



Budget Statement 2012-2013

Government of the Kingdom of Tonga

"CREATING OPPORTUNITY IN EXTRAORDINARY TIMES"



'Ikale Tahi players rejoicing after victory over France at the 2011 Rugby World Cup, 1st October 2011, Wellington Regional Stadium

**Ministry of Finance & National Planning,
Nuku'alofa, June 2012.**

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1 FOREWORD

The new Government came into power on January 2011 at a time when the economy was trying to recover from the effects of the global crisis and domestic instability. Since then we have established the Tonga Strategic Development Framework (TSDF) 2011-2014 to guide us on the delivery of services to the people, and how to cope within the context of our current difficult economic and fiscal situations.

Our first budget, for 2011/2012, focussed on prudent budgeting and management of our limited resources to get us back onto a firmer financial footing. We were able to successfully negotiate an increase in budget support, linked to our reform programme, and maintain fiscal stability. We have managed this budget carefully and will end the year with a safe level of cash balances to give us space to address unforeseen emergencies, however, the overall financial conditions remain tight.

The TSDF review shows that in the 2011/2012 Budget we have been able to mobilize both domestic and aid funds to deliver a wide range of initiatives which are outlined in this budget summary. The economic review confirms that growth has improved due mainly to related construction works provided through overseas loans and grants. Both reviews confirm the validity of the TSDF, but there is a need to stay focussed on key areas, and not to try and spread our limited resources too thinly. We need to improve the quality of growth and ensure that its benefits are spread more evenly across the Kingdom.

The 2012/2013 budget is built on the theme “*Creating Opportunity in Extraordinary Times*”. It continues the 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.

Government is aware of the new responsibilities placed on it by our new democratic government, and the increased demands and expectations of the people. This is truly an ‘extraordinary time’ in our history. The Government remains committed to improving the quality of expenditure by more effective delivery of core services, while also redirecting resources from non-priority to priority sectors to stimulate domestic economic activities and to achieve a more rapid sustainable inclusive growth.

The budget support we have received from our development partners has helped to maintain the desirable level of government expenditure; however, Tonga must over time live within its fiscal means to ensure ongoing macroeconomic stability. The Government believes more can be done to deliver quality services and boost economic activity within a sustainable budget envelope. At the same time the ongoing support of our development partners is much appreciated.

But none of the above measures is possible for Government to carry out alone. Our ‘extraordinary times’ demand more than just a change in how the people choose their leaders; it requires a stronger, more transparent and inclusive partnership between the Government of the day and the people. It requires us all to raise the standard of our contribution through raising the standard of our professionalism and performance. This requires ‘extraordinary changes’ and evolution of our culture to complement our political changes. The Budget is aimed to support these developments but it is only a part of the process. Our Budget will only make a real contribution if we are sure that it makes a difference in the lives of the people we are serving.

It is my sincere hope that this Budget will be another step forward on the long path of ‘extraordinary’ changes that our Kingdom is going through to ensure we are “*Creating Opportunity in Extraordinary Times*”.

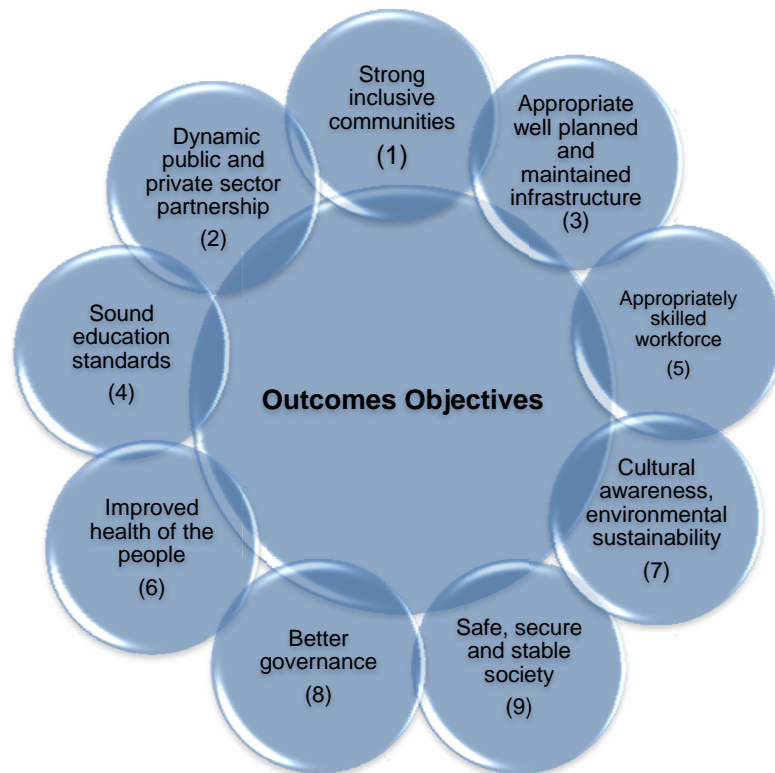
.....
Hon. Lisiate ‘Aloveita ‘Akolo
Minister for Finance and National Planning

2 THE NATIONAL DEVELOPMENT VISION

“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”.

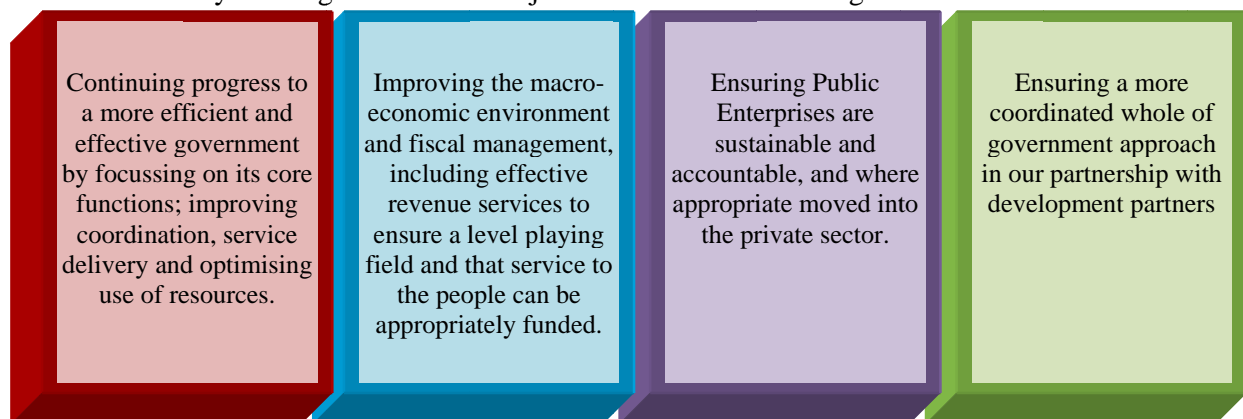
2.1 Outcome Objectives

The Government’s Vision in the Tonga Strategic Development Framework (TSDF) is to be achieved by delivering the following outcome objectives:



2.2 Enabling Themes

The delivery of Tonga’s Outcome Objectives is facilitated through:



3 BUDGET ESTIMATE AT A GLANCE

The TSDF informs and guides the Ministries plans on budget allocation and the need to contribute to our theme of “*Creating Opportunity in Extraordinary Times*”.

The *Budget 2012/2013* is based on four priority areas and six fiscal policies:

Priority Areas:

- Improve private sector development (for enhanced growth)
- Improve community development (for lifting of the standards of living of the people)
- Enhance governance (for greater transparency)
- Improve productivity and effectiveness of the public sector (for improved delivery of services to the people).

Fiscal Policy:

- To operate responsibly and prudently
- Pursue non-distortionary tax collection and remove leakages
- Improve service delivery and maintenance of assets
- Keep public debt within sustainable levels observing Governments interim “No New Loan Policy”
- Continue rationalization of Public Enterprises
- Improve donor coordination for better utilization of aid resources

Total Appropriation (cash): \$225.9 million of which \$179.9 million government (including Budget support of \$22.5 million) and \$46.0 million development.

Total Budget (cash plus in-kind): \$332.2 million, of which in-kind \$106.3 million.

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

Outcome Objectives	2012/2013				
	Government (Recurrent)	Donor (Cash only)	Donor (In-kind only)	Total Donor Cash & In-kind	Total Recurrent & Development
1. Strong inclusive communities	8.8	5.4	1.9	7.2	16.0
2. Dynamic public and private sector partnership	13.0	7.4	2.0	9.4	22.5
3. Appropriate well planned and maintained infrastructure	6.6	3.6	60.3	63.9	70.5
4. Sound education standards	30.9	14.3	15.6	29.9	60.8
5. Appropriately skilled workforce	1.0	0.8	-	0.8	1.8
6. Improved health of the people	21.4	4.8	0.8	5.5	26.9
7. Cultural awareness, environmental sustainability	2.9	1.7	21.6	23.3	26.3
8. Better Governance	80.4	3.9	3.6	7.4	87.9
9. Safe, secure and stable society	14.9	4.3	0.5	4.7	19.6
Total	179.9	46.0	106.3	152.3	332.2

Table 2: Key Economic and Fiscal Indicators:

	2010/2011	2011/2012	2012/2013
<i>Real GDP Growth</i>	4.7%	-0.2%	0.4%
<i>Nominal GDP¹ in \$ million</i>	783.4	781.5	784.5
<i>(As % of GDP)</i>			
<i>Total Domestic Revenue</i>	20.7%	18.3%	20.1%
<i>Total Budget Support</i>	3.3%	3.6%	2.9%
<i>Total Project Aid Funding (cash)</i>	3.7%	5.0%	5.7%
<i>Total Project Aid Funding (in-kind)</i>	16.4%	17.2%	13.5%
<i>Total Expenditure²</i>	42.8%	38.2%	42.4%
<i>Total Public Debt</i>	39%	45%	45%
<i>Debt Servicing</i>	3%	2%	3%

¹ Official nominal GDP estimate for 2010/2011. All projections (p) based on constant prices

² Total recurrent plus donor cash and in-kind expenditure

Source: Ministry of Finance and National Planning & Statistics Department

4 MAIN BUDGET EXPENDITURE CHANGES

Table 3: Main Budget Expenditure Changes 2012-2013 compared to 2011-2012

<i>Vote</i>	<i>Ministry</i>	<i>* Budget Allocation for FY 2012/2013(\$)</i>	<i>Special Expenditure Features</i>
01	Palace Office	5,393,477	<p>* Government of Tonga: Decrease by \$0.6m due to reduction in overseas travel by \$0.5m</p> <p>* Donor Cash/In-kind Project: Increase by \$0.7m to cater for new equipments and furniture for the Royal Palace</p>
02	Legislative Assembly	4,361,600	<p>* Government of Tonga: Remain with the same Budget Allocation</p> <p>* Donor Cash/In-kind Project: The budget increase from \$0.2m to \$0.6m due mainly to new projects e.g. new Support to Parliament Project funded by AusAid/UNDP of \$0.5m, however, other projects e.g. Induction Project to Parliament, have ended therefore the net increase is only \$0.4m</p>
03	Audit Office	1,196,629	* Government of Tonga: Increase of \$0.07m to accommodate requirements for external auditing service.
04	Commissioner of Public Relations	165,520	* Government of Tonga: Increase by \$0.04m to cater for staff salary
05	Ministry of Foreign Affairs & Trade	8,084,465	<p>* Government of Tonga: Decrease by \$1.1m due to scale-down of the Tonga Overseas Missions in London and Wellington.</p> <p>* Donor Cash/In-kind Project: Increase by \$0.6m due to new mission in Tokyo funded out of Tonga Trust Fund (TTF)</p>
06	Tonga Defense Services	8,639,000	<p>* Government of Tonga: Increase by \$0.5m to cover government contribution to Tonga Defense Services' new pension scheme.</p> <p>* Donor Cash/In-kind Project: Increase by \$1.3m due to allocations from Australian Defense Force (\$0.3m), Afghanistan troops (\$0.8m) and vessel maintenance funded out of the Tonga Trust Fund (\$0.2m)</p>
07	Prime Minister's Office	26,619,424	<p>* Government of Tonga: Overall reduction of \$1.8m due to Government Restructure and transfer of functions to MIA</p> <p>* Donor Cash/In-kind Project: Increase by \$11m due to Tonga Cable Project \$19m (with Prime Minister's office absorbing the functions of the Ministry of Information and Communications).</p>
08	Ministry of Finance & National Planning	64,273,138	<p>*Government of Tonga: Increased due to increased debt repayments and other projects including constituency grant \$2m, Financial assistance to NGO's and CSO's \$0.24m, National Retirement Fund \$1m; and new initiatives including Agricultural Marketing Fund \$1m and Lord Chancellor \$0.6m, Subsidies remains at \$1.6m (including electricity \$0.5m, streetlights \$0.4m, domestic shipping \$0.24m, domestic airline \$0.2m, GPO \$0.3m).</p> <p>*New projects include cash grant from China \$1m, Japan Grant Grassroot Programme \$1.2m, Niuaotupapu Hospital \$2.0m, Social vulnerability project \$1.0m, Niuaotupapu Post Tsunami</p>

			Recovery \$1.4m and Soft Loan \$5.1m, EU TCF funds \$0.5m and other small projects.
09	Ministry of Revenue Services	5,580,300	*Government of Tonga: No change from FY 2011/12 *Donor Cash In-kind Project: Increase in budget from \$1.0m to \$1.5m due to an allocation for an X-Ray machine \$1.0m for Customs however the net increase is only \$0.5 due to other projects e.g. CMS upgrade not going ahead due to limited funded available.
10	Ministry of Public Enterprises	4,420,000	*Government of Tonga: No change from FY 2011/12 *Donor Cash In-kind Project: Increase from \$0m to \$3.75m covering Tonga Village Network upgrade \$3.50m and Tonga Forestry Project \$0.25m.
11	Ministry of Commerce, Tourism and Labour	12,996,444	*Government of Tonga: Increase by \$1.0m to establish the Tonga Tourist Authority, and \$0.5m for the Ministry's new initiatives. * Donor Cash In-kind Project: Increase from \$3.54m to \$7.19m partly due to NZAID contribution for the Tonga Tourism Support Project and other new initiatives that are expected to be implemented in 2012/13 with funding sources to be later determined.
12	Ministry of Justice	3,589,472	*Government of Tonga: Increase by \$0.07m to meet Court of Appeal operations. *Donor Cash In-kind Project: Supreme Court Judge \$0.45m.
13	Attorney General's Office	2,205,000	*Government of Tonga: Increase by \$0.1m to cater for Attorney General's salary.
14	Ministry of Police, Prisons & Fire Services	14,348,001	*Government of Tonga: Increase in Police allocation by \$0.27m, Prison by \$0.28m and Fire by \$0.33m to cater for respective staff restructure. *Donor Cash In-kind Project: Tonga Police Development Project \$3.0m co-funded by Australia & New Zealand.
15	Ministry of Health	28,619,885	*Government of Tonga: Increase by \$.5m to accommodate annual salary increments and utilities (electricity, telephone and water) for the new hospital blocks * Donor Cash In-kind Project: Decrease from \$25m to \$5m due to completion of Vaiola Hospital and Tonga Health Support Sector Project \$4.2m continues.
16	Ministry of Education & Training	62,307,383	*Government of Tonga: Increase by \$3.97m for new teachers (\$2.9m) and scholarships \$0.6m), others (\$0.47m) * Donor Cash In-kind Project: Increase from \$14m to \$29m due to increase in funds for Tonga Education Support Project (TESP 2) by \$5m and rebuilding of Tonga College by \$10m. Other projects such as the support to Training Vocational Education (TVET) will continue with support from both NZAID/AUSAID \$1.5m
17	Ministry of Internal Affairs	4,991,717	*Government of Tonga: New Ministry with divisions from PMO, MEWAC, MOTEYS, MLCI
18	Ministry of Agriculture, Food, Forests & Fisheries	9,566,962	*Government of Tonga: Increase by \$1.5m to cater for annual salary increments \$0.3m, electricity for the Fisheries inshore research facilities and the cooler containers for farmers' export production, agricultural suppliers and overall operation of the ministry.

			* Donor Cash In-kind Project: Decrease from \$3.5m to \$2.10m due to completion of Stabex funds from the EU.
19	Ministry of Infrastructure	37,451,969	<p>*Government of Tonga: Increase by \$1.06m to cater for road maintenance \$1.0m</p> <p>*Donor Cash In-kind Project: Existing projects continue such as the Pacific Aviation Investment Program \$5.0m, Integrated Urban Development Project \$6.8m, Transport Sector Consolidated Program \$12m while new projects will commence such as the Hihifo Road \$1.8m and . St George Palace \$5.0m, as such there is only a net decrease from \$32m to \$31m for the 2012/13 FY</p>
20	Ministry of Lands, Environment, Climate Change & Natural Resources.	26,022,327	<p>* Government of Tonga: Increase by \$0.19m to establish the Climate Change Unit (staff and operation) within the Ministry.</p> <p>* Donor Cash In-kind Project: Decrease from \$25.6m to \$23.3m, new initiatives include UAE funded solar system \$4.5m, Nuku'alofa Urban Development Program \$4.0m, Outer Islands solar electrification \$3.0m, pilot program for climate resilience \$3.0m, Tonga Energy Road Map (TERM) \$7.7m causing the majority of the decrease with other small projects.</p>
21	Public Service Commission	1,407,747	<p>* Government of Tonga: Increase by \$0.1m for additional operational expenses.</p> <p>* Donor Cash In-kind Project: \$0.4m from AusAID</p>
	Total	332,240,459	
* Note: including Government of Tonga Fund, Budget Support, Donor Cash and Donor In-kind			

5 REVIEW OF CURRENT PROGRESS

5.1 Achievements against TSDF Outcome Objectives

This section reviews the major achievements during the first year of the government's term against the nine outcome objectives and four enabling themes of the Tonga Strategic Development Framework (TSDF). The TSDF provides the guiding framework for government's delivery of its mandate provided for the overall benefit of the people.

OUTCOME OBJECTIVE 1: Strong inclusive communities, by engaging districts/villages/communities in meeting their prioritized service needs and ensuring the equitable distribution of development benefits.

Lead Ministries: LA, PMO, MOFNP, MOH, MEWAC, MOTEYS, MAFFF

- **Constituency Grant Assistance:**
 - introduced for first time, to provide \$100,000 to each 17 constituency for community development
- **Support to the most vulnerable:**
 - US\$3m funding for the World Bank (WB) small public works secured to provide employment for those most affected by the fall in remittances, for project to start in 2013
 - US\$0.9m secured for the Asian Development Bank (ADB) and Japan Fund for Poverty Reduction and Social Protection, design phase completed, implementation due to start shortly
- **Grassroots Grants:**
 - implemented 15 projects to upgraded water supplies and renovated schools \$1.2m (Japan), design work for 2012/13 projects well advanced
- **Improving Rural community development planning and investment:**
 - US\$3m secured and Mainstreaming of Regional Development Initiatives (MORDI)/Tonga Trust starting implementation in July 2012
- **Financial assistances to and subsidies support to Community Development:**
 - Non-Government Organisations & Civil Society Organisations (\$0.6m)
 - support for the 'Ikale Tahi Rugby team for the 2011 Rugby World Cup (\$0.7m)
 - Government continues to pay for street lights for all of Tonga \$0.9m, \$0.4m for maintenance of street lights and \$0.5m for tariff
 - subsidization of ferry and air services to the Niuas (\$240k), to continue in 2012/2013
- **National Centre for Culture and the Cultural Mapping Policy:**
 - National Cultural Committee established and operating
- **Support to Women Development:**
 - approved a National Gender Policy
 - continued the consultation on Convention for Eliminating Discrimination Against Women (CEDAW)
 - strengthened outreach programmes for women
- **Government operations on outer islands:**
 - centralized and streamlined activities

OUTCOME OBJECTIVE 2: Dynamic public and private sector partnership as the engine of growth, by promoting better collaboration between government and business, appropriate incentives, and streamlining of rules and regulations.

Lead Ministries: MLCI, MAFFF, MOTEYS, MOR, TVB

- **Improved Public-Private Dialogue and joint working:**
 - established National Growth and Sector Growth Committees to identify constraints, and find solutions and implement them
- **Marketing and promoting:**
 - of agricultural production and fish for domestic consumption and export
 - establishment of agricultural marketing fund of \$1m in the 2012/2013 budget
- **Assistance for Agriculture & Fisheries Sector**
 - training in production and harvesting of watermelons
 - agriculture Demo Farm Project to generate bio-gas; mushroom farming; manufacturing of noodles from sweet potato. \$0.38m
 - fisheries management programme by Forum Fishing Agency.
 - emergency assistance to support agriculture and fishery systems of tsunami affected families in Niuatoputapu (FAO)
 - re-established treatment plants for agriculture exports, supporting increased exports
- **Assist Tourism industry:**
 - Tonga Tourism Support Project to improve product/brand development, accreditation program for accommodation operators and review of the Tourism Act. \$1m
 - approved establishment of the Tonga Tourism Authority in 2012/13 Budget with \$1m GoT, \$4.2m donor partners, to undertake international marketing and promotional activities with strong private sector participation
- **More Business friendly taxation system still able to collect due taxes:**
 - detailed review of revenue system including taxation policy undertaken (PFTAC)
 - improved tracking and consultation for more efficient Private Sector Assessment and Revenue collection
 - modification to Customs Tariff and Excise Tax rates
- **Business Licence Reform:**
 - approved reform roadmap to improve business regulatory environment i.e turn around time for business registration, longer term licence, amendments to Foreign Direct Investment (FDI) policy
 - started implementation of roadmap activities and action plan
- **Addressing cost of fuel:**
 - identifying options for alternative for coconut oil diesel.
 - negotiating alternative arrangements for Medium Range Tanker facility to allow more cost effective purchase of bulk fuel
 - implementation of solar farms to reduce power costs
- **National Retirement Benefit Fund:**
 - established Fund which should provide retirement contribution coverage for members to the amount of approximately \$10m per annum.

- **Public Enterprise Reform:**

- approved to review the Tonga Development Bank's overall performance and its policy/mandate and how to better assist farmers and other small medium businesses
- reform of Tonga Timber to make better use of the forest in 'Eua and generate employment on the island
- working with IFC to divest the International Dateline Hotel
- preparing Tonga Print for privatization

OUTCOME OBJECTIVE 3: Appropriate well planned and maintained infrastructure that improves the everyday lives of the people and lowers the cost of business, by the adequate funding and implementation of the National Infrastructure Investment Plan.

Lead Ministries: MOT, MOW, MLCI, MOH, MLSNRE, MPE

- **Redevelopment of Nuku'alofa Central Business District (CBD):**
 - completed construction of rental offices \$8.7m, road construction \$26.3m, Vuna Wharf \$5.6m, and other projects \$9.2m
- **'Eua airport runway:**
 - upgrade completed \$3m (NZ)
- **Vaiola Hospital Reconstruction (Phase II):**
 - completed \$19m (Japan)
- **Post Tsunami Recovery for Niuatoputapu:**
 - extensive re-construction to be completed 2012/2013 \$6.4m
- **Integrate Urban Development (Phase I):**
 - Roads construction to be completed 2012/2013. \$6.0m
- **Nuku'alofa Urban Development Sector Project (Phase II):**
 - secured grant funds for the upgrade of Waste Authority Ltd. and Tonga Water Board, due to start 2012/2013 \$4.0m
- **Transport Sector Consolidate Project (TSCP):**
 - funding road improvement (\$10.0m), maritime \$0.50m, aviation \$0.22m
- **Foa Causeway:**
 - on progress \$0.70m (final budget cost \$4.4m)
- **Telecommunications Submarine Cable:**
 - contracts signed, and office being built and the winning tender has been awarded for laying the Cable, total project cost \$54m to be completed 2012/2013
- **A3Z Aerial Tower:**
 - replacement of the A3Z aerial tower \$1.0m (Korea), improved radio coverage
- **Pacific Aviation Infrastructure Project:**
 - secured USD\$25m from the World Bank, for the upgrade of Fua'amotu and Vava'u airports

OUTCOME OBJECTIVE 4: Appropriately Sound education standards, by emphasising quality universal basic education.

Lead Ministry: MEWAC

- **Tonga Education Support Programme (TESP):**
 - improve student performances; improve learning environment and teacher proficiency (\$10.6m)

- **Benchmarking education practices against universal standard:**
 - improving sound education standards for universal education starting in Classes 1-8 and Forms 3-7
- **Review of Curriculum:**
 - revised and implemented curriculum for Class 1 to Form 2
- **Revised Education Act, policies and regulations**
- **School Base Management Practices:**
 - for PTA capacity building and accountability provided under TESP program
- **Approved construction and improvement of education infrastructure (details being finalized):**
 - Tonga College (\$27m Japan)
 - Phase 2 of Tonga High School (\$13m China)
- **Scholarship Programs:**
 - funding assistance towards tertiary education \$2m
- **Assistance to Non-government colleges and early childhood education**
 - college \$400/head; early childhood \$50/head

OUTCOME OBJECTIVE 5: Appropriately skilled workforce to meet the available opportunities in Tonga and overseas, by delivery of improved Technical and Vocational Education & Training.

Lead Ministry: MOTEYS

- **TVET programs and projects:**
 - continue providing technical skills and training for teachers \$0.8m
- **Financial assistances to non-government technical institutes:**
 - \$1,200/head
- **Seasonal Employment Scheme:**
 - expanded contracts for overseas work schemes in Australia and NZ, and looking at opportunities in the USA. Provides significant monetary benefits to families in Tonga.
- **Tonga Institute of Sports:**
 - approved to establish, with initial budget \$0.5m
- **Employment schemes and training programmes:**
 - provided to village and community level
- **Early Childhood Development (ECD) and Disability Education Regulations:**
 - financial assistance approved for ECD
 - developing regulation to enforce equal and inclusive policies for disable people as well as to enhance ECD
- **On the job training programme:**
 - provided to students in technical institutes
- **Inmate rehabilitation programme:**
 - current and future technical training for inmates to improve their skills and abilities when re-joining/ re-settling back to the community.

OUTCOME OBJECTIVE 6: Improved health of the people, by promoting healthy lifestyles choices, with particular focus on addressing non-communicable diseases, and providing quality, effective and sustainable health services.

Lead Ministry: MOH

- ***Preventative health programmes:***
 - continued during the year \$1.5m
- ***Non-Communicable Diseases (NCD)***
 - NCD awareness programmes
 - Tonga Health Sector Support Program (THSSP) \$4.2m
 - implementing healthy & balance diet programmes in schools as part of addressing serious threat from NCDs
 - training for NCDs nurses enhancing their skills & knowledge
- ***New Health infrastructure, completed, with medical supplies and training of staff:***
 - health centers for Vaini and Mu'a
 - refurbished Health Centers at Nukunuku, Kolonga and Houma
 - NCD Clinic at Niu'eiki Hospital, 'Eua
- ***Improved Health Statistics:***
 - making more efficient monitoring of health indicators
- ***Up-skilling and improving technical knowledge:***
 - by visiting technical practitioners and medical experts and provide in-house training
- ***Anti-Tobacco Advocacy Act:***
 - established to prevent and limit the impact of tobacco, includes supervision of tobacco outlets

OUTCOME OBJECTIVE 7: Cultural awareness, environmental sustainability, disaster risk management and climate change adaptation, integrated into all planning and implementation of programs, by establishing and adhering to appropriate procedures and consultation mechanisms.

Lead Ministries: MLSNRE, MOT, TDS, MOPPFS, MLCI

- ***National Culture Committee:***
 - provided Cultural Awareness initiatives for the preservation of cultural artefacts and etiquette
- ***Tonga Village Network Upgrade:***
 - extended and upgrading power to villages, due for completion June 2013 \$3.5m
- ***Climate Change and Environment Initiatives currently under implementation:***
 - Sustainable Urban Plan & Environment Protection (UPEP) \$0.45m
 - Joint National Action Plan (JNAP) - climate change, \$1.5m
 - Pacific Adaptation on Climate Change Project \$0.13m
 - Climate Change Adaptation Needs \$0.14m
 - Ozone Depleting Substances Project (ODS) \$0.06m
 - SPC Funds Fisheries \$0.009m
 - Mangrove Ecosystem \$0.07m
 - Sustainable Water Resources & Water Management, \$0.61m
 - Pilot Project on Climate Change Resilience \$3m
- ***Tonga Energy Road Map (TERM):***
 - established single agency to coordinate renewable energy related activities
- ***Large Scale Solar Power Plants:***

- Meridian Solar Project \$6m in Tongatapu due for completion by June 2012
 - Vava'u Solar Farm, funds approved US\$4m
- **Disaster Mitigation and Response Emergency:**
 - equipment upgraded in Metrological Office and National Emergency Management Office
 - review the arrangements for improving disaster mitigation and response
 - improve enforce of building code

OUTCOME OBJECTIVE 8: Better governance, by adherence to the principles of good governance, accountability, transparency, and rule of law.

Lead Ministries: CL, PMO, TDS, MOPFS, AO, MOJ, CPR, MLCI, MOFNP

- **Improved sharing of information and dialogue:**
 - with Parliament Standing Committee on Finance and Public Accounts
- **Attorney General and Interim Lord Chancellor appointed:**
 - as part of the political and judicial reform
- **Mandate of the Audit Office and Internal Audit function of MOFNP-enhanced**
- **Re-enforcing principles of good governance and transparency:**
 - approved establishment of the Good Governance Commission to assist the establishment and management of the (i) Anti-Corruption Act and (ii) Commissioner for Public Relation (Amendments) Act (iii) Ombudsman
 - approved the release of Cabinet decisions and policy directions of public interests to ensure transparency
- **Public Restructure and Reform for a more efficient, effective and affordable public service:**
 - established a Working Group for Government Restructuring (WGGSR)
 - rationalizing the number of ministries in line with the 12 members of Cabinet under the new constitution for implementation in 2012/2013 budget
 - putting in place and guiding a longer term reform process including, enhanced corporate planning, medium term budget framework and improve staff performance management
 - E-government plan being developed to improve delivery of public services and minimize cost
- **Improving corporate planning:**
 - special corporate planning support given to new ministries to help them set up their new structures
 - established project for enhancing Corporate Planning
- **Improving budget and debt management**
 - improve budget implementation and limiting introduction of additional activities for which funding is not available - targets for revenue collection and expenditure up to December 2011 being met
 - established project for Medium Term Budget Framework (MTBF) based on enhanced Corporate Planning.
 - continued prudent debt management to avoid any further increase in debt burden once the existing loans are fully drawn down.
- **Revenue reforms for enhanced collection with less distortions:**
 - imposing a 3% duty rate on all capital items exempted in 2009

- increasing the excise tax rate of imported tobacco from \$200 per kilo/1000 sticks to \$210, while locally manufactured tobacco remains at \$200 per kilo/1000 cigarettes
- increasing the excise tax rate of all imported beer from \$42 per litre of alcohol (lal) to \$50 while decreasing the tax rate of all locally manufactured beer from \$17.85 per lal to \$10 per lal
- imposing 3% duty on all electronic equipment
- reducing to zero the duty rate of infant milk and all plastic bags imported for export of local produce
- review of revenue service identifying administrative reforms for a more efficient service that is more responsive and less disruptive to the operations of private sector businesses
- established Tax Policy Committee to review policy and supervise recommendations for revenue services
- reviewed duty and excise tax for raw materials & packaging materials for local manufacturers and processors
- radio programme introduced during the year to improve public understanding of tax matters
- successful monthly meetings with brokers to sort out relevant customer issues
- Compliance Enforcement Plan already in place to help follow up on tax arrears
- ***Implementation of Public Procurement Regulations (2010)***
 - standard bidding documents introduced across government ministries for consistency, and fair and transparent procurement procedures
 - Government Procurement Committee effectively operating and ensuring implementation of procurement reform
- ***Improving data quality and reporting***
 - regular budget reporting to Cabinet and ministries and posted same on Ministry's website
 - improved monitoring of macro-economic status of economy and key developments, reported in monthly "Economy At a Glance"
 - detailed update of GDP estimates, visitor arrivals and other data
 - completion of the first five (5) Year National Population Census
- ***Improved Coordination and Cooperation with Development Partners***
 - established sound relations and Joint Matrix for Budget Support with development partners to improve the level and timeliness of such support – seen as a leading example in the region
 - Tonga Development Partners coordination Meetings
 - Project & Aid Coordination Committee (PACC) in place
 - improving project and aid management database
 - developing collaboration & partnership with new development partners e.g. Brazil/UAE

OUTCOME OBJECTIVE 9: Safe, secure and stable society, by maintaining law and order

Lead Ministries: CL, MOJ, MOPPFS, TDS

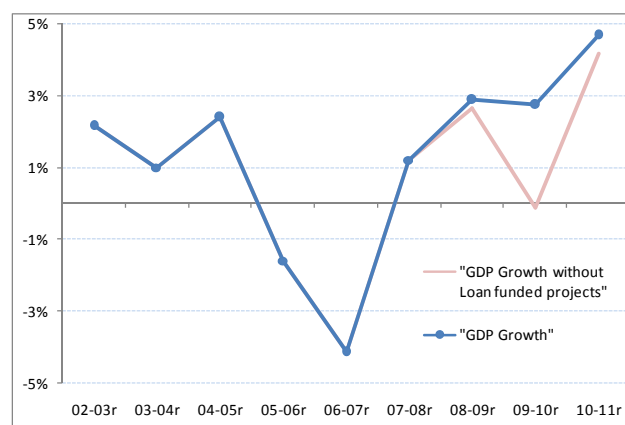
- ***Developing efficient and effective legal system:***
 - encourage participation in the Law Society for continued professional development
 - sponsored Law Week 2011

- consultation and educating the public about Tongan laws
- **Improved policing and prisons**
 - continuation of New Zealand – Australia funded Tonga Police Development Project (\$4m), and negotiation for renewal of the program for the next 3-5 years
 - completed upgraded community policing
 - established joint police committee called the “No Pro Violence”
 - re-designed the Stable Society’s vision to what is called “TAMASI’I MA’A TONGA & FAIAKO MA’A TONGA” (basically when Form 6 & 7 students finish school).
 - inmates institution security, recorded low rate of prison escapes (4 prisoners escaped in 2011)
- **Developing National Security and International Peace keeping**
 - continuous support of Tonga Defense Services (Australian Defence Fund)
 - continued to send TDS staff to Afghanistan, provides training, external earning and good diplomatic relations
 - completion of annual maintenance of Navy vessels

5.2 Recent Economic Progress & Outlook

The Gross Domestic Product (GDP)¹ statistics have been updated to provide a more comprehensive and accurate coverage. The net effect is a slightly higher level for the estimate of GDP over the last few years, and also clarified in more detail the impact of the major aid investments – which in part helped to offset the effects of the global slowdown.

Figure 1- GDP Real Growth 2002/2003 to 2013/2014 with & without Chinese loan for Central Business Area Reconstruction and Road Upgrading



Source: Statistics Department & MOFNP

Figure 1 shows the revised GDP growth over the last decade. 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 90s. By 2007/2008 growth recovered with the start of some rebuilding and gradual return in business confidence.

The government at the time signed the loan with China to help rebuild the Nuku'alofa Central Business District

(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. This effect is shown by the grey line in Figure 1.

¹ Gross domestic product (GDP) measures the market value of all officially recognized final goods and services produced within a country in a given period; this can be measured as total final consumption of goods and services, or total income received in the production of these goods and services since they are two sides of the same coin

The benefit however came at a cost. Government debt has risen above sustainable rates 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 global slowdown and fall in remittances put downward pressure on government revenue despite the loan funded growth in GDP because all imports and activity by the foreign workers and company are tax free, as is standard for foreign development assistance. Government, however, has been successful in negotiating substantial budget support to avoid a further drag on GDP that would have come from government having to cut expenditure.

Overall growth for 2010/2011 was 4.7% with non-loan growth growing slightly over 4%² driven by improvements in a number of areas. Exports were driven by sale of sandalwood, squash, other crops, tuna and sea cucumber. Tourism arrivals grew again and were associated with a big jump in average expenditure of visitors arriving by air helping improve activity in the hotel and restaurant industry. Manufacturing also did well with expansion in local water production and food processing.

Growth was also supported by government maintaining a sound fiscal stance which has allowed foreign exchange reserves to be maintained at sound levels, despite the continued weakness in remittances.

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 Chinese loan funding. Several of the other drivers of growth in 2010/2011 will also fall away as government 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. Government is working with National Reserve Bank of Tonga (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. Tonga Development Bank (TDB) has recently eased its lending conditions.

Factors supporting growth in 2011/2012, include the improvement in tourism, and likely further growth in export of other agricultural and fisheries products which are not suffering from depletion. It has also been possible to avoid cutting government expenditure by maintaining sound revenue collection and continuing to negotiate budget support from our development partners linked to the sound reform performance that they recognize government is implementing.

Looking forward, government is focusing on working more closely with the private sector. Government has listened carefully to the outputs of the consultations on TSDF Progress and the Economic Dialogue sponsored by the NRBT. In response, and as part of the initiative to activate and stimulate the economy, the government moved to strengthening its working

² Source: Ministry of Finance & National Planning and National Statistics Estimates

relationship with the private sector and stakeholders including the formation of the National Growth Committee (NGC) and Sector Growth Committees (SGCs). The objectives for these committees are to help identify constraints to growth and their solutions, and ensure that appropriate actions are taken by government and the private sector to mitigate these constraints. Government calls upon the private sector to participate actively and constructively in these processes for joint cooperation.

Efforts are being made to improve the delivery of services to rural and outer island communities to increase income earning opportunities there. Government is also implementing a restructuring of the public service as part of an ongoing reform programme for a more efficient, effective and affordable service. All these initiatives, which are supported by this Budget, may not provide the same strong boost to total GDP growth that came from the Chinese loan, but it is likely to be a more broad based equitable growth which will actually do more to address the needs of the people and to improve welfare than has been experienced from the recent growth. To be successful, this will need close partnership and cooperation between government, the private sector and communities.

5.3 Public Debt Position

This section summarises the Government's historical debt position that was used for projection for Financial Year 2011/2012, in millions of Pa'anga and in comparison to the previous Financial Year 2010/2011. The information covered external, domestic, on-lent, and guaranteed debt.

These ratios indicate that debt sustainability going forward will face difficulty in maintaining of debt levels within the recommended targets, especially the external debt. It is vital that our current level of economic activity prospects improve together with prudent public debt management, in order to mitigate the vulnerability to shocks.

Table 4: Sovereign Debt Sustainability Indicators

Indicators	IMF Target (%)	GOT Target (%)	FY 2010/2011 (%)	FY 2011/2012 (%)
<i>NPV of External Debt as</i>				
% of GDP ¹	30	40	35	41
% of exports & remittances	90	100	117	151
% of recurrent revenue	200	200	171	212
<i>Total Debt Service as:</i>				
% of exports & remittances	14	15	10	7
% of recurrent revenue	25	25	14	11

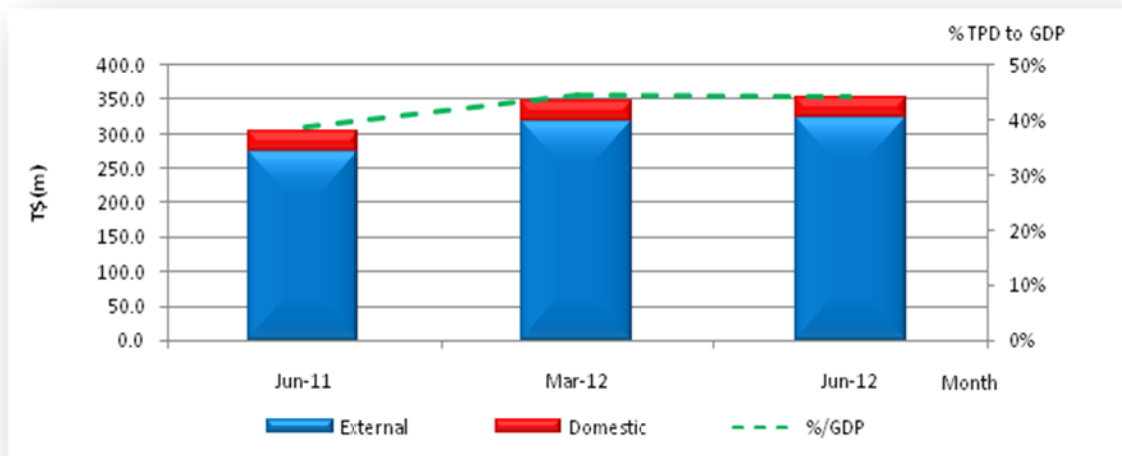
Source: Ministry of Finance & National Planning

¹ Debt measured as NPV is a little less than straight debt, thus this ratio is a little less than the ratio of total debt to GDP used in Table 7 and some of the text.

