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WBG Governor's Statement No. 13

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Statement by the Hon. **TEVITA LAVEMAAU**,
Governor of the Bank for **TONGA**

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Governor of the Bank for Tonga

Mr. Chairman,
Mr. President of the World Bank Group,
Madame Managing Director of the International Monetary Fund,
Fellow Governors,
Distinguished delegates,
Ladies and Gentlemen,

It is truly a great honour and privilege for me, as Minister of Finance and Governor of the Bank and the Fund for Tonga, to have this opportunity to address the International Monetary Fund (IMF or Fund) and World Bank Group (Bank or WBG) Joint Board of Governors 2020 Virtual Annual Meetings on behalf of the Government of the Kingdom of Tonga.

During these unprecedented challenging times due to COVID-19 pandemic, I wish to convey my sincere appreciation and gratitude to Mr. President David Malpass and Madame Managing Director Kristalina Georgieva and both their entire management teams, for their significant contributions and astral leadership at the helm of our Bretton Woods institutions. This has facilitated quick response and special attention towards the developing member countries including Tonga to address the socio-economic fallout from the pandemic, and pave the way for a resilient and inclusive recovery, amid the rising debt burden of vulnerable small island developing states and escalating climate change and natural disasters risks.

We wish to express our deepest sympathy to the scores of lives and loved ones across the world, that have been lost during this pandemic. We wish to acknowledge with solidarity all those working tirelessly on the front lines fighting the pandemic.

Challenging Time

The global economy continues to experience an exceptional negative shock due to the continuous spread of COVID-19 cases and the lack of clear solutions of this pandemic. Member countries have been facing extraordinary needs due to weak health systems, limited fiscal space, and heavy dependence on remittances as a source of income. In addition, the severity of climate change, fragility and high poverty level have limited member countries' options to respond to the COVID-19 and even so with developing economies.

The pandemic has disrupted global trade, supply chains and investment flows. It has left financial and human capital idle, while remittances, transport revenues, and income from tourism have rapidly diminished. In addition, steep drops in commodity prices have harmed commodity-dependent economies. The pandemic has profoundly impacted human capital, including lives, learning, basic wellbeing, and future productivity.

Disruptions in the delivery of essential services and food, combined with employment and income loss for households, are evidently devastating. The pandemic has caused most major economies to lose at least 2.4 percent of the value of their gross domestic product (GDP) in 2020, with potential scarring effects on employment and growth prospects for all countries. In the US for example, the initial jobless claims averaging nearly one million over the four weeks leading to mid-September, well above its peak during the global financial crisis. Although most Pacific Island countries are still COVID-19 free, according to recent projections, the Pacific economies are projected to contract by 5 to 10 percent this year.

Tonga: COVID-19 Impact and Responses

To date, Tonga still remains COVID-19 free which we are very pleased about. However, Tonga's main challenge is its human and financial resources to deal with the pandemic.

Tonga's economy is severely impacted with the forecast now of negative 3.0 percent for FY2019/20 and negative 5.8 percent in FY2020/21. The tourism and associated sectors have been significantly affected due to the closure of Tonga's border as well as the damages of tourist facilities from Tropical Cyclone (TC) Harold. There has been loss of employment opportunities and reduced hours of works; as well as significant loss of income of private sector businesses especially for Small Medium Enterprises (SMEs).

On the other hand, remittances is still holding up but we are expecting to see a downturn going forward. Likewise, the foreign reserves is at 8 months of imports cover which is comfortably above the minimum threshold, largely due to the ongoing flow of remittances and budget support. The lower global oil prices and local food prices have contained inflation with the annual inflation rate at negative 1.6 percent in August 2020. The financial system remains sound supported by the excess liquidity and banks' strong profitability and capital positions.

Fiscal Policy

The COVID-19 pandemic has impacted the revenue streams. We have an estimated loss of revenue of about USD 20 million and could be more for FY2021 and an estimated significant deficit of about USD 30 million.

Prudent fiscal measures are taken to monitor spending including controlling the wage bill while closely reviewing revenue measures, including exemptions and deferrals granted to support affected individuals and businesses.

While we have considered all options including loans for financing the budget deficit, non-debt options are preferred given that Tonga is already at high risk of debt distress. Therefore, we seek WBG and IMF's support in urging multilateral development banks to support Tonga in the form of grants. This should provide fiscal space to combat COVID-19, maintain normal operation, and to support the path to recovery.

Government is implementing its economic and social stimulus package to combat COVID-19. The package includes assistance to the affected social and economic sectors and the most vulnerable citizens. About 78.0 percent of the stimulus package is sourced from

grants from development partners including the WBG which we fully acknowledge and thankful for.

To retain Tonga's COVID-19 status, Government is doing its best to build up its capacity while taking preventative measures to contain the adverse impact of the pandemic. This includes the declaration of state and health emergencies, an Open Border policy with a focus on repatriation, and implementation of the COVID-19 Action Plan.

