. Ltd.	2.2	2.2
MF Taumoepeau Ltd.	7.2	7.2
OG Sanft Ltd.	10.3	10.3
Phase II		
City Assets Ltd.	6.8	6.8
Tungi Colonnade Ltd.	16.6	16.6
Total	64.1	62.6

*Does not include Vuna Wharf

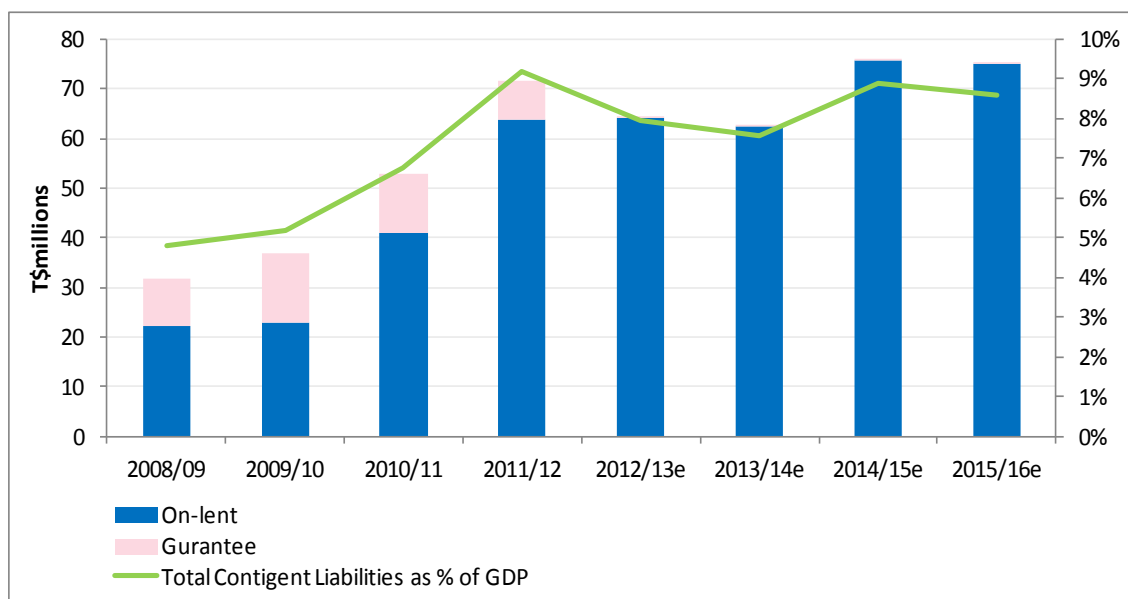
** Already reverted back to Government

Source: Ministry of Finance & National Planning

8.4.2.6 Guaranteed Debt

Total guaranteed debt, at 30 June 2014, is estimated at \$0.15m (0.02 percent of GDP and 0.04 percent of total public debt). The outstanding balance is for a bond issued by TDB. During the year, there were no new loan guarantees by Government and no payment arrears are anticipated.

Figure 32: On-lent & Guaranteed Loans to GDP (%) FY's 2008/09 – 2015/16 (including actual and

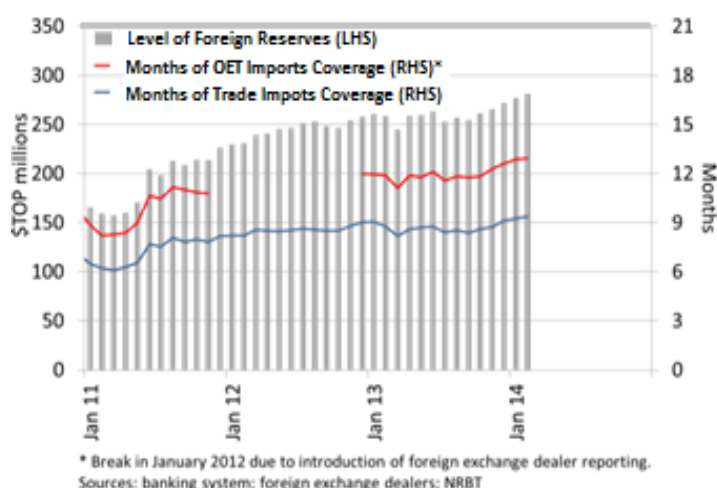


Source: Ministry of Finance and National Planning

8.5 Foreign Reserves and Balance of Payments Outcomes²⁶

8.5.1 Official Foreign Reserves

Figure 33: Gross Official Foreign Reserves



Gross official foreign reserves were \$281.1 million as at the end of February 2014, which represents a 6.8 percent increase so far in this financial year. The level is equivalent to a record 9.4 months of import cover, which is the highest on record and well above the NRBT benchmark of 3 months of imports

Exchange Rate Spreads

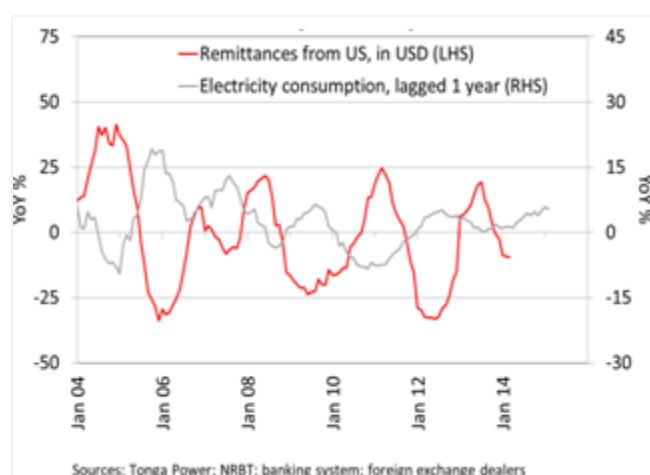
The exchange rate spreads charged by banks are higher in Tonga than in other Pacific countries. The NRBT has imposed limits on the spreads, the telegraphic transfers, since 2009.

The limits are subject to annual review.

8.5.1.1.1 Official Foreign Reserves Outlook

The NRBT expects the level of foreign reserves to increase over the remainder of financial year

Figure 34: Growth in US Remittances to Tonga and Tongan Electricity Consumption



2014, and again over financial year 2015. The forecast profile stems from a balance of factors:

- Remittances will probably be little changed, albeit supported by increased flows to Ha'apai families that have been affected by Cyclone Ian. NRBT research has found that the financial needs of Tongan residents are the key drivers of remittances, with growth in electricity consumption – a proxy for the financial security of households – usually leading to a contraction in remittance receipts. Research conducted overseas has also found similar results. Had it not been for Ian the NRBT would have forecast a slight decline in remittances.
- Imports payments will increase because: much of the NRBT's anticipated increase in bank lending will be used for imports; the Ha'apai reconstruction will drive a pick-up in imported construction materials; Tonga's real trade weighted exchange rate index has depreciated slightly over the past year, lifting the average unit cost of imports; and Tonga has a limited

²⁶ Source of data for this section is the NRBT.

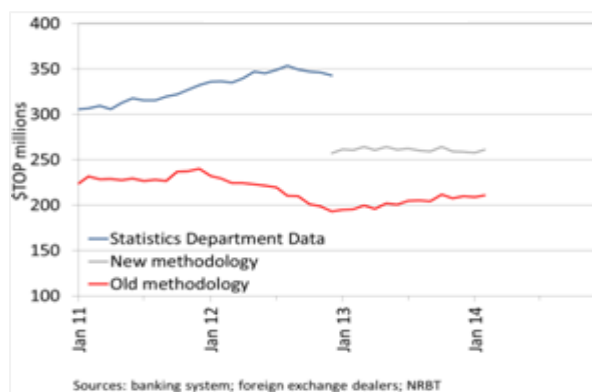
capacity for local import substitution. We expect that falls in global food and oil prices will offset these factors somewhat.

- Recently consistent rainfalls on Tongatapu will support export volumes going forward, as will some new areas of agricultural export activity. At the same time, goods that were previously shipped overseas might be redirected to Ha'apai to assist with relief efforts.
- Growth in travel receipts will be limited, following airline-related disruptions to the tourism industry.
- Official inflow from Tonga's development partners may rise, to assist with the Ha'apai reconstruction efforts.

Uncertainty surrounding the size and timing of government budget support poses the most significant risk to the outlook.

8.5.2 Foreign Exchange Payments

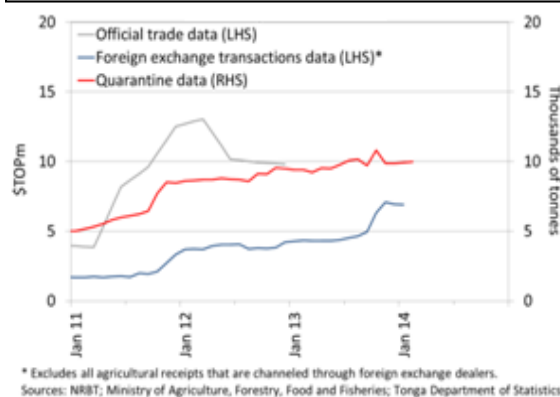
Figure 35: Import Payments (Rolling 12 months total)



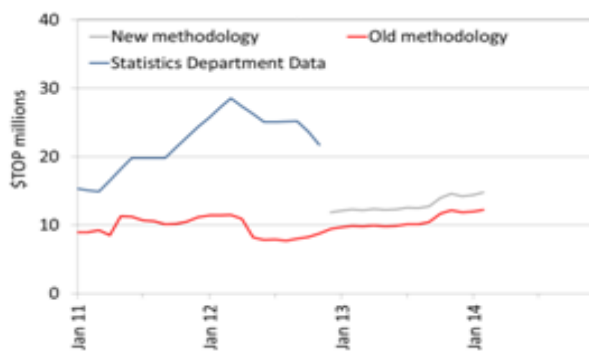
Year-ended merchandise OET adjusted import payments²⁷ have been little changed so far this financial year. The major components have been broadly stable also, with a slight increase in payments for oil and construction materials being offset by a fall in payments for retail goods. The stable outcomes are despite an increase in container registrations. The corresponding data from the Statistics Department are not yet available.

8.5.3 Foreign Exchange Receipts

Figure 36: Total Agricultural Exports (Rolling 12 months total)



²⁷ The Stats Data always captures more data than goes through the Banks. The NRB revised methodology relates to the improvements in methodology for recording remittances.

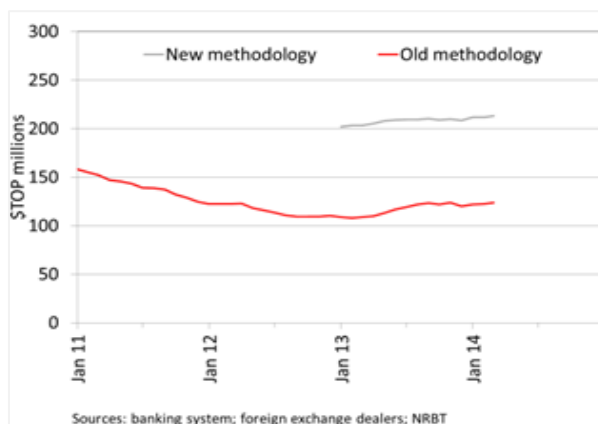
Figure 37: Export Receipts (Rolling 12 months total)

Sources: banking system; foreign exchange dealers; NRBT

Year-ended merchandise OET adjusted export receipts have picked up a little and are now at high levels by recent standards. The increase comes from a rise in agricultural exports, particularly for yams and coconuts, which are still benefitting from cyclone-related export disruptions in Samoa. A slight depreciation of Tonga's trade-weighted index over the past two years has supported export growth also.

NRBT has also been able to revise it remittances data to better capture the cash data: the old methodology is based on information obtained from the banking system only, some of which suffers from netting problems. The new methodology uses data from monetary transfer operators, to adjust for netting problems. These netting problems were becoming increasingly significant and help explain why Tongan cash remittances were not showing a recovery, as in similar countries, since the GFC. This information

help better show the source of income available to maintain standards of living

Figure 38: Remittance Receipts (Rolling 12 months total)

Sources: banking system; foreign exchange dealers; NRBT

in Tonga.²⁸

Remittances, which typically make up more than half of Tonga's current account receipts, have increased slightly over the past year. Increases from Australian and New Zealand sources have been offsetting declines from the US, where unemployment is comparatively still higher. As a share of Tonga's most recent official measure of gross national disposable income (for financial year 2012), remittances are 21 percent.

In addition to these cash figures, other recent improvements to the NRBT's methodology for measuring foreign exchange transactions, has also allowed it to form very rough estimates of in-kind transfers. These have always been known about but are hard to value. These in-kind transfers only cover instances where the remitter sends merchandise goods (not those where the remitter sends pays cash that the recipient receives in the form of goods). The estimate of these in-kind transfers averaged \$7.1 million per month over the year to December 2012, the most recent period for which the NRBT can construct an estimate (the estimates rely on official trade data from the Tonga Department of Statistics). Including these figures suggest that the wider definition of remittances may be closer to some \$300 million (or 30 percent of disposable income) per annum²⁹

²⁸ This also helps contribute to the decreased debt distressed levels for Tonga since remittance are now included in the international indicators: high remittances bring critical indicators well below danger levels.

²⁹ Calculating remittances will always be difficult. There is a complex exchange process between the Tonga people across a range of countries. For example, transactions which might normally be recorded as exports or imports, may stretch over several years making it very hard to match what is a 'pure' remittance and what is a payment for traditional

Most of the reduction in the current account deficit came from a lift in budget support from Tonga's development partners. The budget support funds are recorded as official unrequited transfers.

8.5.4 Capital Account and Unclassified Transactions

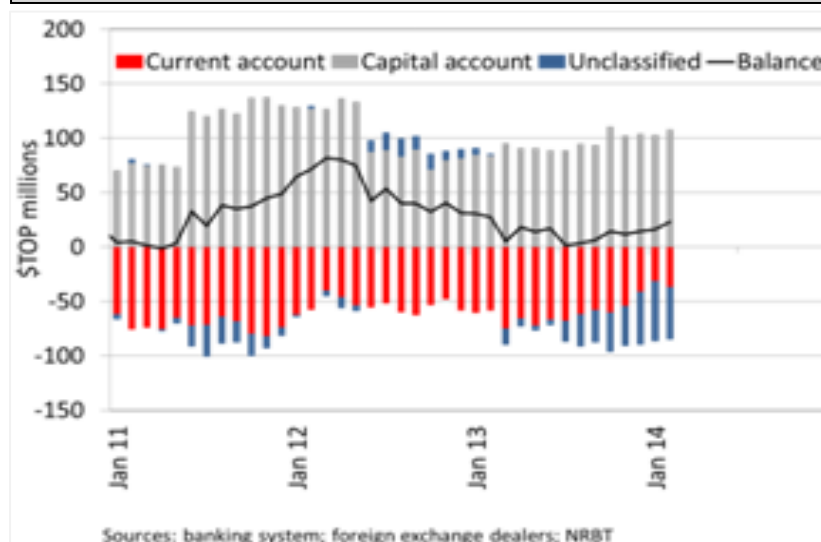
Net capital inflows totaled \$107.8 million over the year to February, most of which were private capital inflows in the form of interbank transfers. The transfers were higher than recorded over the year to June 2013, although the increase was offset partly by a fall in capital grants from overseas.

The balance of unclassified transactions was an average outflow of \$4 million per month over the year ended February 2013. The NRBT is investigating possible sources of the discrepancy.

8.5.5 Balance of Payments: Foreign Exchange Transactions

The balance of foreign exchange transactions, which is the closest to a full balance of payments available, was in surplus over the year to February 2014, wider than the surplus recorded over financial year 2013. The widening reflected a lower current account deficit and a higher capital account surplus.

Figure 39: Balance of Foreign Exchange Transactions (Rolling 12 months total)

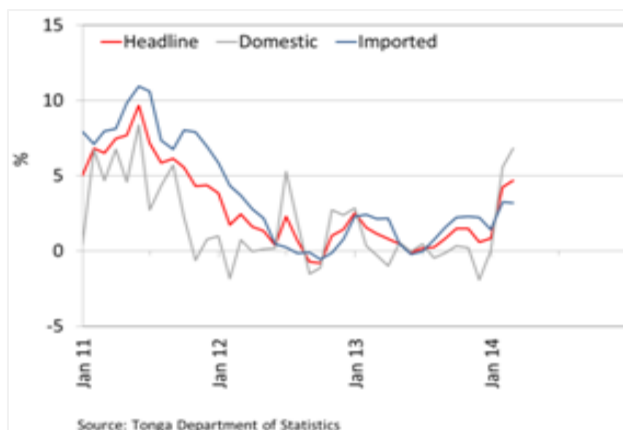


goods 'koloa' or food stuff sent on other occasions. Increasing financial sophistication also means that more cash transactions take place overseas to help cut costs associated with the exchange rate spread and other fees.

8.6 Monetary Outcomes³⁰

8.6.1 Inflation

Figure 40: Inflation (year-ended)



Recent Developments

Consumer prices rose over the 12 months to February 2014 by 4.7 percent. The increase was the fastest since September 2011 but below the NRBT reference range of 6 to 8 percent.

Prices of imported goods rose by 3.2 percent, compared with 2.2 percent at the time of the last monetary policy statement. The rise is broadly in line with the average of the past 5 years.

were for food, particularly for meat and dairy sourced from New Zealand. Prices for the imported clothing and footwear component also rose strongly, by 12.6 percent, after having been unchanged for 3 years. This component has a low weight in the consumer price index basket so its contribution to overall inflation was minor.

The New Zealand Dollar has been appreciating persistently against major currencies since the end of 2011, accounting for much of the recent rise in imported prices. The NRBT estimates that had exchange rates been constant over the past year, imported inflation over the 12 months to February would have been about 3 percentage points lower. Total inflation would have been almost 2 percentage points lower.

The imported inflation figure would have

Figure 41: Contributions to Inflation (year-ended Feb 2014)

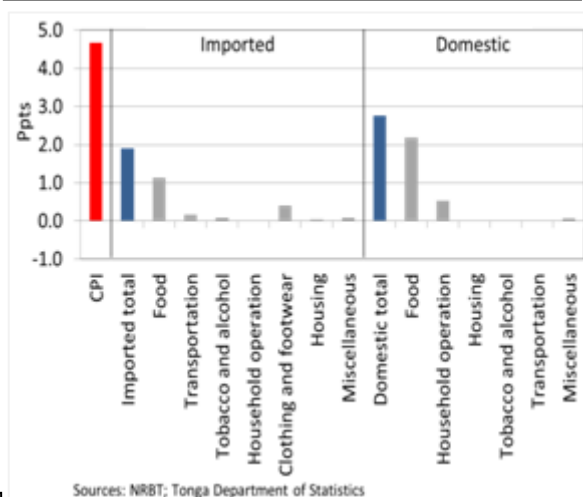
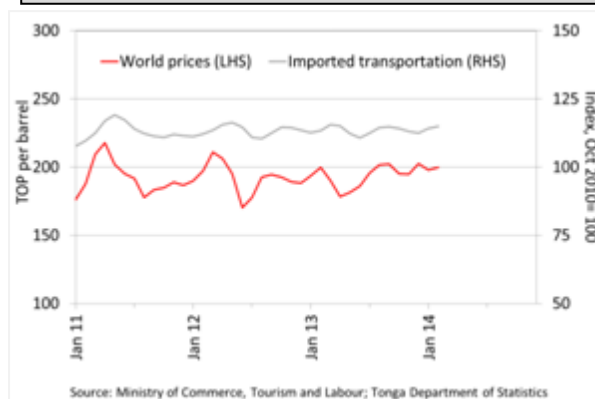


Figure 42: World Oil Prices (Monthly)



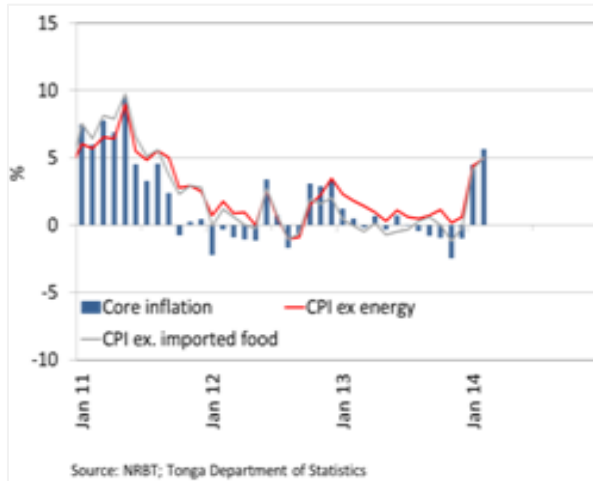
been higher if not for a leveling out of world oil prices. Measured in Pa'anga, world oil prices have changed little over the past year, keeping growth in imported transportation prices down.

The prices of goods produced domestically rose by 6.8 percent over the past year. Most of the rise owed to extreme price rises for vegetables, particularly tomatoes,

³⁰ Source of data for this section is the NRBT apart for inflation data from Statistics Bureau.

cabbage, and capsicum, which have coped poorly with the unusually hot and wet weather conditions prevailing recently.

Figure 43: Alternative Inflation Measures (year-ended)



Some portion of the increase in domestically produced goods also probably stems from the recent lift in imported food inflation. Imported and domestic foods are substitutable, and increases in imported food prices give sellers of local foods more room to increase their prices. Imported goods are sometimes also inputs for domestically produced foods, with price increases passed on to consumers. Domestic inflation outcomes have followed imported inflation outcomes closely for a long time.

