INTERNATIONAL MONETARY FUND

IMF Country Report No. 19/281

MALDIVES

September 2019

2005 ARTICLE IV CONSULTATION—PUBLIC INFORMATION NOTICE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR MALDIVES

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2005 Article IV consultation with Maldives, the following documents have been released and are included in this package:

- A **Public Information Notice** summarizing the views of the Executive Board as expressed during its February 22, 2006 consideration of the staff report that concluded the Article IV consultation with Maldives.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on March 4, 2005, following discussions that ended on November 20, 2005, with the officials of Maldives on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on February 7, 2006.
- An **Informational Annex** prepared by the IMF staff.
- A **Staff Supplement** updating information on recent developments.
- A **Statement by the Executive Director** for Maldives.

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Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No 06/21.
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IMF Concludes 2005 Article IV Consultation with Maldives

On February 22, 2006, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Maldives.[1]

Background

Prior to the tsunami in December 2004, the Maldives had achieved high real GDP growth supported by expanding tourism and sound macroeconomic management. Income per capita rose by 60 percent over the decade up to the tsunami to above $2,500 and social indicators had improved significantly. The economy has, however, remained vulnerable to external shocks due to its undiversified production and small size. It is also at risk from rising sea levels due to global warming.

Economic consequences of the tsunami were severe. Physical damage relative to the size of the economy was the highest among affected countries; the cost of reconstructing housing and infrastructure is estimated at $375 million (about 50 percent of 2004 GDP) and tourism sustained significant damages as well. Real GDP is estimated to have contracted by 3¾ percent in 2005, as tourist arrivals fell by a third. With the decline in tourism, foreign exchange earnings also plummeted, and a current account deficit of 37 percent of GDP is estimated for 2005—exacerbated by higher oil prices. Official reserves declined to 2½ months of imports at end-2005 from 3½ months a year earlier.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. This PIN summarizes the views of the Executive Board as expressed during the February 22, 2006 Executive Board discussion based on the staff report.

The implementation of reconstruction was initially slow—donor pledge of $260 million, notwithstanding—due to problems in local consultation, limited capacity, and insufficient coordination. Measures have recently been taken to address them and reconstruction work has started to accelerate. Tourist arrivals also started to recover strongly toward the end of 2005 and real GDP is expected to rebound in 2006.

Fiscal management became difficult after the tsunami. The 2005 fiscal deficit was 12 percent of GDP as tourism revenues dropped and the government decided to provide new subsidies and expand social sector spending. A gap of 9 percent of GDP was financed by the Maldives Monetary Authority (MMA). Furthermore, the 2006 budget also suffers from a risk of a similarly large deficit as it includes a large spending program based on highly optimistic revenue assumptions. This stance may in part reflect caution the authorities appear to be exercising in adjusting policy against the backdrop of ongoing democratic reforms.

Despite high MMA financing of the budget, inflation has been subdued as domestic currency lending was modest. Commercial banks borrowed from abroad to finance reconstruction of tourist resorts—which in turn used the loan proceeds for imports. This borrowing from abroad also helped finance the balance of payments gap and limited official reserve loss.

The authorities have embarked on several structural reform initiatives—fiscal, state-owned enterprise, and financial sector reforms—to create a business environment conducive to private investment and to support diversified growth. Progress has, however, been slow due in part to limited implementation capacity, and more recently to the tsunami disaster. The authorities have expressed their commitments to accelerate the implementation of structural reforms in 2006.

Executive Board Assessment

Executive Directors expressed deep sympathy for the losses suffered by the Maldives due to the December 2004 tsunami and, noting its serious economic consequences, stressed the importance of reducing the country's vulnerability to external shocks. Directors called for fiscal and monetary reforms to enhance the authorities' capacity to conduct timely demand management along with structural reforms to expand private sector activities.

Directors commended the authorities' recent acceleration, with donor support, of work on post-tsunami reconstruction. These efforts focused on removing constraints to project implementation including, problems in local community consultation, limited capacity, and insufficient coordination within the government and among donors. The donor community is encouraged to commit the additional resources necessary to finance recovery work fully.

Directors urged a return to the firm commitment to fiscal viability and prudent fiscal policy that had been in place prior to the tsunami. They noted that the fiscal stance adopted in the 2006 budget, in which government spending—including on new recruitment and for initiatives unrelated to tsunami recovery—is well above previously envisaged levels and revenue and financing assumptions are optimistic, could jeopardize stability. Directors observed that the high domestic borrowing requirement that could ensue would place significant pressures on inflation and official reserves. Some Directors, however, argued that a delay in the introduction of fiscal adjustment measures would be warranted, given the extent of tsunami damage and taking into account the authorities' past record of fiscal prudence.

Against this background, Directors welcomed the government's recent decision to prepare contingency plans that could be triggered in the event its borrowing from the MMA exceeded certain thresholds or official reserves declined rapidly. At the same time, they noted that the potential impact of the plans on the fiscal balance remained uncertain, and stressed the importance of early action to contain risks of future serious fiscal imbalances. Directors cautioned against inadvertent cuts in spending slated for tsunami recovery.

Looking ahead, Directors stressed that further fiscal reforms will be critical. Experience in the wake of the tsunami showed that the options for fiscal adjustment to macroeconomic imbalances are limited because of rigid revenue and expenditure structures. Directors urged the authorities to increase revenue and its buoyancy through the accelerated introduction of corporate profit taxation and a broad-based sales tax. Expenditure management should reflect realistic revenue projections, while protecting priority spending. Directors agreed that civil service reforms could contribute to containing general administration costs and help appropriately limit the size of the civil service and related wages.

Directors viewed that the exchange rate peg arrangement provides a credible nominal anchor and serves the Maldives well, given the economy's openness and small size and its constrained institutional capacity. They stressed that fiscal and monetary discipline is indispensable to its support and, in this regard, urged a reduction in the large fiscal deficits and an end to automatic financing by the MMA. They stressed that early enactment of the MMA amendment, with set legal limits to the government's MMA borrowing, will be crucial to making the institution more independent.

Directors commended the authorities' efforts to introduce indirect monetary management and improve banking supervision. They welcomed the progress made in preparing for the introduction of a more market-based monetary policy—once the MMA ends its automatic financing of the deficit—including introduction of auctions of MMA certificate of deposits or treasury bills. Directors also commended ongoing efforts to strengthen the MMA's supervision of commercial banks, which has led to a reduction in nonperforming loans.

Directors urged the authorities to accelerate the implementation of structural reforms to enhance the role of the private sector and broaden the productive base. Given the dominant roles played by the public sector and by tourism, Directors noted that a business environment conducive to broad-based private investment, supported by the privatization of public enterprises and the implementation of key economic and financial legislation, both of which had been stalled during the aftermath of the tsunami, would be critical to achieving medium-term viability. Directors welcomed the efforts of the government to put in place the necessary legal framework to combat money laundering and the financing of terrorism.

Directors appreciated the authorities' past efforts to improve the statistical base and encouraged that further resources be devoted to enhance data in a number of areas for effective policy design and evaluation.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise

Maldives: Selected Economic Indicators, 2001–05

	2001	2002	2003	2004	Est. 2005
			(Annual percentage change)		
Growth and prices					
Real GDP	3.5	6.5	8.5	8.8	-3.6
Consumer prices (period average)	0.7	0.9	-2.9	6.4	5.7
Consumer prices (end period)	...	-5.0	-1.5	10.1	5.0
			(Percent of GDP)		
Central government					
Revenue and grants	33.0	33.1	34.9	33.2	48.8
Expenditure and net lending	37.7	38.0	38.3	34.8	61.1
Of which: Capital spending	12.3	12.5	13.6	10.7	22.3
Overall balance	-4.7	-4.9	-3.4	-1.7	-12.3
Financing					
Domestic	2.8	0.4	-1.5	-1.3	9.0
Foreign	1.9	4.5	4.7	4.0	3.2
			(Annual percentage change)		
Money and credit					
Domestic credit	19.4	11.7	-5.8	31.7	56.4
Public sector	7.0	6.5	-25.5	-26.0	109.4
Central government (net)	8.4	5.1	-19.6	-45.2	118.1
Private sector	29.9	15.3	6.8	57.3	45.3
Broad money	9.0	19.3	14.6	32.6	9.1
			(In millions of U.S. dollars)		
Balance of payments					
Exports, including reexports	110.1	132.3	151.9	181.0	169.6
Imports	-346.3	-344.7	-414.3	-567.3	-686.8
Nonfactor services (net)	244.2	251.7	311.1	352.4	118.1
Current account balance	-58.8	-35.7	-31.9	-128.9	-297.9
(In percent of GDP)	-9.4	-5.6	-4.6	-16.1	-36.5
Overall balance	-21.4	39.8	74.3	57.7	-136.4
Gross official reserves (year-end)	94.3	134.6	161.0	205.2	187.2
(In months of imports of GNFS) 1/	2.5	3.5	3.6	3.4	2.5
External debt					
(In millions of U.S. dollars)	209.8	259.0	289.5	331.8	481.6
(In percent of GDP)	33.6	40.4	41.9	41.5	58.9
Of which: Public	29.0	34.8	39.5	39.0	41.4
Debt service	22.0	22.9	22.0	28.4	33.4
(In percent of domestic exports of GNFS)	5.1	5.0	4.0	4.5	7.6
Exchange rate					
Rufiyaa per U.S. dollar (period average)	12.2	12.8	12.8	12.8	12.8
Memorandum item:					
Nominal GDP (in millions of rufiyaa)	7,650.8	8,201.0	8,842.0	10,235.1	10,457.9

Sources: Data provided by the Maldivian authorities; and IMF staff estimates and projections.

1/ GNFS = Goods and nonfactor services.

INTERNATIONAL MONETARY FUND

MALDIVES

Staff Report for 2005 Article IV Consultation

Prepared by the Staff Representatives for the
2005 Consultation with Maldives

Approved by Daniel Citrin and Michael Hadjimichael

February 7, 2006

- The 2005 Article IV consultation discussions were held in Male during November 6-20, 2005. The staff team comprised Messrs. Shishido (head), Tchakarov, Straub, and Zulverdi (all APD). The team's visit overlapped with MFD and STA technical assistance missions as well as World Bank and AsDB missions. The team met with President Gayoom, Finance Minister and Maldives Monetary Authority Governor Qasim, Trade Minister Jaleel, Tourism Minister Shougee, Fisheries and Agriculture Minister Kamaaluddin, Attorney General Saeed, and other senior officials and private sector representatives.
- The 2004 Article IV consultation was concluded by the Executive Board on May 24, 2004. Directors at that time welcomed the strong rebound in growth and improved balance of payments position, and noted that inflation remained subdued. Directors also welcomed the buildup of foreign exchange reserves and the improvement in revenue which had made it possible for the government to avoid domestic financing of their deficit in 2003. However, Directors stressed that the Maldives remained vulnerable to external shocks due to its heavy reliance on tourism and fisheries.
- Following the tsunami disaster in December 2004, the authorities requested a purchase under the Fund's policy on emergency natural disaster assistance on concessional terms. On March 4, 2005, the Executive Board approved the Maldives' request (50 percent of quota or SDR 4.1 million).
- Maldives continues to avail itself of the transitional arrangements under Article XIV of the Fund's Articles of Agreement, but no longer maintains Article XIV restrictions. Furthermore, the Maldives is yet to accept the obligations of Article VIII, Sections 2, 3, and 4, but maintains no restrictions on the making of payments and transfers of current international transactions.
- The principal author of this staff report is Hisanobu Shishido.

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EXECUTIVE SUMMARY

The Maldives suffered devastating damage from the December 2004 tsunami. Although human casualties were limited, damage to infrastructure was extensive, with the cost of reconstruction estimated at nearly a half of GDP. Tourism declined by a third and the economy contracted in 2005. Fiscal management has deteriorated and foreign reserves declined from 3½ months of imports a year ago to 2½ months.

Reconstruction work has progressed slowly in 2005 but the pace is picking up. Recovery work has been slow due to insufficient coordination, problems in local consultation, and limited management capacity. The government and donors have been addressing these problems and the pace of implementation is finally accelerating. Donors have so far pledged 70 percent of assessed reconstruction needs.

The tsunami has revealed the country's vulnerability—dependence of the economy on tourism and an inflexible fiscal structure. The economy remains dependent on tourism and vulnerable to negative shocks that affects the sector. Furthermore, it is structurally difficult to respond to these shocks through fiscal adjustments because raising fiscal revenue in a timely manner is hard and spending is downward rigid.

The 2006 budget (announced soon after the conclusion of the Article IV consultation mission) is highly expansionary and threatens sustainability. The government has added to the fiscal deficit through new recruits, expansion of untargeted social programs, and a large domestically funded public investment program while using optimistic revenue projection. The government needs to renew commitments to tighter policy.

Fiscal reforms are of high priority. To enhance the economy's resilience, corporate taxation and broad based sales tax need to be introduced, and expenditure management improved through adopting a Medium-Term Expenditure Framework (MTEF)—to contain spending in line with realistic revenue projections and protect high priority activities. Civil service reforms also need to be high on the agenda.

Monetary policy should be geared to sustaining the peg arrangement based on indirect management. The objective of monetary policy should be to support the peg arrangement, which has served well as a credible nominal anchor. Automatic financing of the budget deficit by the Maldives Monetary Authority (MMA) should cease and indirect monetary operations need to be adopted based on auctioning of MMA certificate of deposits (CDs) or treasury bills.

