"Economic and Financial Update"

(January—March 2023)

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A. FISCAL UPDATE

- From Jan-March 2023, the ***fiscal balance*** increased by 39% ($11.3m) on a year basis, recording a surplus of $40.7 m. While the government revenue increased by 15% ($17.2m) to $131.3 m, the government expenditure increased only by 5% ($3.7m).
  - At the end of March 2023(Jul-Mar 2023) recorded a fiscal surplus of $35.6 m, comprising of total revenue of $347.6 m and total expenses of $295.8m.

- ***Total revenue,*** including domestic revenue and grants, increased by 15% ($17.2m) for the period (Jan - Mar 2023) . This is mainly attributed to the increase in tax revenue of 43% ($19.8m), compared to the same period in the previous year. When taking into account that the grant funding declined by 15% ($9.7 m) , this shows the consolidated efforts within the government to promote macroeconomic stability through achieving fiscal targets.
  - Total revenue recorded as of March 2023(Jul-Mar 2023) reached $347.6 m or 49% of the original target. This includes $202.9 m of tax revenues being collected ,$123.7 m from Grant and $21 m from other revenue.

- ***Total Expenses*** across the same period(Jan-Mar2023), total expenditure increased by 5% ($3.7m). A major part of this increase was attributed to the increased cost of goods and services of $13.1 m, compared to the previous year. (Jan-Mar 2022)
  - Although spending remains low as of March 2023, accounting for only 46% of the total estimates, it reflects a 5% increase compared to the corresponding period in the previous fiscal year.

- With continuing prudence in spending and strengthening in administration and compliance in revenue collection, a minimal fiscal surplus/deficit is estimated at the end of the financial year (end of June FY 2023) .

Government Financial Statistics (GFS)

Key Indicators	Jan - Mar 2022 ($m)	Jan 2023($m)	Feb 2023($m)	Mar 2023($m)	Jan - Mar 2023($m)	Quarterly	Budget Est 22/23($m)	Actual (Jul-Mar 23)($m)	Variance $	Variance %
	(T$m unless otherwise indicated)									
FISCAL INDICATORS *(Government Financial Statistics (GFS) Basis)*										
Revenue	**114.1**	**74.8**	**26.8**	**29.8**	**131.3**	**15%**	**675.9**	347.6	**(328.3)**	**-49%**
Tax	45.7	22.0	19.6	24.0	65.5	43%	253.3	202.9	(50.4)	-20%
Grant *(cash grants)*	66.3	50.4	4.2	2.0	56.6	-15%	389.6	123.7	(266.0)	-68%
Current Grant	*5.8*	*0.0*	*0.0*	*0.0*	*0.0*	-	*9.8*	*0.0*	(9.8)	-100%
Capital Grant	*60.5*	*50.4*	*4.2*	*2.0*	*56.6*	-6%	*379.9*	*123.7*	(256.2)	-67%
Other Revenue *(non - tax)*	2.2	2.4	3.0	3.9	9.2	317%	33.0	21.0	(12.0)	-36%
Expenses	**80.9**	**22.3**	**29.3**	**33.0**	**84.6**	**5%**	**546.8**	**294.8**	**252.0**	**46%**
Compensation of Employees	41.4	11.8	11.5	11.5	34.8	-16%	177.0	115.3	61.6	35%
Use of Goods and Service	25.7	8.3	14.0	16.5	38.8	51%	298.8	134.6	164.1	55%
Interest	3.6	0.3	0.1	2.8	3.3	-9%	7.9	7.0	0.9	11%
Subsidies	0.0	0.1	0.0	0.0	0.1	133%	1.3	0.5	0.8	65%
Grant	1.1	0.3	0.1	0.1	0.5	-52%	4.3	2.9	1.4	33%
Social benefits	5.4	1.2	1.5	2.1	4.8	-12%	27.2	16.0	11.2	41%
Other Expenses	3.7	0.3	2.1	0.0	2.4	-35%	30.3	18.2	12.1	40%
Gross Operating Balance	33.2	52.5	-2.6	-3.2	46.7	41%	129.1	52.8	76.4	59%
Net Acquisition of Non-financial Assets	3.9	0.8	2.1	3.0	6.0	54%	160.9	17.1	143.7	89%
Net Lending/Borrowing Requirement (Financing)	**29.4**	**51.7**	**-4.7**	**-6.2**	**40.7**	39%	**-31.7**	**35.6**	**(67.4)**	
Total Public Debt *(External & Domestic)* ($million)	N/A	N/A	N/A	N/A	N/A	-	NA	N/A	-	
FISCAL ANCHORS										
Compensation of Employees to domestic revenue to be less than 53% (annual target)										
monthly performance (%)	86%	48%	51%	41%	47%		62%	51%	-	

