

**30 June 2012**



**Government of Tonga**  
***Annual Public Debt Bulletin***

*Prepared by*

Debt Management Section

Ministry of Finance & National Planning

*Authorised for release by*

Minister for Finance & National Planning

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## Table of Contents

1. Introduction.....	1.
2. The Framework for Debt Management Operations.....	2.
2.1 Legislative Arrangements.....	2.
2.2 Role of Central Bank.....	3.
2.3 Reform.....	3.
3. Developments in the Past Year.....	4.
3.1 Macroeconomic Developments.....	4.
3.2 The Borrowing Programme.....	6.
3.2.1 Fiscal Outcome.....	6.
3.2.2 Government Borrowing.....	6.
3.2.3 Domestic Debt Issuance.....	7.
3.2.4 External Debt Borrowing.....	8.
3.2.5 Disbursement of External loans.....	8.
3.2.6 Developments in the Secondary Market.....	9.
4. Public Debt Portfolio.....	9.
4.1 Portfolio Risks.....	12.
4.2 Domestic Central Government Debt.....	14.
4.2.1 Domestic Debt by Instrument.....	15.
4.2.2 Domestic Debt by Holder.....	15.
4.2.3 Domestic Debt by Tenor.....	16.
4.3 External Central Government Debt.....	16.
4.3.1 External Debt by Creditor Category.....	17.
4.3.2 External Debt by Currency.....	18.
4.4 Total Public Debt Service.....	19.
4.4.1 External Debt Service by Creditor Category.....	19.
4.4.2 Principal and interest Payments.....	20.



4.4.3 Debt Service Schedule.....	21.
5. Contingent Liabilities.....	21.
5.1 Loans On-lent.....	21.
5.2 Loan Guarantees.....	23.
6. Debt Sustainability.....	24.
7. Conclusion and Way Forward.....	27.
8. Statistical Annex.....	29.



## Acronyms and Abbreviations

ADB	Asian Development Bank
APDB	Annual Public Debt Bulletin
ATF	Average Time to Refixing
ATM	Average Time to Maturity
AUD	Australian Dollar
BOC	Bank of China
CBD	Central Business District
CNY	Chinese Yuan Renminbi
ComSec	Commonwealth Secretariat
CS-DRMS	ComSec Debt Recording and Management Section
DMS	Debt Management Section
EGS	Exports of Goods and Services
EIB	European Investment Bank
EUR	Euro
EXIM	Export–Import Bank of China
FI	Financial Institution
GDP	Gross Domestic Product
GoT	Government of Tonga
IDA	International Development Association
IDH	International Dateline Hotel
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
MDGs	Millennium Development Goals
MoFNP	Ministry of Finance and National Planning
MTDS	Medium Term Debt Strategy
NRBT	National Reserve Bank of Tonga
NPV	Net Present Value
NZD	New Zealand Dollar
PFMA	Public Finance Management Act
PRC	People Republic of China
SDPTSD	Sustainable Debt Policy for Tongan Sovereign Debt
SDR	Special Drawing Rights
TCC	Tonga Communication Corporation
TDB	Tonga Development Bank
TNRIP	Tonga National Road Improvement Project
TOP	Tongan Pa'anga
TPL	Tonga Power Limited
TSDF	Tonga Strategic Development Framework
WB	World Bank
WBOT	Westpac Bank of Tonga
WPAC - AUS	Westpac Australia
WPAC – NZ	Westpac New Zealand



## Acknowledgements

This is the first *APDB* as based on an Outline recommended by ComSec in line with international reporting requirements of Public Debt Statistics Guide issued by IMF and affiliated associations.

The key role played by the DMS for co-ordinating production of this important report is acknowledged with the assistance by ComSec and the other contributors of data from the Economic and Budget divisions of MoFNP, related divisions of NRBT and the IMF.

Significant milestones have been achieved in the implementation of debt management reforms in the last five years and details are referred in Section 2.3. under Reforms.

It is expected that future series of this annual publication will be ready by end July each year.



## Foreword

The primary objective of GoT's debt management policy is to maintain sovereign debt within levels that are sustainable over time, with regular monitoring against the modified debt sustainability indicators of those provided by the IMF as referred in the SDPTSD approved by Cabinet in May 2009.

This comprehensive format of the *APDB* is the first issue and this report covers the state of public debt management over the last five years with reference to current reforms in this area and also includes projections of both debt stock and debt service over the next ten year period.

The MoFNP will submit this annual report to Cabinet and to other institutions as required and for public information as part of its effort to disseminate information on the public debt position.



Public debt continues to be a major challenge towards achievement of national priorities under the *TSDF* and *MDGs*. GoT's budget is severely limited and without continued budget support and project funding from donors, the fiscal space will deteriorate. As each fiscal year comes, a significant proportion of the GoT budget allocation is to service public debt, leaving inadequate financial resources for Education, Health and pro-poor development programmes.

The need to strengthen public debt management is critical not only to lowering the cost of external debt service especially to the PRC going forward, but also for the development of Tonga's capital markets. Since June 2009, the GoT has been thrust into the high risk of debt distress classification by the IMF and other international financial institutions, as result of the drawdown of the two major infrastructure projects for CBD and Roads from EXIM. As at 30 June 2012, the composition of public debt is *external debt* at 92% and *domestic debt* at 8%, and the *loans from PRC* account for 64% of external debt.

In response to these shortcomings, the MoFNP on behalf of GoT continues to explore strategies that will minimise risks particularly in the external portfolio and with development of a formal MTDS to guide the implementation of public debt management and the priority requirements. Currently, a no new borrowing policy is in place since June 2011 until such time that external debt levels are reduced and to remain within the recommended sustainability levels. Other required action includes follow up of requests to the PRC for consideration on conversion of some external loan portions to developments grants; to look into hedging options and discussion with the major creditors on review of repayment terms in efforts to reduce the substantial external debt servicing costs.



In conclusion, I wish to take this opportunity to express my appreciation to all the stakeholders participating in the on-going public debt management reforms. It is a very challenging time for GoT with its high risk of external debt distress and exacerbated with the low economic growth. However, with the favourable support from the PRC and other international donors as anticipated, it will create some fiscal space to stimulate further development of the Tongan economy over the medium term.



The stamp contains the text "MINISTER FOR FINANCE" at the top, "TONGA" at the bottom, and a central emblem featuring a crown and a cross.

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Hon. Lisiata 'Aloveita 'Akolo

**Minister for Finance & National Planning**





## Executive Summary

- **The total disbursed outstanding debt (DOD)** of loans by Government as at 30th June 2012 in nominal value at millions of Pa'anga's over the 5 year period, is shown below:

Loans	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
External	157.9	202.4	228.8	274.9	322.6	47.7	164.7
Domestic	22.5	22.5	29.5	29.5	29.5	-	7.0
<b>Total Public Debt</b>	<b>180.4</b>	<b>224.9</b>	<b>258.3</b>	<b>304.4</b>	<b>352.1</b>	<b>47.7</b>	<b>171.7</b>
Guarantees	10.5	9.5	14.0	12.1	7.8	-4.3	-2.7
On-lent	26.4	22.3	23.0	40.8	63.9	23.1	37.5
<b>Total Contingent Debt</b>	<b>217.3</b>	<b>256.7</b>	<b>295.3</b>	<b>357.3</b>	<b>423.8</b>	<b>66.5</b>	<b>206.5</b>

- **Total public debt** was estimated at \$352.1m (45% of GDP), with External debt at \$322.6m (41%) and Domestic debt at \$29.5m (4%). During the 5 year period, there was a huge increase in external debt (\$165.0m) mainly due to loan disbursements from Export-Import Bank of China (EXIM) for CBD and Roads and appreciation of the CNY currency.
- **Main external debt creditors** are: EXIM at \$198.4m (62%), and ADB at \$66.0m (20%). During the 5 year period, there was an increase of \$188.8m in the DOD to EXIM including fluctuation in the CNY currency. The total disbursements for CBD is estimated at \$121.3m, and for Roads at \$72.1m.
- **Domestic debt** comprises of bond issues, with the majority of holdings by Financial Institutions (FI) at \$19.3m (66%) and Retirement Fund Board at \$5.0m (17%). During the 5 year period, there was an increase of \$7.0m mainly due to new bond issues.
- The **main external loan currency denomination** is the Chinese Yuan Renminbi (CNY) at \$205.3m (64%) and the Special Drawing Rights (SDR) at \$115.1m (36%). During the 5 year period, there was a significant increase in CNY composition of \$189m (54%), due to the major loan disbursements from EXIM.
- **Total External DOD in net present value (NPV)** by 30 June 2012 is estimated at \$333.1m (43% of GDP) at current FC/TOP rates. In reference to debt sustainability targets below, the external debt position will worsen going forward.



Debt Sustainability Indicators	IMF Target %	GOT Target %	FY 2012 %	FY 2013 %	FY 2014 %
<b>NPV of debt as:</b>					
% of GDP	30	40	43	42	41
% of exports & remittances	90	100	155	124	122
% of budget revenue	200	200	227	208	201
<b>Total Debt Service as:</b>					
% of exports & remittances	14	15	7	8	11
% of budget revenue	25	25	10	13	17

- **External DOD will continue to be in excess of targets** from FY 2011/12 and the main Creditor and Currency composition will remain as EXIM and CNY currency. This results in high risk and exposure to volatility of exchange rates especially with strengthening of the CNY.
- **External debt service** is estimated to significantly increase to \$10m (*at around 1% of GDP and 6% of expenditure*) from FY 2013/14, with commencement of principal loan repayments to EXIM for CBD and Roads, until loan maturity in FY 2029/30.
- **To maintain debt sustainability in future**, it is vital that our current level of economic activity prospects improve together with prudent public debt management through priority implementation of MTDS, in order to mitigate the vulnerability to shocks.



## 1. Introduction

The *APDB as at 30th June 2012* presents the major public debt management activities between July 2011 and June 2012 including review of historical data over the last five (5) fiscal years and with projections over the next 10 fiscal years or so. It reports key data and ratios on the public debt portfolio (stocks and flows) and how these have changed over the course of the year. Looking forward, the Bulletin will discuss the GoT's MTDS and priority action for debt reduction programs, fiscal consolidation, estimations for GDP growth, projections of fiscal deficits and other macroeconomic developments.

**SECTION 2:** Addresses the framework for Public Debt Management Operations

**SECTION 3:** Covers the following recent developments: -

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

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

**SECTION 5:** Position of Contingent Liabilities

- loans on-lent
- loan guarantees

**SECTION 6:** Discusses issues relating to debt sustainability

**SECTION 7:** Conclusion and way forward for debt management



## 2. Framework for Debt Management Operations

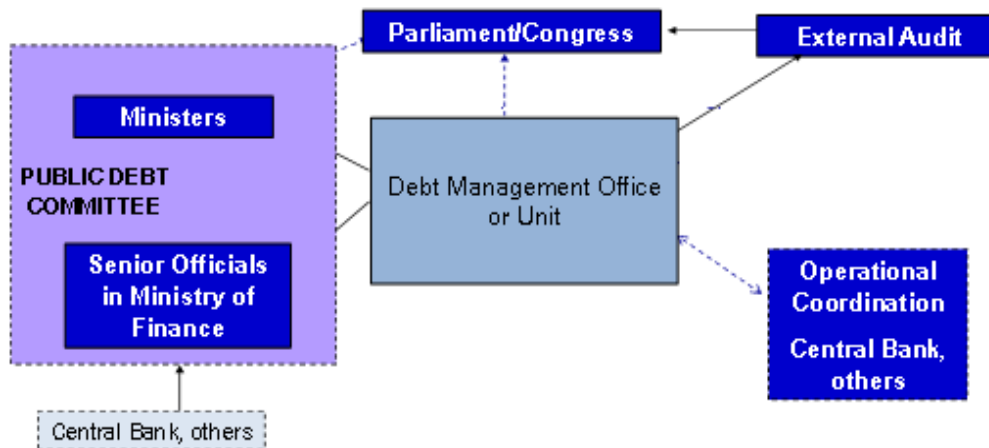
The PFMA 2002 specifies that the Minister of Finance is responsible for economic, fiscal and financial management by Government, Part V, provides the basic legal framework for Government's borrowings, loans and guarantees.

