



Program Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 25-Apr-2022 | Report No: PIDA33912



BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Tonga	P178698	Tonga Second Resilience Development Policy Financing: Supplemental Financing (P178698)	P172742
Region	Estimated Board Date	Practice Area (Lead)	Financing Instrument
EAST ASIA AND PACIFIC	09-Jun-2022	Macroeconomics, Trade and Investment	Development Policy Financing
Borrower(s)	Implementing Agency		
Kingdom of Tonga	Ministry of Finance		

Proposed Development Objective(s)

The proposed Development Policy Operation supports the Government of Tonga to: (i) strengthen public finances; (ii) enhance resilience to climate change, natural disasters, and health-related risks; and (iii) support economic recovery and improved labor market outcomes.

Financing (in US\$, Millions)

SUMMARY

Total Financing	20.00
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DETAILS

Total World Bank Group Financing	20.00
World Bank Lending	20.00

Decision

The review did authorize the team to appraise and negotiate

B. Introduction and Context

Country Context

The proposed operation provides US\$20 million in supplemental financing for the Second Resilience Development Policy Operation with a Catastrophe-Deferred Drawdown Option (parent DPO2/Cat-DDO, P172742) to help the Government of Tonga (GoT) cover an unanticipated financing gap that has arisen due to the impact of the Hunga-



Tonga-Hunga-Ha’apai (HT-HH) volcanic eruption and subsequent tsunami. On January 15, 2022, the HT-HH volcanic eruption and subsequent tsunami waves and ashfall caused damages of at least US\$102.2m (20.4 percent of GDP), while overall damages and losses could be over US\$182m (36.4 percent of GDP). Preliminary GoT estimates indicate that the total public sector response and recovery costs are likely to be at least US\$188m (37.5 percent of GDP), placing a significant strain on the government's fiscal position. The proposed US\$20m DPO supplemental financing from the IDA Crisis Response Window (CRW) for the DPO2 only (not the Cat-DDO) will enable the GoT to close the FY22 unanticipated financing gap and keep the reform program on track.

When the parent operation was approved in November 2021, Tonga’s macroeconomic outlook was expected to gradually recover over the medium term. The volcanic eruption and tsunami, Tonga’s first outbreak of COVID-19, and the Russian invasion of Ukraine will have a substantial effect on the outlook for economic activity over the next three years. The triple shocks will put upward pressure on food prices in the short term. Modest fiscal deficits are projected over the period FY22 to FY24 due to elevated spending associated with disaster recovery. The current account deficit is expected to deteriorate in FY23 and FY24, before narrowing from FY25 onwards. Reserves are projected to decline due to the delayed recovery in tourism receipts and the temporary spike in imports to support reconstruction activities, before stabilizing at over 8 months of imports cover over the medium term. Monetary policy is expected to remain accommodative, as the central bank aims to support the economic recovery. Public debt is sustainable despite the impacts of the HT-HH disaster, reflecting the government’s commitment to seek available grant financing and only to consider highly concessional debt as a last resort. The macroeconomic policy framework is adequate for the purposes of this supplemental financing operation.

Relationship to CPF

The proposed supplementary financing is consistent with the Bank’s Regional Partnership Framework (RPF) for nine Pacific Island countries FY17-FY21, which includes Tonga (Report #120479, extended by the Board of Executive Directors on February 6, 2020, to FY23). The operation is in line with the RPF’s third focus area on protecting incomes and livelihoods from the impacts of climate change and natural hazards, and the fourth focus area—strengthening the enablers of growth and opportunities—by providing the government with the fiscal space to respond quickly to the volcanic eruption and tsunami. The operation also supports the WB’s adoption of the Green, Resilient and Inclusive Development approach, particularly to help countries safeguard development and better respond to a range of risks and uncertainties including natural, climate, and health-related shocks.

C. Proposed Development Objectives

The proposed supplemental financing Development Policy Operation supports the Government of Tonga to: (i) strengthen public finances; (ii) enhance resilience to climate change, natural disasters, and health-related risks; and (iii) support economic recovery and improved labor market outcomes.

Key Results

The expected results, as per the parent DPO, are:

- Domestic revenue as a share of GDP: 25 percent or higher (FY25)
- Cash balance as a share of recurrent expenditure (months): 1 – 2 months (average FY22-FY24)
- 100 Percent of new external debt is concessional (FY21-FY24)
- Public-sector wage bill as a share of domestic revenue: 53 percent or lower (average FY24-FY25)
- The Housing Sector Resilience Office is established, and its annual work plan is submitted to the National



Emergency Management Committee (FY23)