Table 1: *Source:* MOF

Note: Fiscal data are provisional (unless indicated) and are still subject to change until audited. Fiscal data based on last update in 9 of May 2023)

B. ECONOMIC UPDATE

The economy has gradually improved, since the HTHH eruption and the COVID-19 pandemic. The government, along with financial help from development partners and remittances, have helped to keep the economy going and protect those who are vulnerable. The country is now facing the challenge of reconstructing the economy while dealing with high inflation due to global energy and food prices. In response, the government focus is on recovery, reconstruction, and social protection in the short-term, whilst, continuing reforms and increase investment to revive the economy and growth in the medium-term.

The economic growth for FY 2023 is expected at 2.8 percent, reflecting an economic recovery after the international border re-opened in August 2022. Over the medium term (FY 2024 - 2026), the outlook is positive for the domestic economy, with an estimated average growth rate of around 2.5 percent. This growth is expected to be led by the reconstruction activities and the development of Agriculture and Fisheries local production.

Figure 1: Growth

REAL GDP GROWTH (%)

20/21 21/22 est 22/23 (f) 23/24 (f) 24/25 (f) 25/26 (f)
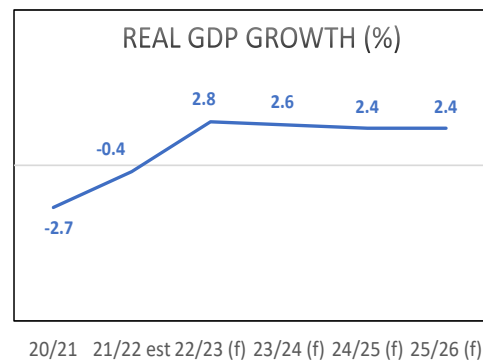
The following table/chart outlines key selected economic indicators to describe the current economic situation for the period .

◊ **Primary:** FY2023,the sector projects a positive growth of 1.6 percent reflecting an upward trend in the agricultural sector, mainly in squash (butternut), root crops and bananas. It is expected that both exports and local produce will increase, as the government plans to distribute more funds through public-private partnerships to support the sector.

◊ **Industrial :** The sector is estimated to rebound from the negative growth of 3.9 percent in FY 2022 to a negative growth of 0.7 percent in FY 2023. This is attributed to the ongoing economic activities, including the HTHH recovery reconstruction, climate change related projects.

◊ **Services:** The services sector projects growth at 4.1 percent for FY 2023, reflected resumption of economic activities in all the services sub-sectors following the re-opening of boarder in September, 2022.

◊ The **outlook** for Tonga is positive - estimated to grow at an average of 2.5 percent over the medium term, attributing to the continuous recovery activities and planned development projects expected to occur in outer years.