5.3.1 Total Public Debt at 30 June 2012

Total public debt at 30 June 2012 is estimated at \$353.1m (*at 45% of GDP*), an increase of \$48.7m from June 2011. This is mainly due to increase in external debt by 18 percentage points of GDP, resulting from the disbursements from Export-Import Bank of China (EXIM) for the major infrastructure projects of CBD Reconstruction (\$23m) and Roads Improvement (\$26m). Based also on movement of the main borrowing currencies since June 2011, it is projected that the Chinese Yuan Renminbi (CNY) will appreciate by 3% and the Special Drawing Rights (SDR)³ will depreciate by 2%.

Figure 2 - Total Public Debt to GDP as at 30 June 2012

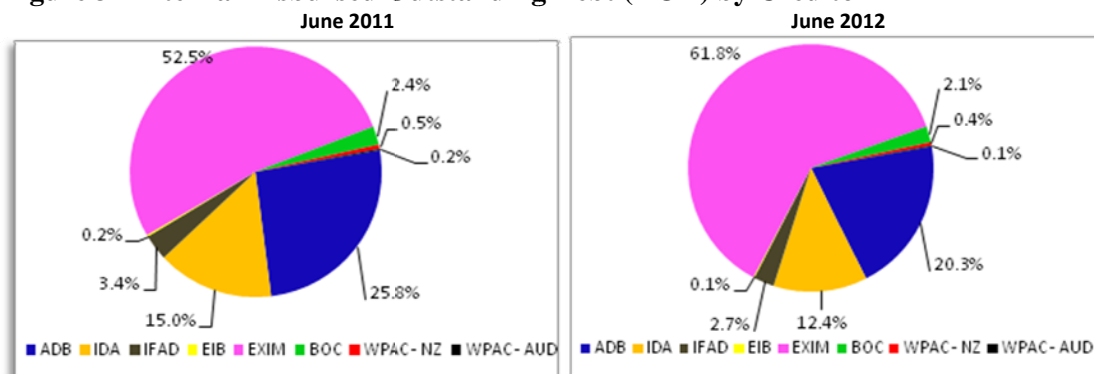


Source: Ministry of Finance & National Planning

5.3.2 External Debt

Total external debt at 30 June 2012 is estimated at \$323.6m (*41% of GDP*) with the total outstanding amount of \$199.9m (*62%*) with EXIM, the Asian Development Bank (ADB) with \$65.7m (*20%*) and IDA (International Development Agency- World Bank) with \$40.1m (*12%*). There are other smaller borrowings from IFAD, EIB, BOC and Westpac Bank that make up the remaining 6%. The projected increase from June 2011 to June 2012 is mainly due to the outstanding disbursements of loans from EXIM estimated at \$55.5m.

Figure 3- External Disbursed Outstanding Debt (DOD) by Creditor



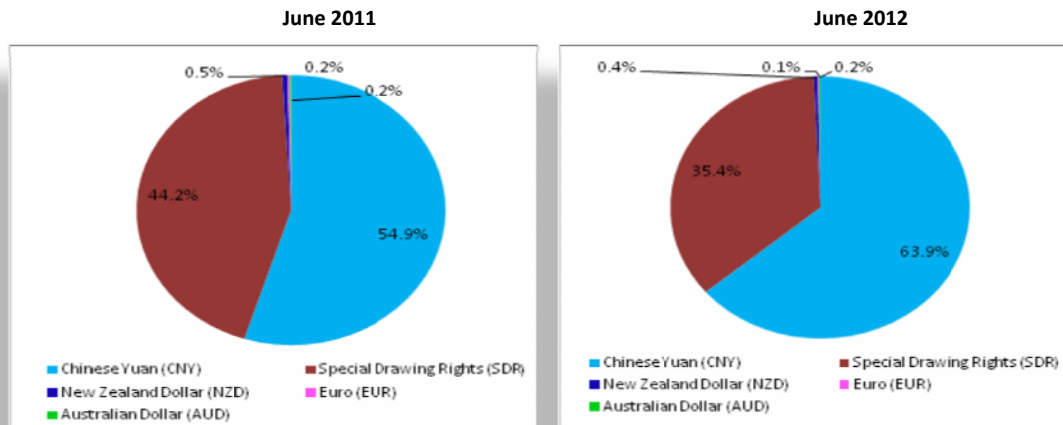
Source: Ministry of Finance & National Planning

³ Special Drawing Right – is defined by a weighted currency basket of four major currencies: the Euro, the US dollar, the British Pound and the Japanese YEN.

5.3.3 Currency Denomination

The main outstanding currency denomination of the external debt as at 30 June 2012, estimates the CNY at \$206.7m (64%) and the SDR at \$114.6m (35%), with note on the significant increase in the CNY composition of \$55.8m (EXIM \$55.5m and BOC \$0.3m). The changes in movement of the Pa'anga against the borrowing currencies during June 2011 to June 2012 is projected to: depreciate against the CNY (3%) and NZD (1%) and appreciate against the EUR (7%); SDR (2%) and AUD (1%).

Figure 4- External DOD by Currency - June 2011 and June 2012

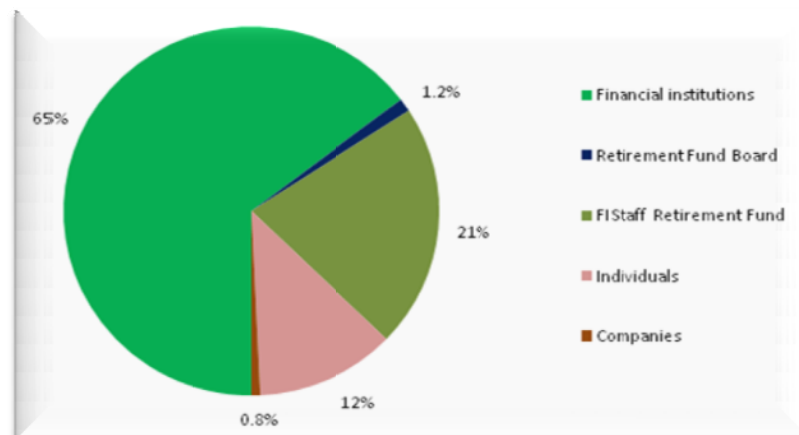


Source: Ministry of Finance & National Planning

5.3.4 Domestic Debt

Total Domestic debt as at 30 June 2012 is estimated at \$29.5m (4% of GDP), for the Government bonds on issue. The main bond holders are Financial Institutions at \$19.1m (65%); Staff Retirement Funds at \$6.3m (21%) and Individuals at \$3.6m (12%). There have been no major changes expected in the outstanding domestic debt between June 2011 and June 2012.

Figure 5- Government Bond Holders (%) as at 30 June 2012



Source: Ministry of Finance & National Planning

5.3.5 Debt Service

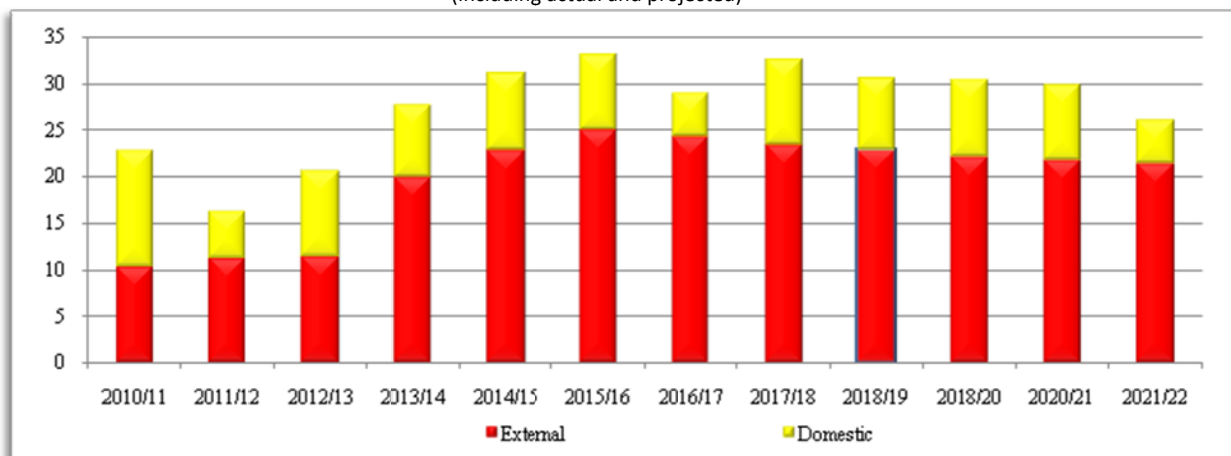
Total debt service (expenditure) for period ended 30 June 2012 is estimated at \$15.4m, with external of \$10.5m (68%) and domestic of \$4.9m (32%). The total debt service is estimated to consume 2% of GDP, and in ratio to recurrent revenue (GoT) at \$143m (11%), and to recurrent expenditure at \$171m (9%). For external loans, the main repayment months are September 2011 at \$3.2m (30% of total external debt service) and March 2012 at \$2.6m (25%) being mainly to EXIM; and for domestic loans are August 2011 at \$1.5m (31% of total domestic debt service) and October 2011 at \$1.4m (29%) for bond principal and interest. There are no public debt payment arrears anticipated. There was a decrease in total debt service during the one (1) year period of \$7.4m mainly due to settlement of the Treasury Notes issued during FY 2010/2011.

Projected total public debt service going forward for the next 10 year period shows a significant rise in external debt service in FY 2013/14 to \$19.9m, which is estimated at over T\$9m or a further 1.2% of GDP. This is mainly due to the principal repayments beginning for the two major loans from EXIM China for Reconstruction in September 2013 and Roads in March 2015 with the debt service continuing over the next 15 years.

These projections include external debt service based on 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 bond roll-overs (principal) on maturity at an average of five (5) years duration and (interest) at weighted average of 5.74% on the total bonds on issue.

Figure 6- Total Public Debt Service (TOPm) FY's 2010/2011 - 2020/21

(including actual and projected)



Source: Ministry of Finance & National Planning

5.3.6 On-lent Debt

Total on-lent debt as at 30 June 2012 as due to Government from various public and other enterprises is estimated at \$63.67m (8% of GDP and 20% of total external loans). The main sub-borrowers are Janfull IDH Ltd. at \$10.29m (26%); OG Sanft Ltd. at \$10.25m (25%); and MF Taumoepeau Ltd. at \$7.16m (18%) for the external loans from EXIM China and also loan to Royco Amalgamated Co. Ltd. at \$2.2m (6%). The above sub-borrowers are under Phase I of the Nuku'alofa CBD Reconstruction loan signed in December 2010. Sub-borrowers of Phase II include Tungi Arcade at \$16.57m and City Assets at \$6.76m.

Current total debt service (revenue) at 30 June 2012 is estimated at \$0.98m, for on-lent loan repayments from TDB of \$0.58m (59%); TCC of \$0.29m (30%) and instalment payments beginning from Royco Amalgamated Co. Ltd. of \$0.11m (11%).

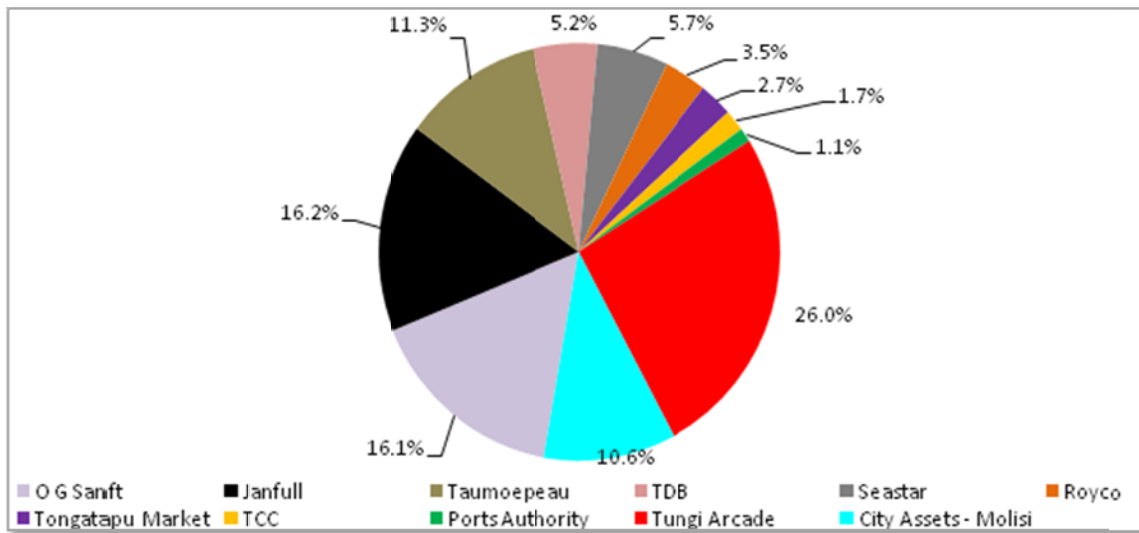
The total on-lent loan payment arrears is estimated at \$12.8m, for loans due from Janfull at \$7.2m (56%) and Seastar at \$5.6m (44%). The decrease of \$0.5m in the outstanding on-lent debt between June 2011 and June 2012 is due to the principal repayments made by TDB and TCC and also fluctuations in the CNY and SDR denominated debt (ie: Loan from EXIM to Janfull and loans from ADB to TCC and TML).

Table 5: On-lent Loans

Sub-borrower	Jun-11(\$m)	Jun-12 est. (\$m)
<i>Tonga Development Bank</i>	3.79	3.32
<i>Tonga Communications Corporation</i>	1.30	1.06
<i>Sea Star Fishing Co. Ltd</i>	3.65	3.65
<i>Janfull International Dateline Hotel Ltd</i>	9.94	10.29
<i>Ports Authority Tonga</i>	0.70	0.70
<i>Tongatapu Market Ltd</i>	1.76	1.72
CBD Reconstructions Project		
<i>Royco Amalgamated Co. Ltd.</i>	2.21	2.20
<i>Taumoepeau Ltd.</i>	7.16	7.16
<i>OG Sanft Ltd.</i>	10.25	10.25
<i>Tungi Arcade</i>	-	16.57
<i>City Assets</i>	-	6.76
TOTAL	40.75	63.67

Source: Ministry of Finance & National Planning

Figure 7 - On-lent DOD by Borrower (%) as at 30 June 2012

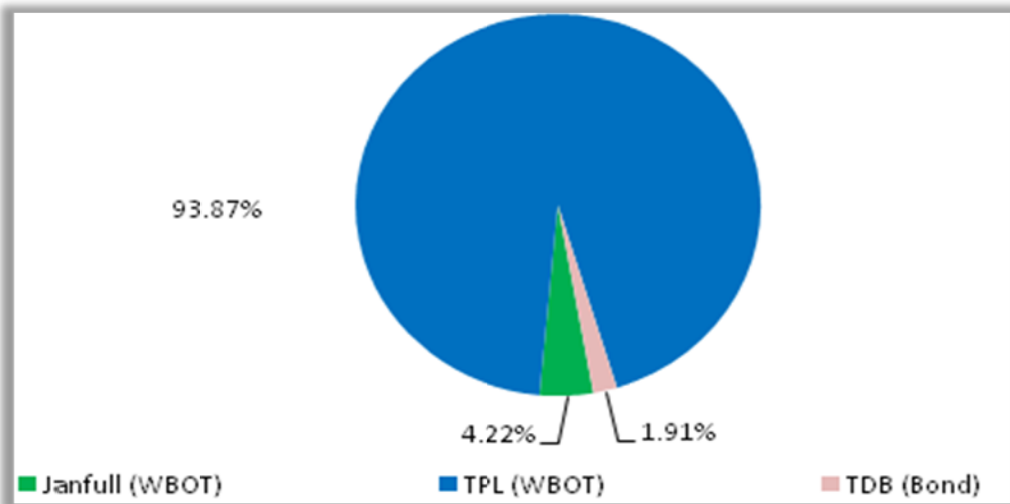


Source: Ministry of Finance & National Planning

5.3.7 Guaranteed Debt

Total guaranteed debt at 30 June 2012 is estimated at \$7.8m (1 % of GDP and 2% of total public debt). This is for loans at WBOT taken by Tonga Power Limited (TPL) at \$7.34m, Janfull IDH Ltd at \$0.33m, and bond issued by TDB at \$0.15. The expected decrease in the guaranteed debt from June 2011 to June 2012 of \$4.3m is due to settlement on maturity of some term loans taken by TPL. No guaranteed loan payment arrears are anticipated.

Figure 8 - Guaranteed DOD by Borrower (%) as at 30 June 2012



Source: Ministry of Finance & National Planning

Table 6: Summary Debt Ratios

Particulars	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12
Total Public Debt (USD\$)	179.9	189.8	197.7	203.9	189.8
Total Public Debt (TOP\$)	304.3	327.3	342.2	348.1	353.1
Domestic Debt	29.5	29.5	29.5	29.5	29.5
External Debt	274.9	297.8	312.8	318.7	323.6
Total Public Debt to GDP (%)	38.8%	43.6%	45.6%	43.6%	45.2%
External Debt to GDP	35.1%	38.1%	40.0%	40.0%	41.4%
Domestic Debt to GDP	3.8%	3.8%	3.8%	3.8%	3.8%
Total Debt Service (\$)	22.8	6.1	9.0	13.4	15.4
Principal	16.3	3.6	5.8	7.5	8.7
Interest	6.5	2.5	3.2	5.9	6.7
External	10.3	3.5	5.1	9.0	10.5
Domestic	12.5	2.6	3.9	4.4	4.9
External Debt by Creditor category (\$)	274.9	297.8	312.8	318.3	323.6
Multilateral	122.0	120.3	117.5	117.0	115.1
Bilateral	150.9	175.6	193.5	199.5	206.7
Commercial	2.0	1.9	1.8	1.9	1.9
Debt Composition by Instrument Type (\$)	304.3	327.3	342.2	348.1	353.1
Loans	274.9	297.8	312.8	318.7	323.6
Bonds	29.5	29.5	29.5	29.5	29.5
Foreign Currency Risk (%)					
% of debt in Chinese Yuan	54.9%	59.0%	61.8%	62.7%	63.9%
% of debt in SDR	44.2%	40.2%	37.4%	36.6%	35.4%
% of debt in other currencies	1.0%	0.8%	0.7%	0.7%	0.7%
Fiscal Indicators (%)					
Total Debt Service to Expenditure	12.9%	3.6%	5.3%	7.9%	9.0%
Total Debt Service to Revenue	12.2%	4.3%	6.3%	9.4%	10.8%
Interest cost to Expenditure	3.7%	1.5%	1.9%	3.5%	3.9%
Vulnerability Indicators (%)					
Reserves to External Debt	57.2%	69.9%	68.4%	72.0%	70.9%
External Debt Service to Exports/Remits	4.3%	1.5%	2.3%	4.2%	4.8%
External Debt Service to Exports	12.5%	4.1%	6.0%	10.8%	11.6%

Source: MOFNP, NRBT & IMF Country report No. 11/110

Reconstruction and Road Improvement Loans

The terms and conditions of the two (2) major loans from China, comprising of the Nuku'alofa CBD Reconstruction project (under A) and Tonga National Road Improvement project (under B) are detailed below.

A. Nuku'alofa CBD Reconstruction Project

1. *Loan amount:* CNY 440m, latest estimates at T\$122m
2. *Maturity period:* 20 yrs from effective date (5 years grace period for principal, 15 years principal repayment);
3. *Payment frequency:* 21st day of September and March annually
(1st interest payment 21 March 2009, last payment 21 September 2028; 1st principal payment 21 September 2013, last payment 21 September 2028);
4. *Interest rate (IN):* 2% per annum over 360 daily basis (from 1st drawdown date on 24 September 2008);
5. *Management fee (MF):* 1% on loan amount (paid 12 September 2008, for lump sum due 30 days from effective date and before first drawdown date);
6. *Commitment fee (CF):* 0.75% per annum on undrawn loan balance (due 30 days after effective date)

Table 7 shows the status on allocation of funds under this project. The on-lent loan portion is fixed at the applicable CNY/TOP rate of 24 September 2008, and the other loan portion is based at CNY/TOP rate on 25 May 2012):

Table 7: Reconstruction Loan Project Allocation

	Projects	TOTAL LOAN (T\$m)	Total to Loan (%)
	PHASE I	19.61	16%
1	MF Taumoepeau & Sons Ltd	7.16	6%
2	OG Sanft & Sons Ltd	10.25	8%
3	Royco Amalgamated Co. Ltd	2.20	2%
	PHASE II	23.33	20%
4	Tungi Arcade	16.57	14%
5	City Assets Ltd	6.76	6%
	Total on-lent projects	42.94	36%
	PHASE I		
6	Palace extension	14.13	12%
	PHASE II		
7	Vuna wharf	33.01	27%
8	Civil works	19.16	16%
9	Asphalt Plant	5.20	4%
	Total GOT projects	71.50	59%
10	Geographic report (stage 1)	0.56	0.5%
11	Mobilisation (stage 1)	1.74	1%
12	Design (stage 1 & 2) - adjustment	1.48	1%
13	Consultancy (stage 1)	0.78	1%
14	Insurance (stage 1)	0.28	0.2%
15	Consultancy (stage 2)	0.63	0.5%
16	Insurance (stage 2)	0.40	0.3%
17	Contingency sum	1.30	1%
	Total other loan portion	7.17	5%
	TOTAL LOAN AMOUNT	121.61	100%

Source: Ministry of Finance & National Planning

Tonga National Road Improvement Project

1. *Loan amount:* CNY 291m, latest estimates at T\$82m
2. *Maturity period:* 20 yrs from effective date (5 years grace period for principal, 15 years principal repayment);
3. *Payment frequency:* 21st day of September and March annually
(1st interest payment 21 March 2010, last payment 21 March 2030; 1st principal payment 21 March 2015, last payment 21 March 2030);
4. *Interest rate (IN):* 2% per annum over 360 daily basis (due from 1st drawdown date on 15 March 2010);
5. *Management fee (MF):* 1% on loan amount (paid 25 February 2010, for lump sum due 30 days from effective date and before first drawdown date);
6. *Commitment fee (CF):* 0.75% per annum on undrawn loan balance (due 30 days after effective date)

Table 8 shows the status on allocation of loan funds for this project (estimates) and is based at CNY/TOP rate on 25 May 2012:

Table 8: Roads Improvement Loan Project Allocation

<i>Projects (TOP)</i>	<i>TOTAL LOAN T\$(m)</i>	<i>Total to Loan (%)</i>
<i>Tongatapu</i>	55.18	67.3%
<i>Vava'u</i>	6.85	8.3%
<i>Ha'apai</i>	1.89	2.3%
<i>Eua</i>	2.50	3.0%
<i>Establishment</i>	1.70	2.1%
<i>Mobilisation</i>	1.84	2.2%
<i>Road survey, geographical, prospecting, geography report</i>	1.70	2.1%
<i>Road designing</i>	6.56	8.0%
<i>Consultant fee</i>	2.46	3.0%
<i>Insurance</i>	0.45	0.6%
<i>Contingency sum</i>	0.89	1.1%
<i>Total other costs (CCECC)</i>	15.61	19.0%
TOTAL LOAN AMOUNT	82.03	100.0%

Source: Ministry of Finance & National Planning

5.4 Key Challenges Identified

The Review of TSDF Progress, shown above and in more detail in *Annex I*, and the Analysis of Economic and Social Performance, summarized above, and in detail in *Annex II*, and discussions such as the Economic Dialogue, indicate that progress is being made and the economy is stabilizing after the large shocks of recent years. However, remittances, our biggest source for foreign exchange earnings, are still declining, imposing uncertainty in our future development.

The following situation and challenges are identified as key in helping to identify the focus of the Budget:

- Recent GDP growth sustained by borrowing is focussing in Nuku'alofa area, future development plans to extend to the outer islands and rural areas
- after large fall, exports show some signs of improvement
- economic sectors are still generally weak, with some improvements in some areas
- indications of greater poverty, especially away from Nuku'alofa
- non-communicable disease and increasing threat to life expectancy and human capital
- high trade deficit contributed by high inflow of aid and remittances, could create structural dependency on imports
- decline in cash remittances but possible increase in in-kind
- high liquidity but declining domestic credit
- excess debt and debt service, so little option for borrowing
- domestic revenue remains weak, but recent improvement
- large wage bill and other non-discretionary expenditure
- dependency on budget support to avoid having to cut service delivery
- dependency on project aid (grants and loans) to fund most government investment
- public service needs to be made more performance oriented to improve delivery of services and development objectives
- need for major reforms in core operations of government

6 GOVERNMENT BUDGET RESPONSE TO CURRENT SITUATION

6.1 Priority Focus for Budget

Taking account of the above reviews, in the 2012/2013 Budget, Government will continue to provide funding to enhance the quality of expenditure to achieve development priorities across all nine outcome objectives. While the TSDF Review indicated progress in many areas, it re-emphasized the conclusion that government needs to be more focused in its budget allocations to address the most important constraints to economic and social growth and development. The Review identified four areas for special focus. As a result, the following sectoral expenditure priorities have been identified for the 2012/2013 budget:

- Improve private sector development (for enhanced growth)
- Improve community development (for lifting of the standards of living of the people)
- Enhance governance (for greater transparency)
- Improve productivity and effectiveness of the public sector (for improved delivery of services to the people).

6.1.1 Improved Private Sector Development

Government is committed to supporting a stable macroeconomic environment and enabling business environment for all participants who engage in lawful business activities and help generate increased incomes and employment.

To be successful, however, it requires closer cooperation between government and the private sector to identify constraints, find solutions and ensure they are implemented. Several public-private sector dialogues and joint-committees have been set up for the purpose. These include the National Growth Committee, which provides key forum for this cooperation, and supports more detailed Sector Growth Committees covering Agriculture, Fisheries, Tourism, Commerce and Manufacturing/Processing. The 2012/2013 budget includes a range of initiatives to help deliver this key area, as shown under Outcome Objective 2 in the next section.

6.1.2 Improved Community Development

Growth alone is not enough, as has been indicated by the unbalanced nature of recent growth in Tonga. The benefits of increased private sector activity, employment and growth need to be felt more widely throughout the Kingdom. While Tonga retains a strong social net work, changing conditions are putting this under strain and we can no longer rely on it to ensure that all vulnerable groups are protected. Government is seeking to direct more development funding to support community level development and considering ways of introducing affordable social protection for the most needy. This budget includes a range of initiatives to help deliver this key area, as shown under Outcome Objective 1 in section 6.2.

6.1.3 Enhanced Governance

Continuing efforts to improve governance will in turn improve private sector growth and community development. Improving governance is one of the pillars of Government's efforts towards improving effectiveness and efficiency without compromising underlining principles of accountability and transparency in the provision of public service. Government knows this

is challenging but is committed to work with all stakeholders to improve governance. This budget includes a range of initiatives to help deliver this key area, as shown under Outcome Objective 8 and 9 in the next section.

6.1.4 Improved productivity and effectiveness of the public sector

While good governance is critical it is not enough if we are to successfully deliver the TSDF, and in particular the focus on growth and communities. We need a more efficient, effective and affordable public service to deliver services and development objectives. The budget will see the introduction of the government restructuring to streamline functions across ministries and agencies. But this is only the start. An ongoing programme of reform, including public enterprises, with particular focus on core functions of planning, finance, project management, human resource and staff management and overall performance management is being put in place. This has been tried in the past with mixed results. Government is committed to pursue this reform with renewed vigour to ensure that we have public services that is relevant to the needs of our political reform and delivers to the expectations of our people. This budget includes a range of initiatives to help deliver this key area, as shown under Outcome Objective 8 in Section 6.2.

6.2 Planned Government Activities by All Outcome Objectives

The detailed government key initiatives, with Key Performance Indicators (KPIs), are listed against each of the nine Outcome Objectives below. These are activities that are funded either from government funds, or anticipated to be funded from aid funds in the Budget. The overall beneficiaries from the achieving these objectives are the people.

OUTCOME OBJECTIVE 1: Strong inclusive communities, by engaging districts/villages/communities in meeting their prioritized service needs and ensuring the equitable distribution of development benefits.

Lead Ministries: LA, PMO, MOFNP, MOH, MET, MIA, MAFF

- **Constituency Grant Assistance:**
 - allocation of \$2m (increased from \$1.7m last year) to be shared among the 17 constituencies, for immediate and urgent community development activities where alternative funding is not available
 - the extra allocation of \$300k is to provide for requests from the outer islands of Ha'apai and Vava'u that each of their shares be increased by \$100k, with the remaining \$100k to be reserved for residential offices of the 7 MPs from the outer islands (3VVU, 2HPP, 1 'Eua, 1 Niua)
- **Support to the most vulnerable:**
 - employment in the community funded by the World Bank (US\$3m) small public works secured to provide employment for those most affected by the fall in remittances,
 - Social Vulnerability Projects funded by ADB (US\$0.9m): pilot project to support vulnerable and disabled in the community to help alleviate the increase in poverty in the rural areas
- **Grassroots Grants:**
 - provision of water supply systems as well as small upgrades/renovations to schools (\$1.2m Japan)
- **Improving Rural community development planning and investment:**

- US\$3m, International Fund for Agricultural Development – IFAD, for implementation by Mainstreaming of Regional Development Initiatives (MORDI)/Tonga Trust. Sixty communities at the end of the project will have community plans with some of those immediate needs funded.
- **Financial assistance to and subsidy support to Community Development:**
 - Non-Government Organisations & Civil Society Organisations including Women Crisis Centers (\$0.6m)
 - Government continues to pay for street lights for all of Tonga (\$0.9m), street lights maintenance (\$0.4m), and tariff (\$0.5m)
 - subsidization of the ferry and air services to the Niua (\$240k)
- **National Centre for Culture and the Cultural Mapping Policy:**
 - next stage is public consultation however pending availability of funds
- **Support to Women Development:**
 - work is ongoing to implement national gender policy
 - ongoing work on CEDAW convention – related to land regulation
 - strengthened outreach programmes for women
- **Government operations/Local government centralization continuing to:**
 - ensure effective government services delivery to the public and support the development of the outer-islands
 - improve extension services to the community in areas such as health, agriculture, training and employment
 - strengthen the communication with government through these local offices
- **Assistance to Forum of Church Leaders:**
 - service desk at MIA (\$0.07m)
- **Introduction of clean energy by Solar Home System – Vava'u/TBU Outer Islands**
 - distribution of solar energy to households of outer islands

OUTCOME OBJECTIVE 2: Dynamic public and private sector partnership as the engine of growth, by promoting better collaboration between government and business, appropriate incentives, and streamlining of rules and regulations.

Lead Ministries: MCTL, MAFF, MIA, MOR

- **Further improve Public-Private Dialogue and joint working:**
 - fully establish the Sector Growth Committees covering agriculture, fisheries, tourism, commerce and manufacturing, to effectively identify constraints, and find solutions and implement them, within the framework of appropriate sector plans
- **Marketing and promoting:**
 - Agricultural Marketing Fund \$1m
 - promoting locally made product and services with the launch of “Buy Tongan Made” campaign
- **Assistance for Agriculture & Fisheries Sector**
 - MAFF re-established treatment plants for agriculture exports, as well as focusing on community based development
- **Assist Tourism industry:**
 - Tonga Tourism Support Project to continue
 - Tonga Tourism Authority funded in the 2012/13 Budget with \$1m GoT, \$4.2m NZAID, to undertake international marketing and promotional activities with strong private sector participation

- ***Tax Reforms:***
 - appropriate implementation of the approved recommendations on Small Business Tax (Presumptive tax) and Natural Resources tax
 - implementation of the recommendations from the PFTAC Revenue Review Report
- ***Business Licence Reform Roadmap to enhance the business regulatory environment. MLCI will continue to streamline licences through the following amendments to the business licences:***
 - longer term licence (even the option of indefinite licence with new administration provisions and stipulated conditions for termination, national interests and public safeguards), electronic and online application process and registry, electronic payment system etc.
 - amendment to the Foreign Investment Act including review of the reserve/restricted lists
 - ministry's internal restructure to prioritize ease of doing business (reduce issuance of licence from 7 working days to only 1 day), and consolidate inspectorate of business compliance, enforcement of statutory administration to ensure satisfactory protection of public health and safety
- ***Addressing cost of fuel:***
 - establish alternative arrangements for Medium Range Tanker facility to allow more cost effective purchase of bulk fuel
 - establishment of solar farm in Vava'u \$4.5m by UAE
 - continue renewable energy projects under TERM to realise the potential of renewable energy
- ***National Retirement Benefit Fund:***
 - continuous Government contributions towards the initial operation of the Fund, \$1m from recurrent budget, while seeking donor funding
- ***Public Enterprise Reform, on-going work in progress :***
 - review of Tonga Development Bank overall performance and its policy/mandate and how to better assist farmers and other small medium businesses
 - for the reform of Tonga Timber to make better use of the forest in 'Eua and generate employment on the island
 - in working with IFC to divest the International Dateline Hotel
 - in preparing Tonga Print for privatization

OUTCOME OBJECTIVE 3: Appropriate well planned and maintained infrastructure that improves the everyday lives of the people and lowers the cost of business, by the adequate funding and implementation of the National Infrastructure Investment Plan.

Lead Ministries: MOI, MCTL, MOH, MLCCNR, MPE,

- ***Redevelopment of Nuku'alofa business district:***
 - buildings and other infrastructure nearly finished (loan from EXIM Bank of China)
- ***Post-tsunami rehabilitation of Niuatoputapu:***
 - World Bank for housing USD \$5m, Japan for water supply \$0.3m, EU for hospital \$2m, and UNDP with the early warning system \$0.5m
- ***Integrate Urban Development (Phase I):***

- Roads construction to be completed 2012/2013. \$6.0m, throughout the country (through loan from EXIM Bank of China, grants from ADB, World Bank)
- ***Nuku'alofa Urban Development Sector Project (Phase II):***
 - funds (\$4.0m) for the upgrade of Waste Authority Ltd. and Tonga Water Board
- ***Transport Sector Consolidate Project (TSCP):***
 - funding road improvement (\$10.0m), maritime \$0.50m, aviation \$0.22m
 - road maintenance funded by AusAID through the World Bank Transport Sector Consolidation Project \$2m
 - Pacific Aviation Infrastructure Project (PAIP) secure funding of \$27m, implementation to start 2012/2013
- ***Tongatapu and Vava'u airport runway upgrading (USD \$27m World Bank grant)***
- ***Foa causeway:***
 - (German funded) targeted to complete by December, 2013 \$4.4m
- ***Friendly Island Shipping Agency:***
 - seeking options for management and operations
- ***Submarine Cable Project:***
 - World Bank, ADB grant and TCL USD\$33m targeted to be completed in mid 2013
- ***Tonga Energy Road Map:***
 - ongoing to increase efficiency of energy usage and identify options for non-renewable energy (multi-donor) \$9m
- ***Management of Vuna Wharf:***
 - arrangements being clarified and first cruise ships to be welcomed in mid 2012
- ***National domestic airline:***
 - operational arrangements under consideration for implementation during the year

OUTCOME OBJECTIVE 4: Sound education standards, by emphasizing quality universal basic education

Lead Ministry: MET

- ***Tonga Education Support Program (TESP):***
 - continue focus to improve student performances; improve learning environment and teacher proficiency: i) review of Curriculum ii) revised and implemented curriculum for Class 1 to Form 2 iii) benchmarking education practices against universal standard iv) improving sound education standards for universal education starting in Classes 1-8 and Forms 3-7 v) School Base Management practices trainings – ongoing training for principals and PTA (only available for non-government schools except LDS and primary schools)
- ***Revised Education Act, policies and regulations***
 - draft policy and regulation to submit in 2012 together with the revised Education Act phase 2.
- ***Construction and improvement of education infrastructure:***
 - Tonga College (\$27m Japan)
 - Phase 2 of Tonga High School (\$13m China)
- ***Scholarship Programs:***
 - continuing funding assistance towards tertiary education \$2m
- ***Quality and Assurance Control Office, improve its efficiency in monitoring improvement in education***

OUTCOME OBJECTIVE 5: Appropriately skilled workforce to meet the available opportunities in Tonga and overseas, by delivering of improved Technical and Vocational Education & Training (TVET)

Lead Ministry: MIA

- **TVET Programmes (NZAID/AUSAID)**
 - continue providing technical skills and training for teachers \$0.8m from the recurrent budget
- **Financial assistances to non-government technical institutes:**
 - \$1,200/head from the recurrent budget
- **Seasonal Employment Scheme:**
 - continue the bilateral and multilateral trade negotiations to expand the opportunities of sending Tongan workers to New Zealand, Australia, USA and other countries, to expand the seasonal work scheme to other skills, including trade and services
- **Tonga Institute of Sports:**
 - approved to establish, with initial budget \$0.5m
- **Employment schemes and training programmes:**
 - Ongoing provision of training programs to village and community level
- **Early Childhood Development (ECD) and Disability Education Regulations:**
 - financial assistance approved for ECD
 - developing regulation to enforce equal and inclusive policies for disable people as well as to enhance ECD
- **On the job training programme:**
 - continue to provide to students in technical institutes
- **Inmate rehabilitation programme:**
 - provides technical training to inmates to improve their skills and abilities when re-joining/ re-settling back to the community.
 - improving skills for graduates to find gainful employment and contribute to their communities
- **Technical training for Tonga Defence Service (Australia, NZ, USAID)**

OUTCOME OBJECTIVE 6: Improved health of the people, by promoting healthy lifestyle choices with particular focus on addressing non-communicable diseases, and providing quality, effective and sustainable health services

Lead Ministry: MOH

- **Preventative health programmes:**
 - continuation in the 2012/2013 with an increase allocation of \$1.9m from \$1.5m in current Financial Year 2011/2012.
- **Non-Communicable Diseases (NCD)**
 - NCD awareness programmes
 - Tonga Health Sector Support Program (THSSP) \$4.2m
 - implementing healthy & balance diet programmes in schools as part of addressing serious threat from NCDs
 - training for NCDs nurses enhancing their skills & knowledge
- **New Health Infrastructure:**
 - new hospital Niuatoputapu – EU \$2.0m construction 2012/2013
- **Improved Health Statistics:**

- ongoing with the current activities in the effort to provide quality health indicators to help identify focus areas in health delivery
- ***Up-skilling and improving technical knowledge:***
 - ongoing visit by technical practitioners and medical experts to provide in-house training
- ***Anti-Tobacco Advocacy Act:***
 - established to prevent and limit the impact of tobacco, includes supervision of tobacco outlets
- ***Immunization program:***
 - continue successful program
- ***Tonga Health to raise awareness on healthy life styles:***
 - continue support
- ***Medical Treatment Scheme (MTS)***

OUTCOME OBJECTIVE 7: Cultural awareness, environmental sustainability, disaster risk management and climate change adaptation, integrated into all planning and implementation of programs, by establishing and adhering to appropriate procedures and consultation mechanisms.