Achieving medium-term viability remains a significant challenge. In addition to pursuit of prudent macroeconomic policy, implementation of structural reforms is indispensable for sustaining robust growth and reducing the economy's vulnerability by creating business environment conducive to broad-based private investment. Priority actions include privatization of state-owned enterprises (SOE)—the public sector still dominates activities that in other countries are carried out by the private sector—and adoption of key economic and financial legislations.

I. Introduction and Background

1. **The Maldives suffered devastating damage from the tsunami in December 2004.**[1] Physical damage relative to the size of the economy was the highest among affected countries and livelihood was severely disrupted—including displacement of 5 percent of population. The cost of reconstructing housing and infrastructure is estimated at $375 million (about 50 percent of GDP), and private tourist resorts sustained damages amounting to $100 million (largely covered by insurance). However, the damage in Male was less severe and key productive assets and infrastructure in the capital region were largely spared.

2. **The serious economic consequences of the tsunami are evident.** Real GDP is estimated to have contracted by 3¾ percent in 2005, as tourist arrivals fell by 33 percent. With the decline in tourism, foreign exchange earnings have plummeted, and an overall balance of payments deficit of $140 million is projected for 2005—exacerbated by higher oil prices (Figure 1, Table 1). The fiscal balance for 2005 worsened as tourism revenues dropped while new initiatives were taken to provide power and water subsidies and increase (untargeted) social sector spending. Even though the government decided to limit administrative spending and increase revenue collection during the last quarter of the year, financing from the Maldives Monetary Authority (MMA) amounted to 9 percent of GDP (Figure 2). Tourist arrivals started to recover strongly toward the end of 2005 as most tourist resorts reopened, and real GDP is expected to rebound in 2006. But significant fiscal and external gaps are still projected.

3. **Reconstruction work proceeded slowly in 2005 because of implementation difficulties and, for some sectors, inadequate donor support**.[2, 3] Aid amounting to $260 million has been pledged so far, but disbursements and reconstruction were initially slow due to problems in local consultation, limited capacity, and insufficient coordination. Measures have been taken to address them and reconstruction work has started to accelerate (Box 1). To fully reconstruct infrastructure, however, additional donor commitments of around $100 million are still needed—especially in sectors such as transport and water and sanitation.

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[1] The Maldives consists of some 1,200 low-lying islands, of which 200 are inhabited. These islands spread over 900,000 square kilometers.

[2] A working group comprising the IMF, World Bank, AsDB, United Nations Development Program, and the office of the U.N. Special Envoy for Tsunami Recovery (former President Clinton) has been formed to assist the authorities in mobilizing necessary donor support and in preparing a package of economic policy reforms that could support additional assistance.

[3] On March 4, 2005, the Fund extended emergency natural disaster assistance on concessional terms (50 percent of quota or SDR 4.1 million).

Box 1: Progress in Tsunami Recovery

Many recovery projects remain unfunded. Donors have so far pledged to finance around 70 percent of estimated recovery costs ($375 million). Water, transportation, and power projects are particularly underfunded.

Implementation was initially slow even in areas with donor funding. As of October 2005, 18 percent of donor pledges (or about 6 percent of GDP) has been disbursed. About half of internally displaced people still live in temporary shelters and tents and more than 30 percent are doubling up with others.

Implementation of Tsunami Recovery Projects
(As of October 31, 2005)

	Number of required projects	Completed	Under construction	Construction not started
		(Percent of required projects)		
House repairs	5,212	15.4	25.1	59.5
House reconstruction	2,596	0.1	8.6	91.3
Harbor	106	0.0	2.8	97.2
Sanitation system	29	0.0	0.0	100.0
Education	19	89.5	10.5	0.0
Health (hospital, etc)	57	12.3	28.1	59.6

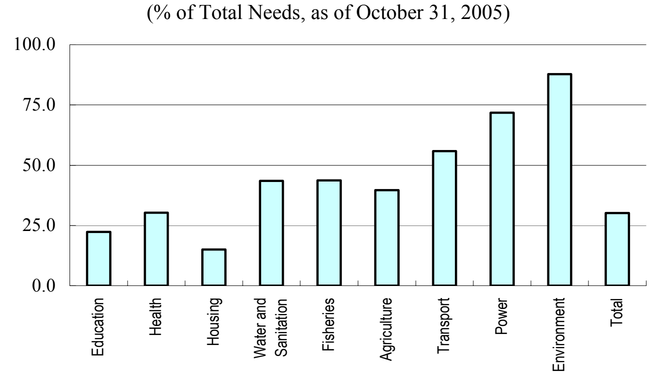
Source: Maldives Ministry of Planning and National Development.

These delays were caused by prolonged community consultation, problems in the tender process, inadequate local capacity, and insufficient coordination. Residents' psychological attachment to their islands complicated implementation of projects involving relocation. Tenders have been time consuming because results can be revoked if any party complains about the outcome. Engineers and project managers are in short supply. There is also scope for improving donor coordination and clarifying responsibilities within the government.

The government and donors have taken measures to accelerate implementation. The government has started to devolve project implementation to local authorities, which has proven effective in expediting housing reconstruction. Tender processes are being reviewed, and donors have provided project managers and site engineers. Workshops have been conducted to improve donor coordination, and, to improve monitoring, development data systems are being installed with UN assistance. As a result, the pace of reconstruction has started to accelerate.

The budgetary impact of recovery efforts is hard to measure as it depends on the pace of implementation and disbursement of donor funds. In addition, it is hard to capture donors' direct payments and some donors operate outside the budget framework. With these caveats, recorded budgetary reconstruction spending as of October 2005 was Rf 300–400 million (3 percent of GDP) including a government contribution of 1 percent of GDP. The government estimates that the total recovery efforts in 2005 should amount to over 10 percent of GDP. In the 2006 budget, donor funding of recovery efforts is expected to be about Rf 2.4 billion or 20 percent of GDP. In addition, the government contribution included in the budget is 1–2 percent of GDP.

Financing Gaps of Tsunami Recovery Projects
(% of Total Needs, as of October 31, 2005)



Source: Maldives Ministry of Finance and Treasury

4. **Furthermore, donors' efforts to provide budget support have been impeded by insufficiently tight fiscal policy.** The World Bank and the Asian Development Bank (AsDB) are considering extending budget support totaling nearly $40 million (of which about half could be disbursed in 2006) provided a sound fiscal framework is reestablished. In the event, however, the 2006 budget adopted immediately after the conclusion of the Article IV mission is much more expansionary than envisaged or discussed with the mission; both the World Bank and AsDB are urging the authorities to recommit to a prudent policy.

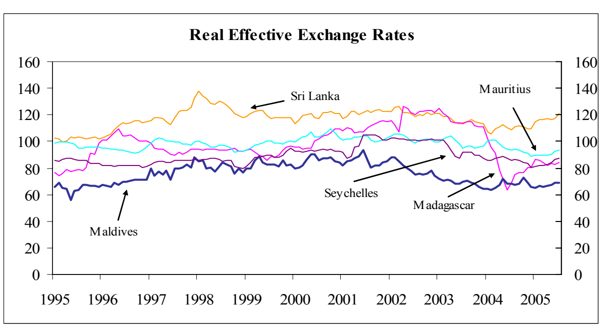
5. **These developments have taken place against a backdrop of ongoing reforms to introduce multiparty democracy**. A longstanding ban on political parties was lifted in June 2005, and the government announced that democratic multiparty elections would be held soon. But consensus has not been reached on the pace of implementing these reforms and there have been confrontations between security forces and the opposition. In this environment, the government appears to be proceeding cautiously in adjusting fiscal policy in response to emerging revenue shortfalls and financing constraints.

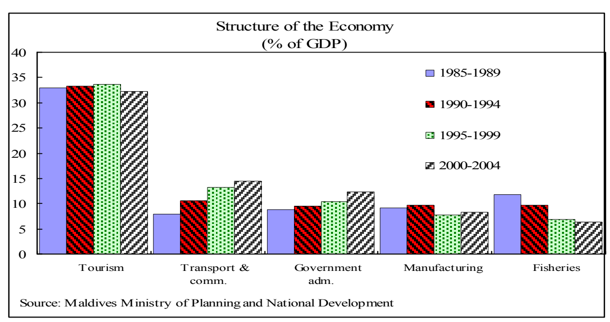
II. Stocktaking and Recent Developments

Maldives: Developments in 1995-2004

	1995-1998	1999-2001	2002-2004
GDP growth	9.2	5.1	7.5
Tourism growth	8.6	4.1	8.7
Fiscal revenue/GDP	25.8	29.9	33.0
Current expenditure/GDP	19.2	24.5	26.6
Domestic financing/GDP	-0.5	3.5	-0.8

6. **The Maldives achieved high real GDP growth over the decade up until the tsunami based on expanding tourism**. The tourism sector contributed nearly half of the growth, with fisheries activity, reflecting recent private participation, also contributing. Meanwhile, the dollar peg provided the Maldives with a stable nominal anchor generally helping to preserve external competitiveness. As a result, income per capita grew by 60 percent over the decade (through 2004) to above $2,500, and social indicators improved significantly.[4]





[4] Due to the strong economic performance, the UN decided to graduate the Maldives from the least developed countries (LDC), just a few days before the tsunami. After the tsunami, the graduation has been postponed by three years in response to the authorities' request.

7. **However, the economy has remained vulnerable to external shocks due to its undiversified production, small size, as well as geography**—as demonstrated in the tsunami and its aftermath. The narrow production and export base—tourism and fisheries—is highly vulnerable to external shocks and the scope of policy response is correspondingly limited.[5] At the same time, global warming and rising sea levels pose a long-term threat.

8. **Macroeconomic management has generally been sound, but fiscal performance has fluctuated with external conditions and spending slippages**. The authorities increased revenues by 9–10 percentage points of GDP over the last decade through higher tourism revenues and state-owned enterprise (SOE) transfers. Although current expenditure rose slightly faster, domestic financing of the budget was kept manageable largely through restraint on capital spending, and foreign financing. However, the government's capacity to respond to adverse shocks through timely fiscal adjustment is limited. Revenues are inflexible in the short run (the "bed" tax is nominally fixed per overnight stay of a tourist, and resort lease payments and SOE transfers are pre-determined for each budget), and expenditures tend to be rigid downward.[6] During 1999–2001, a combination of spending slippages and a global tourism slowdown led to high recourse to MMA borrowing and a currency devaluation in 2001.

9. **During 2003–04, growth remained strong with improved fiscal performance**. Real GDP growth averaged 8 percent over 2003–04 while nonfood inflation was stable. The fiscal deficit declined and was largely financed by concessional foreign borrowing. Robust revenues associated with buoyant tourism contributed to this improvement. This performance was only partially offset by a 40 percent rise in civil servants' wages in September 2004, the first adjustment in five years that more than offset the real wage erosion since the last adjustment. The original 2005 budget also envisaged practically no domestic financing—the higher wage bill was to be financed by enhanced revenues.

10. **With the tsunami, however, the fiscal situation deteriorated dramatically.** The supplementary budget prepared in August 2005 envisaged a budget deficit (including foreign grants) of Rf 1.6 billion (15 percent of GDP)—up from 4 percent of GDP in the original budget—and a domestic financing requirement of 12 percent of GDP. Because of the tsunami, tourism-related revenues declined by 4 percent of GDP and new revenue

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[5] The scope of diversification may be limited by the county's endowments including small size and dispersed human settlements. High and growing income flows from tourism may also be raising domestic wages and limiting development of competitive manufacturing activities.

[6] SOE transfers are based on enterprises' profits in the previous year.

measures included in the original budget (2 percent of GDP) were not implemented.[7] On the spending side, domestic contributions to higher relief and recovery outlays and newly announced initiatives each added 2 percent of GDP to the fiscal deficit. Recognizing the risk associated with such an expansionary stance, the authorities started to take action during the last quarter of the year, and saved about 3 percent of GDP mainly by reducing administrative expenditures. This, however, still left an estimated deficit of 12 percent of GDP with MMA borrowing of 9 percent of GDP (Table 3).[8]

2005 Fiscal Developments
(In millions of rufiyaa)

	Initial Budget	Supplementary Budget	Most Recent Budget
Total revenue & grants	4,207	5,043	5,108
Tax revenue	1,878	1,604	1,598
Import duties	1,194	1,133	1,133
Tourism tax	557	344	336
Nontax revenue	2,221	1,774	1,844
SOE transfers	650	647	647
Resort lease and land rent	759	546	616
Others	812	581	581
Grants	83	1,637	1,637
Expenditure and net lending	4,636	6,642	6,392
Current expenditure	3,475	4,240	4,120
Capital expenditure	1,268	2,335	2,205
Overall balance	-429	-1,598	-1,284
(In percent of GDP)	(-4.1)	(-15.3)	(-12.3)
Financing	429	1,598	1,284
Foreign financing	408	339	339
Domestic financing	21	1,259	945

Source: Ministry of Finance and Treasury.

11. **High domestic financing of the budget notwithstanding, inflation has been subdued as private domestic currency lending was modest.**[9] In particular, foreign-owned commercial banks borrowed about $100 million from their headquarters abroad and on-lent the funds largely to tourist resorts, which in turn used the proceeds for importing reconstruction materials.[10] Thus, while government borrowing surged, total domestic currency lending was more limited and inflation has remained well below 5 percent (year-on-year) (Table 4).

