

Economic and Social Survey of Asia and the Pacific 2024

Boosting affordable and longer-term financing for governments

Maldives
National Policy Dialogue

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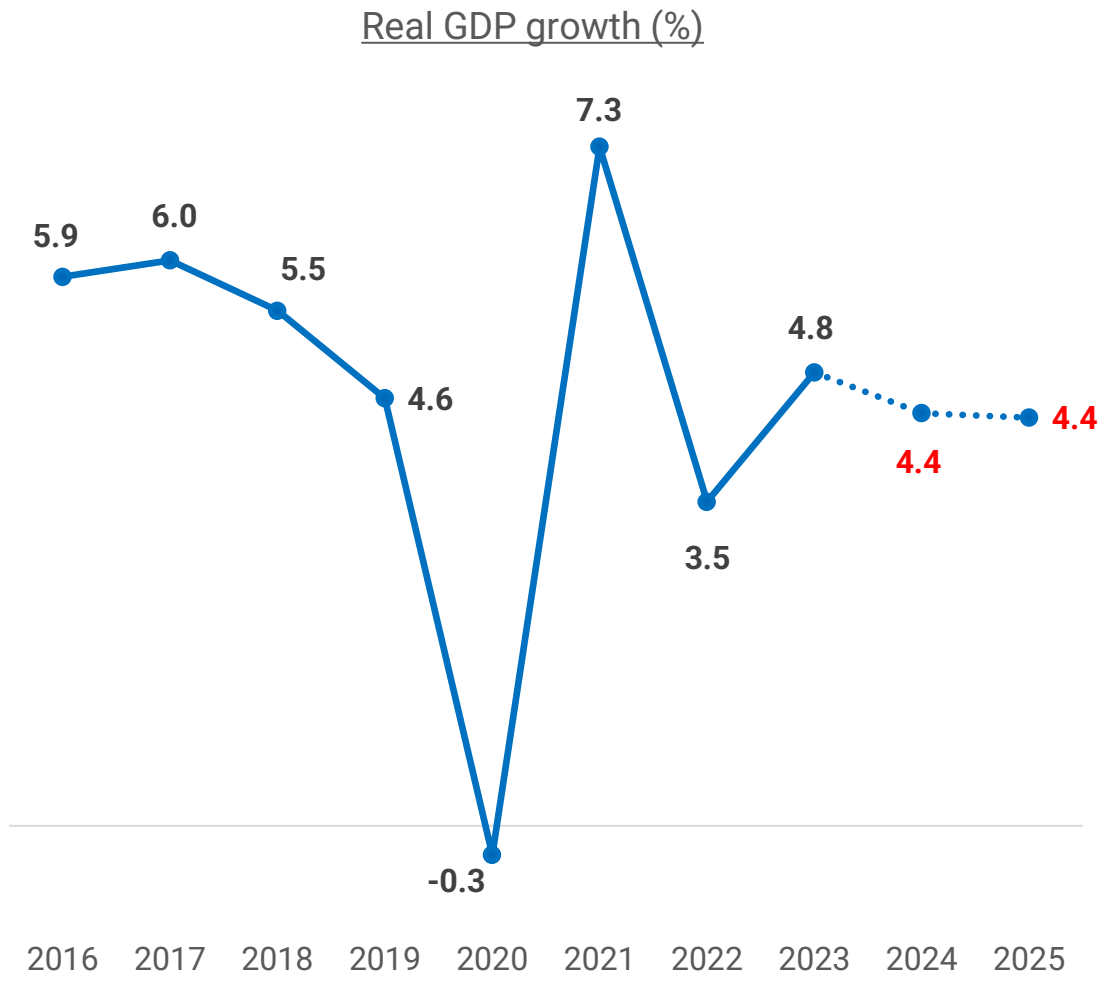
22 August 2024

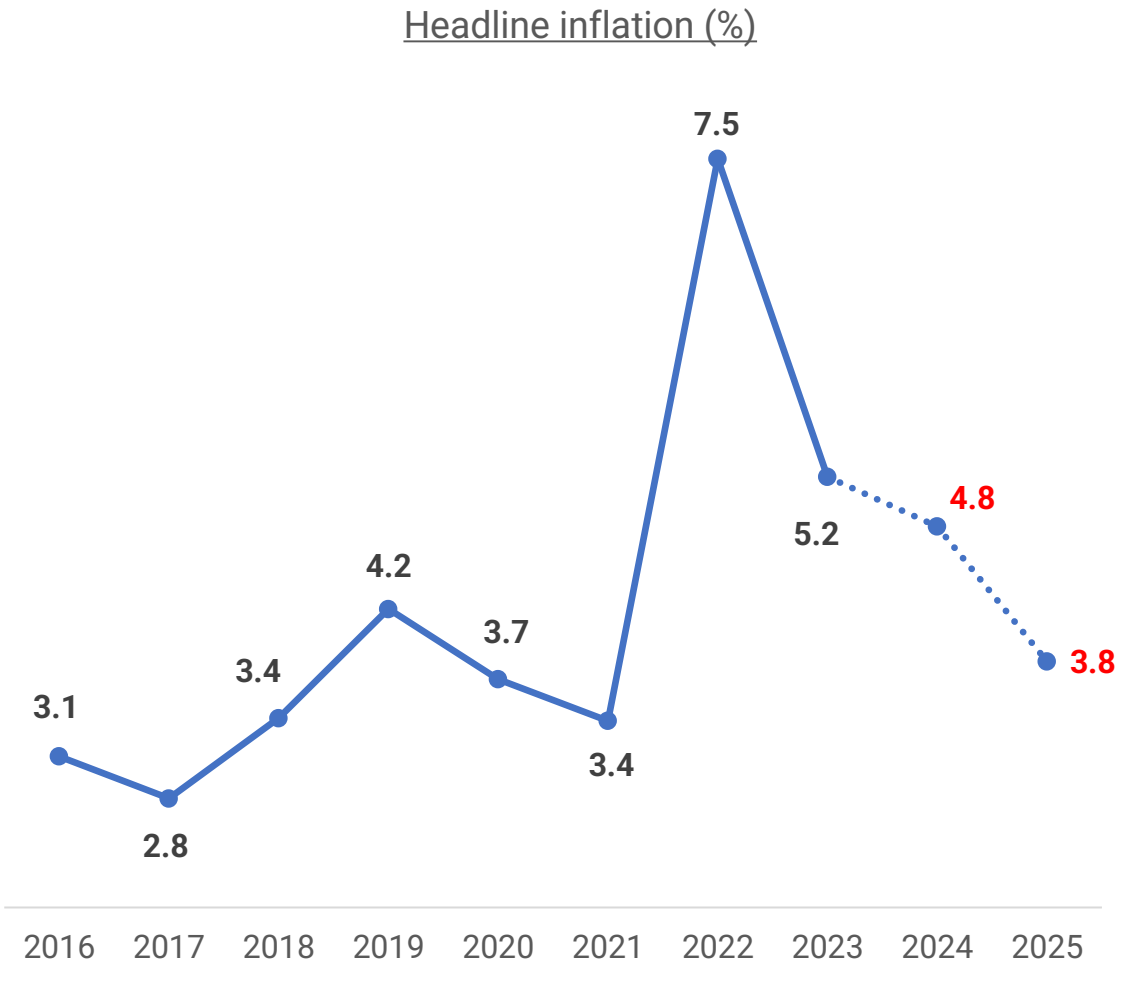
Highlights

- The **slower than expected recovery in global tourism** weighs on Maldives' economy, although domestic inflation has moderated.
- **High fiscal deficits** driven by fast expansions in public expenditure, together with **heightened public debt levels** and debt servicing burdens, remain the most pressing macroeconomic challenge.
- Further revenue mobilization can prove challenging and policy thrusts to safeguard fiscal sustainability can focus on **optimizing the selection, pace and efficiency of public expenditure items**.
- **Sectoral policies with a focus on job creation** for Maldivians and prudent leverage of development cooperation with regional powers can also be considered.
- Meanwhile, Maldives should be mindful of the coming global and local **mega trends**.

Macroeconomic prospects and challenges

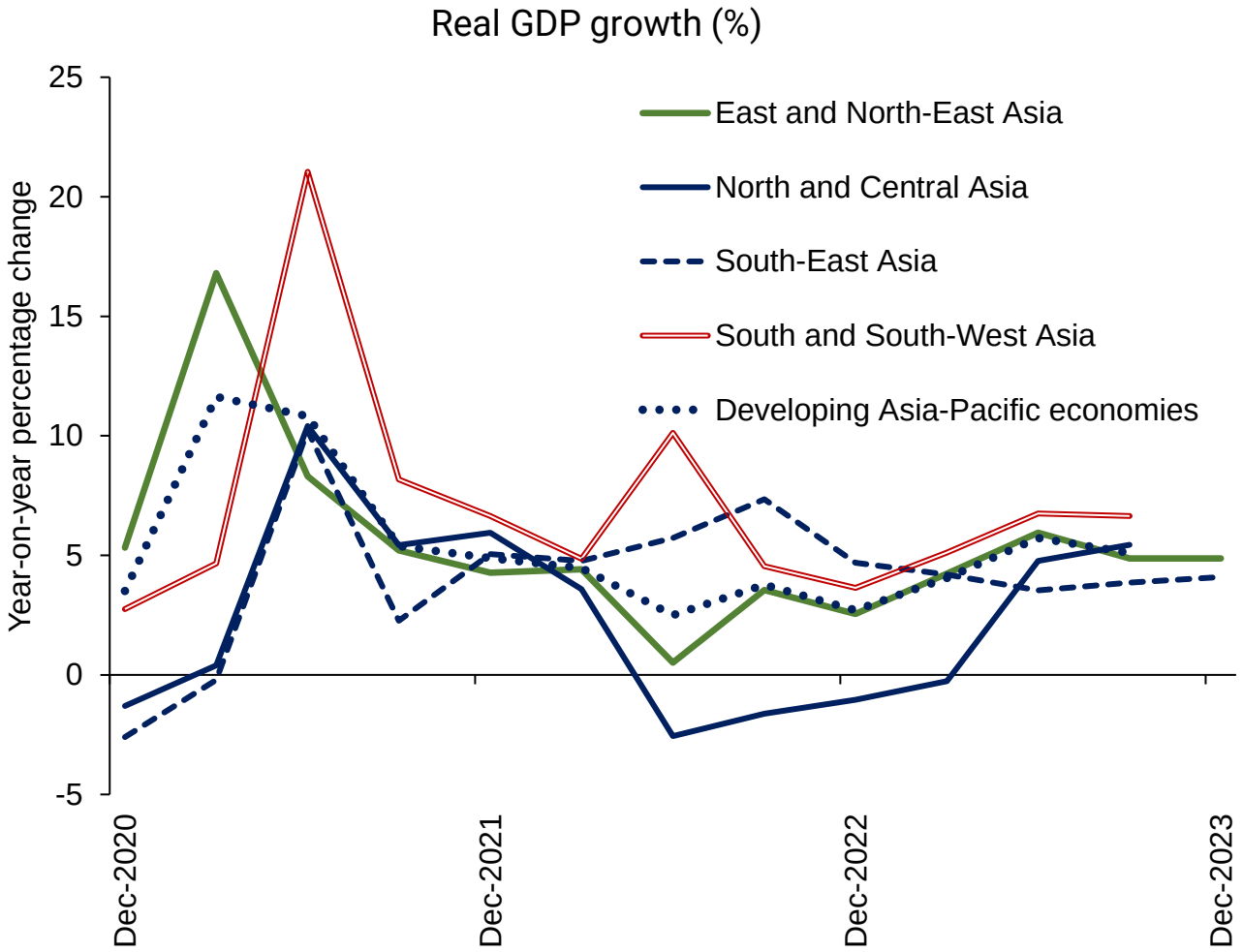
Steady, yet below-trend GDP growth in the Asia-Pacific region, with relatively high inflation

