

ASIAN DEVELOPMENT BANK

**COUNTRY ASSISTANCE PLAN
(2000-2002)**

TONGA

December 1999

CURRENCY EQUIVALENTS

(as of 30 November 1999)

Currency Unit	—	Pa'anga (T\$)
T\$1.00	=	\$0.614400
\$1.00	=	T\$1.62760

ABBREVIATIONS

ADB	-	Asian Development Bank
ADF	-	Asian Development Fund
CEDAW	-	Convention on the Elimination of All Forms of Discrimination Against Women
EPSRP	-	Economic Policy and Public Sector Reform Program
EU	-	European Union
GDP	-	Gross Domestic Product
OCR	-	Ordinary Capital Resources
PFTAC	-	Pacific Financial Technical Assistance Centre
PIER	-	Pacific Islands Economic Report
POHQ	-	Pacific Operations Division
RETA	-	Regional Technical Assistance
SPPF	-	South Pacific Project Facility
SPRM	-	South Pacific Regional Mission
SSFCL	-	Sea Star Fishing Company Ltd.
TA	-	Technical Assistance
TDB	-	Tonga Development Bank
TEPB	-	Tonga Electric Power Board
UNDP	-	United Nations Development Programme

NOTES

- (i) In this Report, "\$" refers to US dollars.
- (ii) The fiscal year (FY) of the Government ends on 30 June.

FOREWORD

The Country Assistance Plan describes the planned program of assistance by the Asian Development Bank for Tonga covering the three-year period 2000-2002. It includes loan and technical assistance projects, as well as possible cofinancing from other donors. The CAP was prepared by the ADB between April and June 1999, in close consultation with the Government of Tonga, and other stakeholders. The CAP was discussed with the Board of Directors in October 1999 and has been revised by the ADB to incorporate recent developments. The assistance plan described in the CAP is only indicative and may be revised to reflect future developments.

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TONGA

I. Country Performance Assessment

A. Economic Performance Assessment

1. Tonga's economic growth performance over the last decade has been mixed. Between 1989/90 and 1994/95, real gross domestic product (GDP) grew at the average annual rate of 4.5 percent. In the subsequent three years, the economy has been in recession. Real GDP declined by 1.5 percent, 6.6 percent and 0.3 percent in 1995/96, 1996/97 and 1997/98 respectively. The inflation rate in the last year was 3 percent, up from 2.1 percent in 1997. The economic downturn largely reflected the performance of agriculture. This sector contracted in each of the last three years as squash production declined due to drought, disease, and lower world market prices. In addition, commerce, hotels and restaurants contracted in 1996-97, partly reflecting falling tourist numbers; and activity in the construction sector dropped dramatically in 1997 as a number of aid-funded projects were completed. While the manufacturing sector was stagnant, government services, which constitute about 15 percent of GDP, expanded at about 3 percent annually. Tonga has not been affected directly or indirectly by the Asian financial crisis, except through availability of cheaper oil.

2. In 1997-98, the merchandise trade deficit worsened as a result of declining squash exports and a resurgence of imports that was fuelled by a strong credit expansion. Between the end of the March quarters of 1997 and 1998, private sector credit rose 40 percent, while the Government changed from becoming a net lender to a net borrower as its budgetary position worsened. Although private remittances held up, tourism receipts declined as the currency was allowed to appreciate substantially in real terms. The balance of payments was placed under considerable pressure. The current account deficit grew to 11.1 percent of GDP by the end of the fiscal year, and the import cover of gross foreign reserves fell to around 2 months, compared with a cover of 5 months in 1996-97.

3. In response to balance of payments pressures, the Reserve Bank raised the reserve requirement on banks from 10 to 15 percent and sought to reduce liquidity through the tendering of short-term securities, though action in this regard was constrained by the weakness of its profit base. Fiscal policy was not supportive of the tight monetary policy. The historic practice of balancing the recurrent budget ceased in the 1996-97 fiscal year, and the overall budget deficit in 1997-98 was approximately 3 percent of GDP. Initially, devaluation of the currency was not contemplated, even though this would have encouraged greater inward remittance flows and improved Tonga's international competitiveness. However, by late 1999, balance of payments pressures had forced a devaluation of 11 percent against the US dollar. According to Government data, the increased budget deficit was partly due to a 15 percent increase in Government expenditure on wages and salaries.

4. The outstanding current economic issues are the ongoing recession, the stance of fiscal policy, and the fragility of the balance of payments. Zero growth in real GDP is expected in 1998/99. The 1998/99 budget envisages a return to a small recurrent budget surplus and an 18 percent rise in development expenditure, but these outcomes would only be achievable if extra-budgetary appropriations and past overprogramming of development spending were avoided. Indications are that an overall budget deficit of 1.8 percent of GDP is likely. The current account position is likely to improve in 1998/99 as squash production recovers, but there is a need for continued restraint of domestic demand. In this regard, the mix and the setting of macroeconomic policy are crucial.

5. Medium-term economic growth prospects depend heavily on the extent to which business confidence and private investment can be encouraged. The Government has committed to deregulation and public sector reform, but progress has been slow. The Government will need to show evidence of its openness to foreign investment, diversify export structure, ensure stability in the financial system, reduce the size of the public sector, and implement structural reforms in the economy. In particular, distortions in the current tax and tariff structures need to be removed, and the cumbersome system of granting business, trade and development licenses reformed. Also, a simple company registration system and a neutral, transparent policy towards foreign direct investment are needed. The tourism and fisheries sectors would be major beneficiaries of increased foreign investment flows.

6. Failure to implement such reforms will likely result in higher fiscal deficits, increased price volatility and a further decline in private sector investments. This will also lead to further deterioration in the current account position and economic growth, and dangerously low levels of foreign reserves.

B. Assessment of Socio-Environmental Performance

1. Poverty and Human Development Issues

7. Consistent with the pattern of other Pacific Island countries, Tonga has a small and narrow economy driven mainly by agriculture and, to a lesser extent, fisheries and tourism. Natural resources are limited, commodity prices are vulnerable to fluctuations in the world market, and the country is physically isolated and susceptible to natural disasters, particularly cyclones. Tonga comprises 169 low-lying coral and volcanic islands, only 36 of which are inhabited. The country has a total land area of less than 700 sq km.