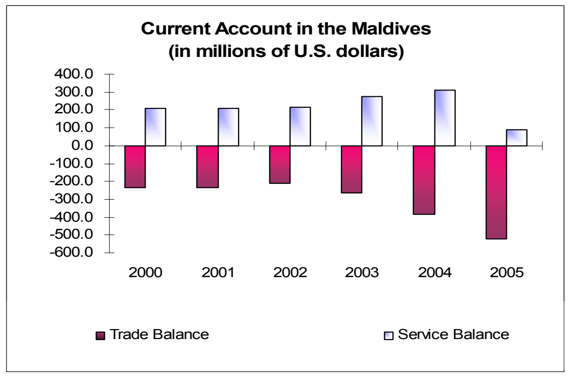
[7] These measures were: a new foreign investment royalty, increased cost recoveries, and higher land tax rates. In addition, measures announced immediately after the tsunami were also not fully implemented such as refraining from granting import duty waivers for resort reconstruction. The authorities argue that slow insurance payments made it difficult not to grant these waivers.

[8] Agencies are allowed to spend capital budget allocations till March of the following year. Thus, actual MMA borrowing during 2005 was limited to 6 percent of GDP and the remainder is expected to materialize in the first quarter of 2006.

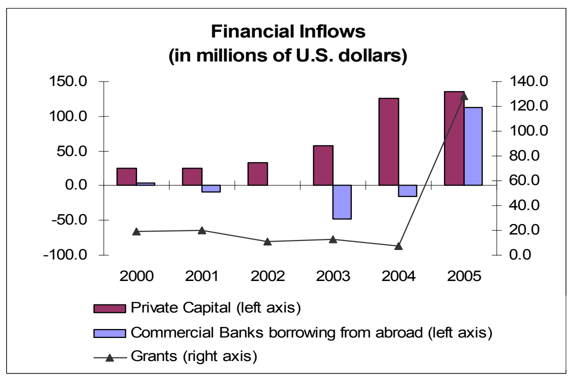
[9] The banking system comprises three state-owned foreign banks (from India, Pakistan, and Sri Lanka), a local state-owned bank (Bank of Maldives), and a foreign private bank. In addition, a leasing company (in part IFC-funded) and state-owned Housing Development Finance Corporation were established in 2004.

[10] During the first nine months of 2005, commercial banks' private sector lending in foreign currency increased by $94 million, 80 percent of private credit growth.

12. **More generally, monetary policy has been passive with the MMA automatically financing the fiscal deficit.** The authorities introduced tap sales of MMA CDs in 1995, liberalized interest rates (except for a 20 percent ceiling on lending rates) in 2001, and lowered the minimum reserve requirement (MRR) from 35 percent to 30 percent in 2003 in line with Fund advice. They are now preparing for the introduction of indirect monetary management. But these steps have not led to proactive policy implementation. The MMA has continued its automatic financing of the fiscal deficit; the MRR has remained at 30 percent; and tap sales of MMA CDs continue with a fixed interest rate of 4 percent regardless of the level of market liquidity. Commercial bank interest rates have also remained broadly unchanged since mid-2002 reflecting limited competition and underdeveloped links with external markets. The amended MMA Act (drafted in 2003) to make the central bank independent of the government and set limits to government borrowing was recently withdrawn from the parliament for further revision.[11]



13. **Commercial bank borrowing from abroad helped reduce the balance of payments gap.** With a $160 million decline in tourism receipts and high oil import prices, the current account deficit for 2005 is estimated to have been a record high $300 million (37 percent of GDP). But commercial banks' borrowing from foreign headquarters, primarily to finance reconstruction, covered a large portion of total import needs, and the reserve loss was limited to about $20 million (Table 2). Official reserves at end-2005 amounted to $187 million (2½ months of imports).



14. **The pace of structural reforms has lagged.** The authorities have embarked on several structural reform initiatives—fiscal, SOE, and financial sector reforms—to create a business environment conducive to private investment and to support diversified growth. Progress has, however, been slow due in part to limited implementation capacity, and more recently to the tsunami disaster (Box 2). In the fiscal area, the Business Profit Tax (BPT) Act is yet to be enacted despite lengthy parliamentary debate, and preparations for the introduction of the sales tax and a medium–term expenditure framework (MTEF) did not progress last year. On privatization, past efforts notwithstanding, SOEs continue to operate

[11] The Minister of Finance and Treasury is also Governor of the MMA.

Box 2: Structural Reform Agenda and Status

The authorities' major structural reform agenda comprise the following.

- **Fiscal Reforms.** Revenues are to be enhanced through introduction of a BPT and a sales tax, and by improved customs administration. The BPT Act is being debated in the parliament. Collection of about 3 percent of GDP is to start by 2008 although the mission recommended earlier implementation. The authorities also intend to prepare a broad-based sales tax to replace a large portion of import duties, but its timetable remains unclear. The Customs Administration Act, also in the parliament, will establish sound customs procedures. On expenditures, the MTEF, prepared with World Bank/AsDB assistance, should set multiyear resource envelopes based on realistic revenue projections and ensure that expenditure decisions will be guided by strategic goals. The authorities intend to introduce the MTEF in 2010 and have taken few concrete actions lately. The Public Finance Act was enacted in December without the provision for limiting government access to MMA borrowing.

- **Civil Service.** A parliamentarian submitted the Public Service Bill (approval expected mid-2006). The bill will create a civil service commission which determines civil service size and salaries and recruits civil servants. In addition, a pension reform is considered with World Bank assistance although no concrete action has been taken so far.

- **Public Enterprises.** No firm has been privatized since 2001 due in part to a concern over its perceived negative revenue impact. The government plans to sell shares of Allied Insurance, Housing Development and Finance Corporation, and Water and Sewerage Company in 2006, and gradually proceed with further privatization/corporatization. The preparation of a Public Enterprise Act has been delayed due to disagreements over whether line ministries or the finance ministry should control SOEs.

- **The Financial Sector.** On-site examinations of three major banks have been completed with MFD assistance. Efforts to make the MMA independent of the government continue, but the amendment to the MMA Act (drafted in late 2003) was temporarily withdrawn from the parliament for revision due to disagreements on the role of government officials on the MMA's Board. The Banking and Securities Acts were drafted in early 2005 and will be submitted to the parliament in 2006. Insurance legislations are also under preparation.

- **Foreign Trade.** The Export and Import Act assigns control of rates/coverage to Finance Ministry while Trade Ministry is to retain regulatory power. The Act also will remove duty waivers on imports related to resort construction and fisheries. To stimulate regional trade, South Asian Free Trade Agreement (SAFTA) rules of origin have been lowered to 40 percent value addition with further 10 percent derogation for lower income members. Lower-income SAFTA members including the Maldives are to reduce tariffs to 0–5 percent in 10 years.

in key areas that in most countries are left to the private sector (for example, tourism, trade, insurance, and communications). A number of key legislations (including acts on public enterprises, banking, securities, and customs administration in addition to the amendment of the MMA Act) are at different stages of preparation—but progress has generally been slow.

III. Policy Discussions

15. Discussions focused on: steps to address the large fiscal deficit that emerged after the tsunami; monetary policy reforms towards an indirect management system; and the medium term outlook and structural reforms that could help sustain robust and broad-based growth.

A. Macroeconomic Policies for 2006

Fiscal policy

16. The mission underlined the need to restore fiscal discipline in 2006, with a view to limiting domestic financing to less than 3 percent of GDP. At the time of the mission, the authorities broadly agreed and expressed their intention to strengthen revenues while lowering spending significantly. On the revenue side, they intended to implement the measures originally proposed in the 2005 budget and also to largely eliminate import duty exemptions. They also expected higher resort lease payments due both to increases in lease rates and advance lease payments expected from winners of tenders of five new resort islands.[12] On expenditures, the government intended to limit domestic spending to the original 2005 budget level except for the following two adjustments: (i) an increase in the wage bill due to internal promotions and new recruits mostly in education, health, police, and national security (amounting to 3 percent of GDP); and (ii) elimination of power, water, and food subsidies (saving 2 percent of GDP). If these intentions were implemented, the domestic financing requirement could be slightly less than 3 percent of GDP.

17. **In the event, the government adopted a 2006 budget that includes significantly higher spending.** While details of this increase (about 7 percent of GDP) are not yet available, it appears to include an even higher wage bill and additional health and education spending that is not tsunami related. Allocations for domestic investment projects, not donor-funded, have also increased significantly.[13] In addition, there is a significant risk to

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[12] While the Ministry of Finance initially indicated that 40–50 islands could be tendered for lease next year, there was agreement during the mission that a prudent level to assume would be at most five resorts considering that the tender process has in the past often been protracted. See, however, Paragraph 18.

[13] Almost all tsunami recovery activities are expected to be donor-funded, and government contributions included in the budget amount to about 1 percent of GDP.

the budget as it does not provide for a subsidy to a main power company, which would require tariff increases that are not decided.[14]

2006 Fiscal Developments (In millions of rufiyaa)			
	Art IV Discussion	Government Budget	Staff Estimate
Total revenue & grants	5,998	6,549	6,101
Tax revenue	2,129	2,115	2,115
Import duties	1,520	1,519	1,519
Tourism tax	446	428	428
Nontax revenue	2,020	2,707	2,259
SOE transfers	409	630	630
Resort lease and land rent	796	1,329	881
Others	814	748	748
Grants	1,892	1,695	1,695
Expenditure and net lending	8,069	8,645	8,645
Current expenditure	4,431	4,993	4,993
Capital expenditure	3,698	3,716	3,716
Overall Balance	-2,071	-2,096	-2,544
(In percent of GDP)	(-17.1)	(-17.4)	(-21.3)
Financing	2,071	2,096	2,544
Domestic financing	343	337	1,169
Foreign financing	1,470	1,119	1,119
Budget support requirement	258	640	256

Source: Ministry of Finance and Treasury.

18. **Proposed measures to finance this higher spending appear unrealistic and large domestic borrowing may emerge, threatening macroeconomic stability**. The higher spending is to be funded largely by advance lease payments (amounting to 4½ percent of GDP) paid by winners of tenders of 35 new resort islands along with additional budget support from bilateral donors (3 percent of GDP). However, given experience to date, it is considered difficult to complete 35 island tenders and collect advance lease payments within one year. Assumed donor support also appears optimistic.[15] With shortfalls likely in both revenue and foreign financing, government borrowing from the MMA could exceed 9 percent of GDP. This level of MMA borrowing, following a similar amount in 2005, could precipitate significant inflationary pressure and/or losses in foreign reserves. The authorities recognize the risks associated with this budget and are designing contingency remedial measures (primarily identifying expenditures that could be cut or delayed). These measures, if announced in time, will be reported to Executive Directors through a staff supplement.

19. **The mission stressed the importance of improving fiscal management by enhancing revenues and prioritizing spending through introduction of the MTEF and civil service reforms.** On enhancing revenues, the mission welcomed the authorities' plan to introduce a BPT in 2008 and prepare a sales tax for subsequent implementation. Given

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[14] The budget also includes improvements in fiscal management. Spending that was previously outside the budget (amounting to about Rf 200 million) has now been included, enhancing transparency.

[15] The authorities assume that budget support is forthcoming from some bilateral donors, the World Bank, and the AsDB. But bilateral support is still under discussion and IFI support would likely depend on the extent to which the authorities can conduct fiscal policy in a sustainable manner.

the current fiscal difficulties, the mission stressed that it would be desirable to accelerate implementation of this plan and also to adjust the specific tourist "bed" tax more frequently with a view to turning it into an ad valorem tax. On the expenditure side, an early introduction of the MTEF for capital spending—prioritizing projects according to agreed criteria such as cost-benefit calculations—would likely improve expenditure management significantly. Similarly, there is a need to limit general administration expenses and streamline the public service through implementing civil service reforms—civil servants are 10 percent of the population and their wage bill is 20 percent of GDP. Expeditious enactment of the Public Finance Act and the Audit Act designed to improve public sector management is also important.

20. **The authorities reaffirmed their commitment to improved fiscal management but thought careful preparation was needed.** The authorities stated that most of the measures suggested by staff were already elements of their reform strategy, but did not commit to accelerated implementation stressing the need for careful preparation. On civil service reforms, the authorities had no specific plan, but pointed out that a parliamentarian had tabled a Public Service Act that would establish a civil service commission. The mission urged the authorities to be more proactive and request donors' technical assistance for designing reforms that could enhance civil service effectiveness while containing its cost. Finally, the Public Finance Act was approved at the end of December. While this is welcome, the Act does not include the long-awaited provision for limiting government access to MMA borrowing. The authorities indicated that their plan now was to include the provision in an amended MMA Act.

Exchange rate regime

21. **The dollar peg continues to be an appropriate exchange rate arrangement**. The mission agreed with the authorities that the peg had reduced transaction costs and exchange rate risks, provided a transparent nominal anchor, and had been consistent with constrained institutional capacity to manage a foreign exchange market. Based on the movements of the real effective exchange rate and the strong recovery of tourism witnessed toward the end of 2005, the level of the exchange rate appears generally appropriate despite near double-digit inflation seen earlier in the year and concerns about possible foreign exchange shortages expressed by the business community. These concerns were dissipated with the strong recovery of tourist arrivals during the last quarter of the year, and there is no parallel market. If, however, the expansionary fiscal stance implied in the 2006 budget were to be sustained, inflationary pressures would likely mount and the peg rate could ultimately be jeopardized.