- Annual report submitted to the National Disaster Risk Management Committee on the implementation of disaster risk reduction initiatives under the national disaster risk management policy
- Establishment of national registries of public schools and health facilities that include asset vulnerability information, and are used for policy and operational decisions to enhance resilience of public assets
- Proportion of the eligible population (aged 15 years and over) that have received the COVID-19 vaccine: 75 percent (female) and 75 percent (male) (FY23)
- Increased number of Tongans in Ministry of Internal Affairs (MIA) worker pools, with increased female participation: 2000 Tongans in the MIA worker pools, of which 37 percent are female (June 2023)
- Annual reporting on credit union sector regulatory and supervisory activities submitted to National Reserve Bank of Tonga Board (FY24)
- Confidential data is collected and maintained annually on: (i) sexual harassment complaints and how they were dealt with, disaggregated by ministry, procedure followed (formal or informal) and gender; and (ii) officials' experiences of sexual harassment, and knowledge and satisfaction of the policy

D. Project Description

In the parent DPO, the first development objective of the proposed operation is to strengthen public finances to support a resilient, inclusive recovery. The second development objective supports the GoT's efforts to reduce Tonga's vulnerability to the current and long-term threats of climate change, natural hazards, and public health emergencies. The third development objective supports the GoT's efforts to lay the foundations for a sustainable and inclusive economic recovery and strengthen labor market outcomes.

The GoT remains fully committed to the DPO Program, and there has been satisfactory progress with implementation since the approval of the parent DPO2/Cat-DDO in November 2021. The GoT has a history of committing to and successfully completing development operations, with 11 DPOs approved by the World Bank Board between FY11 and FY22. Implementation progress in each reform area of the DPO2/Cat-DDO has been satisfactory, with no policy reversals, during the short implementation period thus far. The parent operation is being implemented in compliance with the provisions of the Financing Agreements for the DPO2 and the Cat-DDO. More than half of the Results Indicators are also on track to being achieved.

E. Implementation

Institutional and Implementation Arrangements

There has been no change to monitoring and evaluation arrangements since the parent DPO. Through the Budget Support Management Committee, the MoF will provide overall guidance for the budget support program, and will assume overall responsibility for coordinating the implementation, monitoring and evaluation of the operation. The MoF will also be ultimately responsible for reporting progress and coordinating actions among other concerned government agencies. The Bank will continue to work with the Government to assess the progress of implementation of the policy actions supported by the parent operation.

F. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts



There are no changes to the assessment of poverty and social impacts since the parent DPO/Cat-DDO was approved. Reforms supported by all three pillars of the parent operation are expected to help reduce poverty and boost shared prosperity. The reforms under Pillar 1 will help ensure that the GoT has the fiscal space to respond to future economic shocks and disasters, which tend to impact the poor disproportionately, while maintaining basic services on which the bottom 40 per cent are particularly dependent. Under Pillar 2, the Disaster Risk Management (DRM) bill and disaster risk financing strategy (DRFS) are expected to have significant positive poverty and social impacts since they are designed to enhance the resilience of vulnerable households and to ensure that vulnerable groups are supported adequately before, during and following a disaster. Labor mobility reforms under Pillar 3 are expected to have significant net positive effects through the provision of substantial household benefits, which translate into positive poverty and distributional effects.

Environmental, Forests, and Other Natural Resource Aspects

There are no changes to the assessment of environmental aspects since the parent DPO/Cat-DDO was approved. Policy actions under the parent operation are not expected to have significant negative impacts on Tonga's environment, forests, and natural resources. The DRM bill and the DRFS would likely have significant positive environmental impacts through the encouragement of sustainable risk reduction investments while all other reforms are expected to not have any negative environmental impacts. Tonga has an established environmental impact assessment (EIA) process administered by the Ministry of Meteorology, Energy, Information, Disaster Management, Environment, Climate Change, and Communications. It is mandatory for the EIA of all new developments to be approved by the Minister and Chief Executive Officer of Environment and Climate Change.

G. Risks and Mitigation

The overall risk rating has increased to substantial from moderate under the parent operation. Macroeconomic risk has increased from moderate to substantial. This reflects the economic impact of the recent disaster and the associated deterioration of the fiscal position. These risks are being mitigated by: (i) the provision of this supplemental financing along with substantial development partner assistance—and the expectation that additional commitments will be made for the medium-term recovery—helping to close the financing gap; and (ii) the response by GoT to control spending and the ongoing commitment to seek only highly concessional financing. Risks related to institutional capacity have increased from moderate to substantial. Given the recent impact of the disaster, there is now a risk that achievement of the target results associated with the reform program could be delayed, as significant parts of the bureaucracy need to shift their attention to recovery efforts, at least in the short term. This risk is being mitigated by: (i) additional development partner financial support (to alleviate the acute fiscal pressure); and (ii) additional technical assistance to support disaster recovery planning and execution. Other risks have increased from moderate to substantial due to the domestic outbreak of COVID-19. Domestic transmission has compounded the negative effects of the HT-HH shock. Domestic lockdowns have disrupted recovery efforts and further stretched the government's capacity. Risks related to institutional capacity would be compounded by a severe domestic outbreak and associated lockdowns—a risk which has materially increased since the parent operation was submitted to the World Bank Board. This risk is being mitigated to some degree by additional in-kind donations to support the management of the COVID-19 outbreak (including additional vaccines, cold chain equipment, personal and protection equipment, and treatment facilities).



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APPROVAL

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Approved By

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