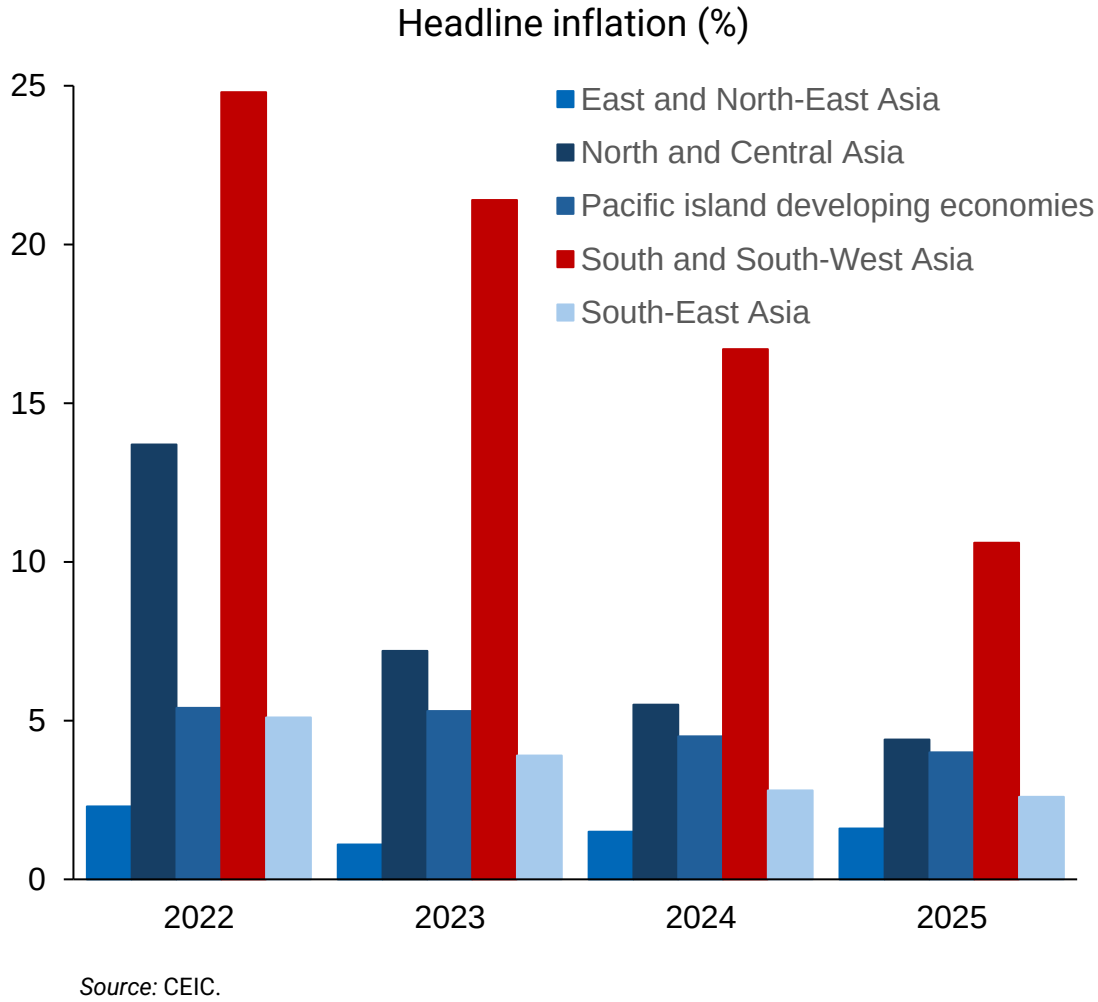




Source: ESCAP estimates and projections as of February 2024.

SSWA growth moderated slightly amid weak exports and consumption; inflation remained highly elevated





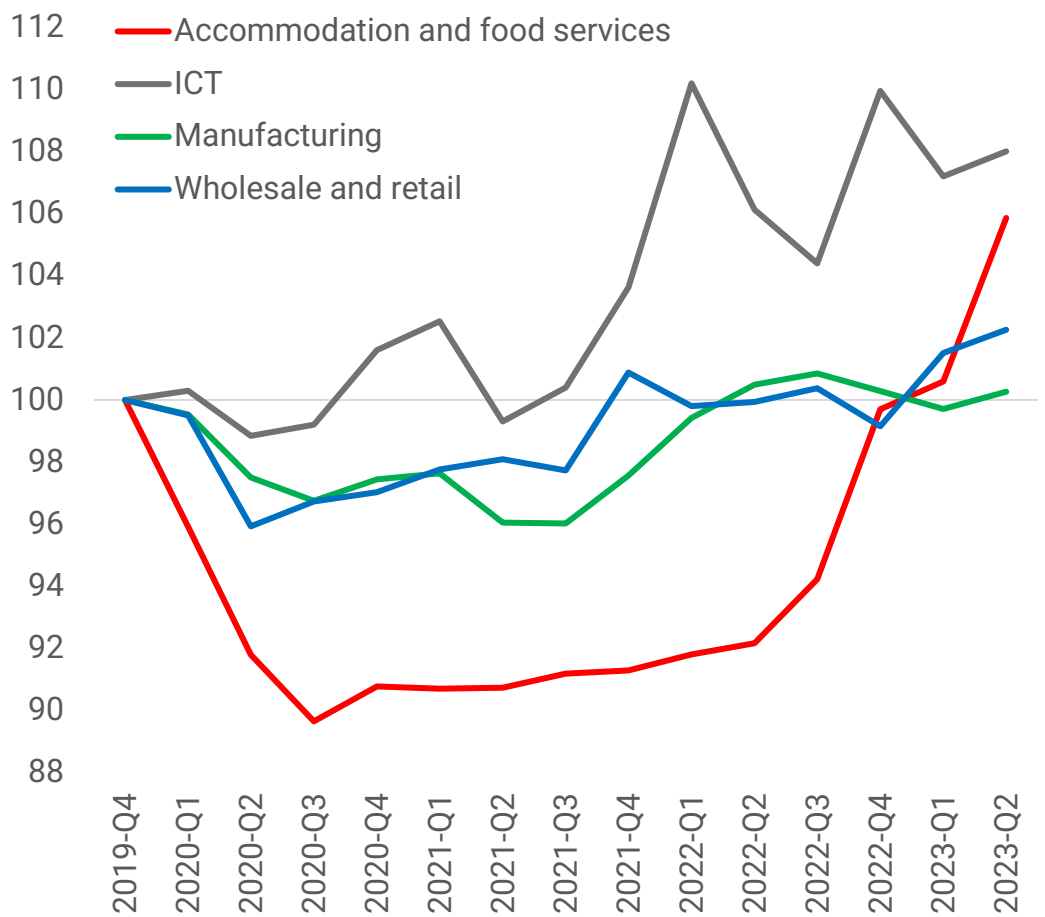
Source: ESCAP estimates and projections as of February 2024.
Note: Subregional aggregates are weighted averages, based on 28 economies in Asia and the Pacific for which quarterly GDP data are available.

Source: CEIC.

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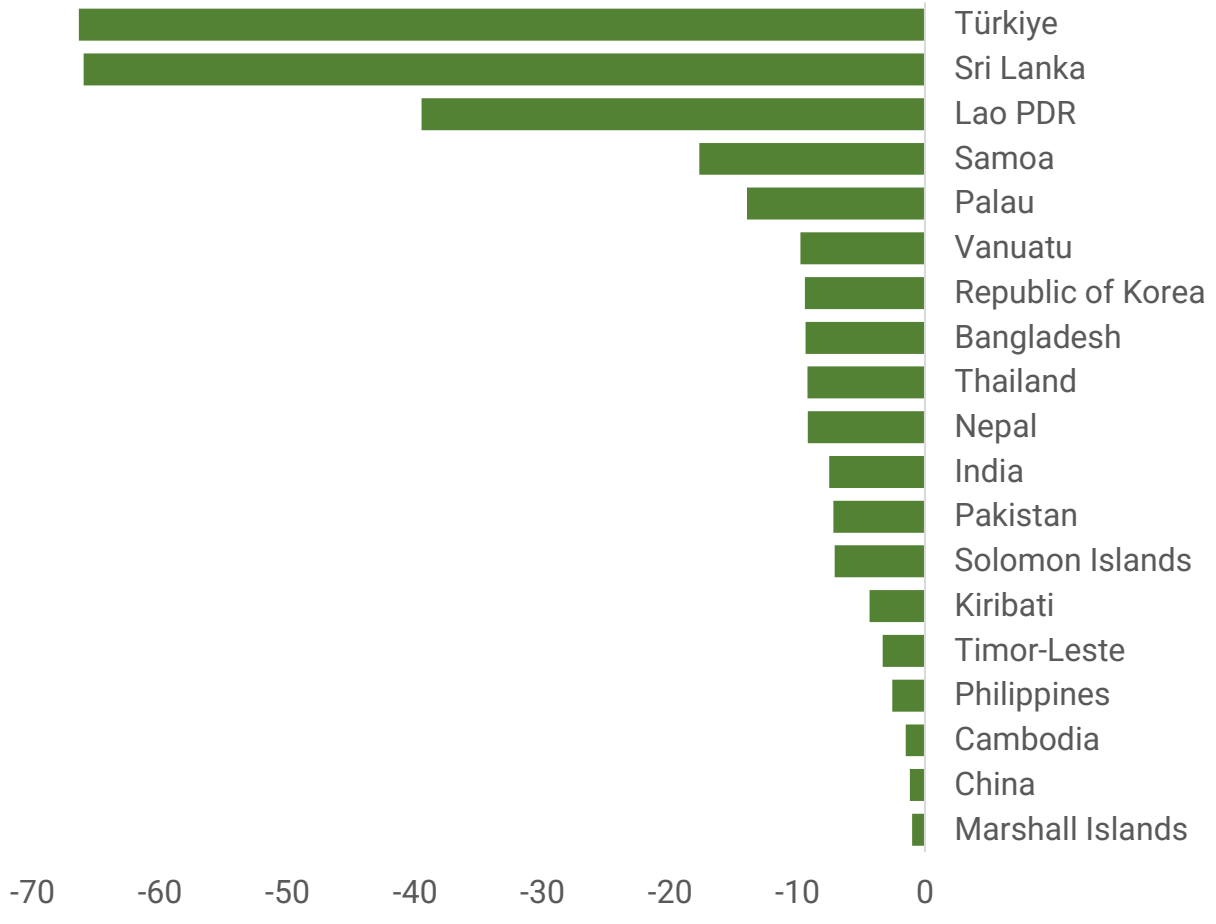
Subdued post-pandemic job recovery and weaker purchasing power

Number of persons employed (Q4/2019 = 100)



Source: ESCAP, based on CEIC.

Declines in inflation-adjusted national minimum wages in 2022 (%)



Source: ESCAP, based on ILOSTAT database.