The DMS under the Treasury Division is primarily responsible for debt management duties on behalf of MoFNP and the mandated task of meeting the GoT's objective for public debt management which was approved by Cabinet in May 2009:

*The objective of public debt management is that "the GoT maintains sovereign debt within levels that are sustainable over time" for use on regular monitoring of debt levels against the modified GoT thresholds (on those recommended by the IMF).*

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

Figure 1: Typical Governance Structure



### 2.1 Legislative Arrangements

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



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

## 2.2 Role of the Central Bank

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

## 2.3 Reforms

Since the late 1990s, the CS-DRMS has been the primary source of register for GoT's loan portfolio. Over the years, various upgrades have been made to the system from a unix-dos base to a windows base.

The DMS was set up in 2005 to separately conduct debt management tasks with development since of full time staff to improve in MoFNP's management of GoT's growing loan portfolio and commendable progress has been achieved in consolidating debt management operations under DMS. There are 3 main databases used by DMS to record external debt, domestic debt and on-lent debt and record is also made of the guaranteed debt data, as possible. As result, this has improved the quality of debt data, a pre-requisite for effective debt management. In addition, supported by a reliable debt database and improved coordination of debt management functions, debt service payments are settled promptly and on-going efforts to monitor performance of contingent liabilities (on-lent loans and guarantees). There is satisfactory monitoring and regular internal and external reporting on the position of GoT's debt management activities in the medium term.

In 2006, a fibre optic link of CS-DRMS was made between MoFNP and NRBT for browser access but due to limited staff capacity it has not had pro-active use.

On-going capacity building of staff is mainly taken out through donor funded trainings and in-country missions on various aspects of debt management (CS-DRMS and policy issues).

**During the 1 year period (FY 2011/12),** some of the main debt management activities were carried out:



- (i) Monthly reporting to Cabinet on the status of GoT's loan portfolio, with progress of the CBD and Roads loans and Quarterly Debt Sustainability Analyses.
- (ii) A Public Debt Management Committee was re-established in September 2011, comprising senior officials from MoFNP and NRBT, with the objective to advise MoF on GoT's policy and strategy on the public debt portfolio, borrowing and performance including contingent liabilities. Meetings are conducted on a quarterly to bi-annual basis;
- (iii) A Scoping Mission by ComSec on Debt & Cash Management from 31 October 2011 to 4 November 2011, with recommendations and order of priority for work to be done and assistance by ComSec, as possible.
- (iv) Issue of a Quarterly Debt Bulletin from December 2011 via MoFNP website for public access on status of GoT's loan portfolio.

## 3. Developments in the Past Year

### 3.1 Macroeconomic Developments

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

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
Gross Domestic Product	659.3	664.3	711.4	783.4	781.5	-1.9	122.2
Fiscal Balance	-3.3	-19.4	33.6	24.5	23.7	-0.8	47.4
Current Account Balance	-58.6	-97.8	-52.6	-69.8	-86.2	-16.4	-27.6
Inflation (%)	9.6	5.6	1.7	6.0	3.4	-2.6	-6.2
Exports of Goods & Services	93.6	95.1	83.2	100.2	103.1	2.9	9.5
Debt Service	14.8	16.9	17.0	22.8	15.2	-7.6	0.4
Expenditure	148.9	207.8	175.8	177.5	165.2	-12.3	16.3
Revenue	161.8	186.8	159.6	151.0	146.6	-4.4	-15.2
Remittances	202.8	175.2	157.4	146.5	112.3	-34.2	-90.5
Foreign Reserves	89.1	136.3	170.5	203.8	246.1	42.3	157.0

In reference to the GoT's Budget Statement of 2012-12 and its theme of "Creating Opportunity In Extraordinary Times". This continues policy from the last fiscal year of prudent fiscal management, to ensure that we move to a sustainable financial and debt position over time despite the challenging conditions both domestically and globally.

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



Early in the decade, growth reflected similar performance to that of the 1990s, but fell sharply as a result of the domestic disruptions, to negative rates worse than anything seen during the 1990s. By 2007/2008 growth recovered with the start of some rebuilding and gradual return in business confidence.

The GoT signed the CBD loan with PRC in November 2007 to help rebuild the CBD after the civil unrest. This massive increase in expenditure was well timed to mitigate the impact of the global economic crisis and associated falls in remittances, which would have suppressed GDP and likely have resulted in negative growth in 2009/2010.

The benefit however came at a cost with GoT debt rising above sustainable rates and removing the capacity for any further borrowing for some years, and will increase debt service significantly. The growth was strongly focused in Nuku'alofa with much of the value added produced by foreign workers and company who were based in Tonga long enough to be included in GDP estimates. This unbalanced growth in GDP (which is not a measure of welfare) has been associated with increased hardship in some parts of the country and difficulties experienced by local business. Household Consumption per capita, a better measure of welfare, has fallen despite the rise in GDP per capita driven by the large loan funded expenditure.

The rate of GDP growth for 2011/2012, as has been anticipated is expected to drop with the end of the loan funded construction and quarrying boom. While a number of new grant funded projects have been negotiated with our development partners, they will not be of the same magnitude as the loan funding from PRC. Several of the other drivers of growth in 2010/2011 will also fall away as GoT has had to ban further export of sandalwood and sea cucumber to protect the rapidly dwindling stock.

Domestic lending remains weak as banks recover from the excess underperforming loans.

GoT is working with NRBT and others to find ways to create an environment where banks will be willing to make more use of the available liquidity and start to expand lending in a responsible manner. The TDB has recently eased its lending conditions.

Looking forward, GoT is focusing on working more closely with the private sector.



## 3.2 The Borrowing Programme

Given the GoT's current position of high risk for debt distress, Cabinet approved in June 2011 to implement a "No New Loan Policy", as part of the priority actions under the MTDS.

The annual borrowing by GoT during FY 2011/12 is approved by Legislative Assembly in July 2011 as part of the Budget estimates. This includes projections of external loan disbursements from PRC (EXIM) as required this year for the CBD and Roads projects at \$47.5m (the initial approval for these 2 loans were made in prior fiscal years), and roll-over for financing of maturing bonds (\$3.0m).

Financing of \$3.0m for roll-over of maturing bonds remained within the statutory limit of \$15.0 million as stated in PFMA Section 25(1). Section 31(1)(b) also refers that the total level of guarantees outstanding at \$7.8m, does not exceed 5 percent of GoT fund appropriated.

There were no other borrowings taken.

### 3.2.1 Fiscal Outcome

Central GoT public deficit position has continued over this period since the surplus position in 2008, and as a ratio of GDP at 2 percent for the period 2012.

**Table 2: Fiscal Outcome in TOP\$m**

Item	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
1. Total Receipts	161.8	186.8	159.6	151.0	146.6	-4.4	-15.2
2. Total Expenditure	148.9	207.8	175.8	177.5	165.2	-12.3	16.3
3. Gross Fiscal Deficit/Surplus	12.9	-21.0	-16.2	-26.5	-18.5	-8.0	31.4
<b>As a % of GDP</b>	<b>-2.0</b>	<b>3.2</b>	<b>2.3</b>	<b>3.4</b>	<b>2.4</b>	<b>-1.0</b>	<b>4.4</b>
4. Financing of Fiscal Deficit							
(a) Local Currency Financing							
(i) Bonds	6.3	7.0	6.6	10.4	3.0	-7.4	-3.3
(b) Foreign Currency Financing							
(i) Loans	7.3	43.0	41.4	67.6	47.5	-20.1	40.2

### 3.2.2 Government Borrowing

In this section, the Bulletin will discuss the GoT's borrowing target and borrowing strategy for the year under review (FY 2011/12). External debt accounts for 92% and domestic debt accounts for 8%. Loans sourced externally are mainly on a concessional basis at an average of





35 years and 1.62% interest per annum, mainly from the ADB and IDA. Domestic debt comprises of public bonds issued on a more commercial basis at an average of 5 years and 5.74% interest per annum.

**Table 3: Government Borrowing in TOP\$m**

	FY 2012 Original	FY 2012 Actual	change
<b>Total Net Borrowing</b>			
Domestic	3.0	3.0	-
External	32.0	47.5	15.5
<b>Total</b>	<b>35.0</b>	<b>50.5</b>	<b>15.5</b>
<b>Gross Borrowing by Instrument</b>			
Bonds	29.5	29.5	-
Loans	323.6	322.6	-1.0
<b>Total</b>	<b>353.1</b>	<b>352.1</b>	<b>-1.0</b>

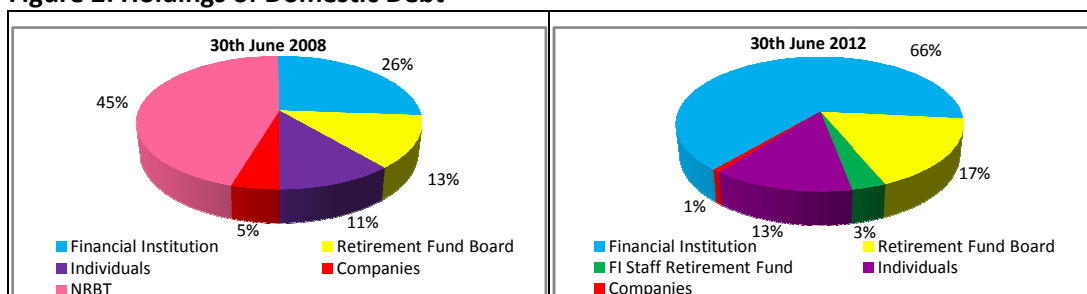
On net basis, total borrowings was estimated at \$35.0m in 2012. Of this total, \$32.0 million and \$3.0 million to be raised from external and domestic sources, respectively. However, total net borrowings exceeded the original target by \$15.5m due to the fluctuation of FC/TOP rates as used in the original external estimates and the actual position as at 30 June 2012.

### 3.2.3 Domestic Debt Issuance

Over the last 5 fiscal year period, domestic debt has increased by 37.5% to current level of \$29.5 million. As result of the global financial crisis, a couple of bond issues were required during FY 2009/10 for budget support of \$8.0 million. During FY 2010/11, a 3-6 month Treasury Bill of \$7.0 million was also issued to support GoT's operations and it was settled by June 2011 once the budget support funds was received from donors.

GoT's bonds are mainly issued on a roll-over basis with exception of any redemptions or new issues. Financial Institutions (commercial banks) now account for the majority of holdings at \$19.4m with Retirement Fund Board at \$5.01m and Individuals at \$3.8m. Since amendment of NRBT Act in 2007, they no longer have any holdings of GoT's securities.

**Figure 2: Holdings of Domestic Debt**





### 3.2.4 External Debt Borrowing

The grant element specifies the level of concessionality of external loans taken from bilateral or multilateral creditors. In countries such as Tonga with higher debt vulnerabilities, the concessionality threshold or minimum grant element as recommended by the IMF and WB should at least be 35%.