Lead Ministries: MLCCNR, MOI, TDS, MOPPFs, MCTL

- ***Promoting Cultural Awareness***
 - National Culture Committee: promoting awareness for the preservation of our cultural benefits in collaboration with a Korean institution that is helping to train staff
 - encouraging traditional cultural activities in schools: through sponsoring and supporting cultural exchanges, festivals and competitions in schools
 - extend and maintain collections of resources and archive materials related to culture and values
- ***Tonga Village Network Upgrade:***
 - complete and extension and upgrading power to villages, due for completion June 2013 \$3.5m
- ***Climate Change and Environment Initiatives currently under implementation:***
 - Sustainable Urban Plan & Environment Protection (UPEP) \$0.45m
 - Joint National Action Plan (JNAP) - climate change, \$1.5m
 - Pacific Adaptation on Climate Change Project \$0.13m
 - Climate Change Adaptation Needs \$0.14m
 - Ozone Depleting Substances Project (ODS) \$0.06m
 - SPC Funds Fisheries \$0.009m
 - Mangrove Ecosystem \$0.07m
 - Sustainable Water Resources & Water Management, \$0.61m
 - Pilot Project on Climate Change Resilience \$3m
- ***Tonga Energy Road Map (TERM):***
 - coordination of renewable energy (solar)
- ***Large Scale Solar Power Plants:***
 - Meridian Solar Project \$6m in Tongatapu due for completion by June 2012
 - Vava'u Solar Farm, funds approved US\$4m
 - ADB outer island renewable energy project US \$5m (approved and signed in November 2012/2013)

- WB energy project \$8m (approved 2012/2013)
- ***Disaster Mitigation and Response Emergency:***
 - equipment upgraded in Metrological Office and National Emergency Management Office
 - review the arrangements for improving disaster mitigation and response
 - improve enforce of building code
- ***Review of disaster mitigation and response***
 - establishing early warning systems and training in disaster response
 - continuing support to the National Emergency Management office and other disaster response activities
 - implement improved arrangements for disaster mitigation and response to make them more effective
- ***Active operation of Environmental Impact Assessment (EIA) Committee***
 - maintain effective operation of the Environmental Impact Assessment (EIA) Committee
 - environment and Climate Change projects continue implementation

OUTCOME OBJECTIVE 8: Better governance, by adherence to the principles of good governance, accountability, transparency, and rule of law

Lead Ministries: AGO, PMO, TDS, MOPPFS, AO, MOJ, CPR, MCTL, MOFNP

- ***Closer working with Parliament Standing Committee on Finance and Public Accounts to improve public expenditure management and accountability***
- ***Strengthen judicial system with clear operating arrangements between Ministry of Justice, Attorney General's Office, Chief Justices Office, and Lord Chancellors Office***
- ***Mandate of the Audit Office and Internal Audit function of MOFNP-enhanced***
- ***Re-enforcing principles of good governance and transparency:***
 - establish the Good Governance Commission to administer the Anti-corruption Commission and Ombudsman offices
 - developing improved communications strategy, with more transparent publication, e.g. Cabinet decisions, government publications
 - ensure all changes and policies affecting the public service are made available through the PSC's website for all to be aware of
- ***Public Restructure and Reform for a more efficient, effective and affordable public service:***
 - establish new ministries and ensure clear and effective operating links between all ministries and agencies
 - ensure integrated reform continues across government
 - decide on options for implementing an E-government plan to improve delivery of public services and to minimize cost
- ***Implement an enhanced corporate planning process produce the 2013/14 corporate plans:***
 - on a three year rolling basis with clear outputs and indicators
 - provide guidance to budget formulation, improve management, and staff performance
- ***Improving budget and debt management:***
 - further improve budget and debt service management, ensuring Cabinet papers with budgetary implications are screened by MOFNP before they go to Cabinet

- where possible build up cash reserves to provide cover for increasing loan repayments in next few years
 - implement three year rolling MTBF based on enhanced Corporate Plans
 - continue prudent debt management to avoid any further increase in debt burden once the existing loans are fully drawn down.
- ***Revenue reforms for enhanced collection with less distortions:***
 - continue to strengthen tax administration
 - further develop communications with private sector to ensure appropriate tax is collected with minimal disruption to business activity
 - ensure correct implementation of new tax incentives and monitor for any unintended consequences
- ***Implementation of Public Procurement Regulations (2010):***
 - ensure standard bidding documents fully understood and used for open and transparent procurement procedures
 - provide adequate staffing so that procurement system can operate without causing unnecessary delays
- ***Improving data quality and reporting:***
 - review structure and operations on National Statistics Bureau to improve its operations
 - enhance cooperation within Government and with other stakeholders, for improved data collection for better analysis and policy formulation
- ***Improved Coordination and Cooperation with Development Partners:***
 - ensure all agreed reforms in Budget Support Matrix are implemented, and provide the base for negotiations with development partners of future budget support
 - identify long term solution for a sustainable project information management system

OUTCOME OBJECTIVE 9: Safe, secure and stable society, by maintaining law and order

Lead Ministries: AGO, MOJ, MOPPFs, TDS

- ***Developing efficient and effective legal system:***
 - encourage participation in the Law Society for continued professional development
 - sponsored Law Week 2011
 - ongoing consultation and educating the public about Tongan laws
- ***Improved policing:***
 - continuation of Tonga Police Program jointly funded by Government of Tonga, NZAID and Australia Federal of Police
 - establishment of community police stations in several villages of Tongatapu and Vava'u
 - creating and embedding a community policing style with increased visibility and presence
 - educating Tongans on ways to keep themselves and their families safe from crime and road trauma
 - enhance response to emergencies, including search and rescue, and armed incidents
- ***Developing National Security and International Peace keeping:***
 - continuous support of Tonga Defence Services (Australian Defence Fund)

- continue to send TDS staff to Afghanistan, provide training, external earning and good diplomatic relations
- mobilize support for maintenance and operations of Navy vessels

6.3 Summary of 2012/2013 Budget Estimate

6.3.1 Government Financial Statistics (GFS)

The Budget Statement is presented on a GFS basis to meet international standards. GFS presentation combines all Government revenue and expenditure from different sources to ensure comprehensiveness. Expenditure and revenue associated with recurrent Government operations and donor projects are combined (although in-kind grant funding is not included in this GFS format).

Table 9 : Revenue and Expenditure in GFS Format (cash and in-kind loans T\$ millions)

	Actual 2010/2011 (p)	Budget Estimate 2011/2012	Estimated Outturn 2011/2012	Budget Estimate 2012/2013
Total Revenues and Grants	203.8	206.7	215.5	217.8
Total Revenues	151.0	139.3	149.3	149.3
Grants	29.2	39.5	29.2	46.0
Budget Support	23.6	27.9	37.1	22.5
Total Expenditure and Net Lending	261.1	232.1	239.2	216.6
Total Expenditure	249.9	214.4	230.0	216.1
Net lending	11.2	17.7	9.2	0.5
Total Budget Balance	(57.3)	(25.4)	(23.7)	1.2
Total Financing	57.3	25.4	23.7	(1.2)
External financing	65.5	25.4	43.5	(1.2)
Domestic Financing	(8.2)	-	(19.9)	-

Source: Ministry of Finance and National Planning

Total expenditure and net lending⁴ will decrease by \$22.6 million over 2011/2012 outturns. This is driven by falling in total expenditure associated with the China EXIM bank loan, which lead to a decrease in total expenditure by \$13.9 million from \$230.0 million to \$216.1 million in estimated outturn 2011/2012.

Total revenue and grants will increase by \$2.3 million from the 2011/2012 estimated outturn. This increase is driven by increase in grant (which include project grants and budget support) of \$2.2 million⁵. Government tax revenue projected for 2012/2013 will reach \$127.7 million⁶,

⁴ Amount of repayments of on-lent loans from Public Enterprises and Sub-borrowers.

⁵ Ref Table 9 above, pg 41: increase in project grant from 2011-2012 to 2012-2013 = \$16.8m (\$29.2m to \$46m). Decrease in budget support from 2011-2012 to 2012-2013 = \$14.60m. Net increase is \$2.2m (\$16.8m – \$14.6m)

⁶ Ref Table 19, pg 107.

an increase of \$3.1 million compared to the estimated 2011/2012 outturn. Budget support is lower by \$14.6 million compared to the 2011/2012 estimated outturn⁷.

Revised estimate indicates that on a GFS basis Government will generate a total budget deficit of \$23.7 million for 2011/2012 compared to a surplus of \$1.2 million estimated for 2012/2013 Budget. This large turn around is due to the completion of most of the projects associated with China EXIM projects.

In-kind grant⁸ funded projects are not included in the earlier GFS standards. If they were included the net effect would be to increase total grants and total expenditure by the same amount leaving the balance and financing requirements unchanged. In-kind loans⁹, and their expenditure, however, are included since they influence the Total Financing.

Box 1: Government Domestic Payments and Receipts

The Budget Statement is presented on a GFS basis to meet international standards. However, a key interest of government is the total funds under its direct control. Before the introduction of the integrated budget this was referred to as the Recurrent Budget. This treats loan repayments differently to the GFS. Repayment of debt is treated as “expenditure” and drawdown of loans as a “revenue”, while in the GFS these are recorded under financing. Total Government controlled expenditure and revenue is thus better called payments and receipts to avoid confusion with the terms under the GFS.

Government Cash Payments and Receipts

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est. Outturn 2011/12	Budget Estimate 2012/13
Total Payments	177.5	170.9	170.2	179.9
Wages and Salaries	98.8	92.5	92.4	95.9
Purchase of Goods and Service	20.2	19.1	18.5	21.1
Debt Management	25.0	20.9	18.9	23.7
Other	36.5	38.4	40.4	39.2
Total Receipts	185.7	170.9	190.1	179.9
Government Receipts	162.1	143.0	153.0	157.4
Budget Support	23.6	27.9	37.1	22.5

NOTE: Wages and Salaries of \$95.9 million includes all expenditure items under category 10 (Establish Staff Expenses) a total of \$93.4 million and category 11 (Unestablished Staff Expenses) a total of \$2.5 million.

NOTE: Payments include expenditure plus repayment of debt, while Receipts include revenue, budget support and domestic loan drawdowns.

Payments during 2011/12 remained very close to original budget estimates. Receipts exceeded original budget estimates by \$19.2 million, largely due to strong performance in tax revenues and the receipt of budget support from EU which was expected for 2010/11. Total Government payments is expected to increase by \$9.9 million, or 6 percent, during 2012/13 to meet cost pressures in priority areas. Expenditure on wages and salaries, however, will increase by less than 4 percent, reflecting Government commitment to reduce the proportion of payments allocated to payroll expenditure. Government is committed to a balanced cash budget during 2012/13 thus leaving cash balances unchanged.

⁷ Ref Table 19, pg 107.

⁸ Non-cash grant is a contribution or input which can be given a value. E.g. A donor contributes solar energy equipment and TA to the outer-islands of Vava'u.

⁹ Non-cash loan is the amount paid by EXIM bank direct to contractors (CCECC) without going through GoT.

6.3.2 Revenues and Grants

Total project grants (cash) are expected to increase by \$16.8 million¹⁰ from 2011/2012 estimated outturn.

Tax revenue gains come mainly from corporate tax (\$0.4 million) and consumption tax (\$1.6 million) because of improved compliance. In addition, excise tax is estimated to pick up \$0.6 million which reflects the positive outcome of the increase in excise tax on imports tobacco from \$200 to \$210 per 1,000 sticks/kg.

Non-tax revenue is expected to decrease by \$3.8 million mainly from Entrepreneurial & Property Income and Administrative Fees and Charges reflecting the impact of the competition in the telecommunication sectors, as well as loss from Public Enterprises. Declines in telecommunication settlement fees account for the majority of the decrease of revenue estimated to be collected from fees and charges.

Capital revenue is estimated to increase by \$0.7 million from \$1.6 million in 2011/2012 estimated outturn¹¹. This increase is due to increase in other interests.

6.3.3 Expenditure and net lending

The government's overall expenditure and net lending for 2012/2013, on a GFS basis, is made up of total expenditure of \$216.1 million and a net lending of \$0.5 million.

Total Capital expenditure in 2012/2013 will reach \$14.7 million, a decline of \$34.2 million from an estimated outturn of \$48.9 million in 2011/2012. This decline is almost entirely due to falling capital expenditure associated with China EXIM bank loans as for reconstruction of the Nuku'alofa CBD nears completion.

6.3.4 Financing

The overall fiscal balance for 2012/2013 is an estimated surplus of \$1.2 million which will be financed externally due to total external repayments being greater than the remaining drawdown of the China EXIM loan.. Domestically, the government intends to undertake a \$7.5 million in bond issues in 2012/2013 with the purpose of financing a \$7.5 million rollover bonds, scheduled to mature in 2012/2013 but this will have no impact on net financing so domestic financing will be zero.

6.3.5 Focus of Aid Funded Expenditure in Budget

Estimated expenditure from development assistance 2012/2013 is \$152.2 million, of which \$46.0m is cash and \$106.2 million is in-kind, an overall decline of \$21.2m on last year's estimate¹². Major projects coming to completion in 2011/2012 include: completion Vaiola Hospital Reconstruction Phase 2 (Japan, \$19m), Road Improvement projects (PRC, \$32m), Meridian Solar PV Plant (NZ, \$6.3m) and Post Tsunami Recovery Project (World Bank, \$7.0m). More details of completed projects are listed in *Table 10* and *Table 11*.

Major new projects planned to start in 2012/2013 include: Tonga-Fiji Submarine Cable (World Bank, Asian Development Bank (ADB), \$54m), Pacific Aviation Investment Project (World Bank USD \$25m), Vava'u Solar PV Plant (UAE fund, \$4.5m), Nuku'alofa Urban

¹⁰ Table 19, page 107.

¹¹ Table 19, page 107.

¹² Table 19, page 107

Development Sector Project (ADB, \$12m) and Pilot Project on Climate Change Resilience (ADB \$25m). These new projects will in particular contribute to the focus areas of supporting private sector growth and community development.

Section 6.3.5.2 provides more details of the projects planned to start in the Budget and contributing to the theme of “Creating opportunity in Extraordinary Times”.

6.3.5.1 Aid Funded Project Expenditure by Ministry

Table 10 shows the allocation of projects, both historically and looking forward, based on the new by ministry/agency structure. Key changes are:

- **Ministry of Health:** decreased by 78% due to the completion of the Vaiola Hospital Reconstruction Phase 2.
- **Ministry of Finance and National Planning:** declined by 71% due to the final draw down of a soft loan from China in 2011/2012 for reconstruction and roads.
- **Ministry of Public Enterprises:** substantial increase due to the Tonga Forest Products and Tonga Village Network Upgrade Projects.
- **Ministry of Infrastructure:** Integrated Urban Development and Transport Sector Consolidated Projects are near completion and contribute to decline of 3%
- **Ministry of Education and Training (MET):** substantial increase in expenditure related to the existing Tonga Education Support Programme (TESP) (New Zealand and Australia).
- **Prime Minister’s Office (PMO):** increase by 89% due to the Tonga Fibre Optic Cable project
- **The Ministry of Commerce, Tourism, and Labour:** increase 103% due to the Tonga Tourism Support Project (NZAID)

Table 10 : Development Expenditure by Ministry (cash and in-kind T\$ millions)

Ministry Name	Estimated Outturn for 2010-11 (\$m)	Budget Estimate for 2011-12 (\$m)	Estimated Outturn for 2011-12 (\$m)	Budget Estimate 2012-13 (\$m)	Projection for 2013-14 (\$m)	Projection for 2014-15 (\$m)
Attorney General's Office	0.03	0.02	0.00	0.82	-	-
Commissioner of Public Relations	0.01	0.01	0.01	-	-	-
Legislative Assembly	0.13	0.27	0.16	0.65	0.58	0.58
Ministry of Agriculture, Food, Forests & Fisheries	5.91	3.55	0.05	2.10	1.37	-
Ministry of Commerce, Tourism and Labour	0.49	3.54	1.49	7.19	6.21	1.21
Ministry of Education & Training	15.26	14.94	11.00	29.87	30.14	29.15
Ministry of Finance & National Planning	77.44	49.63	60.18	14.60	2.94	2.94
Ministry of Foreign Affairs	0.32	0.05	0.17	0.72	-	-
Ministry of Health	9.59	25.34	22.76	5.52	6.13	0.50
Ministry of Infrastructure	33.44	32.11	9.28	31.18	15.00	10.00
Ministry of Internal Affairs	2.03	0.06	1.44	0.05	0.05	-
Ministry of Justice	0.04	-	-	0.45	0.45	0.45
Ministry of Lands, Environment, Climate Change & Natural Resources	2.23	25.66	11.59	23.35	14.02	7.00
Ministry of Police, Prisons & Fire Services	2.32	3.81	1.62	3.47	0.26	-
Ministry of Public Enterprise	0.39	-	2.53	3.75	0.25	-
Ministry of Revenue Services	1.14	1.00	0.38	1.57	0.57	0.57
Palace Office	0.19	0.20	-	0.70	0.70	0.70
Prime Minister's Office	5.41	12.74	3.51	24.04	15.00	15.00
Public Service Commission	0.32	0.26	0.17	0.66	-	-
Tonga Defence Services	0.76	0.30	1.87	1.60	0.60	0.30
Grand Total	157.44	173.48	128.22	152.28	94.26	68.40

Source: Ministry of Finance and National Planning

6.3.5.2 Aid Funded Project Expenditure by Development Partners

Given our current financial situation, nearly all capital/project expenditure is financed by the kind support of our Development Partners. Government continues to work closely with our development partners to realise opportunities for enhanced donor coordination, harmonisation and alignment with the TSDF as well as local administrative systems and processes. Government appreciates the ongoing support of our partners, which includes much advice and policy support in addition to funding.

Table 11 shows total allocation of aid funded project expenditure by Development Partners. The major changes are:

- World Bank: increase both their cash and in-kind assistance by 7%. Major projects, include Pacific Aviation Investment Program (\$5m), Tonga Energy Roadmap Support (\$7m), Tonga –Fiji Submarine Cable (\$19m) and continued support of the Transport Sector Consolidated Project (\$12m).
- New Zealand: continues assistance through Tonga Tourism Support Project (\$6m), Tonga Village Network upgrade (\$3m), development scholarships (\$3m) and well as the provision of a new High Court Judge among other projects.

- Australia: continues to fund development scholarships (\$3m), Tonga Health Support Program (\$4m), assistance to Climate Change (\$4m) and provisions of technical assistance to line ministries (\$1m) among other projects.
- Pooled funds, New Zealand and Australia: anticipated to increase considerably by 45% due to additional resources for the TESP program (\$10m), TVET (\$1.5m) under MET, and the Tonga Police Development Program (\$3m).
- People's Republic of China: in-kind assistance is expected to decline by 65% due to completion of the major loan funded infrastructure projects at the end of this financial year but continuing support on road maintenance amongst other important economic initiatives. However, new projects are in the pipeline and are likely to be funded through grants.
- Japan: will decline by 45%, mainly due to completion of the Vaiola Hospital and new large projects are being negotiated they are not anticipated to have significant expenditure in 2012/2013. Grassroot Grant Program (\$1.2m) continues to provide assistance to communities and outer islands.
- European Union (EU): increasing their support by 71%, even though they have completed the Stabex programs. The EU are currently funding the Niuatoputapu hospital (\$2m) and assisting the energy sector.
- United Nation Development Program (UNDP): increasing by 102%, including Sustainable Land Management Project (\$0.3m), Millennium Development Goals (\$0.2m), Tonga Post Tsunami Project and the support to the Parliament (\$0.08m).
- UAE Fund for International Development: a new development partner for Tonga and the Pacific Region, is supporting the Vava'u Solar Electrification Project. An encouraging sign that non-traditional development partners are considering Tonga as a country worth supporting.
- The Asian Development Bank continues to support urban planning with the Integrated Urban Planning Development Sector Project (IUDP) nearing completion their level of assistance is maintained in the 2012/13 financial year with the beginning of the Nuku'alofa Urban Sector Development Project (NUDP) \$12m.

Table 11 : Development Expenditure by Development Partner (Cash and in-kind)

Development Partners	Estimated Outturn for 2010-11 (\$m)	Budget Estimate for 2011-12 (\$m)	Estimated Outturn for 2011-12 (\$m)	Budget Estimate for 2012-13 (\$m)	Projection for 2013-14 (\$m)	Projection for 2014-15 (\$m)
Asian Development Bank (ADB)	6.21	23.89	12.05	23.25	12.76	12.28
Australia Defence-Cash	0.34	0.30	0.69	0.60	0.60	0.30
Australia Other	0.09	0.09	0.09	0.04	0.04	0.04
Australia/New Zealand Pooled Fund	8.25	10.11	9.82	14.63	14.92	16.08
Australian Bilateral	10.52	16.71	5.81	14.82	11.03	4.38
Commonwealth Fund Tech Coop	0.07	0.02	-	0.13	0.02	1.00
Commonwealth Local Government Fund	0.01	0.01	-	-	-	-
European Union	8.06	1.47	0.65	2.52	0.52	0.52
Food & Agriculture Organisation (FAO)	-	2.38	-	1.42	1.22	-
Forum Fisheries Agencies (FFA)	0.05	0.10	0.04	0.10	0.10	-
Germany	-	0.70	-	-	-	-
India Fund	0.13	0.04	0.06	-	-	-
International Union for Conservation of Nature (IUCN)	0.02	-	0.12	0.13	-	-
Japan Government/JICA	30.18	20.00	19.05	11.00	10.00	7.00
Japan TTP	1.00	0.46	0.45	1.21	1.20	1.20
Korean Fund	-	-	0.10	0.10	-	-
Local Level Contributions	0.00	-	0.00	-	-	-
New Zealand Bilateral	7.08	13.95	11.14	14.87	10.02	3.37
New Zealand Non-Government	0.01	-	-	-	-	-
NZAID/World Bank Trust Fund	1.10	-	-	-	-	-
Pacific Islands Forum Secretariat (PIFS)	0.10	-	-	-	-	-
Pacific Regional Initiatives for Basic Education (PRIDE)	0.05	0.09	-	-	-	-
People's Republic of China	73.52	40.90	52.57	14.23	5.00	-
Secretariat of the Pacific Community (SPC)	0.55	0.09	0.04	0.25	0.05	-
South Pacific Geoscience Commission (SOPAC)	0.26	0.03	0.68	0.02	-	-
South Pacific Regional Environmental Program (SPREP)	0.21	0.10	0.13	0.20	-	-
Tonga Trust Fund	0.19	0.20	-	1.50	0.70	0.70
Turkey	0.02	-	-	-	-	-
United Kingdom Government	0.01	0.01	1.21	0.82	-	-
UN Family Planning Association (UNFPA)	0.14	0.01	0.09	0.01	-	-
UN International Children's Fund	0.03	-	0.01	-	-	-
UNESCO	0.95	-	0.35	0.07	-	-
Unidentified Donor	0.50	0.00	0.28	-	-	-
United Arab Emirates	-	-	0.55	4.50	-	-
United National Development Program (UNDP)	0.69	0.48	0.35	0.97	0.04	0.04
United Nations Environment Program	0.10	0.03	0.06	0.04	-	-
World Bank/International Development Agency (IDA)	5.70	41.32	11.06	44.37	25.54	21.00
World Health Organization (WHO)	1.29	-	0.74	0.50	0.50	0.50
Grand Total	157.44	173.48	128.22	152.28	94.26	68.40

Source: Ministry of Finance and National Planning

6.3.5.3 Budget Support

This modality is consistent with the emphasis on country ownership, systems and capacity, key elements of the Paris Declaration. It also enables a focus on overall progress and direction rather than on individual project results and contributes to longer term sustainable development.

Development partners continue to appreciate the financial challenges facing Tonga and continue to provide budget support to avoid reduction in delivery of key services; although the total budget support is decreasing from \$27.9m to \$22.5m between 2011/2012 and 2012/2013.

This support is provided in recognition that Government has demonstrated its preparedness to deliver a Government determined reform programme to improve the public service. Government is pleased that in 2011/2012 budget support was disbursed for the first time based on reduced number of policy actions and more coordinated approach. Government has developed with development partners a budget support “one policy matrix” to which all development partners can link their budget support.

The focal areas of reform work undertaken under this policy matrix for 2011/2012 and to continue in 2012/2013 are important parts of governments wider reform programme, they include:

1. Strengthening Public Financial Management (PFM) Building Blocks
2. Strengthening Fiscal Policy
3. Promoting Structural Reform
4. Improving Social Protection

Over time Government wishes to reduce its fiscal gap and therefore need for budget support to cover recurrent expenditure, but in the meantime Government appreciates the flexibility of development partners in providing this support.

Government also continues to welcome the opportunity to engage with development partners on activities and policy actions to encourage Development Partners to adapt an incremental and holistic approach that emphasises institutional and sectoral capacity development.

7 CONCLUSION

The government, over a short period of time, has achieved a lot in implementing its vision as stipulated under its Tonga Strategic Development Framework. Much is needed however, in term of time and resources, to consummate many of the policy initiatives that have yet to be started or to be completed. Government is therefore committing to continuing to fulfil its responsibilities in the 2012/2013 budget, and beyond.

Looking forward, the international outlook remains uncertain and will continue to place limits on government finances and income opportunities for our people. This makes it even more important that we work closely together, and with our development partners, to focus on the key areas to create an even more efficient, effective and affordable public sector; to enhance the environment for private businesses across the Kingdom; and to address key health and education constraints that impede the development of our people, and to ensure that the best is harvested out of the opportunities available to us.

Despite the difficult situations we have faced, it is with pleasure that I recommend this Budget for the consideration of Parliament. We have worked hard to take account of the many challenges we face, our tight financial situation and the real needs and aspirations of our people in these ‘extraordinary times’. Under these conditions, it is not possible to craft a Budget that will be fully acceptable to everyone, however, we believe that this Budget goes a long way to balancing the expectations of our people with the realities of the world conditions that we face. As part of improving our transparency, government is publishing the Budget as approved by Cabinet, so the people can fully appreciate any amendments that are made by Parliament. We are also providing draft copies earlier to Parliament Standing Committee on Finance and Public Accounts to help the members to have more time for well informed deliberations.

We trust that this will be a Budget that helps “*Create Opportunity in Extraordinary Times*” working in close partnership between the government and the people of Tonga, as well as with others who kindly join us in partnership.

Hon. Lisiate ‘Aloveita ‘Akolo
Minister for Finance and National Planning

ANNEX I: TSDF REVIEW

ANNUAL REVIEW OF TONGA STRATEGIC DEVELOPMENT FRAMEWORK (TSDF) 2011- 2014

Progress During 2011

January 2012

MINISTRY OF FINANCE AND NATIONAL PLANNING

1 Executive Summary and Focus Areas

The new government has developed a clear Vision supported by the nine (9) Outcome Objectives and four (4) Enabling Themes, with respective strategies, in the TSDF. This is providing the guiding basis for governments various endeavours.

On taking office it was clear that the new government faced a number of constraints to the effective implementation of the TSDF, including:

- a weak world economy;
- inappropriate structure and scope of government;
- lack of adequate systems including the need for better planning, budgeting, monitoring and evaluation;
- weakness in capacity including the need for better management and focus on staff performance, in addition to various technical skills;
- failure to adequately prioritize resulting in doing a lot poorly rather than enough well;
- a very tight financial situation, made worse by recent heavy borrowing which is placing extra stress on the budget;
- weak private sector in need of a more supportive business environment;
- development funding too heavily focused on Nuku'alofa.

These, and other constraints, have developed over time so it will take time to address them. While this report suffers a little from the weaknesses noted above, it outlines a wide range of initiatives that government has supported over the past year, 2011, to help both improve delivery in the short term, while addressing these longer term constraints which must be addressed if we are to have a more efficient, effective and affordable public service.

During 2011, Tonga has continued to face an uncertain external economic climate. Remittances have continued to fall. Tourism receipts fell after the global crisis, but have recovered since then, but tourist arrivals has declined, exports, despite some limited short recovery, remain very low. Government has been successful in negotiating direct budget support and is on track to receive the total anticipated by the end of the fiscal year. Government revenue and funded expenditure remain on track by carefully limiting funding for any new activities not in the budget. This overall restrictive environment continues to place severe limits on how rapidly government can pursue its Vision and objectives and thus reflects the limitation to progress in many areas.

Despite these constraints, government has been successful in mobilizing substantial increase in grant funding for budget support, as well as projects, from our development partners. This support is recognized and appreciated. As a result, significant projects have been implemented or are in the design phase over all the nine outcome objectives. The new approach to government is being embedded, and major progress has been made in putting in place the restructuring and reform of the public service required for our new political reality and the delivery of our Vision.

1.1 Focus areas in 2012/2013

This review confirms that the range of issues in the TSDF remains valid and a good guide to the challenges facing government and the Kingdom, however, it is also clear that a few of these constraints are the most significant and additional focus is required to address them in the near term. The areas for intense focus in 2012/2013 are detailed below:

1. **Government restructuring and reform for a more performance oriented service by:**
 - a. Completing the restructuring of government in the 2011/2012 financial year
 - b. Continue to improve transparency and accountability of government
 - c. Continuing with the enhancement of corporate plans that set clear outputs that are attainable within our available resources
 - d. Developing sector and district planning to improve management and delivery of projects
 - e. Developing a medium term budget framework to improve financial planning
 - f. Improving staff performance monitoring with a focus on improved management and delivery
 - g. Improving overall monitoring and evaluation of progress to allow better tracking of progress and for future planning and budgeting.
2. **Enabling environment for a successful private sector by:**
 - a. Continuing to address the government imposed constraints to private sector operations while maintaining appropriate controls on business activities to protect consumers and ensure sound business practices.
 - b. Fully establishing a sound mechanism for open dialogue between the private sector and government that will help identify other constraints and find viable options for addressing them.
3. **Encouraging a healthy and productive population by:**
 - a. Improving access to basic health and education services where possible.
 - b. Addressing more effectively the increasing threat of non-communicable diseases which are killing increasing numbers of people in their prime.
 - c. Addressing the decline in literacy and numeracy among school children.
 - d. Focusing skills training on the needs of the domestic private sector as well as to make use of overseas employment opportunities.
4. **Ensure inclusive community development where the benefits of development are widely shared by:**
 - a. Ensuring government investment in key infrastructure on outer islands and rural areas (water supplies, roads, wharfs, drainage)
 - b. Seeking options for improved communications and transport services to all parts of the country
 - c. Developing programs to protect the more vulnerable and isolated groups and individuals
 - d. Improving the quality and delivery of local government

2 Introduction

During 2011, the first fully elected government reviewed the existing national strategic framework and updated it to take account of the new demands facing this new administration. This resulted in the Tonga Strategic Development Framework (TSDF) which contains nine (9) high level Outcomes Objectives, with associated strategies, and four (4) Enabling Themes with strategies to help deliver these outcomes.

The TSDF was substantially completed early in the year, but to due to reviews was not formally approved until July 20, 2011. This review, however, is based on developments over the whole year. A series of interviews were held with most ministries to collect more detailed information on key achievements/successes and constraints/difficulties, and where possible identify some gaps in need of urgent attention. There were also nationwide consultations throughout the Kingdom held during January and February 2012 aiming to keep the communities informed of what had been achieved during the first year of TSDF and to increase public awareness on the national development's vision, outcome objectives, enabling themes and TSDF's linkages to MDGs, Sectoral/ Outer Islands Master Plans, and other related development plans. There were a number of issues raised during the consultations and the main issues raised by islands were summarized in *Appendix 2*. Majority of the main issues raised were already covered in the government and development partners' existing program.

The first key constraint that became clear is that lack of clear and realistic targets/indicators had anticipated in Chapter 2: 'Monitoring Matrix' to use as an overall effective monitoring and evaluation process for gathering such information. As already recognized, Ministry Annual Reports are based on different periods (calendar year) to the Corporate Plans and Budgets (fiscal year). There is also limited linkage back to the TSDF outcomes. As part of the reform program, it has been agreed that the Annual Reports will now be aligned with the same period as the enhanced Corporate Plans and Budget so that they can directly report on progress against Corporate Plan indicators. Other improvements are also planned for monitoring of progress against the TSDF and the sector/district plans which will make future reports, such as this, much more timely and comprehensive.

To help fill the gaps in the information received directly from the ministries, other sources have been used to fill out this report as much as possible.

Tonga has continued to face an uncertain external economic climate. Remittances have continued to fall, Tourism receipts fell after the global crisis, but have recovered since then, but tourist arrivals have declined, exports, despite some limited short recovery, remain very low. Government has been successful in negotiating direct budget support and is on track to receive the total anticipated by the end of the fiscal year. Government revenue and funded expenditure remain on track by carefully limiting funding for any new activities not in the budget. This overall restrictive environment continues to place severe limits on how rapidly government can pursue its Vision and Objectives and thus reflects the limitation to progress in many areas.

Despite these constraints, government has been successful in mobilizing substantial increase in grant funding for budget support, as well as projects, from our development partners. This support is recognized and appreciated. As a result, significant projects have been implemented or are in the design phase over all the nine outcome objectives. The new approach to government is being embedded, and major progress has been made in putting in place the restructuring and reform of the public service required for our new political reality and the delivery of our Vision.

3 Review of Progress

3.1 Review against the TSDF 9 Outcome Objectives (OOBJ)

The following sections summarize the key achievements and challenges under each of the nine Outcome Objectives of TSDF.

OOBJ1: Strong inclusive communities, by engaging districts/villages/communities in meeting their prioritized service needs and ensuring the prioritized and equitable distribution of development benefits

Key achievements/successes

- *Constituency Grant - \$1.7 m* – Government allocated in its 2011/2012 Budget \$1.7m to be shared among the 17 constituencies of Tonga to assist with their respective community development activities, particularly, in urgent areas where alternative funding was not available. It is up to each constituency, through their respective Member of Parliament (MP), to decide what projects or activities to be utilized from their share of the fund, however once decided, accountability is ensured by all invoices being submitted through their MPs to the Hon Minister for Finance & National Planning to endorse for payment.
- Various donors' projects for community development including the World Bank Community Driven project (US\$3m) and the ADB/Japan Vulnerable assistance scheme (US\$900k). Currently, work in progress is underway for the implementation.
- Japan continues to provide assistance to villages and outer islands mainly with their water supplies. New Zealand provides support with Mainstreaming of Regional Development Initiatives (MORDI) towards community plans and rural development such as jetties/wharfs.
- Government allocated \$100,000 from its budget under the MOFNP votes to provide continued assistance to various Non-Government Organizations (NGOs) and Civil Society Organization (CSOs) & Vulnerable groups such as the Tonga Red Cross, Alonga, Women and Children Centres for their recurrent costs and operations. To date, approx \$80,000 have been disbursed so far. A one off contribution of more than \$700,000 to the Tonga Rugby team for the preparation of the 'Ikale Tahi Rugby team for the 2011 Rugby World Cup. Outer islands development committees (namely Vava'u, Ha'apai, 'Eua, and Niua) are well established and operating during the year. They are mandated to plan the development of their respective districts and assist in managing the development activities/projects under each district. Currently, almost each district has a master plan although reviews of these plans are required (except for the 'Eua Master Plan reviewed last year) to reflect the priority needs for these islands. Some of the main development projects currently underway included the Ha'apai Foa Causeway project, Niu'ui hospital foreshore protection, the Vaipua Bridge, the 'Eua Runway airport, 'Eua ferry proposal, and the tsunami recovery project in Niua.
- Government pays for street lights costs for the whole of Tonga and provides subsidies to the Ferry and Air services to the Niua.
- The National Emergency Fund has been established to reserve funds for time of disaster. The fund has helped the delivering of food to Ha'apai people after the Tropical Cyclone Wilma

- The Government Administration in the outer islands is being centralized to starting with Human Resources and Finance. This is to ensure more effective government that deliver services to the people and support the development of these outer-islands.
- Completion of the first Five (5) year National Population Census and able to identify update issues from census on rural urban migration.
- Community outreach programs carried out by the Women Affairs and Culture unit cooperate with the Langa Fonua Association and culture unit in the Palace Office and other private organizations work together for communities; they arrange funding requests through investors which helps in daily operation including the outer islands.
- The Cabinet approved to establish a National Centre for Culture and the Cultural Mapping Policy is completed and is now seeking funds for public consultations.
- The Gender policy has been completed and approved by the Cabinet and now continue deliberation with the SPC regarding equity of women and men in workforce.
- Work is on-going on the Convention on the Elimination of all forms of Discrimination Against Women (CEDAW) – related to land regulation.
- Continuous support for elderly & vulnerable groups provided by the Latter Day Saints Church in partnership with the Ministry of Health.

Key constraints/difficulties

- Need District Plans for Tongatapu and clear links between district and sector plans.
- Need more focused attention from Central Government to outer islands.
- Funding constraints.

Gaps and Urgency for addressing

- Need for more coordination of work closely with the People's Representatives to Parliament, district/town officers, related government agencies and all members of the society.

<p>OOBJ 2: Dynamic public and private sector partnership as the engine of growth, by promoting better collaboration between government and business, appropriate incentives, and streamlining of rules and regulations.</p>
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Key achievements/successes

- Modification to the Customs tariff and excise tax rates and exemptions to regularize rates and provide incentives to the private sectors, businesses and local manufactures, including:
 - Imposing a 3% duty rate on all capital items exempted in 2009; it is expected that this will be reviewed soon, to consider zero rate duty for major development projects
 - Increasing the excise tax rate of imported tobacco from \$200 per kilo/1000 sticks to \$210
 - Increasing the excise tax rate of all imported beer from \$42 per lal to \$50 while decreasing the tax rate of all locally manufactured beer from \$17.85 per lal to \$10 per lal;
 - Imposing 3% duty on all electronic equipment; this will be reviewed to consider zero rate for education and other development purposes, and
 - Reducing to zero the duty rate of infant milk and all plastic bags imported for export of local produce.
- Cabinet's approved the '*Business Licence Reform Roadmap*', which aims to undertake additional reforms to enhance the business regulatory environment. MLCI has started streamlining licences through the following amendments to the business licences.

- Longer term licence (even the option of indefinite licence with new administration provisions and stipulated conditions for termination, national interests and public safeguards), electronic and online application process and registry, electronic payment system etc.
- Amendment to the Foreign Investment Act including review of the reserve/ restricted lists, electronic and online application process, and also considers the merit of connecting business visa issuance to be more efficient.
- Ministry's internal restructure to prioritize ease of doing business (Reduce issuance of licence from 7 working days to only 1 day), and consolidate inspectorate of business compliance, enforcement of statutory administration to ensure satisfactory protection of public health and safety.
- Tourism – assistance including NZAID (\$1.3m) and World Bank (\$1.8m), Government (\$1.2m) to develop Tourism industry including local/individual operators. Main activities include the tourism for community development (NZAID funding), improve product/brand development (marketing), conducting of the accreditation program for accommodative operators and review of the Tourism Act.
- MAFFF re-established treatment plants for agriculture exports, as well as focusing on community based development.
- MAFFF continuous effort in collaboration with the private sector to deal with the issue of 'markets (both domestic & international)', promoting exports of both agricultural production and fish. Further, the effort to discuss and consider possible ways in dealing with the financial institutions such as the Tonga Development Bank to assist farmers at the grassroots level and small businesses to gain access to loan at very low interest rate.
- Pursuing options for energy savings through more efficient energy usage and alternative energy such testing viability for re-establishing coconut oil for diesel production on outer islands.
- Recognizing the continued role of fossil fuels for some time, exploring various options for reducing cost of petroleum imported to Tonga, drawing on successful lessons from experience in Samoa and elsewhere.
- Grant JAWS 12 months exclusive and sole right to ship cargo and freight directly between New Zealand and the Vava'u and Ha'apai island groups, and provide support facilities on island, with the intention to promote exports from these islands on a much cheaper costs. Unfortunately, JAWS service was withdrawn after a few weeks due to objection to the exclusive right arrangement.
- Updated reports on Private Sector Assessment, and Revenue Collection to help identify areas that need addressing, both set up in monitoring frameworks for tracking how these issues are being addressed
- Re-established meetings with Tonga Chamber of Commerce & Industries (TCCI) and other private sector business associations to help improve dialogue with the private sector, options under consideration on how to widen this dialogue, including regular links to the Macro Technical Committee which now focuses also on promoting growth.
- Established the Cabinet Economic Development Committee (CEDC) of Ministers covering economic sectors, with advice from the Macro Technical Committee, to focus on addressing key policy issues constraining growth.
- National Retirement Benefit Fund was established and currently carries out process to be able to be in full operation by 1 July 2012.
- Starting the process for the establishment of the Tonga Tourist Authority expected to be in operation in the second half of 2012.