The rate of core inflation, which excludes food and energy prices, increased by 5.6 percent over the year to February.

Outlook

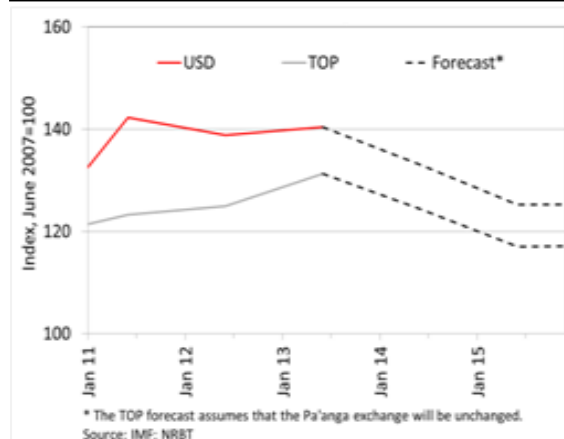
The NRBT projects headline inflation will fall to around 2.5 percent in June, before falling to 0 percent at the end of 2014.

The forecast is based on three key factors:

- The IMF expects world food prices to be about 5 percent lower over calendar year 2014 than in calendar year 2013, owing to an increase in world food supply.
- Market economists expect world oil prices to fall by 7.2 percent over calendar year 2014, due to a lift in global supplies amid easing tensions in the Middle East.
- Exchange rates are assumed to be unchanged.

As always, global economic uncertainties and weather patterns pose large risks to the inflation outlook.

Figure 44: World Food Prices (yearly)



8.6.2 Lending and Deposits Balances and Interest Rates

Interest rates on each of the key bank lending categories have fallen by between 36 and 71 basis points since the end of the last financial year. The weighted average rate on all bank loans has fallen by more, because the composition of lending has shifted towards lower-risk lending products. The general decline in interest rates has been encouraged by:

- the NRBT's expansionary monetary policy setting
- potential competition from the new Pacific International Commercial Bank
- an anticipated expansion of Tonga Development Bank Services
- a temporary moratorium on principal and interest payments for loans in cyclone-affected Ha'apai.

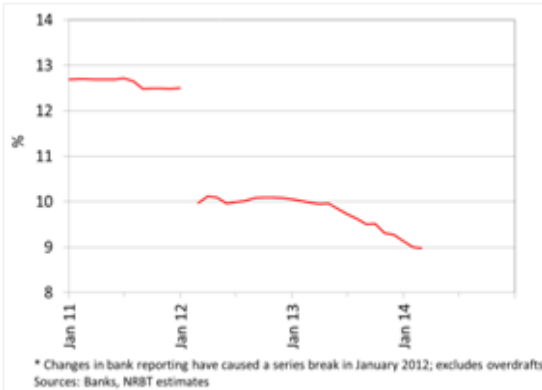
8.6.2.1 *Lending Rates***Table 14: Lending Rates (weighted average of all banks)**

Lending Rates (Weighted average of all banks)					
	Level as at			Change	Loan share
	12-Jun	13-Jun	14-Feb	Jun 13 - Feb 14	as at Feb 14
	% p.a.	% p.a.	% p.a.	bps	%
All	9.99	9.73	8.98	-75	100
Housing	9.03	9.02	8.65	-36	34
Other Personal	13.15	13.24	12.83	-42	18
Business	9.74	9.81	9.1	-71	28
Other	8.54	6.52	5.97	-55	20

Source: banking system

Figure 45: Lending Rates

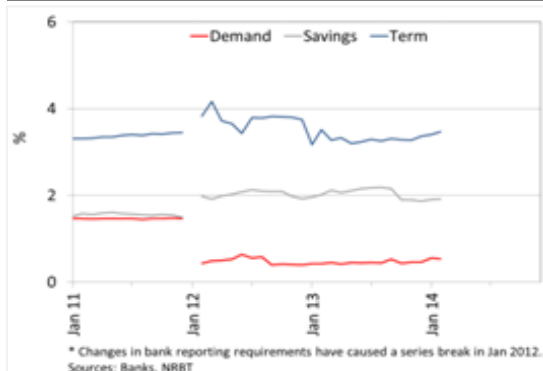
(Weighted average of all banks, all products,



Lending rates are now low by the standards of the past decade, although recent improvements to reporting requirements are complicating historical comparisons.

8.6.2.2 *Deposit Rates***Figure 46: Deposit Rates**

(Weighted average of all banks, all products,



The forces acting on deposit rates have been largely offsetting each other since the end of the

last financial year. The NRBT's expansionary monetary policy has pressured rates to fall, while heightened potential competition from Pacific International Commercial Bank and Tonga Development Bank would have pressured rates to rise. On balance, the weighted average deposit rate has been little changed. An increase in rates on demand and term deposits has compensated for a decline in rates on savings deposits.

The banks' official net interest spread has fallen by 20 basis points since June last year, to 3.4 percent. The difference between the highest lending rate and the lowest deposit rate has fallen by 4 basis points over that time, to 18.4 percent.

Total bank lending balances grew by 8.9 percent over the year to February 2014. The growth is the fastest recorded for five years and compares with a year-ended contraction of 3.7 percent over financial year 2013. Including loans extended by the Retirement Fund Board (RFB), South Pacific Business Development (SPBD) and Government of Tonga (both for building reconstruction and other), lending would have grown by 10.9 percent over the year.

Bank lending balances to households grew by 2.2 percent over the year to February, through a marked lift in non-housing lending. Still, the headline growth figures understate the strength of household lending at the moment because banks have been writing-off large quantities of loans that became impaired many years ago. The banks have been offering more attractive packages for borrowers lately and, as such, new household commitments are at high levels by historical standards. Also, after adjusting for the non-bank lending programs, year-ended growth in household lending would have been faster than 10 percent (though some of the extra household lending balances would ideally be classified under business lending).

8.6.2.3 *Lending and Deposit Balances*³¹

Figure 47: Household Lending Balances (monthly)

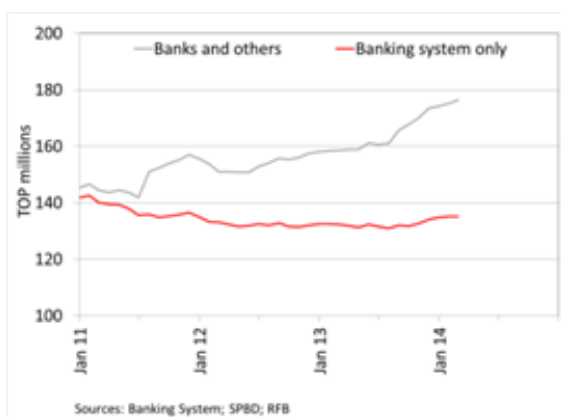
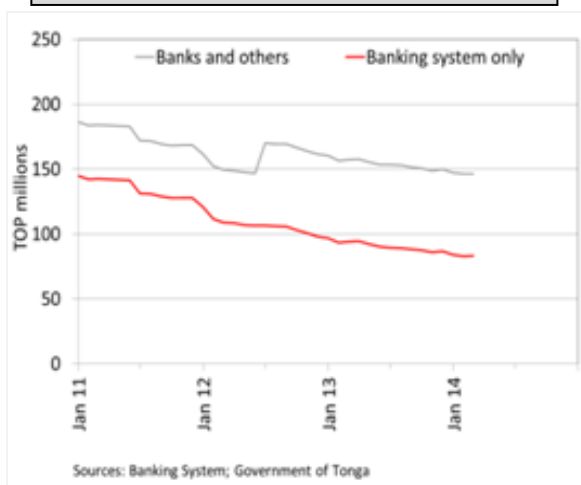


Figure 48: New Household Commitments from Banks (monthly)



Figure 49: Business Lending Balances



Business lending balances contracted over the year to February 2014, but more slowly than they had been over the previous five years. All key industries except for distribution and agriculture recorded falls. As with household lending, write-offs of impaired loans dampened the growth figures. Including the non-bank sources of lending, the contraction over the past year would have been slower.

³¹ This data represents Private Sector Credit Growth.

Much of the growth in total bank lending over the past year has come from large loans extended to two local public enterprises (classified neither as households or businesses). Some of the amounts committed remain undrawn.

The overall increase in bank lending balances and a lift in Tonga's net foreign assets have caused broad money balances to grow by 5.2 percent over the year to February. The components of broad money have, however, grown at very different speeds. The fastest growth has been recorded for the components that earn the lowest interest and are most suited for transactional purposes, consistent with the NRBT's expectations for faster economic growth this year. Term deposits balances have contracted markedly.

Table 15: Consolidated Balance Sheet of Depository Corporations

	Level			YoY change	
	12-Feb	13-Feb	14-Feb	14-Feb	
	\$TOPm	\$TOPm	\$TOPm	\$TOPm	Percent
Broad money liabilities	316.4	335.7	353.2	17.5	5.2
Currency in circulation	24.6	27.4	33.8	6.4	23.3
Demand deposits	94.9	108	132.7	24.7	22.9
Savings and Term deposits*	196.9	200.3	186.7	-13.6	-6.8
<i>equals</i>					
Net foreign assets	217.4	251.9	270.3	18.4	7.3
<i>plus</i>					
Net domestic assets	98.9	83.8	82.9	-0.9	-1.1
Gross bank lending**	268.8	257.4	279	21.6	8.4
Other***	-169.9	-173.6	-196.1	-22.6	13
* Also includes very minor amounts for securities other than shares.					
** Differs slightly from standard measures of bank lending by amounts classified as accrued interest.					
*** Includes mostly the banks' and NRBT's capital accounts, and their net claims on the central government.					
Sources: banking system; NRBT					

8.6.2.4 Outlook

When the moratorium on Ha'apai loan repayments expires, official measures of interest rates are likely to rise a little. However, taking a longer term perspective, the NRBT still sees a little room left for lending rates to fall, because after having removed the 100 basis point interest rate on Exchange Settlement Account balances in November 2012, the banks' lending rates have generally fallen by slightly less. Competition from the new and expanding banks will also support lower lending rates. Banks have indicated in liaison that significant declines from here are highly unlikely.

The NRBT is forecasting lending to grow by 10 percent over the current financial year, on the back of imminent draw downs of some large loan commitments, the expected fall in interest rates, and a general improvement in economic conditions. Similar growth is expected in financial year 2015, perhaps a little softer. The NRBT will continue to encourage lending through its monthly liaison with the banks.

If it eventuates, the anticipated increase in lending will drive further rises in broad money liabilities.

8.7 Social and Community Outcomes

8.7.1 Tonga Millennium Development Goals' (MDG) Progresses

Tonga is now looking beyond the end of the MDG journey in 2015. The MDGs had been integrated into the TSDF, as well as the line ministries Corporate Plans, so monitoring their progress provides a good indicator of high level progress against the TSDF. While sharing the sense of MDGs ownership with stakeholders and the public, consistency in the MDGs messages are also paramount.

8.7.1.1 MDG Acceleration Framework (MAF)

The MAF focuses on Goal 6C, the goal that is most off track, associated with an epidemic in non-communicable diseases, falling life expectancy and rising death rates. The state of NDCs is a national crisis. It is understood that MDG Goal 1 (Poverty) and MDG Goal 3 (Gender Equality and Empower Women) will also be considered in the framework of achieving Goal 6C

The Cabinet approved the MAF to be implement prior to the preparation of the MDG final report, 2015. There are five (5) high interventions outlined in MAF to drive progress on the 3 lagging goals; including:

- Improved Food Security
- Income generating opportunity for women
- Curative health service at hospital setting and disease specific risks factor screening
- Advocacy for healthy life styles (churches, workplaces, and communities)

The Government, through Ministry of Health, is taking the lead in working partnership with other relevant stakeholders, inside and outside of Government, to ensure the above interventions are fully implemented and better progress is made towards these last MDG goals by 2015' however, it is realized that a few will not reach the planned level.

The Government also acknowledges the support provided by UNDP and Australia throughout the lifetime of the MDGs. The UNDP organization is continued to support the implementation of MAF through financial assistance.

8.7.2 Health Performance³²

Government continues to provide significant support to the health services in the country through the recurrent budget to the Ministry of Health complemented by sector budget support from Australia. Most of the health services and community clinics are funded by the Government and only a few operates privately. The first output of the Ministry of Health for the next three years is "To increase their capacity to respond efficiently through quality preventive health services in their collective battle against NCD.

As seen with the MAF, Government places high priority on encouraging healthy lifestyles to address the high risks of the incidence of NCDs. It emphasizes that NCD are currently the main cause of mortality in Tonga. This has been verified by a study, which confirms a rising adult mortality and falling life expectancy in the last 10 years, in spite of a sustained low, under-five mortality. It is at a national crisis level with major increase in diabetics and heart conditions. The incidence of obesity is among the worst in the world. The key challenges in reducing NCD control relate to the risk factors that drive NCDs: poor diet, lack of physical activity, and the consumption of alcohol and tobacco. The NCD crisis is resulting in an increased number of people dying in mid-

³² All Health statistics come from the Ministry of Health

life. Between the period 2001-2004 and 2005-09, life expectancy for males dropped from 69 to 65 years and for females from 72 to 69 years.

Response from the Regional Dialogue on NCDs:

Economic Cost of NCDs was brought to the attention of the Regional Forum of Economic Ministers Meeting held in Tongatapu on the 3rd-5th July 2013. The meeting recognized the NCD crisis in the Pacific and the need for active participations of ministries of finance and economic development in mobilizing resources for proven initiatives to address it. This should include the use of taxation as a preventative tool. The governments need to encourage an effective 'whole of government' and 'whole of community' approach to addressing the crisis. This includes regional wide sharing of experience and lessons learning. The Tonga Government is in full support of these actions and is building them further into its response to the crisis.

8.7.3 Education Performance³³

Education is one of the most valuable assets a person can possess. Well-informed, educated, skilled, professional experienced and ethical people of integrity are fundamental to society's well-being. It is through education that individuals can achieve fulfillment, attain goals, and improve living standards. Education in Tonga encourages people to think and work for them, and to actively contribute to the welfare and development of their communities and society.

Based on the 2011 census, Tonga's literacy rate was reported to be 98.2%, which is higher than the literacy rate for the Asia Pacific of 94.7% - however, there are other indications that suggest the rate may not be this high beyond basic literacy. Based on the same survey, the percentage of population aged between 5 to 14 years old enrolled in primary school is 94.4%, while the percentage of population aged 15 and older with secondary education is 74.6%. The lower percentage of population with secondary school education is mainly attributed to the higher level drop outs in high school, especially starting from Form 6 (with most dropouts being males). The higher attendance by girls is represented in the active role of women in middle and higher management of government and many private businesses. The primary school student/teacher ratio has decreased overall, from 24.9 in 2010 to 21.2 in 2012, while the ratio for secondary school also decreased, from 14.9 in 2010 to 14.5 in 2012.

Based on the 2011 Census, the percentage of population with vocational/professional/TVET training was 9.6% (up from 8.1% in the 2006 Census) and the percentage of population with tertiary education was reported to be 16.1% (up from 2.7% in 2006 Census). Therefore, higher education has increased, with a significant increase in tertiary education compared to vocational training.

The Ministry of Education and Training is focusing on the education standards required locally and internationally. They focused on priorities activities to ensure that the education quality reaches the standard level required locally and internationally such as³⁴:

Year 1: 2013-2014

- Setting and achieving Performance Standards for Students, Teachers and Schools
- Strengthening Teaching and Management (Principals) Capacity

³³ All Education statistics come from the Ministry of Education and Training

³⁴ MOET Corporate Plan 2013/14-2015/16

Year 2: 2014-2015

- Advancing Curriculum Development
- Creating Safe, Conducive and Accessible Learning and Teaching Environments for Students

Year 3: 2015-2016

- Consolidating Higher Education
The Government committed to provide financial assistance through a Student Loans basis for student who wishes to further their study to the degree level but they can't afford the fees of student international. The objective of the initiative is to increase the professional skills and improve degree level for student in Tonga. The initiative anticipated to commence in the next financial year, 2014/15 with an amount of TOP1million. The administrative and operating of the loan will manage by the Tonga Development Bank (TDB) through their loan procedures. The initial stage of the loan is currently undertaken such as formulating a policy framework that will guide the operation of the funds. This work is comprising of Ministry of Education, Tonga Development Bank and coordinated by the Ministry of Finance & National Planning.

8.7.4 Labor Force Participation in Tonga

The Tonga economy and workforce continuous to have a large subsistent element making it difficult to measure levels of labor force participation and unemployment. Several measures of unemployment are calculated by the Census of Population and Housing. This means the most recent data on unemployment is from 2011, which is reported to be 1.6% which covers those who did not work but were looking for and available for work. If discouraged workers³⁵ are included, the adjusted unemployment rate is 6.5 percent. If including subsistence workers³⁶, on the grounds that these people might look for work if they believed cash work was available, the figure becomes 33.2 percent. This implies that subsistence workers constitute some 29% of the working population.

Subsistent worker, as in most countries, is a flexible term. Some of these people work part time for cash employment or sell excess produce. Because of internal remittances from those working in the formal sector, or overseas, the reserve wage for subsistent workers is higher than it would be otherwise. While this helps to maintain standards of living, it may sometimes act as a disincentive to actively seek formal employment. Social time, with family, church, kava clubs and other activities are also given high value. Sometimes there may be competition between these alternative social activities. Some question, for example, whether kava clubs are beneficial for social cohesion, or whether they keep men away too long from their families.

The number of Tongans on overseas employment schemes has increased from 833 in 2010 to 2,772 in 2013, an increase of 233 percent. The large increase is a very positive development, as remittances from Tongans on overseas employment schemes are a major source of income for many families. While most of the workers are involved in Recognized Seasonal Workers (RSE)

³⁵ Discourage workers are those who believed no work was available (e.g. due to weather conditions or unable to pay transport costs)

³⁶ Subsistence workers are workers who hold a self-employment job and produce goods/services which are mostly consumed by the household (e.g. growing/gathering produce or fish to feed the family)

scheme which allows Tongans to work in New Zealand's horticulture and viticulture industries, the largest percentage increase related to the Seasonal Workers Program (SWP) based in Australia. Under the SWP scheme, the number of Tongans increased from 46 in 2010 to 733 in 2012. The SWP is more attractive due to the higher minimum wage for fruit picking in Australia of AUD\$18million compared to NZD\$13million, or 57 percent higher factoring in exchange rate differences.

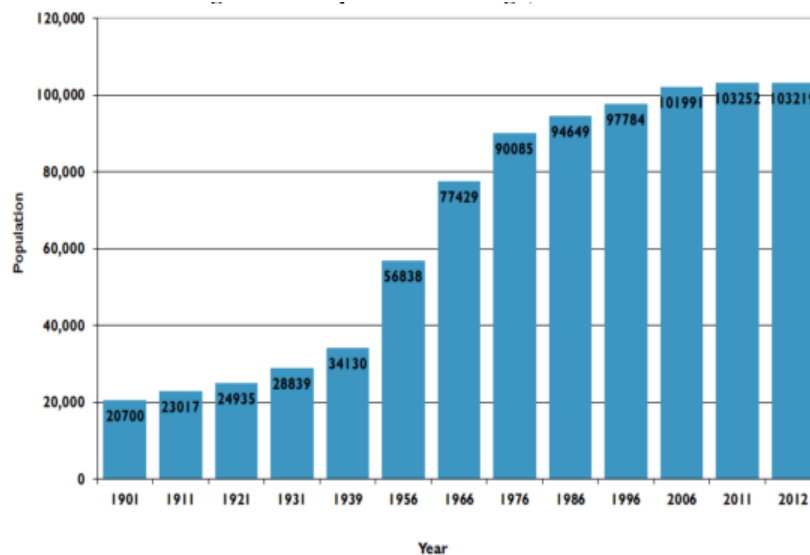
While these external sources of employment may further increase the reserve wage in Tonga, and make it difficult to find workers at certain times of the year, some business value the working skills and responsibility that these workers have gained overseas and bring to the Tongan workplace.

Through Ministry of Internal Affairs (MIA), it has been confirmed that the big challenges with trying to improve the RSE and SWP program is the coordination and communicating system. The government proposed to contract a counterpart/focal contact person in Australia and New Zealand to focus on coordinating of the Programs and also to responsible for any requirements may request by these two countries.

8.7.5 Changing demographics in Tonga

The population of Tonga is estimated to be 103,219 on the 30th June 2012, which is roughly five times higher than the population in 1901 (MOH Annual Report,2012).

Figure 50: Population of Tonga, 1901-2012



Source: MOH Annual Report,2012

The population of Tonga grew at an average annual rate of 0.2 percent from 101,911 (2006 Census) to 103,252 (2011 Census). Despite a total fertility of about 3.8, the small actual increase reflects the large and continued net out migration from the Kingdom. Tongan household increased 3.4 percent in total from 17,462 to 18,053 resulting in an insignificant fall in average household size from 5.8 to 5.7 persons.

