

Economic Update: July 2008

From the Office of the Prime Minister, Nuku'alofa, 29 July 2008

Economic Growth

The Tongan economy showed its resilience in 2007/08 rebounding strongly from the events of the previous year. The civil disturbance of November 2006 resulted in negative growth in 2006/07 as both the December 2006 and March 2007 quarters activities were significantly suppressed. However, subsequent information confirms that the Tongan economy was far more resilient than commentators predicted and the private sector bounced back by mid 2007.

On the tourism front, there has been a significant increase in weekly international flights to Tonga over the last two years with the introduction of Pacific Blue and increased flights from Fiji. A second domestic airline commenced operations in April 2008, resulting in increased certainty and services to the outer islands.

International air arrivals increased by 20 percent and cruise ship arrivals by 50 percent for the first nine months of 2007/08 compared to the same period the previous year, which led to Tourist receipts, as measured by the National Reserve Bank of Tonga, rising to record levels for the September and December quarters of 2007.

Electricity consumption, a good indicator of economic growth, grew by 6.5 percent in the first six months of 2007/08 compared with same the same period the previous year.

Private remittances continue to grow after a slowdown in 2006/07. For the first nine months of 2007/08 private remittances have grown by 7.0 percent compared to the same period the previous year.

The reconstruction of the Nuku'alofa central business district is now underway. Donor assistance has increased significantly in recent years. In 2007/08, the Government's of Australia and New Zealand contributed an additional \$15 million over and above their normal aid programs to assist with reconstruction of the central business district. This was on top of the \$5 million they had provided in 2007 in the form of the Business Recovery Facility which aimed at assisting with business cash flow and restocking after the events of November 2006.

The Tongan economy is forecast to grow by 3 percent in 2008/09. This forecast has been endorsed by international donors such as the World Bank and International Monetary Fund.

The Coronation is anticipated to result in a significant increase in remittances for the months of July and August 2008. The Coronation will also draw an extra 5,000 arrivals alone in July 2008, giving a very healthy start to the 2008/09 year. The Coronation itself will showcase the Kingdom worldwide and is an opportunity to promote the "Friendly Isles".

The New Zealand Recognized Seasonal Employment work-scheme is underway with employment

opportunities for Pacific Islanders growing at 5 percent each year. This new scheme is expected to further contribute to growth in remittances.

In the construction sector, a People's Republic of China grant of \$4 million is currently being utilised for the maintenance and upgrade of secondary roads on Tongatapu. Added to this is an Asian Development Bank grant of \$25 million for infrastructure projects including for roads, drains, etc. due to begin implementation in September this year. The Government is also working with the Ports Authority on a major redevelopment of Vuna Wharf. The wharf will be rebuilt to cater for cruise ships and naval vessels. The yacht harbor and shore based facilities will be developed in conjunction with the private sector.

Discussions are currently underway with a number of businesses to build in the Central Business District utilising the People's Republic of China soft loan and physical construction is due to commence not long after the coronation festivities are completed.

For too long Tonga has been relying heavily on one major export commodity, squash to Japan. Due to the vagaries of this market and the inability to secure guaranteed prices from the Japanese importers, the average Tongan farmer has not been able to obtain a consistent and viable income from this commodity. Recently, the industry diversified to shipping baby squash to Korea and after a number of years of trials a butternut market to the United Kingdom has been secured.

The Government is currently working with the private sector on further export diversification, and the production of maize for stock feed for Fiji and Papua New Guinea looks promising. Japanese sweet potato trials are currently underway which could result in \$3 million exports per annum to the Japanese market. The government is also promoting freeze-dried root crop exports to Tongan's living overseas. A feasibility study is also underway to look at opening a Tongan-made market centre in Auckland for both agriculture and processed products.

Foreign investment

The Warwick International Hotel Group has signed a lease with the Government of Tonga to build a resort in the island of Taunga and on the island of Ngau, adjoined by a sand bar. The signing is an historic event as it is the first time that an international Hotel Chain has developed a resort in Tonga. The Warwick International Hotels commitment to invest in the tourist industry in Tonga is a major vote of confidence for the Government and people of Tonga.

A second major tourism investment, Lomipeau Marina Resort Holdings, which includes a hotel, resort, and marina facilities, is proposed for Nuku'alofa. The investment in this project alone is estimated at \$150 million.

In November 2007 Digicel Pacific Ltd acquired the operations of Tonfon. Since its launch in the South Pacific in November 2006, Digicel Pacific has become the fastest-growing mobile operator in the Pacific. Prior to its official launch in May 2008 Digicel reportedly spent \$20 million on upgrading systems and has significant plans for future investment.

Nautilus Minerals is recognized as a world leader in sea bed mineral exploration. It is the first company in the world to commercially explore the seafloor for high-grade gold-copper-zinc-silver massive sulphide

deposits. Nautilus currently has the survey ship DEA Surveyor in Tonga waters. DEA Surveyor is here as part of Teck Cominco's US\$12 million offshore 2008 exploration program in Papua New Guinea and Tonga. Early signs are encouraging for the prospect of moving to commercial sea bed mining in Tongan waters.

Government Initiatives

For the first time in a number of years the Government has delivered an expansionary budget. Fiscal year 20087/09 sees a \$30 million increase in spending over the previous year. Importantly, the government is able to do this while maintaining fiscal discipline by ensuring the budget is balanced.

The Government over the next 3-5 years sees investment in economic infrastructure as a priority to further developing a private sector led economy. The coming year will see significant investment in infrastructure, including \$6 million for roads, \$3 million for the Foa causeway in Ha'apai, \$1.5 million for the first phase of a new prison, a further \$1 million for police infrastructure and equipment, and \$2 million for setting up new consulates in Wellington, Canberra, and Brussels. The Government and Tonga Airports Ltd are working on a major upgrade of 'Eua airport, involving sealing and extending the runway, and a new terminal building.

The Government of Tonga recognises the impact of the world fuel price crisis as one of the main Issues facing Tongan citizens, whether it be through increased prices at the bowser, or increasing electricity tariff rates. As such, the Government has embarked on a major renewable energy campaign with a target of

having **50 percent of our electricity from renewable energy sources**

within three years

. To achieve this goal, Tonga is currently working with the European Union on a \$50 million wind farm project. A second exciting prospect is a \$30 million bio-mass plant which is currently in the feasibility stage. The combined impact of these two projects could see electricity prices at 40 percent of their current rates, but not only would people receive significantly cheaper power but the lower tariff rates would be sustainable as Tonga would be moving more and more to renewable energy.

Recent Government pro-poor policies include the removal of import duties on meat and poultry and on fuel for domestic air and shipping companies. Both of these initiatives are aimed at easing the impact of rising world food and oil prices. The impact of the meat and poultry duty relief alone will put \$5 million back into the pockets of the Tongan citizens. The Government also subsidizes the first 200 units of household power. The government has also removed duties on over 800 capital items to encourage private sector investment. .

From Economic Advisor, PMO, Nuku'alofa, Tonga. 29 July 2008