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Key risks to the economic outlook



Maldives' GDP growth moderated while inflation slowed down

	Real GDP Growth				Inflation			
(Percentage)	2022	2023	2024	2025	2022	2023	2024	2025
South and South-West Asia	**6.0**	**5.5**	**5.2**	**5.6**	**24.8**	**21.4**	**16.7**	**10.6**
Afghanistan	-10.8	...	...	...	13.7	...	...	...
Bangladesh	7.1	6.0	5.6	5.8	6.2	9.0	7.5	6.7
Bhutan	5.2	4.2	4.0	4.0	5.7	4.5	4.2	3.8
India	7.0	6.8	6.9	7.2	6.7	5.5	4.5	4.0
Iran (Islamic Republic of)	3.8	4.5	3.7	3.3	38.2	43.0	28.0	26.0
Maldives	13.9	8.7	6.6	7.0	2.3	2.9	2.5	2.2
Nepal	5.6	1.9	4.2	5.0	6.3	7.9	6.7	6.3
Pakistan	4.7	1.7	2.0	2.3	12.1	29.1	26.0	12.2
Sri Lanka	-7.4	-2.3	1.5	3.0	50.0	19.5	5.0	4.5
Türkyie	5.6	4.5	3.1	3.9	72.3	53.4	43.0	22.0

Tourism remains the economic backbone of Maldives



Source: UNWTO, 9 August 2024

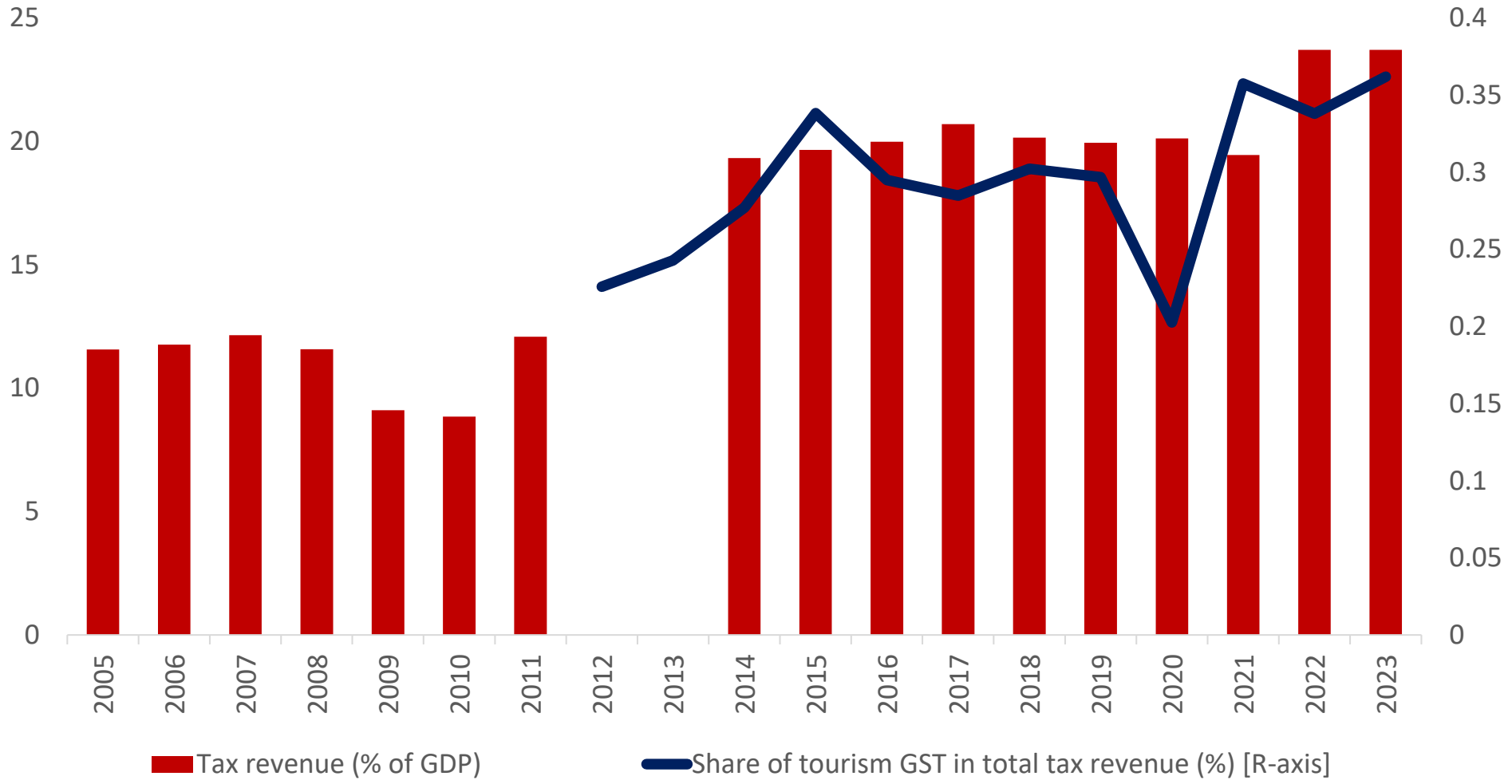
But the tourism dip during COVID-19 and its slower-than-expected recovery has weighed heavily on Maldives current account balance…



Source: CEIC and IMF, 10 August 2024

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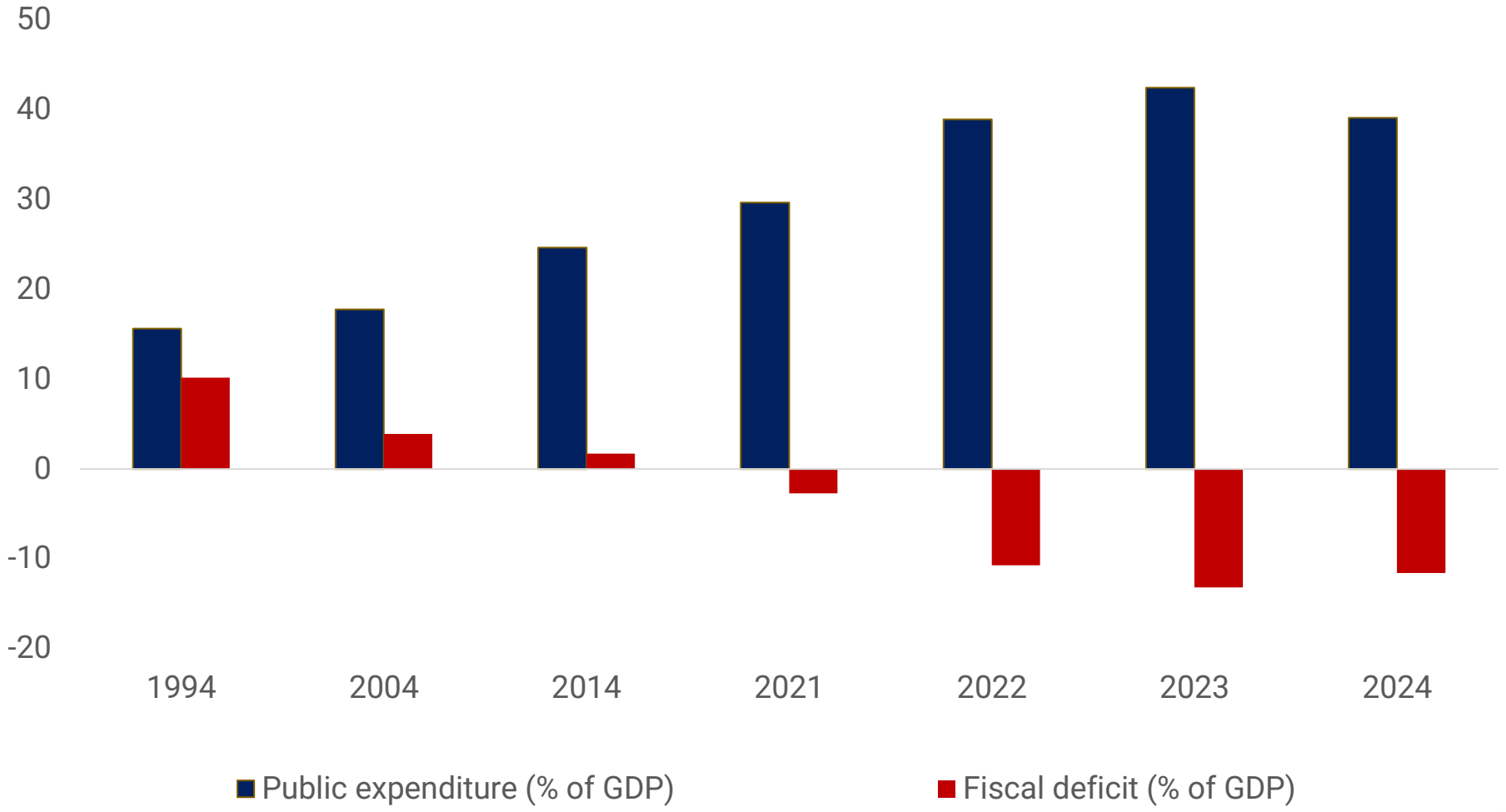
… and on fiscal margins



Source: CEIC, IMF, Maldives Monetary Authority, Maldives Ministry of Finance, 10 August 2024

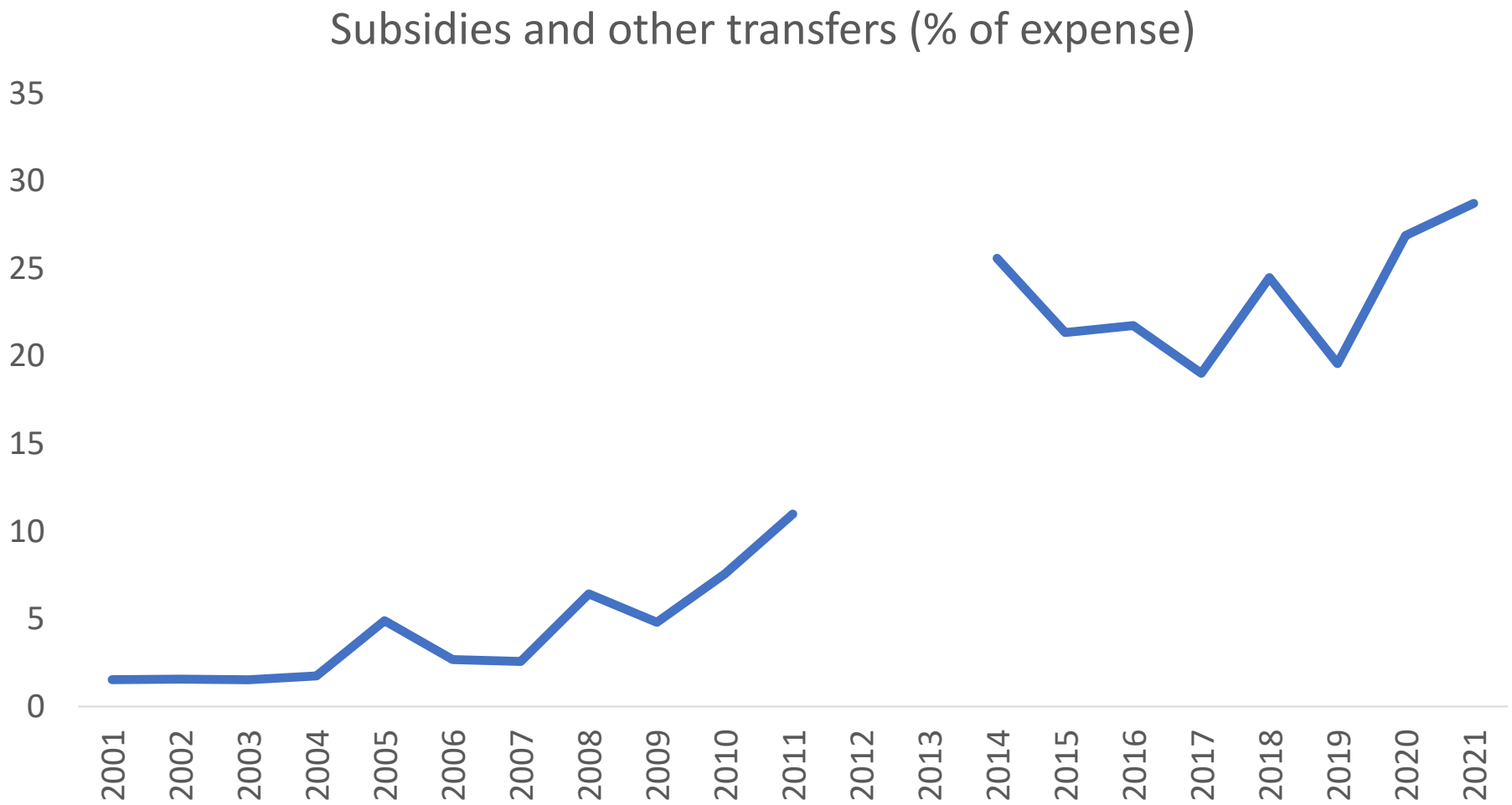
Note: Tourism GST rate raised from 12% to 16% in 2023