Key constraints/difficulties

- The operations of the National Economic Development Committee have been dormant needing to identify suitable alternatives.
- Issues identified from the recent studies and reports on private sector business need to be better understood and addressed.
- No clear direction for addressing the decline of the local fishing industry.
- Need to ensure that the merger of MLCI and Ministry of Tourism helps the streamlining of licensing while ensuring that the conversion of the TVB to a marketing authority efficiently executed.
- Delay in establishing a more definitive arrangement over the management of the new cruise ship wharf (Vuna Wharf) limiting the effective use of this new infrastructure; marketing for the wharf takes two (2) to three (3) years but cruise ships have already planned routes this far in advance.
- Failure in various attempts to establish an international airport route to Vava'u which could greatly increase tourism numbers, by promoting a direct route from Nadi.
- The need for the International Dateline Hotel needs to be managed by a reputable hotel chain in order to bring in greater number of tourists.
- Most of the development in accommodation is of a small scale at the moment.
- The tourism survey at the airport delivered different results from the banks' estimates; total tourist receipts of \$58m in 2010 make tracking of contributions difficult.
- High interest rates mean that businesses are not keen to borrow more to expand their businesses; banks continue to apply tight lending policy while rehabilitating loans portfolios.
- Some concerns about higher focus on social sectors/outcomes, and not on economic development; which is needed to generate the local revenue to drive achievement of outcomes in the social sector. There is need to balance competing demand.
- Different opinions about whether the private sector has the drive and initiative in order to be self propelling, and the extent to which government should take the direct lead in supporting some bigger developments to help the private sector get more fully established, and then government can step back.
- Concerns about maintaining a viable air service within Tonga, what should be the balance between working more closely with the existing private sector (Chatham's and/or Air Pacific) and the setting up of the new government airline to safeguard industry from monopolistic control and to provide competition for cheaper airfares.
- Needs stronger enforcement of the Procurement Process to ensure transparency on public bidding.

Gaps and urgency for addressing

- Need to focus more on supporting the development of a dynamic partnership *to avoid engine from sputtering*.
- Need to ensure support to expansion of tourism.
- Need to support agriculture including overseas marketing of agricultural produce and explore other options to reactivate fisheries industry.

OOBJ 3: Appropriate, well planned and maintained infrastructure that improves the everyday lives of the people and lowers the cost of business, by the adequate funding and implementation of the National Infrastructure Investment Plan

Key achievements/successes

- Major reconstruction works included the constructions of the CBD, Vuna wharf, 'Eua airport and other construction projects in the outer islands as covered in the Outcome Objective 1 above.
- Tonga Transport project on Tongatapu and outer island, Urban redevelopment of Nuku'alofa continues
- Roads repair works from both donor and government funds
- Started work on the Tonga Cable project to provide more rapid link between Tonga and the rest of the world, will facilitate e-government plan
- Maintenance of school buildings, 35 schools (primary & secondary) were renovating in the last support program from World Bank. 53 schools identified to be renovated funded by Australia & NZ. It should be completed by June 2012.
- A3Z replaced the aerial tower after 50 years, under a T\$1 million project based on universal access background funded by Korea.
- Service suppliers are now required to provide universal access by providing mobile services to the outer islands. Right now, only the TCC serves the two Niuas. Identifying options for providing the internet connection and services of Digicel Company to the two Niuas is underway.
- Enforcement of private operators to meet infrastructure and regulatory issues, such as certifying new equipments; e.g radio in maritime and aviation
- Improving Building Control capacity to ensure compliance to the building codes.

Key constraints/difficulties

Heavy infrastructure investment, accompanying heavy borrowing, activating vibrant economic activities, but likely to fall off due to completion of the major infrastructural constructions works

- Major infrastructural investment heavily focused in Nuku'alofa, and much of the GDP activity construction works shared with foreign companies and workers.
- Appearing lack of capacity for ongoing maintenance especially of newly built building structures
- Delay in reviewing and updating the National Infrastructure Investment Plan, with the view of funding capital for implementation of priority projects, especially those that support employment and other economic development activities.

Gaps and urgency for addressing

- Need to focus more on funds to establish high priority projects , and ensure that international safety obligations are met to avoid restriction on delivers of transport services
- Need to improve maintenance plan and its implementation
- Need to ensure proper standards in construction and good use of infrastructure eg. cruise ship facilities for new wharf in Nuku'alofa

OOBJ 4: Sound education standards, by emphasizing quality universal basic education
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Key achievements/successes

- Major achievements from TESP and ongoing focus on the three main key result areas; (i) Student Outcome (ii) Improvement of Learning Environment and (iii) Teacher Proficiency, including the following activities
- All curriculums for classes 1-8 (class 1 in primary school to form 2 in secondary school) have been completely revised and implemented; this was funded by NZ & Australia.
- Improving sound education standards for universal education, has started on classes 1-8, and Form 3-7 will start in 2012.
- School Based Management Team training principals & the PTA on how to manage and mind their funds, under Australian and NZ funded project.
- Currently drafting policy & regulation to submit in 2012 together with the revised Education Act phase 2.
- Cuba Scholarship continues to be offered.

Key constraints/difficulties

- New analysis shows that literacy and numeracy is lower than estimated before.

Gaps and urgency for addressing

- Improvement on basic literacy and numeracy

OOBJ 5: Appropriately skilled workforce to meet the available opportunities in Tonga and overseas, by delivering of improve Technical and Vocational Education & Training (TVET)

Key achievements/successes

- There were various TVET programs and projects continued during the year which provided technical skills to youths and general public. Financial assistance from government to non-government technical institutes was also paid during the year via grants from New Zealand and Australia.
- Seasonal Work Employment schemes with New Zealand and Australia continued during the year providing significant benefits to many families in Tonga. Similar work scheme opportunities are being explored for the USA.
- Cabinet approved to establish the Tonga Institute of Sports for further development of the sport talents of Tongan youths and people.
- There were various employment training programs carried out during the year especially at community level both in Tongatapu and the outer islands.
- Regulations for TVET, Early Childhood Development ECD & Disability (Inclusive Education – regardless your physical condition you will have an opportunity to study) are being drafted for submission to Parliament in 2012.
- Government ministries provided opportunity for students in technical institutes to attach to them on short term on-the-job training
- Selected technical training provided to prisoners to improve their skills especially to better prepare them for re-joining the community after serving their sentence.

Key constraints/difficulties

- Impact of large number of seasonal workers going overseas on domestic business consistent supply of labor
- Poor record of absconding workers that threatens the future of the program.
- Lack of Skills: Need recruitment of skilled technical officers to train prisoners on appropriate technical skill to strengthen the local workforce when they re-join the community.

Gaps and urgency for addressing

- Need to strike a balance in supply of labor between overseas work schemes and domestic business

<p>OOBJ 6: Improved health of the people, by promoting healthy lifestyle choices with particular focus on addressing non-communicable diseases, and providing quality, effective and sustainable health services</p>

Key achievements/successes

- The Tonga Health program continued operation during the year and funded partially from government.
- Health Statistics are well monitored with improved health indicators to help identify focus areas in health delivery
- Addressing the issue of non-communicable diseases (NCDs) by currently implementing a program on healthy & balance diet in schools, and including it in schools' curriculum, as part of a wider program of advocating and addressing the serious threat from NCDs
- In March 2012, the final phase of the Vaiola hospital infrastructure was completed according to the original plan with Japanese funding.
- Modern health centers have been established and funded by China for towns of Vaini, Mu'a, Nukunuku, Kolonga and Houma, and health centers also established in 'Eua funded by Japan (JICA).
- Australia is funding a 10-year project for improvement of health centers, standardizing the services provided in all regions, and promote NCDs in these health centers. They also fund the training of staff like NCDs nurses, and provide supplies for the health centers.
- Increasing number of visits from overseas health partners conducting free public health services.

Key constraints/difficulties

- NCDs are very serious problem consuming large public fund resources.
- Need to better access and use available funding.
- Outer islands seem to have been neglected and isolated from enjoying the same health services and opportunities in Tongatapu.
- Health managers are mostly technical but need administrative and managerial support.
- Need to have more focus on putting more resources into the implementation of policy process.

Gaps and urgency for addressing

- Need wider commitment addressing NCDs which are striking down many people in mid-life when they are productive and have much to contribute to the society.

OOBJ 7: Cultural awareness, environmental sustainability, disaster risk management and climate change adaptation, integrated into all planning and implementation of programmes, by establishing and adhering to appropriate procedures and consultation mechanisms.

Key achievements/successes

- The existence of the National Culture Committee being chaired by Lord Vaea. Cultural Awareness for the preservation of our cultural benefits is being promoted in collaboration with a Korean institution helps to train staff.
- The Environmental Impact Assessment (EIA) Committee was active during the year in ensuring that all infrastructural projects have proper environmental impact assessment. This is an on-going task.
- There were many environment and climate change projects carried out during the year, including the securing of the Pilot Project on Climate Change Resilience, worth USD \$15m.
- The Ministry of Works continues to enforce the building code to ensure that all buildings are safe, and able to withstand natural disasters.
- The arrangements for improving disaster mitigation and response are being reviewed to make them more effective.
- The allocation of fund ex-2012/13 Budget for the establishment of a standalone Climate Change Division within the Ministry of Lands, Survey & Natural Resources.

Key constraints/difficulties

- Detailed planning weak, National Infrastructure Investment Plan (NIIP) needs update, CP is generic, limited tracking of sector plans, below-average project tracking, M&E weak
- District planning started on outer islands - but how much are these issues included?

Gaps and urgency for addressing

- Need significant strengthening of Corporate Plans to guide ministries, linked into Sector and Outer Islands Master Plans with participation of appropriate stakeholders.
- Need to establish M&E and reporting.
- Need to improve all related systems.
- The above will make it easier to integrate the various other factors into plans.

OOBJ 8: Better Governance, by adopting the qualities of good governance, accountability, transparency, anti-corruption, security and rule of law

Key achievements/successes

- The establishment of the Parliament Standing Committee on Finance and Public Accounts has been vital. The government continues to support the work of this committee by providing requested information.
- Appointment of the Interim Attorney General and Interim Lord Chancellor as part of the reform process in the judicial system.
- Government requested Parliament to review the operation of the Nuku'alofa Development Council (NDC) and special investigative work was conducted during the year.
- The Audit Office carried out investigative reports on certain issues that warranted audit investigation regarding the usage of public funds and resources.

- Implementation of the Government of Tonga (GoT) *Public Procurement Regulations* (2010) during 2011 and the introduction across the Ministries of the *Standard Bidding Documents under the Public Procurement Regulations* for consistent fair and transparent procurement procedure.
- The progress of government restructuring and public sector reforms programs are reported under the enabling themes.
- E-government plan being developed to improve service delivery and reduce cost.
- Cabinet approved to release Cabinet decision of public interest to ensure transparency.
- Government approved to establish a Good Governance Commission to administer the Anti-Corruption Act and Public Relations Act, and to be effective by the second half of 2012 after the amendment to the above said Acts are considered by Parliament).
- Government to post its monthly budgetary support on the website within 40 days from the end of the month. This is to widen transparency on public fund.

Key constraints/difficulties

- Constant follow up on embedding political reforms.
- Merging of involved Ministries will put a challenge on the budget process.
- Limited resources.

Gaps and urgency for addressing

- Need to continue and enhance focus on keeping the reform program on track and address corruption and other issues that would threaten good governance.
- Stronger focus needed on efficient, effective and affordable spending of public fund.
- Stronger focus needed on early planning so that implementation of projects has a higher probability of success.
- Need greater recognition of accountability and commitment to procedures outlined under the Government Procurement Regulations.

<p>O OBJ 9: Safe, secure and stable society, by maintaining law and order</p>
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Key achievements/successes

- Community policing
- Encourage participation in the Law Society for continued professional development.
- Joint police committee called the No Pro Violence.
- Re-design the Stable Society's vision to what is called "TAMASI'I MA'A TONGA & FAIAKO MA'A TONGA" (basically when Form 6 & 7 students finish school).
- Maintain security level of prisoners.
- Maintain low rate of prison escapes (4 prisoners escape in 2011).
- Reduce prisoners' crime rate inside the prison.

Key constraints/difficulties

- Increase in crime

Gaps and urgency for addressing

- Need for more focused approach to address increased pressures from urban migration, increasing crime and general changing social conditions.

3.2 Review against the TSDF 4 Enabling Themes

The following sections summarize the key achievements and challenges under each of the four Enabling Themes of TSDF.

Enabling Theme 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*

Key achievements/successes

- Establishment of a Working Group and carrying out government restructuring and reforms for a more efficient, effective and affordable public service:
- Rationalizing the number of ministries in line with the 12 members of Cabinet under the new constitution for implementation in 2012/2013 budget
- Helping to streamline operations of ministries
- Putting in place and guiding a longer term reform process including, enhanced corporate planning, medium term budget framework and improve staff performance management.
- PSC reforms programs continued during the year.

Key constraints/difficulties

- Finding time to fit the reform into existing work load.

Gaps and urgency for addressing

- Achievement of expected outcomes from the government's restructuring reform.
- Improving public service to get the outcomes provided and expected under the TSDF.

Enabling Theme B: *Improving the macro-economic environment and fiscal management, including effective revenue services to ensure a level playing field and those services to the people can be appropriately funded*

Key achievements/successes

- Improved monitoring of macro-economic status of economy and key developments, reported monthly to Cabinet under the heading "Economy At a Glance".
- Regular Budget reporting to Cabinet and ministries to help improve budget implementation and limiting introduction of additional activities for which funding is not available, as part of overall improvement in financial management, resulting in targets for revenue collection and expenditure up to December 2011 being met.
- Review of revenue services completed identifying a range of administrative reforms that needed to be undertaken for a more efficient service that is more responsive and less disruptive to the operations of the private sector.
- Established Tax Policy Committee to review policy and supervise recommendations from review of revenue services
- Established project for Medium Term Budget Framework based on enhanced Corporate Planning.
- Continued prudent debt management and avoiding further increase in debt burden once the existing loans are fully drawn down.
- Reviewed rate of Raw Materials & Packaging for local manufacturers.
- Radio Programme introduced during the year to improve communications about tax matters.
- Since September, the Ministry of Revenue Services (MRS) has had successful monthly meetings with brokers to sort out concerning customers issues.

- Compliance Enforcement Plan put in place for timely payment of tax, and to follow up on tax arrears.

Key constraints/difficulties

- Consistency on Application and strict enforcement of rules on customs, tariffs and duties required.
- Consumption Tax and its refund is a concern to private businesses, and being alleged as a major constraint on management of businesses.
- Duties and excise taxes on import of raw materials/packaging materials for local manufacturing of products need to be reviewed.
- Need for improved IT System for RMS (Revenue Management System) & CMS (Custom Management System).
- Need assistance in processing of returns (either tax or custom) to be able to do the comparison, capture data and no undervalue of goods; with the aim of consistency in applying tax charges.
- A need to monitor the performance of tax agents, brokers and other tax service providers.

Gaps and urgency for addressing

- Need to ensure transparent and sensitive system that collects required revenue while avoiding damage to the profitability of private sector businesses.

<p><u>Enabling Theme C: Ensuring Public Enterprises are sustainable and accountable, and where appropriate moved into the private sector</u></p>

Key achievements/successes

- Reform of a number of Public Enterprise businesses and statutory boards to improve their efficiency.
- Government commissioned a review of the performance of the Tonga Development Bank (TDB) and its policy/mandate, and how to better assist farmers and other small medium enterprises.
- Reform of Tonga Timber to make better use of the forest in 'Eua and generate employment on the island.
- Divestment of interests and ownership of the International Dateline Hotel and the selling of the Sea Star.
- Preparing Tonga Print for privatization.

Key constraints/difficulties

- Limited management and technical skills in the PEs, and limited number of skilled staff in MPE
- Uncertainty remains about the role of PEs in and the balance between providing a cost effective service to the public and generating profits for delivery of public services.

Gaps and urgency for addressing

- Be clear on the role of PEs and striking a balance between providing cost effective goods and services to consumers, and securing sound return on investment for government.

Enabling Theme D: Ensuring a more coordinated whole of government approach in Tonga's partnership with development partners
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Key achievements/successes

- Established sound relations and Joint Matrix for Budget Support with development partners, – seen as a leading example in the region.
- Good Tonga Development Partner Coordination Meetings.
- Working on improving project database.
- Making sure there's a close collaboration & partnership with new development partners e.g. United Arab Emirate, Brazil.
- Access to US democracy fund (MOFNP) : only NGOs and Civil Society.

Key constraints/difficulties

- Need to strengthen staff and systems in Aid Management.
- Coordination of all development partners for maximum benefits.
- Consistency in discussions and negotiations with development partners on extension, and new developmental projects.
- Inadequate database for tracking projects from planning phase to implementation and completion stages.

Gaps and urgency for addressing

- Need to ensure that all donors' grant and funded projects are in line with national development priorities and demand driven.
- Ensure effective project data base for improved tracking and monitoring of projects from planning, through implementation, as part of more comprehensive monitoring and evaluation system.

Attachment 1 - Relationship between TSDF and other Plans

The following diagram shows the desired relationship between the high level TSDF and the other planning and budgeting activities. The extent to which detailed planning at the sector/district level may be required depends on a variety of factors. They can play an important role between the high level TSDF, and the detailed plans of government ministries and the private sector. At the same time, care is needed to avoid having too much planning getting in the way of implementation.

Currently there is a well articulated TSDF setting the overall direction of government. The other parts of the planning system are in varying stages of development. A few sector plans exist but without any integrated approach to how they are developed. District Plans (formally called Regional Plans but the name changed to take account of the needs of Tongatapu and to avoid confusion with the Pacific region) exist for the four main outer island groups of 'Niuas, Vava'u, Ha'apai, and 'Eua. No District Plans are currently in place for Tongatapu. There is no clear link between the existing Sector and District Plans – this matters since at the project level, sector and district is just two different ways of grouping projects. This raises the importance of a project management information system which tracks all the projects no matter which plans they are in.

During this review exercise it became clear that further work is needed to clarify how this system may work effectively in Tonga.

At *national level*, TSDF outlines the overall direction the Government wishes to go as per the national vision. It is based on the elected government's development priorities to address its mandate from the electorate.

At the *sector level*, sector and district plans align to the national vision and development priorities outlined by the TSDF. These Plans bring together all relevant groups and outline the projects and initiatives needed, in particular by government, but also from others, to develop that sector/district in line with the direction of the TSDF.

At the *operational level*, government ministries and agencies each require a Corporate Plan (with appropriate Annual Management Plans) to define their outputs and how they are to be delivered. These will include projects specifically related to the reform of these ministries/agencies. The private sectors/NGOs will have their own 'plans' aligned in varying degrees to the TSDF. Strategies set out in the TSDF and Sector Plans will be used by ministries/agencies for their internal planning. The CP/AMP link directly to the annual budget (soon to be a three year medium term budget framework), through which resources are allocated based on macro consideration of available funding and the TSDF priorities.

The reform program underway in government is focusing on enhancing all these levels of planning and the budget system, along with improved staff management and performance systems.

Attachment 2 - Main issues raised by Outer Islands consultations

The following tables summarize the key issues raised in the various TSDF consultations. Where a response has been possible, this is noted in the right hand column. In some cases, further discussions will be needed within government before a conclusion can be reached.

Main issues from Niuas consultations

Main issues from Niuas consultations	Response
Transportation issues:	
i. Ferry: The need for a 5 – 6 weeks frequency of travel to and from the Niuas. This will help travelling and ease of the financial burden especially from high airfare but also for distribution of goods to the island.	Cabinet has endorsed that the M. V. 'Otuanga'ofa to travel to the Niuas on every 6 weeks. <i>(Proposal endorsed by Cabinet)</i>
ii. Wharf/Habour: The need for reconstruction of the existing wharf and harbour. The current condition of the Niuatoputapu harbour is that M. V. 'Otuanga'ofa cannot anchor right at the wharf due to its size. This needs a small boat for delivery of the passenger and cargo from the ferry to the wharf. There is also need for upgrading of the wharf in Niuafu'ou or provision of the small boat would cater for this need.	The World Bank has also approved the proposal for funding but there are more steps to discuss before transferring the funds. <i>(W/Bank takes up the work)</i>
iii. Airport: The need to upgrade the airports' runways and terminals for both Niuas iv. Airfare: The need for a government intervention with the airfare to and from the Niuas. Currently the rate is too high, \$598 one way, which is very high compared to their level of income. The community's main source of income is from selling of their handicrafts and only a few are working in private sectors and government. Hence, the community needed assistance from the government either to subsidize or find and allow another company to operate to and from the islands so they will compete for a cheaper and affordable price to the community.	Minister is currently working on this proposal, <i>upgrading the airport runway and terminal</i> , with World Bank. <i>(Ongoing dialogue with W/Bank on the issue)</i>

<p>v. Road: The need for re-construction and maintenance of the main and agriculture roads on the island. This is needed as the current road conditions are not in a satisfactory level especially during the wet seasons.</p>	<p>Part of the issue raised will be covered in the W/Bank funded Tsunami Recovery Project and work of MOW.</p>
<p>Communication issues:</p>	
<p>vi. Telephone/Internet: The need for a good communication facility for the island.</p> <p>There is also a need and request made from both islands for the operation of the Digicel Company to be extended to both Niuas. This is one of the major problems faced by the community, the difficulty to stay connected with their children and families who are in Tongatapu and in other islands of Tonga for study and work. Although the A3Z aerial post has been replaced the community still don't receive the call of the Friendly Island loud and clear</p>	<p>The connection of Digicel services to the Niuas is included in the workplan of the Ministry of Information and Communication (MIC) as it is part of the law.</p> <p>There was also a meeting hold with the Digicel Company regarding the connection of their network to the Niua. The intention from the government is to connect from Samoa to Niua which is close compare to Vava'u, however, Digicel does not agreed with the suggestion as they want to connect directly from Tongatapu as Niua is part of the Tonga network. Minister is seeking for another option that Digicel can be able to reach and operate in the Niuas.</p> <p><i>(Issue is already included in MIC workplan and an ongoing dialogue with Digicel on the proposal)</i></p>
<p>Water system:</p>	
<p>vii. Water: The need for a new engine for the water pump of Vaipoa community. There also a need for water supply and water tanks for all households in Niuafo'ou.</p>	<p>The materials for Vaipoa water supply will transport over to the island in the next ferry which is next month.</p> <p>The Japan Grants approved the water proposal for Niuafo'ou and Minister will travel to the island with the Ambassador in April 26, 2012.</p> <p><i>(JICA takes up this water project)</i></p>

Main issues raised from 'Eua Consultation

Main issues from 'Eua consultation	Response
Water system:	
<p>viii. Water:</p> <ul style="list-style-type: none"> - The need for a new engine for the water pump of Houma community. The water for this village is not included in the water supply system for the whole island. - The need for water tanks for households as back up during the wet seasons since the current water system, particularly the filters, cannot tolerate the thickness of mud at this time. - This also raised other issue such as how to treat water for households with rusty roof and still living in a Tongan house. 	<p>This needs to be put into one package as a request for the whole island.</p> <p>Under the water category includes the water tank and engine for water pump and other needs related for water supply. <i>(Such proposal may fit in with the JICA's scheme for Grassroot level and AusAID)</i></p>
Transportation issues:	
<p>ix. Ferry: The need for more clarification on whether the constituency grants can be used for cost of purchasing ferry. Also need to clarify the status of approval from the Cabinet and the status of work on the ferry project.</p>	<p>The project proposal was approved by Cabinet for the Minister and Ministry of Finance and National Planning to look for funding for this project. At the moment, the ministry is currently working to compile the document for a proper project proposal.</p> <p>There are also numbers of development partners (NZAID/WB) that we have been meeting with regards to the project proposal. The Constituency Fund is too small for this project. <i>(Development of project proposal and on-going dialogue with donors is currently underway)</i></p>
<p>x. Road: The need for re-construction and maintenance of roads in the island, including agricultural and tourism roads. The current road conditions are not satisfactory, especially during the wet seasons. There is also the need to have a proper drainage system for the island, which will be very helpful for the sustainability of the new roads</p>	<p>The Chinese Company has already started the working on the Houma road. <i>(CCECC)</i></p> <p>The work for a proper drainage system is currently underway. <i>(PUMA is responsible for the designing)</i></p>

Community Halls:	
<p>xi. Community Hall: The need for multipurpose halls for communities, which will be using for 'fono' meeting of the district and town officers with the community, women's daily activity such as koka'anga – making of tapa, weaving and other handicrafts activities as well as youth's activity. There is also a need for more clarification on how to treat existing halls without out restrooms and kitchens facilities, can these be upgraded?</p>	<p>The same thing applies for these. It would be very helpful if provision of information with clear specification on the list of new halls, list for renovation, and list for those halls that need only restrooms and kitchen. This will be much easier for preparing project document for development partners' assistance.</p> <p><i>(Once the proposal document is completed, it will be submitted to PACC for funding request)</i></p>
Community Development Projects:	
<p>xii. Process and channel of communication: The need for clear clarification on the process and channel of communication for project requests.</p>	<p>All project proposals from any groups of communities in 'Eua will have to go through the 'Eua Council prior submission to the 'Eua Development Committee (EDC). The proposal will be then submitted to the Project and Aid Coordination Committee (PACC) if approved by the EDC.</p> <p>Once the proposal endorsed from PACC, the Project and Aid Management Division of the Ministry of Finance and National Planning will start submitting the proposal to the donors based on the nature of the project proposal.</p> <p>Prior for submission to donors, a relevant application form must be completed in addition to the proposal document.<i>(Regular visit of Project & Aid Management Division to communities is needed for training on the process and informing of the communities on the channel of communication.)</i></p>

Main issues raised from Ha'apai Consultation

Main issues from Ha'apai consultation	Response
Infrastructure issues:	
xiii. Foa Causeway: Need to know the status of the construction and it's an urgent request from the people of Foa District.	KTEC Consultant, executing agency is the Ministry of Transportation. HDC is working together with the Consultant, Mr. Tahifisi Vehikite to tender the implementation of the project and to find contractor for the implementation in April. <i>(This is funded by German in a swap debt with Tonga for the purchasing of the MV Olovaha. Works are scheduled to commence after the cyclone season)</i>
xiv. Lifuka Foreshore: This is a very high need as they urgently requested for construction of a foreshore for both protection and landfill from Hihifo to Koulo (Lifuka District)	Government considered the construction of a foreshore along these areas. The EIA is currently being conducted by the Ministry of Environment and Climate Change, prior the construction activity take place, to identify the impacts that will occurs when the technical works take place. The target timeline for the survey to complete is Dec, 2012.
xv. Road: The need for re-construction and maintenance of the main and agriculture roads in the island. This is needed as the current road conditions are not in a satisfactory level especially during the wet seasons. There is an urgent need to fix the major road at Holopeka as the underground has been eroded by the sea.	Ministry of Infrastructure is coordinating a road maintenance funded by China. This is currently in Tongatapu and anticipating proceeding to the outer islands included Ha'apai in July this year.
Economic issues:	
xvi. Economic Plan: There is a need from the private sectors (tourism, fisheries, agriculture) to formulate an Economic Plan to guide them to a more coordinated effort.	The Government is currently conducting a dialogue with the Private Sectors to improve the coordination and partnership on identifying and addressing issues that will help to drive all the economic development. To include in relevant ministries' developing of sector plan This is an issue to be included in the review of Ha'apai Master Plan.

Main issues raised from Vava'u Consultations

Main issues from Vava'u consultation	Response
Infrastructure issues:	
Road issues: Maintenance is needed for the main roads of Neiafu. The need for re-construction and maintenance of the main and agriculture roads in the island.	The second phase of roads maintenance program would be scheduled to include Vava'u (CCECC)
Public Toilet Facilities: A need for a public facility (toilets) in Neiafu for tourist and others to access	The proposal should be initiated from the Ministry of Tourism Branch in Vava'u or through Vava'u Tourism Association. (Need government's attention)
Drainage: The need to improve drainage along the hill roads to cease water damage on the current tar seal	Government is considered this improvement request in second phase of roads construction. (CCECC)
Vaipua Bridge: Concerns regarding ongoing delays in the refurbishment of Vaipua bridge	Ministry of Infrastructure is now confirmed that Vaipua bridge would be completed by early December 2012.
Tourism issues:	
Tourism Marketing: Concerns about marketing of Vava'u by Ministry of Tourism needs to improve. Need better coordination of tourist industries for Vava'u	Government would see what else they could do and support the social marketing of Vava'u tourist sector
Tourism Zone: Need to establish tourism zone on one of island in Vava'u, 'Utulei. This refers for a recreational centre and any activities for tourists.	This is looking at a million projects and government is considered this in development projects pipeline as well as feasibility study to be undertaken.
Education/Training Issues:	
Education: Need maritime school to be established in Vava'u. Scholarship and school opportunities to be fairly distributed according to student's population.	
Fisheries issues:	
Capacity Building: Need government support to fisheries industry by providing training fishing personnel	The ministry of MAFFF to consider the related training overseas or in-country for the interested fishermen of Vava'u.

Main issues raised from Tongatapu Consultations

Main Issues raised from Tongatapu consultations	Response
Water System Issues:	
i. The need to provide funding assistance for Vaini's water supply's system maintenance.	<p>Japan is currently helping out with providing water supply systems as part of their aid program to Tonga.</p> <p>The community may submit a proposal to JICA through Ministry of Finance and National Planning (Project & Aid Management Division)</p>
Social Issues:	
<p>1. Senior/Disable citizens: The need to facilitate easier access to public transportations.</p> <p>2. Tongan deportees: The need to establish a Counsellor's Council assisted by the Government to provide resources, trainings and guidance for these people (deportees). If they're not taken care of, these people are and will contribute most to increase in crime rates.</p> <p>3. Micro-finance: The need for the accessing process to be fair across the board for everyone.</p> <p>4. Community Trainings: The need for workshop sessions to train locals (especially those unemployed) to work interdependently towards a goal/target, and don't always depend on the Government to provide assistance.</p> <p>5. Gender Equality:</p> <ul style="list-style-type: none"> - The need to have gender equality exercised, for example, Free Church of Tonga needs to welcome women to join their church conferences. - There's a need for a policy/law in place to enforce and support women to have a place in parliament 	<p><i>This could be included in the project of the Vulnerable Groups co-funded by Japan Fund for Poverty Reduction (JPFR) and Asian Development Bank (ADB).</i></p> <p><i>Langikapo mei Hevani (NGO) had done some assistances – counselling and activities to take care of this group</i> <i>MOFNP is trying to locate funding for the purpose</i></p> <p><i>Micro finance is implemented by Tonga Development Bank. Approval of Loan Application will be monitored and administer and monitor by MOFNP. Interest rates charged on borrowing are very low. Target group for this program is for grass roots level. This is funded by ADB and Japan.</i></p> <p><i>Church policy is out of government's authority</i></p> <p><i>Women already have the right to stand for parliament. We need to better understand why women do not stand very often, so we can find a way to address the constraints they face. Under the amended constitution, women can be appointed to Cabinet. The PM has appointed a</i></p>

	<i>female minister for Education.</i>
Private Sector Issues:	
<p>i. Business Licenses:</p> <ul style="list-style-type: none"> - The need to lower business license fees. - Local businesses need to be consecutively reminded of paying up late penalties prior to due date of payment. <p>ii. Local vs. Foreign Companies:</p> <ul style="list-style-type: none"> - There is a need to protect local businesses and provide them a more enabling environment in doing business compared to foreign owned companies. <p>iii. Improve TCCI & Local businesses Partnership:</p> <ul style="list-style-type: none"> - The need for Government to intervene and encourage local businesses to be more involved with the TCCI, by making them understand the coordination between this two is the key portal for getting assistance from the Government. <p>iv. Privatization of Public Enterprises:</p> <ul style="list-style-type: none"> - The need to privatize public enterprises (except essential services like electricity) 	<p>Government made few policy directions included various changes to the Customs Tariff and excise tax rates and exemptions in purpose to provide incentives to the private sectors, businesses and local manufacturer. MLCI has started work on streamlining businesses licenses.</p> <p>Local business already have some advantages over foreign companies</p> <p>The Government is currently trying to adopt the concept of having a dynamic public-private partnership with regular review of actions for addressing identified constraints. Government encourages business to cooperate to avoid having lots of separate groups and individual business approaching government which makes the dialogue more difficult. But ultimately it is for the private sector to sort out their coordination arrangements.</p> <p>Government is looking at options for privatizing some PE and options for public-private partnerships in some areas.</p>
TVET & Education Issues:	
<p>i. The need to support and encourage females to enter technical schools (e.g. offer scholarships) as a potential to reduce unemployment of females in Tonga</p> <p>ii. The need for more scholarship opportunities especially to overseas institutions as there are capable kids out there but school tuition fees remain quite expensive for parents to afford.</p> <p>iii. The concern if in the future, the Government can also provide kindergarten schools; as in a way it re-assures kids will be getting quality education before they enter primary schools.</p> <p>iv. The need to think twice about the new Tongan Language Policy applied in high school level, the Tongan subject should be optional instead of being compulsory (how useful is the subject)</p> <p>v. The need to confirm on up to what age is a student allowed to study without paying school fees (according to constitution that is)</p>	<p>The possibility of offering student loan and when the child work then start paying back, could be considered</p> <p>Constitution stated that a child can enter school without paying school fees until she/he reach 14 years old. There are other government grants to NGOs schools including assisting in teacher's salary.</p> <p>Government is seeking to partner with the private sector to help create the conditions for economic growth and employment</p>

<p>vi. The need to create more employment especially for graduates that end up with no jobs available to match their skills.</p>	
<p>Agriculture & Fisheries Issues:</p>	
<p>i. The need for local exporters to ship their agricultural products to overseas markets (marketing issue). Government should establish a committee inclusive of farmers, MAFFF and MOFNP which will assist farmers in searching for markets.</p> <p>ii. There needs to be a proper plan provided by MAFFF to help direct farmers to what they should produce and at what appropriate time. This would give guidance to farmers on when and what is demanded in the market, whether overseas or local.</p> <p>iii. The need for funds to help increase more fishing vessels, as this is a potential area (fisheries) to help grow the economy.</p> <p>iv. The need to encourage more ‘exports’ and local agricultural production (import substitution), explore potential comparative advantages and not heavily rely on budget support and remittances.</p> <p>v. The need to lessen wharfage fees for fishing boats.</p> <p>vi. The need to allow the Niuaus’ waters open for fishing opportunities considering the short distance it has to travel when exporting fish products (from the Niuaus to Pangopango and straight to Hawaii) plus at better prices too.</p> <p>vii. Locals need to have easier access in obtaining licenses and hired to do fishing instead of granting them to the Chinese.</p>	<p>The Growers Federation is continually being funded by the Government which is suppose to work together with the private sectors to work out these marketing issues.</p> <p>Related issues have been considered and part of the private-public dialogue to find viable solutions</p> <p>The ADB & Japan are funding a micro-finance scheme (Tonga Social Protection Scheme) in which can help address these agricultural export needs (encourage agricultural production for exports)</p> <p>Under the 2012/2013 budget, Government has earmarked \$1m (and hoping to be matched by a foreign donor) for establishment of an agricultural marketing fund, specifically for up-front payment of the growers before their produce are exported.</p>
<p>Financial Sector Issues:</p>	
<p>i. The need to lower the interest rate charged on borrowing, for people to borrow and generate economic activities. Also food and fuel prices are rising and with no money in-hand, people are suffering even more.</p> <p>ii. Exchange rate issue (unfavourable for our exports)</p>	<p>The ADB & Japan are funding a micro-finance scheme (Tonga Social Protection Scheme) which will aim at granting loans at lowest interest rate possible (lower than what normal banks charge)</p> <p>Can be looked into at the up-coming National Economic Dialogue being organized by the NRBT</p>

Infrastructure Issues:	
<p>i. Roads</p> <ul style="list-style-type: none"> - The need to fix and maintain agricultural roads which is very much needed by the communities, especially those living in rural areas whose main source of income are agricultural crops. - The need to improve roads near schools (e.g. at the Takuilau college in Lapaha) to help ensure kids' safety for those using these roads. Especially when it rains, parents even prefer sending kids to schools in town where they can just take the bus without being affected from mud and puddles in the road. <p>ii. Street Lights</p> <ul style="list-style-type: none"> - The need to establish and fill street lights in all main roads in Tonga (e.g. Lapaha's main road) <p>iii. Foreshore</p> <ul style="list-style-type: none"> - Construct foreshore protection along the coastal of Nukunuku. These areas are eroded by the sea especially strong waves in cyclone season and high tides. 	<p>The Government is currently working with China on getting new machineries and equipments expected to arrive in March 2012 to assist with this need to fix and maintain roads and will include these agricultural roads.</p> <p>Main roads are the first priority. Agricultural Roads as mentioned earlier would be our second priority and other roads.</p> <p>The Government pays for all Tonga's street lights except for those in minor roads; however the Government will add other roads on a case by case basis. But currently all main roads should have street lights and the Tonga Power Ltd is the implementing agency in setting up street lights in all main roads.</p> <p>Need to raise up with related agencies, including MECC, MOW & MOT, to assess the area, conduct EIA and determine the scope of work and seek for development partners whether this proposal can include in their aid program.</p>
Government Reform/Restructure Process Issues:	
<p>i. The need to change back the Fisheries department into a ministry as before, running separate from the Agriculture department; as it appears that the Fisheries department is being under-utilized because Agriculture seems to dominate the ministry as a whole.</p> <p>ii. The need to present a graph similar to the MDG progress chart, showing Tonga's economic progress/achievements after each year in the new Government (4 years term).</p> <p>iii. The need to assign the right and appropriate Minister for the most suitable ministry in terms of his/her background, experience and knowledge of the industry. This would further encourage closer relationship working together with the private sector.</p>	<p>The rationale for MAFFF to stay as one ministry due to limitation of scope for number of ministry. Also it needs to keep the common and related issues in one ministry.</p> <p>Noted for action in the next review of TSDF by end of 2012</p>
Health Issues:	
<p>i. The need for the MOH to target groups that are most vulnerable to diseases (e.g. people in poverty of basic needs) and help reduce the increasing numbers of</p>	<p>Increasing focus on Non-Communicable Diseases (NCD)</p>

<p>young adults suffering from diabetes.</p> <p>ii. The need for a health policy to restrain importing of unhealthy products.</p>	
Development/Community & Constituency Funds issues	
<p>i. The need for funds to renovate and help improve Health Centre in Kolomotu'a</p> <p>ii. The need to focus using the Constituency funds for other productive and needy projects instead for maintenance of roads, when it continues to be damaged and less result of improvements made.</p> <p>iii. The need for a transparent system to monitor and maintain big development projects (e.g. road construction project)</p> <p>iv. There needs to be a clear guideline on how the Constituency Fund is being utilized and accounted for. Should not be used by peoples' representatives for campaigning purposes but for people's best interest and the community's overall benefit.</p> <p>v. The need to consider increasing town officers' salary, as it doesn't reflect the load of work they carry out including numerous meetings they're expected to attend.</p> <p>vi. The need to provide incentives/motivation for community police officers, as they are very important in keeping and maintaining peace in a community 24/7 e.g. provide salaries, equipments or life insurance</p>	<p>Japan is currently willing to help establish health centres as part of their aid programs to Tonga. If there are project proposals that are within the Government's or donors' list of actions then the Government/donor can handle this without the constituency having to use their constituency fund, rather it can be used for other needy proposals.</p> <p>The Government is looking at ways to cover road maintenance e.g. may come from fuel levies. Seeking ways for more transparent reporting of projects.</p> <p>The main purpose of this fund is for community development and to develop relationship among the community and their Representative and the government. It is not for campaigning.</p> <p>Need to verify with the Ministry of Police if this is within their budget (taking care of community police officers' expenses and needs) or it should be within the community's own fund raising.</p>

Annex II: ECONOMIC & SOCIAL DEVELOPMENT AND OUTLOOK

1 Global and Regional Development

After suffering a major setback during 2011, global prospects were gradually strengthening again, but downside risks remained elevated. Improved activity in the United States during the second half of 2011 and better policies in the euro area in response to its deepening economic crisis have reduced the threat of a sharp global slowdown. However, in the last few weeks problems in the Euro zone have resurfaced with the Euro zone nearly in recession. Weak recovery, at best, may resume in the major advanced economies. Activity is expected to remain relatively solid in most emerging and developing economies.

