



Report Number : ICRR0022743

## 1. Project Data

**Country**  
Tonga

**Practice Area(Lead)**  
Macroeconomics, Trade and Investment

**Programmatic DPL**  
**Planned Operations:** 0

**Approved Operations:** 0

**Operation ID**  
P155133

**Operation Name**  
Tonga First Inclusive Growth DPO

**L/C/TF Number(s)**  
IDA-57710,IDA-D1070

**Closing Date (Original)**  
30-Jun-2017

**Total Financing (USD)**  
2,251,502.20

**Bank Approval Date**  
16-Mar-2016

**Closing Date (Actual)**  
30-Jun-2017

	<b>IBRD/IDA (USD)</b>	<b>Co-financing (USD)</b>
Original Commitment	2,000,000.00	0.00
Revised Commitment	2,000,000.00	0.00
Actual	2,251,502.20	0.00

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**Operation ID**  
P159262

**Operation Name**  
Tonga Second Inclusive Growth DPO ( P159262 )



<b>L/C/TF Number(s)</b> IDA-57710,IDA-60200,IDA-D1070,IDA-D1780,IDA-D3490	<b>Closing Date (Original)</b> 31-Dec-2018	<b>Total Financing (USD)</b> 14,775,064.03
<b>Bank Approval Date</b> 27-Apr-2017	<b>Closing Date (Actual)</b> 31-Dec-2018	
	<b>IBRD/IDA (USD)</b>	<b>Co-financing (USD)</b>
Original Commitment	15,000,000.00	0.00
Revised Commitment	15,000,000.00	0.00
Actual	14,775,064.03	0.00

**Operation ID**  
P159263

**Operation Name**  
Tonga Third Inclusive Growth DPO ( P159263 )

<b>L/C/TF Number(s)</b> IDA-57710,IDA-D1070,IDA-D4580	<b>Closing Date (Original)</b> 30-Sep-2020	<b>Total Financing (USD)</b> 5,565,640.03
<b>Bank Approval Date</b> 16-May-2019	<b>Closing Date (Actual)</b> 30-Sep-2020	
	<b>IBRD/IDA (USD)</b>	<b>Co-financing (USD)</b>
Original Commitment	5,500,000.00	0.00
Revised Commitment	5,500,000.00	0.00
Actual	5,565,640.03	0.00

## 2. Program Objectives and Policy Areas

### a. Objectives

The Inclusive Growth Development Policy Operation (IGDPO) consisted of a programmatic series of three operations. The original Project Development Objective (PDO) described in the Program Document (PD) for



the first operation was to support policy reforms to: (i) *increase fiscal resilience*; (ii) *support a more inclusive, modern and accountable state*; and (iii) *support a more dynamic and inclusive economy*. Objectives (ii) and (iii) were adjusted for the third operation in the series, removing the concept “inclusiveness” from the second objective to avoid duplication with the third objective.

For the purposes of this ICRR, the objectives of the series are simplified as follows:

- *Increasing fiscal resilience* by strengthening revenue, debt and expenditure management
- *Supporting government accountability*

*Supporting a more dynamic and inclusive economy* by improving the environment for private sector activity.

## **b. Pillars/Policy Areas**

The series was structured around three pillars/policy areas. It included 21 prior actions (PAs) spread over the three operations (see Section 3b).

**Pillar 1: *supporting fiscal resilience*** by stronger revenue mobilization, and debt and public service management through revenue and customs legislation; a medium- term debt strategy; and a new public sector remuneration framework.

**Pillar 2: *supporting government accountability and private sector regulation*** by improving compliance with procurement regulations; improving budgetary classifications; introducing more robust systems to pursue audit recommendations; and introducing new regulatory frameworks into selected sectors.

**Pillar 3: *supporting a more dynamic and inclusive economy*** by adopting investor-friendly foreign investment legislation; improving oversight and private participation in public enterprises; and introducing regulation into private sector labor markets.

## **c. Comments on Program Cost, Financing, and Dates**

The three-operation DPO totaled US\$22.5 million equivalent, of which US\$22.6 million equivalent was disbursed. The first operation of the series was approved on March 16, 2016, and the third one closed on September 30, 2020.

DPO 1 was an IDA credit of US\$1.0 million equivalent and a grant of US\$1.0 million equivalent, approved on March 16, 2016, and effective on May 11, 2016. It closed on June 30, 2017, having disbursed US\$2.25 million equivalent.

DPO 2 consisted of two grants and one IDA credit totaling US\$15.0 million, approved on April 27, 2017, and effective on June 15, 2017. It closed on December 31, 2018, having disbursed US\$14.8 million equivalent.

DPO 3 consisted of a grant of US\$5.5 million equivalent, approved on May 16, 2019, and effective on June 18, 2019. It closed on September 30, 2020, having disbursed US\$5.6 million equivalent.