But the fast expansion in government expenditure is a greater driver of the fiscal challenge…



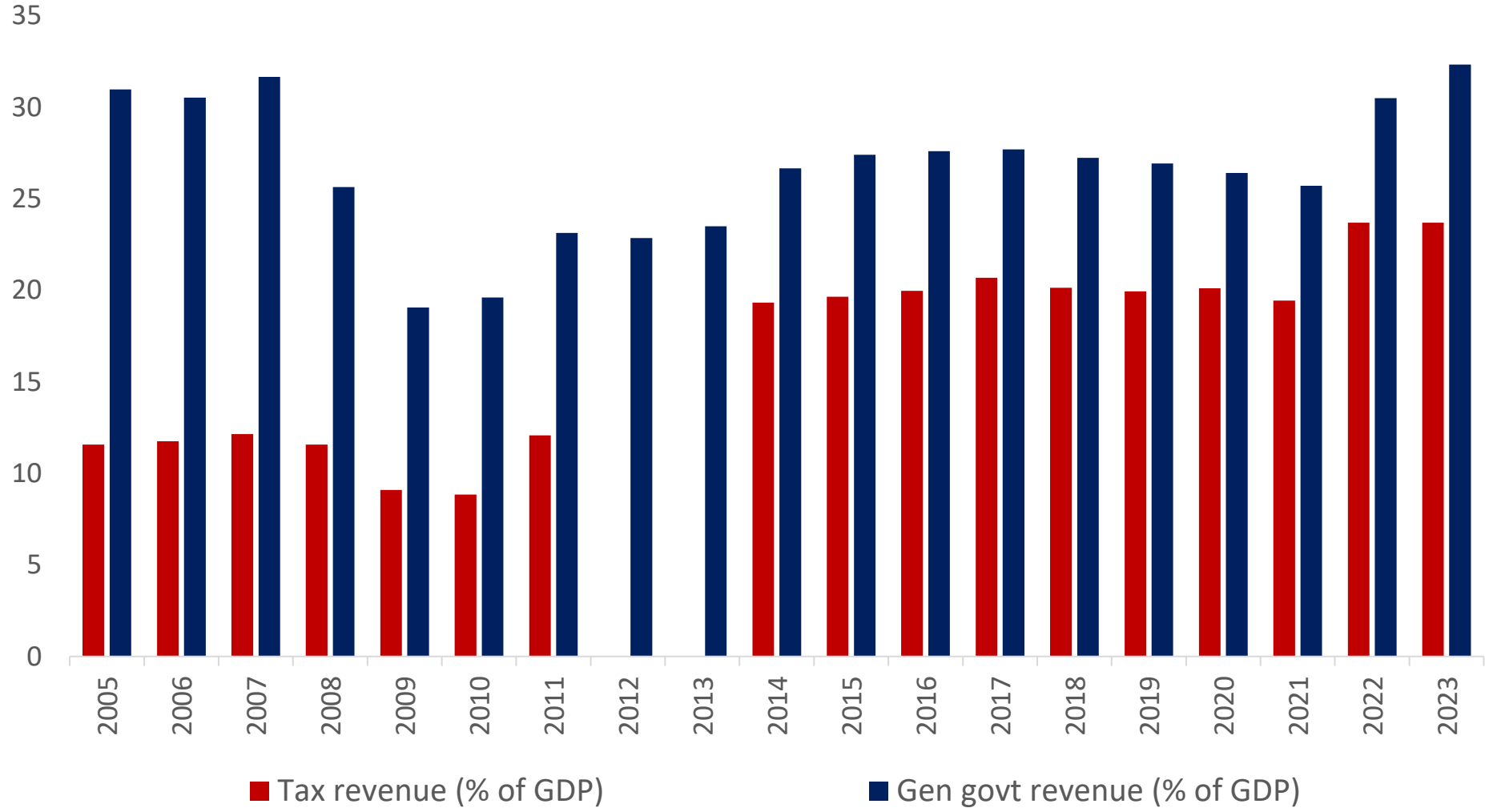
Source: World Development Indicators, World Bank, and Maldives Ministry of Finance, 10 August 2024

…due to rising capital expenditure and subsidies and transfers…



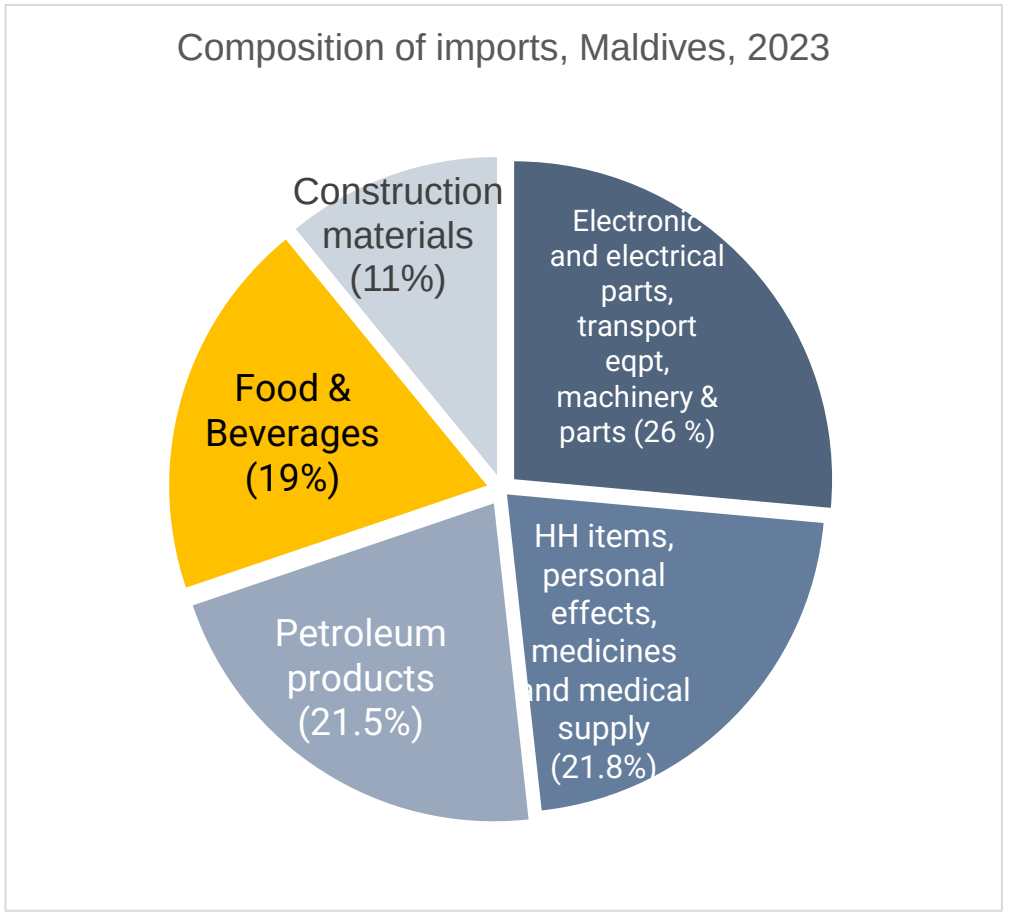
Source: World Development Indicators, World Bank, 10 August 2024

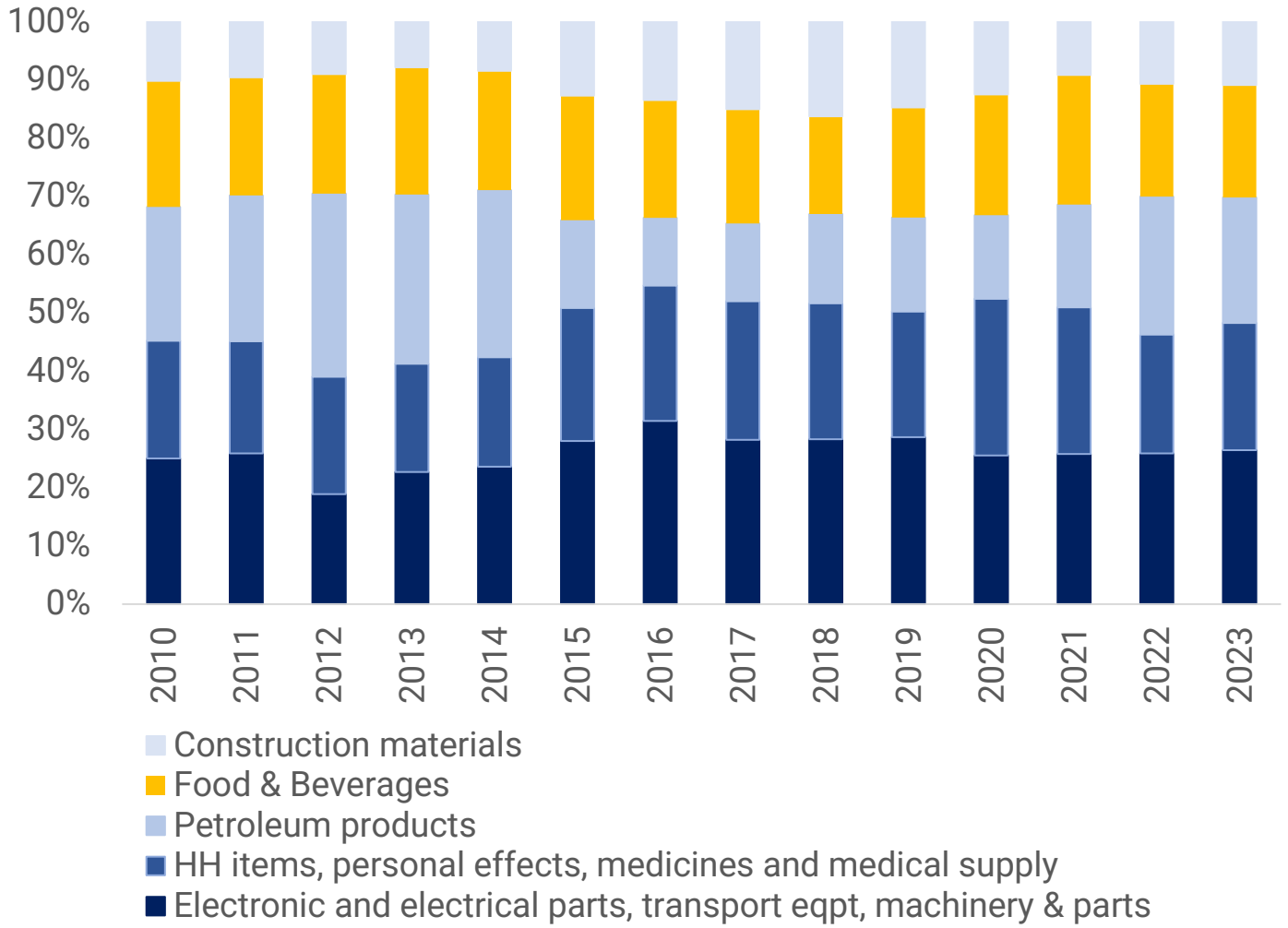
…despite significantly strengthened effort in tax revenue mobilization



