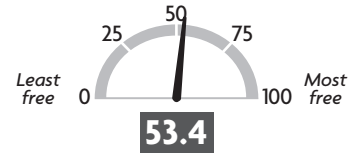


# TONGA

## Economic Freedom Score



World Rank: **127** Regional Rank: **26**

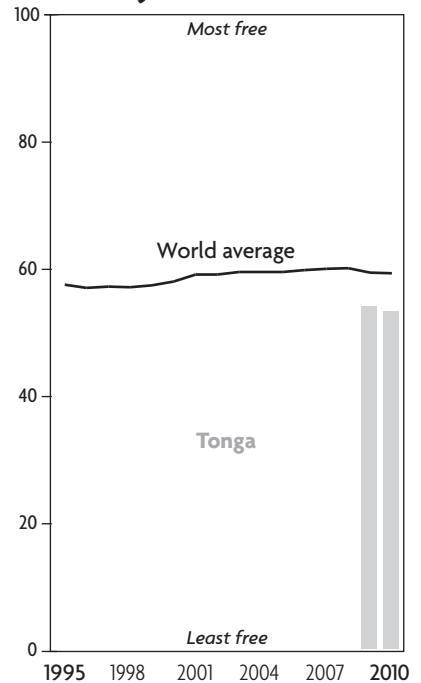
Tonga's economic freedom score is 53.4, making its economy the 127th freest in the 2010 *Index*. Its score has decreased by 0.7 point from last year, reflecting reduced scores in four of the 10 economic freedoms. Tonga is ranked 26th out of 41 countries in the Asia-Pacific region, and its overall score is below the world average.

Tonga's economy has expanded at a very slow rate. Over the past five years, growth has averaged just about 1 percent annually. Dominated by the public sector, the economy has long suffered from a lack of macroeconomic stability and the absence of a dynamic private sector to foster sustained economic growth and employment. Inefficient state-owned enterprises perpetuate low productivity, crowding out competition and investment from the private sector.

The economy of Tonga remains heavily dependent on overseas remittances, which account for more than 20 percent of GDP, outweighing income from tourism, agricultural exports, and other economic activities. The poor entrepreneurial environment has contributed significantly to a low level of economic dynamism despite a workforce that is considered the best educated among the Pacific Island nations. The government is the largest source of employment. Tonga's legal and regulatory framework remains weak, and opaque commercial regulations increase uncertainty and raise the overall cost of business activity. Protection of property rights is weak, and corruption remains a serious problem.

**BACKGROUND:** The Kingdom of Tonga is the South Pacific's last Polynesian monarchy. Some 100,000 people are spread across 48 of its 171 islands. Tonga has been independent since 1970, and its political life is dominated by the royal family, hereditary nobles, and a small number of other landholders. There are no political parties. More than half of Tonga's population lives abroad. Agriculture is the principal productive sector of the economy.

## Country's Score Over Time



## Quick Facts

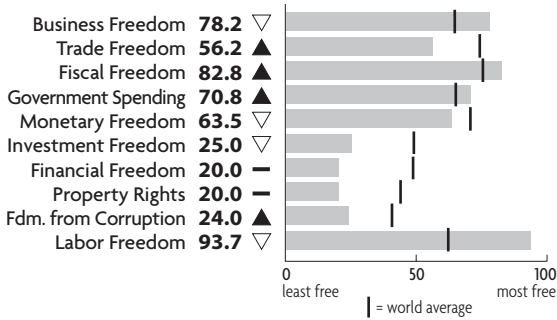
- Population:** 0.1 million
- GDP (PPP):** \$0.4 billion
  - 1.2% growth in 2008
  - 1.0% 5-year compound annual growth
  - \$3,824 per capita
- Unemployment:** estimated to be over 10%
- Inflation (CPI):** 14.5%
- FDI Inflow:** \$6 million

2008 data unless otherwise noted  
Data compiled as of September 2009

### How Do We Measure Economic Freedom?

See page 457 for an explanation of the methodology or visit the *Index* Web site at [heritage.org/index](http://heritage.org/index).