Discrepancies between amounts allocated and amounts disbursed are due to exchange rate fluctuations.



### 3. Relevance of Objectives & Design

#### a. Relevance of Objectives

The Program Objectives are aligned with government policy and Bank strategy for Tonga and are considered essential elements in building a resilient and inclusive economy while addressing challenges posed by its geography – small islands spread over a large and remote area in the Pacific – which pushes up the cost of economic activity, offers limited scope for growth while the narrow economic base and high reliance on imports leave it vulnerable to economic shocks.

The Bank worked with the government (and development partners –ADB, Australia, New Zealand, EU) to elaborate the key reform actions supported under the Program. They are aligned with the government’s national development plan for 2015-2025, and continue themes introduced under previous DPOs, deepening reforms to revenue mobilization and public financial management including reform of state-owned enterprises, and measures to address non-communicable diseases (NCD). They are aligned with the Bank Group strategy as articulated in the Regional Partnership Framework for the Pacific Island Countries 2019-2021. There, the current Program covers three focus areas: strengthening macroeconomic management, protecting incomes and livelihoods by addressing NCDs, and enhancing access to employment opportunities by broadening opportunities for labor mobility.

The macroeconomic policy stance was considered adequate for the GDPO program at the time of GDPO 1 (2016) and for the two subsequent GDPOs. However, with a slow recovery from the 2018 cyclone Gita, and the subsequent twin shocks of COVID-19 and cyclone Harold, the 2020 IMF Article IV consultation assessment of the short- and medium-term outlook in 2021 is of a modest and fragile economy. While proactive and timely actions helped mitigate these external shocks, the economy nevertheless contracted by some 2.5 percent in 2020 and is estimated to have contracted by 3.5 percent in 2021. Tourism and remittance inflows are expected to decline, and reconstruction-related imports, are expected to rise, worsening the current account deficit. Tonga had requested IMF financial assistance under the Rapid Credit Facility

**Rating**

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#### b. Relevance of Design

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**Rating**

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### 4. Achievement of Objectives (Efficacy)



## Objective 1

### Objective

Improve fiscal resilience

Supported by PAs 1 to 6 and PAs 7 to 9. Progress measured by RIs 1 to 5.

### Rationale

Fiscal resilience was supported by measures that contributed to stronger revenue mobilization and greater fiscal sustainability. The increase in excise taxes and import duty rates was partly achieved, with positive effects on tax collection and consumption of health damaging products. A revised revenue services administration bill introduced additional sources of revenue, as did a new Customs bill set to international standards, and a simplified customs administration. Positive effects/trends were negatively impacted by external shocks (weather, COVID 19). Still, the ICR indicates a rise in domestic revenues from an average of 21.5 percent of GDP over FY14-16 to 24.2 percent over FY18-20, albeit below the target of 25 percent of GDP set for FY18-20.

Fiscal sustainability was reinforced through stronger medium-term fiscal planning and monitoring, and better management and control over the public sector wage bill. A new medium term debt strategy was approved, as was a target-based fiscal anchor system and monitoring framework – both strengthening medium-term fiscal planning and monitoring. There were two targets – one to maintain concessional borrowing above 35 percent of total external borrowing, the indicator was relevant, measurable, and achieved. A second indicator sought consistency between annual budget estimates and medium-term fiscal anchors over the FY18-20 period. Annual budget estimates for the period were consistent with medium-term fiscal anchors. In summary, the achievements of four out of five RIs was high, and one – RI1 – was substantial.

Outcomes per results indicator:

RI1 (domestic revenue as a proportion of GDP) increased from a baseline of 21.8 percent on average over FY14-FY16 to 24.2 percent for FY18-FY20, compared to a target of over 25 percent. Thus, the achievement of this RI was substantial.

RI2 (concessional borrowing above 35 percent of GDP) remained at a baseline of 100 percent. The achievement of this RI was high. RI3 (consistency between annual budget estimates and medium-term fiscal anchors); annual budget estimates were consistent with medium-term fiscal anchors. The achievement of this RI was high.

RI4 (public wage bill as a proportion of domestic revenue) declined from a baseline of 57 percent in FY14 to an average of 50.1 percent for FY18-20, surpassing the target of 53 percent or lower. The achievement of this RI was high.

RI5 (annual moderated performance process completed and ratings used in determining public sector wages) – new remuneration framework was applied. The achievement of this RI was high.

Thus, with all RI targets rated either substantial or high, efficacy at the Objective level is rated **satisfactory**.

### Rating

Substantial



## **Objective 2**

### **Objective**

Improve government accountability

Supported by PAs 10, 11 and 13. Progress measured by RIs 6 to 8, of which, the achievements of 2 of 3 RIs were negligible, and one was high.