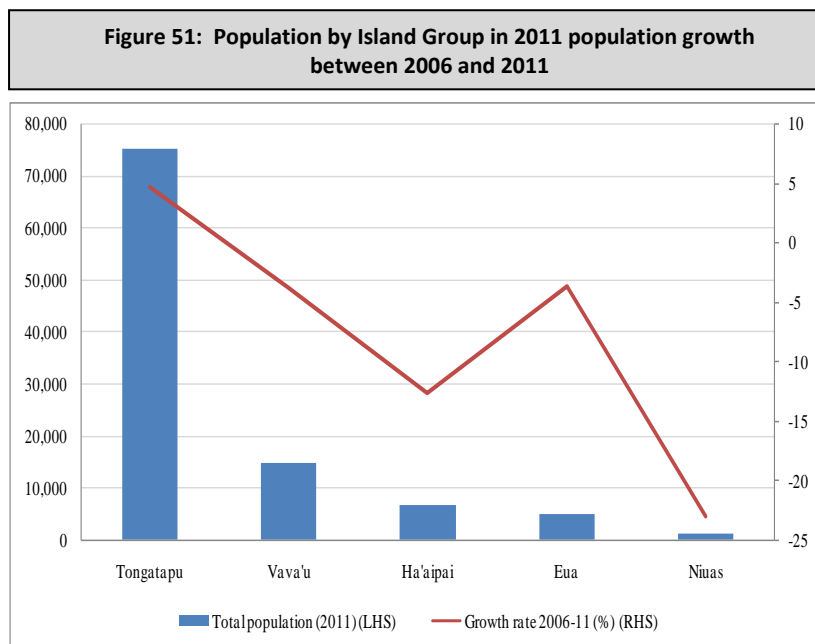
Population growth was largely influenced by these main factors namely:

- Fertility rate which was 3.9 in 2012 (4.2, 2006 and 4.3 1996)³⁷
- Crude Birth Rate was estimated at 26.8 per 1000³⁸, 2011
- Mortality Rate which is estimated at 6.4 per 1000, 2011³⁹, and
- Migration which is estimated at -20 per 1000 population, 2011⁴⁰.

These combinations of factors derive an annual population growth of 0.2 percent. Population should have been increase faster if it was not for the high out migration of population to overseas countries.

Tonga has 170 islands with approximately 33 inhabited. They are grouped into five major island groups, with 73 percent of the population resident on Tongatapu. There has been a steady net migration from the four outer island groups to Tongatapu between the two censuses with populations on outer islands falling between 3 and 23 percent over the period, as shown in Figure 51. This movement has also been associated with an annual growth in urban population of 0.5 percent and rural population on Tongatapu of 0.2 percent.

The population movements reflect the greater opportunities and better infrastructure available on Tongatapu, and in particular Nuku'alofa. These movements have consequences for where to build infrastructure and provide services. It also means that land on outer islands is increasingly being left idle while there is more pressure on land in Tongatapu, in particular in the urban areas.



Source: Statistics Department

There are various reasons why people moved from the outer islands to the main land and also overseas.

- Lack of Higher Education such as Tertiary Institutions
- Lack of Opportunities to get a good jobs(industries and professional) to earn good income
- Poor health facilities
- Sea level rise and climate change risks

³⁷ Demographic Health Survey, 2012

³⁸ Ministry of Health, 2011/12

³⁹ Ministry of Health, 2011/12

⁴⁰ Demographic Health Survey, 2012

- Difficult to access good quality infrastructures including transportation (roads, wharves, shipping), communications, water supply and electricity

This recent movement is part of a longer term rural/outer-island to urban migration as show in **Table 16**. This is common to all countries as they grow and development. Government is faced by the challenge of covering the increased demands for services in Nuku'alofa resulting from the growing population while continuing to ensure adequate services are provided on the outer islands.

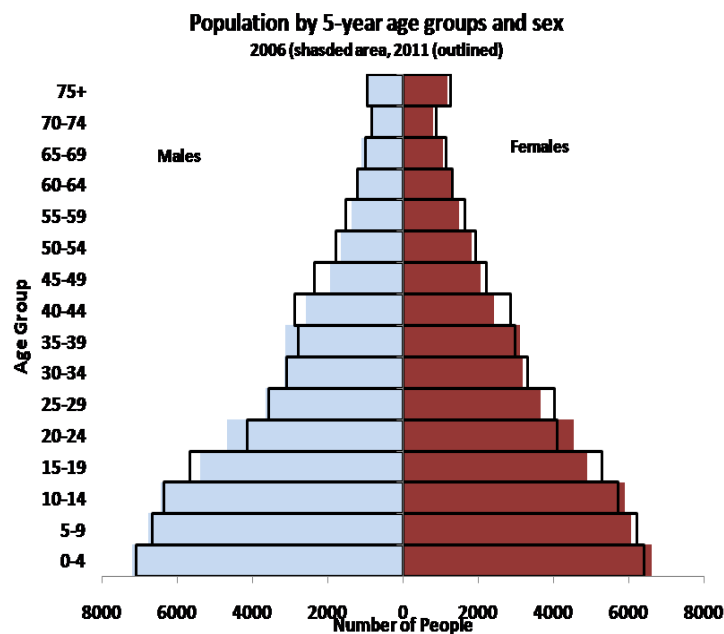
Table 16: Total Population by Division⁴¹

Islands	1986	1996	2006	2011
Tonga	94,649	97,784	101,991	103,252
Tongatapu	63,794	66,979	72,045	75,416
Vava'u	15,175	15,715	15,505	14,922
Ha'apai	8,919	8,138	7,570	6,616
'Eua	4,393	4,934	5,206	5,016
Niuas	2,368	2,018	1,665	1,282

Source: Ministry of Finance and National Planning

A population pyramid shows the number of males and females in five-year age groups, starting with the youngest age group at the bottom, and increasing with age towards the top of the pyramid. The number of males is portrayed on the left and the number of females on the right. The shaded areas show the population count of the 2006 census, while the outlined areas show the population count of 2011 census.

Figure 52: Population by 5 year age groups and sex



Source: Statistics Department

⁴¹ Population Census, 2011

Tonga's population pyramid has a wide and narrower bars represent smaller counts as age increases, meaning that a large percentage of people are in the younger age groups. Such as population structure is associated with relatively high fertility rates eg. high numbers of births per woman.

8.7.6 2013/14 Parliament Constituency Report

The 2013/14 Annual Parliamentary Visits were completed for all constituencies except for Constituency No.17 (the Niuas). The Constituency Reports as shown on **Figure 53** were adopted by Parliament and are now with Government for consideration. The attached graph outlines the main needs which consist mainly of physical infrastructure such as water, roads, foreshore, street lights, classrooms, and community halls. Non-infrastructure needs include funds for the elderly, minimize costs of utilities, and scholarships.

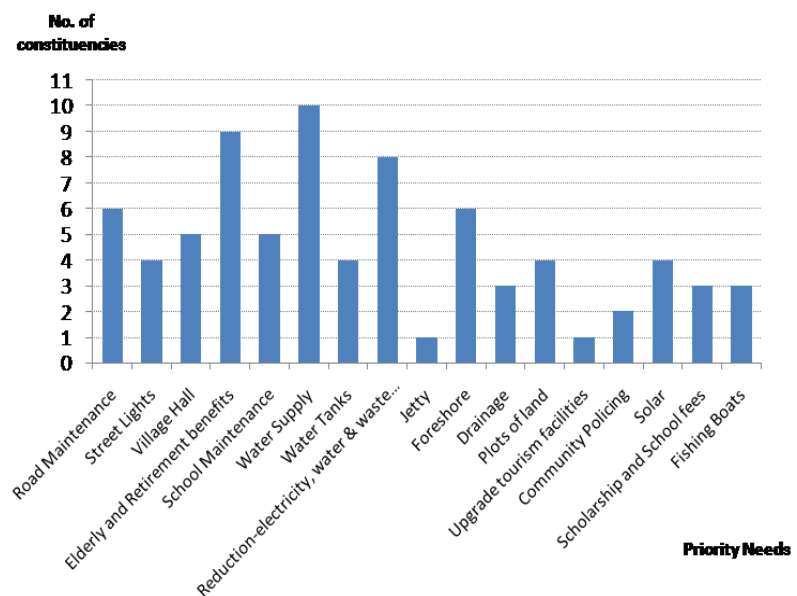
The needs were submitted to the Project and Aid Coordination Committee on 11th April, 2014 with the recommendation that further work is required to develop detailed project proposals for further processing.

A meeting was also held with Members of Parliament (MPs) on 15th May, 2014 to discuss the same. The MPs were informed that the list of needs have been submitted to relevant Ministries for their consideration to include them in their Three Year Corporate Plans. The assistance of MPs was also sought with regards to developing of project proposals particularly if donor funding is to be identified. The MPs indicated the need to establish an office together with qualified staff for each constituency to assist them with writing of project proposals and other work that is required.

Government will consider funding this request in 2015/16. Meantime, the staff of the Project and Aid Management Division will provide assistance, if required, for writing up of project proposals.

The Constituency Reports together with motions approved by Parliament have been considered in the 2014/15 budget.

Figure 53: Constituency Report 2013 - Priority Needs



Source: Constituency Report to Parliament (Tonga)

8.8 Poverty Reduction and Social Protection Outcomes

8.8.1 Background

Tonga, like many countries, has relied on the family and community to provide social protection to the more vulnerable and less successful members of the society. As a result, extreme poverty and destitution tended not to exist although society did not always treat its more vulnerable members with the same level of awareness and sensitivity which are considered more acceptable today. Rapid social change and economic development, associated with movement away from traditional communities to urban areas and overseas have undermined many of the traditional support structures. Traditionally, elderly were respected and looked after by their families. There is now developing more cases of elderly without family to take care of them. While Government wishes to encourage further growth, it also recognizes that this may further undermine traditional support structures so government policy must increasingly address the growing need for social protection. Government also recognizes that such programs can become very costly so is seeking cost effective ways of providing this support in partnership with community groups.

Social protection programmes tackle multiple dimensions of poverty and deprivation (decent work, education, health care, food security, income security) and can therefore be a powerful tool in the battle against poverty and inequality. Social protection can play a fundamental role in creating more inclusive and sustainable development pathways. With rapid social and economic change, in the absence of social protection, more vulnerable people in Tonga, are subjected to increased risks of sinking below the poverty line or remaining trapped in poverty for generations. Social protection is thus an important instrument for the pursuit of many of the MDGs.

Tonga's population enjoys a relatively high standard of living by regional standards, as the country's human development indicators show. **Table 17** shows Tonga ranked first among Pacific developing member countries that were included in the United Nations Development Programme's 2012 Human Development Report. High public spending on education and health has resulted in universal primary enrolment and good basic health outcomes, with the exception of the high incidence of non-communicable disease.

Table 17: Tonga's HDI indicators for 2012 relative to selected countries and groups

Country	HDI Value	HDI Rank	Life Expectancy at birth	Expected years of schooling	Mean Years of schooling	GNI per capita (PPP US\$)
Tonga ⁵	0.71	95	72.5	13.7	10.3	4,153
Federated States of Micronesia	0.645	117	69.2	11.4	8.8	3,352
Solomon Islands	0.53	143	68.2	9.3	4.5	2,172
East Asia and the Pacific	0.683	-	72.7	11.8	7.2	6,874
Medium HDI	0.64	-	69.9	11.4	6.3	5,428

⁵ Life expectancy for Tonga based on UN total population estimates which are slightly higher than Government recent average estimates of 65 for male, 69 for females

Source: United Nation Development Programme (UNDP)

Despite good living standards and achievements in education and health, little cash employment is available in the rural areas of Tongatapu and the Outer Islands. This lack of economic independence and the high rate of out-migration are sources of fragility. Tonga is also vulnerable to environmental hazards including natural disasters that result in chronic shocks to the Pacific island economies. We have seen this with Cyclone Ian devastating the Island of Ha'apai and damaging nearly 80 percent of living structures. During past disaster years, Tonga's economic losses averaged 14 percent of GDP and can affect large portions of the population.

Families receive different types of support such as remittances from overseas. While other families receive social protection activities through informal social safety net mechanisms. Many vulnerable groups and families in Tonga require extra support to ensure their well-being, particularly in times of crisis. While no systematic attempt has been made to identify vulnerable groups, social research shows that vulnerable groups in Tonga include those elderly without family support; persons with disabilities; those living in the outer islands where services and infrastructure are poor; and women raising children alone.

Government hopes to address the gaps experienced by vulnerable groups in Tonga by lowering the eligibility age for old age social assistance, providing aged care services for vulnerable elderly, and early intervention services for infants born with a disability or developmental delay.

8.8.2 Old Age Social Assistance: lowering it from 75 to 70 years old

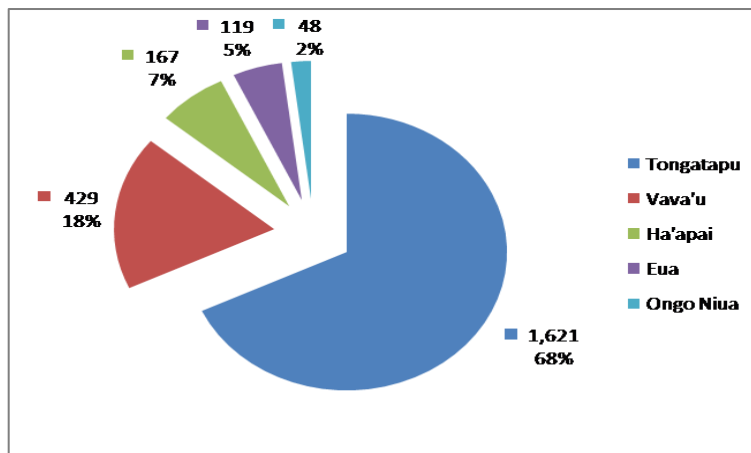
In September 2012, Government introduced the first social assistance payments. All Tongan citizens by birth, irrelevant of their degree of vulnerability, who are 75 years old or older, residing in Tonga, and no longer working at a paid job are eligible to participate in this Social Assistance Scheme. Currently, \$65 is paid per month. Payments are made by the Retirement Fund Office or paid directly into the elderly member's bank account. In the budget, Government is extending this support to all citizens 70 years and older. **Table 18** shows the numbers that are anticipated to be covered.

Table 18: Eligible Beneficiaries 70 Years Old and Older	
Female	2161
Male	1812
Total Beneficiaries	3973
Estimated cost	
60% of eligible beneficiaries accepting assistance	\$1.86 million
100% of eligible beneficiaries accepting assistance	\$3.10 million

Source: Ministry of Finance and National Planning

An effective system of cash benefits requires a capable and accountable administrative system; this is why Government has started the first scheme with the Retirement Fund Office who already has arrangements with many of the elderly. **Table 18** shows the estimated eligible number of beneficiaries for the 2014-15 financial year and cost of services.⁴² Last year, an estimated 60 percent of eligible elderly beneficiaries received the benefit. The remaining 40 percent either were unaware or chose not to receive the benefit.

⁴² Tonga Census of Housing and Population, 2011

Figure 54: Elderly 70+ Estimated Eligible Beneficiaries Willing to Accept Social Assistance in 2014-15

Source: Ministry of Finance and National Planning

If the 2013-14 trend continues, then an estimated 2383 beneficiaries will choose to accept the social assistance at the estimated cost of some \$1.86 million. The distribution of this group is shown in **Figure 54**.

8.8.3 Public Private Partnership (PPP): GoT, ADB-JFPR, & NGO

In November 2011, an Inception Workshop was conducted to commence the Asian Development Bank-Japan Fund for Poverty Reduction (ADB-JFPR) Project-Social Protection of the Vulnerable in the Pacific. This is a Regional Project which includes the Cook Islands and the Republic of the Marshall Islands. This project entailed three component areas:

- A. Micro-Finance
- B. Social Protection
- C. Regional Conference and Knowledge Sharing

The Micro-finance component is a revolving fund to assist individuals and groups with income generating activities. Due to the challenges and hardships some local women groups were experiencing with the high level of interest rates of local micro-finance agencies, ADB-JFPR and the Government of Tonga negotiated a, grant funded, loan product that would be more manageable for vulnerable groups touting a lower interest rate, no fees, and shorter terms; these are shown in **Table 19**.

Table 19: ADB-JFPR Loan Product with the Tonga Development Bank

Loan Size	Interest Rate	Bank Fees	Grace Period-First Payment	Term
Up to \$3000	10% p.a.	Nil	Up to 3 months	12 months

Source: Ministry of Finance and National Planning

ADB-JFPR convened the *Regional Conference component* in February 2014, representatives from Tonga attended a workshop in the Marshall Islands to present the design and activities of the Tonga Social Service Pilot (TSSP) project. The project was well received and touted as a model for the region.

The *Social Protection component* also known as the Tonga Social Service Pilot (TSSP) commenced in August 2012 with disability services and Aged Care Services. The TSSP continues to rely heavily on training and capacity building of aged care and disability staff. For instance, aged care staff will begin a Certificate III programme accredited by Metro College of Technology of Australia on May 2014, running for 20 weeks. The staff working with the disabled went through

an intensive four month training in August 2012, physiotherapy training in January 2013, speech therapy training in November 2013, and early intervention/child development training in May 2014. Furthermore, the disability staff has quarterly clinic reviews with the Ministry of Health's Chief Paediatrician.

Prior to TSSP, there were no formal social services conducted by the Government of Tonga. In the short span of 20 months the Government of Tonga, through the ADB-JFPR project; have provided age care services to over 151 vulnerable elderly and 55 infants born with a disability and/or developmental delay aged 0-3 years. The growth in the service is shown in **Table 20**. **Figure 55** shows the break down by gender and district.

Table 20 : Impacts of TSSP

Social Protection in the form of Social Services	Prior to August 2012	August 2012	August 2013	Current
Aged Care Services ¹	Nil	60	142	151
Early Intervention ² (0-3 yrs old)	Nil	15	25	55*

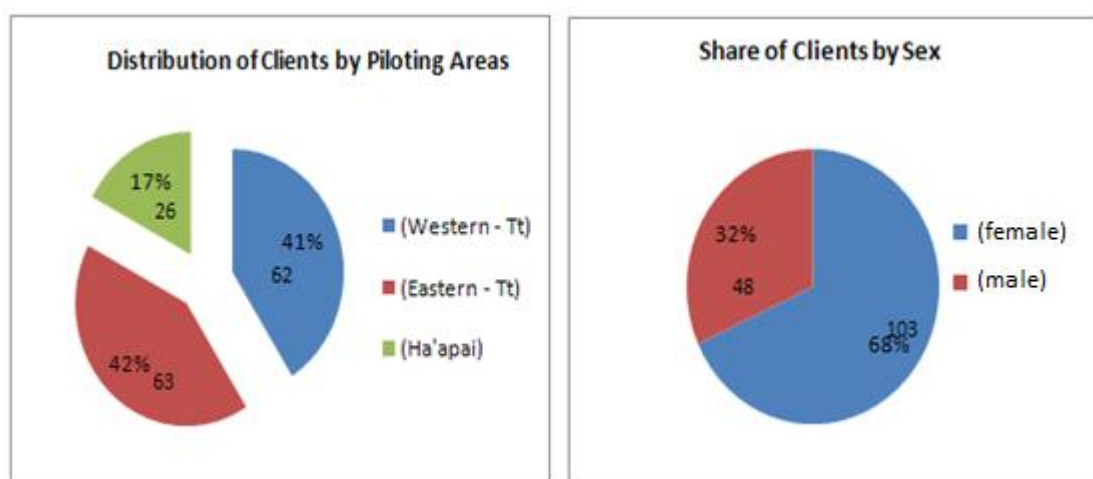
¹ There is currently a waiting list since the pilot project only provides services in the rural areas of Tongatapu and Lifuka, Ha'apai

² Children graduate from the programme at age 4 yrs old

*This entails all infants served from the beginning of the project. There are currently a total of 36 infants receiving services on a weekly basis as of April 2014

Source: Ministry of Finance and National Planning

Figure 55: Aged Care Clients by Gender and District (March 2014)



Source: Ministry of Finance and National Planning

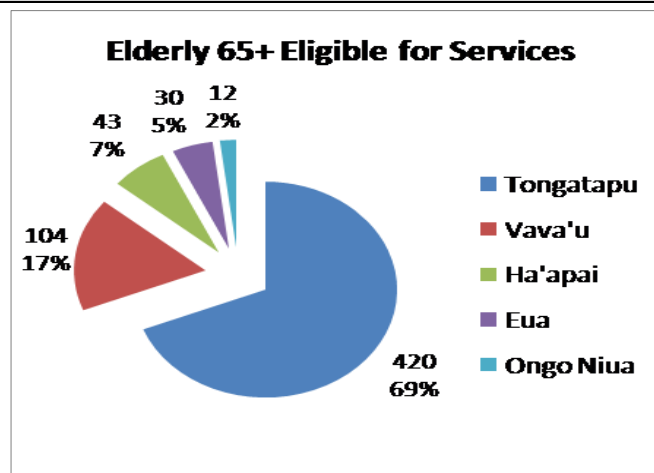
8.8.4 Moving from the ADB Pilot Funding: Social Protection of the Vulnerable in Tonga

A new budget allocation will fund a new post of Deputy Secretary for Social Protection (DSSP) within the Ministry of Internal Affairs (MIA). It is proposed that this will provide the basis for the longer term establishment of a full new division. This division will become responsibility to advocate and implement new policies, regulations, monitoring and evaluation framework, ombudsman, quality assurance, and human service standards necessary to properly oversee and manage NGOs and other entities providing social services or payments to our vulnerable populations. DSSP will oversee and manage the transition of ADB-JFPR project activities and will be responsible for key areas and services:

- Aged Care Services (formerly managed by ADB-JFPR)
- Early Intervention Services-First Step (formerly managed by ADB-JFPR)
- Poverty Impact Assessments on new policies
- Country Focal Point for Disability
- National Disability Policy
- **Proposed:** Paralympics
- UN Convention of Rights for Persons with Disabilities (CRPWD)
- **Proposed:** Convention on the Rights of the Child (CRC)
- **Proposed:** Payments to the elderly (administered by Retirement Fund with oversight by DSP)
- Ombudsman Services
- Human Services monitoring of standards and quality assurance (Government, NGOs, and CSOs)
- Monitoring of regulations and standards (Government, NGOs, and CSOs)
- Liaison for National Emergency Management of Vulnerable populations
- Liaison for Climate Resilience for Vulnerable Populations
- Liaison for Inclusive Education
- Liaison for Millennium Development Goals (MDGs)

8.8.4.1 National Aged Care Services

Figure 56: Vulnerable Elderly and Eligible for Services by Island group



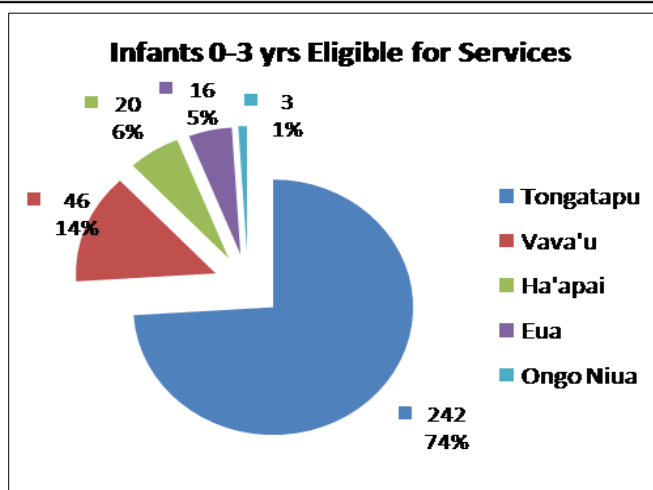
Source: Ministry of Finance and National Planning

When feasible, the new division will manage the national roll out of social services which will include aged care services to the most vulnerable elderly Tongan citizens 65 yrs and older. Using the 2011 Tongan Population and Housing Census, it is estimated that there are 6,089 elderly 65 yrs and older, of which about 609 (10 percent) will be eligible for aged care services. **Figure 56** shows the distribution of eligible elderly by island. The national share of eligible at 10 percent is much the same on all island groups.