## TONGA'S TEN ECONOMIC FREEDOMS



### BUSINESS FREEDOM — 78.2

The overall freedom to start, operate, and close a business is respected under Tonga's regulatory environment. Starting a business takes an average of 25 days, compared to the world average of 35 days. Obtaining a business license requires less than the world average of 18 procedures. Closing a business is time-consuming and costly.

### TRADE FREEDOM — 56.2

Tonga's weighted average tariff rate was 16.9 percent in 2006. Tonga has made progress in liberalizing its trade regime, but import restrictions, import taxes, import certification requirements, and inadequate infrastructure add to the cost of trade. Ten points were deducted from Tonga's trade freedom score to account for non-tariff barriers.

### FISCAL FREEDOM — 82.8

A comprehensive tax reform package implemented in late 2007 resulted in consolidation of the corporate tax and simplification of the overall system. The top income tax rate is 10 percent, and the top corporate tax rate is 30 percent. Other taxes include a value-added tax (VAT) and a vehicle tax. In the most recent year, overall tax revenue as a percentage of GDP was 26.8 percent.

### GOVERNMENT SPENDING — 70.8

Total government expenditures, including consumption and transfer payments, are moderate. In the most recent year, government spending equaled 31.2 percent of GDP. Steps have been taken to renationalize the private Shoreline power company.

### MONETARY FREEDOM — 63.5

Inflation has been high, averaging 11.5 percent between 2006 and 2008. The government influences prices of petroleum products and other commodities through regulations. The ruling family and other Tongan nobles control other key prices through their ownership of most enterprises and utilities. Fifteen points were deducted from Tonga's monetary freedom score to adjust for measures that distort domestic prices.

### INVESTMENT FREEDOM — 25

Involvement of foreign investors in certain sectors must be approved by the government. The government allows full ownership by a foreign investor in cases where manu-

facturing activities are using imported raw materials for export or the investments are too large for local investors; joint ventures are encouraged. Bureaucracy is generally transparent and efficient. The repatriation of funds, including dividends, profits, capital gains, interest on capital and loan repayment, and salaries, faces some restrictions. Land may be leased but not owned.

### FINANCIAL FREEDOM — 20

Tonga's small financial sector remains underdeveloped and dominated by banking. It consists of two foreign-owned commercial banks, a locally incorporated commercial bank, and the government-owned Tonga Development Bank. The relatively high costs of credit and limited access to financing impede dynamic entrepreneurial activity. A considerable portion of the island's population is outside of the formal banking sector. Tonga's complex collateral system is inefficient and makes lending risky, particularly lending to small businesses. The National Reserve Bank of Tonga oversees banking, and the state-owned Tonga Development Bank finances many development projects. There are no capital markets.

### PROPERTY RIGHTS — 20

Tonga has a fairly efficient legal system based on British common law. The judiciary is independent and conducts generally fair public trials, although all judges are appointed by the monarch. Property rights are uncertain. The constitution mandates that an 8.25-acre plot of communally owned land be given to each male at age 16, but there is not enough land available to fulfill that mandate for the rapidly growing population, and this is a source of dissension. Tonga has legislation protecting intellectual property rights, but enforcement of IPR laws is weak. A bill on enforcement and border measures has been endorsed by the cabinet and is under consideration. This legislation aligns Tonga's laws with its World Trade Organization obligations and contains stricter border controls for counterfeit products, which continue to be widely available on the local market.

### FREEDOM FROM CORRUPTION — 24

Corruption is perceived as pervasive. Tonga ranks 138th out of 179 countries in Transparency International's Corruption Perceptions Index for 2008, a significant improvement over 2007. Although the law provides criminal penalties for official corruption, government officials sometimes engage in corrupt practices with impunity. Government preferences appear to benefit businesses associated with members of the royal family. An Office of the Anti-corruption Commissioner, charged with investigating official corruption, was established in 2008.

### LABOR FREEDOM — 93.7

Tonga's labor regulations are flexible. The non-salary cost of employing a worker is low, and dismissing an employee is not costly. However, the formal labor market is not fully developed.