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Statement by the Hon. **SIOSIUA T.T. 'UTOIKAMANU**,
Governor of the Bank for **TONGA**,
at the Joint Annual Discussion

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Governor of the Bank for Tonga,
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Mr. Chairman
Managing Director Rodrigo de Rato y Figaredo
President Wolfowitz
Fellow Governors
Distinguished Delegates
Ladies and Gentlemen

It is indeed an honor for me to address the Board of Governors of the International Monetary Fund and the World Bank Group on behalf of the Government of the Kingdom of Tonga at the 2006 Annual Meetings.

At the outset, I wish to express my appreciation to the government and the people of Singapore for the excellent arrangements of these major events and for the most generous hospitality.

I also wish to convey my government's deep gratitude to President Wolfowitz and Managing Director de Rato and to my fellow Governors who have offered their condolences following the passing away of our beloved monarch, King Taufa'ahau Tupou IV.

We meet against a background of rapid global economic growth, with 2006 forecast to be the fourth year of GDP growth above 4 percent. It is encouraging to see a broadening of the expansion beyond the United States of America and China, with all major regions of the world currently experiencing solid economic growth. While this portends well for global efforts to reduce poverty, nevertheless, the risks to growth are undoubtedly slanted to the downside.

Prices of oil and other commodities are at record highs and core inflation is on an upward trend. Small island economies, like the Pacific Island economies, are especially vulnerable to these risks. As such, we would certainly appreciate help from the IMF to provide a buffer for us in dealing with these risks.

Turning to the Fund's policy agenda, we welcome the decision to increase the quota and voting rights of China, Korea, Mexico and Turkey. This represents a tangible recognition of the emerging market countries' increased weight in the global economy. This is just the first step. We generally support moves to better align quota shares with economic weight in the global economy, but we believe it should be balanced with enhanced participation of low-income countries in the governance covenants of the fund. This is a

particularly important issue for a small-island economy such as Tonga. In this regard, we note the Executive Board's recommendations to: (1) at least double the basic votes to a minimum in order to protect the existing voting share of low-income countries as a group; and (2) introduce a mechanism that will safeguard the proportion of basic votes in the total voting power in the future.

We support efforts to align the capacity-building activities of the Fund more closely with the needs of member countries. We agree with the Fund's emphasis on strengthening governance, transparency and accountability. These factors are critical for building sound institutions, which are critical for macroeconomic stability, achieving sustained economic growth and reducing poverty. We also acknowledge that the Fund is emphasizing increased country ownership in its technical assistance and training activities.

We welcome the Fund's greater focus on sustainable economic growth in supporting the achievement of the Millennium Development Goals. Whilst Tonga may have achieved many of the health and education related targets, it is important that we look behind and beyond the data provided. Much of the data available for the MDG indicators masks crucial inequities at the grassroots level, such as access to quality primary education and adequate primary health services. Similarly, while poverty per se is not apparent in Tonga, hardship is evident throughout Tonga, amongst the vulnerable groups and particularly in the remote islands. Tonga's pro-poor strategies intend to address those in hardship.

The suspension of the Doha Round of Trade Talks was disappointing. Failure to conclude the talks will adversely affect global economic prospects and the growth of low-income countries in general, such as Tonga. We urge WTO members to maintain their commitment to the rules-based multilateral trading system; preserve progress that has already been achieved; and continue negotiations. We also urge the donor community to move forward with the delivery of 'aid for trade' independent of the Doha Round. Regional cooperation on trade-related projects has the potential to promote the competitiveness of low-income countries, such as the Island economies in the Pacific.

On the domestic front, the past year has been eventful and very challenging. Growth in GDP is estimated to have eased slightly in 2005/06; international reserves have remained above the equivalent of four months of imports; while average annual inflation fell to 7.2 percent, the lowest level in six years. The fall in inflation has been a significant achievement, particularly given the doubling of world oil prices over the past two years. The improvement in inflation partly reflected the favorable inflation performances of our major trading partners, as well as favourable weather conditions locally.