8.8.4.2 National Early Intervention Services

Similar to Aged Care Services, when feasible, the new division will manage the national roll out of social services for infants 0-3 yrs old born with a disability or developmental delay. Nationally there are an estimated 10,879 children between 0-3 yrs old. **Figure 57** shows the estimated 0 to 3 years infants eligible for service are distributed across the islands. It is estimated that about 3 percent, or 82 infants, will be born with a disability or developmental delay (Pre-Mature) each year.

Figure 57 : Eligible Infants for Service



Source: Ministry of Finance and National Planning

9 ANNEX II: FISCAL REVIEW OF THE BUDGET

9.1 Government Financial Development

9.1.1 Overview

This is the first year that government has changed from presenting the full budget from the GFS1986 to the GFS2001 format. This provides a more transparent presentation consistent with international norms.

This section provides an overview of the current estimate 2013/14 and new expenditure initiatives in the 2014/15 Budget. It also explains the trends in aggregate general government expenditure over the forward estimates period.

The changes between GFS1986 and GFS2001 are provided at the end of section of 6.1. The major impact of the move to adopt the more contemporary GFSM 2001 system of classifying fiscal transactions for economic analysis has been to :

- move net lending “below the line” where they are recorded as an asset of the Government
- separate the government’s investment activity in nonfinancial assets (often described as capital expenditure; and
- incorporate all in-kind transactions for and on behalf of the Government.

The equivalent of the former budget balance in GFSM 2001 is the net borrowing requirement, the net of transactions in financial assets, (primarily cash and loans and equity injections) and liabilities (borrowing by Government). **Table 21** shows estimated transactions for the budget and following financial year that give rise to its net lending requirements.

Table 21 : Overall Fiscal Balance (Current \$ million)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Revenue	251.9	350.9	302.3	436.9	406.6	405.8
Tax and non-tax revenue	152.3	157.3	158.8	169.4	182.0	186.7
Grants						
Current	52.7	114.0	116.0	116.2	112.5	98.9
Capital	46.9	79.6	27.6	151.4	112.1	120.2
Expense	203.0	257.8	265.7	294.7	262.2	269.3
Gross Operating Balance	48.9	93.1	36.6	142.3	144.4	136.5
Net Acquisition Of Nonfinancial Assets	56.6	79.1	28.0	156.0	134.6	130.6
Net Lending/Borrowing Requirement	- 7.7	14.0	8.6	- 13.7	9.8	5.9
Net Acquisition Of Financial Assets And Liabilities (Financing)	- 7.7	14.0	8.6	- 13.7	9.8	5.9

Source: Ministry of Finance and National Planning

Reflecting the need to finance an urgently needed ongoing scheme to promote new initiatives in strengthen the private sector, and to address long outstanding arrears in relation to the government’s contribution to the retirement benefits scheme, the government will undertake

new domestic bond borrowings in 2014/15 the first such borrowings for quite some time. This is possible due to the progress in improve the finances and the reclassification of Tonga as only medium debt distressed as discussed in Section 5. The increase in borrowing by the Government in 2014/15 will of course be partly offset in the net financing component of the Government's accounts by a financial asset that represents the extent of net loans made through the revolving funds financed from the bond issue.

The estimated net borrowings necessary in 2014/15 is \$13.8 million. After that one off injection into the economy to address some critical priority needs the Government is expecting to return to more normal government fiscal position and finish the year with strengthened overall cash balances as well as a significant reduction in its net debt position (which includes changed in cash balances and ownership of assets in addition to changes in gross debt).

The fiscal indicators for 2014/15 imply that the fiscal outlook of the Government remains relatively tight and will be so in the short to medium term. The challenge for the Government is to sustain this fiscal stance of reducing its net debt over the longer term to help strengthen and build the private sector and therefore its revenue base in light of emerging pressures associated with the ageing population and continuing increases in competing demand for quality services from the public such as health and education.

In the face of those challenges, the Government's aggregate net borrowing requirement is expected to decline from its peak in 20014/15, by about \$23.6 million in 2015/16, with a further reduction of \$5.9 million in the following year. The increase in the net borrowing requirement in 2014/15 reflects in a large part the impact of Government's new policy initiatives in the economic, social, and public sectors, through the establishment of the agricultural, fisheries, tourism and manufacturing fund concessional loan schemes to stimulate targeted sectors in the private sector, assistance to the education of Tonga's young leaders through a scheme to provide low interest loans to assist financing the costs of tertiary education, and the payment of long outstanding arrears in relation to retirement benefit contributions of Government of Tonga staff. The revolving nature of those loan schemes mean this will be a one off injection to assist these sectors with future low interest loans to be financed through the repayment of earlier loans.

From 2014/15, Government is also borrowing, on highly concessional terms, for World Bank and ADB budget support. In addition the project support from World Bank to fund urgent reconstruction of housing damaged in Ha'apai from cyclone Ian. The move towards splitting the assistance between grants and loans reflects Tonga's elevation from high to medium debt distress status consistent with the rules governing those banks' activities. As a result this sort of assistance moves from 100 percent grant to 50 percent grant, 50 percent concessional loan. It is, in part a reflection of the comparative strength of the Tongan economy and a judgment about how well the Government has been able to impose constraints on its fiscal activity over recent years.

Total revenue and cash grants (covering both projects and budget support) will increase by \$134.6 million compared with the 2013/14 estimated outturn of \$302.3 million. This increase is overwhelmingly driven by an increase in donor grants of \$124 million (which include current grants of \$116.2 million and capital grants of \$151.4 million) and an increase of \$10.5 million in tax and non- tax revenues. Grant receipts during 2013/14, are due to fall short of the budget estimate by \$50 million. In 2014/2015 projected grant from donors is \$267.6 million.

Preliminary data indicates that Government is projected a total GFS borrowing requirement of \$7.7 million for 2012/13 largely financed by a rundown of cash balances and the drawdown of the final tranche of the Chinese EXIM Bank loan. The estimated result for 2013/2014 is a negative net borrowing requirement of \$8.6 million reflecting the tight fiscal policies constraining expenditures by ministries and improvement in tax revenue collections. With donor grant assistance offsetting the expenditures of those grants, this improvement in the budget result will allow total cash

reserves to be rebuilt. Total expenditure is estimated to increase during 2013/14, and that increase is largely financed by donor assistance, including budget support from Tonga's donor partners.

The other notable feature of the 2013/14 estimated outturn data has been the deferment of principal repayments on the China EXIM loan. This repayment has been deferred for further five years.

9.1.2 Total Expenditure

The government's overall expenditure (current plus capital), in **Table 22**, for the financial year 2014/15, as classified on a GFS basis, is expected to be \$450.7 million. This comprised of total current expenditure of \$294.7 million, and total capital expenditure estimated at \$156.0 million. Total expenditure is projected to decrease in 2013/2014 as a result of slow implementation of some of the capital projects, deferment of the principal loan repayment to the EXIM Bank, and the tight fiscal constraints on the overall spending of the line ministries that are now estimated to be spending below what have been targeted for the end of the financial year. The total expenditure for 2014/15 is expected to increase. The details of changes to both current and capital expenditures are given in more detail in the next sections.

Table 22 : Total Expenditure on GFS Basis (Current/Capital \$ millions)

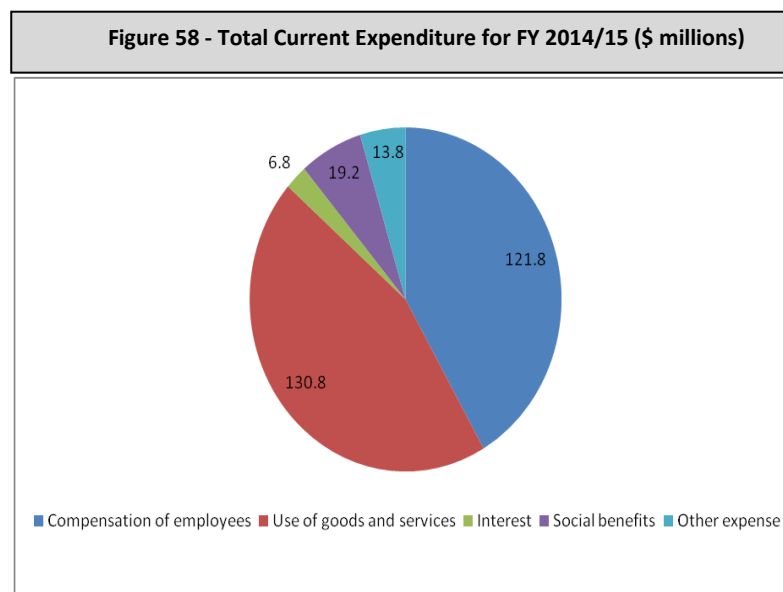
	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Expense (Current)	203.0	257.8	265.7	294.7	262.2	269.3
Compensation of employees	94.9	102.4	105.4	121.8	117.0	118.7
Use of goods and services	76.1	119.8	122.7	130.8	102.9	108.4
Interest	7.1	7.6	7.6	6.8	8.2	8.1
Subsidies	0.8	0.3	0.3	0.1	0.1	0.1
Grants	2.5	2.2	1.9	2.2	2.2	2.2
Social benefits	13.8	14.8	16.5	19.2	19.1	19.1
Other expense	7.7	10.7	11.3	13.8	12.7	12.7
Net Acquisition Of Nonfinancial Assets (capital)	56.6	79.1	28.0	156.0	134.6	130.6
Fixed assets						
Buildings and structures	5.8	17.7	5.2	85.8	94.4	105.5
Machinery and equipment	34.1	51.1	18.3	48.3	36.4	21.1
Other fixed assets	16.7	10.2	4.5	21.8	3.8	3.8
Land	0.1	0.1	0.1	0.1	0.1	0.1
Total Payments	259.6	336.9	293.7	450.7	396.8	399.9
Note: Payments associated with the acquisition of non-financial assets with the amounts in the GFS reports, the amount of the estimate receipts from the sale of capital items needs to be deducted from the figures in this table						

Source: Ministry of Finance and National Planning

NOTE: (1). Payments associated with the acquisition of nonfinancial assets with the amounts in the GFS reports, the amount of the estimated receipts from the sale of capital items needs to be deducted from the figures in this table.(2). Compensation of Employees comprises of Wages and Salaries and social contributions. 3. Wages and salaries include some expenditure items in category 10, 11 and 14 plus donor expenses. 4. Social contribution include established staff contribution to Retirement Fund and transfer value.

9.1.2.1 Current Expenditure

Current expenditure, recorded as Expense in **Table 22**, is expected to increase in FY2014/15 by \$29.0 million from the 2013/2014 estimated outturn. As indicated in **Figure 58** below, much of this increase results from projected increase in purchase of goods and services including those associated with donor projects, and increases in compensation of employees (account of the increase transfer value arrears and salaries previously awarded and wages increases). The Government will commence new domestically funded initiatives associated with a rise in social benefits, private sector marketing fund, and the preparation for the upcoming coronation and parliamentary election. Current expenditure associated with donor projects is projected to increase in 2014/2015, due to substantial anticipated increase in the provision of donor funding including budget support.



Source: Ministry of Finance and National Planning

Figure 58 shows 2014/15 current expenditure across the five major expenditure groups. Use of goods and services account for the largest dollar value growth in proportion to total expenditure, while compensation of employees accounted for the second largest proportion of the overall budget.

9.1.2.1.1 Wages and Salaries

Total GFS expenditures on wages and salaries for financial year 2014/15, in **Table 23**, is budgeted at \$121.8. This is higher than the amount shown in the Budget Estimates, set out in **Table 24** which shows a total of \$110.4 million. The differences arise from GFS including a few small payments (e.g. to Jurors, from Cat 14) as well as the repayment of the transfer value, which for 2014/15 is \$10 million. Using the Budget Estimates the figure represents a \$7.2 million increase (6.9 percent) from the estimated outturn in 2013/14. The increase reflects the impact of the implementation of 5 percent COLA over a full year (it only covered half of 2013/14) and its impact in all salaries and wages related expenditure items such as overtime and other allowances, listed in **Table 25**. Of this \$110.4 million, \$96.9 million is funded by government and \$13.5 million from donor support. 97.4 percent of salary expenditure is allocated to established staff. This proportion has increased from 2013/14.

Table 23: Compensation of Employees

	Actual 2012/13	Estimate 2013/14	Revised Estimate 2013/14	Estimate 2014/15	Projection 2015/16	Projection 2016/17
Compensation of employees						
Wages and salaries	84.5	92.5	95.5	101.9	105.8	107.2
Social contributions	10.5	9.9	9.9	19.9	11.2	11.5
Total	94.9	102.4	105.4	121.8	117.0	118.7

Source: Ministry of Finance and National Planning

The Government recognizes the importance of rebalancing expenditure away from salaries and wages to ensure improved service delivery. The Government is committed to finding solutions to high wage bill in the future through restraint in civil service expansion and salary increases (but giving line ministries recruitment flexibility to ensure critical services are not affected). In 2014/15, line ministries' vacant positions are provided for within their estimate.

Ministry of Finance and National Planning with the assistance of the Public Service Commission are continuing to be tasked to scrutinize recruitments. The establishment of new positions will depend on the confirmation of funds by the Ministry of Finance and National Planning while Public Service Commission reviews the line ministries' organizational structure, core functions, and existing total number of staff. More importantly, recruitment of staff in line ministries must be in line with their Corporate Plan.

Table 24: WAGES AND SALARIES (CURRENT \$ MILLIONS)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Compensation of employees						
Wages and salaries	84.3	93.2	95.3	101.5	105.4	106.7
Salaries	69.0	82.3	82.7	86.2	90.0	91.3
Overtime	4.0	1.4	3.3	2.3	2.9	2.9
Cost of Living Allowance	0.2	1.0	0.0	5.5	5.5	5.5
District and Town Officers Salaries	1.0	1.2	1.0	1.2	1.2	1.2
Privy Purse	0.4	0.4	0.4	0.1	0.1	0.1
Wages	2.8	2.4	2.5	2.5	2.5	2.5
Temporary Staff	0.1	0.1	0.1	0.1	0.1	0.1
Contract Labour	0.3	0.5	0.4	0.4	0.4	0.4
Others	6.6	4.0	4.9	3.3	2.8	2.8
Social contributions	9.9	7.9	7.9	8.9	9.2	9.5
Government Contributions to	9.9	7.9	7.9	8.9	9.2	9.5
Total	94.2	101.1	103.2	110.4	114.6	116.2

Source: Ministry of Finance and National Planning

Notes: The Table excludes CAT 14, the transfer value, and the 5% COLA for the last six months of 2013/14 and variations of GFS 1986 to GFS 2001

9.1.2.1.2 Social Contributions

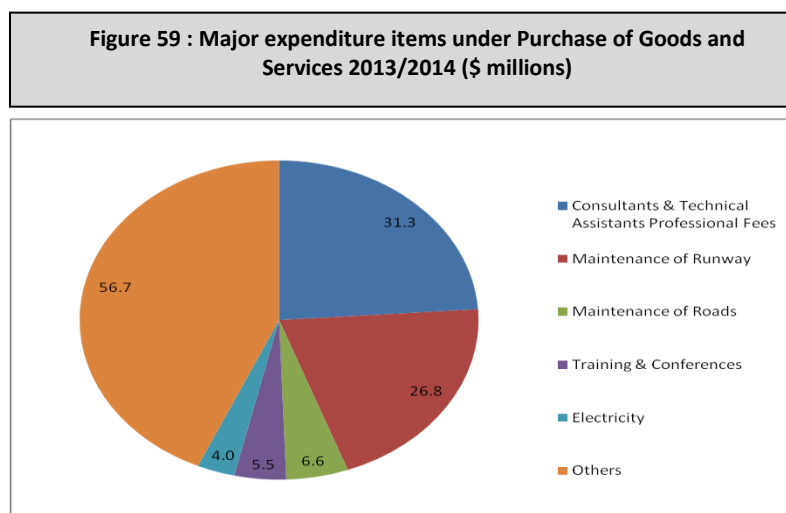
Social contributions are estimated at \$19.9 million in the 2014/15 budget, which consists of \$8.9 million for contributions to the Retirement Fund and \$11.0 million as transfer value to meet part of the Government's long standing arrears bill. This will leave arrears of approximately \$7 million. The increase in contributions to retirement fund reflects the impact of the annual increment for staff as well as the implementation of the 100 percent of the 5 percent COLA for Civil Servants that was approved by Cabinet towards the end of the first half of 2013/14.

The 5 percent COLA was awarded only for the second half of the 2013/14 and will be funded for the full year in 2014/15.

9.1.2.1.3 Purchases of Goods and Services

The purchase of goods and services for 2014/15 is set to increase to \$130.8 million, representing an 8.1 percent increase from the estimated outturn in 2013/14. Of the total budget for purchase of goods and services, \$64.2 million will be funded from donor assistance and \$66.6 million from government. Other purchases of goods and services are only expected to increase marginally. Wages and salaries are planned to account for a reduced proportion of total expenditure.

The major areas of increase in the 2014/15 budget compared to the 2013/14 outturn are maintenance of runway (\$12.8 million increase) a project funded by the World Bank for the Fua'amotu Airport, consultants and technical assistants professional fees (\$6.1 million increase), training and conferences (\$1.7 million increase), and maintenance of roads (\$0.7 million increase), and electricity (\$0.6 million increase) which donor funded.



Source: Ministry of Finance and National Planning

9.1.2.1.4 Interest payments

Total interest payments, **Table 25**, are estimated at \$6.8 million for 2014/15, slightly down from the 2013/14 estimated outturn of \$7.6 million. Interest payments are comprised of two parts; domestic (20.6 percent of total interest payments) and foreign (79.4 percent of total). In the future, payments for foreign loans will be dominated by servicing of the Chinese EXIM Bank Reconstruction loans and older loans from Asian Development Bank and World Bank. Further details are provided under the Public Debt Section.

Table 25: INTEREST (CURRENT \$ MILLIONS)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Interest						
To nonresidents	5.3	6.0	6.0	5.3	5.6	5.5
To residents other than general government	1.9	1.6	1.6	1.5	2.6	2.6
Total	7.1	7.6	7.6	6.8	8.2	8.1

Source: Ministry of Finance and National Planning

9.1.2.1.5 Subsidies

On GFS basis, expenditure on subsidies is estimated at \$0.1 million for 2014/15, see **Table 26**. This represents a decrease of \$0.2 million from the estimated outturn 2013/14. A significant change in this area is a subsidy to non-financial Public Enterprises of \$0.1 million, part of which is being the assistance to the Development Committees for the outer islands.

Table 26: SUBSIDIES (CURRENT \$ MILLIONS)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Subsidies						
Subsidies to public corporations	0.7	-	-	-	-	-
Subsidies to private enterprises	0.1	0.3	0.3	0.1	0.1	0.1
Total	0.8	0.3	0.3	0.1	0.1	0.1

Source: Ministry of Finance and National Planning

9.1.2.2 Capital Expenditure

Total Capital expenditure (or the acquisition of nonfinancial assets), shown in **Table 27**, in 2013/14 will reach \$28.1 million, a reduction of \$51.0 million from the original estimate of \$79.1 million in 2013/14. 2012/13 being the final year of capital expenditure related to the China EXIM loan.