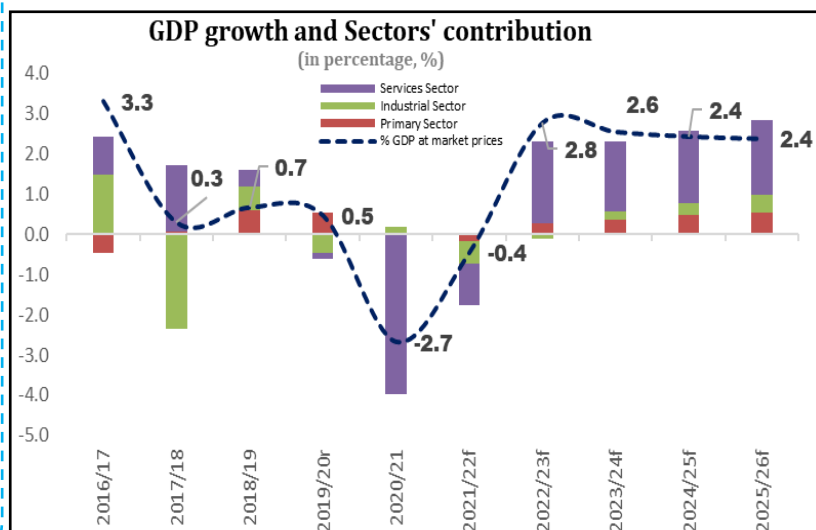**Figure 2: Economic Growth and Sector's Contribution**

GDP growth and Sectors' contribution (in percentage, %)

◊ The **Inflation** outlook is uncertain due to the current global economic conditions and ongoing geo-political events. Based on current data and analysts' expectations, inflation is projected to remain above the threshold of 5% referencing target by the end of the current financial year. However, in the medium term, inflation is expected to stabilize.

◊ **Foreign Reserve** is projected to remain comfortable at around 11 months of import cover by the end of 2023, sustained by large inflows of grants and donor funds for development projects in the near term. However, budget support and remittance receipts are expected to slow down, and import outflows are expected to continue to increase in line with the domestic economic recovery.

◊ Considering the ongoing labour mobility schemes and work opportunities available in Australia and New Zealand, it is anticipated that **Remittances** will increase.

Table 1: Selected Key Economic Indicators

PERIOD	Jan-23	Feb-23	Mar-23
Inflation(%)	9.7	8.7	9.4
Domestic	*13.3*	*10.4*	*12.7*
Imported	*7.0*	*7.4*	6.9
Foreign Reserves (mil)	911.1	911.2	883.7
Import Cover (Trade)	14.0	13.7	13.0
Fuel : Petroleum	3.35	3.48	3.52
Diesel	3.76	3.75	3.63
Remittances (mil)	485.2	494.8	-

Source: MOF&NRBT&MTED

Table 2: Recurrent Budget Performance (February FY2023)

	Original Budget 2022/23($m)	Budget (Jul-Mar)($m)	Actuals (Jul-Mar)($m)	Variance ($m)	Variance (%)	% spent/ received (Jul-Mar)
Total Receipts	406.8	305.1	293.6	-11.5	-3.8%	72%
Total Payments	437.0	327.8	267.6	60.1	18.3%	61%
Balance	**-30.3**	**-22.7**	**25.9**	**-71.6**		

	Original Budget 2022/23($m)	Budget (Jul-Mar)($m)	Actuals (Jul-Mar)($m)	Variance ($m)	Variance (%)	% spent/ received (Jul-Mar)
Revenues	**406.8**	**305.1**	**293.6**	**-11.5**	**-3.8%**	**72%**
Domestic Revenues	325.3	244.0	250.6	6.6	2.7%	77%
Tax	245.6	184.2	197.6	13.3	7.2%	80%
Income Tax	48.2	36.1	36.4	0.3	0.8%	76%
Trade Taxes	23.3	17.5	19.3	1.8	10.4%	83%
Tax on Goods & Services	106.6	80.0	94.9	15.0	18.7%	89%
Excise Tax	67.6	50.7	46.9	-3.8	-7.4%	69%
Non-Tax	79.7	59.7	53.0	-6.7	-11.2%	67%
Fees & Licenses	28.2	21.1	19.7	-1.5	-6.9%	70%
Entrepreneurial& Property	11.6	8.7	6.8	-1.9	-22.1%	58%
Miscellaneous	1.2	0.9	0.3	-0.6	-63.6%	27%
Capital & Transfers	38.6	29.0	26.2	-2.7	-9.5%	68%
Budget Support	81.5	61.1	43.0	-18.1	-29.6%	53%
Expenditures	**437.0**	**327.8**	**267.6**	**60.1**	**18.3%**	**61%**
Wage Bill	172.9	129.6	117.5	12.1	9.4%	68%
Operations	204.1	153.0	110.7	42.3	27.7%	54%
Assets	16.5	12.4	9.6	2.8	22.3%	58%
Debt	43.6	32.7	29.8	2.9	8.9%	68%
Balance	**-30.3**	**-22.7**	**25.9**	**-48.6**		