Source: CEIC, IMF, Maldives Monetary Authority, Maldives Ministry of Finance, 10 August 2024

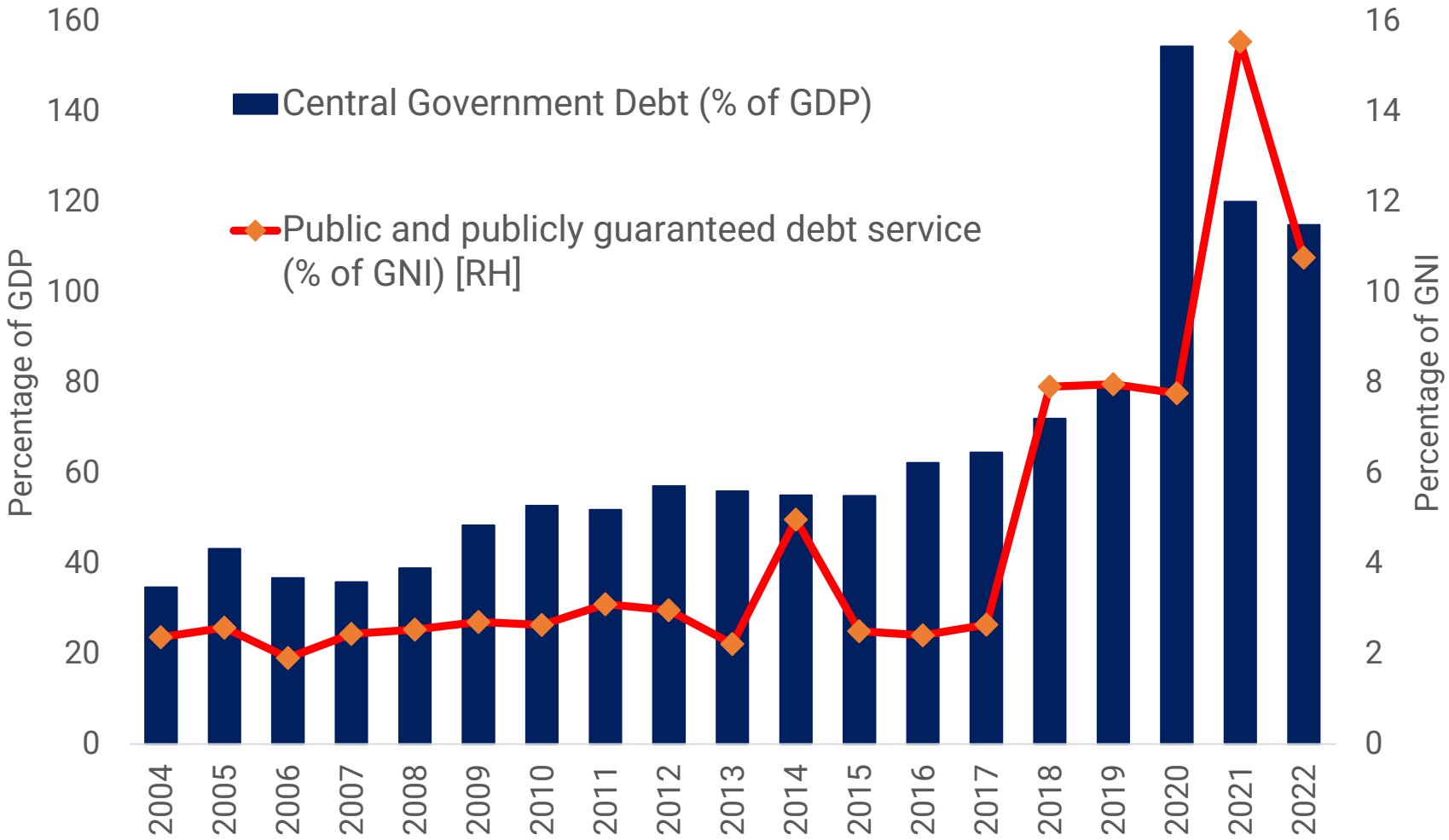
Heightened expenditure is a main source of balance-of-payment deficits as well, given Maldives' high dependence on imported consumption and capital goods





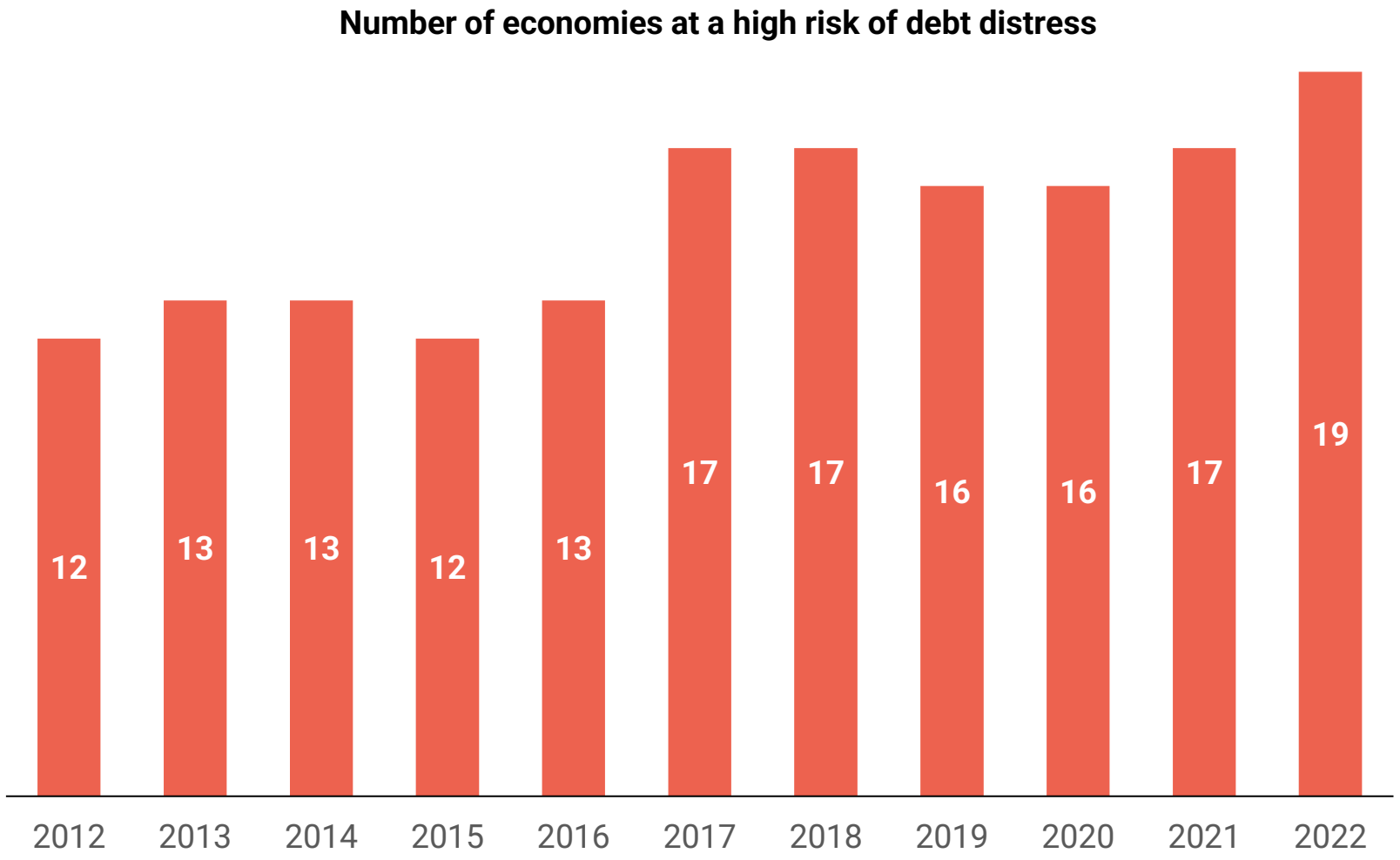
Source: Maldives Monetary Authority, 10 August 2024

The combined effect is swiftly accumulating public debt and debt servicing costs…



Source: World Development Indicators, World Bank, IMF Global Debt Database, 10 August 2024

…and Maldives remains among countries rated as having a high risk of debt distress in Asia and the Pacific in 2024

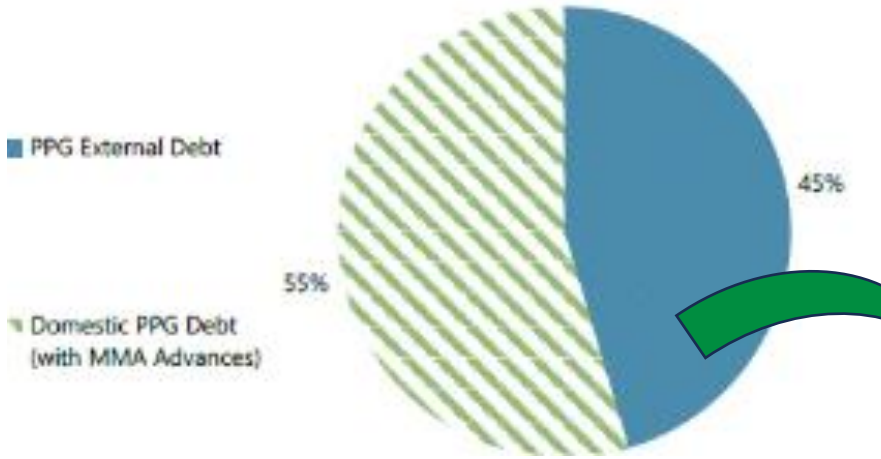


East and North-East Asia
Mongolia *
North and Central Asia
Kyrgyzstan *
Russian Federation
Tajikistan *
South and South-West Asia
Afghanistan *
Maldives *
Pakistan
Sri Lanka
Türkiye
South-East Asia
Cambodia *
Lao People's Democratic Republic *
Pacific islands
Fiji *
Kiribati *
Marshall Islands *
Micronesia (Federated States of) *
Papua New Guinea *
Samoa *
Tonga *
Tuvalu *

Source: Joint IMF-World Bank Debt Sustainability Analysis 2012-2022, countryeconomy.com, Moody's, Fitch Ratings, S&P Global

Note: * is countries in special situations (LDC, LLDC and SIDS).

Domestic creditors and external bondholders account for a lion's share of Maldives direct public debt, but debt restructuring with them proves far more difficult than with bilateral creditors



	US$ million	Percent of total PPG debt	Percent of PPG external debt
Direct External debt	2,175	31.6	70.8
Multilateral	447	6.5	14.6
Bilateral	1,028	14.9	33.5
o/w China	588	8.5	19.1
Commercial	700	10.2	22.8
Guaranteed External debt	897	13.0	29.2
Multilateral	38	0.5	1.2
Bilateral	277	4.0	9.0
o/w China	169	2.5	5.5
Commercial	582	8.5	18.9
o/w China	534	7.9	17.8
Total	3,072	44.6	100.0

External lenders for Maldives' central government (BCG) debt (US dollars)

Lender	2021 (April-June)	2021 (Oct-Dec)	2022 (April-June)	2022 (Oct-Dec)	2023 (April-June)	2023 (Oct-Dec)	2024 (Jan - March)
Bondholders (External)	357 mn	559 mn	500 mn	500 mn	500 mn	501 mn	501 mn
China EXIM	613 mn	665 mn	626 mn	589 mn	553 mn	531 mn	501 mn
India EXIM	15 mn	92 mn	129 mn	216 mn	283 mn	408 mn	438 mn

Source: IMF, and Observer Research Foundation (ORF) ,10 August 2024

Strategic considerations

- Maldives' welfare spending, housing projects and infrastructure investment are arguably all **"best-practices" by the book** for an effective pursuit of the SDGs.