Total Capital expenditure in 2014/15 is estimated at \$156.0 million, an increase of \$127.9 million from an estimated outturn of \$28.1 million in 2013/14. Major area of capital expenditure projected for 2014/15 is on buildings and structures. This includes the reconstruction work planned for Ha'apai of over \$40.0 million as well as the work being undertaken at the Fua'amotu Airport. Machinery and equipment will comprise the second largest portion of the capital expenditure as well as other fixed assets. The capital expenditure for 2014/15 will be funded substantially from cash and in-kind grants by numerous development partners.

Table 27: CAPITAL EXPENDITURE (CAPITAL \$ MILLIONS)

	Actual 2012/13	Estimate 2013/14	Revised Estimate 2013/14	Estimate 2014/15	Projection 2015/16	Projection 2016/17
Fixed assets						
Buildings and structures	5.8	17.7	5.2	85.8	94.4	105.5
Machinery and equipment	34.1	51.1	18.3	48.3	36.4	21.1
Other fixed assets	16.7	10.2	4.5	21.8	3.8	3.8
Land	0.1	0.1	0.1	0.1	0.1	0.1
Total	56.7	79.1	28.1	156.0	134.7	130.5

Source: Ministry of Finance and National Planning

Donor cash capital investment for 2014/15 is estimated at \$154.4 million, an increase of 98.7 percent from 2013/14 estimated outturn of \$24.0 million. Major estimated donor investments for that year are detailed in the later section on Development Projects.

Government's Capital expenditure for 2014/15 amounts to \$1.6 million, a reduction compared with the original estimate in 2013/14 of \$4.1 million. The major Government-financed capital project for 2014/15 is the new Kitchen for the Prisoners, essential new vehicle purchases, and critical new technical equipment necessary to provide essential services for all Tongans.

9.1.2.3 *Financing*

Table 28 outlines the financing transactions of the Budget for 2014/15. The overall net borrowing requirement is \$13.8 million.

Table 28 : Estimated Financing Transactions (Current \$ millions)

	Actual 2012/13	Estimate 2013/14	Revised Estimate 2013/14	Estimate 2014/15	Projection 2015/16	Projection 2016/17
Financial Assets						
Domestic						
Currency and deposits	- 6.5	0.0	5.2	0.0	0.0	0.0
Loans	0.3 -	0.7 -	1.3	11.4 -	0.9 -	0.9
Shares and other equity	0.7	0.1	0.1	6.2	6.2	6.2
Foreign						
Loans	-	-	-	-	-	-
Total Assets	- 5.5	0.6	4.0	17.6	5.3	5.3
Financial Liabilities	2.3	14.6	4.6	31.3	4.4	0.6
Total Financial Assets and Liabilities	- 7.7	14.0	8.6	13.8	9.8	5.9

Source: Ministry of Finance and National Planning

Domestically, the government plans to undertake \$26.0 million in bond issues in 2014/2015 with the purpose of financing \$6.0 million of rollover bonds, scheduled to mature that year. The rollover has no net impact on financing. The \$10 million will be used by Government to support the Private Sectors by implementing revolving funds for the new loan schemes targeted priority

sectors of the economy and supporting Private Student studies. The other \$10 million will be used to pay government's long standing arrears with the civil servants retirement fund.

Also, as part of building the Government's financial assets, donor (New Zealand) is assisting the electricity in the villages through the Tonga Power Board with the aim of improving the electricity source of the people in the community and to ensure affordability is achieved through low cost electricity is reached to the grassroots in all areas of Tongatapu and some of the outer islands. This expenditure is recorded as increase in government's equity with TPBL.

Borrowing from overseas reflects the decision made by World Bank and the Asian Development Bank, that grants (project and budget support) from these two multilateral Banks will be on a 50:50 basis, that is, half grant and half concessional loan. This applies to their budget support and the World Bank reconstruction of Ha'apai. The decision by those organizations reflects the overall improvement of Tonga's fiscal position as well as the comparative strength of the Tongan economy.

9.1.3 Revenue and Grants

Table 29: Total Revenue and Grants (Current \$ million)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Revenue						
Taxes	132.7	135.5	136.7	141.4	152.2	156.4
Grants	99.5	193.6	143.6	267.6	224.6	219.2
Other revenue	19.6	21.8	22.1	27.9	29.8	30.2
Total	251.8	350.9	302.4	436.9	406.6	405.8

Source: Ministry of Finance and National Planning

The total revenue and grants, **Table 29**, estimated outturn for 2013/14 financial year amounted to \$302.4 million, falling short by \$48.5 million from the original budget estimate of \$350.9 million, however \$50.6 million higher than 2012/13 actual. The shortfall was primarily caused by lower than anticipated receipts of grants, only \$143.6 million compared to the original budget of \$193.6 million. Tax and other revenue (non-tax) were on targets recording an estimated outturn of 0.8% and 1.3% above the budgeted forecast. These outturns formed the platform of revenue forecast in the new Budget 2014/15.

Total revenue and grants for 2014/15 are projected at its highest level ever at \$436.9 million, which is \$134.6 million higher than the estimated outturn of \$302.3 million in 2013/14. Of the total revenue and grants, 32.4% comes from tax revenue, 61.2% from grants and 6.4% from non-tax revenue. Tax and non-tax revenue are expected to increase incrementally in nominal terms, with income and corporate tax, consumption and excise tax, property income and administrative fees being the primary sources of the increase.

The significant increase in 2014/15 budget, however, lies in the grants component expected from development partners which increased by 86.4% to \$267.6 million. At the outset, this may look like an unrealistic number, however, the major difference in this year's presentation of grants is the inclusion of both cash and in-kind grants to reflect the overall envelopes of development assistance that government is working on and expected to get approval from our development partners. In the estimated outturn of grant for 2013/14, this estimate may be undervalued due to in-kind grants not being recorded in the MOFNP financial system ("cash basis system"). Recording of in-kind grants is still a work in progress with our development partners. The estimate of grants for 2014/15 included projects for reconstruction of Ha'apai, resurfacing of

Fua'amotu and Vava'u airport, construction of St. George Palace and renewable energy project at Vaini and Outer-islands in addition to other ongoing projects.

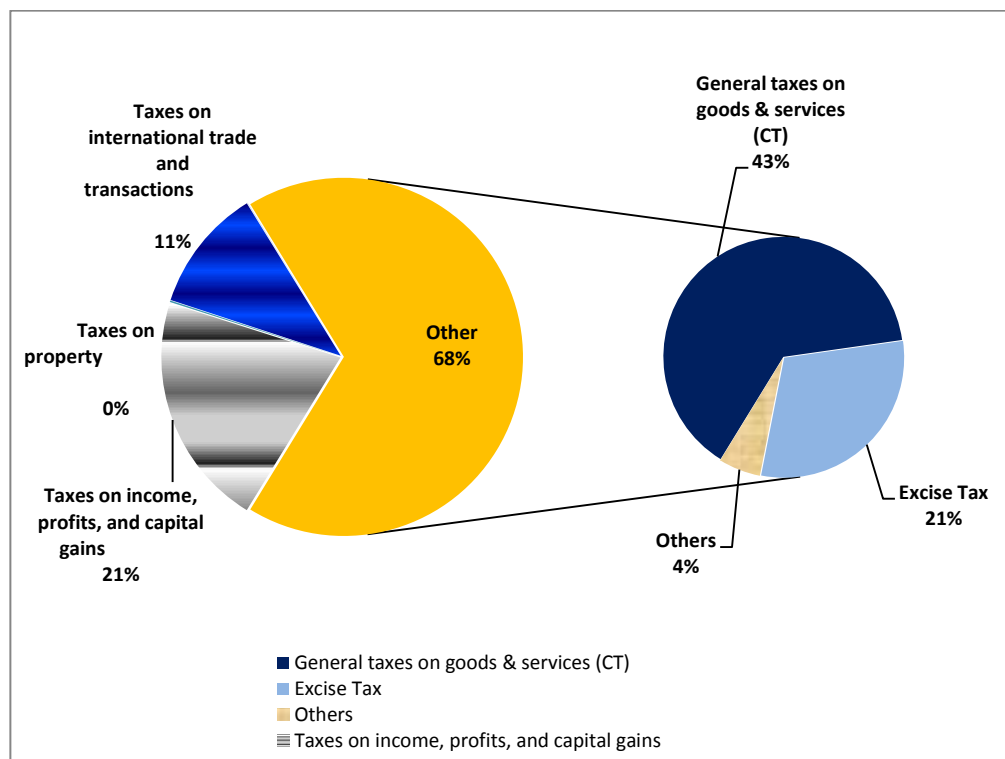
The budget also provided preliminary projections for the outer years 2015/16 and 2016/17 based on the macroeconomic parameters but most importantly to give government a framework to monitor fiscal sustainability into the medium term years, as well as providing government through line ministries a platform for their respective reform initiatives. Projected revenue and grants for outer years is in the vicinity of \$406.6 million and \$405.9 million.

9.1.3.1 Taxes Revenues

Tax revenues, **Table 30**, for 2014/15 are projected at \$141.4 million, an improvement of \$4.7 million from the estimated outturn of \$136.7 million in 2013/2014. Taxes on goods and service, which includes consumption and excise tax, continued to account for the largest portion of tax revenue, at 67.5%, followed by taxes on income and corporate tax at 21.1% and international trade tax at 11.2%.

The following pie-chart depicts the contribution of tax revenue components to the total and **Figure 60** sets out the detailed components of tax revenue in 2014/2015 and forecast for the medium term framework

Figure 60: Composition of Tax Revenue 2014/15



Source: Ministry of Finance & National Planning

Table 30: Taxes Revenue 2012/13 to 2016/17 (Current \$ million)

	Actual 2012/13	Estimate 2013/14	Revised Estimate 2013/14	Estimate 2014/15	Projection 2015/16	Projection 2016/17
Taxes						
Taxes on income, profits, and capital gains	30.3	25.2	25.0	29.9	33.3	33.9
Taxes on property	0.7	0.1	0.1	0.2	0.2	0.2
Taxes on goods and services	86.9	95.0	96.3	95.5	101.5	103.5
Taxes on international trade and transactions	14.7	15.2	15.3	15.8	17.1	18.8
Other taxes	-	0.0	0.0	0.0	0.0	0.0
Total	132.7	135.5	136.7	141.4	152.2	156.4

Source: Ministry of Finance and National Planning

9.1.3.2 Taxes on Income and Profits

The estimated outturn for Taxes on Income and Profits, **Table 31**, 2013/14 is on par with budgeted targets of \$25.2 million although this is much lower than actual in 2012/13. The forecast for 2014/15 took into account expected growth in business activities related to various reform initiatives government is undertaking in regulatory reform and SOE reform. The government has also put more efforts to tighten revenue compliance although Tonga is at the high end in the Pacific in compliance efficiency of 80-85%.

Taxes on Income & Profits for 2014/2015 are projected at \$29.9 million, \$4.9 million above the 2013/2014 estimated outturn. The increase is expected to come from corporate tax, \$2.1 million, tax debt recovered, \$1.9 million, and \$0.9 million from Income Tax (PAYE).

Table 31: Taxes on Income & Profits (Current \$ million)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Taxes on income, profits, and capital gains						
PAYE	14.2	12.5	13.4	14.3	15.6	15.9
Corporate Tax	15.5	12.2	10.5	12.6	14.2	14.5
Tax Debt Recovered	0.6	0.5	1.1	3.0	3.5	3.5
Total	30.3	25.2	25.0	29.9	33.3	33.9

Source: Ministry of Finance and National Planning

9.1.3.3 Taxes on goods and services

The total taxes on goods and services, **Table 32**, for 2014/2015 are estimated at \$95.5 million, representing a marginal decline of 0.8% from the 2013/2014 estimated outturn. The decline is attributed to a significant reduction in the amount budgeted for “communication individual license” outweighing marginal increase in consumption and excise tax.

Consumption tax for 2014/2015 is estimated at \$61.1 million showing marginal increase of \$1.2 million, or 2.0%, from the estimated outturn 2013/2014. The increase reflects continuous strong domestic demand and improved economic activities noting increases in collections above budgeted targets from year to year since 2011/12. This is also aided by improved compliance.

Excise tax is estimated to increase slightly in 2014/2015 by \$0.7 million to \$29.0 million. The increase reflects revisions to the excise tax schedule to increase the excise tax rate on tobacco from \$200 to \$250 per 1,000 sticks/kg and introduction of duties on sugared drinks and animal fat that support improved health outcomes. Continued growth in revenues will also rely on tight control of ad-hoc exemptions.

Table 32 : Taxes on Goods and Services

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Taxes on goods and services						
Consumption Taxes	54.5	56.5	59.9	61.1	63.7	64.7
Excise Taxes	29.0	28.7	28.3	29.0	30.0	31.0
Other Taxes	3.4	9.8	8.1	5.4	7.8	7.8
Total	86.9	95.0	96.3	95.5	101.5	103.5

Source: Ministry of Finance and National Planning

9.1.3.4 Trade Taxes

Trade taxes, **Table 33**, for 2014/2015 amounted to \$15.8 million, a marginal increase of \$0.5 million or 3.4% higher than the estimated outturn 2013/2014.

Table 33: Taxes on international trade and transactions (Current \$ million)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Taxes on international trade and transactions						
Business import duties	14.7	15.0	15.2	15.7	17.0	18.7
Government import duties	-	0.1	0.1	0.1	0.1	0.1
Recoverable charges	-	0.1	-	-	-	-
Total	14.7	15.2	15.3	15.8	17.1	18.8

Source: Ministry of Finance and National Planning

9.1.3.5 Non-tax Revenues

Non-Tax Revenue as shown in **Table 34** below is expected to increase in 2014/2015 by \$5.8 million, or 26.4%, from the 2013/2014 estimated outturn. The increase is mainly derived from anticipated growth in property income which includes dividends from government state own enterprises, and improved collection from administrative fees and charges.

Table 34 : Non-Tax Revenue component (Current \$ million)

	Actual 2012/13	Estimate 2013/14	Revised Estimate 2013/14	Estimate 2014/15	Projection 2015/16	Projection 2016/17
Other revenue						
Property income [GFS]	6.7	7.3	9.2	12.0	12.3	12.4
Sales of goods and services	11.5	13.1	11.5	15.2	16.7	17.0
Fines, penalties, and forfeits	0.4	0.5	0.5	0.6	0.6	0.6
Voluntary transfers other than grants	0.7	0.9	0.9	-	-	-
Miscellaneous and unidentified revenue	0.2	0.0	0.1	0.2	0.2	0.2
Total	19.6	21.8	22.2	28.0	29.8	30.2

Source: Ministry of Finance and National Planning

9.1.3.5.1 Entrepreneurial and Property Incomes

Revenue from entrepreneur and property income, **Table 35**, is expected to increase in 2014/15 to \$12.0 million, an increase of \$2.8 million from estimated outturn recorded in 2013/14. This is attributed to increase in rental by \$1.1 million, interest income collected from government deposit and on-lent loan to public enterprises by \$0.8 million, and dividend receipts increase by \$0.9 million. The latter, dividends have increased significantly from \$5.5 million collected in 2012/13 and \$8.0 million in 2013/14 to \$8.9 million budgeted in 2014/15. The increase reflected improvements in performance of public enterprises as government undertake reforms in efficiency, accountability and good corporate governance.

Table 35: Entrepreneurial and Property Income (\$ millions)

	Actual	Estimate 2013/14	Revised Estimate 2013/14	Estimate 2014/15	Projection 2015/16	Projection 2016/17
Entrepreneur and Property Income						
Interest	0.5	1.1	0.4	1.2	1.7	1.8
Dividends	5.5	5.4	8	8.9	8.7	8.7
Rental	0.7	0.8	0.8	1.9	1.9	1.9
Total	6.7	7.3	9.2	12	12.3	12.4

Source: Ministry of Finance and National Planning

9.1.3.5.2 Sales of goods and services

Table 36: Sales of Goods and Services(\$ millions)

	Actual 2012/13	Estimate 2013/14	Revised Estimate 2013/14	Estimate 2014/15	Projection 2015/16	Projection 2016/17
Sales of goods and services						
Administrative fees	10.3	11.8	10.3	13.4	14.8	15.1
Incidental sales of non-market establishments	1.2	1.3	1.2	1.8	1.9	1.9
Total	11.5	13.1	11.5	15.2	16.7	17.0

Source: Ministry of Finance and National Planning

The overall sales of goods and services, **Table 36**, are projected to increase by \$3.7 million or 31.9% to \$15.2 million in 2014/2015 compared to the estimated outturn in 2013/2014. The increase reflects the introduction of a new seabed mineral exploration license, sales of sand and exports and post harvest processing fees. The major components of this category are seabed mineral exploration license at \$2.9 million, school fees (\$1.8 million), passport fees (\$1.3 million), visa fees (\$0.9 million) and motor driving licenses (\$0.9 million).

9.1.3.5.3 Grants (Projects and Budget Support)

The total grants, **Table 37** for the financial year 2014/15 are projected at \$267.6 million, an increase of \$124.0 million from the 2013/14 estimated outturn; however, given the difficulty in predicting when projects will start, the budgeted amount is usually greater than the outcome. The increase is still \$74 million greater than the budget for 2013/14. Details of major projects are included in **Table 39**.

Table 37: Total Grants (Current \$ million)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Grants						
Current	52.7	114.0	116.0	116.2	112.5	98.9
Capital	46.9	79.6	27.6	151.4	112.1	120.2
Total	99.6	193.6	143.6	267.6	224.6	219.1

Source: Ministry of Finance and National Planning

The current component of grants is related to projects or activities such as purchases of goods and services, consultant fees, host of conference and workshops, salaries of staffs and training.. It also includes budget support. The estimated current grant for 2014/15 is \$116.2 million. In terms of capital grants, these are linked to direct cost of acquisitions of capital asset such as construction of building, schools, solar plant, construction of airport runway and roads. Capital grant is estimated at \$151.4 million in 2014/15.

Every year, the government reviewed and signs a work programme with many of its key development partners, for example the "Country Operations Business Plan" (COBP) with ADB, the "Country Partnership Strategy" (CPS) with WBG and IFC, the "Tonga-Australia Partnership for Development" with Australia etc. These programmes determined what government sees as priorities, in line with the Tonga Strategic Development Framework (TSDF) 2010-2014, and maps

with development partners' area or sector of comparative advantages. This helps guided the identification and prioritization of projects relative to the limited resources allocated by respective donors that appear in the annual budget, with grant (as well as loan funding). Some of the projects are ongoing for a number of years, and some are new projects that government expects to be approved in the budgeted financial year. The amount included in the budget estimate is an indicative budget of how much will be spend in that particular year and does not necessary indicate a firm commitment by the development partner. This is even more the case for the two outer years.

In the 2014/15 budget, the government has attempted to include all assistances from development partners including cash and in-kind grants as well as loan funding though it is not included in the Table above. The cash grant is easy for government to estimate and report in financial system. However, in the case of in-kind grant, while funding agreed projects, the money is managed by the development partner (off the government's cash system). The project construction and delivery is also managed by either the development partner or a third party. Getting estimates of the value depends on information provided by development partners, which can take time, and for some projects – such as regional ones – it may not be easy to identify the Tongan component.

9.1.3.5.4 Development Partners

Tonga's traditional development partners continued to provide significant assistance in partnership with government and other stakeholders in the 2014/15 budget. **Table 38** lists a summary of assistance by major development partners from 2012/13 to 2016/17.