At a grant element of 35%, this implies that loans will have a longer grace and maturity period with lower interest rates. Concessionality of GoT's external loans over the last 5 year period, is shown below:

**Table 4: Average Terms of New Loans**

	FY 2008	FY 2012
Maturity (Years)	20.0	20.0
Grace Period (Years)	5.0	5.0
Interest Rate (%)	2.0	2.0
Grant Element (%)	58.3	55.6

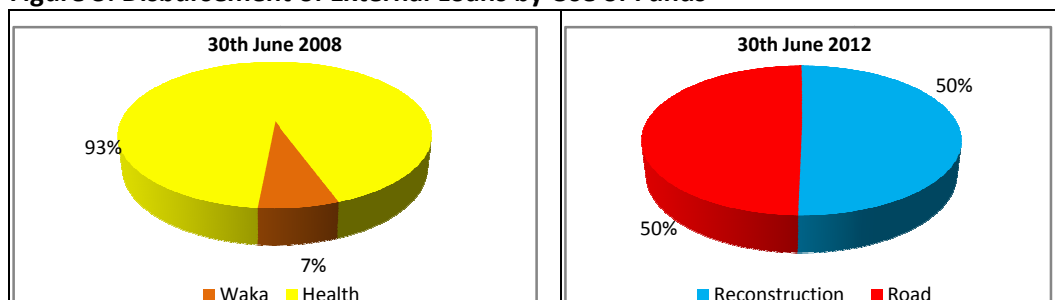
### 3.2.5 Disbursement of External Loans

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

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

DETAILS	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
Disbursed Outstanding Debt	157.9	202.4	228.8	274.9	322.6	47.7	164.7
Disbursements	7.1	42.9	41.4	67.6	47.5	-20.1	40.4
Principal Repayments	4.6	4.7	4.6	6.0	5.7	-0.3	1.1
Net Flows On Debt	2.5	38.2	36.8	61.6	41.8	-19.8	39.3
Interest Payments	2.1	3.6	3.8	4.3	4.8	0.5	2.7
Net Transfers On Debt	0.4	34.6	33.0	57.3	37.0	-20.3	36.6
<b>Total Debt Service</b>	<b>6.7</b>	<b>8.3</b>	<b>8.4</b>	<b>10.3</b>	<b>10.5</b>	<b>0.2</b>	<b>-6.5</b>

**Figure 3: Disbursement of External Loans by Use of Funds**





### 3.2.6 Developments in the Secondary Market

Since FY 2008/09 there has been excess liquidity in the banking system and market interest rates have been declining. Prior to amendment of the NRBT Act in 2007 to repeal Section 49 in the Principal Act that NRBT may hold GoT bonds, NRBT held the majority of holdings in GoT's bonds and the Financial Institutions now account for the main bond holders.

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

There is a need to develop the domestic market and particularly the issue of GoT's securities according to best market practices. A mission from ComSec on Domestic Market Development was conducted during 16 to 27 July 2012 and recommendations made by experts on the way forward will be submitted to MoFNP by September 2012.

## 4. Public Debt Portfolio

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

Gross public sector debt increased by 15.7% between 2011 and 2012, continuing the upward trend since 2008, as result of the external debt position.

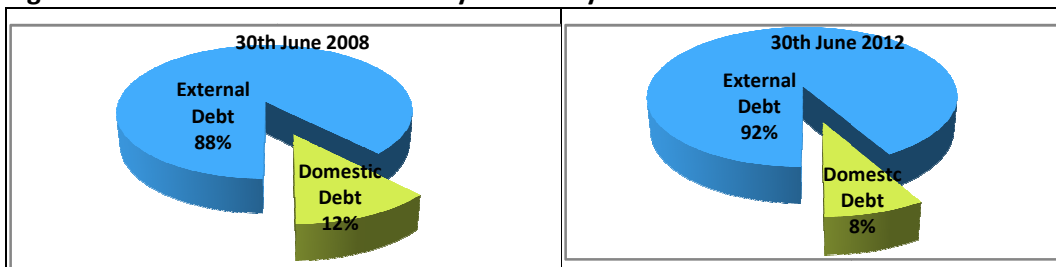
**Table 6: Main Debt Indicators in TOP\$m**

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
<b>Gross central government debt</b>	<b>180.4</b>	<b>224.9</b>	<b>258.3</b>	<b>304.4</b>	<b>352.1</b>	<b>47.7</b>	<b>171.7</b>
<i>Debt-to-GDP (%)</i>	27.4	33.9	36.3	38.9	45.1	6.2	17.7
<b>External Debt</b>	<b>157.9</b>	<b>202.4</b>	<b>228.8</b>	<b>274.9</b>	<b>322.6</b>	<b>47.7</b>	<b>164.7</b>
<i>External debt-to-GDP (%)</i>	23.9	30.5	32.2	35.1	41.3	6.2	17.4
<i>External debt-to-EGS(%)</i>	194.0	237.0	260.9	302.4	375.1	72.7	181.1
<i>External debt-to-Reserves (%)</i>	177.2	148.5	134.2	134.9	131.1	-3.8	-46.1
<b>Domestic Debt</b>	<b>22.5</b>	<b>22.5</b>	<b>29.5</b>	<b>29.5</b>	<b>29.5</b>	-	<b>7.0</b>
<i>Domestic debt to GDP(%)</i>	3.4	3.4	4.1	3.8	3.8	-	0.4



As at 30<sup>th</sup> June 2012, the external debt stock increased to \$322.6m, which is equivalent to 41% of GDP at 92% of total debt. By contrast, domestic debt remained constant at T\$29.5m and only makes up 4% of GDP at 8% of total debt (Figure 4).

**Figure 4: Central Government Debt by Residency of Creditor**



External debt continues to account for the majority of total public sector debt. Access to financing from external sources is readily available especially from PRC, and the increase of 4% during the 5 year period (June 2008 to June 2012) is due to further drawdown of the two major infrastructure loans from EXIM China for the CBD and Roads projects.

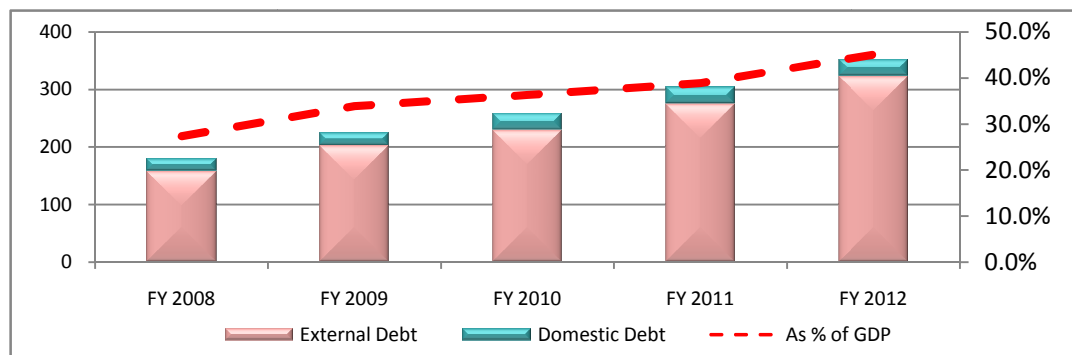
The breakdown of GoT debt by instrument type is referred below.

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

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
Gross central government debt	180.4	224.9	258.3	304.4	352.1	47.7	171.7
Debt-to-GDP (%)	27.4	33.9	36.3	38.9	45.1	6.2	17.7
Gross debt by instrument type							
Loans	157.9	202.4	228.8	274.9	322.6	47.7	164.7
Securities	22.5	22.5	29.5	29.5	29.5	-	7.0
Arrears	-	-	-	-	-	-	-

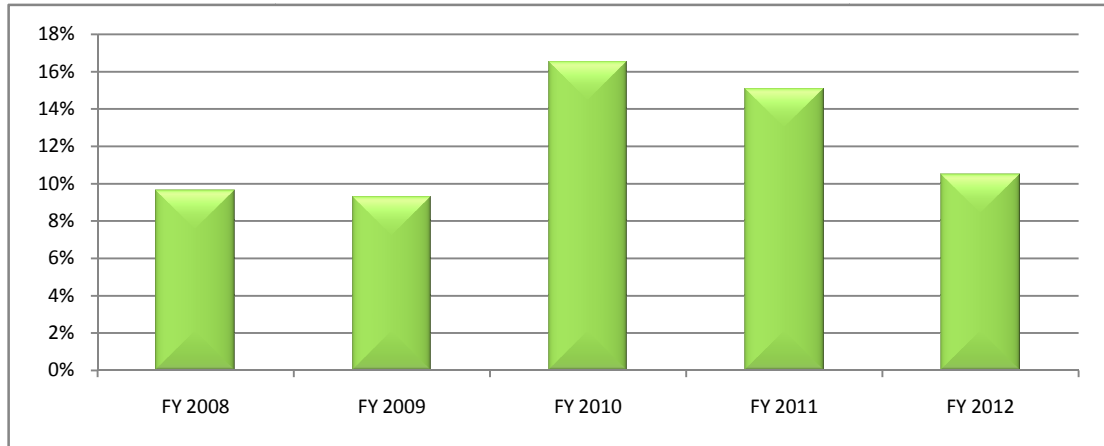
**Other essential items on status of the public debt portfolio are:**

**Figure 5: Nominal Central Government Debt and to GDP**

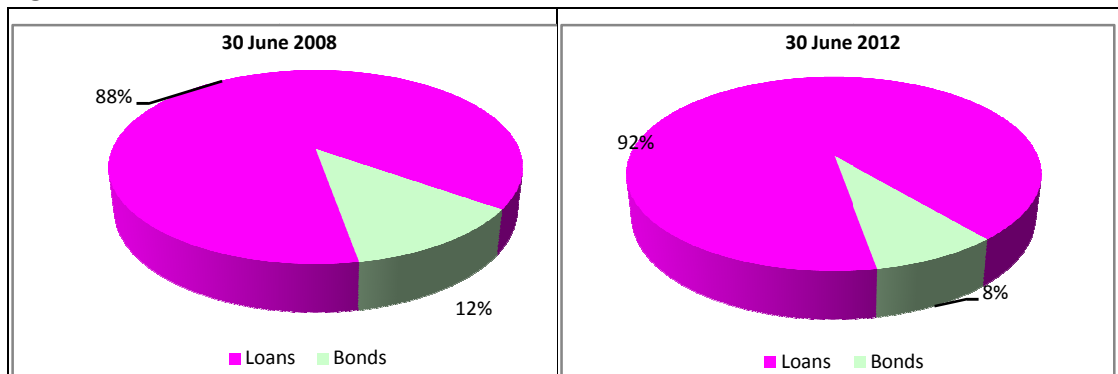




**Figure 6: Total debt service payments as % to revenue**



**Figure 7: Instrument**

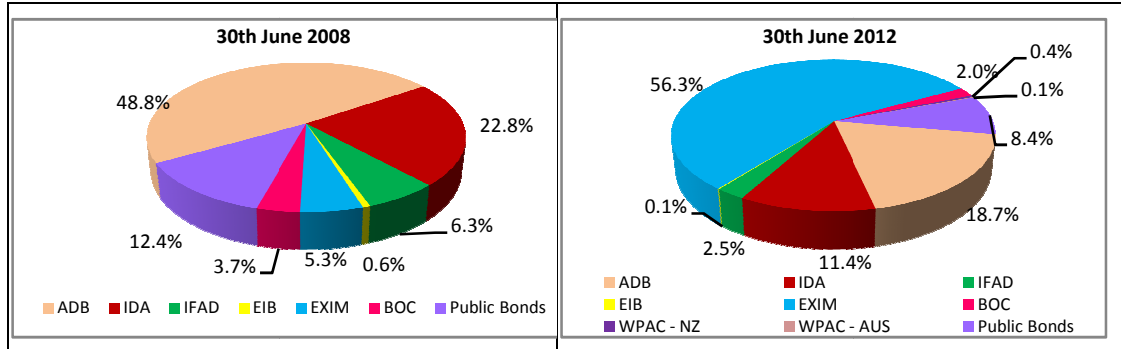


**Table 8: Creditor**

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1yr change	5yr change
<b>Central Government Debt</b>							
Bilateral	16.4	57.9	92.5	150.9	205.3	54.4	188.9
Commercial Bank	-	-	1.6	2.0	1.8	-0.2	1.8
Multilateral	141.5	144.5	134.7	122.0	115.5	-6.5	-26.0
Other	22.5	22.5	29.5	29.5	29.5	-	7.0
<b>Total Government Debts</b>	<b>180.4</b>	<b>224.9</b>	<b>258.3</b>	<b>304.4</b>	<b>352.1</b>	<b>47.7</b>	<b>171.7</b>
<b>External Debts</b>							
Bilateral	16.4	57.9	92.5	150.9	205.3	54.4	188.9
Commercial Bank	-	-	1.6	2.0	1.8	-0.2	1.8
Multilateral	141.5	144.5	134.7	122.0	115.5	-6.5	-26.0
<b>Total External</b>	<b>157.9</b>	<b>202.4</b>	<b>228.8</b>	<b>274.9</b>	<b>322.6</b>	<b>47.7</b>	<b>164.7</b>
<b>Domestic Debts</b>							
Public Bonds	22.5	22.5	29.5	29.5	29.5	-	7.0
<b>Total Domestic</b>	<b>22.5</b>	<b>22.5</b>	<b>29.5</b>	<b>29.5</b>	<b>29.5</b>	<b>-</b>	<b>7.0</b>