Monetary Policy

The National Reserve Bank of Tonga (NRBT) maintained accommodative monetary policy stance to buttress domestic economic growth and provide liquidity support, while remaining vigilant to risks to financial stability. Key monetary policy measures over the medium term continue to encourage the banks to utilize the excess liquidity productively and prudently, which includes maintaining the: (i) monetary policy rate at 0 percent; (ii) minimum loan/deposit ratio at 80 percent; (iii) Statutory Reserve Deposit ratio at 10 percent; and (iv) inflation reference rate of 5 percent. In addition to providing financial support to the Government's COVID-19 stimulus package, the NRBT stands ready to provide further assistance to support the banking system if needed while preserving financial stability. Timely and effective engagement with banks and all stakeholders is critical to maintain public confidence in the financial system and to ensure essential financial services are available in line with the national directives and requirements. The commercial banks have offered loan moratoriums and restructuring to support their customers who are affected by the global pandemic and TC Harold. The NRBT has strengthened its supervisory role by closely monitoring developments in both the banking and non-banking sectors for early identification and addressing of vulnerabilities that may impair the stability of the financial system.

Partnerships

The exceptional global challenges require timely, decisive, collective and innovative responses to overcome the severe socio-economic effects of COVID-19. We concur that multilateral partnerships and all other partnerships should be positioned, at these unprecedented times, to tackle these complex issues and the Bank and Fund should play a leading role via their lending, investments, knowledge, and convening capacity. Reviving prosperity and financial sustainability of developing economies would enable the achievement of the Sustainable Development Goals and other International Agreements. Going forward, the Bank and the Fund should remain agile and continue to adapt their policies to the evolving challenges faced by the membership and strengthen their role in coordinating multilateral solutions.

Partnership with WBG

We appreciate the WBG's effort in playing a key role in assisting member countries through this crisis with advice, capacity development and financing, that will be critical to resilient, inclusive, and sustainable recovery. We commend the WBG for the speedy response and scale-up of its COVID-19 facility across its member countries, including Tonga through the Crisis Response Window (CRW), Contingency Emergency Response Component (CERC) instrument, Pacific Catastrophe Risk Assessment and Financing

Initiative (PCRAFI) insurance, and the International Development Association (IDA) development policy operations.

These efforts have helped strengthen Tonga's health system and Government's economic stimulus package, to assist containing the impact of the pandemic, thus increasing preparedness and resilience against future pandemics. **We trust that through our collaboration and partnership we will be able to bounce back and recover well from this downturn that we are facing today.**

We are hopeful that the efforts to find a vaccine will come to fruition soon; however, we are pleased with the recent approved funds for IDA and International Bank for Reconstruction and Development (IBRD) countries to support vaccine purchase and deployment. Therefore, we support our small state family in requesting the WBG to assist with affordable and equitable access to tests, treatments, and vaccines for its member countries, especially those in the developing countries who are mostly affected by this pandemic crisis.

In this context, we would like to urge the Bank and other relevant agencies to give special attention to small island developing states, with small population like Tonga with only over a 100,000 people, to be able to have full coverage when a vaccine is found.

We are aware that digital technologies can secure vital medical consultations, maintain educational services, and allow businesses to survive. We, thus welcome WBG operations that are expanding digital connectivity while safeguarding security and data privacy, broadening the reach of digital financial services and supporting digital transformation. These efforts help the member countries firm their adaptation to the crisis, enhance competitiveness, maintain employment, and continue the delivery of critical services, including in education, health, social protection, and access to finance.

We also welcome the swift work by the WBG to approve an initial \$14 billion COVID-19 response package, including a **Multiphase Programmatic Approach (MPA)**, aimed at combatting the spread and mitigating the effects of COVID-19 in all recipient countries including Tonga, as well as International Finance Corporation (IFC) investments in trade finance, working capital, and companies in the real sector, to support the crisis response. Moreover, we fully support the WBG's aim to increase the volume of its assistance substantially to support further economic and social response and recovery efforts over the next 15 months. We note the special attention that the Bank gives to human capital in Tonga to improve its Human Development Index (HDI) which is currently at 0.53, according to the WBG HDI 2020 update report. This significant capacity reflects the financing and reform implementation associated with the 2018 capital increase package and record Nineteenth Replenishment of the IDA-19.

We also appreciate the joint World Bank Group-IMF initiative to establish the G20 **Debt Service Suspension Initiative (DSSI)**, calling on official bilateral lenders to suspend all debt payments for IDA countries. Tonga has been approved by its main creditor to benefit from the DSSI, which frees up fiscal space to implement the COVID-19 Plan. At the same time, work is in progress to complete the requirements for Tonga's application to access

the **Rapid Credit Facility (RCF)** from the IMF, while awaiting the finalisation of the debt management strategy to assist in managing future loan repayments.

Hence, we would like to support the request to further extend the DSSI to the end of 2021, and to encourage all official bilateral creditor institutions to participate; and for the WBG and IMF to support debt relief especially for Small Island Developing States (SIDS) like Tonga with high exposure to natural disasters and climate change.