8. According to official statistics, absolute poverty does not exist in Tonga. Traditional community-oriented lifestyles and strong extended family ties provide safety nets for most community and family members. Tonga has a total population of about 98,000 and a very low population growth rate¹. Social indicators such as average life expectancy, adult literacy, education levels and GDP per capita are all relatively high (Appendix 1, page 2).

9. Nevertheless, these official statistics mask some serious emerging problems, with important implications for social services, the labor market, and living standards.

10. The low population growth rate, for example, is largely due to high levels of international migration. Natural population growth is much higher, at 2.5 percent for the 1986 - 1996 period. The age structure of the population also has serious social implications, with 51 percent of the population under 20 years of age. Integration into the global economy and other forces of social change are eroding some aspects of traditional culture, including the extended family and its supporting values of reciprocity and redistribution. Although remittances continue to be high, it remains to be seen whether this trend will continue in the face of such changes.

¹ The average annual population growth rate since 1986 has been 0.3 percent, a further decline from the low 0.5 percent recorded for the 1976 to 1986 period.

11. Already, there are indications that poverty is prevalent in some sections of Tongan society. The vast majority of Tongans are in the subsistence or informal sector, and the search for employment, cash income and education has resulted in a high concentration of the population on the main island of Tongatapu. In 1986, one third of the population lived in the capital, Nuku'alofa. By 1996, this figure had risen to 68 percent. The rate of urban population growth is now more than five times higher than that in the rural areas. Squatter settlements exist in Nuku'alofa and Pangai in particular, where people live in wretched conditions, often in makeshift housing in swamps or by rubbish dumps, without clean water supply and with inadequate sanitation. There have been cases of child malnutrition and food deprivation within the poorer sections of society, including severe cases of marasmic malnutrition (protein and calorie deficiency). In 1994, the United Nations Development Programme (UNDP) estimated that 2 percent of all children under the age of five in Tonga were malnourished.

12. Further, as a result of high fat diets, high cigarette and alcohol consumption and more sedentary lifestyles, non-communicable diseases are increasing in Tonga and it is estimated that 15-20 percent of the adult population in Tonga is diabetic. Infant mortality has risen from 12.2 per 1,000 live births in 1991 to 16.2 in 1996, and the prenatal mortality rate is also relatively high at 15.5 deaths per 1,000 births in 1996.

13. There has also been little attention given to the social implications of the high degree of international migration from Tonga, although there are indications that this warrants more serious analysis. For example, as much as 75 percent of admissions to the pediatric ward of the main hospital are children living with grandparents or other relatives, their parents having migrated. The nature of international migration and remittances is also changing. There is an increasing tendency for migrating families to leave their children in Tonga with relatives; and to remit support in kind rather than cash.

2. Gender Issues¹

14. The status of women in Tongan society is inextricably linked to the highly stratified feudal order that lies at the heart of this constitutional monarchy. Unlike many Pacific countries, women in Tonga have traditionally had a nominal status generally superior to that of men, based on the cultural obligation of men to their sisters. This status has gradually been declining as a result of demographic and social changes, including the trend towards giving greater precedence to women's status as wives, rather than their cultural status as sisters. Further, rapid urbanization has seen a commensurate decline in traditional values, rising poverty and landlessness. One consequence of large-scale international migration is that women are often left behind to manage as single parents.

15. Contrary to traditional stereotypes and national accounting indicators, women are vital players in virtually all agricultural work, including commercial agriculture. This is in spite of the difficulties women face in obtaining access to credit, by virtue of their negligible land rights. Despite women's better repayment rates and overall creditworthiness, few women are able to access loans for commercial crops like vanilla, squash or coffee, even though their role in these sectors has become increasingly important.

16. Women's economic activity remains largely invisible and undervalued in national accounts and sectoral reporting, due to data shortages and biases in most areas. As a result,

¹ Bain, A.H. *Women in Tonga*, ADB Country Briefing Paper, 1998.

the mainstreaming of gender into national planning and macroeconomic policy is seriously inhibited. Gender biases in the definition of work, for example, mean that official statistics show as much as 58 percent of women over 15 years as not being economically active. According to national statistics, only 119 women were employed in agriculture and fisheries in 1996.

17. Even in areas of employment where women are better represented formally and where non-discriminatory human resource management policies apply, gender biases persist. For instance, about 46 percent of civil service employees are women. Yet almost 85 percent of these women are in lower level positions. There is only one woman employed at the most senior level in the civil service.

18. Unlike those of other Pacific countries, the Tongan Constitution carries no general affirmative action provision that could be invoked in favor of women. Tonga has yet to ratify the United Nations Convention on the Elimination of All Forms of Discrimination Against Women (CEDAW). Ratification is by no means assured in the near future either, as it would require the Tongan Government to guarantee, through legal and other measures, the equality of women in national law and policy. In this regard, discrimination in the area of land law is one of the most politically sensitive issues.

3. Environment

19. Tonga's limited land resources in conjunction with high population growth rates in urban centers have put considerable pressure on the country's natural resources and worsened its environmental problems. Due to limited land resources, mangrove forests have been cleared and filled to make home sites. Conversion of forest land for agriculture purposes in the past has virtually destroyed Tonga's entire indigenous forest resources with the remaining area of natural hardwood forest being estimated at about 4,000 hectares, most of which is located on steep and inaccessible areas of 'Eua island.

20. As a result of unregulated fishing by an increasing number of artisanal and commercial fishermen as well as the introduction of more efficient fishing technology, coastal and near coastal fisheries has suffered from over-exploitation of traditional marine species and much of the near shore fisheries show signs of being over-fished. As a consequence, the Government introduced a complete ban on the export of sea cucumber, a closed season for turtle and mullet fishing, and introduced minimum sizes for the harvest of certain marine species.

21. Environmental administration is vested with the Environmental Planning Section (EPS) of the Ministry of Lands, Surveys and Natural Resources. Although environmental impact assessment (EIA) policy is in place, few in-house EIAs have been carried out. There is a large body of legislation related to environmental issues but most of this is outdated (50 years and older). Given the difficulties in administering environmental controls in a cohesive and coordinated manner, discussions are underway to introduce comprehensive environmental legislation.