Overall Summary:

♦The **total recurrent** budget originally estimated a $30.3m deficit by the end of FY 2023. As of end of March 2023, the budget is currently at a $25.9m surplus, due to the World Bank budget support of $43m and $21m loan receipts from the IMF which have already been received at the beginning of the FY, coupled with low spending levels.

♦By end of March 2023, a **benchmark** of 75% is estimated to be received and spent from the original estimates. This translates to collecting $305.1m worth of receipts, and spending at $327.8m, resulting in an estimated deficit of $22.7m. However, in comparison to the actual performance as of end of March 2023, spending was 18.3% less and revenues was less by 3.8%.

♦**Total receipts** recorded as of March 2023 reached 72% or $293.6m of the original target. This includes 80% of targeted tax revenues being collected, or $197.6m, which is 20% higher than pre-pandemic levels. This better than expected performance includes attribution to higher prices (inflation) particularly in the revenues being collected from consumption tax on imports.

♦**Budget support** from development partners (normal annual allocations) have not been received to date, but will be before the end of the FY, except $23m from the World Bank and ADB.

♦Despite that **spending** is low as of Mar 2023 at only 61% of the total estimates, it is 10% higher in comparison to the same period last financial year due to higher operational spending, largely in overseas travels due to international borders re-opening. In comparison of spending on overseas travels alone in Jul-Mar 2023 and pre-pandemic times, is 26% or $1.1m higher.

Table 3: Gross Domestic Product (GDP)

Key economic indicators	20/21p	21/22f	22/23f	23/24f	24/25f	25/26f
Nominal GDP (*T$m*)	1,068.8	1,188.7	1,340.4	1,480.3	1,632.9	1,783.5
Real GPD per Capita (TOP)	106.4	118.8	130.3	140.4	151.1	161.2
Growth (%)	(2.7)	(0.4)	2.8	2.6	2.4	2.4

Table 4: Selected Key Social Indicators

Period	2018	2019	2020	2021	2022
Labor Force (15+)	**29504**				**32,319**
Male (%)	56.2				58.9
female (%)	43.7				41.1
Employment (15+)	28,598				31,037
Labor force participation rate					
male (%)	56.2				55.3
female (%)	38.4				37.3
Youth Unemployment Rate	8.9				
15-24					
Male					
Female					
Urban (youth unemployment)	9.2				
Youth unemployment rate by Island Division					
Tongatapu	19.5				
Vava'u	5.2				
Ha'apai	-				
Eua	12.7				
Niuas	-				
Total Unemployment rate (%)	**3.1**				**4.0**
Source:Labour force survey 2018,Statistic Department & ILO November 2022					
Total established staff					6,262
Total Civil Servants					6,390
Total Contract Staff					1,001
Daily Labor					809
Professional Contracts					189
Source: MOF,Statistic Department					
Total Number of Labor Mobility workers					
RSE (NZ scheme)	2,790	3,738	2,025	826	1,202
PALM (Australia scheme)	2,025	3,738	2,025	749	2,491
Source: Overseas employment Division ,MIA					

More employment demand over the month

National Reserve Bank job survey (March 2023) shows that :

♦ There has been a significant increase of 101.8% (58 job vacancies) in the number of advertised vacancies compared to the previous month.

♦ The main contributors to the monthly increase were the public administration, hotel and restaurant, and education sectors.

♦ The significant number of vacancies in these sectors also suggests that the New Year began with the initiation of various public and private projects.

♦ At annual rate, the advertised job vacancies significantly increased by 500 job vacancies (140.8%).

♦ This can be partly attributed to the growing availability of residency visas offered by the governments of Australia and New Zealand, which encourage the movement of domestic workers, in addition to the ongoing labor mobility schemes.