Global growth is projected to drop from about 4 percent in 2011 to about 3½ percent in 2012 because of weak activity during the second half of 2011 and the first half of 2012. The January 2012 *WEO Update* had already marked down the projections of the September 2011 *World Economic Outlook*, mainly on account of the damage done by deteriorating sovereign and banking sector developments in the euro area. Much remains to be done by policy makers to fully address the fundamental problems in the global financial system. Each round of monetary easing and expansion is proving to be less and less effective, but opposition to attempts at imposing austerity are rising.

The euro area is still projected to go into a mild recession in 2012 as a result of the sovereign debt crisis and a general loss of confidence, the effects of bank deleveraging on the real economy, and the impact of fiscal consolidation in response to market pressures. Because of the problems in Europe, activity will continue to disappoint for the advanced economies as a group, expanding by only about 1½ percent in 2012 and by 2 percent in 2013. Job creation in these economies will likely remain sluggish, and the unemployed will need further income support and help with skills development, retraining, and job searching. Real GDP growth in the emerging and developing economies is projected to slow from 6¼ percent in 2011 to 5¾ percent in 2012 but then to reaccelerate to 6 percent in 2013, helped by easier macroeconomic policies and strengthening foreign demand; resulting in about 4 percent global growth in 2013.

The ripple effect of the global economic crisis had a major impact in the Pacific region. The Small Island economies has weakened significantly as tourism, agriculture, and manufacturing industries slowed due to the decline in global demand.

Remittances declined by as much as 20% as source economies slowed. Underlying structural weaknesses and the residual effects of high inflation in late 2008 added to the severity and pace of the slowdown felt during 2009 and early 2010, as did natural disasters.

Pacific Island economies has experienced improved economic growth in 2010 averaging 5.5%, with further strengthening to 7.0% in 2011. The major contributors to this performance were Papua New Guinea (PNG), Solomon Islands, and Timor-Leste, with mixed performance over other countries. Increased value of agricultural production and higher tourist arrivals helped Fiji's economy recover from contraction in 2010, increased phosphate exports lifted Nauru's economy, and increased tourist arrivals contributed to faster economic growth in Palau. Spending related to infrastructure projects raised economic growth in Kiribati, the Republic of the Marshall Islands, the Federated States of Micronesia, Tonga and Vanuatu.

Inflation in the Pacific region rose from 5.6% in 2010 to 8.6% in 2011 due to higher global commodity prices in the first half of the year. Lagged effects of the price increases are still being felt in certain economies.

Economic growth projections for most Forum Island Countries (FICs) in 2011 and 2012 are expected to slow, however, a relatively positive outlook is expected for Nauru, PNG, Solomon Islands, and Vanuatu. The current economic crisis has reduced growth prospects for most leading economies, but

at this stage the consensus view suggests that the Pacific region will experience less impact. In part, this is due to relatively optimistic economic prospects of the region's major trading partners, Australia and New Zealand. However, growing inflationary pressures as well as indirect effects from the economic crisis will contribute to downside risks to the region.

Figure 9 - FIC GDP Growth Outlook

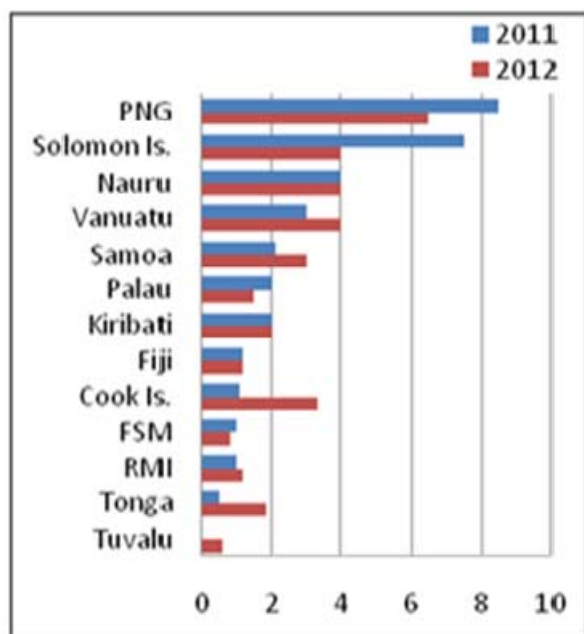
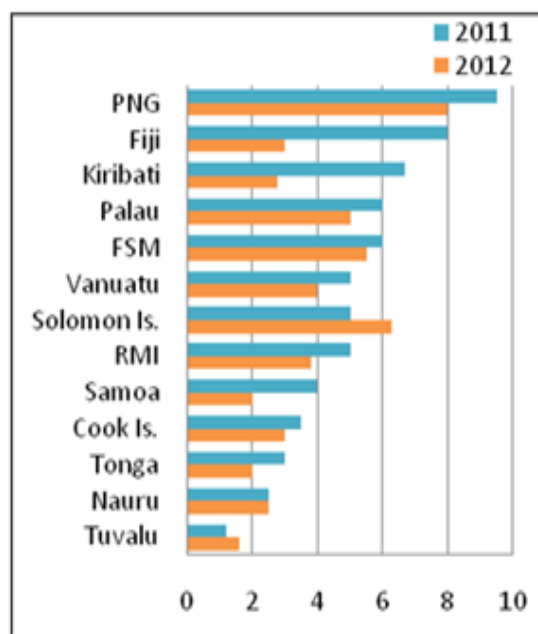


Figure 10 - FIC Inflation Outlook



Source: Pacific Island Forum Secretariat

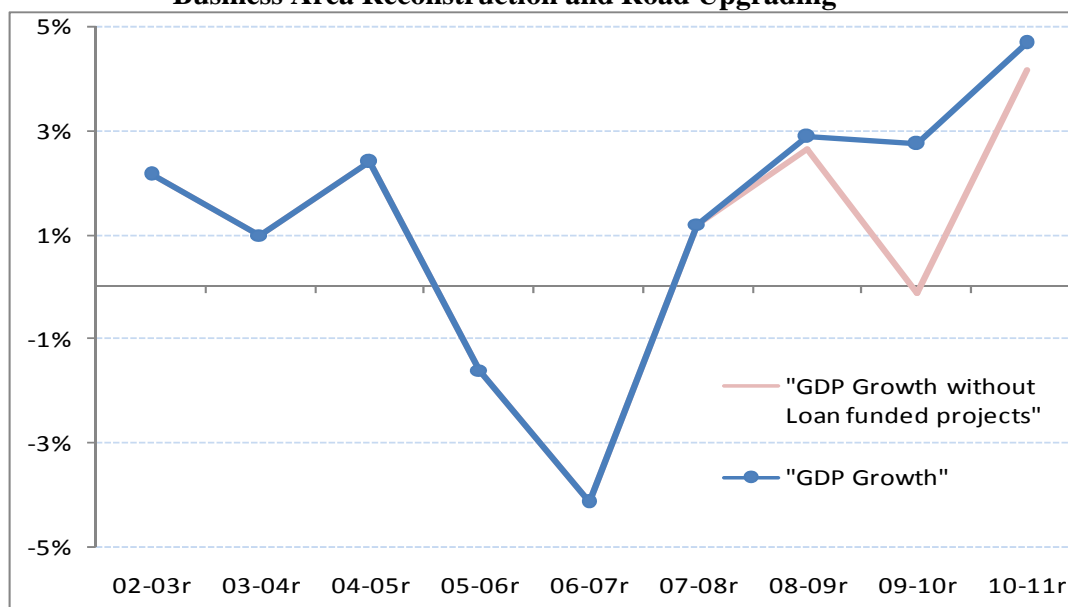
Favourable conditions related to commodity exports ensures an optimistic outlook for the PNG economy from Liquefied Natural Gas LNG and minerals production, the Solomon Islands economy from mining and logging activities, and the Nauru economy through its phosphate exports. Vanuatu, Samoa and the Cook Islands in particular are expected to benefit from an increase in tourism from Australia and New Zealand, especially in 2012. Growth for the other FICs remains low. Driven by high cost of fuel and food prices, an average inflation rate of about 4 percent is expected across all FICs in 2011 (see *Figure 10*), increasing inflationary pressures and contributing to downside risks for the region. Effects of the global economic crisis on the FICs, although limited at this stage, could also affect growth prospects for the region indirectly, through trade and investment linkages between the Euro-zone and the Pacific's economic partners, declining values of Pacific trust funds, and possible declines in tourism and remittance flows from other markets such as the United States and Japan. However, the positive outlook over the short term in the major FIC trading partner economies of Australia and New Zealand support an anticipated increase in tourism to the Pacific, particularly in 2012.

2 Recent Economic Progress and Outlook in Tonga

A major update of Gross Domestic Product (GDP) statistics has just been completed. The new work has allowed more accurate estimates of national income and GDP. Large number of projects funded by development partners, especially in-kind, have now been captured accurately. The coverage of the business sector has been improved, in particular with the inclusion of activities such as Airports and Ports Authorities which had been moved out of government accounts and were not being picked up in the GDP estimates. Coverage of other rapidly growing business areas, such as communications, are now much more comprehensive. Efforts have also been made to improve the methods for estimating other inputs where limited data still remains.

The net affect has been to increase the level of GDP estimates over the last few years, and also clarified in more detail the impact of the major aid investments – which in part helped to offset the effects of the global slowdown.

Figure 11 - GDP Real Growth 2002/03 to 2010/2011 with & without Chinese loan for Central Business Area Reconstruction and Road Upgrading



Source: Statistics Department

Figure 11 shows the revised GDP growth over the last decade. Growth in the early part of the decade continued to reflect similar rates to that of the 90s. The effect of the domestic disruptions, cumulating with substantial damages to the central business area of Nuku'alofa, resulted in substantial falls in GDP during 2005/06 and 2006/07, bigger than anything seen during the 90s. By 2007/08 growth recovered with the start of some rebuilding and gradual return in business confidence.

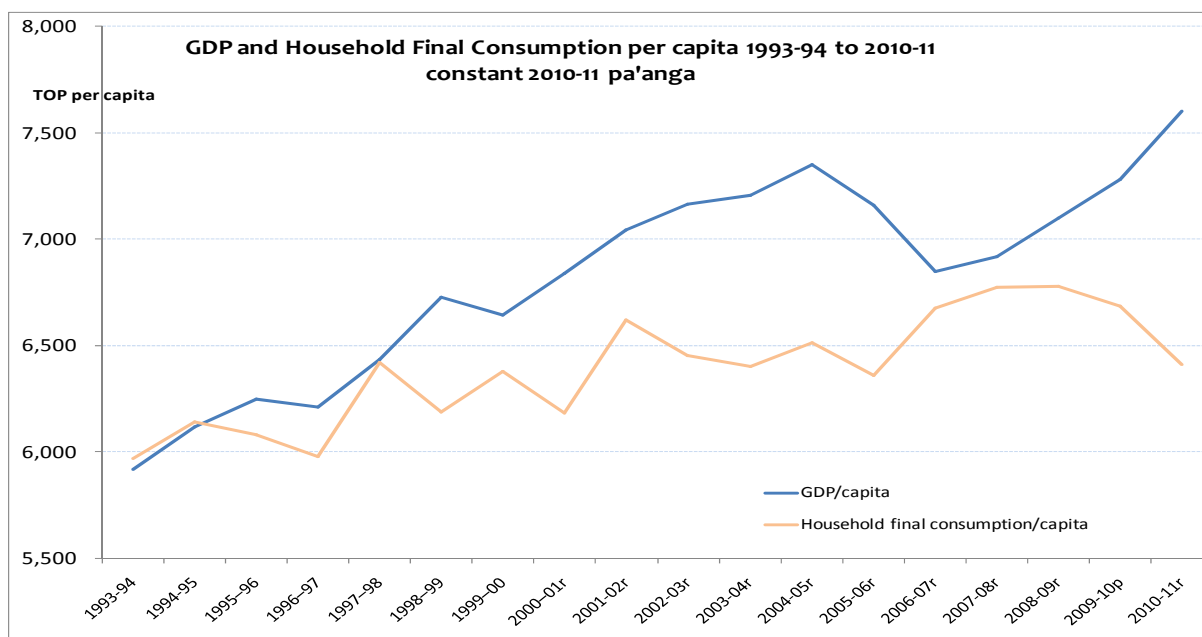
From 2008/09 a major new factor came into play which helped offset the impact of the global crisis on domestic growth. The government signed a loan with China in 2007 with the intention of helping to rebuild the Nuku'alofa Central Business District (CBD) after the civil unrests. This massive increase in expenditure had the effect of keeping both the level and growth of GDP up despite the impact of the global economic crisis, and falls in remittances.

The chart in Figure 11 also attempts to show the impact of the loan on GDP by extracting the GDP associated with the construction and quarrying work under the loan, and thus the impact they have on GDP. The growth was also focused in Nuku'alofa and much of the value added was produced by foreign workers and company who were based in Tonga long enough to be included in GDP estimates. While the linkages to the rest of the economy from these loan funded expenditure are very

limited, some impact on water and power usage and manufacturing is possible. The chart shows that without the loan funded activities, GDP would have contracted slightly in 2009/10.

GDP is not intended as a measure of welfare. The limited links to the Tongan economy can be further seen by the decline in household final consumption per capita, even while GDP per capita has increased, as show in *Figure 12*.

Figure 12 - GDP and Household Final Consumption per capita 1993/94 to 2010/2011
(2010/2011 prices) pa'anga



Source: Statistics Department

The global slowdown and fall in remittances put downward pressure on government revenue despite the loan funded growth in GDP because all imports and activity by the foreign workers and company are tax free, as is standard for foreign development assistance. Government, however, has been successful in negotiating substantial budget support to avoid a further drag on GDP that would have come from government having to reduce expenditure. For 2010/2011 improvements in a number of areas such as agriculture, fisheries and tourism helped boost non-loan growth.

The rate of GDP growth will likely slow considerably in 2011/2012, even drop slightly, however, with the large drop in construction associated with the completion of the loan funded projects, and other large projects. While new grant funded projects have been negotiated with the support of our development partners they will not be of the same magnitude as the loan. And borrowing is not possible for some years.

The high level of primary exports, sandalwood and sea cucumber, cannot be repeated, resulting in a short fall in these sectors. Further, export of these products has been banned due to the serious depletion of their resource base. However, other areas such as the growth in squash pumpkin and tuna fishing could, with care, be sustained. Tourist arrivals also look like continuing to hold up.

Looking forward, government is focusing on working more closely with the private sector. As part of the initiative to activate and stimulate the economy, the government moved to strengthening its working relationship with private sectors and stakeholders including the formation of the National Growth Committee (NGC) and Sector Growth Committees (SGCs). The objectives for these committees is to help identify constraints to growth and their solutions, and ensure that, were

possible, appropriate action is taken by government and the private sector to mitigate these constraints.

Efforts are also being made to improve the delivery of services to rural and outer island communities to increase income earning opportunities there. All these initiatives may not provide the same strong boost to total GDP growth that came from the loan, but it is hoped a more broad based equitable growth will actually do more to address the needs of people and to improve welfare than has been experienced from the recent unbalanced GDP growth. To be successful this will need close partnership and cooperation between government and private.

3 GDP Sector Performance

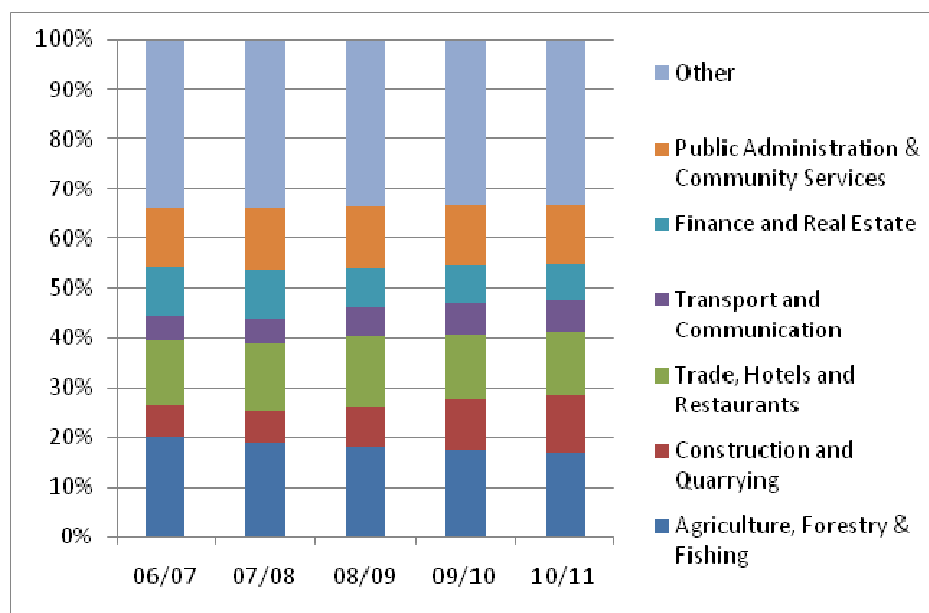
The latest official Gross Domestic Product (GDP), at 2010/2011 prices, stood at \$783.4 million for 2010/2011, representing real economic growth of 4.7%. This level is higher than the 2.3% average growth rate for Tonga in the three years to 2009/10. The borrowing program maintained the economic activity and growth of GDP in the last three years. The high growth was also supported by the building of Vaiola Hospital. Exports of primary products including squash pumpkin, sea cucumber and sandalwood also improved, along with expanded exports for forestry and fisheries, which led to a 3.7% growth in this sector for 2011/2012.

Table 12 : GDP Real Growth

Growth Rates	Statistics (provisional)				MOFNP (estimate & projection)		
	07/08	08/09	09/10	10/11	11/12	12/13	13/14
Agriculture, Forestry & Fisheries	-5.8%	-2.1%	-0.7%	3.7%	-1.3%	2.1%	2.2%
Manufacturing	-0.6%	-7.6%	-2.5%	7.2%	-2.5%	2.4%	-0.1%
Construction	0.9%	35.0%	21.7%	16.9%	-5.7%	-9.5%	-5.6%
Commerce, Restaurants and Hotels	5.7%	7.7%	-5.5%	3.4%	1.4%	2.1%	2.2%
Transport and Communication	3.9%	15.1%	13.4%	2.3%	2.1%	2.0%	2.0%
Finance and Real Estate	2.6%	-16.3%	-1.4%	0.6%	0.0%	-1.0%	-0.1%
Government Services	4.6%	2.5%	0.9%	0.5%	0.2%	0.1%	0.1%
Other	2.2%	4.1%	4.6%	4.7%	1.4%	1.7%	2.2%
GDP	1.2%	2.9%	2.7%	4.7%	-0.2%	0.4%	0.9%

Source: Statistics Department and Ministry of Finance & National Planning

The relative sizes of the main sectors of the economy, as shown in *Figure 13*, have changed significantly in the last three years compared to five years ago. The Construction and Mining and Quarrying have increased while other sectors like Finance and Real Estate and Agriculture, Forestry and Fisheries declined as a total share of GDP.

Figure 13 - Sectors contribution to GDP (%), 2010/2011

Source: Statistics Department and Ministry of Finance & National Planning

Of the individual sectors, the Agriculture, Forestry and Fishing industry remains the highest contributor to economic activity at 17% of GDP, followed by: Trade, Hotels and Restaurants (13%); Public Administration and Community Services (12%); Construction and Quarrying (11.3%); Finance and Real Estate (7.4%); Transport and Communication (6%); and other sectors (3%).

3.1 Primary Sector

The agricultural, forestry and fisheries sector continues to play a vital role in the Tongan economy in terms of providing food security, distribution of wealth and act as a social safety net during time of hardships. In 2010/2011 the primary sector accounted for 19.3% of GDP and over 90% of total exports. The forecast for the primary sector for 2011/2012 financial year is not looking good. It is expected that the sector will experience a negative growth of 1.3% after a strong performance of 3.7% recorded in 2010/2011. The fall is driven by the cut in exports of sandalwood and sea cucumbers due to depletion of available stock.

Some key initiatives in the sector included Food Agriculture Organisation (FAO) continuous support and promote of Food Security, Forestry & Community Development, and Floriculture Project that targeted women's income generating activities. People's Republic of China (PRC) is also supporting Agriculture Demo Farm Project, which generate bio-gas, cultivate mushrooms and make noodles out of sweet potato.

Table 13 : Real GDP growth for Primary Sector (percentage change) (2011/2012 and beyond forecasts)

	06/07	07/08	8/09	09/10	10/11	11/12	12/13	13/14
Primary sector	0.6	-5.8	-2.1	-0.7	3.7	-1.3	2.1	2.2
Agriculture	7.4	-4.3	0.8	-0.8	0.7	2.0	2.0	2.0
Forestry	0.6	8.0	3.1	-8.8	72.1	-68.3	5.0	5.0
Fisheries	-23.3	-14.8	-19.1	1.2	11.7	-2.8	2.5	2.8

Source: Statistics Department and Ministry of Finance & National Planning

3.1.1 Agriculture

The projection for the agricultural sector for 2011/2012 is for an increase of 2.0% compared to a modest growth of 0.7% in 2010/2011 and negative growth of 0.8% in 2009/10. The challenge that the agricultural sector faces are fall in export prices, increased in cost of production, unfavourable weather patterns, unreliable shipping schedules and persistent marketing and quality control problems.

Despite challenges facing the agricultural sector, it is anticipated that exports will hold up in the coming years due to the increase in demand for squash during the off-season from the Japanese market and opening of the Korean market. Squash production expanded from 846 metric tons in 2010/2011 to 3,341 metric tons in 2011/2012. Exports of root crops such as cassava, yams and taro continued to be strong in 2011/2012 recording an estimated volume of 2.3 metric ton, a 25% increase from its level in previous year. Exports of vanilla, kava, and coconuts on the other hand declined but from a very low base.

The recovery in agricultural exports was sustain by the improvement of the quarantine facilities at the wharf; the revitalization of Heat Treatment Force Air (HTFA) at the airport, and the persistent efforts of the Pacific Horticultural Agricultural Marketing Accesses (PHAMA) project to facilitate exporting of fresh produce to the New Zealand market, such as watermelon, pawpaw and breadfruit. In addition, the new agro processing facilities under Stabilisation Export (STABEX) Project, completed in December 2010, such as blast freezer, cooler and other associated agro processing tools and equipment are expected to support exports of root crops for supermarkets and other retail distributors in New Zealand and Australia in the next financial year.

3.1.2 Forestry

The positive growth experienced by the forestry sector in 2010/2011 was largely due to the over harvesting of sandalwood – that is 77 metric tons in comparison to the 25 metric tons harvested during 2011/2012. The Chinese exporters under contract arrangement with local growers operated their owned sandalwood replanting program, however, it takes many years for sandalwood to mature. The over-harvesting of sandalwood prompted government to pass a moratorium over harvesting and exporting of sandalwood starting mid 2011/2012 financial year.

Production at 'Eua forestry is now contracted to the Tonga Forest Product Ltd (TFP), which will supply electric poles to the Tonga Power Limited. They are also increasing the domestic sale of various types of timber for local furniture and construction.

3.1.3 Fisheries

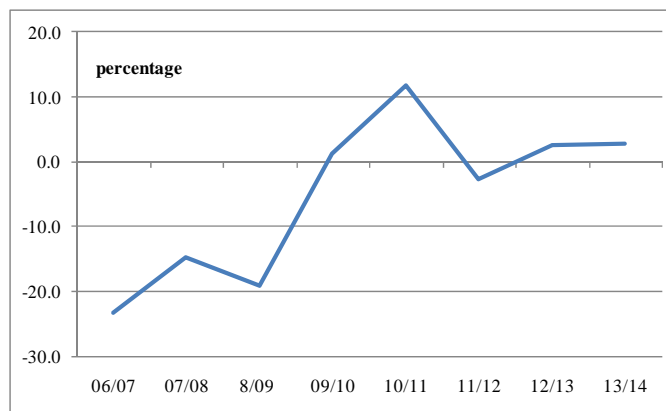
The strong growth experienced by the fisheries sector in 2010/2011 of 11.7% was due to increase in the volume of sea cucumber exported by 62% as well as the increased in exports of tuna, by 150%. Furthermore, sea weed export also increased because of the re-opening of overseas market to Japan and China.

Forecast for the fisheries sector looks gloomy for 2011/2012 with a fall of 2.8% compared to the strong growth in 2010/2011 and moderate growth of 1.2% in 2009/10. The moratorium imposed on harvesting of sea cucumber exacerbate by the decline in the volume of exporting other marines products, (from 183 metric ton to 137 metric ton) and decrease in the number of fishing vessels, from 5 to 3 contributed to the negative growth forecasted for 2011/2012.

Despite the negative growth projected for 2011/2012, the industry is still hoping for better results. It is expected that the re-opening of Tongan fisheries waters to foreign fishing vessels, the proposed increase in the size of vessels from 15m to 23m to allow use of hydraulic reels for snapper fishery and use of scuba diving gear for aquarium fishery, farming of economic potential marine species including sea cucumber and pearl, the development of aquaculture areas and provision of proper

infrastructure, as well as development of management plans will contribute to a more productive sector in the future. The Ministry of Agriculture, Foods, Forestry and Fisheries is also targeting to increase the number of foreign vessels that are licensed to fish in our waters.

Figure 14 - Fisheries growth rates



Source: Statistics Department and Ministry of Finance and National Planning

The Ministry continues to work with various communities on the initiative of Special Management Areas (SMA). In 2011, the number of interested communities in the SMA has increased. The existing SMA communities are 'Atataa, 'Eueiki, 'O'ua, Felemea, Ha'afeva, Nomuka and Ovaka. The request for Taunga SMA is still in development process.

Donors' initiatives assisting in the development of the fisheries sector including technical and financial support for the Fisheries Department from the Commonwealth Secretariat, Pacific Islands Forum Fishing Agency, Intra ACP programme from European Union (EU), and FAO funded project on Milkfish.

3.2 Secondary Sector

The secondary sector comprises mining & quarrying, manufacturing, electricity & water and also construction. In 2010/2011, it continued to drive the GDP Growth compared to the other two sectors. There has been a huge increase in this sector since 2007/08, with it still growing at over 11% in 2010/2011. The large falling forecast from 2011/2012 is due to the completion of a number of major projects and programs without new ones of the same magnitude to replace them.

Table 14 : GDP growth at constant price for Secondary Sector (2011/2012 and beyond forecasts)

	06/07	07/08	8/09	09/10	10/11	11/12	12/13	13/14
Secondary sector	-2.8	0.8	9.5	11.3	11.1	-3.9	-4.3	-2.6
Mining and quarrying	-5.9	26.6	16.8	137.6	-1.8	-5.9	-5.9	-5.9
Manufacturing	-3.4	-0.6	-7.6	-2.5	7.2	-2.5	2.4	-0.1
Electricity and water	-1.2	1.7	-4.6	-3.5	2.9	0.8	1.8	3.0
Construction	-2.8	0.9	35.0	21.7	16.9	-5.7	-9.5	-5.6

Source: Statistics Department and Ministry of Finance & National Planning

3.2.1 Mining and Quarrying

The Mining and Quarrying sector performance is closely related to the various activities in the construction sector. The projection for 2011/2012 is a further negative growth of 5.9% from the negative growth of 1.8% recorded in 2010/2011. The decline reflected the completion of major

construction projects including Nuku'alofa Central Business District, Vuna Wharf Reconstruction, as well as roads improvements construction funded from the Chinese loan. The sector is expected to continue at a lower level similar to that in the past.

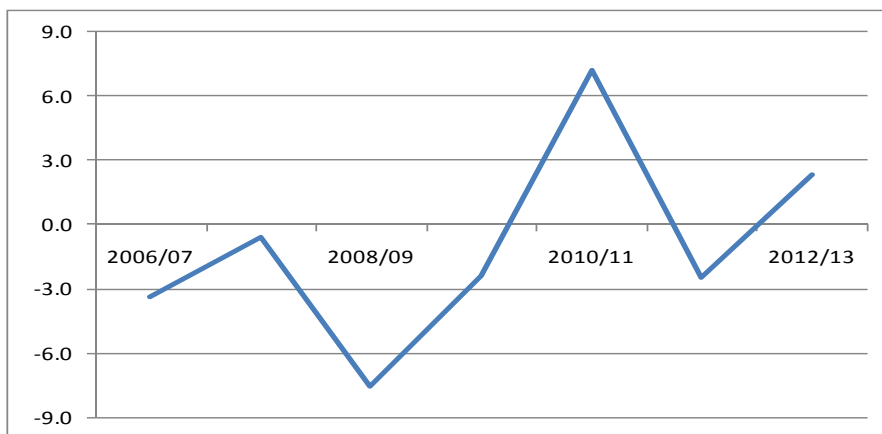
3.2.2 Manufacturing

Manufacturing sector contributes around 6.7% of total GDP after averaging negative 3.5% between 2006/07 and 2009/10. Growth for 2010/2011 increased by 7.2%.

The improved performances from the sector including the strengthening of the Manufacturing Association (MAT) - number of membership in the MAT has grown from 12 in late 2010 to about 31 companies today; developing and diversifying into new products; continue searching for more commercial and industrial opportunities; and to promote export to high value markets.

Manufacturing activities includes arts and crafts, food and beverages, printing and technology, construction, joinery and furniture, fibreglass, paints, painted garment, agriculture, fisheries, and industries. Tonga Forest Product Ltd. has been contracted to supply electricity posts to the Tonga Power Limited, thus replacing importing of electrical post from New Zealand.

Figure 15 - Manufacturing sector growth rates.



Source: Statistics Department and Ministry of Finance and National

It is estimated to decline by -2.5% in 2011/2012 as Nuku'alofa CBD reconstruction and Vaiola Hospital are completed.

The industry has the potential to contribute positively to economic growth in Tonga in terms of exporting, import substitution, providing employment opportunities, utilizing resources that are

available locally such as coconuts, taro, cassava, chilli, rain water and underground water, gravels, sand, medicinal plants, forestry, vegetables, fruits, local meat (beef and pork), marine resources, agricultural resources, and building a stronger, skilful workforce. The efforts in reducing barriers to the industry in terms of removing taxation of raw and packaging materials, regulatory issues has been identified as a small step in developing the industry to meet its potential.

3.2.3 Electricity and Water supply

There is a projected slowdown in growth for the utilities industry from 2.9% in 2010/2011 to only 0.8% in 2011/2012 compared to a fall of 3.5% in 2009/10. The slowdown in electricity and water growth in 2011/2012 is associated with a levelling off in the ongoing construction projects, but some expansion in demand associated with the growth in other areas of activity.

Sales of water showed an increase, by 9.4% in 2010/2011. Increase in investment has helped to improve services to the public. However, demand for water still exceeds supply so there is further potential for expanding production of water.

Most energy needs are supplied by imports making Tonga vulnerable to the volatility of world fuel prices. In recent years, the Government has invested heavily in infrastructure including improving

the power distribution. Government is also seeking ways for more effective purchase and distribution of fossil fuels which can help to lower costs. Under the Tonga Energy Road Map (TERM), projects are already in the pipeline, 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 Niuaas, alternative options for the management of the fuel farm and supply of fuel, Tonga Village Network Upgrade and improve options for micro energy generation. Government continues to provide recurrent funding for streetlight maintenance. There are also community solar power projects in operation in the outer islands.

3.2.4 Construction

Construction sector continued to play a vital role in stimulating economic activity in the last 4 years commencing from the reconstruction of Nuku'alofa in 2008/09 recording an average growth rate of around 18%. However, projection for 2011/2012 suggests that the sector growth will be a negative 5.7%, associated with the completion of the reconstruction of Nuku'alofa as well as the completion of the Vaiola Hospital. Reinforcing the base set in 2011/2012 are WB post-tsunami rehabilitation at Niuatoputapu; the WB Transport Sector Consolidation Project (TSCP) - financed by AusAid; ADB's Integrated Urban Development Project; and NZAid reconstruction of 'Eua airport as well as the Popua Solar plant project.

The prospect for 2012/2013 included the construction of the submarine cable project, upgrading of airport under the WB Pacific Aviation Investment Project (PAIP) project, United Arab Emirates (UAE) and ADB solar project for Vava'u and outer islands, ADB's completion of the Integrated Urban Development Project (IUDP) project as well as the commencement of the new Nuku'alofa Urban Development Sector Project (NUDSP) project focusing on water, sanitation and urban planning, and the rehabilitation of Foa Causeway.

Government acknowledges the huge contributions of donor/loan funded projects in the overall growth of Tonga; but government is also concerned about the limited contribution of some of these to employment opportunities for Tongans and increase activities to domestic businesses.

3.3 Tertiary Sector

Table 15 : GDP growth at constant price for Tertiary Sector (2011/2012 and beyond forecasts)

	06/07	07/08	8/09	09/10	10/11	11/12	12/13	13/14
Tertiary sector	-5.5	3.3	1.4	0.6	2.1	1.3	1.3	1.5
Trade	-0.5	5.7	7.9	-5.6	3.3	1.2	1.6	1.7
Hotels and restaurants	-10.3	6.0	7.1	-4.9	3.7	2.1	3.9	4.0
Transport and Communication	-1.1	3.9	15.1	13.4	2.3	2.1	2.0	2.0
Financial intermediation	-1.0	2.9	-20.4	-2.7	-1.2	-0.7	-0.2	0.2
Real estate, renting and business services	-5.1	1.0	1.1	2.7	6.4	2.1	-3.0	-1.0
Public administration and services	-15.1	4.6	2.5	0.9	0.5	0.2	0.1	0.1
Education	-11.6	-7.5	-0.7	5.7	1.5	1.3	1.2	1.2
Health and social work	-9.4	0.7	10.2	1.5	-0.9	0.3	0.3	0.3
Recreational, cultural and sporting activities	-0.1	8.2	1.2	-1.0	5.9	2.5	2.5	2.5
Other community and personal services	-12.4	0.3	5.7	3.3	12.4	7.2	7.6	9.1
Ownership of dwellings	2.1	1.7	1.0	1.4	1.2	1.7	1.5	1.4

Source: Statistics Department and Ministry of Finance & National Planning

3.3.1 Whole Sale and Retail Trade

Figure 16 - Wholesale/Retail Trade contribution to GDP



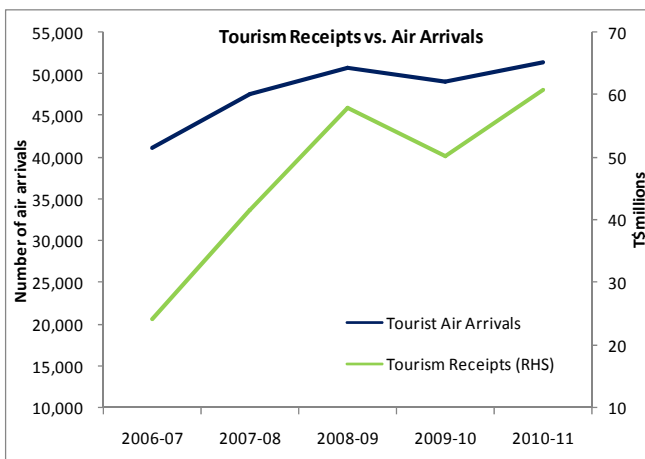
Source: Statistics Department and Ministry of Finance & National Planning

The wholesale and retail sector contributed about 11.3% to total GDP or 18.8% of the Tertiary sector in 2010/2011. The sector grew by 3.3% in 2010/2011 compared to negative growth in 2009/10 of 5.6%. These rates are correlated with the 8% decline in imports in 2009/10, and the increase in imports of 11% in 2010/2011 which was largely due to increased importation of industrial supplies and fuel.

3.3.2 Hotels & Restaurants

The Hotels & Restaurants sector only contributes 3.3% to GDP. Growth increased by 3.7% in 2010/2011, after a decline of 4.9% in 2009/10. This change in growth was largely due to an increased in the number of tourist air arrivals by 5% in 2010/2011 compared to a decline of -3% in 2009/10. Tourism receipts also fell sharply in 2009/10 before recovering strongly in 2010/2011, even faster than the increase in air arrivals.

Figure 17 - Tourist Receipts vs. Air Arrivals



Source: Tonga Visitors Bureau

Over the years, the sector has faced various challenges such as competition from tourists' destinations from other Pacific Island countries; substandard quality accommodation facilities as well as poor public perception of the industry¹³.

The launching of the four-star Scenic Hotel Tonga, as part of the well known NZ-owned Scenic Hotel Group's, includes its aspiration to provide training to local employers on its principles and practices. This should help to set a bench mark for the industry to follow thus improving public perceptions and hopefully the quality of accommodation facilities available for tourist in the Kingdom.

One of the resorts in Tonga received the Golden Palmtree Award¹⁴ for the most outstanding adventure vacation category from over 100 entries. This should help with advertising Tonga, in addition to other tourism-related venture programs with overseas partners along with The Ministry of Tourism's newly developed website¹⁵, which provides more information for potential tourists. The

¹³ According to feedbacks from the Lumsden Research (an Exit survey on departure visitors from Tonga, conducted by Tourism Tonga)

¹⁴ A special award from Geo Saison, the most highly level Travel Magazine in Germany

¹⁵ www.thekingdomoftonga.com

number of licensed hotels and restaurants in Tonga¹⁶ has also increased from 134 in 2010 to 150 in 2011; and in the first four months of 2012, four new restaurants have already been registered.

3.3.3 Transport and Communication

The transport and communication sector consists of air, land and sea transport and telecommunication. Overall the sector continued to post positive growth projected at 2.1% in 2011/2012 although this is much lower than the average growth of around 6% in the last five years.

Economic growth in the communications sub-sector during 2011/2012 largely stemmed from having a competitive environment which allows Tonga Telecommunication Corporation and Digicel to compete in the telecommunication and related services.

The continued competition between the two telecommunication companies, Tonga Communication Corporation (TCC) & Digicel have driven growth, contributing around 70% of growth in the combined transport and communications sector. Both companies have expanded investments in additional mobile money services, money wallet, internet access and cellular roaming services in an effort to strengthen market position and maximize competitiveness. The Submarine Cable Project funded by the World Bank, Asian Development Bank and TCC, estimated at USD\$33 million, is expected to boost performance of this sector through increase capacity, faster connectivity and lower telecom prices. There is high expectation that faster and cheaper internet connection will bring significant economic investment and activities, and social benefits through our education and health systems. The installation of the project is due to be complete by mid 2013.

Transport sub-sector showed slight improvements in 2011/2012 reflecting various activities in the domestic and international shipping services, air and road transportation. In terms of shipping, the regular shipping services to the outer islands provided by the new ferry M.V. 'Otuanga' ofa in late 2010 has stabilised this sub-sector although some disruption in other route occurred during the year. The government continued to provide subsidies to the Niua with the ferry making a trip every six (6) week. The WB funded TSCP project with government is looking at ways to strengthen a safe and secure maritime sector.

International shipping services has shown improvement from previous years with volume of cargo at wharfs increased by 10 percent from its level in previous year, despite a drop in the number of vessels ported at the wharf in same period. The government in conjunction with Pacific Forum Line (PFL) coordinated new shipping schedules to and from Auckland commencing at end of April which now provide 9-10 days frequency service. This is expected to improve performance of this sub-sector and support other economic initiatives of the country in the next financial year.

3.3.4 Financial Intermediation

Activities in the Finance and Business sector have continued to decline in the last two years, by 2.7% in 2009/10 and 1.2% in 2010/2011, following the ongoing bank consolidation. Lending over the past two years has declined and subsequent tighter credit conditions caused this deterioration. This tight bank lending is creating financial difficulties for the private sector by weakened an already low investment level. As described in more detail under the section on Private Sector Credit Growth, lending has continued to decline into 2012.

The bank's tight credit criteria continued to make it difficult for productive sector to borrow coupled with the continuing decline in remittances over the past 4 years. This tight lending with ongoing high interest rates were among those issues discussed in the Economic Dialogue, held on 7-8 March 2012. Tonga Development Bank has reduced their interest rate by 1% on all customers loan. They also

¹⁶ Source: Tonga Visitors Bureau

reduced repayment by 50% for three months to allow its customer to meet social obligations like education fees. There has also been a rapid expansion in microfinance lending by SPBD since it was established in Tonga three years ago. As of December 2011, they had 4099 clients with a loan portfolio of \$2.9m million pa'anga.