Partnership with IMF

The Fund's steadfast efforts to assist the membership in addressing the socio-economic impact of the COVID-19 pandemic is commendable. We welcome the Managing Director's Global Policy Agenda which rightly focuses on helping members navigate the crisis, restore confidence, and promote a more resilient global economy, while protecting the most vulnerable people and countries. We underscore the importance of flexibility and pragmatism in the Fund's approach taking due consideration of countries' specific circumstances including small states like Tonga with limited policy space, tools and access to finance.

We welcome the Fund's effort to enhance surveillance during and beyond the COVID-19 crisis. Ongoing engagement with country authorities and practical policy advice is critical in informing the authorities' policy decisions. To this end, we welcome the resumption of bilateral surveillance which has included small states with significant vulnerabilities such as Tonga with its Article IV consultation to begin in November 2020. More up to date assessments of the country's economic performance and challenges also help to inform Tonga's negotiations with its development partners. We support the ongoing policy work to attune the surveillance toolkit to members' evolving needs such as the comprehensive surveillance review and integrated policy framework.

We acknowledge the Fund's enhanced focus on small states and look forward to the Independent Evaluation Office's (IEO) review of the Fund's engagement with small states. This would help strengthen the quality, evenhandedness and effectiveness of future Fund engagement with small states.

A slow recovery is envisaged for small states as the pandemic intensifies the pre-existing challenges such as high vulnerability to natural disasters, narrow production base and lack of economies of scale. This calls for tailored and innovative policy guidance on workable fiscal and debt management options to support growth and ways to get around the domestic constraints while maintaining debt sustainability. Additionally, policy advice to better prepare for the materialization of risks to financial stability would be necessary. Beyond the crisis, addressing debt vulnerabilities remains a priority and we look forward to the Fund's continued assistance on ensuring Tonga's debt sustainability and supporting its debt management capacity. We also welcome the Fund's agenda to support ongoing digital transformation to expedite and foster a resilient recovery.

We note the Fund's work on climate issues to help enhance countries' mitigation and adaption policies. Building resilience to natural disasters and climate change is paramount for highly vulnerable small states like Tonga. We underscore the need to proceed with the

next steps for Tonga's climate change policy assessment (CCPA), particularly fast-tracking access to international climate finance. Continued coordination with the Bank and other stakeholders to leverage on their expertise in this area is warranted.

We appreciate the refinements to the Fund's lending toolkit to meet the members' exceptional financing needs during the crisis. Tonga's request to access the RCF will benefit from the approved temporary higher access limits for the emergency financing facilities. We support the ongoing efforts to enhance the lending toolkit while ensuring the Fund is well-resourced to meet members' financing needs. All funding options should be considered in light of the extraordinary circumstances to ensure the Poverty Reduction and Growth Trust (PRGT) is adequately resourced to accommodate any future financing needs from low income countries (LICs) who are facing multiple shocks including Tonga, during and beyond the pandemic. We also support ongoing fundraising efforts to enable subsequent debt relief for LICs under the Catastrophe Containment and Relief Trust (CCRT).

We take positive note of the Fund's efforts to swiftly adapt its capacity development (CD) delivery to meet members' needs in the wake of the COVID-19 crisis. Continuing to align CD with the priorities identified in the surveillance and lending activities ensures CD remains tailored to meet countries' evolving needs. We acknowledge the provision of technical assistance and capacity development activities for Tonga from the IMF headquarters, Pacific Financial Technical Assistance Center (PFTAC), and IMF-Singapore Regional Training Institute as well as virtual missions since the onset of the pandemic.

IDA Voting Rights and 2020 Shareholding Review

We welcome the request to endorse reviewing of the IDA Voting Rights. We also support the review and the rationale behind the proposal as it is both timely and appropriate given IDA's transition to a hybrid financing model and the issues members have highlighted with the current framework being too complicated and the framework should do more to enhance and balance incentives for increasing contributions by existing and new donors, amongst others.

We appreciate the 2020 Shareholding Review undertaken and welcome the conclusion and recommendations therein. We also support, together with other member countries, the shareholding architecture that has been developed in recent years ("The Lima Principles"). Our support also extends to the need to provide further technical work for options for a gradual adjustment of IBRD and IFC shareholding but still maintain the legitimacy of the shareholding structure. For IBRD, this includes a careful and thorough consideration of under-representation of members and extreme misalignment, timing of a potential realignment given the recent capital increase, and the ongoing subscription process. While on IFC's case, the adoption of an agreed baseline for future shareholding reviews would strengthen the WBG's shareholding architecture by putting the shareholding frameworks for IFC and IBRD on an equal footing, in the spirit of one WBG.

Conclusion

Last but not the least, we would like to acknowledge the continuous strong partnership and the assistance from the WBG and IMF towards Tonga's ongoing reforms and development.

The Government of Tonga is highly committed to additional policy reforms under the Joint Policy Reform Matrix as conditions for the significant budget support grant from the Bank which we anticipate to receive by the end of the year.

Thank you very much