- It is confronted with **a typical development trilemma**: the conflict of development ambitions, limited economic and fiscal means, and a political/social need to raise or maintain living standard.

- When development ambitions outsize domestic economic and fiscal means, there are generally **three options**.
  - Be hard on the people: work more, save more, but consume less.
  - Take more risks to finance development with debt.
  - Look for external support, including from large countries

- The balance between development ambitions and risk-taking depends on the discretion of the nation and its people.

Policy options

- **Revenue mobilization**
  - Lowering personal income tax exemption threshold
  - Strengthening beneficiary contribution to social protection programmes

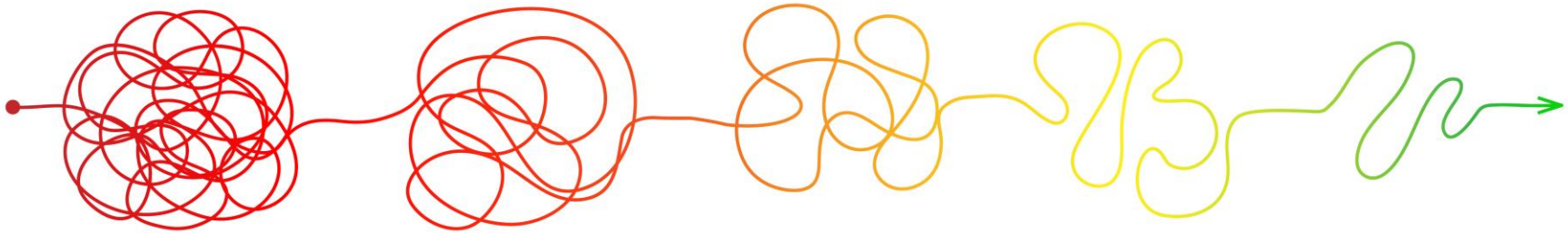
- **Expenditure management**
  - Taking a slower pace in capital investment
  - Rationalizing welfare expenditure
    - Transition from indirect and universal subsidies to targeted minimum income and welfare support.
    - Reduction in debt-financed current consumption, as opposed to investment.
  - Better prioritization of public investments with a focus on economic payoffs
    - Prioritizing investments with higher certainty, quicker payoffs and lower initial investment demands (e.g. investments in renewable energy)
    - Strengthening scrutiny on the economic and financial viability of mega public projects
  - Cost-saving effort on operational expenses of the government and its subsidiaries

Policy options

- **Economic policies**
  - Strengthening value addition of the tourism sector
  - Creating more job opportunities for Maldivian labour force in tourism and construction
  - Promoting economically viable fishery and agriculture

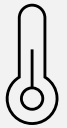
- **Seeking external support**
  - Maintaining a balance between China and India to cultivate a benign competition of the two focusing on supporting Maldives' own development
  - Debt restructuring an option? But what about domestic debt and private bondholders?

Keeping in mind global megatrends



Global megatrends affect fiscal policy through various channels

Demographic shifts 

Climate change and environmental degradation 

Technologies and digitalization 

Fiscal space and public debt sustainability

Fiscal policy conduct

Revenue

Expenditure

Borrowing cost

Design and implementation

Effectiveness

Potential fiscal impacts of megatrends are notable, diverse and uncertain

(Lower) revenue

- Shrinking workforce
- Lower production capacity
- Profit shifting in digital economy

(Higher) expenditure

- Old-age health care and social protection
- Public investment in climate projects
- Post-disaster rebuild of public infrastructure

Borrowing cost

- **Higher** inflation
  - Green taxes & investment
  - Output loss due to natural disasters
- **Lower** inflation
  - Less demand for durable goods

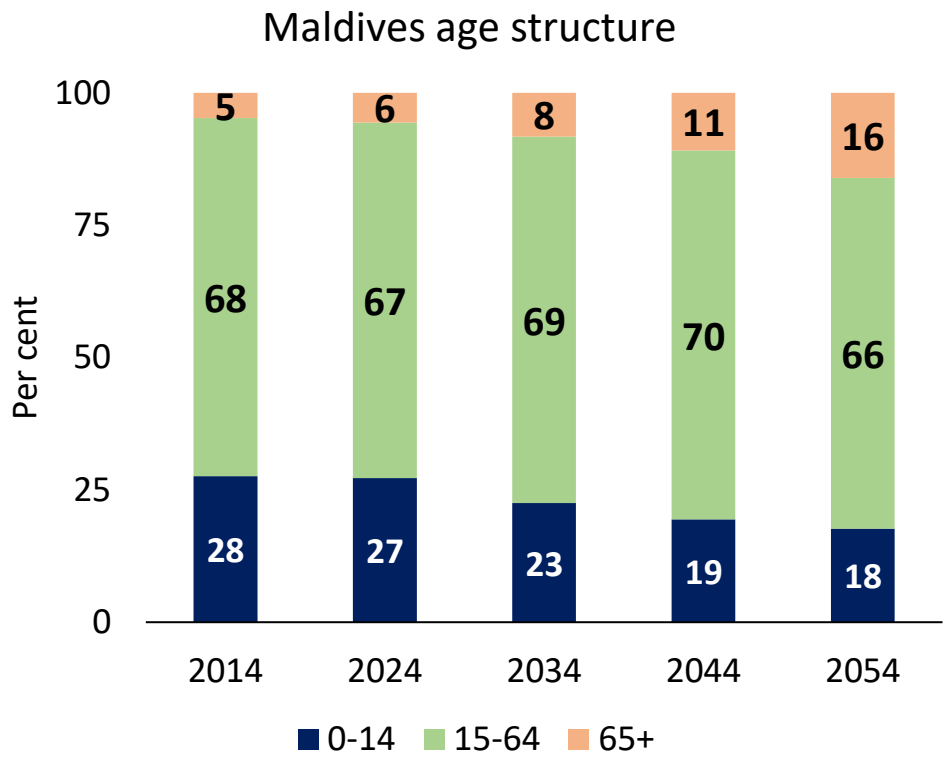
Design and implementation

- Disaster risk-informed fiscal planning
- Digitalizing public financial management
- Stronger multilateral tax cooperation

(Lower) effectiveness

- Old-age consumption responds less to fiscal stimulus

Demographic shifts – Maldives are still “young”



Source: UNDP, 2022.

Demographics STILL works in favour of Maldives economy as of 2024.

Demographic dividend needs to be capitalized through:

- education and
- employment;

and channeled into fiscal revenues and expenditures.

Demographic shifts – fiscal impact

1. **Fiscal revenues**
   - Supported by relatively large labour force.
   - As new cohorts enter labour market, the total of tax inflows potential grows.
   - High potential for tax revenue increase through changes in taxation (PIT, VAT).
2. **Fiscal expenditures**
   - The focus will gradually shift from education towards health care and social protection.
   - Social protection expenditure needs will continuously grow.
   - Fiscal multipliers will decrease as demand will shift from services to durables.

Policy actions

1. Roll out social protection schemes amid still low old-age (65+) population share.
2. Never too early to support pension schemes through life-long learning and old-age employment policies.



Encourage old-age employment



Support lifelong learning

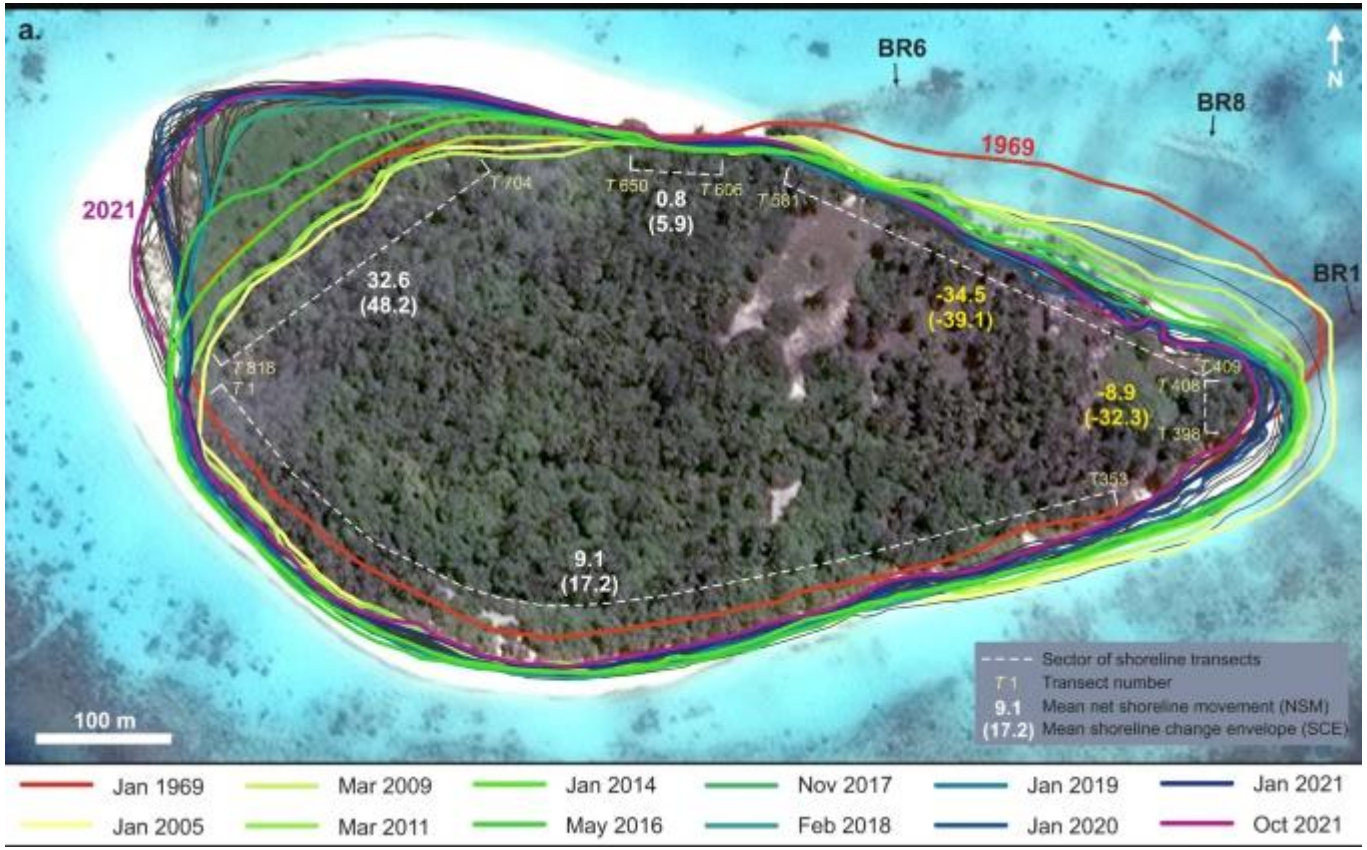


Invest in old-age health care



Expand flexible pension systems

Climate change – tough opponent for Maldives



Summary changes in the Kandahalagalaa shoreline 1969–2021.
Source: Kench, *et al.*, 2023.

As the islands “drift” and change in shape,

so do urban, economic and fiscal plans

adjusting to changing climate and its impact.

Climate change – tough opponent for Maldives



1. Prioritize – as resources are limited, fiscal expenditure on climate mitigation and adaptation must aim for highest impact, for example, coastal adaptation and green energy.