Monetary and banking sector policy

22. **Automatic financing of fiscal deficits by the MMA should cease and monetary policy needs to focus on supporting the exchange rate peg.** Important elements of such a strategy would be:

- Expediting the adoption of the amended MMA Act which makes the monetary authority independent and sets legal limits to the government's domestic borrowing (as the Public Finance Act excludes this provision).

- Reducing the reserve requirement further to improve intermediation, continuing with development of a liquidity forecasting framework, auctioning MMA CDs, and eventually replacing the CDs with treasury bills.

- MMA could in the meantime consider an adjustment of CD rates to absorb liquidity created by the government's high domestic borrowing.

The authorities intend to implement these actions (with ongoing MFD technical assistance) although proceeding cautiously with regard to starting CD auctions or raising CD rates because of concerns about the impact of high interest rates on the weak economy.

23. **Turning to the banking sector, the mission welcomed progress made in supervision.** The MMA has continued on- and off-site inspections of commercial banks on a regular basis focused on improving risk management practices in these banks. These inspections have facilitated a decline and restructuring in nonperforming loans (NPLs).[16] Even then, as commercial banks in the Maldives tend to have high concentration risk and increasing net open foreign exchange positions, the MMA should closely monitor developments. The authorities requested continued MFD technical assistance in this effort.

B. Medium-Term Outlook and Structural Reforms

24. **A medium-term strategy in line with the stance adopted in the 2006 budget—with limited reform—would carry serious risks.** The budget, announced after the mission's departure from Male, is based on higher spending and more optimistic revenue levels than discussed during the mission. Table 5 presents a scenario that illustrates the possible outcome of such a policy approach. With revenues weaker than envisaged, official reserves would likely decline steadily implying the need for strong corrective actions down the road.

25. **Achieving sustainable growth over the medium term remains a challenge even with prudent fiscal management and structural reform implementation**. Discussions during the mission focused on an alternative medium-term scenario in which real GDP growth stabilizes at around 5 percent after a rebound in 2006 (Table 6). The mission stressed that achieving such an outcome in an environment of declining foreign aid would require prudent fiscal management and vigorous pursuit of structural reforms. To limit

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[16] NPLs average less than 4 percent of loan portfolio for three of the four commercial banks. One bank has an 18 percent NPL ratio but satisfactory measures have been taken to address them.

domestic borrowing to a sustainable level, a large fiscal adjustment would appear necessary—revenues need to be raised by 4–5 percentage points of GDP in five years and domestic recurrent spending lowered also by 4–5 percent. This would allow growth with low inflation while strong revenue efforts would allow current spending to be maintained at a level higher than before the tsunami. However, even with the large fiscal adjustment assumed in this scenario, official reserves are projected to increase minimally due largely to declining foreign aid and the need to amortize ongoing foreign borrowing by commercial banks.

26. **The authorities agreed that structural reforms must be pursued vigorously** in part to realize the private capital inflows assumed in the projection. Key reforms include public enterprise reforms and development of a sound economic and financial legal framework.

- **Renewed efforts are needed to privatize or corporatize public enterprises.** The mission welcomed the authorities' plan to sell shares of three SOEs in 2006 and urged the authorities to consider full privatization of entities directly competing with the private sector while completing corporatization of remaining SOEs. The authorities indicated that they would like to coordinate privatization exercises with introduction of a BPT to minimize possible revenue loss associated with privatization.

- **On economic and financial legislation, the authorities believe that significant progress can be made in 2006**. Following delays due in part to the impact of the tsunami, they were ready to accelerate efforts in this area.

27. **Debt sustainability would also be threatened by the expansionary fiscal stance of the newly approved budget**. The Maldives' external debt has increased to about 60 percent of GDP from 42 percent in 2004 as aid for tsunami recovery came partly in the form of loans and as foreign-owned commercial banks borrowed significantly from their overseas headquarters. A scenario based on the newly announced 2006 budget (Table 5) raises the fiscal debt-to-GDP ratio—and erode foreign reserves in the external analysis—to such levels that would likely call for abrupt corrective actions in the coming years (Tables 8 and 9). Sensitivity analyses indicate that the economy's debt burden may increase even further in the event additional exogenous or policy induced shocks occur. A debt sustainability analyses—based on a prudent policy approach (Table 6) indicate that the debt-to-GDP ratio could stabilize over the medium term (Tables 10 and 11).

C. Other Issues

28. **The mission discussed prospective changes in import tariffs.** Under the SAFTA, signed in early 2004, agreements have been reached on rules of origin, sensitive product lists, and compensation for revenue losses of LDC members. LDC members, including the Maldives, have 10 years to reduce tariff rates to 0–5 percent. While the authorities have not made concrete plans for tariff reductions, they agreed with the mission that they would need to be phased in taking into account the pace of tax reforms, in particular introduction of a

broad-based sales tax, to minimize revenue losses. In this connection, the staff stressed the importance of reducing tariffs on a most favored nation basis to limit trade diversion. Finally, garment exports were decimated due to the expiry of the multi-fiber agreement, but the impact on the economy and the current account was limited since these exports were based on imported inputs (including labor) and the value added was marginal.

29. **The authorities are implementing initiatives on anti-money laundering and combating financing terrorism.** The MMA has set up a financial intelligence unit and received LEG/MFD TA to develop comprehensive AML/CFT legislative, institutional, and supervisory frameworks. The legislation is currently being reviewed by the Law Commission and expected to be presented to the parliament during 2006. The authorities reiterated their commitment to implementing the recommendations of LEG and MFD.

30. **Further improvement in the collection and dissemination of statistics is needed.** The authorities have requested assistance from the Fund in the areas of balance of payments and government finance data in addition to the ongoing assistance in monetary statistics. The authorities are also to seek assistance from other agencies to improve their national accounts.

31. **The exchange system remains free of restrictions on the making of payments and transfers for current international transactions**. The authorities would like to wait one or two more years until the disruption due to the tsunami was fully behind them before considering acceptance of the obligations of Article VIII, Sections 2, 3, and 4.

IV. Staff Appraisal

32. **The December 2004 tsunami revealed the Maldives' vulnerability to external shocks.** The tsunami has shown that adverse shocks affecting tourism have serious implications for the economy given its dependence on the sector. To reduce vulnerability, fiscal and monetary reforms are needed to enhance the authorities' capacity to conduct timely demand management along with structural reforms to expand private sector activities and enhance the supply side resilience—although the scope of rapid diversification appears limited.

33. **Reconstruction work has progressed slowly but commendable efforts have recently been made to accelerate the pace.** Implementation of recovery projects was slow in 2005 due to problems in local consultation, limited capacity, and insufficient coordination. The government and donors have been addressing these problems and the pace of implementation is accelerating. These efforts need to be sustained vigorously and additional donor commitments are required to finance the necessary recovery work.

34. **The fiscal stance adopted in the 2006 budget jeopardizes stability and corrective measures are needed.** The government raised spending in the budget to a level much above what had been previously envisaged on the back of optimistic revenue and foreign financing assumptions. As a result, a high domestic borrowing requirement to the

tune of 9 percent of GDP could arise, which in turn could place significant pressures on inflation, official reserves, and (ultimately) the peg. The government needs to renew its commitment to fiscal viability by resisting demands for higher wages, recruitment, and other spending initiatives that appear to have become intense against the backdrop of ongoing political reforms.

35. **To enhance the economy's resilience over the medium term, further fiscal reforms are imperative.** The tsunami and its aftermath have shown that the room for maneuver on the fiscal front to correct macroeconomic imbalances is limited because of rigid revenue and expenditure structures. Revenue and its buoyancy should be increased through introduction of corporate taxation and broad based sales tax, and expenditure management improved—to contain total spending in line with realistic revenue projections and prioritize spending to protect high priority activities. There is scope for containing general administration costs, the wage bill, and domestic capital spending. Civil service reforms should also be high on the agenda.

36. **The peg arrangement has served the Maldives well as a credible nominal anchor and should be continued**. The arrangement is justified by the economy's openness and small size and its constrained institutional capacity and needs to be safeguarded by an appropriate macroeconomic and structural policy mix. The current level of the exchange seems broadly appropriate—given the strong tourism recovery witnessed in the recent past and absence of a parallel foreign exchange market—assuming prudent macroeconomic policy in the period ahead.

37. **Monetary policy should be geared to sustaining the peg arrangement.** Large fiscal deficits and their automatic financing by the MMA undermine the exchange rate peg and should cease. Early enactment of the MMA amendment is crucial, making the institution more independent and setting legal limits to the government's MMA borrowing.

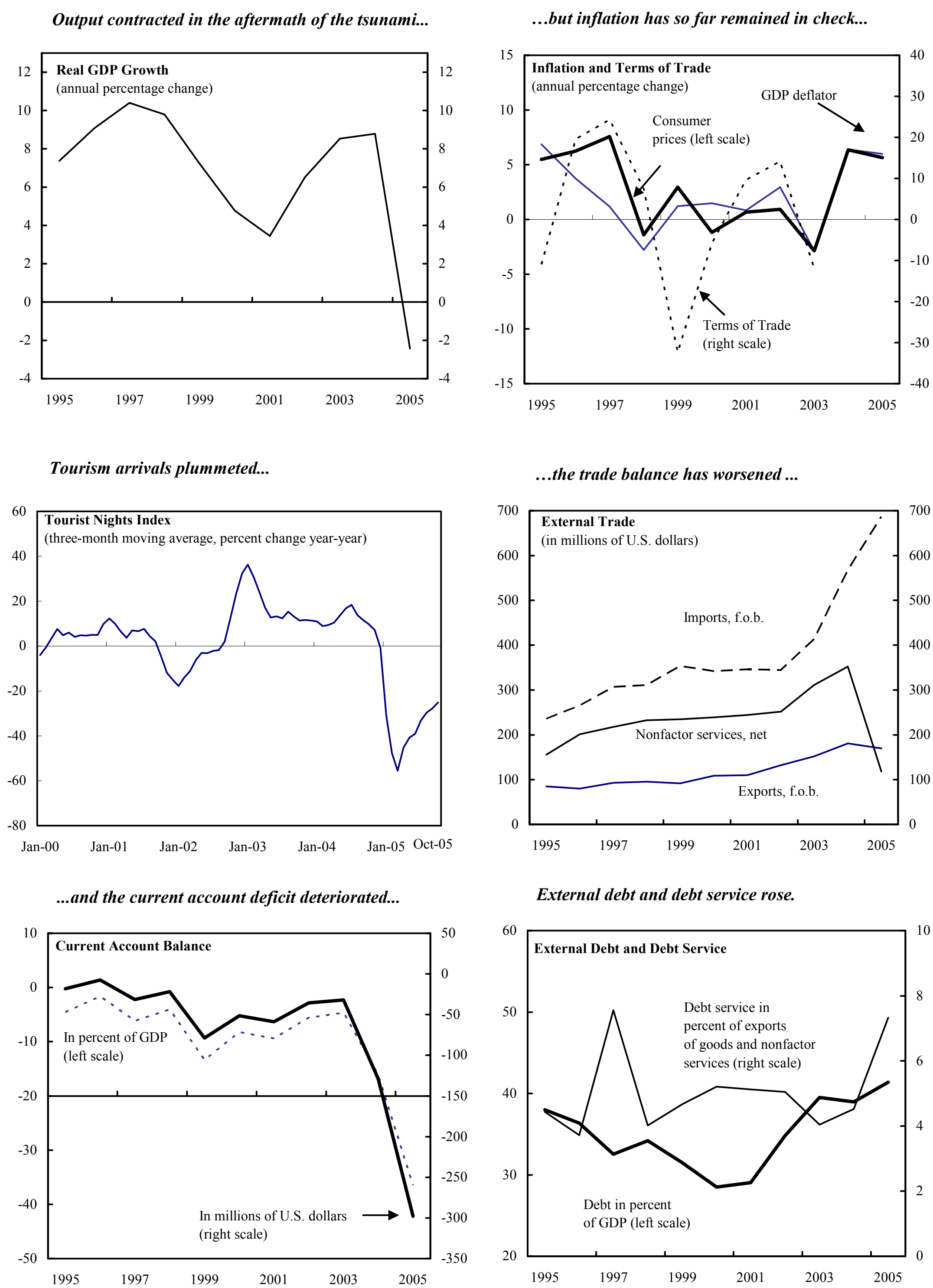
38. **The authorities' efforts to introduce indirect monetary management and improve banking supervision are commendable.** Progress has been made in preparing for introduction of a more market-oriented monetary policy—once the MMA ends its automatic financing of the deficit. The next steps include reducing reserve requirements and introducing auctions of MMA certificate of deposits or treasury bills to tap domestic savings and absorb liquidity. The MMA's supervision of commercial banks has also been strengthened, leading to a reduction in NPLs.

39. **Over the medium term, structural reforms are indispensable for sustaining robust growth and reducing the economy's vulnerability**. The economy, dominated by the public sector and dependent on tourism, remains vulnerable, and achieving medium-term viability remains a challenge. Reforms are needed to create a business environment conducive to broad-based private investment. Priority actions include privatization of SOEs and implementation of key economic and financial legislation such as the BPT Act, the amended MMA Act, the Banking Act, the Audit Act, and the Public Enterprises Act.