3.3.5 Public Administration and Services

Public Administration and Services sub-sector contributed an average of 12% to GDP in 2010/2011, which is the largest component in the Services Sector. Provisional figures indicated a growth rate of 0.2% in 2011/2012 compared to a 0.5% in 2010/2011. Growth in this sub-sector has slowed with the constraint on the government's budget. Given the fiscal situation, government continued to receive financial supports from development partners both from project and budget support. Without this support this sector would have had to reduce government expenditure. Government is looking at how to improve quality of spending without compromising service delivery. A slight growth is projected for 2012/2013 in this sector with further budget support expected to maintain expenditure. Continuation of the same level of supports in the future is yet to be confirmed.

3.3.6 Education, Health and Social Work

Education, Health and Social work sector contributed an average of 3% to GDP in 2010/2011. It only covers private sector and non profit institutions. Government funded Health and Education is included under Public Administration. It was estimated that the growth rate for Education in 2011/2012 was 1.2%, down from 1.5% in 2010/2011. Government grant supported this sector with a grant of \$400 per student to assist private schools to recruit and retained qualified teachers. Health and Social Work sector's growth fell by 0.9% in 2010/2011 after increasing 1.5% in 2009/10. It is expected that this sector will continue to grow at a slower rate with continuous supports from government and development partners.

3.3.7 Recreation, Cultural and Sporting Activities

Entertainment and private services (family and cultural activities) contributed 1% to GDP in 2010/2011. This sector grew at 5.9% in 2010/2011 and is projected at lower rate in 2011/2012.

4 Foreign Reserves and Balance of Payments

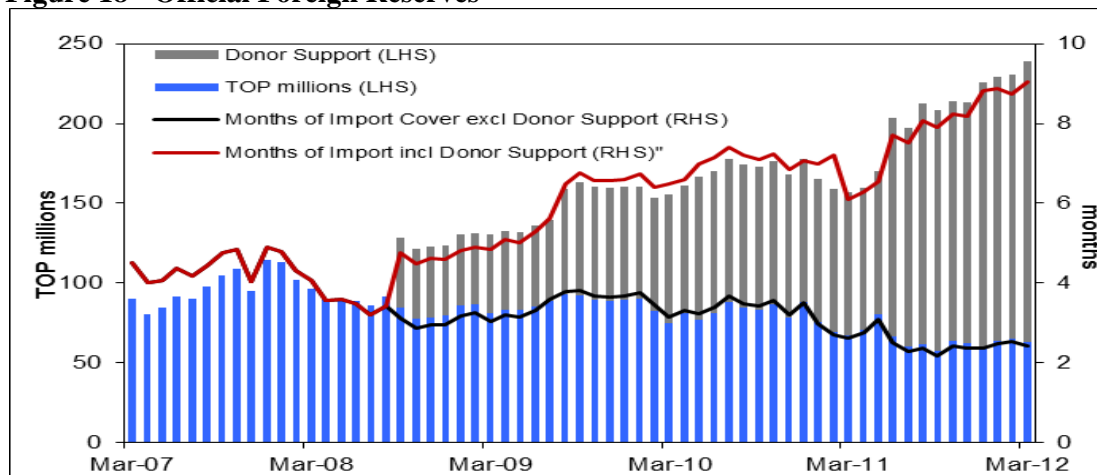
4.1 Official Foreign Reserves

Gross Official Foreign Reserves remained high over the past six months, reaching a new record high of \$239.2 million at the end of March 2012. This is an increase from \$208.1 million at the end of September 2011 and equivalent to 9.1 months of import coverage at the end of March 2012. The significant increase in the level of foreign reserves over the last six months was mainly due to the receipt of foreign aid from Tonga's development partners including budgetary support. This is reflected in a build up in government cash balances, which was one of the agreed roles of the budget support. The high level of foreign reserves also reflected weak domestic demand for credit compounded by the decline in remittances and tighter lending criteria which discourages borrowers. As clearly pointed out in the Economic Dialogue, hosted by National Reserve Bank, borrowers from productive sectors of the economy claimed that the lending criteria is inflexible and does not help to them to invest in new stocks and recapitalize on productive capital goods. Government is working with the NRBT to better understand the position of the banking system and how to address the constraints to lending.

Excluding the effects of donor support the situation is much more troubling with falling reserves and import coverage to well below desirable levels. To the extent that donor supported reserves are related to projects, improved project implementation rates would cut this reserve position. To the

extent the aid funded reserves reflect accumulated cash reserves from budget support, the situation is dependent on government being able to maintain these new high cash balances. If budget support or revenue proved to be lower than budgeted, or expenditure was to increase, it is possible that the cash balances and thus reserves could fall. Government recognizes the importance of improved coordination between fiscal and monetary policy and is strengthening its regular dialogue with the NRBT of these issues.

Figure 18 - Official Foreign Reserves

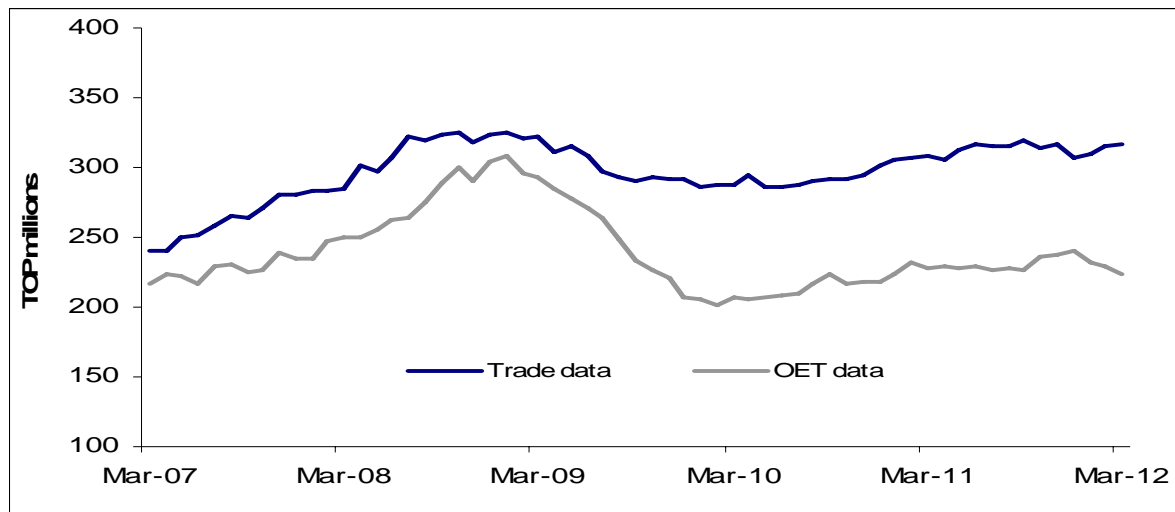


Source: NRBT Monetary Policy Statement, March 2012

4.2 Foreign Exchange Payments

Total payments (OET basis) fell substantially in the six months to March 2012 by \$50.9 million to \$170.2 million compared to \$221.1 million recorded in the six months to September 2011. The fall was attributed to lower official and private capital outflows as well as lower import payments.

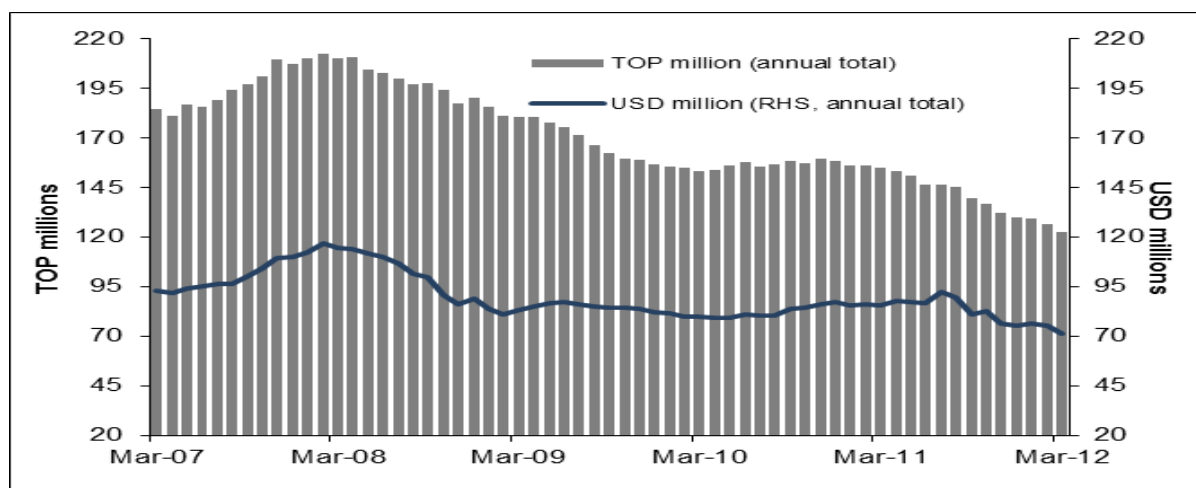
Import payments decreased by \$7.2 million to \$108.6 million in the six months to March 2012 from \$115.8 million in the six months to September 2011. This fall was mainly due to lower payments for wholesale and retail goods as well as oil imports. The fall in wholesale and retail import payments partially reflected slower domestic demand attributed to the continuing fall in private remittances. The stable level of imports on a trade basis may reflect the impact of remittances in kind and imports for the China loan projects where payments are not captured by the OET. On an annual basis, import payments fell to \$224.4 million from \$226.8 million a year earlier, mainly due to lower import payments for wholesale and retail goods.

Figure 19 - Import Payments (annual total)

Source: NRBT Monetary Policy Statement, March 2012

4.3 Foreign Exchange Receipts

Total receipts (OET basis) fell dramatically to \$194.2 million in the six months to March 2012 from \$280.4 million recorded in the six months to September 2011, largely due to lower capital inflows. Remittances continued to fall over the same period by \$12.2 million to \$55.1 million in March 2012 from \$67.3 million in the six months to September 2011. On a yearly basis, remittances fell by 21 percent year on year (\$32.2 million) to March 2012 compared to an increase of 0.9 percent (\$1.4 million) in the same period last year. The strengthening of the Tongan pa'anga against the US dollar contributed to the fall in remittances; however, given imports are costed in US and other foreign currencies, the impact on the ability of Tongans to purchase imports is less severe than suggested by the fall in remittances in pa'anga terms.

Figure 20 - Remittances

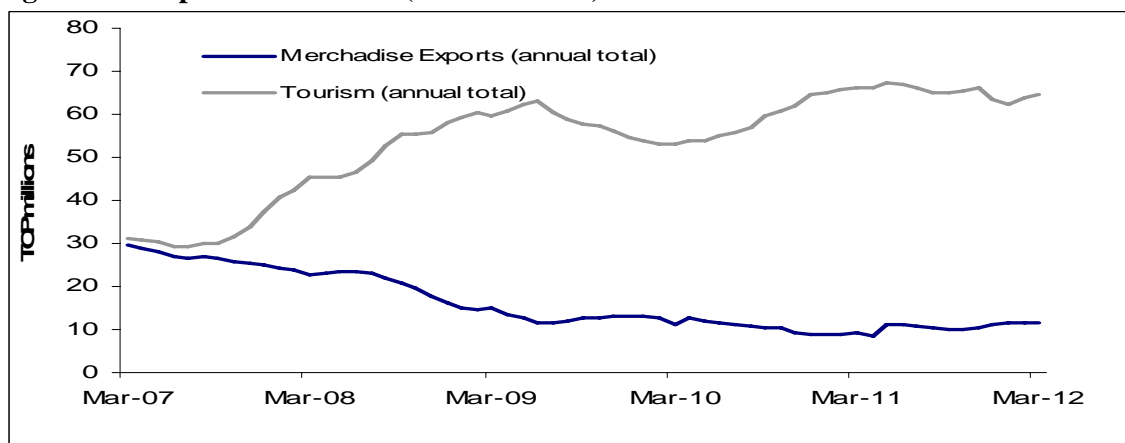
Source: NRBT Monetary Policy Statement, March 2012

Remittances accounted for the equivalent of 55 percent of total imports in the year ended March 2012 compared to 62 percent in the year ended September 2011 and 68 percent in the same period a year earlier. This reflected more of the rise in imports funded by foreign aid, aid received in kind and remittances in kind sent to private individuals instead of cash. The shift of remittances away from the

banking system to other methods is only partly captured in this remittances data. For example transfers through the new phone transfer system is captured, but goods paid for overseas and then picked up by Tongans from shops in Tonga are not. Government is seeking ways to gain a better understanding of these changes. The strengthening of the Pa'anga against the US dollars also contributed to the lower import bill as most import payments are made in US dollars.

Merchandise exports (OET basis) fell to \$4.8 million in the six months to March 2012 from \$6.8 million in the previous six months, reflecting the end of the trade season for sandalwood in the September quarter and lower proceeds from sea-cucumber exports. However, export earnings increased by 25 percent to \$11.5 million for the year ended March 2012 compared to a decline of 0.8 percent year on year to September 2011 which was mainly due to lower proceeds from sea-cucumber. There is also strong evidence that OET is not correctly capturing all exports. More work is required to improve this data.

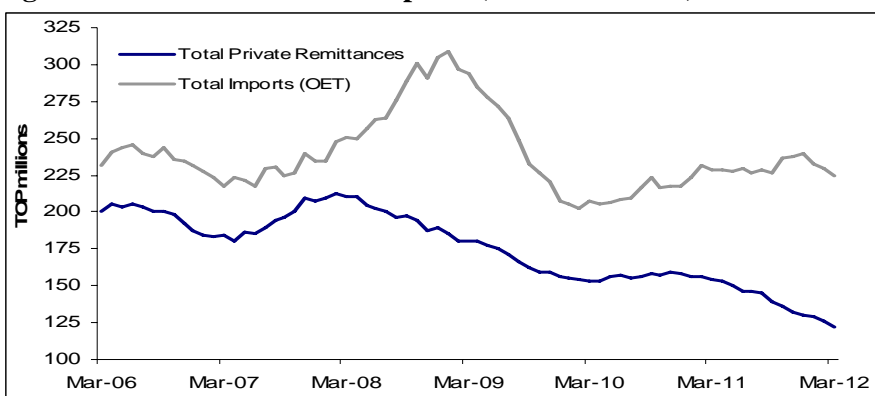
Figure 21 - Exports & Tourism (OET estimate)



Source: NRBT Monetary Policy Statement, March 2012

Travel receipts (OET basis) decreased by \$2.7 million to \$27.5 million in the previous six months to March 2012, reflecting the end of the holiday season and the Christmas festivities. On an annual basis, tourist earnings fell from \$59 million recorded in March 2011 to \$56 million for the year ending March 2012. A large amount of the travel receipts are from foreign card transactions which are recorded as travel receipts. This creates difficulties where residents use foreign cards for transactions.

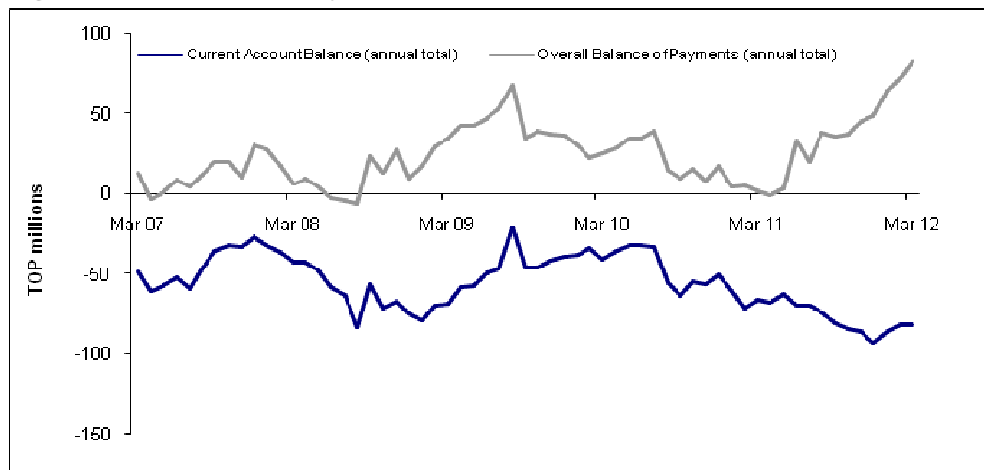
Figure 22 - Remittances and Imports (12 months total)



Source: NRBT Monetary Policy Statement, March 2012

4.4 Balance of Payments

Figure 23 - Balance of Payments (OET estimate)



Source: NRBT Monetary Policy Statement, March 2012

The current account deficit widened to \$43.9 million in the six months to March 2012 from \$37.4 million in the previous six months, reflecting lower receipts from private remittances and

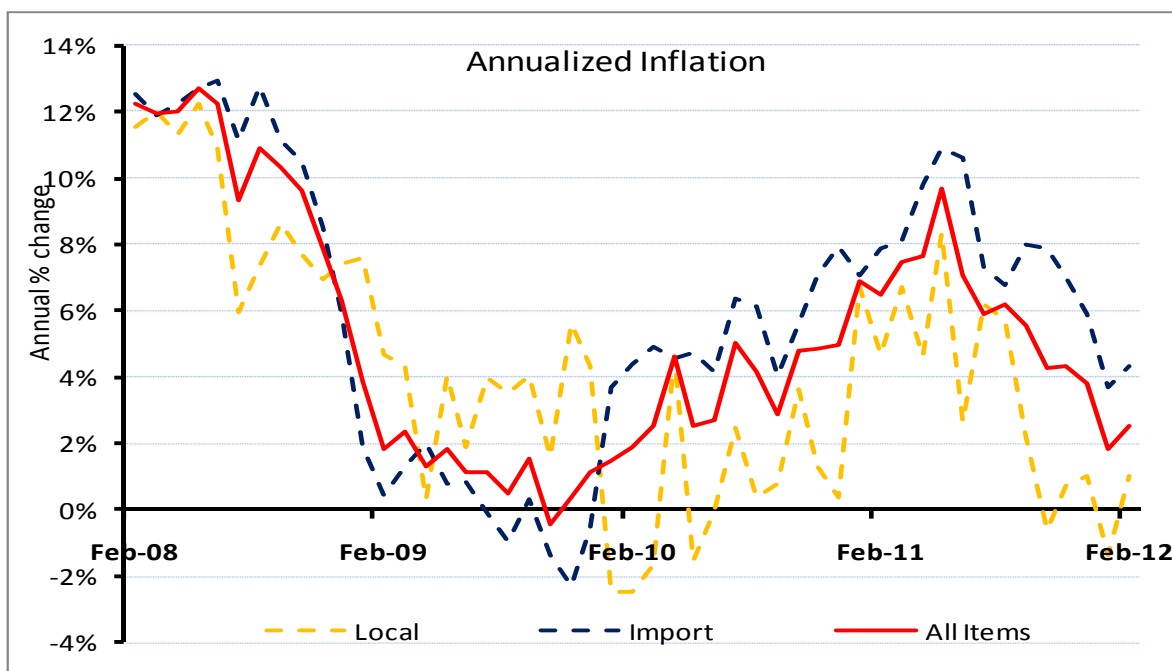
exports combined with higher payments for transportation services. The absence of the large capital inflows from the previous six months contributed to the decrease in the capital account falling from \$96.7 million in September 2011 to \$68.9 million in March 2012. In the year ended March 2012, the net capital inflows together with the net unrecorded inflows more than offset the deficit in the current account which resulted in an overall balance of payments surplus of \$82.1 million.

Foreign reserves are expected to remain high driven by the expected receipts of official aid funds in the next six months. However, the expected repayment of government and private foreign currency loans will exert downward pressure on the level of foreign reserves. The domestic activities are expected to pick up from the utilization of aid funds, and remittances are projected to remain stagnant despite signs of improvement in the United States economy and the fall in the unemployment rates of the remitting source countries.

5 Review of Monetary Conditions

5.1 Inflation

Figure 24 - Annualized Inflation, 2008 – 2012



Source: Statistics Department and Ministry of Finance & National Planning

The 2010/2011 peak in inflation was in May 2011 at 9.7% and has continued to decline to 2.6% in February 2012, largely due to an easing in international food and fuel prices during this period. The average annual inflation rate increased from 1.7% in 2009/10 to 6.0% in 2010/2011 and 5.0% for the first half of 2011/2012. This was mainly due to a surge in prices of imports, for food, fuel and tobacco as well as in the domestic agricultural market.

The inflation rate for imported consumer goods and services increased to 10.6% in the year ended June 2011, from 4.1% in the same period a year ago. The increase in the cost of imported fuel stemmed from the soaring global oil prices - averaging around US\$76 per barrel in June 2010 to US\$114 per barrel in June 2011. The strengthening of the Tongan Pa'anga against the US dollar overshadowed soaring global oil prices. However, the fall in the value of Tongan pa'anga against the New Zealand dollar push up prices of imported goods from New Zealand. Higher government excise tax on tobacco also contributed to higher import inflation.

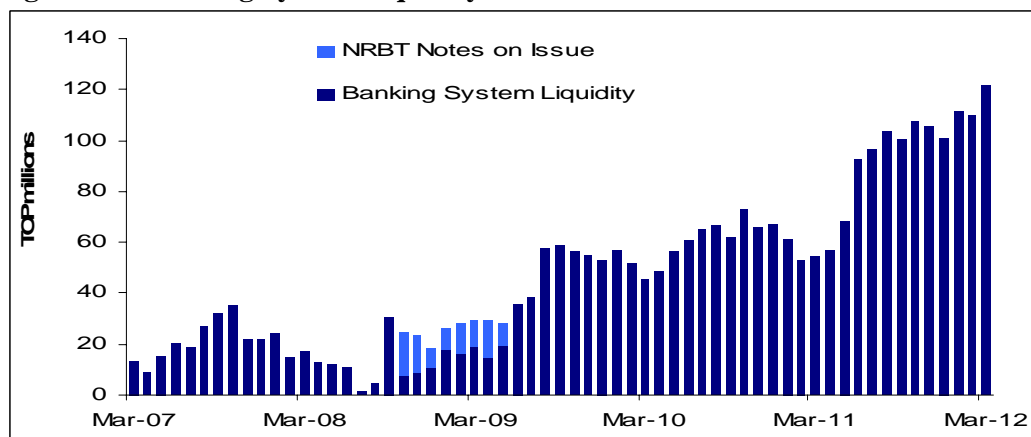
Local inflation on products and services increased to 2.7% in the year ended June 2011, from -1.0% in the same period a year ago; largely due to an increased in prices of electricity and power, which is in line with the rise in diesel prices (up by 15%) during the same period. The Government has subsidized the first 100 kilowatts used by each household in June 2011 to September 2011. This has helped to curb local inflation a little.

Inflation is forecasted to moderate in 2012 as international commodity prices have tended to ease from the higher prices in 2011. Global food prices fell by 6% in March 2012 year-on-year compared to a rise of 25% in March 2011 year-on-year. Fuel prices are expected to remain stable, but are particularly at risk due to geopolitical concerns in the Middle East. Recent data also shows the Tongan Pa'anga is strengthening against the U.S and NZ dollars and its appreciation may help mitigate inflationary pressures through cheaper imports.

5.2 Liquidity

Liquidity in the banking system rose to \$121.3 million at the end of March 2012 from \$100.4 million in September 2011, in line with the rise in foreign reserves.

Figure 25 - Banking System Liquidity

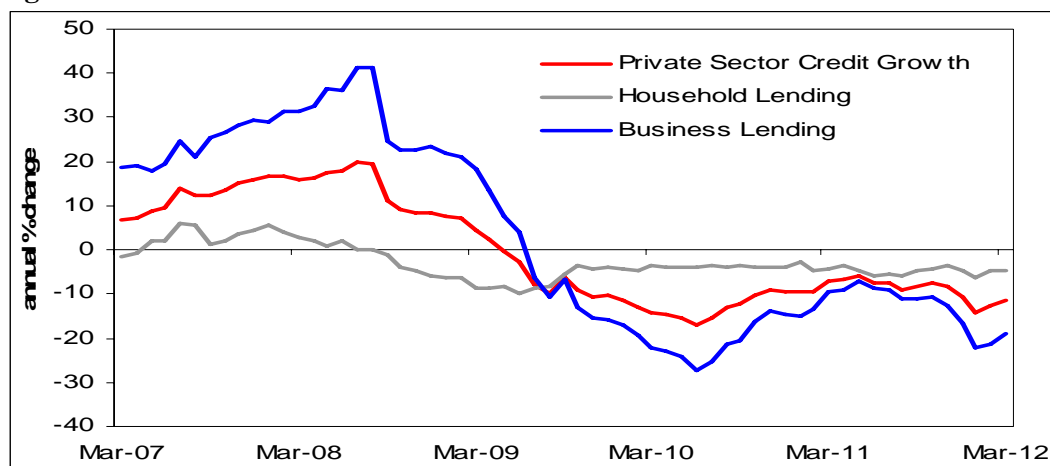


Source: NRBT Monetary Policy Statement, March 2012

5.3 Private Sector Credit Growth

Total private sector credit growth in the banking system continued to contract in the past six months to March 2012. Credit growth slowed to a negative 11.5 percent in the year ended March 2012 compared to the 8.4 percent fall in the year ended September 2011. Lending to the business sector declined by 19.0 percent mainly to wholesale and retail sector in the year ended March 2012 compared to 11.1 percent decline in the year ended September 2011. Household credit also fell by 4.8 percent in the year ended March 2012 similar to 4.8 percent fall year on year to September 2011. However, the overall credit growth to the private sector would have fallen by 7.0 percent during the year ended March 2012 when the on-lent amount of the loan from the People's Republic of China for the reconstruction of buildings destroyed by the 2006 civil unrest is included.

Figure 26 - Private Sector Credit Growth



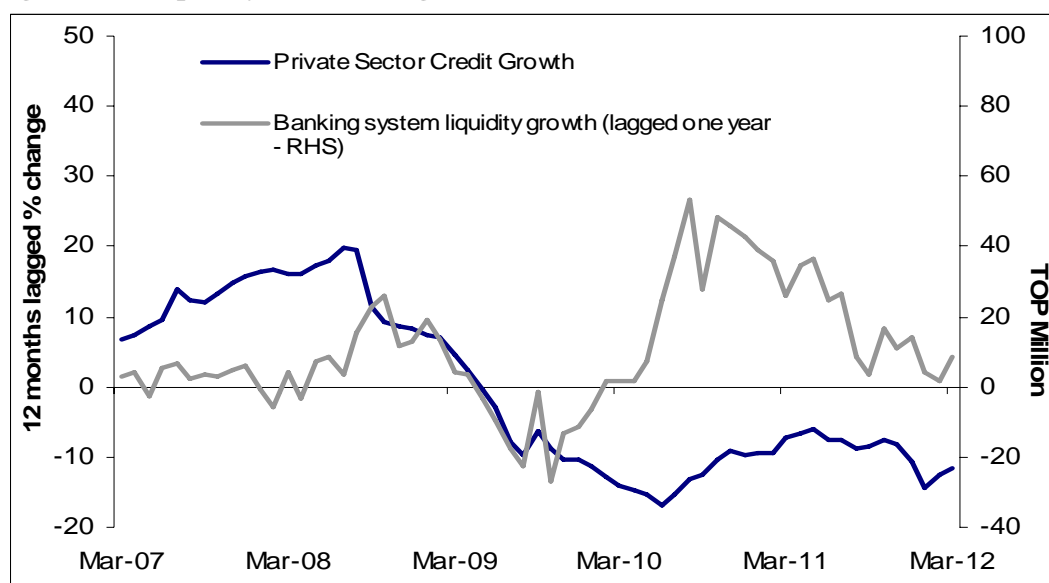
Source: NRBT Monetary Policy Statement, March 2012

The overall negative growth in private sector credit reflected the one off settlement of large private loans, the competition from the Government Retirement Fund small loan scheme, the lending by the South Pacific Business Development (SPBD) Microfinance Ltd, the slow economic recovery and the write off of bad loans. The banks' tight credit criteria continued to affect private sector credit growth, at the same time, domestic demand for credit has been suppressed by the continuing decline in cash remittances over the past 4 years.

At the end of March 2012, of the total private sector credit, 53 percent was lent to the household sector and 46 percent to the business sector. Lending by the banking system to the household sector has been mostly directed to housing while lending to the business sector was mostly directed to the wholesale and retail sector.

The net credit position of government with the banking system continued to improve in the six months to March 2012, reflecting the current effort of government to build up reserves as well as the receipt of funds from Tonga's development partners.

Figure 27 - Liquidity and Lending Growth



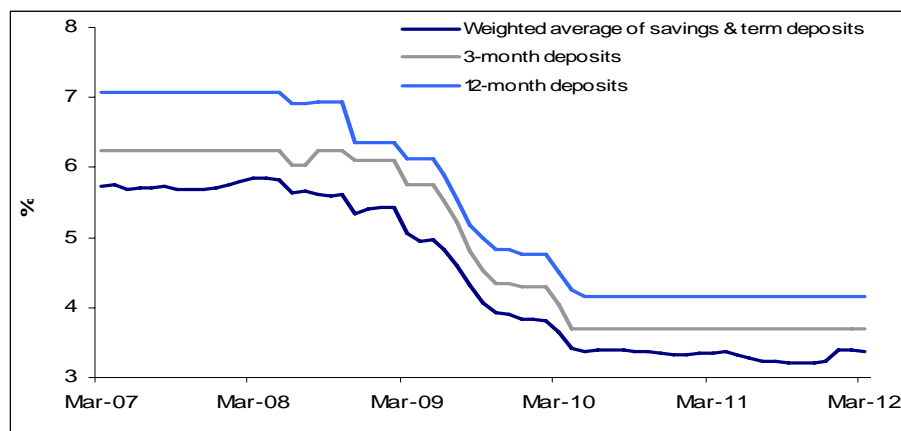
Source: NRBT Monetary Policy Statement, March 2012

5.4 Interest Rates

Interest rates on deposits and loans have remained unchanged in the past six months to March 2012.

The 3-month and 12-month term rates remained at 3.70 percent and 4.17 percent respectively. However the commercial banks' weighted average interest rates for deposits on 3 to 48 months increased from 3.89 percent in September 2011 to 3.96 percent in March 2012 as depositors moved from 3 months out to longer term investment. At the same time, the weighted average interest rates on saving deposits increased to 1.82 percent in March 2012 from 1.56 percent in September 2011 due to the fall in total saving deposits. TDB has just recently announced a small cut in its lending rate.

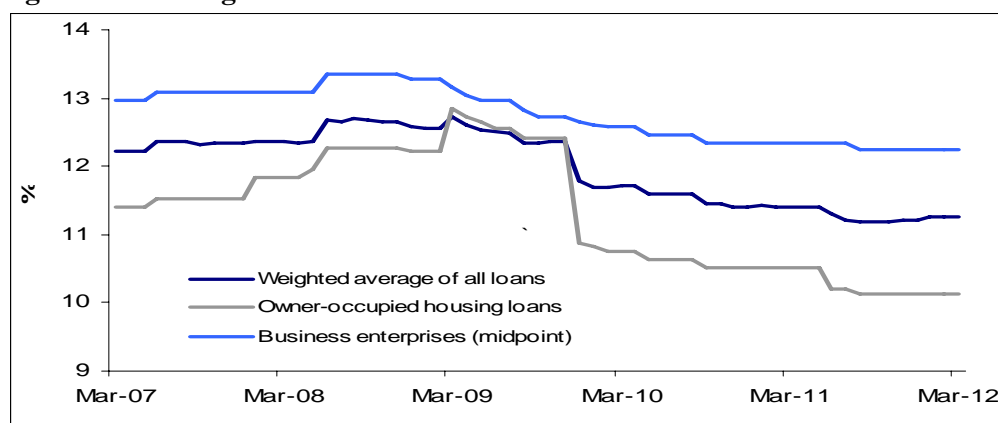
Figure 28 - Deposit Rates



Source: NRBT Monetary Policy Statement, March 2012

The lending indicator rate, a weighted average of interest rates across household and business lending, increased by 8 basis points (bps) to 11.26 percent in March 2012 from 11.18 percent in September 2011. This reflected the decline in outstanding loans to these sectors. The average business lending rates remained unchanged at 12.26 percent. The average lending rates for owner-occupied housing and other personal loans also remained unchanged at 10.13 percent and 14.51 percent respectively.

Figure 29 Lending Rates



Source: NRBT Monetary Policy Statement, March 2012

5.5 Outlook

Liquidity in the banking system will continue to remain high in the next six months given the slow economic recovery and the anticipated receipts of foreign aid inflows.

Credit growth to the private sector is projected to remain negative in the next six months while the total credit growth in the banking system is expected to slightly pick up on the back of new loans to public enterprises. The overall credit environment of the country will continue to be affected by the weak economic condition prevailing in Tonga, the impact of the economic growth slowdown in Australia and the continuing slow economic recovery in the United States.

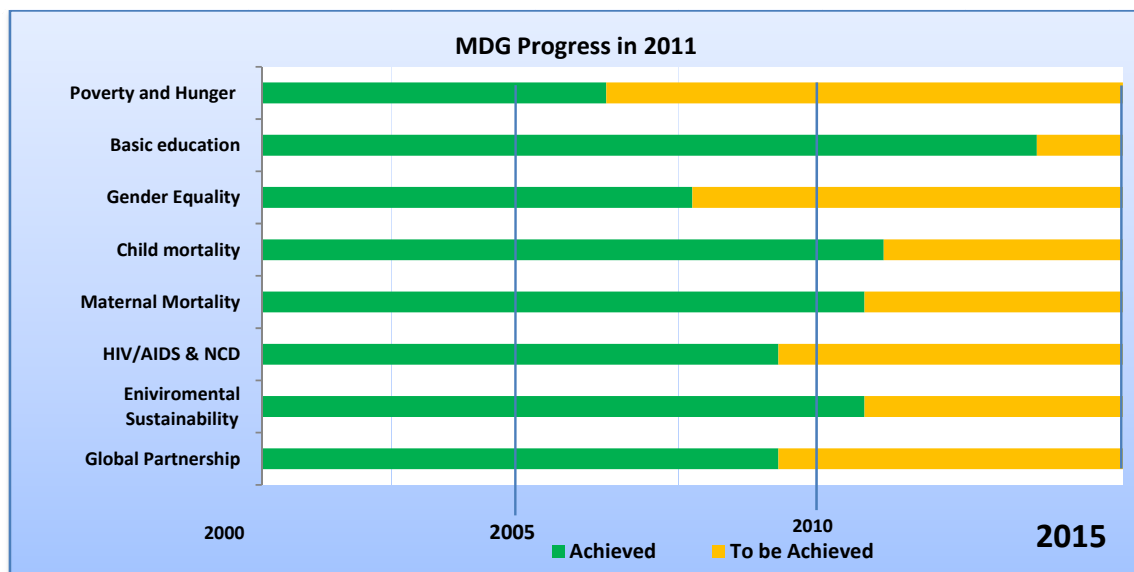
6 Social and Community Progress

6.1 Tonga's status and progress towards Millennium Development Goals (MDGs)

The government welcomes the progress against the eight MDGs overarching goals for Tonga and the contribution made by the Tonga MDG Taskforce. Substantial development and progress is being made on MDGs 2, 4, 5, 6, 7 and 8, with mixed result on MDG1 and 3, and off track on MDG 6c.

Government continues to implement development strategies to provide the final push on the lagging MDGs meant to be achieved by 2015, and recognizes the need for strengthened political commitment and sufficient sustainable resources.

Figure 30 - MDGs progress in 2011



Source: Tonga 2nd Status Report – MDG, 2010

Tonga's progress in attaining the MDG is based on the following:

- recently completed MDG assessment report
- MDG mainstreamed into National Planning Framework TSDF, and Corporate Plan of related line ministries
- support and ownership from Government and Civil Society for the achievement of MDGs.

6.1.1 Changing demographics in Tonga

The recent population Census highlights two important demographic issues for the attainment of the MDGs:

1. Young population
2. Relatively high mortality rates

These issues continue to put pressure on services available to the rural areas around Tonga. Rural-to-urban migration has put more pressure on urban infrastructure, while resources for rural social services have been reduced.

The large number of young people joining the labour force each year is an issue of growing concern. A lack of employment opportunities has created some social challenges around urban areas in Tonga which associated with overseas migration is creating increased social stresses. At the same time the loss of skilled personnel, in particular in health and education to international migration is affecting the provision of services across much of government.

Government increasingly recognizes the need to improve data and analysis related to the impact of demography and migration, both short and long term, on economic and social development. Establishing the Statistics Department as a Bureau of Statistics is part of this process for improving data. Greater attention to these issues is also being considered in the formulation of the MDGs Acceleration Plan 2012 -2015.

6.2 Education Performance

Education in Tonga is compulsory from age six to fourteen years old (but will soon be amended to eighteen years). Government has fully funded the public education institutions such as the Early Childhood Education (ECE), most Primary Schools, some Secondary Schools, and post-secondary institutions such as the Tonga Institute of Education (TIOE) and Community and Development Training Centre (CDTC). Such a move has given every child and young person opportunities to access primary education at almost no cost.

As was reported on the 2006 Census, Tonga literacy rate was estimated at a record high of 98.6 % which supports the good access to basic education in Tonga. This result, however, was challenged through the TSDF 2011 review which estimated a lower level, hence the recommendation to obtain a more accurate result for analysis.

Table 16 : Enrolment in Primary and Secondary Education

	2009	2010	2011p
Primary School	16,719	16,848	16,923
Secondary School	14,676	14,777	14,874
Total Enrolment	31,395	31,625	31,797

Source: Annual Report, Ministry of Education, Women Affairs and Culture

Total primary and secondary school enrolments have increased slightly over the past three years averaging 31,300 students between 2009 and 2011 as showed in *Table 16*. This includes government and non-government schools. Non-government schools educate 11% of the primary students and 64% of the secondary students in 2010. The ratio of girls to boys in primary and secondary schools is about equal.

2011 preliminary figures indicate: the proportion of students started Grade 1 was 60%; the achieving rate for those who go on to the last grade was 96%; and the repetition rate was 21%. However there is a room for improvement given enrolment at Early Childhood Education (ECE) and post-secondary education levels. It is expected that the result for the next five years will be better. There is a major concern regarding the rising number of school-aged children who are dropping out and not attending school due to varieties of reasons including parents' lack of commitment to education and financial hardship.

In the past three years it is estimated that teacher to student ratio was 1:24 for primary education and 1:14 for secondary education. The government through the Ministry of Education, Women Affairs and Culture (MEWAC) recruited more staff to provide cover for those staff that are on leave and assist in classes which are overloaded. Upgraded training is provided for teachers from the non government education systems to ensure that they have the attributes required of “Faiako Ma’a Tonga” and hence qualified to teach in Tongan schools. Grants to such schools have been increased in 2011/2012 from T\$200 to T\$400 per head to assist the non-government education systems to recruit and retained suitably qualified teachers. Nevertheless, there are over 200 untrained teachers in these systems and it will require at least three to four years for all of them to be trained. In coming years, all teachers must be qualified before they can register.

Curriculum reform is under review and development of curriculum for primary education (Class 1 to Form 2), ECE ages 4 and 5, secondary education (Form 3 to 7) and post secondary education are expected to be complete in the next five years.

The Minimal Service Standards (MSS) used to assess school performance in four main areas:

- (i) Students Achievement,
- (ii) Teacher’s Competencies,
- (iii) Teaching and Learning Environments
- (iv) Administration and Management

Providing adequate maintenance and upgrading of facilities in all schools at all levels and building new ones to meet emerging demands, and improving teaching and learning resources in schools remains problematic. Government continues to seek development support to help cover these needs.

6.3 Health Performance

The final phase of Vaiola Hospital, funded by Japan, was commissioned in May 2012 which will permit major progress in health delivery. Super health centers have been established and funded by China for the towns of Vaini and Mu’a. Health Centers at Nukunuku, Kolonga and Houma were refurbished with funds from AusAID. There is also a newly developed Non Communicable Disease (NCD) clinic build in Niu’eiki Hospital, ‘Eua. This centre was funded by Government of Japan (JICA).