2. Investment horizon – embrace forward-looking, climate-resilient investment.

3. Flexibility – as climate change impact channels evolve, fiscal policies must quickly adjust.

4. Risk and uncertainty - review fiscal expenditure decision-making strategies, as climate change impact understanding evolves and improves.

Technological shifts – tailwind for fiscal management and economy

Digitalize public financial management



1. Lower cost – digital systems lower fiscal management costs
2. Efficiency – faster, more secure, better control of fiscal tax collection and expenditure
3. Debt management – improved transparency, data for investors, more efficient cash management, lower borrowing costs.

Ensure shared benefits of 4th industrial revolution 4IR

1. Connectivity – broadband internet boosts local economies, expanding labour market, facilitating trade in goods and services, and increasing fiscal revenues.
2. Inclusivity – even populations in the most remote islands can be included into digital economy and e-government services.
3. e-Government– e-healthcare, e-education and online banking are often the only and the most efficient solution from fiscal perspective.
4. Vulnerable populations – government support is always required, for example, at the bottom of income pyramid.

Key takeaways

- **Poverty** and **socioeconomic inequality** concerns persist despite steady economic performance.
- Urgency of boosting affordable and long-term financing for governments:
  - *Governments*: increase **fiscal credibility** and the **supply of long-term capital**
  - *International development partners*: adopt **fresh perspectives** to guide operations.
- Implications of **demographic shifts, climate change** and **technological advancements** for fiscal policymaking should not be ignored.



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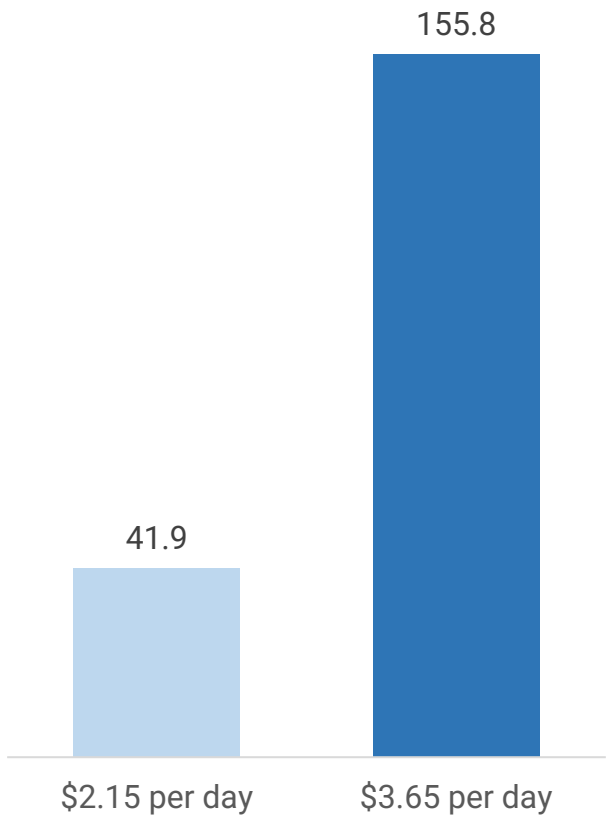
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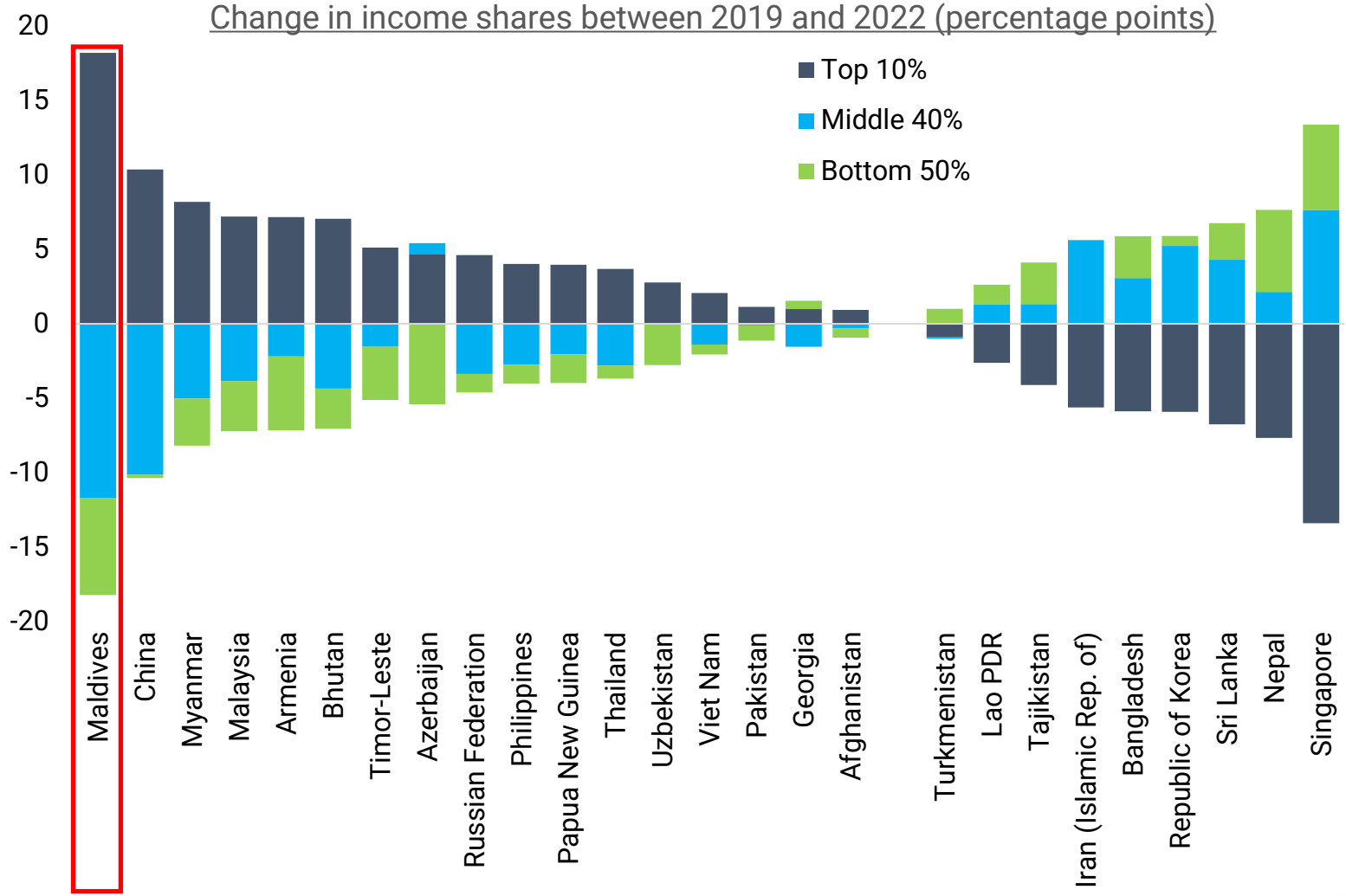
Increase in poverty and income inequality

Millions of people in Asia-Pacific who could have been pushed into poverty in 2022



Source: ESCAP estimates.

Change in income shares between 2019 and 2022 (percentage points)

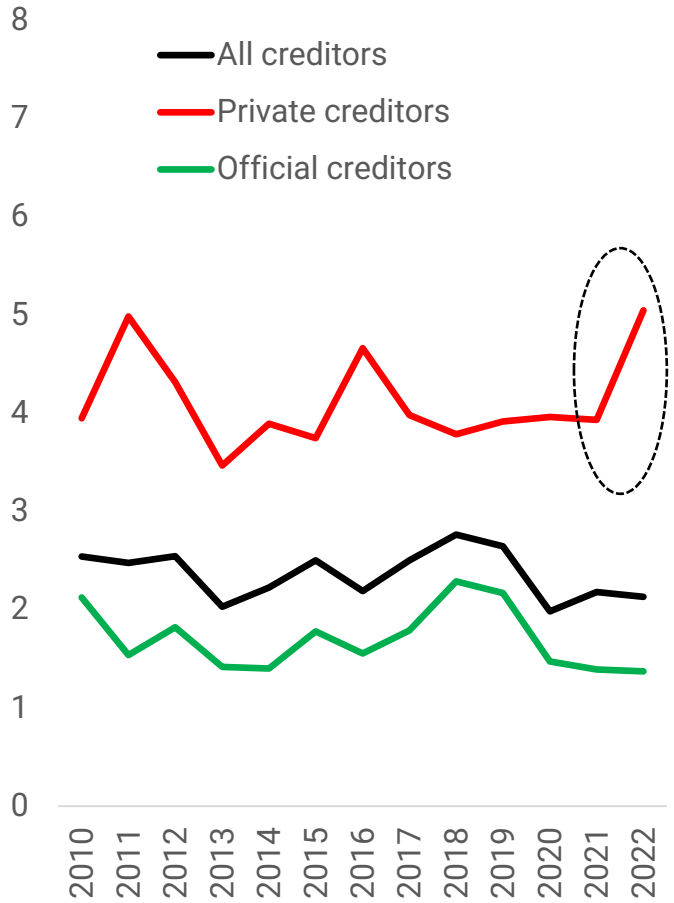


Source: ESCAP, based on World Inequality Database.

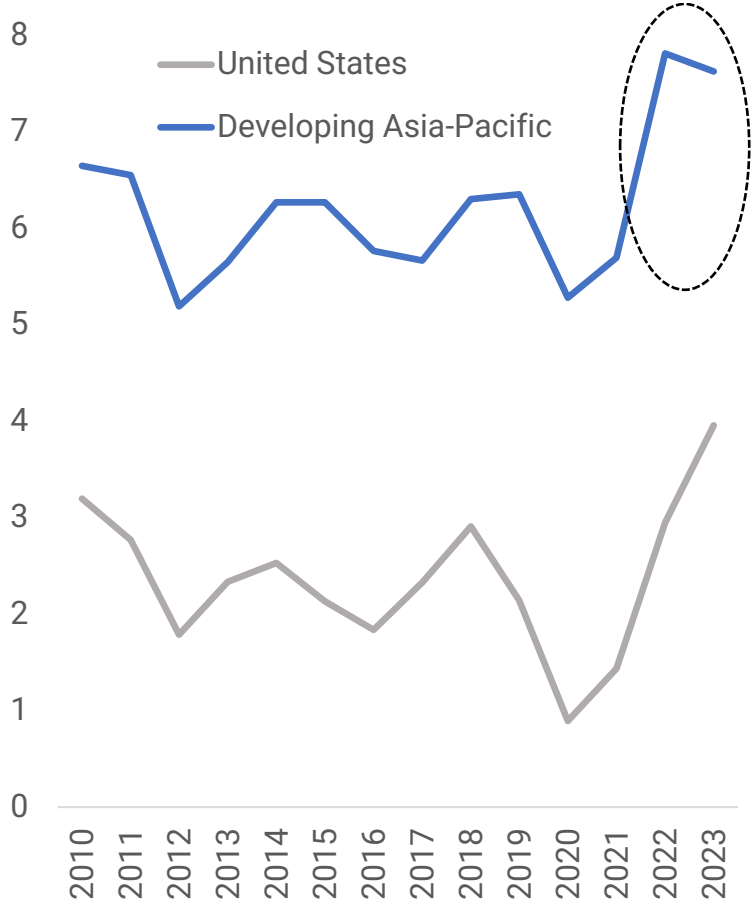
The need for affordable and long-term financing for governments in developing Asia-Pacific

Government borrowing costs in Asia-Pacific are rising, with shorter loan maturity