40. **While some progress has been made, economic analysis continues to be impeded by problems in availability, timeliness, and consistencies in certain economic data**. Data provision is not fully adequate for surveillance purposes as data on government finances and balance of payments (especially capital flows) are not available in a timely manner and are subject to frequent revisions. Furthermore, improvements are needed in the national accounts data.

41. It is recommended that the next Article IV consultation with the Maldives take place on a standard 12-month cycle.

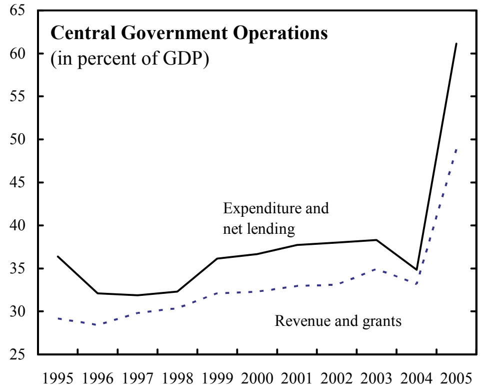
Figure 1. Maldives: Real and External Sector Developments, 1995-2005



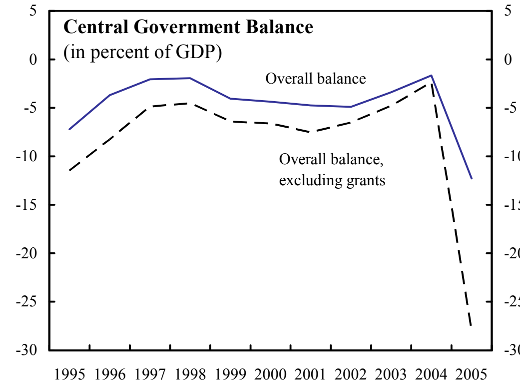
Sources: Maldivian authorities; and IMF staff estimates.

Figure 2. Maldives: Fiscal and Monetary Sector Developments, 1995-2005

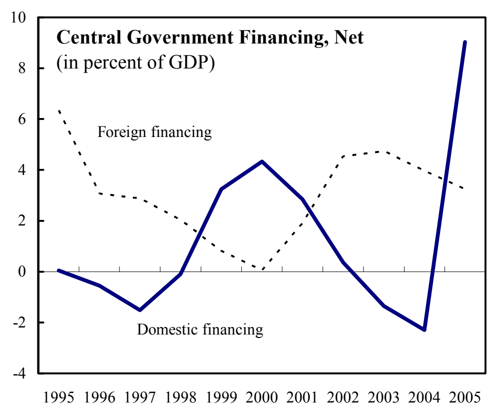
With expenditures growing faster than revenues...



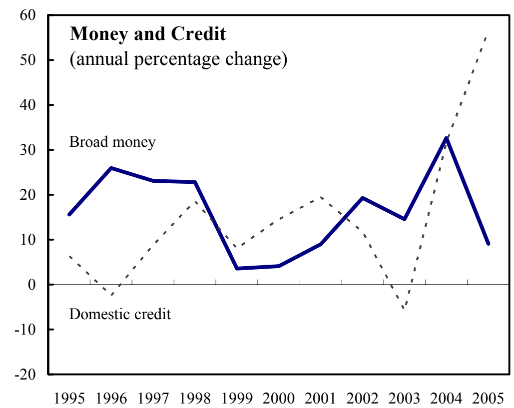
…overall balance plunged deep into negative territory...



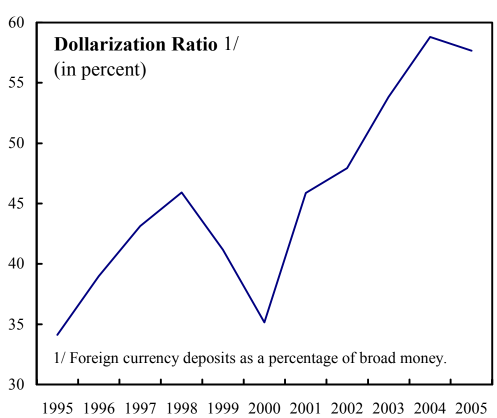
…and domestic financing of the deficit swelled.



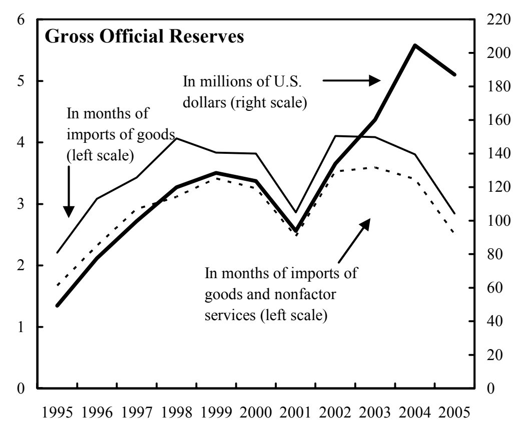
Broad money remained constant as falling net foreign assets offset rising net domestic assets.



Dollarization increased...



…and a loss of foreign reserves.



Sources: Maldivian authorities; and IMF staff estimates.

Table 1. Maldives: Selected Economic Indicators, 2001–06

Population (2004):	299,520
Nominal GDP (in millions of U.S. dollars, 2004):	799.6
GDP per capita (in U.S. dollars, 2004):	2,670
Quota (in millions of SDRs):	8.2

				Est.	Proj.	
	2001	2002	2003	2004	2005	2006
			(Annual percentage change)			
Growth and prices						
Real GDP	3.5	6.5	8.5	8.8	-3.6	8.0
Consumer prices (period average)	0.7	0.9	-2.9	6.4	5.7	7.0
Consumer prices (end period)	...	-5.0	-1.5	10.1	5.0	5.0
			(Percent of GDP)			
Central government						
Revenue and grants	33.0	33.1	34.9	33.2	48.8	51.1
Of which: Grants	2.8	1.6	1.4	0.7	15.7	14.2
Expenditure and net lending	37.7	38.0	38.3	34.8	61.1	72.3
Of which: Capital spending	12.3	12.5	13.6	10.7	22.3	31.1
Overall balance	-4.7	-4.9	-3.4	-1.7	-12.3	-21.3
Overall balance, excluding grants	-7.5	-6.5	-4.8	-2.4	-27.9	-31.7
Financing						
Domestic	2.8	0.4	-1.3	-2.3	9.0	9.8
Foreign	1.9	4.5	4.7	4.0	3.2	9.4
Additional financing requirement	…	…	…	…	…	2.1
			(Annual percentage change)			
Money and credit						
Domestic credit	18.2	11.9	-6.0	33.1	55.5	26.9
Public sector	4.4	6.8	-26.5	-23.2	109.4	72.8
Central government (net)	5.2	5.4	-20.7	-43.0	118.1	99.1
Private sector	29.9	15.3	6.8	57.3	44.3	12.9
Broad money	8.0	19.5	14.5	32.8	9.1	20.2
			(In millions of U.S. dollars)			
Balance of payments						
Exports, including reexports	110.1	132.3	151.9	181.0	169.6	182.8
Imports	-346.3	-344.7	-414.3	-567.3	-686.8	-811.9
Nonfactor services (net)	244.2	251.7	311.1	352.4	118.1	198.1
Current account balance	-58.8	-35.7	-31.9	-128.9	-297.9	-359.0
(In percent of GDP)	-9.4	-5.6	-4.6	-16.1	-36.5	-38.5
Official capital (net)	7.8	26.8	34.4	26.0	26.5	114.9
Private capital (net)	24.3	33.9	56.8	125.3	135.0	156.0
Errors and omissions (net)	5.2	14.9	15.5	35.3	0.0	0.0
Overall balance	-21.4	39.8	74.3	57.7	-136.4	-88.2
Financing						
Change in MMA reserves	29.7	-40.2	-26.5	-44.0	17.2	23.2
Change in commercial banks' NFA	-8.3	0.4	-47.8	-14.8	113.0	45.0
Additional external financing requirement	…	…	…	…	…	20.0
Gross official reserves (year-end)	93.8	134.0	160.3	204.4	187.2	164.0
(In months of imports of GNFS) 1/	2.5	3.5	3.6	3.4	2.5	1.9
External debt 2/						
(In millions of U.S. dollars)	209.8	259.0	289.5	331.8	481.6	657.6
(In percent of GDP)	33.6	40.4	41.9	41.5	58.9	70.4
Of which: Public	29.0	34.8	39.5	39.0	41.4	48.5
Debt service	22.0	22.9	22.0	28.4	32.2	34.8
(In percent of domestic exports of GNFS) 3/	5.1	5.0	4.0	4.5	7.3	6.3
Exchange rate						
Rufiyaa per U.S. dollar (period average)	12.2	12.8	12.8	12.8	12.8	12.8
Memorandum item:						
Nominal GDP (in millions of rufiyaa)	7,650.8	8,201.0	8,842.0	10,235.1	10,457.9	11,949.7

Sources: Data provided by the Maldivian authorities; and IMF staff estimates and projections.
1/ GNFS = Goods and nonfactor services.
2/ Includes additional external financing, assuming equal proportions of grants and loans.
3/ Domestic exports are defined as merchandise exports net of reexports.

Table 2. Maldives: Balance of Payments, 2001–06

	2001	2002	2003	2004	2005	2006
	(In millions of U.S. dollars)					
Current account balance	-58.8	-35.7	-31.9	-128.9	-297.9	-359.0
Trade balance	-236.1	-212.4	-262.4	-386.3	-517.2	-629.2
Exports, f.o.b (including reexports)	110.1	132.3	151.9	181.0	169.6	182.8
Imports, f.o.b	-346.3	-344.7	-414.3	-567.3	-686.8	-811.9
Services (net)	207.0	216.3	272.7	311.6	90.4	162.4
Balance on nonfactor services	244.2	251.7	311.1	352.4	118.1	198.1
Receipts	354.1	362.9	432.1	505.2	326.1	437.2
Of which: Tourism receipts	327.1	337.1	401.6	470.9	269.1	360.8
Payments	-109.8	-111.1	-121.0	-152.9	-207.9	-239.1
Balance on factor services	-37.2	-35.4	-38.4	-40.8	-27.7	-35.7
Receipts	8.2	5.6	6.2	10.3	11.3	12.3
Payments	-45.4	-41.1	-44.6	-51.1	-39.0	-48.0
Unrequited transfers (net)	-29.7	-39.6	-42.3	-54.2	128.9	107.8
Official	19.9	10.6	12.7	6.9	127.9	147.8
Private	-49.6	-50.2	-54.9	-61.1	1.0	-40.0
Nonmonetary capital (net)	37.3	75.5	106.7	186.6	161.5	270.9
Official medium- and long-term	7.8	26.8	34.4	26.0	26.5	114.9
Disbursements	23.4	43.5	51.1	47.6	50.5	139.6
Amortization	-15.6	-16.7	-16.7	-21.6	-23.9	-24.7
Private capital	24.3	33.9	56.8	125.3	135.0	156.0
Net errors and omissions	5.2	14.9	15.5	35.3	0.0	0.0
Overall balance	-21.4	39.8	74.3	57.7	-136.4	-88.2
Monetary movements	21.4	-39.8	-74.3	-58.8	136.4	88.2
Maldives Monetary Authority	29.7	-40.2	-26.5	-44.0	17.2	23.2
Commercial banks	-8.3	0.4	-47.8	-14.8	113.0	45.0
Borrowing from the IMF					6.2	0.0
Additional external financing requirement	…	…	…	…	…	20.0
Memorandum items:						
Domestic export growth (value, in percent) 1/	0.3	18.7	24.4	8.8	-7.7	4.7
Import growth (value, in percent)	1.3	-0.4	20.2	36.9	21.1	18.2
Tourism receipts growth (in percent)	2.0	3.0	19.1	17.3	-42.9	34.1
Current account balance (in percent of GDP)	-9.4	-5.6	-4.6	-16.1	-36.5	-38.5
Gross official reserves (in millions of U.S. dollars)	93.8	134.0	160.3	204.4	187.2	164.0
(In months of imports of GNFS) 2/	2.5	3.5	3.6	3.4	2.5	1.9
External debt (in millions of U.S. dollars) 3/	209.8	259.0	289.5	331.8	481.6	657.6
External debt (in percent of GDP) 3/	33.6	40.4	41.9	41.5	58.9	70.4
Debt service (in millions of U.S. dollars)	22.0	22.9	22.0	28.4	32.2	34.8
Debt service (in percent of domestic exports of GNFS) 1/	5.1	5.0	4.0	4.5	7.3	6.3
Exchange rate (rufiyaa per U.S. dollar, average)	12.2	12.8	12.8	12.8	12.8	12.8
GDP (in millions of U.S. dollars)	625.0	640.7	690.8	799.6	817.0	933.6

Sources: Data provided by the Maldivian authorities; and IMF staff estimates and projections.

1/ Domestic exports are defined as merchandise exports net of reexports.
2/ GNFS = Goods and nonfactor services.
3/ Includes additional external financing, assuming equal proportions of grants and loans.