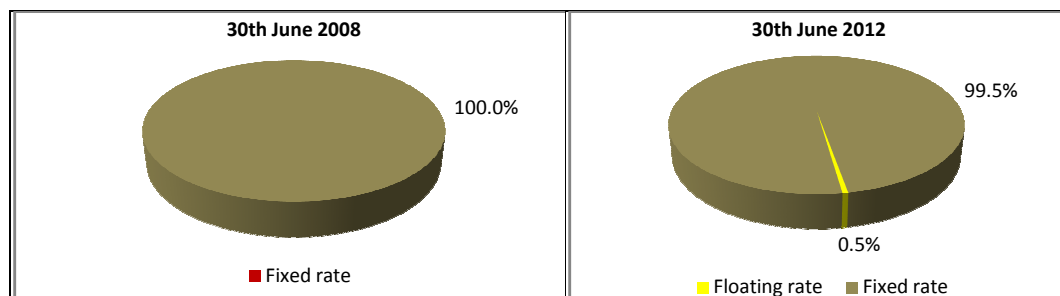
**Figure 8: Creditor**



### 4.1 Portfolio Risks

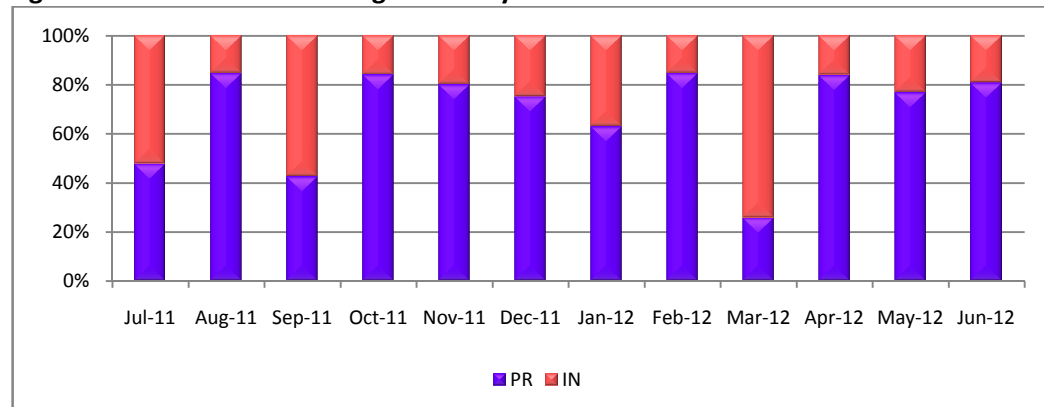
The basic risk measures include:

**Figure 9: Share of fixed rate to floating rate debt**



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

**Figure 10: Share debt maturing within 1 year**

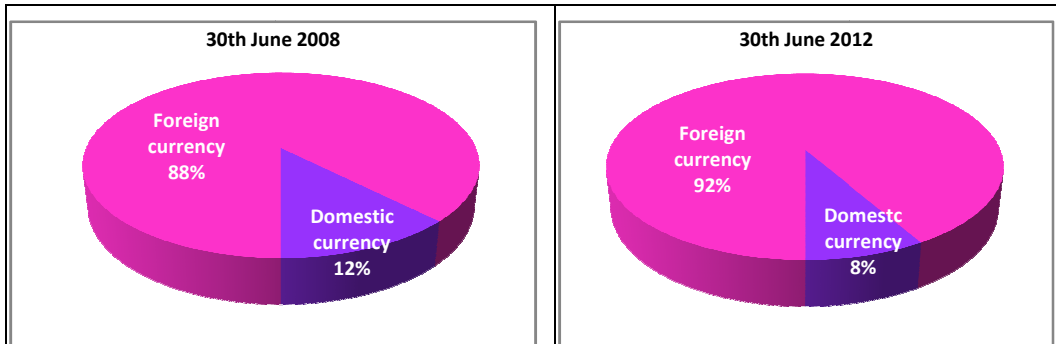




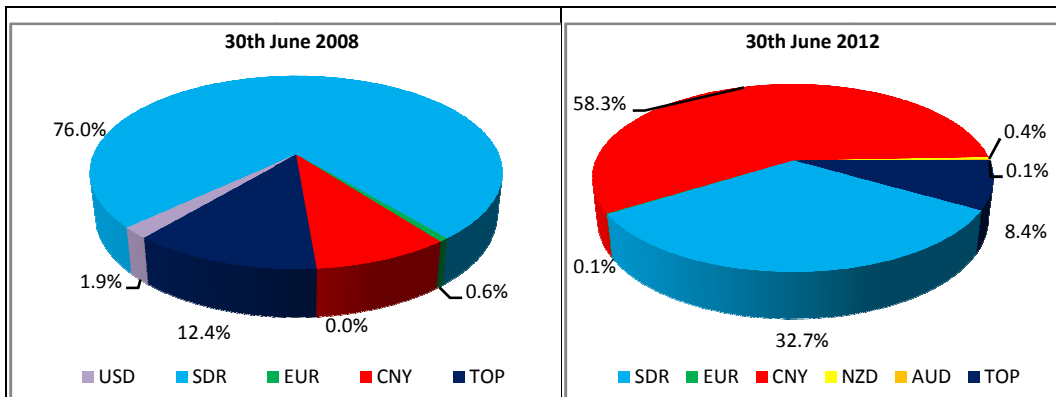
**Table 9: Average time to interest rate re-fixing (external debt)**

Years	Fixed	Variable	ATF
1 - 2	0.22	1.80	0.01
3 - 5	5.05	-	0.1
5 - 10	2.92	-	0.1
10 - 15	21.04	-	0.8
+15	291.61	-	13.6
<b>TOTAL</b>	<b>320.84</b>	<b>1.80</b>	<b>14.5</b>

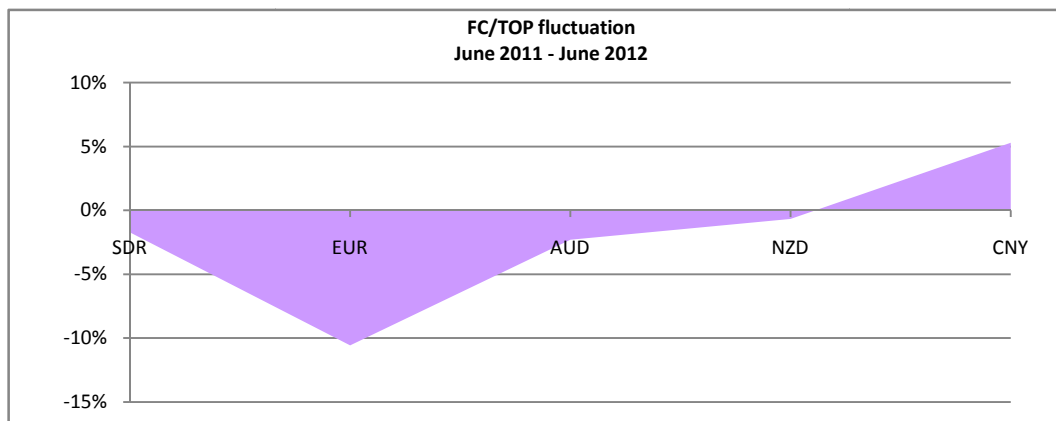
**Figure 11: Share of foreign currency to domestic currency debt**

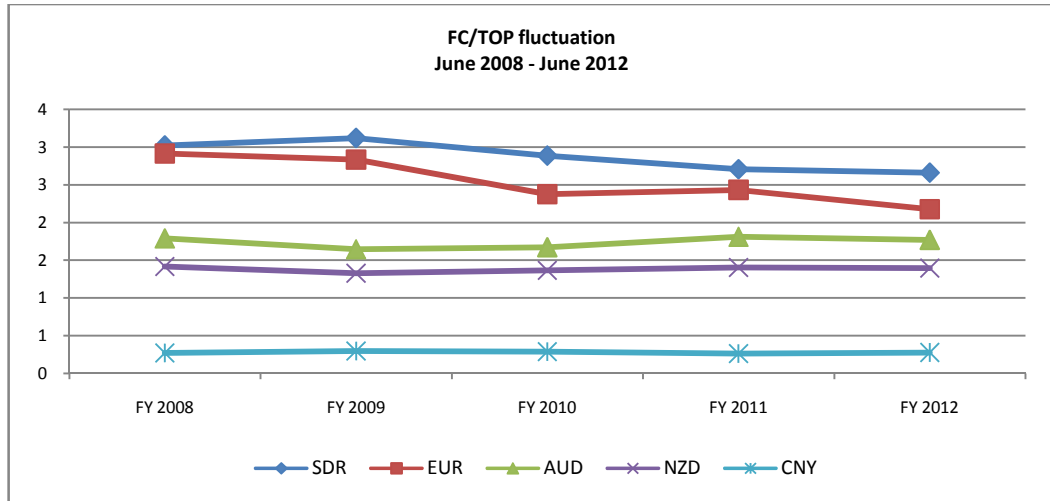


**Figure 12: Currency composition**



**Figure 13: Volatility of Foreign Exchange Rates to Tongan Pa'anga**



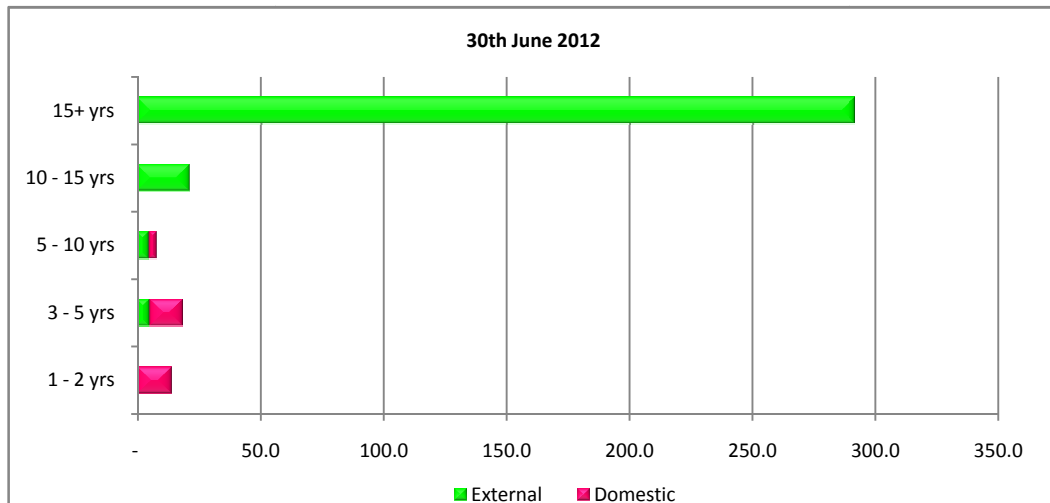


**Table 10: Average maturity of the debt (external debt)**

Years	Redemption	ATM
1 - 2	0.2	0.0
3 - 5	5.1	0.1
5 - 10	4.7	0.1
10 - 15	21.0	0.8
+15	291.6	13.6
<b>TOTAL</b>	<b>322.6</b>	<b>14.6</b>

At the end of 2012 the proportion of external debt with maturity of 10 to 15 years was 6.5% of external debt while 90.4% of external debt had more than 15 years maturity with repayments in the distant future. Domestic debt of 45.8% will mature in 1 - 2 years.