C. Governance: Sound Development Management

22. Tonga's constitutional monarchy represents a unique political system in the Pacific region. Tonga is also the only country in the region that succeeded in protecting itself from colonization, a fact that has given strength to the country's aristocratic system and cultural values over the years. Political life is dominated by the King and 33 hereditary nobles. The King appoints the Prime Minister and members of the Privy Council, the country's highest

executive body. Although there is a pro-democracy movement in Tonga, the emphasis is on seeking to improve accountability within Government; the King is greatly respected, and few challenge retention of the monarchy. Although the sluggish nature of the economy was a major factor in the March 1999 election, for instance, the effect was to diminish support for the pro-democracy movement. Of the nine directly-elected parliamentary seats, the share held by pro-democracy supporters fell from seven to five. The other nine seats are directly appointed by the King from amongst the 33 nobles.

23. The public sector in Tonga is characterized by low productivity, inefficiencies and a bias against foreign investment. The size of the public sector and its role in the economy remain major issues that are impacting negatively on economic development. For instance, a 15 percent increase in public sector wages since 1995/96 has been a major contributor to the declining fiscal situation. Although the Government has committed to public sector reform, progress is slow. The structure of decision-making, and the autonomy given to Ministers, make it difficult to undertake integrated reform.

D. Implementation Assessment

1. The Portfolio

24. The Asian Development Bank (ADB) has approved 14 loans totaling \$47.8 million from ADF to Tonga since it joined the ADB in 1972. The most recent of these was approved in December 1996 and to date has not become effective. Since 1972, the ADB has also provided technical assistance grants totaling \$10.8 million, for 43 projects. Four loans and nine technical assistance activities are currently under implementation.

25. Of the 14 loans, Project completion reports have been prepared for 10 project loans, eight of which have been post-evaluated (see Appendix 2).

26. The three multiproject loans were evaluated as being generally successful. The subprojects supported under these loans significantly increased the cash incomes of over 1,000 smallholder and artisanal fishermen, provided safe and reliable shipping services to the outer islands, significantly improved education, health and transport infrastructure, and contributed successfully to industrial development and employment generation through the establishment of the small industries center. Among the three development finance loans to the Tonga Development Bank (TDB), the first loan, which was approved in 1978, was rated as being partly successful, while the two subsequent loans were rated as generally successful. These latter two loans have achieved their objective of supporting industrial and agricultural development in the country. The technical assistance activities linked to these loans also improved TDB's institutional efficiency. Nevertheless, concerns remain with TDB's increasing level of arrears and its declining profitability as a result of high operating costs.

27. The ADB's loan portfolio currently under implementation consists of four projects, all administered by the South Pacific Regional Mission (SPRM).

28. The most recent review by the ADB has been of the ongoing Outer Islands Agriculture Development Project. The review found that, while implementation of the agriculture development and telecommunication components has generally been satisfactory, the components related to the construction of roads and buildings have experienced major delays. These have been due to the lack of road building equipment, cumbersome internal Government procedures in the awarding of civil works contracts, and the non-availability of adequate

amounts of counterpart funds for building construction. There were also delays in the establishment of community funds. Finally, the loan covenant related to preparation of an action plan to achieve cost recovery for Tonga Trade has yet to be complied with.

29. The *Fisheries Development Project*, approved in 1990, only became effective in 1994. Although it began poorly, the pace of implementation has improved since September 1996 particularly, when the ADB approved the procurement of second-hand fishing vessels. With support from the loan and related technical assistance, the executing agency, Sea Star Fishing Company Ltd. (SSFCL), has been able to improve significantly the efficiency of its operations. Major progress has also been made in relation to the privatization of SSFCL. The sale of all Government equity in SSFCL is expected to be completed in 1999.

30. Implementation of the *Transport Infrastructure Project* is progressing satisfactorily and the project is effectively addressing the Government's policy to enhance infrastructure facilities in the outer islands. Based on the findings of an ADB review in September 1998, the project is also likely to exceed the economic benefits assessed during appraisal. The project is due for completion in December 1999, and all components are expected to be successfully completed on schedule.

31. Since approval was obtained in December 1996, the *Second Power Development Project* loan has never become effective, due to protracted delays in submitting legal opinion and signing the Subsidiary Loan Agreement. In the meantime, the Government privatized power generation in March 1998, rendering the project design obsolete. Although the Tonga Electric Power Board (TEPB) requested a reformulation to focus the project on power distribution rather than power generation, the ADB's assessment was that the revised project was unlikely to be economically or financially viable. In January 1999, the ADB recommended that the loan be allowed to lapse.

32. The ongoing technical assistance program is focused on macroeconomic and fiscal management, the promotion of trade, cost recovery and pricing policy for physical infrastructure, as well institutional strengthening of the Ministry of Agriculture, SSFCL, the Ministry of Marine and Ports and Tonga Trade. While some of these activities have been affected by insufficient availability of counterpart staff and a slow consultant recruitment process, implementation of most ongoing technical assistance activities is smooth and all are expected to contribute significantly to the strengthening of the institutions concerned.

2. Issues in Project Implementation

33. For most ADB projects in Tonga in the past, project implementation has been constrained by the insufficient availability of counterpart funds and weak project management. Problems related to loan effectiveness have also been experienced under two projects. In addition, delays in the procurement of goods and services have been experienced due to executing agencies' lack of familiarity with the ADB's procurement procedures, as well as burdensome and excessive coordination and approval procedures within both the Government and the ADB (e.g. *Fisheries Development Project*). Compliance with loan covenants, in particular with those related to financial statements, is another issue affecting all projects currently under implementation.

34. To improve project implementation and to assess the impact on the ground, project performance management systems, based on measurable success indicators, are gradually being introduced for all projects in Tonga. To avoid problems delaying loan effectiveness in

future, (as experienced under the *Fisheries Development Project* and the *Second Power Development Project*), confirmation will be sought from the Government that all pipeline projects are firmly anchored in its national development plans and are given high priority with respect to counterpart funding and staffing.