Table 3. Maldives: Central Government Finance, 2001–06

	2001	2002	2003	2004	Proj. 2005	Proj. 2006
			(In millions of rufiyaa)			
Total revenue and grants	2,522.6	2,714.9	3,087.9	3,395.2	5,107.6	6,100.7
Total revenue	2,310.9	2,582.4	2,964.3	3,320.7	3,470.5	4,405.4
Current revenue	2,294.3	2,577.9	2,936.8	3,302.4	3,442.2	4,373.7
Tax revenue	1,046.6	1,091.7	1,268.7	1,638.1	1,598.4	2,114.9
Import duties	661.7	692.1	817.1	1,126.7	1,133.4	1,519.2
Tourism	292.7	305.2	359.8	412.2	336.2	427.8
Other	92.2	94.4	91.8	99.2	128.8	167.9
Nontax revenue	1,247.7	1,486.2	1,668.1	1,664.3	1,843.8	2,258.8
SOE profit transfers	383.7	422.6	570.6	545.1	646.5	629.6
Resort lease payments	433.1	601.0	575.7	553.6	616.0	881.0
Other	430.9	462.6	521.8	565.6	581.3	748.2
Capital revenue	16.6	4.5	27.5	18.3	28.3	31.7
Grants	211.7	132.5	123.6	74.5	1,637.1	1,695.3
Expenditure and net lending	2,885.9	3,117.3	3,388.2	3,565.3	6,391.6	8,644.7
Current expenditure	1,971.4	2,109.4	2,345.7	2,657.9	4,120.4	4,993.4
Capital expenditure	940.7	1,026.1	1,206.2	1,100.2	2,335.5	3,716.4
Net lending	-26.2	-18.2	-163.7	-192.8	-64.3	-65.1
Overall balance	-363.3	-402.4	-300.3	-170.1	-1,283.9	-2,544.0
Overall balance, excluding grants	-575.0	-534.9	-423.9	-244.6	-2,921.1	-3,791.3
Current balance	322.9	468.5	591.1	644.5	-678.2	-171.7
Domestic financing	217.5	30.0	-118.9	-235.3	944.7	1,168.9
Foreign financing	145.8	372.4	419.2	405.4	339.2	1,119.1
Additional external financing requirement	…	…	…	…	…	256.0
Government debt (end of period)	3,326.4	3,856.9	4,157.2	4,327.3	5,611.2	8,155.2
Of which: Foreign	1,831.3	2,203.7	2,622.9	3,028.3	3,367.5	4,742.6
			(In percent of GDP)			
Total revenue and grants	33.0	33.1	34.9	33.2	48.8	51.1
Current revenue	30.0	31.4	33.2	32.3	32.9	36.6
Tax revenue	13.7	13.3	14.3	16.0	15.3	17.7
Import duties	8.6	8.4	9.2	11.0	10.8	12.7
Tourism	3.8	3.7	4.1	4.0	3.2	3.6
Other	1.2	1.2	1.0	1.0	1.2	1.4
Nontax revenue	16.3	18.1	18.9	16.3	17.6	18.9
SOE profit transfers	5.0	5.2	6.5	5.3	6.2	5.3
Resort lease payments	5.7	7.3	6.5	5.4	5.9	7.4
Other	5.6	5.6	5.9	5.5	5.6	6.3
Capital revenue	0.2	0.1	0.3	0.2	0.3	0.3
Grants	2.8	1.6	1.4	0.7	15.7	14.2
Expenditure and net lending	37.7	38.0	38.3	34.8	61.1	72.3
Current expenditure	25.8	25.7	26.5	26.0	39.4	41.8
Capital expenditure	12.3	12.5	13.6	10.7	22.3	31.1
Net lending	-0.3	-0.2	-1.9	-1.9	-0.6	-0.5
Overall balance	-4.7	-4.9	-3.4	-1.7	-12.3	-21.3
Overall balance, excluding grants	-7.5	-6.5	-4.8	-2.4	-27.9	-31.7
Current balance	4.2	5.7	6.7	6.3	-6.5	-1.4
Domestic financing	2.8	0.4	-1.3	-2.3	9.0	9.8
Foreign financing	1.9	4.5	4.7	4.0	3.2	9.4
Additional external financing requirement	...	...	...	...	...	2.1
Government debt (end of period)	43.5	47.0	47.0	42.3	53.7	68.2
Of which: Foreign	23.9	26.9	29.7	29.6	32.2	39.7
Of which: Domestic	19.5	20.2	17.4	12.7	21.5	28.6
Memorandum items:						
Exchange rate (rufiyaa per U.S. dollar, average)	12.2	12.8	12.8	12.8	12.8	12.8
Nominal GDP (in millions of rufiyaa)	7,650.8	8,201.0	8,842.0	10,235.1	10,457.9	11,949.7

Sources: Data provided by the Maldivian authorities; and IMF staff estimates and projections.

Table 4. Maldives: Summary of Monetary Accounts and MMA Balance Sheet, 2001–05

	Dec.				Proj.
	2001	2002	2003	2004	2005
	(In millions of rufiyaa)				
Monetary survey					
Broad money	3,293.2	3,936.0	4,507.5	5,983.7	6528.1
Net foreign assets	1,172.7	1,676.6	2,646.5	3,379.4	1,689.4
Monetary authorities (net)	1,191.1	1,704.9	2,041.2	2,614.6	2,383.8
Foreign assets	1,201.2	1,715.1	2,051.4	2,625.6	2,475.2
Foreign liabilities	-10.2	-10.2	-10.2	-11.0	-91.4
Domestic credit	3,058.4	3,421.7	3,216.8	4,282.8	6,661.2
Public sector	1,231.1	1,314.5	965.9	741.5	1,552.5
Central government (net)	1,047.1	1,103.5	875.6	499.5	1,089.5
Other	2,011.3	2,318.2	2,341.2	3,783.3	5,571.7
Public enterprises	184.0	211.0	90.4	242.0	463.0
Private sector	1,827.2	2,107.2	2,250.8	3,541.3	5,108.7
Other items (net)	-937.9	-1,162.3	-1,355.8	-1,622.6	-1,822.6
	(Annual percentage change)				
Broad money	8.0	19.5	14.5	32.8	9.1
Net foreign assets	-10.6	43.0	57.9	27.7	-50.0
Domestic credit	18.2	11.9	-6.0	33.1	55.5
Public sector	4.4	6.8	-26.5	-23.2	109.4
Central government (net)	5.2	5.4	-20.7	-43.0	118.1
Other	26.4	15.3	1.0	61.6	47.3
Public enterprises	-0.4	14.7	-57.2	167.8	91.3
Private sector	29.9	15.3	6.8	57.3	44.3
Memorandum items:					
GDP (in millions of rufiyaa)	7,650.8	8,201.0	8,842.0	10,235.1	10,457.9
Rufiyaa per U.S. dollar	12.8	12.8	12.8	12.8	12.8
Velocity	2.3	2.2	2.1	1.8	1.7
Official reserves (US$ million)	93.8	134.0	160.3	204.4	187.2
Commercial banks' NFA (US$ million)	-1.4	-2.2	47.3	58.8	-54.2

Sources: Data provided by the Maldivian authorities; and IMF staff estimates.

Table 5. Maldives: Base Case Medium-Term Scenario, 2004–10

		Proj. 1/					
	2004	2005	2006	2007	2008	2009	2010
	(Annual percentage change)						
Output and prices							
Real GDP growth	8.8	-3.6	8.0	4.0	3.0	3.0	3.0
Consumer prices (period average)	6.4	5.7	7.0	6.0	6.0	6.0	6.0
	(In percent of GDP)						
Central government							
Revenue and grants	33.2	48.8	51.1	42.8	41.3	40.8	40.3
Tax revenue	16.0	15.3	17.7	17.5	19.9	19.4	19.0
Nontax revenue	16.3	17.6	18.9	18.9	19.3	19.6	19.6
Grants	0.7	15.7	14.2	6.2	1.8	1.6	1.5
Expenditure and net lending	34.8	61.1	72.3	53.0	48.4	46.0	43.5
Current expenditure	26.0	39.4	41.8	38.0	36.0	34.0	32.0
Capital expenditure	10.7	22.3	31.1	15.5	13.0	12.5	12.0
Overall balance	-1.7	-12.3	-21.3	-10.2	-7.2	-5.1	-3.2
Overall balance, excluding grants	-2.4	-27.9	-31.7	-16.4	-8.9	-6.8	-4.7
Financing							
Domestic	-2.3	9.0	9.8	6.0	4.3	4.0	6.0
Foreign	4.0	3.6	9.4	4.3	2.8	1.1	-2.8
Additional external financing requirement	…	…	2.1	…	…	…	…
Total public sector debt 2/	45.3	56.6	73.0	76.9	78.1	77.1	74.0
Of which: Foreign debt	39.0	41.4	48.5	48.3	47.1	44.2	37.7
	(In millions of U.S. dollars, unless otherwise indicated)						
Balance of payments							
Domestic exports (in percent change) 3/	8.8	-7.7 4/	4.7	5.0	5.1	6.1	6.1
Merchandise imports (in percent change)	36.9	21.1	18.2	-6.4	3.7	3.6	4.9
Tourism receipts (in percent change)	16.9	-35.5	34.1	20.7	20.5	11.6	13.5
Trade balance	-386.3	-517.2	-629.2	-565.4	-581.6	-595.2	-620.3
Nonfactor services (net)	352.4	118.1	198.1	374.8	478.7	547.4	638.3
Current account balance	-128.9	-297.9	-359.0	-221.9	-179.0	-124.9	-60.3
(In percent of GDP)	-16.1	-36.5	-38.5	-21.6	-15.9	-10.2	-4.5
Overall balance	57.7	-136.4	-88.2	-62.9	-32.1	4.0	12.1
Additional external financing requirement	...	...	20.0	...	...	...	...
Memorandum items:							
Gross official reserves (year-end)	204.4	187.2	164.0	101.1	54.0	38.0	30.1
(In months of imports of GNFS) 5/	3.4	2.5	1.9	1.3	0.7	0.5	0.4
External debt (year-end) 6/	331.8	481.6	657.6	649.7	666.7	662.7	604.5
(In percent of GDP)	41.5	58.9	70.4	63.1	59.3	54.0	45.1
Debt service	28.4	32.2	34.8	42.8	48.6	51.9	52.8
(In percent of exports of GNFS) 5/	4.5	7.3	6.3	6.6	6.3	6.1	5.5

Sources: Data provided by the Maldivian authorities; and IMF staff estimates and projections.

1/ Based on the approved 2006 budget.

2/ Includes state enterprise debt.

3/ Domestic exports are defined as merchandise exports net of reexports.

4/ The decline in exports in 2005 reflects the expiration of garment export privileges. Garments account for about one-fourth of merchandise exports. However, effects on the real economy are negligible since textile production yields little value added.

5/ GNFS = Goods and nonfactor services.

6/ Includes additional external financing, assuming equal proportions of grants and loans.

Table 6. Maldives: Reform Case Medium-Term Scenario, 2004–10

		Est.	Proj. 1/				
	2004	2005	2006	2007	2008	2009	2010
			(Annual percentage change)				
Output and prices							
Real GDP growth	8.8	-3.6	10.2	7.0	6.5	6.0	5.0
Consumer prices (period average)	6.4	5.7	5.7	3.8	2.5	2.5	2.5
			(In percent of GDP)				
Central government							
Revenue and grants	33.2	48.8	49.2	41.0	38.7	38.7	38.7
Tax revenue	16.0	15.3	17.5	16.5	19.3	19.1	19.1
Nontax revenue	16.3	17.6	15.9	18.2	17.5	17.7	17.9
Grants	0.7	15.7	15.5	6.0	1.7	1.6	1.5
Expenditure and net lending	34.8	61.1	66.2	48.1	42.4	40.5	38.5
Current expenditure	26.0	39.4	36.4	33.0	32.0	31.0	29.0
Capital expenditure	10.7	22.3	30.3	15.5	11.0	10.0	10.0
Overall balance	-1.7	-12.3	-17.0	-7.0	-3.7	-1.8	0.2
Overall balance, excluding grants	-2.4	-27.9	-32.5	-13.0	-5.4	-3.4	-1.3
Financing							
Domestic	-1.3	9.0	2.8	2.9	1.0	0.7	2.6
Foreign	4.0	3.6	12.1	4.2	2.8	1.1	-2.8
Additional external financing requirement	…	...	2.1	0.0	--	--	--
Total public sector debt 2/	45.3	56.6	67.6	68.3	66.7	63.6	59.1
Of which: Foreign debt	39.0	41.4	47.6	47.0	45.8	43.3	37.4
			(In millions of U.S. dollars, unless otherwise indicated)				
Balance of payments							
Domestic exports (in percent change) 3/	8.8	-7.7 4/	4.7	8.1	8.6	9.2	8.2
Merchandise imports (in percent change)	36.9	21.1	14.8	-7.8	5.8	6.1	5.5
Tourism receipts (in percent change)	16.9	-35.5	34.1	20.7	20.5	11.6	13.5
Trade balance	-386.3	-517.2	-606.0	-529.6	-555.4	-582.7	-609.1
Nonfactor services (net)	352.4	118.1	198.1	374.8	478.7	547.4	638.3
Current account balance	-128.9	-297.9	-335.8	-186.0	-152.7	-112.4	-49.0
(In percent of GDP)	-16.1	-36.5	-35.3	-17.6	-13.2	-9.0	-3.6
Overall balance	57.7	-136.4	-65.0	-17.1	4.1	21.5	33.4
Additional external financing requirement	--	…	20.0	17.1	…	…	…
Memorandum items:							
Gross official reserves (year-end)	205.2	187.9	187.9	187.9	177.0	178.5	191.9
(In months of imports of GNFS)5/	3.4	2.5	2.2	2.6	2.3	2.2	2.2
External debt (year-end) 6/	331.8	481.6	674.6	711.0	710.7	703.9	646.3
(In percent of GDP)	41.5	58.9	70.8	67.3	61.6	56.1	47.9
Debt service	28.4	31.6	34.4	43.3	49.1	52.3	53.2
(In percent of exports of GNFS) 5/	4.5	7.2	6.2	6.6	6.3	6.1	5.5

Sources: Data provided by the Maldivian authorities; and IMF staff estimates and projections.