**Figure 14: Residual Maturity**







## 4.2 Domestic Central Government Debt

As shown in Table 11, GoT's domestic debt stock grew by \$7.0m over the review period from \$22.5m to \$29.5.

**Table 11: Domestic Debt by Instrument and Holder in TOP\$m**

Instrument	FY 2008		FY 2012		5 yr change
	\$m	%	\$m	%	
<b>Total Stock of Deposit Debt (A+B)</b>	<b>22.5</b>	<b>100.0</b>	<b>29.5</b>	<b>100.0</b>	<b>7.0</b>
<b>A. Government Securities</b>	21.5	95.6	29.5	100.0	8.0
Bonds	21.5	95.6	29.5	100.0	7.0
Financial Institutions	5.7	25.3	19.3	65.4	13.7
Retirement Fund Board	2.7	12.0	6.0	20.3	3.3
Other	13.1	58.2	4.2	14.2	-9.9
<b>B. Other Government Debt</b>					
Other	1.0	4.4	-	-	-1.0

### 4.2.1 Domestic Debt by Instrument

As at FY end 2012, Bonds account for 100% of the securities issued. Bonds are the main type of instrument issued on a 5 yearly duration and issue of 3-6 month Treasury Bills were settled during FY 2010/11.

### 4.2.2 Domestic Debt by Holder

GoT financed the deficit during this review period mainly by budget support funding from international donor agencies. Bonds that matured during the fiscal year were rolled over as financing for payments and hence a nil effect. Financial Institutions remain the largest holder of GoT debt, with holdings by non-bank sources decreasing by \$6.6m to \$10.2m, while those of commercial bank increased by \$13.6m to \$19.3m.

**Table 12: Domestic Debt by Funding Source in TOP\$m**

Holder	FY 2008		FY 2012		5 yr change
	Amount	%	Amount	%	
<b>Banks of which:</b>					
Commercial Bank	5.7	25.3	19.3	65.4	13.6
<b>Non Banks of which:</b>					
Other Non Bank Sources	16.8	74.7	10.2	34.6	-6.6
<b>Total</b>	<b>22.5</b>	<b>100.0</b>	<b>29.5</b>	<b>100.0</b>	<b>7.0</b>

The increase of outstanding bonds during the 5 year period, resulted in more holdings by Financial Institutions, Retirement Fund Board and



Individuals, and less holdings by the Companies and Others. Financial Institutions continued to hold the majority (65%) of bonds, followed by Retirement Fund Board (17%) and Individual (13%).

**Table 13: Bonds by Holder in TOP\$m**

Holder	FY 2008		FY 2012		5 yr change
	\$m	%	\$m	%	
Financial Institutions	5.7	26.5	19.3	65.4	13.6
FI Staff Retirement Fund	-	-	1.0	3.4	1.0
Retirement Fund Board	2.7	12.6	5.1	17.3	2.4
Companies	1.0	4.7	0.2	0.7	-0.8
Individuals	2.4	11.2	3.9	13.2	1.5
Other	9.7	45.0	-	-	-10.7
<b>Total</b>	<b>21.5</b>	<b>100.0</b>	<b>29.5</b>	<b>100.0</b>	<b>7.0</b>

### 4.2.3 Domestic Debt by Tenor

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

**Table 14: Bonds by Tenor in TOP\$m (remaining maturity)**

Security Type Bonds (Years)	FY 2008			FY 2012			5 yr Change
	Amount	Cum. Amount	Cum. %	Amount	Cum. Amount	Cum. %	
0 - 1 Years	3.1	3.1	14.4	3.0	3.0	10.2	-0.1
1 - 2 Years	13.6	16.7	77.7	13.5	16.5	55.9	2.9
3 – 4 Years	4.8	21.5	100.0	13.0	29.5	100	8.2
<b>Total</b>	<b>21.5</b>			<b>29.5</b>			<b>8.0</b>

## 4.3 External Central Government Debt

Table 15 shows that the stock of external debt increased from \$157.9m (24% of GDP) at June 2008 to \$322.6m (41% of GDP) at June 2012.

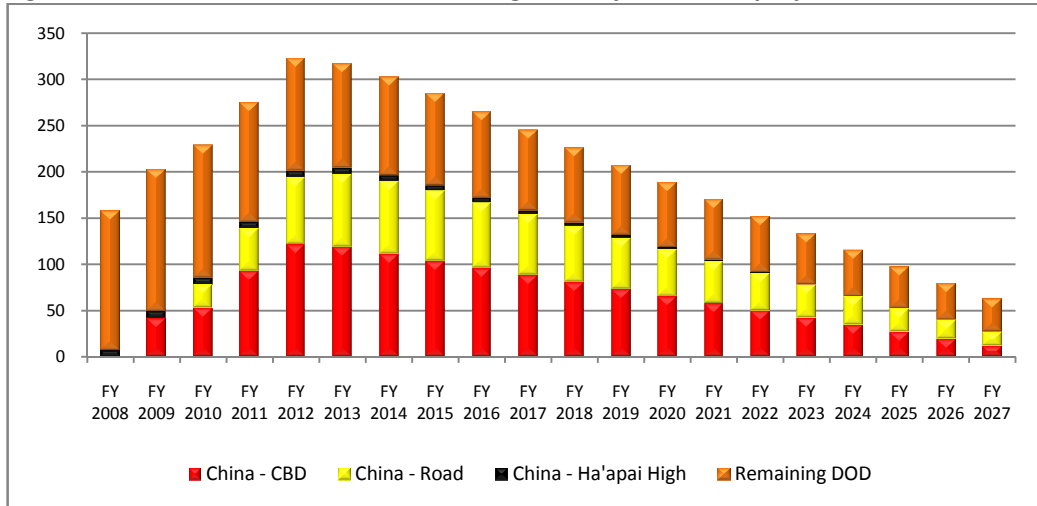
Worthy of note, is the fact that the debt service to exports ratio also significantly increased in 2008 to 2010 from 19% to 30% and gradually decreasing. This is mainly due to the higher rise of debt service for the loans to PRC compared to lower growth rate in exports in the prior years.

**Table 15: Key External Debt Indicators in TOP\$m**

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
External Debt	157.9	202.4	228.8	274.9	322.6	47.7	164.7
Ratio of total external debt to GDP (%)	23.9	30.5	32.2	35.1	41.3	6.2	17.4
Ratio of total debt service to exports (%)	19.2	20.4	30.1	25.1	17.9	-7.2	-1.3
Ratio of concessional debt to total debt (%)	43.2	45.6	42.5	42.8	43.8	1	0.6



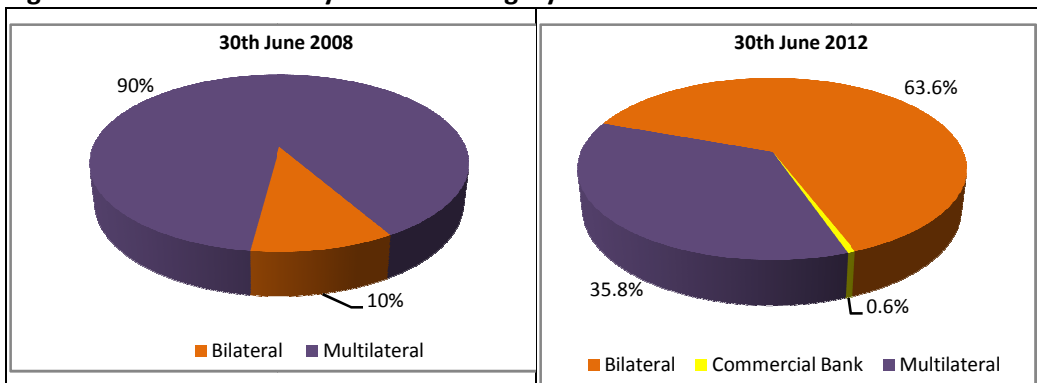
**Figure 15: External Disbursed Outstanding Debt by main PRC project**



### 4.3.1 External Debt by Creditor Category

At the end of June 2012, Tonga’s external debt stock was dominated by debt owed to the bilateral creditors, accounting for 64% of the total debt stock. However in comparison to the position at the end of 2008, multilateral debt accounted for 90% of the total external debt stock.

**Figure 16: External Debt by Creditor Category**



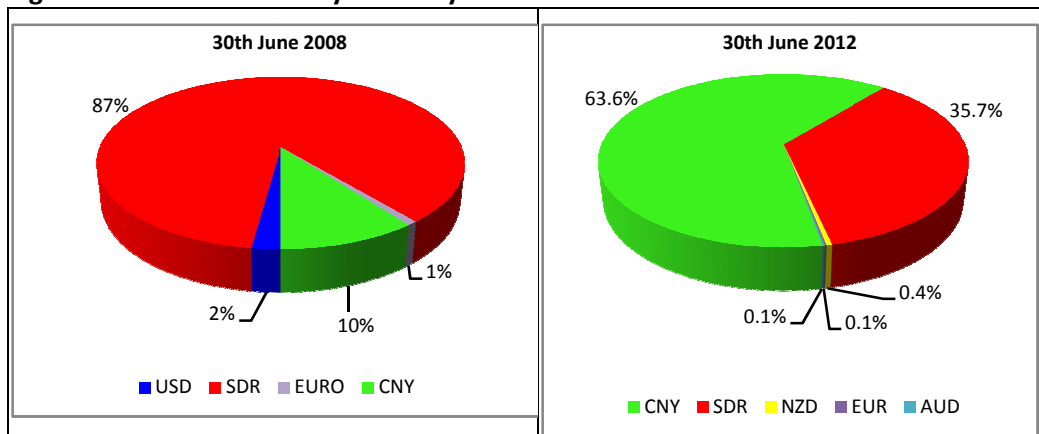
At end 2012, the major creditor was EXIM to whom Tonga’s outstanding liability was \$198.4m at 61.5% of external debt whilst ADB accounted for \$66.0m at 20.5% and IDA of \$40.3m at 12.5%.



### 4.3.2 External Debt by Currency

At the end of 2012, more than 63.6% of Tonga’s external debt was denominated in CNY, SDR at 35.7%, NZD at 0.4%, EUR and AUD at 0.1%, as shown below.

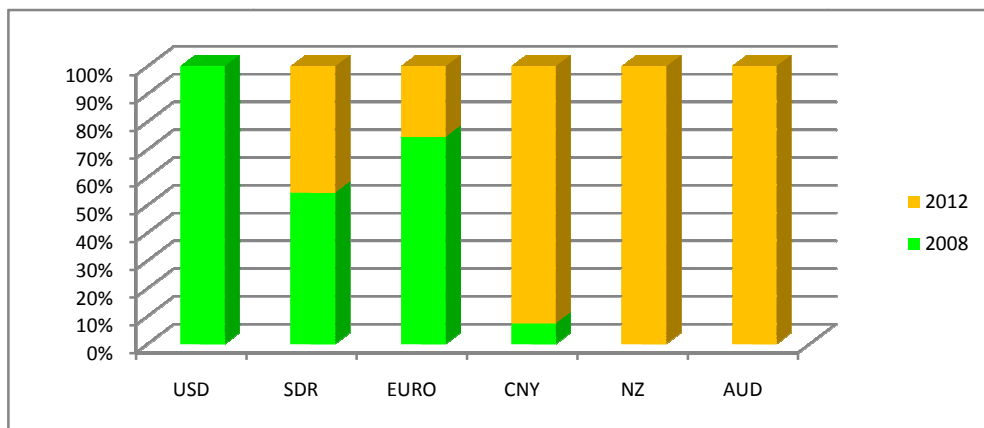
**Figure 17: External Debt by Currency**



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

In 2008, external debt was denominated in four currencies. By 2012, the portfolio contained loans in five currencies, mainly due to revaluation of all ADB loans to SDR from USD and some new foreign loans in NZD and AUD.