Table 38: Grants (project and budget support) by Development Partners (Current \$ million)

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Grants						
World Bank/International Development Agency	31.8	32.0	31.7	61.5	9.5	16.4
Japan - JICA	4.0	2.3	13.4	36.0	27.0	22.0
People's Republic of China	1.0	37.9	15.3	34.7	15.5	0.5
Asian Development Bank (ADB)	11.2	37.1	21.9	31.1	19.0	12.5
Australia	18.0	25.4	15.4	23.7	16.5	16.6
New Zealand Bilateral	12.8	12.2	14.1	19.5	15.6	13.2
EU Budget Support	0.5	8.5	8.5	16.2	8.7	8.7
Pooled Funds - Australia & NZ	8.7	10.8	7.2	10.6	7.8	7.4
Pacific Islands Forum Secretariat (PIFS)	-	7.3	-	4.0	4.1	-
United National Development Program	0.2	1.5	4.7	3.6	4.2	1.0
Secretariat of the Pacific Community	0.6	1.3	0.6	1.6	0.6	0.5
World Health Organisation	0.4	-	0.5	1.5	1.5	1.5
Other and unconfirmed Donors	0.2	4.1	3.9	18.6	92.9	117.7
Consolidated small grants from other international or	10.3	13.2	6.2	4.9	2.0	1.2
Total Grants from Development Partners	99.5	193.6	143.6	267.6	224.6	219.2

Source: Ministry of Finance and National Planning

9.1.3.5.5 Major Projects for 2014/15

Table 39 highlights some of the major projects that government has confirmed for 2014/15 by our traditional partners:

Table 39: Major Development Support by Development Partners (\$ million)

Funded by	Project Name	Budget 2014/15
ADB & ITU	E-Government Project	1.00
Asian Development Bank	Pacific Climate Resilience Project	6.40
Asian Development Bank/Australia	Nuku'alofa Urban Development Project	3.00
Australia & New Zealand	Scholarship	5.00
Australia & New Zealand	Tonga Police Development Programme	2.50
European Union	Niutoputapu Hospital	2.43
European Union	Energy Project	2.00
Government of Japan	Vaini Solar Farm	19.00
Government of Japan	Upgrade of Fua & Nafanua Wharf	15.00
Government of Japan	Grassroot Grant Project	2.00
International Fund for Agricultural Development	Tonga Rural Innovation Projects	1.00
New Zealand	Tonga Village Network Upgrade	6.00
Pacific Island Secretariat Forum	Pacific Environment Community Fund	4.00
People of the Republic of China	St George Palace	20.00
People of the Republic of China	Y12 Airplane	11.00
Pooled Funds- Australia & New Zealand	Tonga Education Support Programme 2	6.00
Telecom International Gateway	International Gateway Project	3.00
World Bank	Ha'apai Housing Reconstruction and Sanitation	20.40
World Bank	Pacific Aviation Investment Program	31.70
World Bank	Transport Sector Consolidated Project	2.80
World Bank/Asian Development Bank	Tonga-Fiji Connectivity Project	14.00
World Health Organization	WHO Training	2.00
Asian Development Bank	Ha'apai Reconstruction and Climate Proofing of Electric Grid	7.60
European Union	Ha'apai Reconstruction and Climate Proofing of Electric Grid	4.50
New Zealand	Ha'apai Reconstruction and Climate Proofing of Schools	8.90
Various Donors	Small Projects below \$1m (or unconfirmed)	47.15
Total		248.38

Source: Ministry of Finance and National Planning

9.1.3.5.6 Budget Support

In addition to the infrastructure and development projects, the government continues, in the 2014/15 budget and the medium term, to receive budget support; recorded as current grants in **Table 39**. Total budget support, including those parts funded by concessional loan, are shown in **Table 40**. Budget support has two main objectives. Firstly, this is an avenue where our development partners, in partnership with government, provide financial assistance to close the government's budget shortfall or strengthen government financial position in order to be more resilient to economic and financial shocks. Secondly, in return for providing budget support, the government commits to an agreed policy reform programme that will help to further strengthen the capacities of the public service to improve its performance and service delivery. These policy reform initiatives also help build a stronger foundation that will better enable government to withstand shocks.

The government budget support programme is developed with assistance from the World Bank, Asian Development Bank, Australia and European Union. Other development partners are all welcome to join if they want to. Government works jointly with development partners to identify key reforms triggers (prior actions) that are included in the Joint Policy Reform Matrix (JPRM), which related to government's policy reform programme. Currently, the JPRM includes reforms triggers related to public financial management, strengthen fiscal policy, enhancing the business enabling environment and various structural reform policies in public enterprises and promoting renewable and more efficient energy usage. This is a collaborative and joint process that has won much praise as a leading approach to donor coordination. The triggers also help government with seeing through the reform programs it is committed to, by providing extra monitoring of progress. **Table 40** provides projected budget supports for 2014/15 and outer years.

The total budget support grants for 2014/15 is projected at \$37.7 million compared to an estimated outturn of \$33.6 million in 2013/14. Both the World Bank and ADB have allocated USD\$5.0 million for budget support, however, due to the government being upgraded from high risk debt distress to moderate, their allocation is now treated as 50% grant and 50% as credit. Australia is still budgeted to provide AUD\$5.0 million. It is anticipated that PNG's leftover budget support in 2013/14 will be received in 2014/15 budget shows the total of all budget support both grant and loan which totals \$37.7 million for 2014/15.

Table 40: Budget Support (grants and loans) by Development Partners (Current \$ million)

Development Partners	Actual for 2012/13	Budget for 2013/14	Estimated Outturn 2013/14	Budget 204/15	Projections 2015/16	Projections 2016/17
World Bank	3.12	8.50	9.66	9.00	2.70	2.70
Asian Development Bank	-	7.60	8.14	9.00	4.50	4.50
Australia	8.70	8.76	6.00	11.46	8.40	8.40
European Union	-	5.76	7.67	6.90	5.70	5.70
Papua New Guinea	-	5.07	2.13	1.34	-	-
Unconfirmed	-	-	-	-	6.70	6.00
Total	11.82	35.69	33.60	37.70	28.00	27.30

Source: Ministry of Finance and National Planning

9.1.4 Reconciliation Tables

Tables 41 and 42 present reconciliation between cash inflow estimates as detailed in the “Programme Budget Estimates 2013/2014” document and the estimates of revenue (inflows) and expenditures (outflows), classified on a GFS Basis. These reconciliations help the understanding of the differences between the economic and accounting presentation of the budget.

Table 41: Reconciliation between Cash Inflows Government of Tonga Fund and Revenues as per GFS basis

		Estimate 2014/15
Receipts		
Government of Tonga Fund (<i>As per Table 7 of the Estimate</i>)	185,210,262	185,210,262
Donor Cash Support		
Tonga Trust Fund	-	
Revolving Fund - Special Government Activities	1,420,000	
Revolving Fund - Private Sector Initiatives	11,000,000	
Local Community	-	
Confirmed Budget Support	37,698,245	
Unconfirmed Budget Support	-	
Project Support	67,393,314	117,511,559
Non-Cash Receipts		
In-kind Project Support (<i>As per Table 17 of the Estimate</i>)	180,988,060	180,988,060
Gross Receipts		483,709,881
Less: receipts associated with the net acquisition		
Receipt associated with the disposal of fixed assets	10,000	
Receipts associated with the repayment of financial assets	1,699,954	
Receipt associated with the incurrence of financial liabilities	45,103,000	46,812,954
Equals		
Estimated Operating Revenues (GFS Basis) (<i>from Operating Statement</i>)		436,896,928

Source: Ministry of Finance and National Planning

Table 42: Reconciliation between Cash outflows Government of Tonga Fund and estimated expenses as per GFS basis.

		Budget Estimate 2014/15
Gross Appropriation (as per Appropriation schedule)		302,717,659
Plus Payments not Authorised by Appropriation		
Estimated in-kind Expenditures by Donors (as per table 13 of the Estimate)	180,988,060	180,988,060
Total Estimated Payments (as per table 1 of the Estimate)		483,705,719
Less payments associated with the net acquisition of assets and liabilities		
Payments associated with the acquisition of fixed assets	155,995,650	
Payments associated with the repayment of financial liabilities	13,784,098	
Payments associated with the acquisition of financial assets	19,250,000	189,029,748
<i>Equals</i>		
Estimated Operating Expenses (from Operating Statement)		294,675,971

Source: Ministry of Finance and National Planning

9.1.4.1 2001 GFS Compared to the 1986 GFS

GFS (Government Finance Statistics) system of classification is a tool to evaluate the impact of bringing together expenditures directed towards like purposes, GFS system of classification also facilitates presentation of information on the total resources devoted by the Government to those purposes and allows international comparisons independently of local administrative structures. It is for these reasons that the primary presentation of budget estimates in the Budget Statements is on a GFS basis.

The new Government Finance Statistics (GFS) system of classification called GFSM 2001, being implemented in Tonga this year, has a number of changes to the 1986 version. The major enhancements implemented in GFSM 2001 include:

- mandating the inclusion with estimates of cash transaction of data related to all in kind assistance provided by donors; and
- greater clarity about:
 - the operating revenues and expenses of government

- the costs of the acquisition and disposal of capital assets (called in GFSM2011 net transactions in nonfinancial assets) by bringing together below the gross operating balance the Governments decisions to invest in both financial and nonfinancial assets
- the acquisition and disposal of financial assets (primarily cash and net lending by government [for GFS 1986 were included within expenditure and net lending] and movements in the government's cash balances)
- the acquisition and disposal of financial liabilities (primarily net borrowing by government by bringing them together in any analysis of the net borrowing requirements of the Government)
- the net borrowing requirement of government (GFS1986 by including net transactions in relation to loans made by government as expenditure does not provide for the ready disclosure of movements in the net indebtedness of government i.e. the difference between loans (and similar financial transactions) made by government – financial assets and loan raising and repayment activity undertaken by government)
- with transactions in both financial assets and liabilities being recorded separately, the sign of certain 'balance sheet' transactions were reversed compared to those in GFS1986 so that positive net transactions in those categories meant an increase in the stock of assets or liabilities as appropriate
- some comparatively minor re-alignments were also made within both the expense and revenue sub-categories, for example capital revenue earned from the disposal of assets is netted of the cost of the acquisition of such assets
- In this way, GFSM 2001, while not reducing budget disclosure in any way, the GFSM Operating Statement aligns more closely to the Profit and Loss Statements used widely within the private sector.

9.2 Development Projects

9.2.1 Overview of Aid Funded Projects

Estimated expenditure from development partners for 2014/2015 is \$248.38 million, of which \$67.40 million in cash and \$180.99 million is in-kind, an overall increase of \$89.57 million on 2013/14 estimate. **Table 43** shows the projections.

Table 43: Total Project Expenditure(\$millions)

Type of Funding	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Estimate 2014-15	Projections for 2015-16	Projections for 2016-17
Cash	50.33	41.71	67.39	43.56	38.79
In-kind	108.48	69.11	180.99	156.68	156.69
Grand Total	158.81	110.82	248.38	200.24	195.47

Source Ministry of Finance and National Planning

9.2.2 Aid Funded Project Expenditure by Ministry

Table 44 contains the details of major project expenditure by Ministry.

Table 44 : Development Expenditure by Ministry (cash and in-kind T\$ millions)

	Ministry	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Estimate 2014-15	Budget Projection 2015-16	Budget Projection 2016-17
01	Palace Office	0.25	0.25	0.30	-	-
02	Legislative Assembly	1.23	1.93	1.77	1.19	0.56
03	Audit Office	0.15	0.15	0.15	0.15	0.15
04	Commissioner of Public Relations	-	-	-	-	-
05	Ministry of Foreign Affairs & Trade	1.40	0.70	0.80	0.30	0.30
06	His Majesty's Armed Forces	1.50	2.83	0.60	0.30	0.30
07	Prime Minister's Office	14.00	1.28	0.06	-	-
08	Ministry of Finance & National Planning	8.81	7.90	10.06	6.18	6.18
09	Ministry of Revenue & Customs	4.75	0.77	4.09	2.14	0.64
10	Ministry of Public Enterprises	1.65	8.35	6.38	6.17	6.00
11	Ministry of Commerce, Tourism and Labour	6.32	0.86	0.89	4.72	3.00
12	Ministry of Justice	0.49	0.50	0.49	0.49	-
13	Attorney General's Office	0.02	-	0.30	0.30	0.30
14	Ministry of Police, Prisons & Fire Services	4.04	4.30	10.49	12.92	10.62
15	Ministry of Health	7.23	4.14	8.83	5.60	5.74
16	Ministry of Education & Training	13.01	10.37	14.80	21.94	31.59
17	Ministry of Internal Affairs	2.61	2.98	1.97	1.50	1.50
18	Ministry of Agriculture, Food, Forests & Fisheries	1.21	0.28	1.09	0.84	0.33
19	Ministry of Infrastructure	52.88	37.09	84.04	73.10	90.00
20	Ministry of Lands & Natural Resources	37.17	25.92	4.28	4.20	4.20
21	Public Service Commission	-	0.20	1.63	1.15	1.15
22	Bureau of Statistics	0.10	0.02	0.08	0.06	0.09
23	Ministry of Environment, Energy, Climate Change, Disaster Management, Meteorology, Information and Communications *	-	-	95.29	56.99	32.82
	Grant Total	158.81	110.82	248.38	200.24	195.47

Source: Ministry of Finance and National Planning

* Ministry will only be established in 2014/15

9.2.3 Aid (Grant and Loan) Funded Project Expenditure by Development Partners

Most of the capital expenditures are kindly funded by Tonga's Development Partners and several projects are co-funded/multi-funded by various donors. Implementing agencies are working together with development partners to ensure that these projects objective and outcomes are achieved. **Table 45** shows the levels of support by Development Partner

Table 45: Large Projects from largest to smallest 2014/15 (\$millions)

Project Name	Funded* by	Budget 2014/15
Pacific Aviation Investment Program	World Bank	31.70
Ha'apai Housing Reconstruction and Sanitation	World Bank	20.40
St George Palace	People of the Republic of China	20.00
Vaini Solar Farm	Government of Japan	19.00
Upgrade of Fuaa & Nafanua Wharf	Government of Japan	15.00
Tonga-Fiji Connectivity Project	World Bank/Asian Development Bank	14.00
Y12 Airplane	People of the Republic of China	11.00
Ha'apai Reconstruction and Climate Proofing of Schools	New Zealand	8.90
Ha'apai Reconstruction and Climate Proofing of Electric Grid	Asian Development Bank	7.60
Pacific Climate Resilience Project	Asian Development Bank	6.40
Tonga Village Network Upgrade	New Zealand	6.00
Tonga Education Support Programme 2	Pooled Funds- Australia & New Zealand	6.00
Scholarship	Australia & New Zealand	5.00
Ha'apai Reconstruction and Climate Proofing of Electric Grid	European Union	4.50
Pacific Environment Community Fund	Pacific Island Secretariat Forum	4.00
Nuku'alofa Urban Development Project	Asian Development Bank/Australia	3.00
International Gateway Project	Telecom International Gateway	3.00
Transport Sector Consolidated Project	World Bank	2.80
Tonga Police Development Programme	Australia & New Zealand	2.50
Niutoputapu Hospital	European Union	2.43
Energy Project	European Union	2.00
Grassroot Grant Project	Government of Japan	2.00
WHO Training	World Health Organization	2.00
Tonga Rural Innovation Projects	International Fund for Agricultural Development.	1.00
E-Government Project	ADB & ITU	1.00
Small Projects below \$1m (or unconfirmed)	Various Donors	47.15
Total		248.38

*Cash, in-kind, grant, loan

Note: shaded projects cover the reconstruction of Ha'apai

Source: Ministry of Finance and National Planning

9.2.4 Development Partners assistance by region

9.2.4.1 Projects in Tongatapu (\$millions)

Table 46 : Grant Allocation by Project Types – Tongatapu

	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Estimate 2014-15
Climate Change	41.40	21.80	9.20
Constructions	22.00	21.58	90.50
Education	16.90	10.70	14.80
Energy	14.20	9.63	25.30
Health	9.10	3.27	6.80
Law and Order	5.40	3.70	6.90
Income Generation	1.30	2.40	1.50
Road	5.80	3.56	2.00
Others	4.00	1.24	4.90
Total	120.10	76.64	161.90

Source: Ministry of Finance and National Planning

The major infrastructural project that ended in 2013/14 was the Integrated Urban Development Projects that upgraded roads and drainage in Tongatapu urban area (\$1m). Major projects for 2014/15 includes :

- Nuku'alofa Urban Development Sector Project aiming at effective, efficient and sustainable water and solid waste services in Nuku'alofa area are co-funded by ADB and Australia
- NUDSP is the second phase of the IUDSP project
- Pacific Risk Resilience Projects assists in strengthening governance mechanism for disaster risk reduction and climate change adaptation, implemented by ADB and funded by Australia
- Transport Sector Consolidation projects currently on its final year with the periodic maintenance of road component left to be completed by the end of December 2015
- Major component of the Pacific Aviation Investment Program which is the resurfacing of Fua'amotu airport runway funded by the World Bank
- Tonga Health Support Project which helps training and providing support to the Vaiola Hospital funded by Australia
- Tonga Governance and Strengthening Project implemented by UNDP and funded by Australia,
- Tonga Police Program co-funded by Australia and New Zealand
- Japan Grassroot Grant Program still continues and funded by the Government of Japan.
- Climate Resilience Sector Project which includes climate proofing of schools and roads funded by ADB
- St George Palace build by the People of the Republic of China
- Vaini micro-grid solar farm by the Government of Japan.

9.2.4.2 *Projects based in Vava'u(\$millions)***Table 47: Grant Allocation by Project Types - Vava'u**

	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Estimate 2014-15
Constructions	14.0	0.3	16.4
Water	0.30	0.5	0.5
Energy	3.0		2.1
Income Generation		0.4	0.3
Climate Change			0.3
Total	17.3	1.2	19.6

Source: Ministry of Finance and National Planning

The major projects include:

- The Fibre Optic Cable Projects extension to Vava'u has been launched and actual work is expected to continue in 2014/15. World Bank, Asian Development Bank and Tonga Cable continue to finance this work.
- The Japan Grassroot Programme has assisted the Mailefihi Siu'ilikutapu College by renovating the boy's dormitory and built the new dining and kitchen with water tank.
- Upgrading of Holonga, Ha'alaufuli and Feletoa village water supply is still in progress and expected to be completed this year.
- Tonga Rural Innovation Projects implemented by MORDI and funded by IFAD is targeting to complete the following sub projects before the end of this financial year, upgrading and maintenance of Hunga community agricultural boundary fence, upgrading and maintenance of community wharf for the islands of Ovaka, Otea, Kapa and Taunga. Construction of a tourist sanitation facility for Lape community, and an agricultural shed for Falevai community.
- The Climate Resilience Project funded by ADB is expected to build a jetty for Ofu island and allocated funds for Special Marine Management Areas for Fisheries.
- Transport Sector Consolidate Projects funded by the World Bank have completed maritime improvement work and will commence with its periodic road maintenance.
- The European Union through the Ministry of Health will be conducting a training workshop on prevention of NCDs in Vava'u islands.

9.2.4.3 *Projects based in Ha'apai(\$millions)***Table 48: Grant Allocation by Project Types - Ha'apai**

	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Estimate 2014-15
Constructions	0.30	0.3	22.5
Education	0.20	0.2	7.5
Health	0.10	0.5	2.8
Water and Sanitation	0.30	0.5	3.6
Income Generation		1.8	1.0
Energy		0.5	2.8
Total	0.90	3.8	40.2

Source: Ministry of Finance and National Planning

As a result of the devastation by cyclone Ian, there is a major expansion in projects in Ha'apai. The Haapai recovery taskforce are working in collaboration with Ha'apai Development Committee in developing the recovery plan. The key projects include:

- Foa Causeway has been successfully completed in 2013/14 funded under the debt swap agreement with the Government of Germany.
- The Climate Resilience Sector projects funded by ADB will relocate and build the Niu'ui Hospital including climate proofing of four schools.
- The Outer Island Renewable Project will commence soon, targeting to construct and install solar power systems with total capacity of 0.2MWp on Ha'apai covering the islands of 'Uiha, Nomuka, Ha'ano and Ha'afeva.
- Community water pumping project funded by IUCN is also expected to be completed by December 2014.
- Ha'apai reconstruction recovery is expected to commence at the end of this year with USD12m from World Bank (50% grant and 50% soft loan) plus US\$1.8 million from EU for housing and sanitation issues.
- The Asian Development Bank has offered USD1.6m and jointly funded by NZAID with NZ\$5m to upgrade schools and power network.
 - Further assistance for the recovery programme from other development agencies are yet to be confirmed. UNDP Cash for work programme are underway with 500 locals have registered to work for the communities and payments will inject cash into household and local economy.

9.2.4.4 *Projects based in 'Eua(\$millions)***Table 49: Grant Allocation by Project Types - 'Eua**

	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Estimate 2014-15
Energy Generation and Supply			0.5
Income Generation	0.3	0.3	0.3
Constructions	0.3	0.07	0.6
Education	0.2		0.05
Health	0.1		
Water and Sanitation	0.3		
Total	1.2	0.37	1.45

Source: Ministry of Finance and National Planning

Key projects include:

- Funds from the Republic of Korea have received to fund 30 water tanks for 'Eua communities. MORDI have yet to implement their infrastructural project in 'Eua and will review several Community Plan in July 2014
- the Government of through their GGP program have funded the upgrading of Hofangahau College and Tufuvai Government Primary School
- Periodic road maintenance under the TSCP project is currently ongoing
- ADB Climate Resilience Project will fund climate proofing of one school and road
- The OIREP project will also connect solar photovoltaic generators of 0.2MWp in Eua.

9.2.4.5 *Projects based in NTT and NF(\$millions)***Table 50: Grant Allocation by Project Types – Niuatoputapu**

	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Estimate 2014-15
Construction	2.40	0.80	0.40
Water and Sanitation	0.60		
Climate Change	0.50	0.01	0.03
Health	2.0		2.40
Income Generation	0	0.30	0.01
Construction	2.40	0.80	0.40
Total	7.90	1.91	3.24

Source: Ministry of Finance and National Planning

Table 51 : Grant Allocation by Project Types – Niuafo’ou

	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Estimate 2014-15
Constructions			0.1
Water			0.03
Total			0.13

Source: Ministry of Finance and National Planning

With the completion of the Tonga Post Tsunami project in December 2013 there is a decrease in the number of projects:

- Niuatoputapu hospital has now confirmed to be built on the 2nd quarter of 2014.
- Japan’s Grassroot program has approved funding for upgrading water supply system for Vaipoa, Hihifo and Falehau villages and is scheduled to commence before the end of this financial year.
- A 0.15 MWp of solar power capacity will be connected to a newly installed distribution system in Niuatoputapu is planned under the OIREP project together with expanding existing solar home system capacity in Niuafo’ou by installing an additional 100 units of 200 watt peak SHSs.
- The Climate Resilience projects will funds climate proofing of 3 schools and conduct water survey in Niuafo’ou and coastal monitoring network in Niuafo’ou . This is funded by ADB for climate change.