1/ 2006 figures are based on a policy scenario discussed during the Article IV mission.

2/ Includes state enterprise debt.

3/ Domestic exports are defined as merchandise exports net of reexports.

4/ The decline in exports in 2005 reflects the expiration of garment export privileges. Garments account for about one-fourth of merchandise exports. However, effects on the real economy are negligible since textile production yields little value added.

5/ GNFS = Goods and nonfactor services.

6/ Includes additional external financing, assuming equal proportions of grants and loans.

Table 7. Maldives: Indicators of External Vulnerability, 1991-2005

	1991–96	1997	1998	1999	2000	2001	2002	2003	2004	Est. 2005
	(In percent of GDP, unless otherwise indicated)									
Financial indicators										
Government debt 1/	45.2	39.7	41.0	40.1	40.9	43.5	47.0	47.0	42.3	53.7
Broad money (annual percent change) 2/	23.3	23.1	22.8	3.6	4.1	8.0	19.5	14.5	32.8	9.1
Private sector credit (annual percent change) 2/	20.3	38.9	25.7	4.0	8.0	29.9	15.3	6.8	57.3	44.3
External indicators										
Domestic exports (annual percent change, in U.S. dollars)	12.1	23.8	1.5	-14.3	19.1	0.3	18.7	24.4	8.8	-7.7
Imports (annual percent change, in U.S. dollars)	12.3	15.6	1.5	13.6	-3.4	1.3	-0.4	20.2	36.9	21.1
Current account balance 1/	-3.1	-6.2	-4.1	-13.4	-8.2	-9.4	-5.6	-4.6	-16.1	-36.5
Capital and financial account balance	9.8	12.1	9.4	12.2	7.0	6.0	11.8	15.5	23.3	19.8
Of which: Official medium- and long-term loans (net)	5.0	25.4	2.7	0.9	-0.3	1.2	4.2	5.0	3.3	3.2
Other	4.8	-13.3	6.7	11.3	7.3	4.7	7.6	10.5	20.1	16.5
Gross official reserves (in millions of U.S. dollars)	42.4	99.7	119.9	128.5	123.6	93.8	134.0	160.3	204.4	187.2
Central bank short-term foreign liabilities (in millions of U.S. dollars)	10.7	0.9	0.9	0.9	0.9	0.8	0.8	0.8	0.9	…
Short-term foreign assets of the banking sector (in millions of U.S. dollars)	14.4	11.5	23.7	19.1	21.9	26.9	33.7	63.9	79.0	…
Short-term foreign liabilities of the banking sector (in millions of U.S. dollars)	18.2	12.8	16.1	27.3	33.6	28.3	35.9	16.6	20.2	…
Official reserves in months of following year's imports GNFS 3/	1.6	2.9	3.1	3.4	3.3	2.5	3.0	2.7	2.8	2.1
Broad money to reserves	2.8	2.0	2.0	1.9	2.1	2.7	2.3	2.2	2.3	2.7
Total reserves to short-term external debt (residual maturity)	142.3	417.5	420.1	308.4	251.3	208.3	254.5	419.7	463.0	118.5
Total external debt	41.3	35.0	37.2	36.1	33.9	33.6	40.4	41.9	41.5	58.9
Of which: Government debt	24.8	25.0	25.6	24.3	22.9	23.9	26.9	29.7	29.6	32.2
Total external debt to domestic exports of GNFS 4/	59.3	46.2	49.5	52.4	49.9	48.8	57.1	53.2	52.9	109.7
Debt service to domestic exports of GNFS	4.3	7.6	4.0	4.7	5.2	5.1	5.0	4.0	4.5	7.3
Exchange rate (rufiyaa/U.S. dollar, end-period)	11.3	11.8	11.8	11.8	11.8	12.8	12.8	12.8	12.8	12.8

Sources: Data provided by the Maldivian authorities; and IMF staff estimates and projections.

1/ The first entry is the average for 1995–96.
2/ Adjusted for the exchange rate change in 2001.
3/ GNFS = Goods and nonfactor services.
4/ Domestic exports are defined as merchandise exports net of reexports.

Table 8. Maldives: Base Case External Debt Sustainability Framework, 2000-10
(In percent of GDP, unless otherwise indicated)

	Actual							Projections 1/						
	2000	2001	2002	2003	2004			2005	2006	2007	2008	2009	2010	
								I. Baseline Projections 10/						**Debt-stabilizing noninterest current account 9/**
External debt 2/	33.9	33.6	40.4	41.9	41.5			**58.9**	**70.4**	**63.1**	**59.3**	**54.0**	**45.1**	**-10.5**
Change in external debt	-2.2	-0.3	6.9	1.5	-0.4			17.4	11.5	-7.3	-3.8	-5.3	-8.9	
Identified external debt-creating flows (4+8+9)	4.1	7.5	2.1	-2.4	2.7			24.7	21.0	8.9	5.0	0.1	-4.4	
Current account deficit, excluding interest payments	7.0	8.4	4.6	3.9	15.3			35.5	37.4	20.4	14.9	9.2	3.6	
Deficit in balance of goods and services	-0.9	-1.3	-6.1	-7.1	4.2			48.8	46.2	18.5	9.2	3.9	-1.3	
Exports	73.2	74.3	77.3	84.5	85.8			60.7	66.4	70.2	75.0	75.9	77.8	
Imports	72.3	73.0	71.2	77.5	90.1			109.5	112.6	88.7	84.2	79.8	76.4	
Net nondebt creating capital inflows (negative)	-2.1	-1.9	-2.6	-4.1	-7.7			-13.2	-13.4	-10.1	-9.2	-8.4	-7.4	
Automatic debt dynamics 3/	-0.8	1.0	0.1	-2.2	-4.9			2.5	-3.1	-1.4	-0.7	-0.6	-0.6	
Contribution from nominal interest rate	1.2	1.0	1.0	0.8	0.9			1.0	1.1	1.1	1.0	1.0	0.9	
Contribution from real GDP growth	-1.6	-1.2	-1.3	-3.2	-3.2			1.5	-4.1	-2.6	-1.7	-1.6	-1.5	
Contribution from price and exchange rate changes 4/	-0.4	1.1	0.5	0.3	-2.5			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 5/	-6.4	-7.8	4.7	3.8	-3.1			-7.3	-9.5	-16.3	-8.8	-5.4	-4.5	
External debt-to-exports ratio (in percent)	46.3	45.2	52.3	49.6	48.4			97.2	106.1	90.0	79.1	71.2	58.0	
Gross external financing need (in billions of U.S. dollars) 6/	93.1	108.0	80.8	84.6	167.1			342.1	516.9	431.3	394.2	327.7	244.7	
in percent of GDP	14.9	17.3	12.6	12.2	20.9			41.9	55.4	41.9	35.1	26.7	18.3	
Key macroeconomic assumptions						10-year historical average	10-year standard deviation							Projected Average
Real GDP growth (in percent)	4.8	3.5	4.1	8.5	8.8	7.4	2.5	-3.6	8.0	4.0	3.0	3.0	3.0	2.9
GDP deflator in U.S. dollars (change in percent)	1.1	-3.2	-1.5	-0.7	6.4	1.0	3.2	6.0	5.8	6.0	6.0	6.0	6.0	6.0
Nominal external interest rate (in percent)	3.6	3.1	2.9	2.1	2.4	3.0	0.5	2.5	2.1	1.8	1.8	1.8	1.7	1.9
Growth of exports (U.S. dollar terms, in percent)	5.3	1.5	6.7	17.9	17.5	9.8	6.6	-27.8	25.1	16.5	16.7	10.5	11.9	8.8
Growth of imports (U.S. dollar terms, in percent)	-2.2	1.0	0.0	17.4	34.6	11.3	11.5	24.2	17.5	-13.1	3.6	3.5	4.6	6.7
Current account balance, excluding interest payments	-7.0	-8.4	-4.6	-3.9	-15.3	-6.4	4.5	-35.5	-37.4	-20.4	-14.9	-9.2	-3.6	-20.2
Net nondebt creating capital inflows	2.1	1.9	2.6	4.1	7.7	2.7	1.9	13.2	13.4	10.1	9.2	8.4	7.4	10.3
								II. Stress Tests for External Debt Ratio						**Debt-stabilizing noninterest current account 8/**
A. Alternative scenarios														
A1. Key variables are at their historical averages in 2006-10 7/								**58.9**	**53.0**	**40.8**	**36.7**	**36.2**	**36.4**	**-9.3**
A2. Country-specific shock in 2006, with reduction in GDP growth (relative to baseline) of one standard deviation 8/								**41.2**	**41.0**	**40.1**	**39.1**	**38.0**	**36.9**	**-6.6**
A3. Selected variables are consistent with market forecast in 2006-10								**58.9**	**70.4**	**63.1**	**59.3**	**54.0**	**45.1**	**-10.5**
B. Bound tests														
B1. Nominal interest rate is at historical average plus two standard deviations in 2006 and 2007								**58.9**	**71.4**	**65.5**	**61.6**	**56.1**	**47.1**	**-10.6**
B2. Real GDP growth is at historical average minus two standard deviations in 2006 and 2007								**58.9**	**72.2**	**64.2**	**59.3**	**53.3**	**43.8**	**-10.9**
B3. Change in U.S. dollar GDP deflator is at historical average minus two standard deviations in 2006 and 2007								**58.9**	**74.3**	**69.3**	**61.5**	**53.4**	**42.3**	**-12.1**
B4. Noninterest current account is at historical average minus two standard deviations in 2006 and 2007								**58.9**	**48.4**	**37.8**	**35.7**	**32.0**	**24.6**	**-9.1**
B5. Combination of 2-5 using one standard deviation shocks								**58.9**	**48.5**	**33.0**	**31.4**	**27.7**	**19.6**	**-10.2**
B6. One time 30 percent nominal depreciation in 2006								**58.9**	**84.6**	**66.6**	**56.4**	**46.8**	**34.6**	**-12.9**

1/ Based on the Article IV mission discussion, figures for 2005 are preliminary estimates.
2/ External debt is based upon the assumption that around 30 percent of private capital flows are debt-creating.
3/ Derived as [r - g - ρ(1+g) + εα(1+r)]/(1+g+ρ+gρ) times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in U.S. dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.
4/ The contribution from price and exchange rate changes is defined as [-ρ(1+g) + εα(1+r)]/(1+g+ρ+gρ) times previous period debt stock. ρ increases with an appreciating domestic currency (ε > 0) and rising inflation (based on GDP deflator).
5/ For projection, line includes price and exchange rate changes, as well as changes in foreign reserves.
6/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.
7/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both noninterest current account and nondebt inflows in percent of GDP.
8/ The implied change in other key variables under this scenario is discussed in the text.
9/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and both noninterest current account and nondebt inflows in percent of GDP) remain at their levels of the last projection year.
10/ The sharp increase in external debt in 2005 is due in part to the rise of commercial bank borrowing from abroad.