II. Country Operational Strategy

35. Through successive Development Plans (the seventh covers 1996-2000), the Government is generally committed to diversifying the economy, increasing employment, controlling external financial balances, reforming the public sector and maintaining a high quality of life with as much equity as possible. The Government's development strategy seeks to promote sustainable economic growth by promoting private sector development, encouraging exports and expanding financial services, as well as through the construction and maintenance of physical infrastructure necessary for economic development. The strategy also seeks to ensure equitable distribution of development benefits and conservation of the environment. The priority sectors for public sector investments¹ are health, education, water and sanitation, and maintenance and rehabilitation of transport infrastructure, including for tourism and communication. The agriculture, fisheries and tourism sectors have been identified as those with the greatest potential for contributing to economic growth. This growth is expected to be fuelled by private sector investments, with the role of government mainly limited to providing supporting infrastructure.

36. In support of the Government's development strategy, the ADB will continue to focus its operations in areas that support private sector development and a corresponding reduction of the current excessive role of the Government in business activities. The Government has now moved toward a rational, forward-looking process of policy formulation and fiscal management, using a program budgeting framework that began with the 1998/99 budget. This will facilitate the implementation of other much-needed reforms such as in the tax system, investment regulations, and management of public enterprises. The ADB's role is to promote the development of an economic environment conducive to business activity and to improve the responsiveness of the public sector to the needs of the business community and general public.

37. The ADB's lending and technical assistance program has been made contingent on the Government's willingness to undertake reforms that have emanated from previous technical assistance activities carried out since 1991. The ADB has not programmed new loans in Tonga since 1996, pending discussions with the Government on its reform directions. Most recently, preliminary discussions have been held in 1999 on the Government's interest in undertaking an *Economic Policy and Public Sector Reform Program (EPSRP)*, with ADB support. The objective of the EPSRP will be to enhance sustainable private sector-led economic growth by improving the efficiency with which public sector services are being delivered and promoting policies that generate an environment conducive to increased investment and employment by the private sector. While the detailed policy initiatives to be included under the EPSRP have yet to be identified and developed, it is likely to address policies to strengthen public sector management, promote private sector-led economic growth, enhance social security and improve financial sector efficiency.

¹ Outlined in Kingdom of Tonga *Guidelines for the preparation of the Government Budget Estimates for the Year 1999-2000*.

38. The ADB's operational program for 2000–2002 includes a number of technical assistance activities to assist in the design and implementation of policy initiatives under the EPSRP. These proposals are detailed in Section III below. EPSRP is to be further developed and the reform program and associated technical assistance to be decided and confirmed after during the later half of the year.

39. In light of this strategy, and Tonga's constrained institutional capacity, the ADB's operational program will be selective in the choice of sectors and will focus on small and sequenced projects, each with measurable performance indicators to assess progress in achieving tangible development impact. In November 1998, Tonga was reclassified by the ADB's Board of Directors from a category A to a category B country. Thus, while Tonga will continue to have access to Asian Development Fund (ADF) resources, the overall loan portfolio in future will also comprise a limited amount of Ordinary Capital Resources (OCR) funding.

III. Sector Strategies

A. Agriculture

40. Agriculture is the mainstay of the Tongan economy, the single largest contributor to GDP. During the past ten years, there have been significant achievements in agriculture, particularly in the development of niche markets crops such as squash and vanilla. At the same time, Tonga is very vulnerable to fluctuating prices, market uncertainties and the challenges of competing in a liberalized global economy. For example, GDP growth fell dramatically between 1993/94 and 1995/96 as a result of fluctuating fortunes in the squash industry. Negative growth has continued in the agriculture sector since, due to declining vanilla exports. Such vulnerability has raised concern about the long term viability of reliance on a small range of niche market crops and highlighted the importance of a more diversified economic base. Given its strategic importance for growth and employment generation, the ADB has agreed to undertake an agriculture sector review in Tonga. This sector has not been assessed for the last ten years. The study will help to ensure that Government interventions in the agriculture sector are in line with its development objectives, and will be undertaken with a view to supporting preparation of agriculture-related policy reforms under a broader reform program. The review will also examine needs for strengthening environmental management.

B. Governance Dimensions of Asian Development Bank Operations

41. The ADB's economic and sector work as well as policy dialogue undertaken since 1992 have focused on budget reform and planning processes, and on improving Government effectiveness, particularly in financial management. The public sector is generally well educated although shortages in some skills have maintained a heavy reliance upon foreign experts funded by various aid donors in key ministries. The ADB's technical assistance work is improving local capacity and will support bilateral efforts to streamline and improve efficiency of the public sector.

42. In the next three years, the ADB's policy dialogue will focus on economic and public sector management and fiscal reform to stimulate economic growth. The strategic focus of the operational program will be on promoting implementation of the reforms that have emanated from previous technical assistance, and will include capacity building and measures to improve public sector efficiency. The Ministry of Finance, supported by the ADB and the international donor community, is actively attempting to improve public sector management, through the

adoption of policies, program budgeting, and better fiscal coordination between Government departments. Also, as a first step in the development of the EPSRP, the ADB has been asked to assist the Government to undertake a review of the public and financial sectors. This technical assistance will support the initiation of a broad-based consultative process among ministries, and will prepare the detailed design of the EPSRP.

C. Gender Dimensions of Asian Development Bank Operations

43. The ADBs' Gender and Development policy seeks to promote gender equity by mainstreaming gender considerations in all ADB operations. Investments in women also make good economic sense, enhancing productivity, economic efficiency and growth prospects. Active effort to promote the participation of women throughout the development process is recognized as crucial to achieving sustainable development. In Tonga, a recent study¹ has highlighted the potential that exists to improve the gender-related development impacts of all ADB-supported programs. These recommendations will be addressed in future programming, as well as in the monitoring and implementation of ongoing activities. One stark example of the potential for improvement has been in the ADB's support for the provision of credit by the Tonga Development Bank (TDB). Women received only six out of a total of 74 loans disbursed in 1996. The fact that few women overall have benefited from this project is the result of design factors that have not created an enabling environment for women borrowers, such as the nature of the targeted projects (capital/structural development) and the large minimum loan size.