**Figure 18: External Debt by Currency**





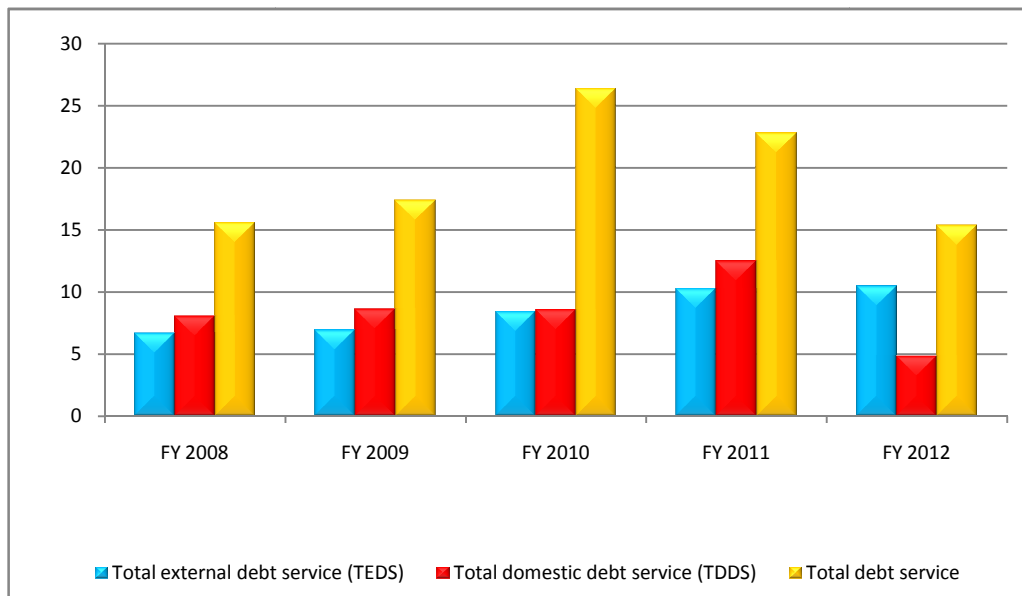
## 4.4 Total Public Debt Service

The structure of debt service changed over the 5 year period from June 2008 to June 2012. External debt service increased from 45% in 2008 to 69% in 2012, while domestic interest payments decreased from 55% in 2008 to 31% in 2012. Total debt service as a percentage of revenue saw an increase of 1.3 basis points, between 2008 to 2012 due to decrease in revenue collection.

**Table 17: Public Debt Service in TOP\$m**

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
External Principal	4.6	4.7	4.6	6.0	5.7	-0.3	1.1
External Interest	2.1	3.6	3.8	4.3	4.8	0.5	2.7
<b>Total External debt service (TEDS)</b>	<b>6.7</b>	<b>8.3</b>	<b>8.4</b>	<b>10.3</b>	<b>10.5</b>	<b>0.2</b>	<b>3.8</b>
TEDS as a % of total debt service (TDS)	45.3	49.1	49.4	45.2	69.1	23.0	23.8
Domestic Principal	6.4	7.0	6.9	10.4	3.0	7.4	-3.4
Domestic Interest	1.7	1.6	1.7	2.1	1.7	-0.4	-
<b>Total Domestic debt service (TDDS)</b>	<b>8.1</b>	<b>8.6</b>	<b>8.6</b>	<b>12.5</b>	<b>4.7</b>	<b>-7.8</b>	<b>-3.4</b>
TDDS as a % of TDS	54.7	50.9	50.6	54.8	30.9	-23.9	-23.8
<b>Total debt service</b>	<b>14.8</b>	<b>16.9</b>	<b>17.0</b>	<b>22.8</b>	<b>15.2</b>	<b>-7.6</b>	<b>0.4</b>
Recurrent Revenue	161.8	186.8	159.6	151.0	146.7	-4.3	-15.1
Export Earnings	93.6	95.1	83.2	100.2	103.1	2.9	9.5
Total debt service as % of revenue	9.1	9.0	10.7	15.1	10.4	-4.7	1.3
Total external debt service as % of exports	7.2	8.7	10.5	10.3	10.2	-0.1	3.0

**Figure 19: Public Debt Service**



### 4.4.1 External Debt Service by Creditor Category

Total external debt service increased significantly from \$6.7m in 2008 to \$10.5m in 2012. Principal repayments increased from \$4.6m in to \$5.7m



in 2012 and the interest payments also increased from \$2.1m to \$4.8m in 2012. In the year ending 2012, a significant proportion of debt service was paid to multilateral creditors at 53% and to bilateral creditors at 44%, of the total debt service.

**Table 18: External Debt Service by Creditor Category in TOP\$m**

Creditor Category	Payments	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 yr change	5 yr change
<b>Bilateral</b>	Principal	0.6	1.2	1.2	1.3	1.1	-0.2	0.5
	Interest	0.7	2.5	2.5	3.0	3.5	0.5	2.8
	<b>Total</b>	<b>1.3</b>	<b>3.7</b>	<b>3.7</b>	<b>4.2</b>	<b>4.6</b>	<b>0.4</b>	<b>3.3</b>
<b>Commercial Bank</b>	Principal	-	0.2	0.3	0.2	0.2	-	0.2
	Interest	-	-	0.0	0.1	0.1	-	0.1
	<b>Total</b>	<b>-</b>	<b>0.2</b>	<b>0.3</b>	<b>0.3</b>	<b>0.3</b>	<b>-</b>	<b>0.3</b>
<b>Multilateral</b>	Principal	4.0	3.1	3.1	4.6	4.4	-0.2	0.4
	Interest	1.4	1.4	1.4	1.2	1.2	-	-0.2
	<b>Total</b>	<b>5.4</b>	<b>4.5</b>	<b>4.5</b>	<b>5.8</b>	<b>5.6</b>	<b>-0.2</b>	<b>0.2</b>
<b>Grand Total</b>	Principal	4.6	4.7	4.6	6.0	5.7	-0.3	1.1
	Interest	2.1	3.6	3.9	4.3	4.8	0.5	2.7
	<b>Total</b>	<b>6.7</b>	<b>8.3</b>	<b>8.4</b>	<b>10.3</b>	<b>10.5</b>	<b>0.2</b>	<b>3.8</b>

#### 4.4.2 Principal and Interest Payments

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

**Figure 20: External Debt Service by payment type**

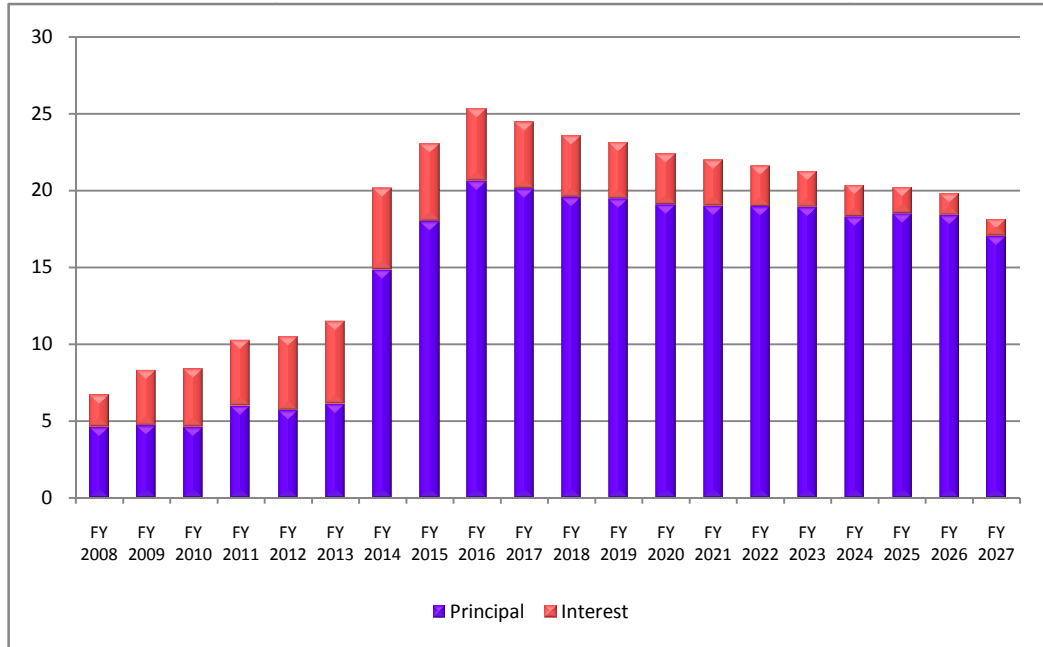
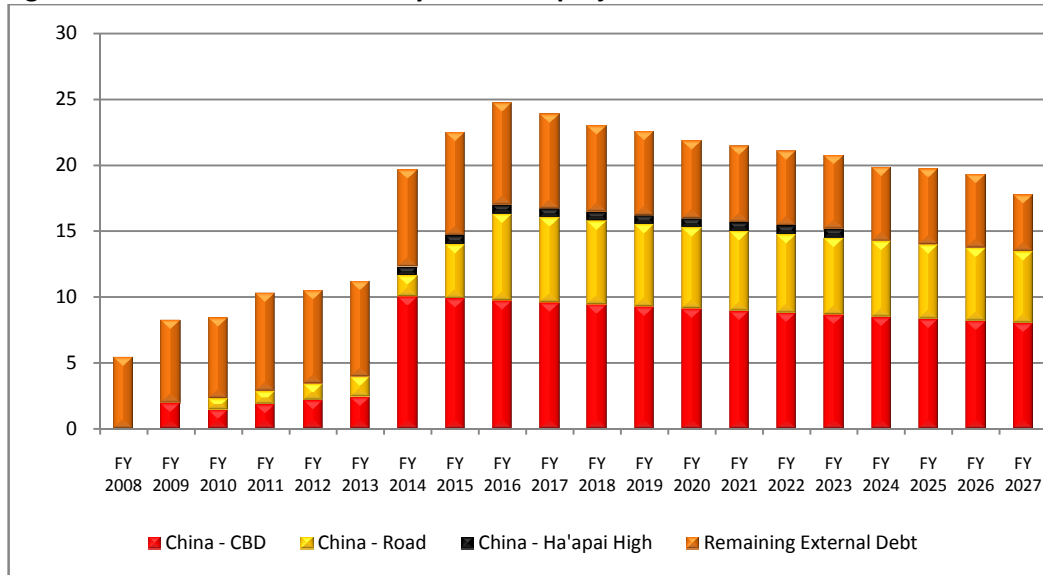


Figure 21: External Debt Service by main PRC project



### 4.4.3 Debt Service Schedule

The principal repayments for the Nuku’alofa CBD Reconstruction loan will begin in September 2013. The MoFNP in its efforts to minimise risks,



and to reduce Tonga's high external debt servicing obligations, has filed requests with the Government of the People's Republic of China and the China EXIM Bank to convert some of the loans to development grants. These include (i) the Ha'apai High School loan (ii) the "Non on-lent" portion of Nuku'alofa CBD Reconstruction loan and (iii) the balance of the Janfull International Dateline Hotel loan. Alternatively, it has requested the Chinese authorities to consider deferment of the repayment of the principal of the Nuku'alofa CBD Reconstruction Loan for another period of 5 years, that is, to September 2018.