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Table 52 : Tonga Selected Indicators, 2006/07 – 2012/13

	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
Output and prices 1/							
Real GDP	-4.5	1.9	3.2	3.3	2.9	0.8	0.7
Consumer prices (period average)	5.1	9.3	5.6	1.7	6.0	3.3	0.7
Money and credit (end-period) 2/							
Broad money (M2) % growth	14.0	8.4	-1.9	5.1	2.6	-2	7.3
Domestic credit	14.8	15.2	-7.1	-11.5	-11.5	-16	-0.4
Private sector credit 3/ % growth	11.4	19.7	-2.9	-15.5	-9.2	-9.6	-7.6
Balance of payments (OET Basis)							
Exports, f.o.b.	26.3	23.5	11.4	11.4	11.2	8.7	12.3
Of which: Squash	5.6	2.7	1.8	0.5	0.7	2.2	
Imports, f.o.b.	-212.9	-262.5	-271.3	-208.0	-229.6	-247.8	-260.9
Services (net)	-35.8	-6.2	-5.4	-7.9	4.9	-4.3	6.3
Income (net)	7.1	6.4	9.6	5.3	4.9	5.6	0.9
Services and Income (net)	-28.7	0.2	4.2	-2.6	9.8	1.3	7.2
Transfers (net)	168.6	180.2	157.9	146.7	136.4	182.4	174.8
Of which: Private transfer receipts	186.8	202.8	175.2	157.4	139	156.8	209.5
Current account balance	-50.9	-58.6	-49.8	-52.6	-72.1	-55.4	-66.5
(In percent of GDP)	-8.4%	-8.9%	-7.5%	-7.4%	-9.3%	-6.9%	-8.2%
Overall balance	8.4	-2.5	47.1	34.3	31.0	38.3	17.3
	-8.4%	-8.9%	-7.5%	-7.4%	-9.3%	-6.9%	-8.2%
Gross international reserves (end-period)							
In millions of pa'anga	91.6	89.1	136.3	170.5	203.8	246.1	263.3
In months of imports cover	4.4	3.5	5.1	7.1	7.4	8.2	8.8
External debt 3/							
External debt/GDP (%)	27%	24%	30%	32%	35%	40%	43%
Exchange rate (period average)							
T\$ per US\$ (end-period)	2.00	1.89	2.08	1.93	1.84	1.70	1.73
Real effective exchange rate (1990=100)	105.7	108.6	116.2	113.6	108.1	118.5	114.7
Nominal effective exchange rate (1991=	60.8	58.8	59.9	59.8	59.9	60.6	59.9
1/ Sources for Output and Prices: Statistics Dept							
2/ Sources for Money, Credit, BOP, Foreign Reserves & Exchange Rates: NRBT							
3/ Sources for External Debt : MOFNP							

Table 53: Tonga Real Sector Developments, 2006/07-2012/13

	2006/07r	2007/08r	2008/09r	2009/10r	2010/11r	2011/12r	2012/13p
Nominal GDP							
In pa'anga mn.	602.9	663.4	664.0	712.9	775.0	800.6	779.7
In US\$ mn.	292.3	339.5	314.3	369.0	422.6	471.5	449.5
GDP per capita (US\$)	2865	3319	3065	3590	4101	4656	4341
Population	102,025	102,276	102,528	102,783	103,033	103,286	103,541
	Annual Percentage Change						
GDP (2010/11 prices)	-4.5	1.9	3.2	3.3	2.9	0.8	0.7
of which:							
Agriculture, forestry, and fisheries	1.0	-5.3	-1.4	0.5	2.0	0.5	3.7
Manufacturing	-7.8	-1.0	-0.2	-1.7	5.9	-2.6	6.7
Construction	-2.8	0.9	35.0	21.7	6.1	1.2	-29.9
Commerce, restaurants, and hotels	-3.4	9.4	4.2	3.9	3.3	0.4	2.5
Transportation and communications	-1.3	4.2	15.4	15.7	-2.9	0.5	2.8
Finance and real estate	-1.9	3.1	-6.8	-1.1	3.1	-4.5	-5.4
Government services	-15.1	4.6	1.5	0.9	0.5	1.5	1.5
	Percentage of GDP						
GDP (by sector; current prices)							
of which:							
Agriculture, forestry, and fisheries	16.7	14.8	15.3	16.4	17.0	16.7	17.6
Manufacturing	7.1	6.7	6.5	6.1	5.9	5.7	6.3
Construction	6.0	5.9	7.0	8.6	9.7	9.3	6.3
Commerce, restaurants, and hotels	10.9	12.3	13.1	12.3	13.0	13.1	14.0
Transportation and communications	5.5	5.7	6.7	6.9	6.2	6.2	6.5
Finance and real estate	9.0	9.2	8.1	7.6	7.7	7.3	7.1
Government services	11.9	11.7	11.7	12.5	11.8	11.7	12.1
Consumer prices (period average)							
All items	5.1	9.3	5.6	1.7	6.0	3.3	0.7
Imported component	1.0	10.5	5.6	1.8	7.7	4.7	0.7
Domestic component	7.2	8.0	5.6	1.6	3.5	1.5	0.6
r - revised estimates							
p - preliminary estimates							
Source: Statistics Department							

Table 54: Annual Average Consumer Price Index for 2007-2013, Base Period (October 2010=100)

	All Items	Food	Housing	H/Hold goods	Clothing and footwear	Transportation	Tobacco and Alcohol	Misc. Goods & Services	Imported Items	Local Items
Weight.	<u>100.0</u>	<u>45.8</u>	<u>2.5</u>	<u>20.8</u>	<u>3.2</u>	<u>11.9</u>	<u>6.0</u>	<u>9.8</u>	<u>57.8</u>	<u>42.2</u>
2007	84.7	82.2	96.5	94.8	89.3	88.3	73.0	93.3	83.7	86.5
2008	93.6	88.5	99.5	104.5	96.2	109	78.9	101.4	93.0	94.3
2009	94.9	95.4	103.8	98.5	100.8	95.2	82.9	104.1	93.2	97.9
2010	98.3	98.3	102.1	99.3	99.8	100.5	93.7	99.4	98.1	98.3
2011	104.4	104.7	99.8	101.6	104.6	112.6	101.6	101.7	106.1	102.2
2012	105.7	106.4	99.6	103.4	104.6	113.0	102.4	102.1	107.4	103.1
2013	106.4	108.2	100.7	103.4	104.6	113.1	99.8	102.5	109.0	103.0

Source: Statistics Department

Table 55: Annual Percentage (%) Change in CPI for December month, 2007-2013

	All Items	Food	Housing	H/Hold goods	Clothing and footwear	Transportation	Tobacco and Alcohol	Misc. Goods & Services	Imported Items	Local Items
Weight.	<u>100.0</u>	<u>45.8</u>	<u>2.5</u>	<u>20.8</u>	<u>3.2</u>	<u>11.9</u>	<u>6.0</u>	<u>9.8</u>	<u>57.8</u>	<u>42.2</u>
2007	6.8	7.9	1.6	3.4	4.3	10.8	6.2	4.1	8.2	4.2
2008	6.4	2.7	7.5	10.4	7.8	10.4	8.1	7.3	6.0	7.4
2009	1.1	8.3	-1.5	-7.7	3.2	-7.6	-1.4	3.5	-0.6	4.3
2010	5.0	3.8	-3.1	1.6	-0.6	4.4	24.0	-5.5	7.9	0.4
2011	3.8	3.2	0.0	3.8	4.6	8.8	1.8	2.6	5.9	1.0
2012	2.5	6.0	0.4	-1.8	0.0	1.7	0.2	-0.2	2.3	2.8
2013	0.8	1.0	1.4	2.4	0.0	-0.8	-2.0	0.8	1.4	0.0

Source: Statistics Department

Table 56: Tonga Domestic Exports by HS Section, 2006/07-2012/13

HS Code	2006/07		2007/08		2008/09		2009/10		2010/11		2011/12		2012/13	
SECTION ITEM	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%
Live Animals;Animal Products	7,357	34.7	5900.0	33.4	4147.4	28.0	9856.8	64.3	9,905	49.9	9,277	36.6	8,029	35.1
Vegetable Products	11,778	55.61	7321	41.5	7087.1	47.8	4019.3	26.2	8,056	40.5	10,593	41.8	11,393	49.7
Prepared Foodstuff;Beverages, Tobacco	654	3.10	190	1.1	87	0.6	216	1.4	240	1.2	358	1.4	494	2.2
Products of the Chemical Or Allied	580	2.74	1489	8.4	907.7	6.1	585.3	3.8	646	3.3	367	1.4	462	2.0
Wood and Articles of Wood;	488	2.30	323	1.8	601.6	4.1	321.9	2.1	433	2.2	416	1.6	424	1.9
Miscellaneous Manufactured Articles	6	0.03	23	0.1	5.7	0.0	22	0.1	5	0.0	27	0.1	112	0.5
Works of Art, Collectors Pieces and Antiques	33	0.15	72	0.4	44.6	0.3	16.6	0.1	56	0.3	144	0.6	26	0.1
Other Exports	284	1.34	2339	13.9	2,338	15.8	289	1.9	526	2.6	4,173	16.5	1,963	8.6
TOTAL	21,180	100	17,657	100.0	14,827	100.0	15,327	100.0	19,869	100.0	25,354	100.0	22,901	100.0
Source: Statistics Department														
p: provisional numbers														

Table 57: Exports by Institutional Sector 2006/07 – 2012/13

	2006/07		2007/08		2008/09		2009/10		2010/11		2011/12		2012/13	
INSTITUTIONAL	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%
Private Sector	21,180	100	17,288	100	14,827	100	15,327	100	19,863	100.0	25,343	100.0	22,866	99.8
Government Sector	0	0	0	0	0	0	0	0	6	0.0	6	0.0	2	0.0
Quasi-Government Sector	0	0	0	0	0	0	0	0	0	0.0	5	0.0	33	0.1
TOTAL	21,180	100	17,288	100	14,827	100	15,327	100	19,869	100.0	25,354	100.0	22,901	100.0

Source: Statistics Department

Table 58: Exports by Country of Destination, 2006/07 – 2012/13

	2006/07		2007/08		2008/09		2009/10		2010/11		2011/12		2012/13	
COUNTRY	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%
New Zealand	4,244	20.0	5,278	31.4	5,283	35.6	3,264	21.3	3,269	16.5	4,801	18.9	6,550	28.6
Australia	1,303	6.2	817	4.9	1,743	11.8	693	4.5	581	2.9	4,622	18.2	1,437	6.3
Fiji	141	0.7	75	0.4	67	0.5	18	0.1	318	1.6	697	2.7	200	0.9
Mainland USA	2,581	12.2	2,939	17.5	2,636	17.8	2,551	16.6	2,685	13.5	2,651	10.5	3,590	15.7
Samoa	483	2.3	666	4.0	783	5.3	492	3.2	543	2.7	375	1.5	479	2.1
Japan	7,550	35.6	2,244	13.3	1,967	13.3	517	3.4	2,862	14.4	6,293	24.8	2,754	12
Korea	1,724	8.1	241	1.4	469	3.2	369	2.4	140	0.7	1,548	6.1	2,020	8.8
Singapore	48	0.2	104	0.6	17	0.1	458	3.0	2	0	30	0.1	171	0.7
American Samoa	443	2.1	635	3.8	428	2.9	178	1.2	213	1.1	282	1.1	323	1.4
Hong Kong	40	0.2	171	1.0	551	3.7	6,433	42.0	7,538	37.9	2,355	9.3	3,579	15.6
All other Countries	2,623	12.4	3,658	21.7	884	6.0	399	2.6	1,719	8.7	1,701	6.7	1,799	7.9
TOTAL	21,180	100.0	16,828	99.9	14,827	100.0	15,327	100.0	19,869	100	25,354	100	22,901	100

Source: Statistics Department

Table 59: Imports by Main HS Section, 2006/07 – 2012/13

HS Code	2006/07		2007/08		2008/09		2009/10		2010/11		2011/12		2012/13	
SECTION ITEM	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%
1. Live Animals; Animal Products	30,162	12.0	30,742	10.0	36,426	11.8	39,502	13.8	40,464	13	39,778	12	43,922	13
2. Vegetable Products	8,243	3.3	9,610	3.1	10,695	3.5	9,347	3.3	10,216	3	10,536	3	10,838	3
3. Prepared Foodstuff; Beverages & Tobacco	37,229	14.8	46,221	15.1	44,154	14.3	45,633	16.0	39,041	12	47,152	14	48,283	14
4. Mineral Products	67,621	26.9	78,863	25.7	81,117	26.2	64,715	22.6	80,726	25	88,675	26	82,697	24
5. Products of the Chemical or Allied	9,268	3.7	14,464	4.7	11,699	3.8	13,684	4.8	13,675	4	14,794	4	14,346	4
6. Wood and Articles of Wood	8,096	3.2	10,057	3.3	7,269	2.3	7,164	2.5	11,243	4	9,434	3	8,063	2
7. Pulp of Wood and Other Fibrous Cellulosic Material	8,679	3.4	9,283	3.0	11,298	3.7	9,148	3.2	10,302	3	12,139	4	12,980	4
8. Base Metals & Articles of Base Metal	12,582	5.0	13,619	4.4	13,893	4.5	13,373	4.7	26,286	8	20,563	6	15,214	4
9. Machinery and Mechanical Appliance	25,380	10.1	38,901	12.7	37,671	12.2	39,244	13.7	41,372	13	46,895	14	41,744	12
10. Miscellaneous Manufactured Articles	6,175	2.5	6,479	2.1	4,899	1.6	4,838	1.7	5,415	2	6,850	2	10,281	3
11. Vehicle, Aircraft, Vessel & Associated Transport Equipment	10,342	4.1	17,374	5.7	17,615	5.7	15,908	5.6	16,110	5	15,516	5	19,394	6
12. Works of Art, Collectors Pieces	12,282	4.9	13,765	4.5	14,899	4.8	4,073	1.4	1,194	0	1,074	0	7,948	2
12. Other Imports	15,537	6.2	17,639	5.7	17,710	5.7	19,126	6.7	21,583	7	32,005	9	29,957	9
TOTAL	251,596	100.0	307,017	100.0	309,344	100.0	285,754	100.0	317,628	100	345,411	100	345,662	100

Source: Statistics Department

Table 60: Imports by Institutional Sector, 2006/07 – 2012/13

	2006/07		2007/08		2008/09		2009/10		2010/11		2011/12		2012/13	
INSTITUTIONAL SECTOR	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%
Private Sector	231,272	91.9	291,762	95.0	294,348	95.2	277,502	97.1	297,987	93.8	300,026	86.9	308,225	89.2
Government Sector	11,162	4.4	12,457	4.1	11,114.10	3.6	5,119.80	1.8	9,227	2.9	23,737	6.9	21,284	6.3
Quasi-Government Sector	9,161	3.6	2,794	0.9	3,882.1	1.3	3,132.7	1.1	10,414	3.3	21,649	6.3	15,579	4.5
TOTAL	251,595	100.0	307,013	100.0	309,344	100.0	285,754	100.0	317,628	100	345,411	100	345,662	100

Source: Statistics Department

Table 61: Imports by Country of Origin, 2006/07 – 2012/13

	2006/07		2007/08		2008/09		2009/10		2010/11		2011/12		2012/13	
COUNTRY	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%
New Zealand	84,365	33.5	100,123	32.6	81,870	26.5	88,715	31.0	107,985	34	100,067	29	101,254	29
Australia	34,666	13.8	34,899	11.4	33,349	10.8	32,714	11.4	23,736	8	19,553	6	17,938	5
USA	25,795	10.3	26,348	8.6	35,884	11.6	41,273	14.4	35,741	11	46,652	14	40,695	12
China	13,218	5.3	17,795	5.8	41,411	13.4	31,007	10.9	25,861	8	29,260	9	27,878	8
Indonesia	3,683	1.5	4,839	1.6	5,184	1.7	3,700	1.3	3,965	1	6,157	2	4,954	1
Fiji	68,710	27.3	32,568	10.6	41,411	13.4	31,007	10.9	25,861	8	29,260	9	27,878	6
Japan	5,845	2.3	8,354	2.7	11,375	3.7	6,844	2.4	8,848	3	17,175	5	20,275	29
Singapore	5,883	2.3	63,666	20.7	62,679	20.3	50,039	17.5	73,804	23	78,725	23	81,146	24
Others	9,432	3.7	18,425	6.0	23,466	7.6	18,297	6.4	18,546	6	22,339	7	31,949	9
TOTAL	251,596	100.1	307,017	100	309,344	100.0	285,754	100.0	317,628	100	345,411	100	345,662	100

Source: Statistics Department

Table 62: Tonga Balance of Payment, 2006/07 – 2012/13

<i>(In millions of pa'anga, unless otherwise indicated)</i>	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
Balance of Trade	244.2	-239.0	-259.9	-196.6	-218.4	-239.1	-248.6
Exports, f.o.b.	26.7	23.5	11.4	11.4	11.2	8.7	12.3
Of which: Squash exports	5.6	2.7	1.8	0.5	0.7	2.2	2.4
Imports, f.o.b.	217.5	262.5	271.3	208	229.6	247.8	260.9
Services (net)	-35.9	-6.2	-5.4	-7.9	4.9	-4.3	6.3
Receipts	38.8	70.1	83.7	71.8	89	99.4	125.2
Of which: Tourism receipts	24.1	33.3	36.7	50.1	60.9	61.7	70.2
Payments	-74.7	-76.3	-89.1	-79.8	84	103.7	118.8
Income (net)	7.1	6.4	57.6	5.3	4.9	5.6	0.9
Receipts	12.9	13.0	64.0	14.7	13.1	13.3	11.7
Payments	-5.8	-6.6	-3.4	-9.4	8.2	7.7	10.8
Current Transfers (net)	168.6	180.2	157.9	146.6	136.4	182.4	174.8
Official transfers (net)	-0.1	0.5	1.2	1.9	29.3	47.0	5.0
Private transfers (net)	168.7	179.7	156.7	144.7	147.8	175.3	246.5
Official transfer receipts	0.5	0.8	2.5	5.7	8.3	45.5	3.5
Official transfer payments	-0.6	-0.3	-1.3	-3.8	21	1.5	1.5
Private transfer receipts	186.8	202.8	175.2	157.4	139	156.8	209.5
Private transfer payments	-18.1	-23.1	-18.5	-12.7	8.8	18.5	37
Current account balance	-50.9	-58.6	-49.8	-52.6	-72.1	-55.4	-66.5
(Percent of GDP)							
Capital account balance	53.9	69.0	117.6	58	124.4	87.5	88.6
Official capital (net)	19.7	22.8	37.0	28.6	68.9	55.1	33.5
Official capital inflows	24.7	26.5	66.4	43	110.6	61.6	38.2
Official capital outflows	-5.0	-3.7	-29.4	-14.4	41.7	6.5	4.7
Private capital (net)	34.2	46.2	80.6	29.4	55.5	32.4	55.1
Private capital inflows	39.9	50.5	88.9	38	77.8	45.2	71.5
Private capital outflows	-5.7	-4.3	-8.3	-8.6	22.3	12.7	16.3
Overall balance	8.4	-2.5	47.2	34.2	31.0	38.3	17.3
Memorandum items:							
Service, income, and transfers (net)	139.7	180.9	214.3	145.8	400.7	493.4	523.0
Receipts	239.0	286.7	325.4	249.6	249.4	315.0	349.9
Payments	-99.2	-106.3	-112.3	-105.7	122.0	131.4	168.1
Gross official foreign reserves (TOP million)	91.6	89.1	136.3	170.5	203.8	246.1	263.3
Months of Import cover	4.4	3.5	5.1	7.1	7.4	8.2	8.8

Source: National Reserve Bank of Tonga

Table 63: Tonga Monetary Survey, 2006/07 – 2012/13

(In millions of Pa'anga, unless otherwise indicated)	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
Net foreign assets	81.7	79.9	121.3	164.8	215.2	235.3	258.6
Foreign assets	103.6	99.9	154.0	186.7	221.6	251.0	268.8
Foreign liabilities	-21.9	-20.0	-32.7	-21.9	-6.5	-15.7	-10.2
Net domestic assets	179.3	202.9	156.2	126.6	84.1	57.9	56.4
Net domestic credit	251.3	286.4	274.0	243.1	208.4	165.5	167.4
Government (net)	-11.7	-29.1	-32.7	-29.1	-32.5	-47.1	-29.2
Non-financial public enterprises	2.5	3.7	3.9	19.6	13.2	10.1	13.1
Private sector	260.5	311.8	302.8	252.6	227.7	202.5	183.5
Non-monetary financial institutions 1/	-6.3	-4.2	-11.7	-8.1	-10.9	-7.2	-8.8
Other items (net)	-65.7	-79.3	-106.1	-108.4	-113.4	-100.4	-102.2
Total domestic liquidity (M2)	261.0	282.8	277.3	291.5	299.2	293.2	314.9
Narrow money (M1)	73.8	72.6	77.9	90.1	96.9	118.1	152.1
Currency outside banks	18.5	18.8	21.9	26.8	27.3	31.3	32.1
Demand deposits	55.3	53.8	56.0	63.3	69.7	86.8	120.0
Quasi money	187.2	210.2	199.4	201.4	202.3	175.1	162.7
Savings deposits	49.3	48.8	43.6	46.4	51.0	41.4	43.0
Term deposits	125.2	150.1	143.0	142.9	139.5	121.8	110.1
Foreign currency accounts	12.8	11.3	12.8	12.0	11.8	11.9	9.7
Annual Percentage Change							
Net foreign assets	12.6	-2.2	51.8	35.9	30.6	9.3	9.9
Foreign assets	9.0	-3.6	54.2	21.2	18.7	13.3	7.1
Foreign liabilities	-2.5	-8.7	63.7	-33.1	-70.3	141.5	-35.0
Net domestic assets	14.7	13.2	-23.0	-18.9	-33.6	-31.2	-2.6
Private sector	11.4	19.7	-2.9	-16.6	-9.9	-11.1	-9.4
Total domestic liquidity (M2)	14.0	8.4	-1.9	5.1	2.6	-2.0	7.4
Narrow money (M1)	32.5	-1.6	7.3	15.7	7.5	21.9	28.8
Quasi money	8.1	12.3	-5.1	1.0	0.4	-13.4	-7.1
In Us dollars							
Net foreign assets	41.9	43.2	60.2	84.4	127.2	134.2	141.8
Foreign assets	53.2	54.0	76.5	95.6	131.0	143.1	147.4
Foreign liabilities	-11.2	-10.8	-16.3	-11.2	-3.8	-9.0	-5.6
Memorandum items:							
Velocity (GDP/average M2)	2.3	2.3	2.4	2.4	2.6	2.7	2.6
Exchange rate (pa'anga per U.S. dollar; end period)	1.95	1.85	2.01	1.95	1.69	1.75	1.82