D. Private Sector Operations

44. Private sector development is at the center of the ADB's country strategy in Tonga. In the past, emphasis has been placed on the provision of lines of credit through the Tonga Development Bank. More recently, the ADB's policy dialogue to promote private sector development has centered on the establishment of an institutional and economic environment conducive to private sector-led economic growth. An initial review of the financial sector undertaken in early 1999, for example, has helped to identify the major financial sector issues to be addressed through the EPSRP. These include increasing the efficiency of monetary policy, strengthening the prudential framework and banking supervision, promoting the development of inter-bank foreign exchange and money market, enhancing the legal environment for commercial lending, and improving access to capital by private sector enterprises.

45. The ADB also supports private sector development in Tonga through its contributions to the South Pacific Project Facility (SPPF), a regional initiative supported by a number of donors to assist Pacific countries in privatization efforts and to provide management advice to private companies. Since its inception in 1990, the SPPF has completed five and has eight ongoing projects in Tonga.

IV. Regional Economic Cooperation

46. As for other Pacific countries, regional and sub-regional cooperation feature strongly in Tonga's national development strategy. Tonga is a member of all the major regional agencies promoting development cooperation in the Pacific. The ADB has also promoted sub-regional cooperation in the Pacific, primarily through regional technical assistance (RETA) activities. These have focused on trade, economic policy and management issues. Tonga has expressed interest in participating in RETA activities, to examine issues such as building trading

¹ Bain, A.H. *Women in Tonga*, ADB Briefing Paper, December 1998.

relationships with larger, more dynamic trading blocs outside the region; cooperative arrangements in transport, particularly aviation and shipping; natural resource management with a focus on fisheries and forestry; and regional approaches to provision of certain economic and social services.

V. Donor Activities and Aid Coordination

47. External assistance to Tonga is estimated to be over 20 percent of GDP. Japan, the European Union (EU), Australia and New Zealand are the main donors other than the ADB (Appendix 3). External assistance is greater than the national recurrent budget and comprises about 80 percent of the development budget. In recent years, grant assistance from Japan has been provided for projects to build roads on the main island of Tongatapu and to develop marine aquaculture. EU grants have been directed to the Vava'u group of islands. Australia and New Zealand channel the bulk of their assistance to support human resource development activities, mostly through scholarships in their home countries. Australia also assists with infrastructure development, while New Zealand has been targeting support for private sector development. The availability of grant funds from these sources has tended to reduce the demand for loan financing from the ADB, particularly in the social sectors.

48. Aid is coordinated by the responsible aid coordinating agencies. The Development Coordinating Committee under the Chair of the Deputy Prime Minister is mandated to advise the Government on aid related issues. However, the island groups of Vava'u and Ha'apai have separate Committees responsible for development. In addition, several other Ministries tend to take the lead in developing their own development budgets. This delineation of responsibilities causes some coordination problems. The Ministry of Finance is responsible for loan management and preparation of the development budget.

49. Donor efforts to promote and assist with various aspects of economic and public sector reform will need to be tightly coordinated in the development of the EPSRP, to ensure that the reforms are appropriately sequenced and supportive of each other.

VI. Cofinancing and Catalyzing External Resources

50. To date, cofinancing possibilities have been limited, as projects are relatively small. However, the ADB maintains regular dialogue with other donors on potential cofinancing opportunities.

VII. Asian Development Bank 's Operational Program

51. The planned loan and technical assistance pipeline for the period 2000 - 2002 is summarized in Table 1. The detailed list of projects is in Appendix 4 and lending by type and sector is summarized in Appendix 5. The project profile of a 2000 loan is in Appendix 6.

Table 1: Lending and Technical Assistance Program, 2000-2002

A. Public Sector Lending Program										
	1998 (Actual)		1999		2000		2001		2002	
	(No.)	(\$ million)	(No.)	(\$ million)	(No.)	(\$ million)	(No.)	(\$ million)	(No.)	(\$ million)
Lending program	-	-	-	-	-	-	1	10.0	-	-
ADF	-	-	-	-	-	-	1	10.0	-	-
OCR	-	-	-	-	-	-	-	-	-	-
Lending Pipeline	-	-	-	-	1	10.0	-	-	-	-
ADF	-	-	-	-	1	10.0	-	-	-	-
OCR	-	-	-	-	-	-	-	-	-	-

B. Technical Assistance Program										
	1998 (Actual)		1999		2000		2001		2002	
	(No.)	(\$'000)	(No.)	(\$'000)	(No.)	(\$'000)	(No.)	(\$'000)	(No.)	(\$'000)
TA Program	-	-	-	-	1	600.0	-	-	-	-
TA Pipeline	-	-	-	-	-	-	1	450.0	1	450.0

^a The Program is comprised of the firm projects.

^b The Pipeline consists of the Program (firm projects) and standby projects. In 2001 and 2002, there is no distinction between firm and standby.

VIII. Economic and Sector Work Program

52. An economic report on Tonga in the *Pacific Islands Economic Report* (PIER) series was published in 1996. A Country Economic Review is planned for 1999-2000. A review of the public and financial sectors will be undertaken in conjunction with the implementation of technical assistance for public sector reform.

IX. Local Cost Financing

53. There is limited capacity for domestic resource mobilization due to the variable and often low returns to investment in Tonga. Therefore, the ADB will continue to provide finance for local currency costs as justified and without adversely affecting the exchange rate or the domestic investment environment.