## 5. Contingent Liabilities

### 5.1 Loans On-lent

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

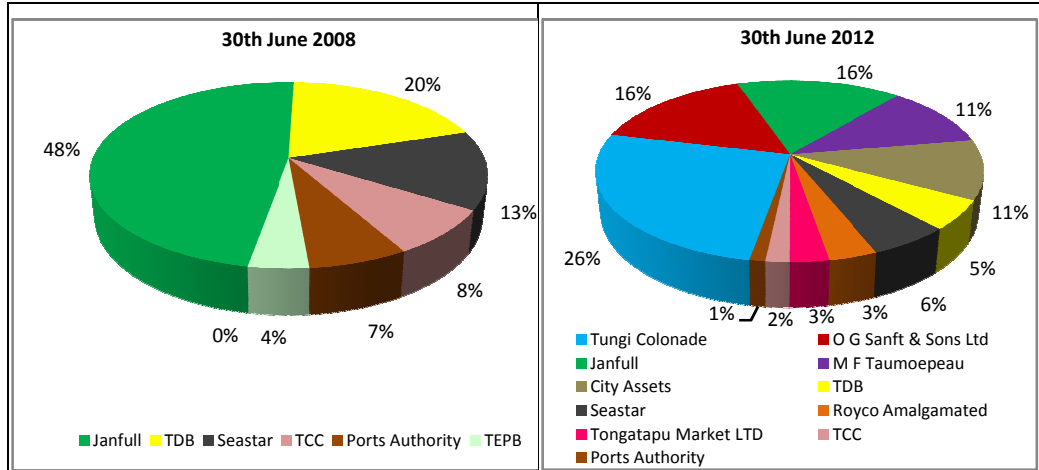
**Table 19: On-Lent Debt in TOP\$m**

Organisation	Loan Balance		5 yr Change
	FY 2008	FY 2012	
OG Sanft & Sons Ltd	-	10.2	-10.2
Janfull International Dateline Hotel	12.6	10.5	-2.1
MF Taumoepeau & Sons Ltd	-	7.2	-7.2
Tonga Development Bank	5.2	3.3	-1.9
Seastar Fishing Co. Ltd.	3.6	3.6	-
Royco Amalgamated Co. Ltd.	-	2.2	2.2
Tongatapu Market Ltd.	-	1.7	1.7
Tonga Communications Corporation	2.1	1.1	-1.0
Ports Authority Tonga	1.8	0.7	-1.1
Tungi Colonnade	-	16.6	16.6
City Assets	-	6.8	6.8
Tonga Electric Power Boarc	1.1	-	-1.1
<b>Total</b>	<b>26.4</b>	<b>63.9</b>	<b>37.5</b>

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

**Figure 22: On-lent Debt by Borrower**





The total on-lent loan repayment as at 30 June 2012 is estimated at \$0.98m. The payments received were from TDB (59.1%), TCC (29.7%) and Royco Amalgamated (11.2%).

## 5.2 Loan Guarantees

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

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

As shown in the table below, during the year, the outstanding Government guaranteed debt decreased by \$4.2m to \$7.8m as at June 31, 2012. At present, the government is not paying on any defaulted guaranteed loans.

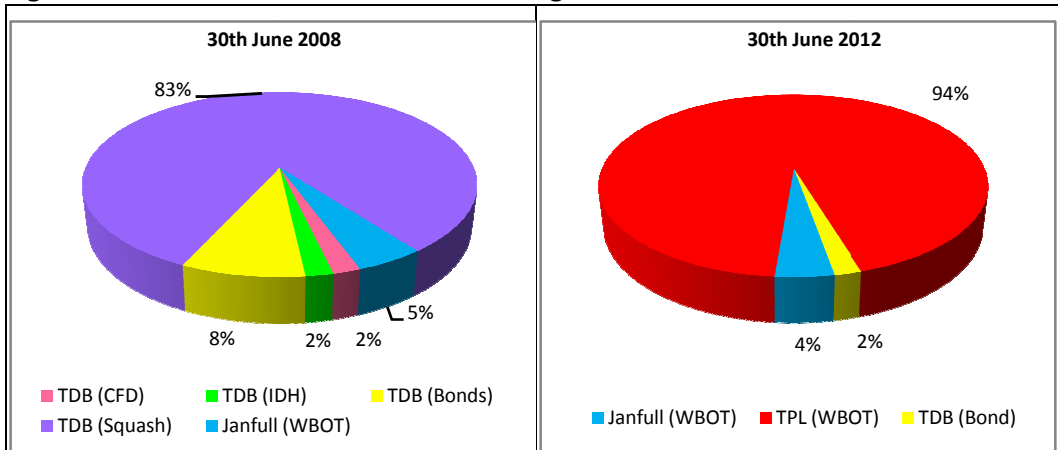
**Table 20: Publicly Guaranteed Debt in TOP\$m**

Organisation	Year Loan Contracted	Obligation Guaranteed	Creditor Country	Loan Balance		5 yr Change
				FY 2008	FY 2012	
Janfull (WBOT)	2007	Renovation Project	Tonga	0.5	0.3	-0.2
TPL (WBOT)	2010	Capital Project	Tonga	-	7.3	7.3
TDB (Bond)	2011	Bond Issue	Tonga	-	0.2	0.2
TDB (CFD)	1995	Development Project	Tonga	0.2	-	-0.2
TDB (IDH)	2003	Hotel Project	Tonga	0.2	-	-0.2



TDB (Bonds)	2003	Bonds Issue	Tonga	0.9	-	-0.9
TDB (Squash)	2004	Development Project	Tonga	8.7	-	-8.7
<b>Total</b>				<b>10.5</b>	<b>7.8</b>	<b>-2.7</b>

Figure 23: Guaranteed Disbursed Outstanding Debt



As at 30 June 2012, there were no guaranteed loan payment arrears.

## 6. Debt Sustainability

### 6.1 Debt Sustainability Analysis

The **Sustainable Debt Policy for Tongan Sovereign Debt** sets the Government's debt objective to maintain sovereign debt within levels that are sustainable over time. To quantify this objective, explicit debt targets are set based on the IMF's sustainable debt indicators. The targets are modified to reflect the unique aspects of the Tongan economy, namely the low formal export base and the large remittance flows. The following **Tables** and **graphs compare the IMF's country debt targets and the GoT's debt targets** to the estimated debt position, **as at 30 June 2012** and including the undisbursed amounts. Based on this analysis, it estimates that the **NPV-of-external debt to GDP ratio** will be **43%**, and *in ratio to exports & remittances* at **155%** and *in ratio to revenue* at **227%**, and **total debt service to revenue** at **10%** and *in ratio to exports & remittances* at **7%**. **All the NPV ratios breach both the recommended IMF and the modified GoT targets.**

In reference to the recent IMF Article IV mission for 2012, Tonga **remains classified** at a **high risk of external debt distress** where under the baseline and extreme scenarios, **both the NPV of debt to**



**GDP and to Exports ratios continue to remain above** the country specific indicative thresholds for a prolonged period.

**Real GDP growth is projected at 0.4% in 2012/13** due to the withdrawal of fiscal stimulus related to the completion of the China EXIM Bank loan funded constructions, and projected to **rebound to around 0.9% in 2013/14** and the medium-term, in line with the average of the past 15 years. This **economic growth is expected to be moderate but is subject to downside risks** including the global economic outlook through lower remittances and tourism receipts. Inflation will likely continue to rise as result of global commodity and food prices and fuel costs and the external position is expected to deteriorate with higher imports. **Tonga's high public debt** leaves the country highly exposed to shocks including natural disasters, and posing a risk to economic prospects. **Challenges remain for Tonga**, where **mitigating the risks** will necessitate fiscal consolidation, **further progress on structural reforms** to raise growth as well as **continued grant provision** from donors. **Macroeconomic policies** focus in coming years, to restore the room for countercyclical policies, reduce the risks to Tonga's external and fiscal sustainability and to lay the foundations for higher potential growth.

**Table 21: Macro data (FY 2011/12 ests – T\$m) and debt data based on FC/TOP rates as at 30 June 2012**

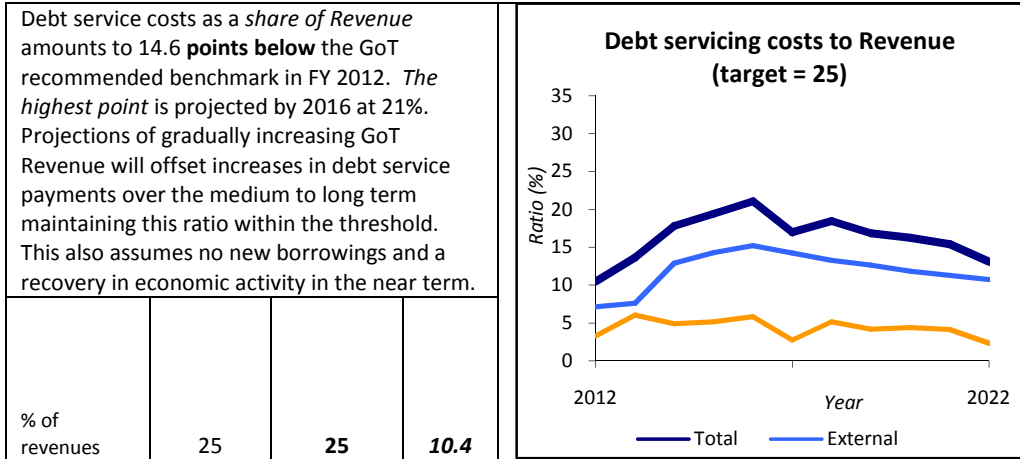
GDP (nominal)	\$781.5
Remittances	\$112.3
Exports of goods & services	\$103.1
Recurrent Revenue	\$146.7
Real growth rate (pa)	-0.2%
GDP deflator/inflation rate (pa)	3.4%

■ = The current status of this indicator is exceeding the IMF and GoT targets

Debt Sustainability INDICATORS	IMF TARGET (%)	GoT TARGET (%)	YTD Jun-12 (%)	PROJECTED Status as at 30 June 2012 and looking forward
<b>NPV of Government External debt</b>				
<p>The <b>NPV to GDP</b> exceeds the recommended <b>GoT threshold of 40%</b> as at FY 2012. Sustainability is not restored until FY 2014 assuming no new borrowing and no depreciation of the Tongan Pa'anga against the major currencies in its debt portfolio.</p>				



<p>% of GDP</p>	<p>30</p>	<p><b>40</b></p>	<p><b>42.6</b></p>																	
<p>The <i>NPV to Exports and Remittances</i> is 54.7% <b>above</b> the recommended GoT threshold of 100% as at FY 2012. However an anticipated recovery in Remittances and Exports along with no new borrowing should return this ratio within the stipulated benchmark by FY 2018.</p>				<p>NPV of Net Government Debt to Exports and Remittances (target = 100)</p> <table border="1"> <thead> <tr> <th>Year</th> <th>Ratio (%)</th> </tr> </thead> <tbody> <tr> <td>2012</td> <td>155</td> </tr> <tr> <td>2017</td> <td>100</td> </tr> <tr> <td>2022</td> <td>55</td> </tr> </tbody> </table>	Year	Ratio (%)	2012	155	2017	100	2022	55								
Year	Ratio (%)																			
2012	155																			
2017	100																			
2022	55																			
<p>% of exports &amp; remittances</p>	<p>90</p>	<p><b>100</b></p>	<p><b>154.7</b></p>																	
<p>The <i>NPV to Revenue</i> is <b>above</b> the recommended GoT threshold of 200% as at FY 2012 <b>by 27.1 points</b> and reducing going forward. However this does not take into account any depreciation of the Pa'anga especially against the CNY and also any decline in Revenues.</p>				<p>NPV of Net Government Debt to Revenue (target = 200)</p> <table border="1"> <thead> <tr> <th>Year</th> <th>Ratio (%)</th> </tr> </thead> <tbody> <tr> <td>2012</td> <td>227</td> </tr> <tr> <td>2017</td> <td>150</td> </tr> <tr> <td>2022</td> <td>85</td> </tr> </tbody> </table>	Year	Ratio (%)	2012	227	2017	150	2022	85								
Year	Ratio (%)																			
2012	227																			
2017	150																			
2022	85																			
<p>% of revenues</p>	<p>200</p>	<p><b>200</b></p>	<p><b>227.1</b></p>																	
<p><b>Total Debt Service</b></p>																				
<p>Debt service costs in nominal terms as a <i>share of Remittances and Exports</i> amounts to 8.0% <b>below</b> the GoT recommended benchmark in FY 2012. <i>The highest point</i> is projected by 2016 at 14%. While debt service payments are increasing over the medium term due to the impact of the two China loans, the recovery in remittance inflows will offset these payments and returning the indicator to the lower limit.</p>				<p>Debt servicing costs to Remittances and Exports (target = 15)</p> <table border="1"> <thead> <tr> <th>Year</th> <th>Total (%)</th> <th>External (%)</th> <th>Domestic (%)</th> </tr> </thead> <tbody> <tr> <td>2012</td> <td>8.0</td> <td>5.0</td> <td>3.0</td> </tr> <tr> <td>2016</td> <td>14.0</td> <td>10.0</td> <td>4.0</td> </tr> <tr> <td>2022</td> <td>8.0</td> <td>7.0</td> <td>1.0</td> </tr> </tbody> </table>	Year	Total (%)	External (%)	Domestic (%)	2012	8.0	5.0	3.0	2016	14.0	10.0	4.0	2022	8.0	7.0	1.0
Year	Total (%)	External (%)	Domestic (%)																	
2012	8.0	5.0	3.0																	
2016	14.0	10.0	4.0																	
2022	8.0	7.0	1.0																	
<p>% of exports &amp; remittances</p>	<p>14</p>	<p><b>15</b></p>	<p><b>7.0</b></p>																	