### **Rationale**

Improvements in government accountability focused on procurement, budget reporting and audit oversight. All three aimed at addressing weaknesses in the control and accountability of public funds and were expected to increase value for money in public financial management. A revised set of procurement regulations with standard bidding documents and procurement manuals was prepared, as well as a new procurement tracking database. Both were operational. The results, however, fell short of intentions as measured by the results indicator, RI6, which measured increases in the share of contracts subject to open competition. The proportion of such contracts reached only 28 percent in 2020 compared to a baseline of 35 percent in 2014 and a target of 50 percent in 2020. The shortfall reflects a lack of capacity in line ministries to fully implement procurement regulations, as well as a challenging regulatory design with several different levels of rigor for different types of contracts. Thus, the achievement rating of RI 6 was negligible.

A new relevant and measurable economic segment was introduced (RI7), following up on PA12 and improving the accuracy of budget reporting. The achievement rating of RI 7 was high.

External scrutiny and timeliness in addressing public accounts' external audit recommendations (RI 8) (a measure of the effectiveness of audit oversight) did not meet its target of 40 percent of audit matters raised in the previous year still outstanding the following year, with some 70 percent still outstanding in FY19 against a baseline of 85 percent (115 of 136 reports not scrutinized). The achievement of RI 8 was negligible.

With achievement of two out of three RI targets rated negligible, efficacy for this Objective is rated **moderately unsatisfactory**.

### **Rating**

## **Objective 3**

### **Objective**

A more dynamic and inclusive economy

Supported by PAs 6, 10, 14-15, 17-18, 21. Progress measured by RIs 9 to 12.

### **Rationale**

The objective was to be pursued by seeking improved regulation of markets with little or no competition. Here, the relevant and measurable results indicator (RI 9) targeted effective regulation in the communications and energy sectors, included as prior actions (PA14 and PA15), that is, regulators in the two sectors established and operational. That has not been achieved, as appropriate funds were not



allocated in the budget (ICR, para. 45); moreover, the relevant national energy bill had not been submitted to parliament at series' closing. Thus, the achievement of RI 9 was negligible.

Employment relations legislation codifying basic labor rights has been passed by parliament and awaits the King's final approval (RI10). That has not yet occurred, as government is concerned that the legislation may be too onerous for employers at this time (given the recent climatic and environmental shocks). The achievement of this RI was modest.

The series supported a foreign investment bill aimed at facilitating foreign investment in Tonga. However, the outcome – number of vetted applications, and perhaps more importantly, the number of approved applications (RI 11) – appeared to be strongly influenced by external factors (climate, etc.) creating variability from one year to the next rather than showing a trend or indicating that the legislation has the desired effect. The target – vetting 30 applicants from a baseline of 21 – was substantially achieved with 27 vetted in FY20. The achievement of this RI was substantial.

To improve governance and operational efficiency of PEs in an environment with a limited pool of suitable candidates (RI 12), reform focused on selected sectors (ICT and utilities) and involved the appointment of shared boards of directors serving multiple PEs in similar fields. The two shared boards will span utilities, covering Tonga Power Limited, Tonga Water Board and Waste Authority Limited; and ICT covering Tonga Broadcasting Corporation, Tonga Communications Corporation, Tonga Post and Fast Print Ltd. Initially, RI12 aimed at reforming at least four PEs, which was later reduced to two. Finally, only one was completed under the operation, with the second one delayed due to external circumstances but is expected to be completed in 2022. The timetable for this item may have been too ambitious as the target was downsized from four PEs to two during implementation. Thus, the achievement of this RI was modest.

In summary, the progress of the establishment of independent regulators for the communications and energy sectors (RI 9) was negligible; basic labor rights have been codified (RI 10), but are not yet official, therefore progress was modest (RI10); the progress for vetting of foreign investment applications (RI 11) was deemed substantial, albeit strongly influenced by external factors; and there was modest progress in the number of reformed public enterprises (RI 12), targeted at at least four, is currently at one.

With at least half of RI targets rated modest or better, efficacy at the Objective level is rated **moderately satisfactory**.

## Rating

## 5. Outcome

With the relevance of prior actions rated satisfactory and efficacy rated moderately satisfactory, the operation's outcome is rated moderately satisfactory.



- a. **Outcome Rating**  
Moderately Satisfactory

## 6. Rationale for Risk to Development Outcome Rating

The sustainability of the series' development outcomes is likely to face a number of risks, including natural hazards, macroeconomic risks, limited implementation capacity, and fluctuating political priorities. While efficiencies introduced under the series – continuous dialogue, technical assistance, selectivity in policy choices - are likely to mitigate the impact of those risks, they are likely to continue to influence implementation of each of the series' objectives.