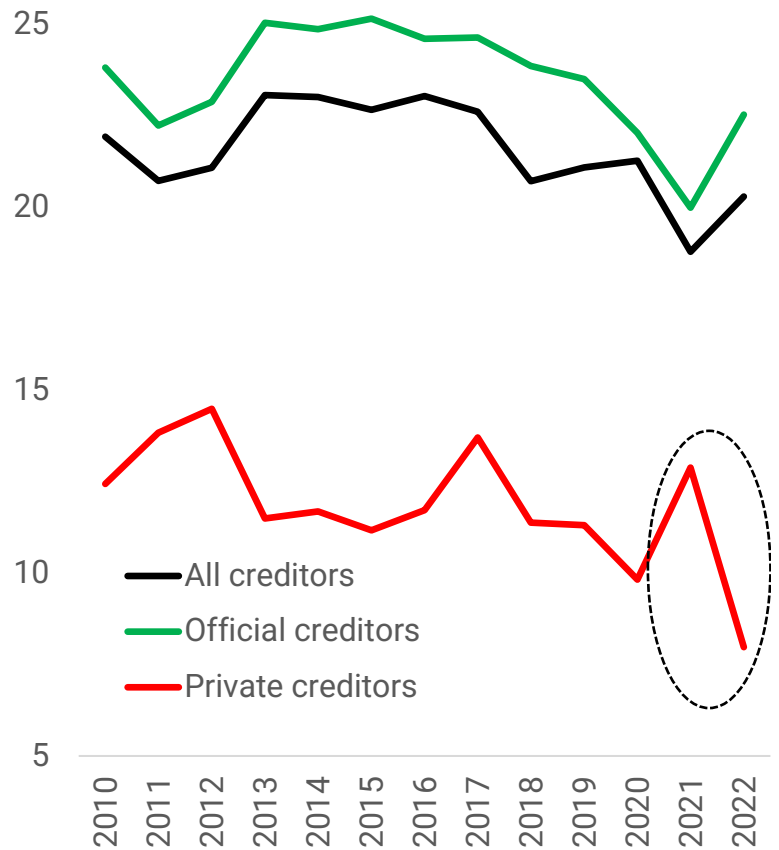
Average **interest** on new external debt commitments (%)



Average local-currency **sovereign bond yields** (%)



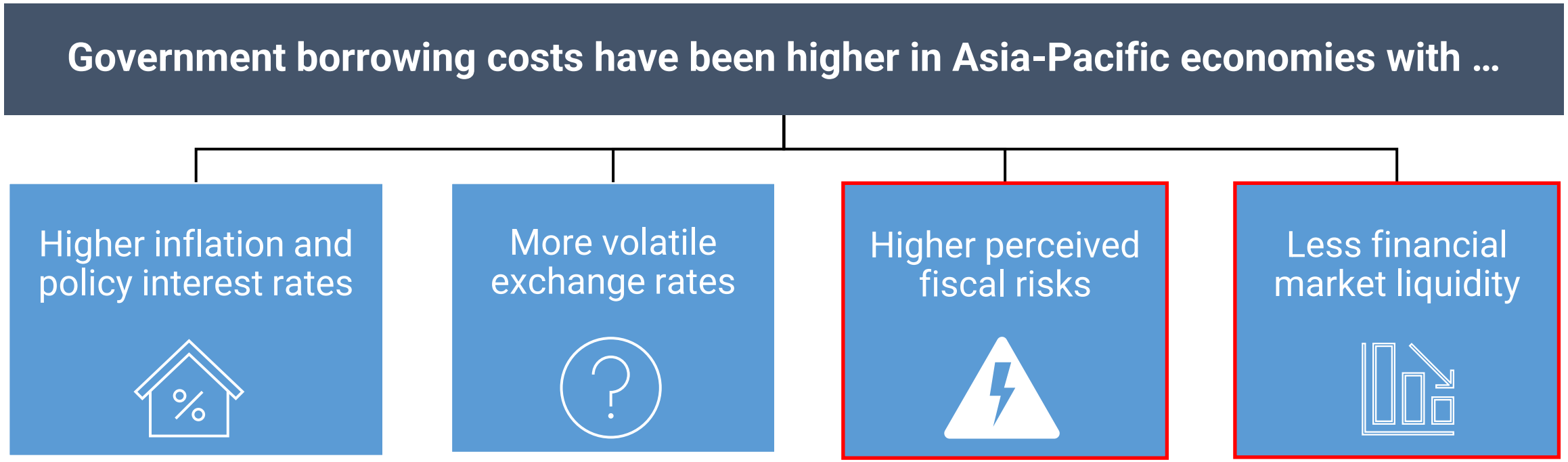
Average **maturity** on new external debt commitments (years)



Source: ESCAP, based on World Development Indicators database and Bloomberg.

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Strong macroeconomic fundamentals keep government borrowing costs at low levels



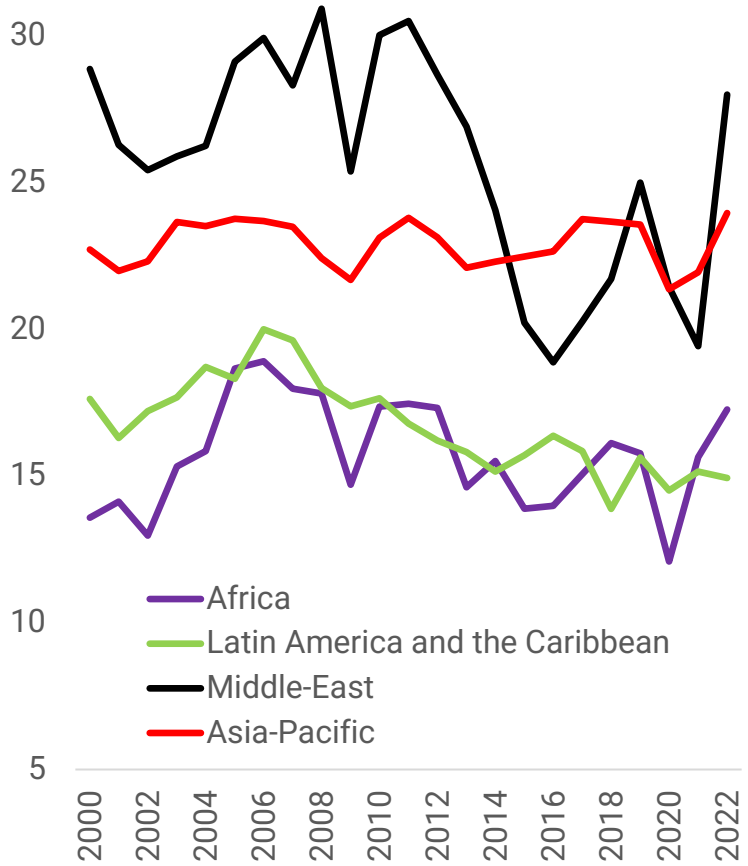
Source: ESCAP analysis.

What can governments do to increase affordable long-term financing?

Closing the tax collection gaps to reduce fiscal risks

Strengthening capital markets to channel sizeable domestic savings for investment

Domestic savings (% of GDP)



Capital market development index

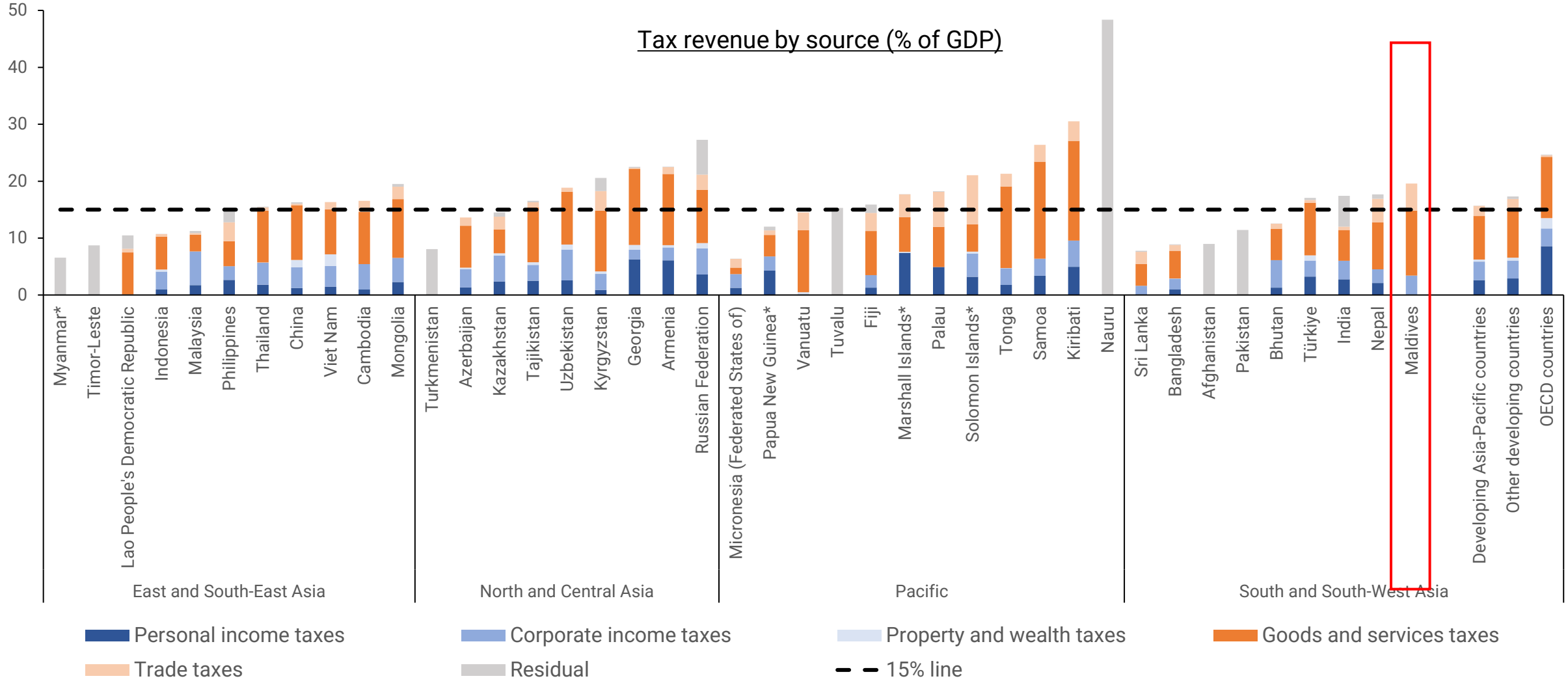


Further developing capital markets

- Widen the investor base
- Increase secondary market liquidity
- Improve risk-sharing mechanisms
- Protect investor rights

Source: ESCAP, based on World Development Indicators database and IMF Financial Development Index database.

Goods and services accounts for the high tax revenues in SSWA



Source: ESCAP, based on the IMF World Revenue Longitudinal Data set.

Note: Data on Maldives is updated to 2022

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As domestic policy actions take shape, how can international development partners help?

Donors: towards a larger and fairer concessional finance system



Provision

- Official development assistance (ODA) in 2022 at **half of the commitment** of 0.7% of gross national income (GNI) made since 1970
- Official **climate finance** should not be counted as part of ODA commitments



Allocation

- *Bilateral* ODA is often shaped by **historical and political factors**
- *Multilateral* ODA still uses **GNI per capita** as a starting allocation criterion
- The UN-led initiative on the **multidimensional vulnerability index** is a way forward

Multilateral development banks: addressing underutilized resources and capacities

Boost lending capacities

- **Increase capital**
  - New round of capital injections
- **Optimize existing capital**
  - Adjust the capital adequacy frameworks

Improve lending terms

- Increase **lending in local currencies**
  - Now 80% is in US dollar
- Cut **administrative burden** of loan packages
  - Safeguard assessments for a World Bank project costs $13.5 million on average

Strengthen systemic coordination and resource allocation among MDBs