TONGA
COUNTRY PERFORMANCE INDICATORS

Item	1994/95	1995/96	1996/97	1997/98	1998/99	1999/00 ^a
A. Income and Growth						
1. GDP per Capita (dollars, current market prices)	1,757.0	1,888.0	1,908.0	1,787.0	1,547.0	...
2. GDP Growth (% in constant prices)	6.3	-3.7	-1.4	0.1	2.2	...
Agriculture	12.1	-9.2	-3.0	-2.1	-0.1	...
Industry	3.5	4.1	-8.9	-6.0	8.6	...
Services	3.1	-1.0	1.0	3.2	2.5	...
B. Saving and Investment (current market prices)						
	(percent of GDP)					
1. Gross Domestic Investment	14.0	...	...	...	...	...
2. Gross Domestic Saving	-15.0	...	...	...	...	...
C. Money and Inflation						
	(annual percent change)					
1. Consumer Prices (annual average)	1.3	3.1	2.1	3.3	...	...
2. Broad Money (M2)	42.2	48.3	55.3	58.7	...	...
D. Government Finance						
	(percent of GDP)					
1. Total Revenue	58.2	62.7	60.6	85.3	75.2	...
2. Total Expenditure and Net Lending	55.5	64.6	61.7	67.3	72.6	...
3. Overall Surplus/Deficit (-)	2.7	-1.9	-1.1	-2.0	2.8	...
E. Balance of Payments						
1. Merchandise Trade Balance (% of GDP)	-32.6	-38.3	-30.0	-110.0	-28.6	...
2. Current Account Balance (% of GDP)	-29.7	-24.9	-8.1	-15.9	-15.8	...
3. Export (\$) growth (annual percent change)	-18.6	-5.6	-20.6	-8.9	22.0	...
4. Import (\$) growth (annual percent change)	35.4	-9.9	-10.0	31.8	...	...
F. External Payments Indicators						
1. International Reserves (T\$ million, end of period)	30.1	29.8	32.8	21.3	35.0	...
- months of imports	3.8	3.8	4.4	2.5	4.2	...
2. External Debt Service (% of exports)	18.1	20.7	28.4	33.0	34.2	...
3. External Debt (% of GDP)	34.9	33.6	30.7	34.9	36.2	...
Memorandum Items:						
GDP at factor cost (current prices, T\$ million)	183.9	191.7	193.2	205.1	208.4	...
GDP at market prices (current prices, T\$ million)	212.2	219.4	227.9	230.4	240.5	...
Exchange Rate (Tonga Pa'anga per US dollar)	0.7800	0.8100	0.8120	0.7310	0.6220	...
Population ('000)	97.4	97.7	98.1	98.4	98.7	...

^a Estimates

The International Reserves for 1998/99 (as of 18th June 99) and 1999/2000 (as of 2 July 99).

The Import Cover (months of Imports) for 1998/99 (as of 18th June 99) and 1999/2000 (as of 2 July 99).

TONGA
COUNTRY PERFORMANCE INDICATORS

	1986	1990	1998
POPULATION INDICATORS			
Total Population ('000)	94.6	...	98.7
Annual Population Growth Rate (% change)	0.5	...	0.3
SOCIAL INDICATORS			
Total Fertility Rate (births per woman)	4.2	...	43.0
Maternal Mortality Rate (per hundred thousand live births)	...	...	160.0
Infant Mortality Rate (below 1 year; per '000 live births)	20.4	12.2	19
Life Expectancy at Birth (years)	65.0	...	68.0
Female	67.0	...	71
Male	63.0	...	65
Adult Literacy (%)	99.6	...	99.0
Primary School Enrollment (% of school age population)	...	...	90.0
Female	...	...	91.0
Secondary School Enrollment (% of school age population)	...	...	67.0
Female	...	...	71.0
Child Malnutrition (% of under age 5 underweight)	...	...	2.0
Population Below Poverty Line (%)	...	...	...
Income Ratio of Highest 20% to Lowest 20%	...	...	...
Population Under 15 Years of Age (%)	...	...	39.0
Population with Access to Safe Water (%)	99.0	...	95.0
Population with Access to Sanitation (%)	...	...	85.0
Public Education Expenditure as % of GDP	...	...	4.6
Public Health Expenditure as % of GDP	...	...	N.A.
Human Development Index	...	...	0.647
Human Development Global Ranking	...	...	107
Human Poverty Index	...	...	5.9
ENVIRONMENTAL INDICATORS			
Forestry			
Deforestation			
Total Area (km ²)	...	...	...
Annual deforestation	...	...	...
Biodiversity			
Nationally protected area	...	...	...
Area	...	...	...
Number	...	...	...
As % of land area	...	...	...
Biosphere reserves	...	...	...
Area	...	...	...
Number	...	...	...
World Heritage sites (number)	...	...	...
Wetlands of international importance	...	...	...
Area	...	...	...
Number	...	...	...
Land Use			
Cropland; permanent pasture	...	...	...
Air Pollution (Ambient concentrations)	...	...	...
Particulates	...	...	...
SO ₂	...	...	...
Water Pollution (concentration of pollutants in water bodies)	...	...	...
Biochemical Oxygen Demand (BOD)	...	...	...
Chemical Oxygen Demand (COD)	...	...	...
Global Environmental Problems	...	...	...
CO ₂ emissions (total and per capita)	...	...	...

Source: Pacific Human Development Report

TONGA

PORTFOLIO PERFORMANCE

Table 1 : Implementation, Disbursement Performance and Postevaluation Results

Public Sector Projects only
(as of 31 December 1998)

A. Project Portfolio ^b	Net Loan Amount \$ million %		Rating (No.) ^a									
			Total		Implementation Progress				Development Objecti			
			No.	%	HS	S	PS	U	HS	S	PS	
Agriculture and Natural Resources	5.84	28.4	2	50.0	-	2	-	-	-	-	2	-
Energy	4.79	23.3	1	25.0	-	1	-	-	-	-	1	-
Finance and Industry	-	-	-	-	-	0	-	-	-	-	0	-
Social Infrastructure	-	-	-	-	-	0	-	-	-	-	0	-
Transport and Communications	9.93	48.3	1	25.0	-	1	-	-	-	-	1	-
Others/Multisector	-	-	-	-	-	0	-	-	-	-	0	-
Total	20.56	100.0	4	100.0	0	4	0	0	0	0	4	0

B. Disbursements ^c	OCR	ADF	Total
(1) Total funds available for withdrawal (\$ mn, active loans only)	-	15.77	15.77
(2) Disbursed amount (\$ mn, cumulative, active loans only)	-	9.86	9.86
(3) Percentage disbursed [(2)/(1)] (%)	-	62.53	62.53
(4) Disbursements (\$mn, active loans only, latest year)	-	4.88	4.88
(5) Disbursement ratio (%) ^d	-	46.33	46.33

C. Net Transfer of Resources ^e (\$ million)	OCR	ADF	Total
Net transfer in 1995	-	5.10	5.10
Net transfer in 1996	-	2.40	2.40
Net transfer in 1997	-	1.50	1.50
Net transfer in 1998	-	4.30	4.30