Source: National Reserve Bank of Tonga

Table 64: Sovereign Debt Sustainability Indicators

Indicators	IMF (GOT) Max Target (%)	FY 2012/2013 Actual (%)	FY 2013/2014 Estimate (%)
NPV of external debt as:			
% of GDP	40	41	40
% of GDP (& remittances)	36	36	32
% of exports	150	222	205
% of exports (& remittances)	120	128.	90
% of recurrent revenue	250	215	208
Total Debt Service as:			
% of exports	20	13	12
% of exports (& remittances)	16	8	5
% of recurrent revenue	20	13	12

Numbers in Red represents those above threshold – IMF Target

Source: Ministry of Finance and National Planning

Table 65: Summary Debt Levels and Ratios

<i>Particulars</i>	<i>Jun-13</i>	<i>Sep-13</i>	<i>Dec-13</i>	<i>Mar-14</i>	<i>Jun-14</i>
Total Public Debt (USD\$)	204.4	205.9	205.8	205.6	204.6
Total Public Debt (TOP\$)	372.6	370.2	378.7	370.7	368.2
Domestic Debt	29.5	29.5	29.5	29.5	29.5
External Debt	343.1	340.7	349.2	341.2	338.7
Total Public Debt to GDP (%)	44.6%	42.0%	44.7%	43.8%	43.5%
External Debt to GDP	3.5%	3.3%	3.5%	3.5%	3.5%
Domestic Debt to GDP	41.0%	38.7%	41.3%	40.3%	40.0%
Total Debt Service (\$)	20.4	4.0	6.6	3.07	19.5
External	11.1	3.5	5.9	3.07	12.1
Domestic	9.3	0.5	0.7	0	7.5
Principal	13.3	1.1	3.1	0.7	12.3
Interest	7.1	2.9	3.5	2.4	7.2
External Debt by Creditor category	343.1	340.6	349.2	341.2	338.7
Multilateral	114.3	114.5	115.7	118.1	116.7
Bilateral	228.4	225.7	233.1	222.7	221.7
Commercial	0.4	0.4	0.4	0.4	0.298
Debt Composition by Instrument Type (\$)	372.6	370.2	378.7	370.7	368.19
Loans	343.1	340.7	349.2	341.2	338.69
Bonds	29.5	29.5	29.5	29.5	29.5
Foreign Currency Risk (%)					
% of debt in Chinese Yuan	66.6%	66.3%	66.8%	65.3%	65.5%
% of debt in SDR	33.2%	33.5%	33.0%	34.5%	34.4%
% of debt in other currencies	0.2%	0.2%	0.2%	0.2%	0.2%
% of Foreign Debt	92.1%	92.0%	92.2%	92.0%	92.0%
Fiscal Indicators (%)					
Total Debt Service to Expenditure	11.4%	2.0%	3.3%	1.7%	10.6%
Total Debt Service to Revenue	12.8%	2.5%	4.0%	1.9%	12.0%
Interest to Expenditure	4.0%	1.5%	1.8%	1.3%	3.9%
Interest to Revenue	4.4%	1.8%	2.1%	1.5%	4.4%
Vulnerability Indicators (%)					
Reserves to External Debt	75.3%	75.9%	76.0%	75.6%	83.0%
External Debt Service to Exports & Remittances	4.1%	1.2%	2.2%	0.8%	3.2%
External Debt Service to Exports	7.2%	2.2%	3.8%	1.9%	7.3%

Source: Ministry of Finance and National Planning

Table 66: Details of the terms and conditions of the 2 major loans from China

	Nuku'alofa CBD Reconstruction	Tonga National Road Improvement Project
Maturity Period	CNY 440m, est T\$127m	CNY 291m, est T\$85m
Maturity Period	20 yrs from effective date (10 yrs grace period for principal, 10 yrs principal repayment)	20 yrs from effective date (10 yrs grace period for principal, 10 yrs principal repayment)
Payment Frequency	21 st day of Sept and Mar annually (1 st interest payment 21 Mar 2009, rescheduled 1 st principal payment 21 Sept 2018, last payment 21 Sept 2028)	21 st day of Sept and Mar annually (1 st interest payment 21 Mar 2010; rescheduled 1 st principal payment 21 Mar 2020, last payment 21 Mar 2030)
Interest Rate (IN)	2% per annum over 360 daily basis (from 1 st drawdown date on 24 Sept 2008)	2% per annum over 360 daily basis (due from 1 st drawdown date on 15 Mar 2010)
Management Fee (MF)	1% on loan amount (paid 12 Sept 2008, for lump sum due 30 days from effective date and before first drawdown date);	1% on loan amount (paid 25 Feb 2010, for lump sum due 30 days from effective date and before first drawdown date)
Commitment Fee (CF)	0.75% per annum on undrawn loan balance (due 30 days after effective date)	0.75% per annum on undrawn loan balance (due 30 days after effective date)
Total Paid	\$12.4m	\$6.5m
IN	\$9.4m	\$5.1m
MF	\$1.3m	\$0.8m
CF	\$1.7m	\$0.6m

Source: Ministry of Finance and National Planning

Table 67: Reconstruction Loan Project Allocation

<i>CBD Project (TOPm)</i>	<i>Total Loan</i>	<i>Total to Loan (%)</i>
Tungi Colonnade Ltd	16.6	13%
OG Sanft & Sons Ltd	10.2	8%
MF Taumoepeau & Sons Ltd	7.2	6%
City Assets Ltd	6.8	5%
Royco Amalgamated Co. Ltd	2.2	2%
<i>Total On-lent projects</i>	<i>42.9</i>	<i>34%</i>
Vuna wharf	33.9	27%
Civil works	19.7	15%
Palace extension	14.5	11%
Asphalt Plant	5.3	4%
<i>Total GoT projects</i>	<i>73.4</i>	<i>58%</i>
Design	3.8	3%
Contingency	2.7	2%
Mobilisation	1.8	1%
Consultancy	1.4	1%
Insurance	0.7	1%
Geographic report	0.6	0%
<i>Total CCECC costs</i>	<i>11.0</i>	<i>9%</i>
TOTAL LOAN	127.3	

Source: Ministry of Finance and National Planning

Table 68: Road Improvement Loan Project Allocation

<i>Projects (TOPm)</i>	<i>Total Loan</i>	<i>Total to Loan (%)</i>
Tongatapu	56.7	67.3%
Vava'u	7.0	8.3%
Ha'apai	1.9	2.3%
Eua	2.6	3.0%
Establishment	1.7	2.1%
Mobilisation	1.9	2.2%
Road survey, geographical, prospecting, geography report	1.7	2.1%
Road designing	6.7	8.0%
Consultant fee	2.5	3.0%
Insurance	0.5	0.6%
Contingency sum	0.9	1.1%
TOTAL LOAN AMOUNT	84.2	

Source: Ministry of Finance and National Planning

Table 69: On-lent Loans, as at 30 June 2014

	<i>Jun-13 (\$m)</i>	<i>Jun-14 est. (\$m)</i>
TDB	2.9	2.5
TCC	0.9	0.0
Seastar	3.7	3.6
Janfull	11.3	11.1
Ports Authority	0.7	0.6
Talamahu	1.8	1.8
Royco	2.2	2.2
Taumoepeau	7.2	7.2
Sanft	10.3	10.3
City Assets	6.8	6.8
Tungi Colonnade	16.6	16.6
Total	64.1	62.6

Source: Ministry of Finance and National Planning

Table 70: Development Expenditure by All Development Partner (Cash+ Inkind, grant+loan)

Development Partners	Budget Estimate 2013-14	Revised Estimate 2013-14	Budget Projection 2014-15	Budget Projection 2015-16	Budget Projection 2016-17
Australia Bilateral	15.92	7.68	11.91	7.72	7.86
Aust Defense	0.7	1.1	0.2	0.3	0.3
Aust Other	0.05	0.6	0.15	0.03	0.03
Germany	0.12	-	-	-	-
Japan Government	-	10.43	-	10	20
Japan TTP	2.31	3	36	17	2
Pooled Funds	10.75	7.23	10.63	7.77	7.42
New Zealand Bilateral	12.2	14.07	19.51	15.6	13.22
People's Republic of China	37.88	15.25	34.7	15.5	0.5
United Kingdom	0.8	1.23	0.4	-	-
Korean Fund	0.3	0.44	0.3	-	-
NZ - Other Government	-	0.05	-	-	-
Republic of Nauru	-	-	0.04	-	-
Inter-Parliamentary Union	-	0.06	-	-	-
Asian Development Bank	29.47	13.81	26.58	16.77	10.27
World Bank/International Development Agency	23.58	22.04	66.51	8.1	15
United Arab Emirates (UAE)	4	0.09	-	-	-
Commonwealth Fund Tech Coop	0.02	0.13	0	-	-
UNESCO	0.02	0.02	0.03	0.03	0.03
European Union	2.75	0.87	9.3	2.97	2.97
Pacific Island Forum Secretariat	7.3	-	4	4.1	-
Government of Turkey	-	-	0.09	-	-
Secretariat of the Pacific Communities	1.28	0.61	1.61	0.57	0.48
South Pacific Regional Environmental Program	0.72	1.5	0.4	0.2	0.1
United Nation Development Program	1.55	4.7	3.6	4.17	1.04
United Nation Family Planning Association	0.1	0.1	0.8	0.5	0.5
Food & Agriculture Organization	0.66	-	0.31	0.01	0.01
International Labour Organization	-	0.01	-	-	-
World Health Organization	-	0.5	1.5	1.5	1.5
South Pacific Geoscience Commission	0.11	0.04	0.11	-	-
United Nations Environmental Program	0.2	0.16	0.2	0.2	-
Forum Fisheries Agency	0.52	0.22	0.5	0.65	0.23
Commonwealth Local Government Fund	0.04	0.04	-	-	-
International Union for Conservation of Natural Resources	0.51	0.06	0.39	0.39	0.34
ASTAE Grant	-	-	-	-	-
Tonga Trust Fund	0.85	0.85	-	-	-
Local Level Contributions	-	-	-	-	-
Other Donors	2.66	2.76	7.91	23.5	11.28
Unconfirmed Donors	1.45	1.18	10.71	62.66	100.39
Grand Total	158.81	110.82	248.38	200.24	195.47

Source: Ministry of Finance and National Planning

Table 71: Health Indicators for Tonga 2007 - 2011

	Indicator	2007	2008	2009	2010	2011
1	Estimated Population (000)	103.3	102.3	103.1	103.6	103.3
2	Annual Population Growth	0.3	0.3	0.3	0.3	0.2
3	Percentage of Population less than 14 years (per 100)	38	38	38	38	38
	Percentage of population 65 years and over (per 100)	6	6	6	6	6
4	Percentage of Urban population (per 100)	23	23	23	23	23
5	Rate of natural increase (per 1,000)	21.3	21.6	19.9	20.7	20.4
6	Crude Birth Rate (per 1,000)	26.5	26.7	25.4	26	26.8
7	Crude Death Rate (per 1,000)	5.2	5.1	5.5	5.3	6.4
8	Maternal Mortality Rate (per 100,000)	36.5	76.1	114.4	37.1	0
	Life Expectancy at Birth (combined)					
9	Life Expectancy (Male)	70	70	70	65	65
	Life Expectancy (Female)	72	72	72	69	69
10	Infant Mortality Rate (per 1,000)	11.7	16.4	14.5	21.5	15.2
11	Perinatal Mortality Rate (per 1,000 live births)					
	Total Health expenditure (000)	17761	21580	21375	22500	22596
12	Per Capita	172	210	207	217	tbc
	As a percentage of total recurrent budget	7.5	10	12	10.1	tbc
	Health Workforce					
13	Medical Officers at post	58	59	55	45	55
	Health Officers at post	17	19	22	21	20
	Nursing and Midwifery at post	302	346	355	tbc	311
14	Percentage of population with safe water supply	98	99	99.9	99	99.9
15	Percentage of household with adequate sanitary facilities	99.6	98	99.7	99	99.5
16	Immunization coverage	99.6	99.5	99.5	99.6	99.8
17	Percentage of pregnant women immunized with tetanus toxic 2	97.6	99.5	99.5	99.6	99.8
18	Percentage of population with access to appropriate health care services with regular supply of essential drugs within one hours walk	100	100	100	100	100
19	Percentage of infants attended by trained personnel	100	100	100	100	100
20	Percentage of married couples practicing contraception	27.7	27	29.8	28.4	33.3
21	Percentage pregnant women attending ante natal care	98.7	98	98.6	97.7	98.6
22	Percentage of deliveries conducted by trained personnel	98	97	98.1	99	98
23	Total Fertility Rate	3.7	3.7	3.7	3.8	3.7
	Source: Ministry of Health					

Table 72 : Full GFS2001 Fiscal Details

	Actual 2012/13	Budget Estimate 2013/14	Revised Estimate 2013/14	Budget Estimate 2014/15	Projection 2015/16	Projection 2016/17
Revenue	251.9	350.9	302.3	436.9	406.6	405.8
Taxes	132.7	135.5	136.7	141.4	152.2	156.4
Taxes on income, profits, and capital gains	30.3	25.2	25.0	29.9	33.3	33.9
Taxes on property	0.7	0.1	0.1	0.2	0.2	0.2
Taxes on goods and services	86.9	95.0	96.3	95.5	101.5	103.5
Taxes on international trade and transactions	14.7	15.2	15.3	15.8	17.1	18.8
Other taxes	-	0.0	0.0	0.0	0.0	0.0
Grants	99.5	193.6	143.6	267.6	224.6	219.2
Current	52.7	114.0	116.0	116.2	112.5	98.9
Capital	46.9	79.6	27.6	151.4	112.1	120.2
Other revenue	19.6	21.8	22.1	27.9	29.8	30.2
Property income [GFS]	6.7	7.3	9.2	12.0	12.3	12.4
Sales of goods and services	11.5	13.1	11.5	15.2	16.7	17.0
Fines, penalties, and forfeits	0.4	0.5	0.5	0.6	0.6	0.6
Voluntary transfers other than grants	0.7	0.9	0.9	-	-	-
Miscellaneous and unidentified revenue	0.2	0.0	0.1	0.2	0.2	0.2
	203.0	257.8	265.7	294.7	262.2	269.3
Expense	203.0	257.8	265.7	294.7	262.2	269.3
Compensation of employees	94.9	102.4	105.4	121.8	117.0	118.7
Wages and salaries	84.5	92.5	95.5	101.9	105.8	107.2
Social contributions	10.5	9.9	9.9	19.9	11.2	11.5
Use of goods and services	76.1	119.8	122.7	130.8	102.9	108.4
Interest	7.1	7.6	7.6	6.8	8.2	8.1
To nonresidents	5.3	6.0	6.0	5.3	5.6	5.5
To residents other than general government	1.9	1.6	1.6	1.5	2.6	2.6
Subsidies	0.8	0.3	0.3	0.1	0.1	0.1
Subsidies to public corporations	0.7	-	-	-	-	-
Subsidies to private enterprises	0.1	0.3	0.3	0.1	0.1	0.1
Grants	2.5	2.2	1.9	2.2	2.2	2.2
Social benefits	13.8	14.8	16.5	19.2	19.1	19.1
Other expense	7.7	10.7	11.3	13.8	12.7	12.7
Gross Operating Balance	48.9	93.1	36.6	142.2	144.4	136.5
				142.2		
Net Acquisition Of Nonfinancial Assets	56.6	79.1	28.0	156.0	134.6	130.6
Fixed assets	56.6	79.0	27.9	155.9	134.5	130.5
Buildings and structures	5.8	17.7	5.2	85.8	94.4	105.5
Machinery and equipment	34.1	51.1	18.3	48.3	36.4	21.1
Other fixed assets	16.7	10.2	4.5	21.8	3.8	3.8
Nonproduced assets	0.1	0.1	0.1	0.1	0.1	0.1
Land	0.1	0.1	0.1	0.1	0.1	0.1
Net Lending/Borrowing Requirement	7.7	-14.0	-8.6	13.8	-9.8	-5.9
Net Acquisition Of Financial Assets And Liabilities (Financing) [assets-liabilities]	7.7	-14.0	-8.6	13.8	-9.8	-5.9
Financial Assets	-5.5	-0.6	4.0	17.6	5.3	5.3
Domestic	-5.5	-0.6	4.0	17.6	5.3	5.3
Currency and deposits	-6.5	0.0	5.2	0.0	0.0	0.0
Loans	0.3	-0.7	-1.3	11.4	-0.9	-0.9
Shares and other equity	0.7	0.1	0.1	6.2	6.2	6.2
Financial Liabilities	2.3	-14.6	-4.6	31.3	-4.4	-0.6
Domestic	-	0.7	1.0	20.0	0.1	3.4
Foreign	2.3	-15.3	-5.7	11.3	-4.5	-4.0

Source: Ministry of Finance and National Planning

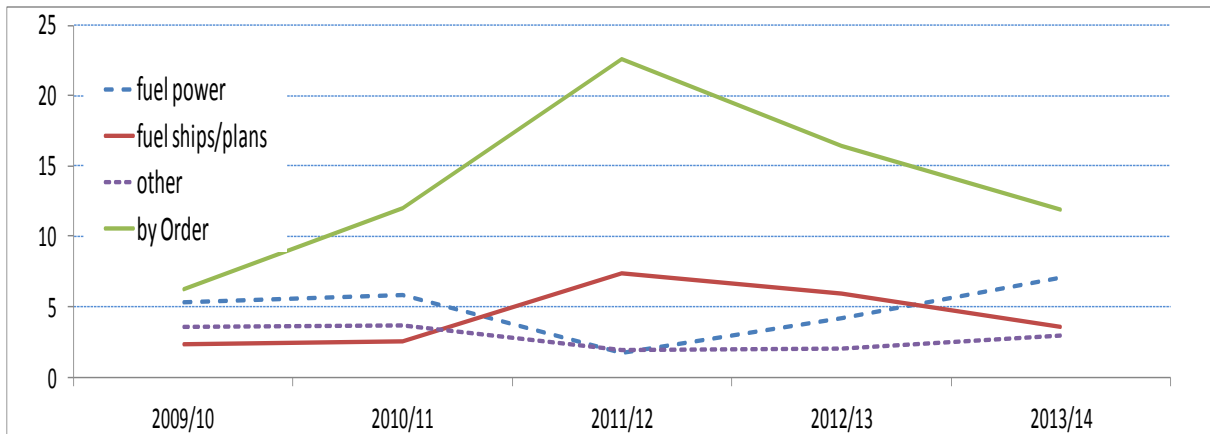
**Table 73 : Tax Expenditure: exemptions by type of tax and key category
(\$ million and % total)**

	2012/13				2013/14			
	CT	Duty	Excise	Total	CT	Duty	Excise	Total
fuel power	0.5	-	3.6	4.1	0.9	-	6.1	7.0
fuel ships/plans	0.8	-	5.2	5.9	0.7	0.0	2.9	3.6
by Order	9.6	3.9	2.9	16.4	7.6	2.5	1.8	11.8
other	0.7	0.4	0.9	2.0	1.0	0.7	1.2	3.0
total	11.6	4.4	12.5	28.5	10.1	3.3	12.0	25.4
fuel power	5%	0%	29%	15%	9%	0%	51%	28%
fuel ships/plans	7%	0%	41%	21%	6%	0%	24%	14%
by Order	83%	90%	23%	58%	75%	77%	15%	47%
other	6%	10%	7%	7%	10%	23%	10%	12%
total	100%	100%	100%	100%	100%	100%	100%	100%

Source: Ministry of Revenue and Customs data

NB: "By Order" covers all exemptions granted by Order of Cabinet and gazetted. These may apply to a whole sector, or may apply to individual businesses: the data is not separated between these two.

**Tax Expenditure Chart: total exemptions for all taxes by key category
2009/10 to 2013/14 (preliminary) (\$ millions)**



Source: Ministry of Revenue and Customs data