Health facilities are accessible throughout Tonga. In per 100,000 populations, there are 406 nurses and midwifery personnel, 44 medical doctor in 2011 and 21 health offices in 2010.

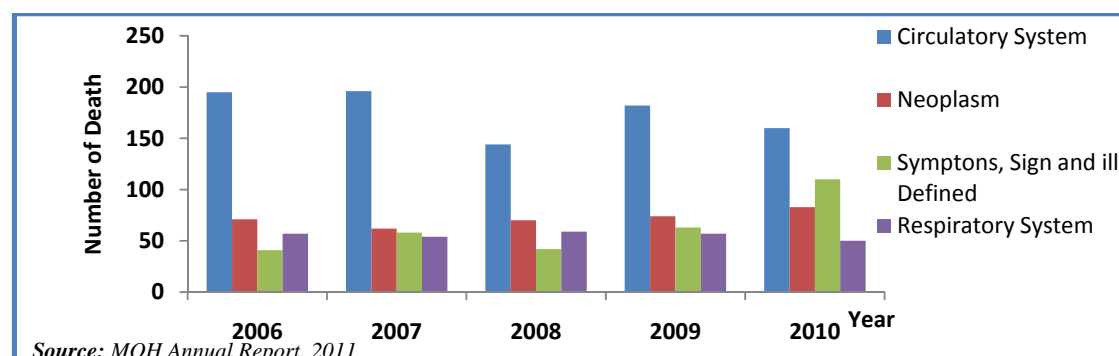
Table 17 : Key Health Indicators

Health Indicators	2008	2009	2010
Life Expectancy at birth			
Male	70	70	65
Female	72	72	69
Infant Mortality Rate (<i>per 1,000 live births</i>)	11.7	17	21.5
Crude Death Rate	5.2	5.5	5.3
Maternal Mortality Ratio (<i>per 100,000 per live births</i>)	36.5	114.4	37.1

Source: MOH, Annual Report, 2010

Reports released by the Ministry of Health show that between 2009 and 2010 the average life expectancy in Tonga has fallen from 70 to 65 for men and 72 to 69 for women. The decrease in life expectancy for adults is mainly due to the increase in fatalities caused by non-communicable diseases such as circulation problems. Failure of the circulatory system is a major cause of mortality in Tonga in the past six years.

Figure 31 - Leading Causes of Mortality in Tonga, 2006-2010



The infant mortality rate was recorded at 21.5 per 1,000 live births in 2010, which is a slight increase on preceding years. Neonatal mortality rate was 10.4 per 1,000 live births in 2010 compared to 22.4 per 1,000 live births in 2009. In the same year the Adult mortality rate was 187 per 1,000 populations (*WHO, 2011*). The crude death rate is 5.3 and maternal mortality ratio is very low varying from 114.4 per 100,000 live births in 2009 to 37.1 per 100,000 live births in 2010 (*MOH Annual Report 2010*). The under 5 mortality rate has fallen from 20 per 1,000 live births in 2000 to 19 in 2009 (*WHO, 2011*).

Although there are no deaths due to HIV/AIDS in Tonga and it continues to remain low, there were two live cases of HIV/AIDS detected in 2010 since the first record of 18 cases in 1987. Tonga is now able to test for Sexually Transmitted Infections (STIs) in the laboratory at Vaiola Hospital and total of 498 people mostly occurred in 16-30 age groups (*MOH Annual Report, 2010*). Although HIV numbers in Tonga are low compared to other more prevalent countries, the high numbers of STIs are worrying as STIs can also facilitate the acquisition and transmission of HIV/AIDS. More health education targeting behaviour change amongst adolescents and young people to reduce risk behaviour will be needed.

Advances in health indicators testify to Tonga's effective primary health care delivery, public health infrastructure and the importance of comprehensive antenatal and postnatal care, immunization, trained & skilled personnel care attend at all births, water sanitation and waste disposal programmes. Infectious and most communicable diseases are under control, primarily as a result of water and sanitation and successful primary health care.

The strength of the health system and the country's commitment to MDG 4 can also be seen in the consistently high proportion of immunized against infectious childhood diseases and measles. In 2010, a high proportion of 98.5% of children were immunized against infectious childhood diseases, 99.4% immunized against measles and 98.5% of new borns were protected against tetanus. The immunization program is very strong in Tonga and has enabled wide gains in reducing vaccine preventable diseases. This program will help in maintaining a low rate of child mortality over the period relate to socioeconomic development, various child survival interventions and reduced maternal mortality.

Most women give birth at the hospital, or at home with the help of a skilled attendant. Reproductive Health (MOH) encourages women to give birth at the hospital or clinics and emphasize the importance of skilled birth attendants. In 2011, approximately 98% of births

were attended by skilled health personnel. It indicates that very few women give birth with the help of traditional birth attendant (*MOH Annual Report, 2010*). Antenatal coverage is high with 98.5% of pregnant women attended at least one antenatal visits in 2011.

As infectious and communicable diseases have been brought under control, non communicable diseases have increased and now constitute a major public health challenge. In 2010, 60% of total deaths (326 out a total of 553) in Tonga died from NCDs. Tonga has joined the rest of the Pacific Island countries in declaring that NCD is in a crises situation. Apart from the fact that it is the leading cause of mortality in every country, it also reduces quality of life, increases disability and imposes significant financial burden on health system especially due to its chronic nature. Tonga is amongst the top 10 ranked countries of the world in terms of prevalence of diabetes (*MDG 2nd Report, 2010*). Based on these depressing conditions, Tonga has developed its National Strategy to prevent and control NCD's, focussing on the four main risk factors that cause NCDs, which are: smoking, unhealthy eating, lack of exercise and alcohol.

The Tonga/Australia partnership in health project is one of the successful partnerships between Tonga and its development partners, in collaboratively working together to tackle this NCD challenge head on, with actions aimed at strengthening primary and secondary health prevention programs order to successfully reduce incidence of NCD's in sustained way.

6.4 Poverty Reduction and Social Protection

The Asian Development Bank and the Japan Fund for Poverty Reduction (ADB/JFPR) grant project aims to assist the government in improving socioeconomic opportunities for the vulnerable population to alleviate the impact of recent economic crises, and building capacity to develop and implement effective safety net programs. The project consists of the three main components: **Component A:** support for disadvantaged women with access to microfinance, and social assistance services for other vulnerable groups; **Component B:** public consultations and capacity development and design social programs for the most vulnerable; and **Component C:** a regional knowledge sharing workshop on social safety net programs. The total grant amount allocated for Tonga is US\$900,000.

A joint effort between the ADB/JFPR Project Management Unit and the Government of Tonga resulted in a social service design for the Elderly and the Disabled, integrating services and oversight provided by NGOs, Churches, and Government. The pilot social services will be implemented by July 2012 and run for twelve to eighteen consecutive months. The budget for social services to the elderly and disabled is estimated at TOP\$300,000 per year.

The ADB/JFPR Project Management Unit and the Government of Tonga is working with the Tonga Development Bank to design a Micro-finance loan product that will favour the most vulnerable individuals and groups residing in village communities throughout Tonga. The goal of the product is to create income generating opportunities and increase financial literacy and experience for the most vulnerable. This joint effort between Government and Development Partners strives to create a micro-finance loan product that has a robust training component, an interest rate that is substantially lower than the current market rates, low or no fees, no collateral, grace period of up to three months, and mandatory savings. The Pilot Micro-loan product will be available on July 2012 and will run for twelve to eighteen consecutive months. The budget for Pilot micro-finance loan product for the most vulnerable is estimated at TOP\$400,000 per year.

ANNEX III: FISCAL REVIEW

1 Government Financial Development

BUDGET THEME: "Creating Opportunity in Extraordinary Times"

1.1 Overview

On a GFS basis, the Government's overall fiscal balance for 2012/2013 is estimated at a surplus of \$1.2 million. This represents an improvement from the \$23.7 million deficit estimated outturn in 2011/2012.

Total expenditure and net lending will decrease by \$22.6 million over 2011/2012 outturns. This is driven by falling in total expenditure associated with the China EXIM bank loan, which lead to a decrease in total expenditure by \$13.9 million to \$216.1 million from the \$230.0 million estimated outturn 2011/2012.

Total revenue and cash grants¹⁷ will increase by \$2.3 million from the 2011/2012 estimated outturn. This increase is driven by increase in grant (which include project grants and budget support) of \$2.2 million. Government tax revenue projected for 2012/2013 will reach \$127.7 million, an increase of \$3.1 million compared to the estimated 2011/2012 outturn. Budget support is lower by \$14.6 million compared to the 2011/2012 estimated outturn.

Preliminary data indicates that Government will generate a total budget deficit of \$23.7 million for 2011/2012 compared to a surplus of \$1.2 million projected at budget time for 2012/2013. This result was due to higher-than-expected capital expenditure associated with China EXIM projects.

Table 18 shows the Government's overall fiscal position using the Government Financial Statistics (GFS).

Table 18 - Overall Fiscal Balance (\$million)

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Total Revenues and Grants	203.8	206.7	215.5	217.8
Total Revenues	151.0	139.3	149.3	149.3
Grants	29.2	39.5	29.2	46.0
Budget Support	23.6	27.9	37.1	22.5
Total Expenditure and Net Lending	261.1	232.1	239.2	216.6
Total Expenditure	249.9	214.4	230.0	216.1
Net lending	11.2	17.7	9.2	0.5
Total Budget Balance	(57.3)	(25.4)	(23.7)	1.2
Total Financing	57.3	25.4	23.7	(1.2)
External financing	65.5	25.4	43.5	(1.2)
Domestic Financing	(8.2)	-	(19.9)	0.0

Sources: Ministry of Finance and National

¹⁷ This version of the GFS format does not include in-kind grants, only in-kind loans because they affect the total financing. In-kind grants would increase total expenditure and total revenue by the same amount leaving the balances unchanged.

Box 1: Government Domestic Payments and Receipts

The Budget Statement is presented on a GFS basis to meet international standards. GFS presentation combines all Government revenue and expenditure from different sources to ensure comprehensiveness. Expenditure and revenues associated with recurrent Government operations and donor projects are combined. Expenditure associated with China EXIM Bank debt-financed projects is also shown.

The following table, however, shows only the portion of the budget under the direct control of Government. While, historically, the term expenditure and revenue have been used, these are slightly different to how they are recorded in the GFS. Repayment of debt is treated as “expenditure” and drawdown of loans as a “revenue”, while in the GFS these are recorded under financing. Total Government controlled expenditure and revenue is thus better called payments and receipts to avoid confusion with the terms under the GFS. Government cash payments are financed by its cash receipts which include general revenue, domestic loan drawdowns and budget support.

Government Cash Payments and Receipts

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est. Outturn 2011/12	Budget Estimate 2012/13
Total Payments	177.5	170.9	170.2	179.9
Wages and Salaries	98.8	92.5	92.4	95.9
Purchase of Goods and Service	20.2	19.1	18.5	21.1
Debt Management	25.0	20.9	18.9	23.7
Other	36.5	38.4	40.4	39.2
Total Receipts	185.7	170.9	190.1	179.9
Government Receipts	162.1	143.0	153.0	157.4
Budget Support	23.6	27.9	37.1	22.5

NOTE: Wages and Salaries of \$95.9 million includes all expenditure items under category 10 (Establish Staff Expenses) a total of \$93.4 million and category 11 (Unestablished Staff Expenses) a total of \$2.5 million.

NOTE: Payments include expenditure plus repayment of debt, while Receipts include revenue, budget support and domestic loan drawdowns.

The table above shows that payments during 2011/12 remained very close to original budget estimates. Receipts exceeded original budget estimates by \$19.2 million, largely due to strong performance in tax revenues and the receipt of budget support from EU which was expected for 2010/11. Total Government recurrent payments is expected to increase by \$9.9 million, or 6 percent, during 2012/13 to meet cost pressures in priority areas. Expenditure on wages and salaries, however, will increase by less than 4 percent, reflecting Government commitment to reduce the proportion of payments allocated to payroll expenditure. Government is committed to a balanced cash budget during 2012/13 thus leaving cash balances unchanged

2 Revenue and Grants

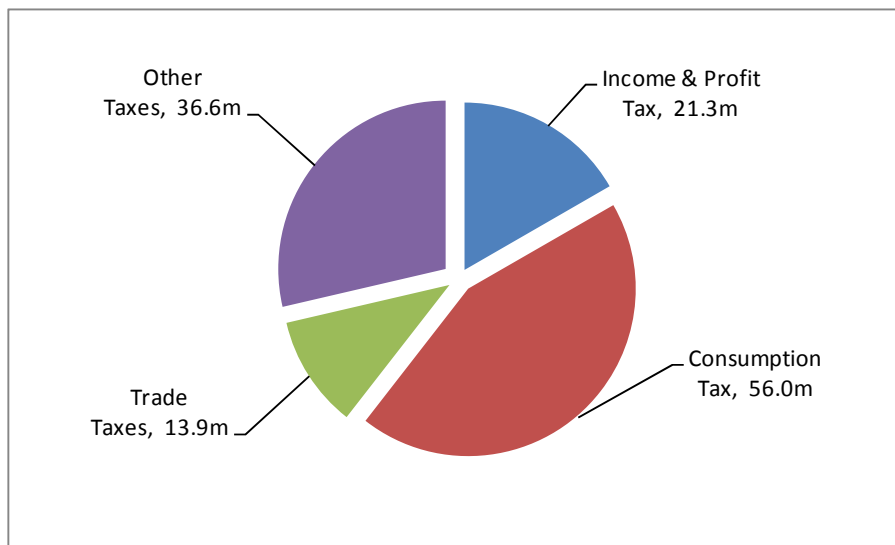
Total revenue and grants are estimated at \$217.8 million for 2012/2013, which is \$2.3 million more than the estimated outturn of \$215.5 million in 2011/2012. Tax revenues are expected to increase by \$3.1 million and grants are expected to increase by \$2.2 million compared to the 2011/2012 outturns. Budget support, is \$22.5 million which is lower by \$14.6 million than the 2011/2012 estimated outturn. *Table 19* sets out the detail components of revenue and grants estimates.

Table 19: Total Revenue and Grants (\$million)

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Total Revenues and Grants	203.8	206.7	215.5	217.8
Total Revenues	151.0	139.3	149.3	149.3
Current Revenue	149.1	137.7	147.7	147.0
Tax Revenue	133.0	114.5	124.6	127.7
Income & Profit Tax	38.3	21.2	21.9	21.3
Consumption Tax	49.6	49.4	54.4	56.0
Trade Taxes	12.7	12.6	13.7	13.9
Other Taxes	32.4	31.3	34.7	36.6
Non-Tax Revenue	16.1	23.2	23.1	19.3
Capital Revenue	2.0	1.6	1.6	2.3
Grants	52.8	67.4	66.3	68.5
Project Grant	29.2	39.5	29.2	46.0
Budget Support	23.6	27.9	37.1	22.5

2.1 Tax Revenues

Tax revenues are expected to slightly improve by \$3.1m or 2.5% from the estimated outturn in 2011/2012. The following pie-chart depicts the contribution of tax revenue components to the increase.

Figure 32 - Tax Revenue 2012/13 (\$millions)

Source: Ministry of Finance & National Planning

Note: Other Taxes comprise– Tax on Property, Excise, Business and Property Licenses, Motor License and Registration, Other taxes on use of goods and services.

2.2 Taxes on Income & Profits

Taxes on Income & Profits for 2012/2013 are estimated at \$21.3 million. This is a decline of \$0.6 million from the 2011/2012 estimated outturn. Strengthened compliance is expected to support Corporate Tax revenue increases of \$0.4 million or 4.5%. These gains, however, will

be more than offset by declines in PAYE and Arrears collection. Arrears collections are expected to continue to decline, following successful efforts in improving compliance and recover arrears during the past two years. The following table portrays the components of taxes on Income & Profit.

Table 20: Taxes on Income & Profits (\$millions)

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
PAYE	11.73	9.40	11.25	11.10
Corporate tax	11.86	8.41	8.80	9.20
Tax Debts Recovered (Corporate)	14.76	3.40	1.83	1.00
TOTAL	38.35	21.21	21.88	21.30

Source: Ministry of Finance & National Planning

2.3 Consumption Tax

Consumption tax for 2012/2013 is estimated at \$56.0m showing an increase of \$1.6 million or 3% from the estimated outturn 2011/2012. Strong ongoing domestic and import consumption tax performance is driven by improved compliance, the stimulus provided by donor project expenditures and increased household consumption spending following the introduction of the retirement loan scheme.

Table 21: Consumption Tax (\$million)

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Consumption Tax - Import	44.9	43.5	45.9	47.7
Consumption Tax - Domestic	4.3	5.0	6.0	7.0
Government Consumption Tax	0.3	0.3	1.8	0.3
Tax Debts Recovered (CT)	-	0.6	0.6	1.0
Total	49.6	49.4	54.4	56.0

Source: Ministry of Finance & National Planning

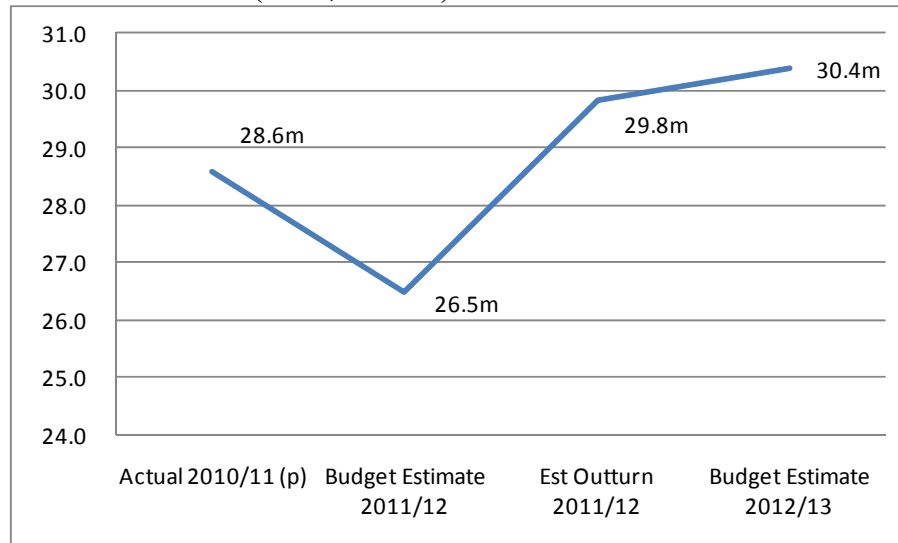
2.4 Excise Taxes

Excise tax is estimated to pick up in 2012/2013 by \$0.6 million as compared to the estimated outturn 2011/2012. This increase reflects the changes in excise tax on imports tobacco from \$200 to \$210 per 1,000 sticks/kg.

Table 22: Excise Taxes (\$million)

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Excise Tax	28.6	26.5	29.8	30.4
Excise Tax - Government	0.0	0.0	0.0	0.0
Total	28.6	26.5	29.8	30.4

Source: Ministry of Finance & National Planning

Figure 33 - Excise Taxes (TOP\$ Million)

Source: Ministry of Finance & National Planning

2.5 Trade Taxes

Tax on imports for 2012/2013 is expected to be slightly higher than the estimated outturn 2011/2012 by \$0.2 million. This increase is in line with the improvement of compliance.

Table 23: Import Taxes (\$million)

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Trade Taxes	12.7	12.6	13.7	13.9
Other Trade Taxes	-	-	-	0.0
Total	12.7	12.6	13.7	13.9

Source: Ministry of Finance & National Planning

2.6 Non-tax Revenues

Non-Tax Revenue is expected to decrease in 2012/2013 by \$3.8m or 16.5% from the estimated outturn 2011/2012 as shown in *Table 24*. This fall is mainly from declining in revenues expected from Entrepreneurial & Property Income and Administrative Fees and Charges.

Table 24 : Non-tax Revenue component

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Entrepreneurial and Property Income	3.3	7.6	7.6	5.9
Administrative Fees and Charges	11.2	15.1	15.1	13.0
Fines and Forfeits	0.6	0.5	0.5	0.5
Other Non-Tax Revenue	1.0	0.0	0.0	0.0
TOTAL	16.1	23.2	23.1	19.3

Source: Ministry of Finance & National Planning

2.6.1 Entrepreneurial & Property Incomes

The reduction on dividends estimated for 2012/2013 reflects the impact of the competition in the telecommunication sectors, which reduces the profitability of the Tonga Communication Corporation (TCC) and lower dividend expected from Public Enterprises as shown in *Table 24 and Table 25*.

Interest earnings, Forum Fishing Agency (FFA) Treaty receipts, and Land Rentals are also expected to decline.

Table 25: Entrepreneurial & Property Income (\$ millions)

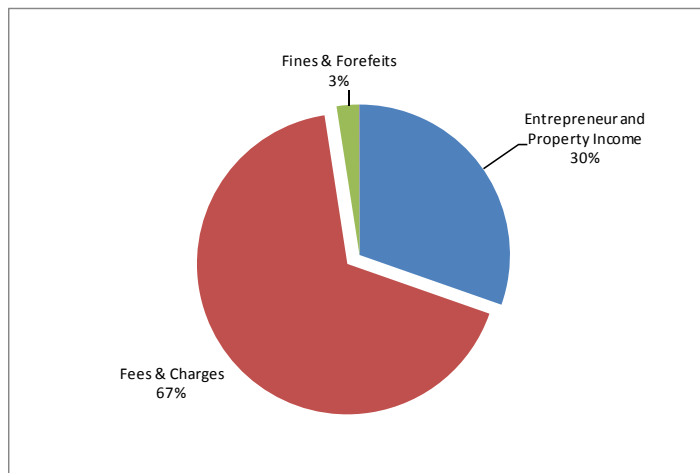
	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Interest	0.39	0.32	0.32	0.28
Dividends	2.42	6.52	6.52	4.95
FFA Treaty	0.10	0.35	0.35	0.30
Land Rental	0.37	0.37	0.37	0.33
Total	3.28	7.55	7.55	5.86

Source: Ministry of Finance & National Planning

2.6.2 Administrative fees & charges

Administrative fees and charges are projected to decline by \$2.1 million in 2012/2013 to \$13.0 million compared to 2011/2012 estimated outturn. Declines in telecommunication settlement fees account for the majority of the decrease of revenue estimated to be collected from administrative fees and charges.

Figure 34 - Administrative Fees & Charges (\$millions)



Source: Ministry of Finance and National Planning

Note: Other non-tax: sundry revenue.

2.7 Capital Revenue

Capital revenue is estimated at \$2.3 million for 2012/2013 illustrating a \$0.7 million increase from \$1.6 million in 2011/2012 estimated outturn. The increase is due to payment of on-lent interest from sub-borrowers to Government. No government asset sales are planned for 2012/2013. The planned sale of the Tonga Print Limited has been delayed, with all bids falling below the reserve sale price.

2.8 Total Grants for 2012/13

2.8.1 Project Grants

Total Project Grants (cash) are expected to increase by \$16.8 million or 57.5 % relative to 2011/2012 estimated outturn as compared to 2012/2013. This increase is attributable to increased donor assistance and other projects still on-going from previous years.

Australia, New Zealand and European Union are the primary sources of grant assistance. Major projects included are: the ongoing implementation of the Tonga Health Support Program, Tonga Education Sector Project (TESP), building of the Niatoputapu Hospital, Tonga Vocational Educational Training (TVET) bilateral assistance, Tonga Police Development Program (TPDP) and upgrading of the Tonga villages network.

2.8.2 Budget Support

Table 26 : Budget Support for 2010/2011 – 2012/2013

Donor Countries	Actual	Budget	Est Outturn	Budget
	2010/11 (p)	Estimate 2011/12		Estimate 2012/13
Aust Fund (Budget Support)	3.7	4.0	8.9	9.0
New Zealand Fund (Budget Support)	1.9	2.5	-	2.5
Asian Development Bank (ADB) (Budget Support)	8.5	-	-	-
World Bank Budget Support	9.5	8.7	15.4	8.5
EU Budget Support	-	12.8	12.8	2.5
TOTAL	23.6	27.9	37.1	22.5

Sources: Ministry of Finance and National Planning

The increase in budget support from the original estimate for 2011/2012 of \$27.9 million to \$37.1 million estimated outturn is mainly due to time lag in receipt of budget support from 2010/2011 and exchange rate fluctuations. Budget Support is expected to decrease by \$14.6m from \$37.1 million estimated outturn 2011/2012 to a budget estimate 2012/2013 of \$22.5 million.

3 Expenditure and Net Lending

3.1 Total Expenditure and Net-Lending

The government's overall expenditure and net lending for the financial year 2012/2013, as classified on a GFS basis, amounted to \$216.6 million. This comprised Total Expenditure of \$216.1 million and a net lending of \$0.5 million. Decrease in total expenditure and net lending by \$22.6 million from the estimated outturn in 2011/2012 of \$239.2 million is mainly driven by the completion of related China EXIM construction projects.

Table 27: Total Expenditures & Net Lending (\$millions)

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Total Expenditure and Net Lending	261.1	232.1	239.2	216.6
Total Expenditure	249.9	214.4	230.0	216.1
Current Expenditure	175.5	185.1	181.1	201.4
Wages and Salaries	91.8	85.5	87.3	90.0
Contr to Retire. Fund	9.1	9.3	9.2	9.0
Other Purchases of G&S	50.8	65.6	61.0	75.5
Interest Payment	6.5	6.8	6.8	7.0
Subsidies & Transfers	17.4	17.9	16.8	19.9
Capital Expenditure	74.4	29.3	48.9	14.7
<i>in which; Chinese EXIM Bank loan</i>	60.4	16.2	41.2	5.1
Net lending	11.2	17.7	9.2	0.5
<i>in which; Chinese EXIM Bank loan</i>	11.05	15.8	8.7	-

Source: Ministry of Finance & National Planning

NOTE: 1. Wages and Salaries comprises of some expenditure items in category 10, 11 and 14 plus donor expenses. 2. Contribution to Retirement Fund comprises of transfer value and established staff contribution to retirement fund.

3.2 Current Expenditure

Current expenditure is expected to increase in FY2012/2013 by \$20.3 million from the 2011/2012 estimated outturn. The majority of this increase results from projected increases in goods and services purchases associated with donor projects and wages and salaries to cover annual performance increment. Others were also increased but not as significant as wages and salaries, and other purchase of goods and services. Current expenditure associated with donor projects is projected to increase in 2012/2013, in comparison to 2011/2012 outturns due to lags in project implementation.

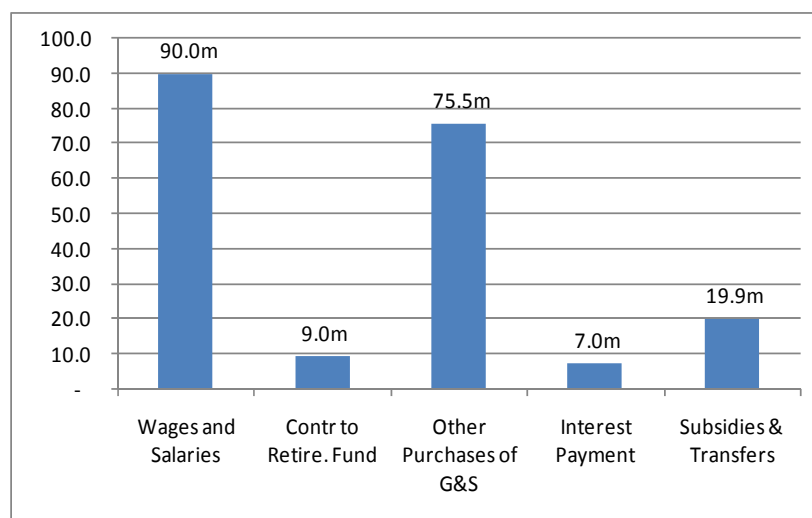
Figure 35 - Total Current Expenditure for FY 2012/13

Figure 35 shows 2012/2013 current expenditure across the five major expenditure groups. Other purchases of goods and services account for the second largest growth in proportion to total expenditure. Wages and salaries continue to account for the largest proportion of the overall budget.

3.2.1 Wages & Salaries

Expenditures on wages and salaries for financial year 2012/2013 are budgeted at \$90.0 million, representing a \$2.7 million or 3% increase from the estimated outturn in 2011/2012. Of this \$90.0 million, \$88.1 million is funded by government and \$1.9 million from donor funded projects. Ninety percent of salary expenditure is allocated to established staff. This proportion has increased slightly from 2011/2012 reflecting the impacts of the annual increment.

The government has set a financial baseline target for salary and wage expenditure at 45% of total government funded expenditure. This target is to be achieved within the next two years. This ratio stood at 39.9% in 2011/2012 and has increased slightly to 41.6% in the 2012/2013 budget. Wages and salaries have not decreased in nominal terms but their share of the budget is declining as growth occurs at a slower rate than overall expenditure growth.

Table 28: Wages and Salaries 2010/11 – 2012/13

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Salaries	81.4	76.6	75.8	80.1
Overtime	1.4	1.6	2.0	1.6
Wages	2.2	1.9	2.1	2.2
Contract Labour and Temporary Staff	0.1	0.1	0.2	0.3
District and Town Officers Salaries	1.8	1.2	1.2	1.2
Privy Purse	0.3	0.3	0.3	0.4
Others	4.5	3.8	5.6	4.2
TOTAL	91.8	85.5	87.3	90.0

Source: Ministry of Finance & 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 contain the wage bill in the future through restraint in civil service expansion and salary increases.

3.2.2 Government Contributions to Retirement Fund

As of July 2012/2013, Government contributions to retirement fund now including Tonga Defence Services is equal to 10% of established staff salaries towards retirement savings. This contribution is estimated at \$9.0 million in the 2012/2013 budget which consist of \$7.1 million for contributions to the Retirement Fund and a \$1.9 million of the old scheme as transfer value.

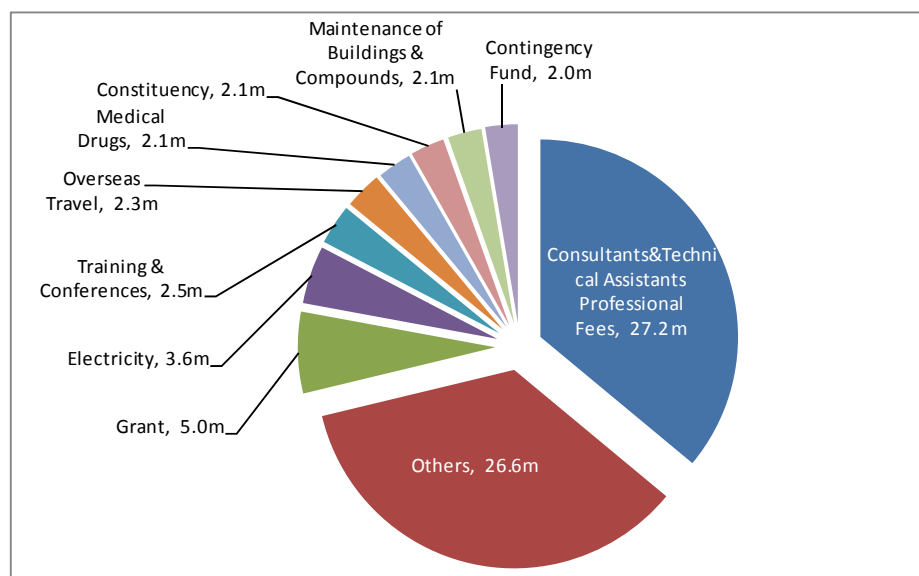
3.2.3 Purchases of Goods & Services

The purchases of goods and services budget for 2012/2013 increased to \$75.5 million representing a 23.8% increase from the estimated outturn in 2011/2012. Of the total \$75.5 million for purchases of goods and services, \$34.9 million is funded from donor assistance and \$40.6 million from government. Other purchases of goods and services are expected to increase as a share of expenditure, which represents important progress towards rebalancing expenditure away from wages and salaries.

The major areas of increase in the 2012/2013 budget compared to the 2011/2012 outturn are consultants & technical assistants' professional fees \$27.2 million; medical drugs \$2.1 million, contingency fund \$2.0 million; maintenance of buildings and compounds \$2.1

million; constituency \$2.1 million; overseas travel \$2.3 million; training and conferences \$2.5 million; electricity \$3.6 million and grant \$5.0 million.

Figure 36 - Major expenditure items under Purchase of Goods & Services



Source: Ministry of Finance & National Planning

NOTE: Others includes rental, rations and diets, office supplies, domestic travel, maintenance of roads, printing and stationery, national retirement fund, street lighting.

3.2.4 Interest payments

Interest payments are estimated at \$7.0 million for 2012/2013, a 3% increase from 2011/2012 estimates outturns of \$6.8 million. Interest payments are dominated by servicing of Chinese EXIM Bank Reconstruction and National Roads Development Loans. Further details are provided under the Public Debt Section.

3.2.5 Subsidies & Transfers

Expenditure on subsidies and transfers is estimated at \$19.9 million for 2012/2013. This represents an increase of \$3.1 million from the estimated 2011/2012 outturn of \$16.8 million. Transfers to other enterprises will include \$0.1m for National Economic Development Council and \$0.28 million for the Development Committee. Transfers to nonprofit organizations will include subsidies of \$6.8 million for Tonga Education Sector Project (TESP), electricity, and intra-islands sea and air transportation, \$1.0million for Agricultural Marketing Fund, Grants for Sports activities, Charitable Organizations and Government Development Project Costs are projected to reach \$0.96 million. Transfers to households will include pensions & gratuities, scholarships and allowances of \$7.8 million. Transfers to government and international organizations total \$2.9 million.

3.3 Capital Expenditure

Total Capital expenditure in 2012/2013 will reach \$14.7 million, a decline of \$34.2 million from an estimated outturn of \$48.9 million in 2011/2012. This decline is almost entirely due to falling capital expenditure associated with China EXIM bank loans as for reconstruction of

the Nuku'alofa CBD nears completion. Substantial in-kind grant funded capital expenditure, however, are anticipated from many development partners.

Donor cash capital investment for 2012/2013 is estimated at \$6.6 million, increasing by 76% from 2011/2012 estimated outturn of \$3.7 million. Major donor investments include the European Union-funded construction of Niuatoputapu Hospital \$2 million and the Tonga Police Development Program \$1.7 million; Tonga Post Tsunami \$0.8 million; Niuatoputapu Early Warning Siren System \$0.5m; equipment and furnitures for the Royal Palace \$0.6 million; Tonga Education Sector Project \$0.6 million, Tonga Health Systems Support Programs \$0.6 million; Tonga Tourism Support Program \$0.1 million; and others \$0.1 million. Government Capital expenditure for 2012/2013 amounts to \$2.8 million. This is an increase of \$0.3 million from the estimated outturns in 2011/2012 of \$2.5 million. The major Government-financed capital project is the ongoing construction of the Foa Causeway.

4 Financing

Table 28 outlines the financing transactions of the Budget for 2012/13. The overall fiscal balance for 2012/13 is an anticipated surplus of \$1.2 million which is totally covered by the difference between external loan repayments and drawdowns.

Table 29 : Estimated Financing Transactions (\$million)

	Actual 2010/11 (p)	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Total Financing	57.3	25.4	23.7	(1.2)
External financing	65.5	25.4	43.5	(1.2)
Disbursements	71.4	32.0	49.9	5.1
Chinese EXIM Bank Loan	71.4	32.0	49.9	5.1
Repayments	6.0	6.6	6.4	6.3
Domestic Financing	(8.2)	-	(19.9)	0.0
Disbursement from Bonds Issued / Domestic Loan	10.4	3.0	3.0	7.5
Repayment of Matured Bonds/Loan	10.4	3.0	3.0	7.5
Net Changes in Government Cash Balances and Investment (- deposits, + drawdown)	(8.2)	-	(19.9)	0.0

Source: Ministry of Finance & National Planning

Domestically, the government intends to undertake \$7.5 million in bond issues in 2012/2013 with the purpose of financing a \$7.5 million rollover bonds, scheduled to mature in 2012/2013. This has no net impact on financing.

5 Tax Expenditures

Tax expenditures¹⁸ have the same effect on the budget deficit as appropriations spending. Therefore the information in this section is an important element of the Government's commitment to fiscal transparency.

The total tax expenditure for the financial year 2009/10 was \$18.2 million pa'anga. It represents an increase of 71% over the \$10.6 million pa'anga of tax expenditures recorded in 2009/10. A summary of the value of key concession categories for 2009/10 and 2010/11 is provided in the *Table below*.

Table 30 : Total Tax Expenditure By Type (\$ pa'anga)

Tax Expenditure by Type	2009/10	2010/11
Fisheries fuel concession	426,584	617,160
International aircraft fuel concession	832,551	1,678,981
Domestic aircraft fuel concession	412,830	475,509
Local passenger vessels fuel concession	669,172	669,172
Electricity Generation	5,482,273	6,071,539
Development Projects	2,040,585	8,059,529
Imports for Educational Support	14,220	84,983
Diplomatic concessions	507,618	196,922
Charitable concessions	20,238	27,022
Other concessions	235,640	362,525
Total	10,641,711	18,243,343

Source: Customs Department.

The increase in the total tax expenditure from 2009/10 to 2010/11 is mainly attributable to the increased concessions to development projects (an increase of \$6.0 million pa'anga). This was primarily due to imports for the construction of Nuku'alofa CBD and Vaiola hospital valued at \$7.8 million pa'anga in 2010/11 (an increase of \$6.2 million pa'anga over 2009/10).

Subsidized fuel for electricity generation also contributed to the increase (an increase of \$0.6 million pa'anga). Subsidized fuel for international aircraft increased to \$1.7 million pa'anga in 2010/11 (an increase of \$0.846 million pa'anga). Diplomatic concessions decreased to \$0.197 million pa'anga in 2010/11 (a decrease of \$0.311 million pa'anga).

¹⁸ Tax expenditures represent the revenue losses incurred from various exemptions provided to different groups. Some exemptions are required by international treaty obligations, others are provided to influence social or economic development.

ANNEX IV: DEVELOPMENT PROJECTS

1 Development Partners assistance by region

This section aims to highlight the different development assistance provided by the development partners by region. Unlike the GFS section, it covers both cash and in-kind funded development assistance. Over time donors have moved away from project based aid to more program and sector based aid. This is in line with government's desired approach.

Determining development assistance by region can be difficult. For example, upgrading the hospital in 'Eua is clearly based on 'Eua and most of the benefits go the people of 'Eua; on the other, the upgraded Vaiola hospital is clearly on Tongatapu, but as the national referral hospital benefits are gained by people from throughout the country. Many other national projects such as the hospital are also based on Tongatapu in particular given it hosts the capital, Nuku'alofa, as well as the major air and sea port infrastructure for connecting the Kingdom with the rest of the world. In addition to nationwide projects, there are also some projects which cover a number of districts, but for which it is difficult to proportion funding.

The figures provided below are the main projects undertaken in the 2011/12 FY and those planned for 2012/13. Some projects have confirmed funding but no activities or location identified yet, therefore the budgets are not yet assigned to a location.

1.1 Projects based on Tongatapu

As noted above, many large national projects are based on Tongatapu but provide benefits to the whole country, or some a number of regions of the country.

Estimated construction for 2012/13 for Tongatapu is at \$38m, this includes roads funded by the China EXIM Loan \$5m, the Integrated Urban Development Sector Project (IUDP) \$6m funded by the Asian Development Bank, the Transport Sector Consolidation Project (TSCP) funded by the World Bank \$12m, the Pacific Aviation Investment Project (PAIP) funded by the World Bank \$5m.

Estimated amount of projects relating to the energy section is \$13m for 2012/13, this is for the successful implementation of the Tonga Energy Roadmap which is Tonga's sector roadmap on how to fix the energy sector. This also includes outer island solar electrification project funded by the ADB \$2m, support from the World Bank through technical assistance as well as cash.