D. Post-Evaluated Projects 1. Postevaluation Rating (as of 31 December 1998)	1968 - 1977		1978 - 1987		1988 - 1998		1968 - 1998	
	No.	%	No.	%	No.	%	No.	%
Rated Generally Successful (GS)	-	-	3	75.0	4	-	7	87.5
Rated Partly Successful (PS)	-	-	1	25.0	-	-	1	12.5
Rated Unsuccessful (US)	-	-	-	-	-	-	-	-
No Rating	-	-	-	-	-	-	-	-
Total	0	0.0	4	100.0	4	0.0	8	100.0

2. Postevaluation Rating by Sector 1968-88 (as of 31 December 1998)	GS		PS		US		NR		Total	
	No.	%	No.	%	No.	%	No.	%	No.	%
Agriculture and Natural Resources	-	-	-	-	-	-	-	-	-	-
Energy	1	12.5	-	-	-	-	-	-	1	12.5
Finance and Industry	2	25.0	1	12.5	-	-	-	-	3	37.5
Social Infrastructure	-	-	-	-	-	-	-	-	-	-
Transport and Communications	1	12.5	-	-	-	-	-	-	1	12.5
Others/Multisector	3	37.5	-	-	-	-	-	-	3	37.5
Total	7	87.5	1	12.5	0	0.0	0	0.0	8	100.0

^a HS: Highly satisfactory; S: Satisfactory; PS: Partially satisfactory; U: Unsatisfactory

^b Excludes loans closed during the year.

^c Excludes loans closed during the year without disbursement.

^d Disbursement Ratio is defined as the ratio of the total disbursement in a given year over the net loan amount available at the beginning of the year plus the loan amounts of newly approved loans which have become effective. "Net loan amount at the beginning of the year" includes all effective loans at the beginning of the year. "Loan amounts of newly approved loans which have become effective" includes loans approved before and after the beginning of the year that have become effective after the beginning of the year.

^e Includes private sector projects for countries with private sector operations.

Source : OPO (A), CTD (B & C), OEO (D)

TONGA
PORTFOLIO PERFORMANCE

Table 2: Status of Project Implementation
Public Sector Projects Only
(As of 31 December 1998)

Sector ^a	Project Title	Net Loan Amount		Approval Date (mm/yy)	Effectivity Date (mm/yy)	Closing Date		Physical Progress (% complete)	Cum Contract Awards (\$ million)	Cummulative Disbursement (\$ million)	Project Performance Rating ^b	
		OCR (\$ million)	ADF			Original (mm/yy)	Revised (mm/yy)				Implement Progress	Development Objective
AGR	Loan No. 1030-TON (SF) Fisheries Development		2.49	Sep-90	Jun-94	Dec-94	Dec-98	99	2.40	2.37	S	S
AGR	Loan No. 1412-TON (SF) Outer Island Agriculture Development		3.35	Dec-95	Dec-96	Jun-01		55	2.36	1.90	S	S
ENE	Loan No. 1497-TON (SF) 2nd Power Development		4.79	Dec-96		Jun-02		0	0.00	0.00	S	S
T&C	Loan No. 1303-TON (SF) Transport Infrastructure		9.93	Jun-94	Aug-95	Dec-99		90	7.69	5.59	S	S
Total		0.00	20.56						12.45	9.86		

^a Sector:

AGR: Agriculture & Natural Resources

ENE: Energy

SOC: Social Infrastructure

I&F: Industry and Finance

T&C: Transport and Communications

OTH: Multisector/Others

^b HS: Highly satisfactory; S: Satisfactory; PS: Partially satisfactory; U: Unsatisfactory

Note: Excludes loan(s) closed during the year.

TONGA
OVERALL EXTERNAL ASSISTANCE

External Source (\$ million)	Past 3-5 Years (annual average)		1998 Approvals	
	Loan/Credit	TA	Loan/Credit	TA
A. Multilateral Assistance				
Bank		2.20		9.62
UNDP		0.40		0.10
World Bank				
Subtotal		2.60		9.72
B. Bilateral Assistance				
Australia		9.10		6.27
New Zealand		3.60		2.97
Canada		0.08		0.17
France		2.00		0.09
Germany		0.60		0.05
Italy	
Japan		10.00		6.11
United Kingdom		0.10		0.10
United States		0.05		0.22
Subtotal		25.53		15.98
Total		28.13		25.70
Memo Items:				
External Assistance as % of Current Expenditures				
External Assistance as % of Capital Expenditures				

Sources: POHQ (estimates), and Government of Tonga.

TONGA
LENDING PIPELINE AND TECHNICAL ASSISTANCE PROGRAM, 2000-2002
(Amounts in \$ million)

Project Name	Strategic		Responsible Division	Year of PPTA	PROJECT COST				Gov't	Cofinancing (Others)
	Dev't Objectives a				TOTAL	Bank		Total		
	Primary	Secondary				OCR	ADF			
2000 STANDBY LOANS										
Others										
1. Economic and Public Sector Reform	ECO		POHQ	1999	10.0	0.0	10.0	10.0	0.0	0.0
Subtotal					10.0	0.0	10.0	10.0	0.0	0.0
Total					10.0	0.0	10.0	10.0	0.0	0.0
2001 LOAN PIPELINE										
Others										
1. Economic and Public Sector Reform	ECO		POHQ	1999	10.0	0.0	10.0	10.0	0.0	0.0
Subtotal					10.0	0.0	10.0	10.0	0.0	0.0
Total					10.0	0.0	10.0	10.0	0.0	0.0
2002 LOAN PIPELINE										
NONE										
2003 LOAN PIPELINE										
To be determined										

^a ECO = Economic Growth; HD = Human Development; POV = Poverty Reduction; WID = Women in Development; and ENV = Environmental Protection.