## 7. Conclusion and Way Forward

As at 30 June 2012, Government's **external debt** in nominal value is estimated at **41% of GDP**, which **exceeds** the **IMF target** of **30%** and at the **Government target** of **40%**. With the projected position including future disbursements on both the Reconstruction and Roads projects, most of these ratios are expected to further exceed the recommended thresholds going forward (*as shown in the NPV graphs above*).

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

For any further external borrowings to the current portfolio, it will push Tonga into a debt distress position and a possibility on requiring a foreign bail-out. It is therefore **highly recommended** that for any **further financial assistance** required by Government **to be sought mainly in the form of grants**. This will assist to preserve any remaining debt headroom for dealing with potential crisis situations.

Possible options that the Ministry of Finance is exploring to maintain Government debt at a sustainable level:

1. No new borrowings in the short to medium term and including any form of loan guarantee;
2. Hedging of debt service repayments for the CNY and SDR currencies in USD-TOP;
3. Seek grant funding for Government priority projects in the short to medium term;



4. Request to the main external loan creditors to review/reschedule loan terms & possibility of fixing FC repayment rate (EXIM/ADB), and consideration for conversion of loan portion/s as development grant/s;
5. Develop a Medium Term Debt Strategy to manage the risk of high external debt level;
6. Government continues to review its macroeconomic policies to cater for the significant rise in projected external debt service in the next 2 years (FY 2013/14).

For some future reforms of debt management to be considered as priority going forward:

- To maintain debt levels within the recommended sustainability thresholds.
- Continue to discuss with PRC officials on request to convert loan portions to grant.
- There is proposal to install the CS-DRMS (Securities Auction System) for use by NRBT to improve management issues of securities and to be explored further with ComSec.
- Given the high risk position for debt distress especially of external debt and the loans taken from PRC, in line with GoT's debt management objective that a formal MTDS is in process and for development of draft Policy Framework for Government Guarantees with assistance from WB during last quarter of 2012.
- Hedging options available by local commercial banks and discussion with main creditors (EXIM and ADB) on possibility for re-denomination of loans to USD or local currency.
- Development of domestic debt market and more involvement of MoFNP in process for issue of securities.
- On-going capacity building of debt staff to ensure consistent operation of tasks as required.



## 8. Statistical Annex

Table 22: Summary Debt Tables

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	1 YR Change %	5 YR Change %
<b>Total Public Debt (USDm)</b>	<b>97.5</b>	<b>111.7</b>	<b>132.3</b>	<b>180.0</b>	<b>200.8</b>	<b>11.6%</b>	<b>105.9%</b>
Total Public Debt (TOPm)	180.4	224.9	258.3	304.4	352.1	15.7%	95.2%
External Debt	157.9	202.4	228.8	274.9	322.6	17.4%	104.3%
Domestic Debt	22.5	22.5	29.5	29.5	29.5	0.0%	31.1%
<b>Total Public Debt to GDP (%)</b>	<b>27.4%</b>	<b>33.9%</b>	<b>36.3%</b>	<b>38.9%</b>	<b>45.1%</b>	<b>16.0%</b>	<b>64.7%</b>
External Debt to GDP	23.9%	30.5%	32.2%	35.1%	41.3%	17.6%	72.4%
Domestic Debt to GDP	2.9%	2.9%	3.8%	3.8%	3.8%	0.0%	31.1%
<b>Total Debt Service (TOPm)</b>	<b>14.8</b>	<b>16.9</b>	<b>17.0</b>	<b>22.8</b>	<b>15.2</b>	<b>-33.3%</b>	<b>2.7%</b>
Principal	11	11.7	11.5	16.4	8.7	-47.0%	-20.9%
Interest	3.8	5.2	5.6	6.5	6.5	-	71.1%
External	6.7	8.3	8.4	10.3	10.5	1.9%	56.7%
<b>External Debt by Creditor category (TOPm)</b>	<b>157.9</b>	<b>202.4</b>	<b>228.8</b>	<b>274.9</b>	<b>322.6</b>	<b>17.4%</b>	<b>104.3%</b>
Multilateral	141.5	144.4	134.7	122	115.5	-5.3%	-18.4%
Bilateral	16.4	58	92.5	150.9	205.3	36.1%	1151.8%
Commercial	-	-	1.6	2.0	1.8	-10.0%	-
<b>Debt Composition by Instrument Type (TOPm)</b>	<b>180.4</b>	<b>224.9</b>	<b>258.3</b>	<b>304.4</b>	<b>352.1</b>	<b>15.7%</b>	<b>95.2%</b>
Loans	157.9	202.4	228.8	274.9	322.6	17.4%	104.3%
Bonds	22.5	22.5	29.5	29.5	29.5	-	31.1%
<b>Foreign Currency Risk (%)</b>							
% of debt in Chinese Yuan	10.4%	28.7%	40.4%	54.9%	63.6%	15.9%	512.7%
% of debt in SDR	88.9%	70.9%	58.5%	44.2%	35.7%	-19.3%	-59.9%
% of debt in other currencies	0.7%	0.5%	1.0%	0.9%	0.7%	-24.2%	-2.6%
<b>Interest Rate Risk (%)</b>							
% of debt at floating rate	0.0%	0.0%	0.7%	0.7%	0.6%	-23.3%	-
% of debt at fixed rate	100.0%	100.0%	99.3%	99.3%	99.4%	0.2%	-0.6%
<b>Roll-over Risk (Yrs)</b>							
Average term to maturity - domestic (years)	5.0	5.0	4.6	4.6	4.7	2.2%	-6.0%
Average term to maturity - external (years)	35.9	36.2	35.6	34.8	34.8	0.0%	-3.1%
<b>Fiscal Indicators (%)</b>							
Total Debt Service to Expenditure	9.9%	8.1%	9.7%	12.8%	9.2%	-28.4%	-7.4%
Total Debt Service to Revenue	9.1%	9.0%	10.7%	15.1%	10.4%	-31.4%	13.3%
Interest cost to Expenditure	2.6%	2.5%	3.2%	3.7%	3.9%	7.4%	54.2%
<b>Vulnerability Indicators (%)</b>							
Reserves to External Debt	56.4%	67.3%	74.5%	74.1%	76.3%	2.9%	35.2%
External Debt Service to Exports & Remittances	2.3%	3.1%	3.5%	4.2%	4.9%	16.8%	115.6%



Annual Public Debt Bulletin (June 2012)

Main Economic Variables (TOPm)	FY	FY	FY	FY	FY	1 YR	5 YR
	2008	2009	2010	2011	2012	Change %	Change %
Gross Domestic Product	659.3	664.3	711.4	783.4	781.5	-0.2%	18.5%
Exports of Goods & Services	93.6	95.1	83.2	100.2	103.1	2.9%	10.1%
Remittances	202.8	175.2	157.4	146.5	112.3	-23.3%	-44.6%
Expenditure	148.9	207.8	175.8	177.5	165.2	-6.9%	10.9%
Revenue	161.8	186.8	159.6	151.0	146.7	-2.8%	-9.3%
Foreign Reserve	89.1	136.3	170.5	203.8	246.1	20.8%	176.2%
Exchange Rate USD/TOP	1.8495	2.0134	1.9518	1.6914	1.7535	3.7%	-5.2%

Sources: MoFNP, NRBT and IMF Country Report No. 11/110

Table 23: External Disbursed Outstanding Debt (TOPm)

	China CBD	China Roads	China Ha'apai High	Remaining External Debt	Total
FY 2008	-	-	6.7	151.1	157.9
FY 2009	41.5	-	7.3	153.5	202.4
FY 2010	52.7	25.0	7.1	143.8	228.8
FY 2011	92.5	46.0	6.5	129.8	274.9
FY 2012	121.3	72.0	6.8	122.4	322.6
FY 2013	118.5	78.3	6.7	113.2	316.7
FY 2014	110.8	78.3	6.0	107.1	302.3
FY 2015	103.2	75.8	5.3	100.4	284.7
FY 2016	95.5	70.7	4.7	93.6	264.6
FY 2017	87.9	65.	4.0	87.4	245.0
FY 2018	80.2	60.6	3.3	81.7	225.9
FY 2019	72.6	55.5	2.6	76.1	207.0
FY 2020	64.9	50.5	2.0	70.9	188.4
FY 2021	57.3	45.4	1.3	65.7	169.9
FY 2022	49.6	40.4	0.6	60.6	151.4
FY 2023	42.0	35.3	-	55.6	133.0
FY 2024	34.3	30.3	-	50.4	115.1
FY 2025	26.7	25.2	-	45.1	97.1
FY 2026	19.1	20.2	-	39.9	79.2
FY 2027	11.4	15.1	-	35.9	62.5

Source: MoFNP

Table 24: External Debt Service (TOPm)

	China CBD	China Roads	China Ha'apai High	Remaining External Debt	Total
FY 2008	-	-	-	5.4	5.4
FY 2009	1.9	-	-	6.3	8.3
FY 2010	1.4	0.9	-	6.2	8.4
FY 2011	1.8	1.0	-	7.4	10.3
FY 2012	2.2	1.2	-	7.1	10.5
FY 2013	2.4	1.5	-	7.3	11.2
FY 2014	10.0	1.6	0.7	7.4	19.7
FY 2015	9.9	4.1	0.7	7.8	22.5
FY 2016	9.7	6.6	0.7	7.8	24.7
FY 2017	9.5	6.5	0.7	7.2	23.9





Annual Public Debt Bulletin (June 2012)

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<i>cont.</i>	<b>China CBD</b>	<b>China Roads</b>	<b>China Ha'apai High</b>	<b>Remaining External Debt</b>	<b>Total</b>
FY 2018	9.4	6.4	0.7	6.6	23.0
FY 2019	9.2	6.3	0.7	6.4	22.6
FY 2020	9.1	6.2	0.7	5.9	21.9
FY 2021	8.9	6.1	0.7	5.8	21.5
FY 2022	8.8	6.0	0.7	5.7	21.1
FY 2023	8.6	5.9	0.7	5.6	20.7
FY 2024	8.5	5.8	-	5.6	19.8
FY 2025	8.3	5.6	-	5.8	19.7
FY 2026	8.2	5.5	-	5.6	19.3
FY 2027	8.0	5.4	-	4.3	17.8

Source: MoFNP