Education is estimated at \$22m for 2012/13, this includes \$10m for the Tonga Education Support Programme co financed by both Australia and New Zealand, even though formulation is based on Tongatapu the benefits from this work will benefit schools throughout the nation, for example development of minimum standards. Scholarships of \$2m will continue as usual, as support towards training and vocational education for the upcoming financial year is \$1.5m. It is also anticipated that the Tonga College Upgrade will be undertaken for \$10m.

Support for the health sector on Tongatapu for 2012/13 is mainly related to the Australian funded Tonga Health Sector support Project (THSSP) \$4m and the medical referrals supported by the New Zealand Aid Program \$0.75m.

Climate Change projects are estimated at \$3.7m for 2012/13, of which \$3m for the 2012/13 is part of the recently approved Pilot Project for Climate Resilience (PPCR) with funds from ADB of USD15m. In addition, there are ongoing projects such as the Climate Change Adaptation Project (PACC) \$0.35m.

Table 31 : Grant Allocation by Project Types - Tongatapu

	Estimate 2011/12 (\$m)	Estimated Outturn 2011/12 (\$m)	Estimate 2012/13 (\$m)
<i>Construction</i>	79.9	75.6	38.1
<i>Energy</i>	28.1	13.4	13
<i>Climate change</i>	3.1	1.4	3.8
<i>Education</i>	7.9	8.5	22.7
<i>Health</i>	6.3	2.9	5
<i>Road</i>	2.2	-	1.8
<i>Law & Order</i>	3.3	1.2	3.4
<i>Income Generation</i>	0.3	0.2	0.3
<i>Others</i>	11.6	4.6	12.7
Total	142.7	107.9	119.8

1.2 Projects based on Vava'u

The Vava'u Development Committee has been established to address the development issues in Vava'u. The government has secured grant assistance from UAE who will install a 500 Mega Watt solar power plant in Neiafu to the value of USD \$4m, this will help lower the cost of electricity. Japan continues to provide its assistance in the water and sanitation sector through the provision of water supply systems for Mataika and Ta'anea. For the 2012/13 financial year it will see the completion of water supply systems for Vaimalo and Ovaka . Under the Pacific Aviation Investment Project both the runway in Tongatapu USD \$14m and Vava'u USD \$2m will be upgraded.

Table 32 : Grant Allocation by Project Types - Vava'u

	Estimate 2011/12 (\$m)	Estimated Outturn 2011/12 (\$m)	Estimate 2012/13 (\$m)
<i>Constructions</i>		0.05	2.05
<i>Water</i>		0.30	0.01
<i>Energy</i>		0.50	4.00
Total		0.85	6.06

1.3 Projects based on Ha'apai

The Ha'apai Management Committee's (HMC) vision is to "develop the standard of living of the people of Ha'apai economically and socially." Their priorities are based on the Ha'apai Master Plan 2011/12 – 2020/21 which, like the other regional plans, are based on the priority needs of island through consultations with their respective communities.

The HMC has focused on the Foa causeway, this is funded from the Government of Germany debt swap agreement with the Kingdom of Tonga, where further repayments of two loans were written off in return for Tonga funding the project. The project is estimated at \$ 4.4m

Ha'apai has received 215 5000 litre water tanks totalling \$0.8m funded by the Government of Australia through the Tonga Community Development Scheme. This was distributed to individual homes, schools as well as public areas.

For the 2012/13 Financial Year there will be renovations and upgrades to the police station through the Tonga Police Development Program as well as upgrades to water supply systems for Nomuka and Ha'afeva. Tongaleleka will receive an ice making machine capable of catering for their refrigeration needs, this is to support and encourage fisheries as well and provide income generating opportunities for the local community.

Table 33 : Grant Allocation by Project Types - Ha'apai

	Estimate 2011/12 (\$m)	Estimated Outturn 2011/12 (\$m)	Estimate 2012/13 (\$m)
Constructions	0.70	0.0	0.03
Water	0.0	0.80	0.23
Total	0.70	0.80	0.26

1.4 Projects based on 'Eua

'Eua Development Committee is responsible for the development of the island with guidance from their 'Eua Strategic Development Plan 2007-2015". This addresses all their priority needs with regards to agriculture, forestry and fisheries, tourism, the environment, community development and private sector support. The 'Eua Airport Runway upgrade project was completed during the year funded by NZAID for \$3m. Support was also provided from the Government of Japan through the Grass-roots human Security Project or GGP for the new children's ward and clinic for children at Niu'eiki Hospital totalling \$0.17m

For 2012/13 the Grass-roots human Security Project will fund the upgrade and renovations to the G.P.S Ha'atua for \$0.17m. Under the sector support towards Police, called the Tonga Police Development Program (TPDP) funded by the governments of New Zealand, Australia and Tonga, there will be renovations to the 'Eua Police Station.

Table 34 : Grant Allocation by Project Types - 'Eua

	Estimate 2011/12 (\$m)	Estimated Outturn 2011/12 (\$m)	Estimate 2012/13 (\$m)
Constructions	3.50	3.40	0.50
Education	0.0	0.0	0.20
Health	0.0	0.20	0.0
Income Generation	0.0	0.0	0.20
Total	3.50	3.60	0.90

1.5 Projects based on Niuatoputapu and Niuafo'ou

Niua Development Committee is responsible for the development of the two Niuaas. Due to the tsunami of 2009 a lot of donor assistance support has been provided to Niuatoputapu. After the immediate relief work the long term recovery plan for Niuatoputapu started. This consisted of major reconstruction including 75 new residential homes and 51 retro fittings to existing homes and community halls funded by the World Bank \$USD5m, progress is being made and this will be completed before the end of the calendar year 2012. Support from the European Union (EU) is provided for the construction of the new health centre which will cost \$2m. Support is also provided by the United Nations Development Programme (UNDP) for an early warning siren system. Procurement will be completed before the end of the calendar year 2012. Japan has indicated that once the construction is complete they will be able to fund the water supply systems for the new residential homes.

Niuafo'ou received in 2011/12 10 5000 ltr water tanks funded by the government of Australia.

Table 35 : Grant Allocation by Project Types - Niuatoputapu

	Estimate 2011/12 (\$m)	Estimated Outturn 2011/12 (\$m)	Estimate 2012/13 (\$m)
Construction	9.20	6.80	1.50
Water & Sanitation	0.0	0.0	0.30
Climate Change	0.0	0.0	0.50
Health	0.0	0.0	2.00
Grand Total	9.20	6.80	4.30

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Table 1. Tonga: Selected Indicators, 2005/06 -2010/11

	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
Output and prices						
Real GDP	-1.6	-4.1	1.2	2.9	2.7	4.7
Consumer prices (period average)	7.2	5.1	9.6	5.5	1.7	6.1
Central government finance (% of GDP)						
Revenue	31.6	30.3	26.9	23.9	20.2	19.4
Grants	2.1	4.6	1.4	7.0	5.2	6.7
Current expenditure	35.5	32.3	26.0	25.8	27.1	22.8
Development expenditure	3.3	1.1	0.5	3.3	6.9	7.3
Overall balance	-4.8	1.6	1.8	1.3	-2.7	1.6
External loans (net)	-0.8	-1.1	-0.8	-0.7	-0.6	-0.8
Domestic financing	-0.2	-0.3	-0.5	0.3	#DIV/0!	0.0
Money and credit (end-period)						
Broad money (M2) % growth	14.4	14.0	8.4	-1.9	9.1	-1.1
Domestic credit	29.0	14.8	15.2	-7.1	-4.2	-17.1
Private sector credit 3/ % growth	23.2	11.4	19.7	-2.9	-18.1	-8.1
Balance of payments (OET Basis)						
Exports, f.o.b.	24.2	26.3	23.5	11.4	11.4	11.2
Of which: Squash	8.3	5.6	2.7	1.9	0.5	0.7
Imports, f.o.b.	-245.4	-212.9	-262.5	-271.3	-208.0	-230.6
Services (net)	-15.7	-35.9	-6.2	-5.4	-7.9	3.9
Income (net)	5.7	7.1	6.4	57.5	5.2	7.8
Services and Income (net)	-10.0	-28.8	0.2	52.1	-2.7	11.7
Transfers (net)	178.5	168.6	180.2	158.0	166.9	138.0
Of which: Private transfer receipts	205.0	185.4	202.8	175.2	157.4	145.7
Current account balance	-45.9	-51	-58.5	-49.8	-32.4	-69.7
(In percent of GDP)	-7.7	-8.5	-8.9	-7.5	-4.6	-8.9
Overall balance	1.1	8.4	-2.5	47.1	34.3	33.3
Gross international reserves (end-period)						
In millions of pa'anga	83.2	91.6	89.1	136.3	170.5	203.8
In months of imports cover	4.3	4.4	3.5	5.1	7.1	7.4
External debt						
External debt/GDP	27.8	26.8	24.0	30.5	32.2	34.7
Exchange rate (period average)						
T\$ per US\$ (end-period)	2.06	1.9	1.9	2.01	1.95	1.84
Real effective exchange rate (1990=100)	104.4	102	113.8	114.5	112.2	104.8
Nominal effective exchange rate (1991=100)	62.7	59.8	58.6	59.5	59.2	59.9

1/ Fiscal year begins in July.

2/ **Sources** for Output and Prices : Statistics Dept

2/ **Sources** for Government finance and External Debt : MOFNP

4/ **Sources** for Money and Credit & BOP & Foreign Reserves & Exchange Rate: NRBT

Table 2. Tonga: Real Sector Developments, 2005/06 -2010/11

	2005/06(r)	2006/07(r)	2007/08(r)	2008/09(r)	2009/10(r)	2010/11(p)
Nominal GDP						
In pa'anga million	594.6	602.9	659.3	664.3	711.4	783.4
In US\$ million	289.2	292.3	337.3	314.4	368.2	427.1
GDP per capita (US\$)	2,847	2,865	3,293	3,056	3,564	4,118
Population (National Accounts estimate)	101,606	102,025	102,446	102,869	103,293	103,719
	<i>Annual percentage change</i>					
GDP (2010/11 prices)	-1.6	-4.1	1.2	2.9	2.7	4.7
of which:						
Agriculture, forestry, and fisheries	-8.2	0.6	-5.8	-2.1	-0.7	3.7
Manufacturing	1.1	-3.4	-0.6	-7.6	-2.5	7.2
Construction	-10.5	-2.8	0.9	35.0	21.7	16.9
Commerce, restaurants, and hotels	-4.2	-2.9	5.7	7.7	-5.5	3.4
Transportation and communications	7.6	-1.1	3.9	15.1	13.4	2.3
Finance and real estate	2.4	-1.8	2.6	-16.3	-1.4	0.6
Government services	-0.3	-15.1	4.6	2.5	0.9	0.5
	<i>Percentage of GDP</i>					
GDP (current prices)						
of which:						
Agriculture, forestry, and fisheries	15.7	16.7	14.9	15.4	16.4	17.0
Manufacturing	7.0	7.1	6.7	6.5	6.1	5.9
Construction	5.8	6.0	6.0	7.0	8.7	10.6
Commerce, restaurants, and hotels	10.5	10.9	12.3	13.2	12.2	12.9
Transportation and communications	5.6	5.5	5.7	6.6	6.7	6.2
Finance and real estate	8.8	9.0	9.3	8.0	7.6	7.4
Government services	14.9	11.9	11.7	12.2	12.5	11.7
Consumer prices (period average)						
All items	7.2	5.1	9.6	5.5	1.7	6.1
Imported component	5.2	4.0	10.5	5.5	1.7	7.7
Domestic component	11.1	7.3	7.9	5.5	1.5	3.7

(r)-revised estimates

(p)-preliminary estimates

Source: Statistics Department Tonga

Table 3: Annual Average Consumer Price Index for 2006 - 2011

Base Period (October 2010=100.0)

	All Items	Food	Housing	H/hold Goods	Clothing and Footwear	Trans- portation	Tobacco and Alcohol	Misc. Goods & Services	Imported Items	Local Items
<u>Weight</u>	<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>
2006	80.1	76.5	92.6	86.4	84.4	86.0	71.2	88.6	82.2	78.8
2007	84.7	82.2	96.5	94.8	89.3	88.3	73.0	93.3	86.4	83.7
2008	93.6	88.5	99.5	104.5	96.2	109.0	78.9	101.4	94.3	93.0
2009	94.9	95.4	103.8	98.5	100.8	95.2	82.9	104.1	97.9	93.2
2010	98.3	98.3	102.1	99.3	99.8	100.5	93.7	99.4	98.3	98.1
2011	104.4	104.7	99.8	101.6	104.6	112.6	101.6	101.7	102.3	106.1

Source: Statistics Department

Table 4: Annual (%) Changes in the CPI for december month 2006 to 2011

	All Items	Food	Housing	Household Goods	Clothing and Footwear	Transporta tion	Tobacco and Alcohol	Misc. Goods & Services	Imported Items	Local Items
<u>Weight</u>	<u>100</u>	<u>45.8</u>	<u>2.5</u>	<u>20.8</u>	<u>3.16</u>	<u>11.93</u>	<u>6.00</u>	<u>9.83</u>	<u>57.8</u>	<u>42.2</u>
2006	4.9	4.5	6.4	9.5	6.9	4.7	1.7	3.9	3.3	7.9
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	4.2	3.2	0.0	5.4	4.6	8.8	1.8	2.6	5.9	1.0

Source: Statistics Department

Table 5: Tonga Domestic Exports by HS Section, 2005/06 -2010/11

HS Code SECTION ITEM	2005/06		2006/07		2007/08/p		2008/09/p		2009/10		2010/11	
	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%
Live Animals;Animal Products	5,340	28.9	7,357	34.7	5900.0	34.1	4147.4	28.0	9856.8	64.3	9905.4	49.9
Vegetable Products	12	0.1	11,778	55.61	7321	42.3	7087.1	47.8	4019.3	26.2	8056.3	40.5
Products of the Chemical Or Allied	344	1.9	580	2.74	1489	8.6	907.7	6.1	585.3	3.8	646.5	3.3
Wood and Articles of Wood;	507	2.7	488	2.30	323	1.9	601.6	4.1	321.9	2.1	432.8	2.2
Miscellaneous Manufactured Articles	0	0.0	6	0.03	23	0.1	5.7	0.0	22	0.1	5.2	0.0
Works of Art, Collectors Pieces and Antiques	20	0.1	33	0.15	72	0.4	44.6	0.3	16.6	0.1	56.1	0.3
Other Exports	12,271	66.4	938	4.43	2160	12.5	2,032	13.7	505	3.3	766	3.9
TOTAL	18,494	100.0	21,180	100	17,288	100.0	14,827	100.0	15,327	100.0	19,869	100.0

Source: Statistics Department

p: provisional numbers

Table 6: Exports by Institutional Sector, 2004/05 - 2010/11

INSTITUTIONAL SECTOR	2004/05		2005/06		2006/07		2007/08/p		2008/09/p		2009/10		2010/11	
	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%
Private Sector	27,123	100	18,494	100	21,180	100	17,288	100	14,827	100	15,327	100	19,863	100
Government Sector	0	0	0	0	0	0	0	0	0	0	0	0	5.7	0
Quasi-Government Sector	0	0	0	0	0	0	0	0	0	0	0	0	0	0
TOTAL	27,123	100	18,494	100	21,180	100	17,288	100	14,827	100	15,327	100	19,869	100

Source: Statistics Department

p: provisional numbers

Table 7: Exports by Country of Destination, 2004/05 – 2010/11

COUNTRY	2004/05		2005/06		2006/07		2007/08/p		2008/09p		2009/10		2010/11	
	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%	(T\$'000)	%
New Zealand	6,203	22.9	1,813	9.8	4,244	20.0	5,278	30.5	5,283	35.6	3,264	21.3	3,269	16.5
Australia	816	3.0	404	2.2	1,303	6.2	817	4.7	1,743	11.8	693	4.5	581	2.9
Mainland USA	3,269	12.1	2,018	10.9	2,581	12.2	2,939	17.0	2,636	17.8	2,551	16.6	2,685	13.5
Hawaii	2,069	7.6	2,991	16.2	2,140	10.1	1,531	8.9	227	1.5	131	0.9	-	0.0
Japan	12,151	44.8	10,143	54.8	7,550	35.6	2,244	13.0	1,967	13.3	517	3.4	2,862	14.4
Singapore	2	0.0	16	0.1	48	0.2	104	0.6	17	0.1	458	3.0	2	0.0
American Samoa	655	2.4	285	1.5	443	2.1	635	3.7	428	2.9	178	1.2	213	1.1
Hong Kong	407	1.5	4	0.0	40	0.2	171	1.0	551	3.7	6,433	42.0	7,537	37.9
France	1	0.0	-	0.0	0	0.0	0	0.0	0	0.0	0	0.0	1	0.0
All other Countries	1,551	5.7	820	4.4	2,831	13.4	3,569	20.6	1,975	13.3	1,103	7.2	2,719	13.7
TOTAL	27,123	100.0	18,494	100.0	21,180	100.0	17,288	100.0	14,827	100.0	15,327	100.0	19,869	100.0

Source: Statistics Department

p: provisional numbers

Table 8: Imports by Main HS Section 2004/05 - 2010/11

HS Code SECTION ITEM	2004/05		2005/06		2006/07		2007/08/p		2008/09/p		2009/10		2010/11	
	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%
1.Live Animals;Animal Products	2,452	1.2	25,698	11.0	30,162	12.0	30,742	10.0	36,426	11.8	39,502	13.8	40,464	12.7
2.Vegetable Products	7,362	3.6	7,302	3.1	8,244	3.3	9,610	3.1	10,695	3.5	9,347	3.3	10,216	3.2
3. Prepared Foodstuff; Beverages & Tobacco	28,538	14.1	31,719	13.6	37,228	14.8	46,221	15.1	44,154	14.3	45,633	16.0	39,041	12.3
4. Products of the Chemical or Allied	10,935	5.4	8,430	3.6	9,268	3.7	14,464	4.7	11,699	3.8	13,684	4.8	13,675	4.3
5. Wood and Articles of Wood	8,536	4.2	9,424	4.0	8,096	3.2	11,065	3.6	7,269	2.3	7,164	2.5	11,244	3.5
6. Machinery and Mechanical Appliance	28,685	14.2	19,051	8.2	25,380	10.1	38,901	12.7	37,671	12.2	39,244	13.7	41,372	13.0
7. Miscellaneous Manufactured Articles	6,457	3.2	4,964	2.1	6,175	2.5	6,479	2.1	4,899	1.6	4,838	1.7	5,415	1.7
8. Vehicle, Aircraft, Vessel & Associated	12,986	6.4	9,672	4.2	10,341	4.1	17,374	5.7	17,615	5.7	15,908	5.6	16,110	5.1
9. Works of Art, Collectors Pieces	1,422	0.7	19,752	8.5	12,281	4.9	13,765	4.5	14,899	4.8	4,074	1.4	1,194	0.4
10. Other Imports	95,156	47.0	96,844	41.6	104,418	41.5	118,392	38.6	124,017	40.1	106,360	37.2	138,897	43.7
TOTAL	202,528	100.0	232,856	100.0	251,596	100.0	307,013	100.0	309,344	100.0	285,754	100.0	317,628	100.0

Source: Statistics Department

p: provisional numbers

Table 9 : Imports by Institutional Sector, 2004/05 – 2010/11

INSTITUTIONAL SECTOR	2004/05		2005/06 /p		2006/07		2007/08/p		2008/09/p		2009/10		2010/11	
	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%
Private Sector	204,436	91.0	210,386	90.4	231,272	91.9	291,762	95.0	294,348	95.2	277,502	97.1	297,987	93.8
Government Sector	15,070	6.7	17,437	7.5	11,162	4.4	12,457	4.1	11,114	3.6	5,120	1.8	9,227	2.9
Quasi-Government Sector	5,087	2.3	5,033	2.2	9,161	3.6	2,794	0.9	3882.1	1.3	3132.7	1.1	10414	3.3
TOTAL	224,593	100	232,856	100	251,595	100.0	307,013	100.0	309,344	100.0	285,754	100.0	317,628	100.0

Source: Statistics Department

p: provisional numbers

Table 10: Imports by Country of Origin, 2004/05 – 2010/11

COUNTRY	2004/05		2005/06		2006/07		2007/08 /p		2008/09 /p		2009/10		2010/11	
	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%	(\$'000)	%
New Zealand	85,030	37.9	81,603	35.0	84,365	33.5	100,123	32.6	81,870	26.5	88,715	31.0	107,985	34.0
Australia	39,948	17.8	24,962	10.7	34,666	13.8	34,899	11.4	33,349	10.8	32,714	11.4	23,736	7.5
USA	19,216	8.6	21,289	9.1	25,795	10.3	26,348	8.6	35,884	11.6	41,273	14.4	35,741	11.3
United Kingdom	410	0.2	551	0.2	276	0.1	391	0.1	714	0.2	1,118	0.4	70	0.0
Fiji	39,157	17.4	62,780	27.0	68,710	27.3	32,568	10.6	41,411	13.4	31,007	10.9	25,861	8.1
Japan	6,641	3.0	8,338	3.6	5,845	2.3	8,354	2.7	11,375	3.7	6,844	2.4	8,848	2.8
Singapore	4,715	2.1	6,292	2.7	5,883	2.3	63,666	20.7	62,679	20.3	50,039	17.5	74,804	23.6
Others	29,475	13.1	27,041	11.6	26,056	10.4	40,664	13.2	42,061	13.6	34,043	11.9	40,582	12.8
TOTAL	224,593	100.0	232,856	100.0	251,596	100.0	307,013	100	309,344	100.0	285,754	100.0	317,628	100.0

Source: Statistics Department

p: provisional numbers

Table 11: Tonga Balance of Payment 2005/06 - 2010/11*(In millions of pa'anga, unless otherwise indicated)*

	2005/06	2006/07	2007/08	2008/09 /p	2009/10/p	2010/11/p
Balance of Trade	-214.4	-190.8	-268.3	-273.2	-296.3	n.a
Exports, f.o.b.	31.0	26.7	23.5	18.3	14.9	n.a
Of which: Squash exports	8.3	5.6	2.7	1.9	n.a	n.a
Imports, f.o.b.	-245.4	-217.5	-291.8	-291.5	-311.2	n.a
Services (net)	-15.7	-35.9	-24.7	-28.5	-16.3	n.a
Receipts	50.9	38.8	66.1	76.4	75.4	n.a
Of which: Tourism receipts	27.0	24.1	33.3	36.7	39.7	n.a
Payments	-66.6	-74.7	-90.8	-104.9	-91.7	n.a
Income (net)	5.7	7.1	14.3	13.1	7.6	n.a
Receipts	9.9	12.9	22.6	21.0	22.4	n.a
Payments	-4.2	-5.8	-8.3	-7.9	-14.8	n.a
Current Transfers (net)	178.5	168.6	200.4	184.6	n.a	n.a
Official transfers (net)	0.0	-0.1	8.4	19.4	n.a	n.a
Private transfers (net)	178.5	168.7	192.0	165.2	n.a	n.a
Official transfer receipts	0.5	0.5	8.7	20.8	n.a	n.a
Official transfer payments	-0.5	-0.6	-0.3	-1.4	n.a	n.a
Private transfer receipts	205.0	186.8	220.1	185.2	n.a	n.a
Private transfer payments	-26.5	-18.1	-28.1	-20.0	n.a	n.a
Current account balance	-45.9	-51.0	-78.3	-104.0	n.a	n.a
(Percent of GDP)	-7.7	-8.5	-11.9	-15.7	n.a	n.a
Capital account balance	45.2	53.9	68.9	188.9	n.a	
Official capital (net)	16.8	19.7	42.7	146.5	n.a	
Official loans, net	0.0	0.0			n.a	n.a
Disbursements	0.0	0.0			n.a	n.a
Amortization	0.0	0.0			n.a	n.a
Official capital inflows	22.8	24.7	52.6	148.0	n.a	n.a
Official capital outflows	-6.0	-5.0	-9.9	-1.5	n.a	n.a
Private capital (net)	28.4	34.2	26.2	42.4	n.a	n.a
Private capital inflows	37.5	39.9	32.6	43.7	n.a	n.a
Private capital outflows	-9.1	-5.7	-6.4	-1.3	n.a	n.a
Financial Account	14.4	21.0	38.4	-1.4	n.a	n.a
Other Credits	37.5	47.1	35.9	-48.6	n.a	n.a
Official Reserve	-1.1	-8.4	2.5	47.2	n.a	n.a
Debits	22.0	17.7	0	0	n.a	n.a
Basic Balance	13.7	23.9	29.0	83.5	n.a	n.a
Errors and omissions	-12.6	-15.5	-31.5	-36.3	n.a	n.a
Overall balance	1.1	8.4	-2.5	47.2	n.a	n.a
Memorandum items:						
Service, income, and transfers (net)	168.5	139.7	198.4	188.6	n.a	n.a
Receipts	266.3	239.0	317.5	303.4	n.a	n.a
Payments	-97.8	-99.2	-127.5	-134.2	n.a	n.a
Gross official foreign reserves (TOP mil)	83.2	91.6	89.1	136.3	170.5	203.8
Months of Import cover	4.3	4.4	3.5	5.1	7.1	7.4

Source: Statistics Department

Table 12. Tonga: Monetary Survey, 2005/06–2010/11

	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
Net foreign assets	72.6	81.7	79.9	121.3	176.3	215.2
Foreign assets	95.0	103.6	99.9	154.0	192.9	221.6
Foreign liabilities	-22.5	-21.9	-20.0	-32.7	-16.6	-6.5
Net domestic assets	156.3	179.3	202.9	156.2	133.7	95.0
Net domestic credit	213.5	245.0	282.2	262.3	251.3	208.4
Government (net)	-19.1	-11.7	-29.1	-32.7	-14.6	-32.5
Non-financial public enterprises	3.9	2.5	3.7	3.9	18.0	13.2
Private sector	233.8	260.5	311.8	302.8	247.9	227.7
Non-monetary financial institutions	-5.2	-6.3	-4.2	-11.7	-7.5	-10.9
Other items (net)	-57.1	-65.7	-79.3	-106.1	-117.6	-113.4
Total domestic liquidity (M2)	228.9	261.0	282.8	277.3	302.5	299.2
Narrow money (M1)	55.7	73.8	72.6	77.9	97.8	96.9
Currency outside banks	17.1	18.5	18.8	21.9	26.3	27.3
Demand deposits	38.6	55.3	53.8	56.0	71.5	69.7
Quasi money	173.2	187.2	210.2	199.4	204.7	202.3
Savings deposits	53.2	49.3	48.8	43.6	48.5	51.0
Term deposits	108.2	125.2	150.1	143.0	142.9	139.5
Foreign currency accounts	11.8	12.8	11.3	12.8	14.1	11.8
Net foreign assets	-6.0	12.6	-2.2	51.8	45.4	22.0
Foreign assets	3.5	9.0	-3.6	54.2	25.2	14.9
Foreign liabilities	53.8	-2.5	-8.7	63.7	-49.4	-61.0
Net domestic assets	27.2	14.7	13.2	-23.0	-14.4	-28.9
Private sector	23.2	11.4	19.7	-2.9	-18.1	-8.1
Total domestic liquidity (M2)	14.4	14.0	8.4	-1.9	9.1	-1.1
Narrow money (M1)	-18.9	32.5	-1.6	7.3	25.5	-0.9
Quasi money	31.8	8.1	12.3	-5.1	2.6	-1.1
Net foreign assets	35.2	43.0	42.1	60.3	90.4	72.9
Foreign assets	46.1	54.5	52.6	76.6	98.9	75.1
Foreign liabilities	-10.9	-11.5	-10.5	-16.3	-8.5	-2.2
Memorandum items:						
Velocity (GDP/average M2)	2.0	1.9	0.9	2.3	2.2	0.0
Exchange rate (pa'anga per U.S. dollar)	2.1	1.9	1.9	2.0	2.0	3.0

Source: National Reserve Bank of Tonga

Table 13: Summary Table of Government Operations, 2007/08 - 2010/11

Years ending June 30	2007/08	2008/09/p	2009/10(p)	2010/11(p)
Total revenue and grants	172.2	225.7	192.1	203.8
Total revenue	163.6	179.9	143.6	151.0
Current revenue	163.6	152.7	143.6	149.1
Tax revenue	139.1	131.5	116.2	133.0
Nontax revenue	24.5	21.2	27.3	16.1
Capital revenue	0.0	27.2	0.00	2.0
Grants (in cash)	8.7	45.8	48.60	52.8
Total expenditure and lending minus repayments	161.5	220.6	230.1	261.1
Total expenditure	161.5	186.5	211.7	249.9
Current expenditure	158.5	167.4	193.2	175.5
Capital expenditure	3.04	19.1	18.4	74.4
China EXIM Bank Loan		1.2		60.4
Total lending minus repayments	-0.05	34.1	18.5	11.2
China EXIM Bank Loan		2.6		11.0
Overall deficit/surplus	10.8	5.1	-38.0	-57.3
Total financing	-10.8	-5.1	38.0	57.3
External financing	-5.0	(1.0)	24.7	65.5
Domestic bank financing	-5.8	(4.1)	13.3	(8.2)
% to GDP				
Total revenue and grants	26.1	34.0	27.0	26.0
Total revenue	24.6	27.1	20.2	19.3
Current revenue	24.6	23.0	20.2	19.0
Tax revenue	20.9	19.8	16.3	17.0
Nontax revenue	3.7	3.2	3.8	2.1
Capital revenue	0.0	4.1	0.0	0.2
Grants	1.3	6.9	6.8	6.7
Total expenditure and lending minus repayments	24.3	33.2	32.3	33.3
Total expenditure	24.3	28.1	29.8	31.9
Current expenditure	23.9	25.2	27.2	22.4
Capital expenditure	0.5	2.9	2.6	9.5
Total lending minus repayments	0.0	5.1	2.6	1.4
Overall deficit/surplus	1.6	0.8	-5.3	(7.3)
Total financing	-1.6	-0.8	5.3	7.3
External financing	-0.7	-0.2	3.5	8.4
Domestic bank financing	-0.9	-0.6	1.9	(1.0)
Effective import tariff (In percent)				
GDP (TOP \$million)	659.3	664.3	711.4	783.4

Source: Ministry of Finance and National Planning

Table 14: Government Revenue Collection, 1991/92 - 2010/11

Year	Foreign Trade Taxes	Domestic Taxes	Others	Total
	(\$)	(\$)	(\$)	(\$)
1991/92	21,409,800	8,695,200	16,124,120	46,229,120
1992/93	23,862,540	11,591,670	16,832,960	52,287,170
1993/94	26,470,240	11,808,990	16,462,630	54,741,860
1994/95	26,774,790	11,068,060	20,375,610	58,218,460
1995/96	27,285,570	13,808,570	23,549,900	64,644,040
1996/97	27,231,170	14,469,290	19,776,140	61,476,600
1997/98	27,132,550	13,882,720	21,687,170	62,702,440
1998/99	27,513,660	17,589,220	21,804,800	66,907,680
1999/00	33,984,206	18,224,700	22,374,923	74,583,829
2000/01	35,777,155	19,692,515	29,300,678	84,770,348
2001/02	48,426,692	23,248,611	22,490,991	94,166,294
2002/03	56,227,260	24,845,971	23,422,871	104,496,101
2003/04	58,443,338	26,316,445	27,560,492	112,320,275
2004/05	66,984,098	30,100,037	20,661,601	117,745,736
2005/06	81,282,340	40,089,379	26,824,876	148,196,594
2006/07	91,206,168	33,605,628	26,695,806	151,507,602
2007/08	100,327,543	37,854,765	23,592,346	161,774,654
2008/09/p	81,698,070	46,060,396	59,063,262	186,821,728
2009/10/p	80,920,362	34,582,975	44,096,676	159,600,013
2010/11/p	86,244,071	46,753,268	18,039,796	151,037,135

Source: Ministry of Finance and National Planning, p: provisional numbers

Table 15: Major Sources of Tax Revenue 2007/08 - 2010/11

	2007/08		2008/09 /p		2009/10/p		2010/11/p	
	\$	%	\$	%	\$	%	\$	%
Import Duties	40,533,515	29.4	16,059,175	12.2	14,914,998	12.8	12,654,874	9.5
Port & Service Tax		0.0		0.0			-	0.0
Excise Tax/Excise Duty	10,835,808	7.9	23,974,263	18.2	25,207,291	21.7	28,644,464	21.5
Income Tax	26,845,560	19.5	40,258,007	30.6	28,070,338	24.1	38,346,253	28.8
Sales Tax / Consumption Tax	59,676,719	43.3	47,192,812	35.9	42,908,911	36.9	49,600,697	37.3
Sub-Total	137,891,602	100.0	127,484,257	96.9	111,101,537	95.6	129,246,288	97.2
Other	-	0.0	4,043,330	3.1	5,140,092	4.4	3,751,051	2.8
TOTAL	137,891,602	100.0	131,527,587	100.0	116,241,629	100	132,997,339	100.0

Source: Ministry of Finance and National Planning , p: provisional numbers

Table 16: Expenditure by Ministry for 2007/08-2010/11 (Tonga Government Fund)

	2007/08		2008/09/p		2009/10/p		2010/11/p	
	\$	%	\$	%	\$	%	\$	%
16 Education	22,450,556	15.1	24,200,091	11.6	26,563,614	15.1	31,879,985	18.0
15 Health	19,212,939	12.9	20,900,972	10.1	22,500,834	12.8	22,430,180	12.6
19 Works	4,250,745	2.9	8,484,544	4.1	3,347,700	1.9	10,048,278	5.7
07 Prime Minister's Office	8,333,077	5.6	8,999,712	4.3	8,344,844	4.7	6,330,447	3.6
Sub-Total	54,247,316	36.4	62,585,319	30.1	60,756,992	35	70,688,890	40
14 Police	8,381,583	5.6	10,880,495	5.2	9,884,854	5.6	9,139,717	5.1
18 Agriculture	5,052,231	3.4	5,717,328	2.8	5,540,339	3.2	5,785,623	3.3
06 Defence	8,078,335	5.4	9,894,917	4.8	8,141,516	4.6	7,244,281	4.1
02 Legislative Assembly	3,935,384	2.6	4,719,628	2.3	4,049,559	2.3	3,844,079	2.2
086 Public Debt	15,592,374	10.5	17,487,685	8.4	26,398,727	15.0	22,801,034	12.8
05 Foreign Affairs	6,767,524	4.5	14,187,765	6.8	10,627,047	6.0	11,052,518	6.2
Financial Appropriations								
085	9,784,920	6.6	41,033,088	19.7	19,108,411	10.9	18,093,192	10.2
Sub-Total	57,592,352	38.7	103,920,906	50.0	83,750,453	47.6	77,960,444	43.9
Other	37,077,358	24.9	41,330,702	19.9	31,302,798	17.8	28,828,106	16.2
GRAND TOTAL	148,917,026	100.0	207,836,927	100.0	175,810,243	100.0	177,477,440	100.0

Source: Ministry of Finance and National Planning

p: provisional numbers

Table 17: GFS Presentation of the Government Finance for 2009/10 - 2012/13

Items	Actual 2009/10	Actual 2010/11	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Total Revenue and grants	192,122,174	203,827,438	206,718,629	215,545,121	217,828,849
Current revenue	143,554,436	149,084,630	137,714,031	147,710,895	147,027,313
Tax revenue	116,241,629	132,997,339	114,544,255	124,596,028	127,734,503
Taxes on income and profits	28,118,228	38,346,253	21,210,000	21,879,677	21,305,000
Taxes on property	76,882	119,059	61,500	61,500	71,000
Domestic taxes on goods and services	72,372,748	81,877,153	80,702,755	88,993,840	92,466,424
Consumption tax	42,908,955	49,600,697	49,425,000	54,392,967	56,005,335
Other taxes	29,463,793	32,276,456	31,277,755	34,600,873	36,461,089
Taxes on international trade and transactions	14,935,478	12,654,874	12,570,000	13,661,012	13,852,080
Customs duties	14,914,998	12,635,635	12,520,000	13,611,012	13,800,000
Other import charges	20,481	19,240	50,000	50,000	52,080
Other taxes	738,293	-	-	-	40,000
Nontax revenue	27,312,807	16,087,291	23,169,776	23,114,867	19,292,810
Entrepreneurial and property income	14,538,914	3,279,521	7,550,383	7,550,383	5,858,864
Administrative fees and charges	10,027,993	11,212,203	15,131,193	15,076,284	12,962,946
Fines and forfeits	516,141	598,697	478,200	478,200	461,000
Other nontax revenue	2,229,758	996,870	10,000	10,000	10,000
Capital revenue	3,050	1,952,505	1,554,935	1,555,435	2,265,296
Grants (in cash)					
From abroad	48,564,689	52,599,759	67,049,663	66,096,310	67,036,240
From other levels of national government	0	190,544	400,000	182,481	1,500,000
Total Grants (in cash)	48,564,689	52,790,303	67,449,663	66,278,791	68,536,240
Expenditure and lending minus repayments	230,150,230	261,094,923	232,070,627	239,199,135	216,610,639
Total Expenditure	202,284,023	249,936,396	214,358,309	230,012,631	216,091,676
Current expenditure	183,837,841	175,546,979	185,097,219	181,149,097	201,390,813
Wages and salaries	82,731,045	91,761,979	85,487,247	87,282,403	89,986,588
Employer contributions	6,939,112	9,138,731	9,289,166	9,186,159	9,018,449
Other purchases of goods and services	69,393,941	50,790,647	65,577,261	61,043,432	75,504,521
Interest payments	5,550,634	6,456,261	6,819,000	6,819,000	7,026,419
Subsidies and other current transfers	19,223,109	17,399,361	17,924,545	16,818,102	19,854,837
Subsidies to non-financial public enterprises	-	-	-	-	-
Subsidies to financial institutions	-	28,603	30,000	11,177	-
Subsidies to other enterprises	1,550,845	1,218,234	865,000	115,252	380,000
Transfers to non-profit institutions	6,427,984	8,346,836	7,771,000	7,601,862	8,770,804
Transfers to households	10,166,947	6,455,807	7,318,341	7,366,849	7,804,032
Transfers abroad	1,077,332	1,349,881	1,940,204	1,722,963	2,900,001
Capital expenditure	18,446,181	74,389,417	29,261,090	48,863,534	14,700,862
Acquisition of fixed capital assets	18,108,115	11,749,236	12,914,596	6,196,671	9,365,627
Purchases of land and intangible assets	59,962	2,066,431	69,402	1,046,275	96,713
Capital transfers	278,105	177,299	77,092	469,902	112,592
in which ; Chinese EXIM Bank loan		60,396,451	16,200,000	41,150,686	5,125,931
Lending minus repayments	27,866,208	11,158,526	17,712,318	9,186,504	518,963
To non-financial public enterprises (net)	28,240,182	112,715	1,912,319	471,325	518,964
To financial institutions (net)	(373,975)	-	(1)	(1)	(1)
Abroad	-	-	-	-	-
in which; Chinese EXIM Bank loan		11,045,811	15,800,000	8,715,180	-
Overall deficit/surplus	-38,028,056	-57,267,485	-25,351,998	-23,654,014	1,218,210

Source: Ministry of Finance and National Planning

Table 18: Full GFS Presentation of Financing Table 2009/10 - 2012/13

Items	Actual 2009/10	Actual 2010/11	Budget Estimate 2011/12	Est Outturn 2011/12	Budget Estimate 2012/13
Total Financing	38,028,055	57,267,485	25,351,998	23,654,014	-1,218,210
External Financing	24,711,843	65,458,489	25,351,998	43,510,404	(1,218,750)
Disbursement	36,282,560	71,443,262	31,999,998	49,865,865	5,125,391
Repayments	4,578,998	5,984,773	6,648,000	6,355,461	6,344,141
Net Change in External Cash Balance	-6,991,719	0	0	0	0
Domestic Financing	13,316,212	(8,191,004)	-	(19,856,390)	540
Bonds Issued/Domestic Loan	14,603,000	10,360,000	3,000,000	3,000,000	7,488,000
Principal Repayment of Matured Bonds/Loan	6,891,255	10,360,000	3,000,000	3,000,000	7,488,000
Net Changes in Government Cash Balances and Investment	5,604,467	(8,191,004)	-	(19,856,390)	540

Source: Ministry of Finance and National Planning