*Fiscal resilience* will continue to face challenges in revenue mobilization and, more generally, in fiscal management: vulnerability to frequent natural disasters and external macroeconomic developments will divert scarce human and financial resources from longer-term reforms to immediate priorities, testing the resilience of more effective tax collection and revenue management. *Stronger government accountability* is still a work in progress, and recent political developments in Tonga have introduced a measure of unpredictability into decision-making at the highest levels that may result in a slower reform process than was originally anticipated, and one that may also deviate from the model introduced under this series. Efforts towards creating a more *dynamic economy* are also still underway: opening markets to competition by regulatory means and by facilitating foreign direct investment have so far only been partially successful, as has been the case with employment legislation. Again, the mixed record of progress reflects political uncertainties in the archipelago. Influencing successful follow-up on all three objectives is Very limited institutional capacity – a small number of civil servants with the necessary qualifications or experience to implement reforms, and often stretched thin among several responsibilities – is also likely to limit implementation of reforms, even when scarce capacity is being buoyed by Bank advice.

- a. **Risk to Development Outcome Rating**

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## 7. Assessment of Bank Performance

- a. **Quality-at-Entry**

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**Quality-at-Entry Rating**

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- b. **Quality of supervision**

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**Quality of Supervision Rating**

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**Overall Bank Performance Rating**

Moderately Satisfactory

**8. Assessment of Borrower Performance**

**a. Government Performance**

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**Government Performance Rating**

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**b. Implementing Agency Performance**

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**Implementing Agency Performance Rating**

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**Overall Borrower Performance Rating**

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**9. M&E Design, Implementation, & Utilization**

**a. M&E Design**

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**b. M&E Implementation**

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**c. M&E Utilization**

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**M&E Quality Rating**

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## 10. Other Issues

### a. Environmental and Social Effects

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### b. Fiduciary Compliance

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### c. Unintended impacts (Positive or Negative)

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### d. Other

None identified.

## 11. Ratings

Ratings	ICR	IEG	Reason for Disagreements/Comment
Outcome	Moderately Unsatisfactory	Moderately Satisfactory	IEG rated PAs satisfactory reflecting their overall relevance and consistency to objectives sought; and efficacy moderately satisfactory, noting that while objectives often were only partly achieved, the process of change was well underway, or achieved, in all key areas.
Bank Performance	Moderately Satisfactory	Moderately Satisfactory	---
Relevance of Results Indicators		Moderately Satisfactory	---
Quality of ICR		Modest	---

### Note

When insufficient information is provided by the Bank for IEG to arrive at a clear rating, IEG will downgrade the relevant ratings as warranted beginning July 1, 2006.



The "Reason for Disagreement/Comments" column could cross-reference other sections of the ICR Review, as appropriate.

## 12. Lessons

The lessons are drawn from the ICR.

**Institutional capacity and political support should be continuously monitored.** In a dynamic institutional and political environment, frequent changes in key counterparts and ministers highlight the importance of working with a broad set of stakeholders. In this series, this was addressed by requiring all participating ministries to appoint working level staff to support coordination and continuity, as well as introducing regular meetings with the Cabinet and/or the Finance Minister, to maintain political support for the reform.

**Politically sensitive reforms should be well-grounded in client ownership.** Success in the wage bill management reform was grounded in analysis undertaken by the government (with development partner assistance). The reform process started with a review of remuneration to ensure a common reference base, followed by extensive consultation and awareness raising about performance-based pay, including extensive training to support implementation, and regular consultations and adjustments to improve implementation.

**While PAs may be highly relevant to achieving Program objectives, they need to be consistent with capacity constraints and efforts to build capacity.** This series underlined the importance of having a stable team or being able to adjust the reform program (including triggers) to ensure its continued relevance. That was a particular concern in attempting to improve accountability in government, as Tonga struggled to address capacity constraints in trying to implement new procurement regulations, better budget reporting and audit recommendations.,

## 13. Assessment Recommended?

No

## 14. Comments on Quality of ICR

The ICR provides a robust evidence base supporting the analysis in the document although it could have made a stronger linkage between the challenges that the operation's interventions were addressing and the subsequent outcomes; now the emphasis is strongly on "PA will do this..." but less so on articulating what deficiency is being addressed. That said, it summarizes well key achievements. In most instances the discussion is mostly results-oriented, allowing assessment of the results and ratings of the operation. ; in some cases, greater emphasis could have been placed on *outcomes* rather than *outputs* (recognizing that that is not always possible. The text is internally consistent, allowing the linking of the various parts of the series. A deviation from this appears to be the ratings for Efficacy and Outcome, both rated Moderately Unsatisfactory. This is based on the assumption that reforms will take time to be fully realized, and when that is the case, it should be reflected in targets and indicators. This is of course valid for many, if not most, reforms, which take time to mature. In Tonga, this may especially be the situation today following the



recent volcanic eruption that is likely to represent a severe setback to the country's development in the short to medium term.

**a. Quality of ICR Rating**  
Modest