TONGA
LENDING PIPELINE AND TECHNICAL ASSISTANCE PROGRAM, 2000-2002

Sector/Project Name	Responsible Division	Type of TA	Amount (\$'000)		
			Bank	Others	Total
2000 TECHNICAL ASSISTANCE PROGRAM					
Others					
1. Economic and Public Sector Reform Phase I	POHQ	AD	600.0		600.0
	Subtotal		<u>600.0</u>		<u>600.0</u>
Total			<u>600.0</u>		<u>600.0</u>
2001 TECHNICAL ASSISTANCE PROGRAM					
Others					
1. Economic and Public Sector Reform Phase II	POHQ	AD	450.0		450.0
	Subtotal		<u>450.0</u>		<u>450.0</u>
Total			<u>450.0</u>		<u>450.0</u>
2002 TECHNICAL ASSISTANCE PROGRAM					
Others					
1. Economic and Public Sector Reform Phase III	POHQ	AD	450.0		450.0
	Subtotal		<u>450.0</u>		<u>450.0</u>
Total			<u>450.0</u>		<u>450.0</u>
2003 TECHNICAL ASSISTANCE PROGRAM					
To be determined					

TONGA
LENDING PROGRAM BY TYPE AND SECTOR, 2000-2002

Classification	2000 (Firm)		2001-2002	
	No.	% ^a	No.	% ^a
By Type				
A. Economic Growth		0.0	1	100.0
B. Projects Directly Aimed at Social Concerns		0.0		0.0
C. Projects Directly Aimed at Environmental Concerns		0.0		0.0
D. Economic Growth-oriented Projects with Social and/or Environmental Concerns		0.0		0.0
Total	0	0.0	1	100.0
By Sector				
A. Agriculture and Natural Resources		0.0		0.0
B. Energy		0.0		0.0
C. Finance		0.0		0.0
D. Transport and Communications		0.0		0.0
E. Social Infrastructure		0.0		0.0
F. Others/Multisector		0.0	1	100.0
Total	0	0.0	1	100.0

^a rounded off.

TONGA

PROJECT PROFILE				
Project Name: Economic and Public Sector Reform Program (EPSRP)			2. Sector/Subsector: Finance	
3. Dev. Objective: Primary: ECO Secondary:			5. Beneficiary Participation in Formulation: Government Ministries, private sector representatives, key community leaders and other relevant stakeholders will be consulted in the process of EPSRP formulation.	
4. Rationale: Recent adverse economic developments in Tonga have raised concern within the Government about the need to introduce measures to ensure macroeconomic stability, expedite the pace of public sector reform, enhance the quality of government services, facilitate private sector development, promote human resource development and minimize the drain on foreign reserves. Experience of other PDMC's undertaking comprehensive reform programs has prompted the Government to approach the Bank for assistance in formulating the proposed EPSRP.				
6. Objectives and Scope: The objective is to enhance private sector-led economic growth by promoting policies that create a conducive environment for increased investment and employment by the private sector and improving the policy framework through which government services to the private sector are being delivered. The project will comprise four primary components: (i) private sector promotion; (ii) financial sector reforms; (iii) rationalization and strengthening of public sector management; and (iv) establishment of a sustainable social security system.				
7. Estimated Cost & Financing Plan (\$):				Remarks
Loan Project Cost (\$m)				
Financing (Source)	FC	LC	Total	
Bank	10.0	0.0	10.0	
Cofinancing	0.0	0.0	0.0	
Borrower	0.0	0.0	0.0	
Total	10.0	0.0	10.0	
8. Estimated Benefits and Beneficiary Groups: After the initial adjustment period, benefits from the EPSRP are expected to arise from faster economic growth and improved private sector employment opportunities, leading to higher levels of income.				
9. Executing Agency: Ministry of Finance PO Box 87, Vuna Road, Nuku'alofa, Tonga			10. Project Implementation Period: Start: to be determined. End: to be determined.	
11. Environment Category: C			12. Processing Year: 2000	

ASIAN DEVELOPMENT BANK

**COUNTRY ASSISTANCE PLAN
(2000-2002)
PIPELINE UPDATE**

TONGA

June 2000

TONGA
LENDING PIPELINE AND TECHNICAL ASSISTANCE PROGRAM, 2000-2002
(Amounts in \$ million)

Sector/Project Name	Strategic		Responsible Division	Year of PPTA	PROJECT COST				Gov't	Cofinancing (Others)
	Dev't Objectives a				TOTAL	Bank		Total		
	Primary	Secondary				OCR	ADF			
2000 STANDBY LOANS										
NONE										
2001 LOAN PIPELINE										
Others										
1. Economic and Public Sector Reform	ECO		POHQ	1999	10.0	0.0	10.0	10.0	0.0	0.0
Subtotal					10.0	0.0	10.0	10.0	0.0	0.0
Total					10.0	0.0	10.0	10.0	0.0	0.0
2002 LOAN PIPELINE										
NONE IDENTIFIED										

^a ECO = Economic Growth; HD = Human Development; POV = Poverty Reduction; WID = Women in Development; and ENV = Environmental Protection.

TONGA
LENDING PIPELINE AND TECHNICAL ASSISTANCE PROGRAM, 2000-2002

Sector/Project Name	Responsible Division	Type of TA	Amount (\$'000)		
			Bank	Others	Total
2000 TECHNICAL ASSISTANCE PROGRAM					
Others					
1. Economic and Public Sector Reform Phase I	POHQ	PP	600.0	0.0	600.0
2. Preparation of an Economic Report (PIER)*	POHQ	AD	124.0	0.0	124.0
3. Poverty Assessment*	POHQ	AD	147.0	0.0	147.0
	Subtotal		<u>871.0</u>	<u>0.0</u>	<u>871.0</u>
Total			<u>871.0</u>	<u>0.0</u>	<u>871.0</u>
2001 TECHNICAL ASSISTANCE PROGRAM					
Others					
1. Economic Planning and Financial Management Support Project Phase I	POHQ	AD	600.0	0.0	600.0
	Subtotal		<u>600.0</u>	<u>0.0</u>	<u>600.0</u>
Total			<u>600.0</u>	<u>0.0</u>	<u>600.0</u>
2002 TECHNICAL ASSISTANCE PROGRAM					
Others					
1. Economic Planning and Financial Management Support Project Phase II	POHQ	AD	450.0	0.0	450.0
	Subtotal		<u>450.0</u>	<u>0.0</u>	<u>450.0</u>
Total			<u>450.0</u>	<u>0.0</u>	<u>450.0</u>

*Approved