The major economic event over the past year has been a significant increase in the salaries of public servants, and the offer of voluntary separation to nearly a quarter of the public service. This involved the government having to arrange financing equivalent to 7

percent of GDP, without raising taxes, in order to pay the salary increase of existing public servants and the payments to public servants who accepted voluntary separation. Financing was achieved through the utilization of the proceeds of a program loan in support of economic reform and cash reserves accumulated from previous years. The budget balance consequently moved from a surplus of 2.4 percent of GDP in 2004/05 to a deficit of 4.8 percent of GDP in 2005/06. On the other hand, the voluntary separation program reduced public service positions by about 30 percent, and supported the Government's objective of targeting broad fiscal balance. The budget for 2006/07 targets a fiscal deficit of about 2 percent of GDP.

Mindful of the enormous challenges facing the Kingdom, in May 2006, the Government of Tonga ratified its Strategic Development Plan 8, better known as SDP8. The SDP8 is the government's road map for the Kingdom's future development path. SDP8 is also a blue print for sustainable development to ensure that the people of Tonga build on our heritage to lead free and worthwhile lives. The SDP8 provides eight goals which are mutually reinforcing, and offers predictable and a coherent policy framework, within which government can deliver results.

The participatory approach of designing the strategies of the Plan entailed full involvement and engagement of relevant groups. This process, in itself, is undeniably a stride towards creating a better governance environment. The SDP8 emphasizes that good governance underpins achievements in all areas of economic, social and political development.

To translate its commitment to better governance, the Government will establish an independent anti-corruption body with investigative capacity to deal with all public sector corruption allegations. Further, other initiatives have included efforts; to strengthen corporate good governance in public enterprises and revenue audit; formulate a leadership code; introduce further compliance initiatives and regulatory reform.

The SDP8 recognizes that prudent macroeconomic policies are crucial in providing a solid foundation for sustainable economic growth. Government has therefore taken corrective steps to ensure that the fiscal balance is broadly maintained as outlined earlier. The public service wages bill has been brought back under control while tax revenue is projected to increase as a result of improvements in the collection of existing taxes. At the same time, the National Reserve Bank of Tonga has tightened monetary policy in order to preserve external balance and dampen inflationary pressures. Despite these measures, downward pressure on foreign exchange reserves is expected to persist and consumer price index is forecast to increase at a time when core inflation in our trading partners is moving higher.

One of the key issues that affect many countries, and which has been accorded international attention, is the topic of international migration and its impact on our global economy. The dynamics of international migration goes unnoticed, as it has supported

the process of global economic growth. Research in this area has shown a strong positive correlation between remittances and poverty reduction strategies in developing countries. The economic contribution of migrants is significant not only for the sending country but also the receiving country. International migration is a critical factor for Tonga's development, for remittances received from migrants constitutes an important source of income, more than Official Development Assistance (ODA) or Foreign Direct Investment (FDI). It is the export of people, or migration, coupled with remittances of cash and goods from those whom reside and work overseas, that sustain the Tongan economy and the present standard of living of the people.

Remittances equivalent to 40 percent of GDP were estimated to have been received in 2005/06 for Tonga. A recent study by the World Bank indicates that official statistics significantly underestimate remittances, and further indicates that approximately 90% of households in Tonga received cash remittances in 2004, averaging US\$3,067 per household and US\$753 per capita. The study concludes that remittances in Tonga has improved income distribution; has positive impact on poverty alleviation; induces higher savings and stimulates business activities and results also in larger investments in education.

International support is required to accord attention to maximizing the positive impact of remittances, particularly the impact of remittances on poverty reduction. This could include the need to encourage further dialogue on liberalizing international labor migration.

Finally, we acknowledge with appreciation the technical and financial assistance that the IMF and World Bank have provided to the government and people of Tonga. We are particularly grateful for the support we receive from the Pacific Financial Technical Assistance Centre and the World Bank's Regional Office for the prompt response they offer to our requests for assistance and advice. The assistance continues to make a tangible difference to the living standards of our people. We look forward to a continued close working relationship with the Fund and the Bank. May I conclude by wishing the Bank and the Fund continued success in resolving the many difficult challenges that lie ahead.