Table 9. Maldives: Base Case Public Sector Debt Sustainability Framework, 2000-10
(In percent of GDP, unless otherwise indicated)

	Actual							Projections 1/						
	2000	2001	2002	2003	2004			2005	2006	2007	2008	2009	2010	
										I. Baseline Projections				Debt-stabilizing primary balance 11/
Public sector debt 2/	40.9	43.5	47.0	47.0	42.3			**53.7**	**68.2**	**72.1**	**73.2**	**72.2**	**69.3**	**-3.4**
Of which foreign-currency denominated	24.7	24.4	25.9	26.9	26.7			37.5	41.0	41.9	30.0	29.5	27.4	
Change in public sector debt	0.7	2.6	3.6	0.0	-4.7			11.4	14.6	3.9	1.1	-1.0	-2.9	
Identified debt-creating flows (4+7+12)	2.1	5.1	2.0	0.0	-4.7			11.4	14.6	3.9	1.1	-1.0	-2.9	
Primary deficit	2.9	3.2	3.2	1.9	0.3			11.0	19.5	7.9	4.7	2.6	0.7	
Revenue and grants	32.3	33.0	33.1	34.9	33.2			48.8	51.1	42.8	41.3	40.8	40.3	
Primary (noninterest) expenditure	35.2	36.2	36.3	36.8	33.5			59.8	70.6	50.7	45.9	43.4	41.0	
Automatic debt dynamics 3/	-0.8	1.9	-1.3	-1.9	-5.1			0.4	-4.9	-4.0	-3.6	-3.6	-3.6	
Contribution from interest rate/growth differential 4/	-0.8	-0.1	-1.3	-1.9	-5.1			0.4	-4.9	-4.0	-3.6	-3.6	-3.6	
Of which contribution from real interest rate	1.0	1.3	0.4	1.8	-1.5			-1.1	-1.2	-1.5	-1.6	-1.6	-1.6	
Of which contribution from real GDP growth	-1.8	-1.4	-1.7	-3.7	-3.6			1.5	-3.8	-2.5	-2.0	-2.0	-2.0	
Contribution from exchange rate depreciation 5/	0.0	2.0	0.0	0.0	0.0			...	...	...	...	...	...	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Other (specify, e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3) 6/	-1.4	-2.5	1.6	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 2/	126.6	131.9	142.1	134.6	127.5			109.9	133.7	168.4	177.5	176.8	171.9	
Gross financing need 7/	21.7	24.5	25.8	24.5	19.4			27.6	42.7	39.2	49.4	48.0	46.3	
in billions of U.S. dollars	135.2	152.9	165.0	169.3	154.7	10-year historical average	10-year standard deviation	225.7	398.7	403.0	555.5	589.3	619.7	Projected Average
Key macroeconomic and fiscal assumptions														
Real GDP growth (in percent)	4.8	3.5	4.1	8.5	8.8	7.4	2.5	-3.6	8.0	4.0	3.0	3.0	3.0	2.9
Average nominal interest rate on public debt (in percent) 8/	3.8	3.9	4.1	3.5	3.2	3.7	0.3	3.1	3.8	3.8	3.8	3.8	3.8	3.7
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	2.7	3.2	1.1	4.2	-3.2	1.7	2.8	-2.9	-2.0	-2.2	-2.2	-2.2	-2.2	-2.3
Nominal appreciation (increase in U.S. dollar value of local currency, in percent)	0.0	-8.0	0.0	0.0	0.0	-0.8	2.5	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	1.1	0.6	3.0	-0.7	6.4	2.0	2.9	6.0	5.8	6.0	6.0	6.0	6.0	6.0
Growth of real primary spending (deflated by GDP deflator, in percent)	6.3	6.3	4.5	9.9	-0.9	8.3	7.7	72.1	27.4	-25.3	-6.7	-2.6	-2.7	10.4
Primary deficit	2.9	3.2	3.2	1.9	0.3	2.3	1.6	11.0	19.5	7.9	4.7	2.6	0.7	7.7
										II. Stress Tests for Public Debt Ratio				Debt-stabilizing primary balance 10/
A. Alternative scenarios														
A1. Key variables are at their historical averages in 2006-10 9/								**53.7**	**53.1**	**52.6**	**52.1**	**51.6**	**51.1**	**-2.8**
A2. Primary balance under no policy change in 2006-10								**53.7**	**68.2**	**72.1**	**73.2**	**72.2**	**69.3**	**-3.4**
A3. Selected variables are consistent with market forecast in 2006-10								**53.7**	**68.2**	**72.1**	**73.2**	**72.2**	**69.3**	**-3.4**
B. Bound tests														
B1. Real interest rate is at historical average plus two standard deviations in 2006 and 2007								**53.7**	**72.6**	**82.5**	**83.1**	**81.6**	**78.2**	**-3.9**
B2. Real GDP growth is at historical average minus two standard deviations in 2006 and 2007								**53.7**	**74.7**	**82.8**	**86.5**	**87.9**	**87.1**	**-4.3**
B3. Primary balance is at historical average minus two standard deviations in 2006 and 2007								**53.7**	**54.2**	**56.6**	**58.4**	**58.1**	**56.0**	**-2.8**
B4. Combination of 1-3 using one standard deviation shocks								**53.7**	**57.2**	**60.8**	**62.4**	**61.9**	**59.6**	**-2.9**
B5. One-time 30 percent real depreciation in 2006 10/								**53.7**	**84.6**	**87.5**	**87.8**	**86.1**	**82.5**	**-4.1**
B6. 10 percent of GDP increase in other debt-creating flows in 2006								**53.7**	**78.2**	**81.5**	**82.2**	**80.7**	**77.4**	**-3.8**

1/ Based on the approved 2006 budget. Figures for 2005 are preliminary estimates.

2/ Total government debt, excluding state enterprise debt.

3/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in currency value of U.S. dollars.)

4/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as -g.

5/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.

6/ For projections, this line includes exchange rate changes.

7/ Defined as public sector deficit, plus amortization of medium-and long-term public sector debt, plus short-term debt at end of previous period.

8/ Derived as nominal interest expenditure divided by previous period debt stock.

9/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

10/ Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

11/ Assumes that key variables (real GDP growth, real interest rate, and primary balance) remain at the level in percent of GDP/growth rate of the last projection year.

Table 10. Maldives: Reform Case External Debt Sustainability Framework, 2000-10
(In percent of GDP, unless otherwise indicated)

	2000	2001	2002	2003	2004	10-year historical average	10-year standard deviation	Projections 1/ 2005	2006	2007	2008	2009	2010	
										I. Baseline Projections 10/				**Debt-stabilizing noninterest current account 9/**
External debt 2/	33.9	33.6	40.4	41.9	41.5			**58.9**	**70.8**	**67.3**	**61.6**	**56.1**	**47.9**	**-10.2**
Change in external debt	-2.2	-0.3	6.9	1.5	-0.4			17.4	11.9	-3.6	-5.7	-5.4	-8.2	
Identified external debt-creating flows (4+8+9)	4.1	7.5	2.1	-2.4	2.7			24.7	16.2	3.1	0.0	-2.6	-6.5	
Current account deficit, excluding interest payments	7.0	8.4	4.6	3.9	15.3			35.5	34.3	16.5	12.2	8.0	2.7	
Deficit in balance of goods and services	-0.9	-1.3	-6.1	-7.1	4.2			48.8	42.8	14.6	6.7	2.8	-2.2	
Exports	73.2	74.3	77.3	84.5	85.8			60.7	65.1	68.7	73.7	75.3	78.5	
Imports	72.3	73.0	71.2	77.5	90.1			109.5	107.9	83.3	80.4	78.1	76.3	
Net nondebt creating capital inflows (negative)	-2.1	-1.9	-2.6	-4.1	-7.7			-13.2	-13.9	-10.1	-9.2	-8.1	-7.6	
Automatic debt dynamics 3/	-0.8	1.0	0.1	-2.2	-4.9			2.4	-4.1	-3.3	-3.0	-2.4	-1.7	
Contribution from nominal interest rate	1.2	1.0	1.0	0.8	0.9			0.9	1.0	1.1	1.0	1.0	0.9	
Contribution from real GDP growth	-1.6	-1.2	-1.3	-3.2	-3.2			1.5	-5.1	-4.5	-4.0	-3.4	-2.6	
Contribution from price and exchange rate changes 4/	-0.4	1.1	0.5	0.3	-2.5			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 5/	-6.4	-7.8	4.7	3.8	-3.1			-7.3	-4.3	-6.7	-5.7	-2.9	-1.7	
External debt-to-exports ratio (in percent)	46.3	45.2	52.3	49.6	48.4			97.2	108.8	98.0	83.5	74.5	61.0	
Gross external financing need (in billions of U.S. dollars) 6/	93.1	108.0	80.8	84.6	167.1			342.1	493.7	395.5	367.9	315.3	233.4	
in percent of GDP	14.9	17.3	12.6	12.2	20.9			41.9	51.8	37.4	31.9	25.1	17.3	
Key macroeconomic assumptions														Projected Average
Real GDP growth (in percent)	4.8	3.5	4.1	8.5	8.8	7.4	2.5	-3.6	10.2	7.0	6.5	6.0	5.0	5.2
GDP deflator in U.S. dollars (change in percent)	1.1	-3.2	-1.5	-0.7	6.4	1.0	3.2	6.0	5.8	3.8	2.5	2.5	2.5	3.8
Nominal external interest rate (in percent)	3.6	3.1	2.9	2.1	2.4	3.0	0.5	2.3	2.0	1.8	1.7	1.8	1.7	1.9
Growth of exports (U.S. dollar terms, in percent)	5.3	1.5	6.7	17.9	17.5	9.8	6.6	-27.8	25.1	17.1	17.2	11.0	12.1	9.1
Growth of imports (U.S. dollar terms, in percent)	-2.2	1.0	0.0	17.4	34.6	11.3	11.5	24.2	14.9	-14.3	5.3	5.6	5.1	6.8
Current account balance, excluding interest payments	-7.0	-8.4	-4.6	-3.9	-15.3	-6.4	4.5	-35.5	-34.3	-16.5	-12.2	-8.0	-2.7	-18.2
Net nondebt creating capital inflows	2.1	1.9	2.6	4.1	7.7	2.7	1.9	13.2	13.9	10.1	9.2	8.1	7.6	10.3
										II. Stress Tests for External Debt Ratio				**Debt-stabilizing noninterest current account 8/**
A. Alternative scenarios														
A1. Key variables are at their historical averages in 2006-10 7/								**58.9**	**58.4**	**54.5**	**50.9**	**50.4**	**51.1**	**-10.2**
A2. Country-specific shock in 2006, with reduction in GDP growth (relative to baseline) of one standard deviation 8/								**41.2**	**41.0**	**40.1**	**39.1**	**38.0**	**36.9**	**-6.6**
A3. Selected variables are consistent with market forecast in 2006-10								**58.9**	**70.8**	**67.3**	**61.6**	**56.1**	**47.9**	**-10.2**
B. Bound tests														
B1. Nominal interest rate is at historical average plus two standard deviations in 2006 and 2007								**58.9**	**71.9**	**69.6**	**63.8**	**58.2**	**49.9**	**-10.3**
B2. Real GDP growth is at historical average minus two standard deviations in 2006 and 2007								**58.9**	**73.6**	**71.0**	**63.5**	**56.7**	**47.5**	**-11.1**
B3. Change in U.S. dollar GDP deflator is at historical average minus two standard deviations in 2006 and 2007								**58.9**	**75.1**	**74.6**	**65.5**	**57.6**	**47.5**	**-11.9**
B4. Noninterest current account is at historical average minus two standard deviations in 2006 and 2007								**58.9**	**52.0**	**48.9**	**44.5**	**40.1**	**32.7**	**-9.4**
B5. Combination of 2-5 using one standard deviation shocks								**58.9**	**53.2**	**47.2**	**42.6**	**38.0**	**29.6**	**-10.9**
B6. One-time 30 percent nominal depreciation in 2006								**58.9**	**86.5**	**75.6**	**63.6**	**54.0**	**42.5**	**-13.1**

1/ Based on the Article IV mission discussion, figures for 2005 are preliminary estimates.
2/ External debt is based upon the assumption that around 30 percent of private capital flows are debt-creating.
3/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in U.S. dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.
4/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).
5/ For projection, line includes price and exchange rate changes, as well as changes in foreign reserves.
6/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.
7/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both noninterest current account and nondebt inflows in percent of GDP.
8/ The implied change in other key variables under this scenario is discussed in the text.
9/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and both noninterest current account and nondebt inflows in percent of GDP) remain at their levels of the last projection year.
10/ The sharp increase in external debt in 2005 is due in part to the rise of commercial bank borrowing from abroad.

Table 11. Maldives: Reform Case Public Sector Debt Sustainability Framework, 2000-10
(In percent of GDP, unless otherwise indicated)

	Actual							Projections 1/						
	2000	2001	2002	2003	2004			2005	2006	2007	2008	2009	2010	
										I. Baseline Projections				**Debt-stabilizing primary balance 11/**
Public sector debt 2/	40.9	43.5	47.0	47.0	42.3			**53.7**	**63.0**	**63.8**	**62.2**	**59.0**	**54.7**	**-0.8**
Of which foreign-currency denominated	24.7	24.4	25.9	26.9	26.7			37.5	37.8	42.3	40.7	39.0	36.0	
Change in public sector debt	0.7	2.6	3.6	0.0	-4.7			11.4	9.4	0.8	-1.6	-3.1	-4.4	
Identified debt-creating flows (4+7+12)	2.1	5.1	2.0	0.0	-4.7			11.4	9.4	0.8	-1.6	-3.1	-4.4	
Primary deficit	2.9	3.2	3.2	1.7	0.1			9.8	14.2	3.6	0.2	-1.6	-3.5	
Revenue and grants	32.3	33.0	33.1	34.9	33.2			48.8	49.2	41.0	38.7	38.7	38.7	
Primary (noninterest) expenditure	35.2	36.2	36.3	36.7	33.3			58.6	63.4	44.6	38.9	37.0	35.2	
Automatic debt dynamics 3/	-0.8	1.9	-1.3	-1.8	-4.9			1.6	-4.9	-2.8	-1.8	-1.5	-0.9	
Contribution from interest rate/growth differential 4/	-0.8	-0.1	-1.3	-1.8	-4.9			1.6	-4.9	-2.8	-1.8	-1.5	-0.9	
Of which contribution from real interest rate	1.0	1.3	0.4	2.0	-1.3			0.1	-0.2	1.1	2.0	1.9	1.9	
Of which contribution from real GDP growth	-1.8	-1.4	-1.7	-3.7	-3.6			1.5	-4.7	-4.0	-3.8	-3.4	-2.7	
Contribution from exchange rate depreciation 5/	0.0	2.0	0.0	0.0	0.0			...	...	...	...	...	...	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Other (specify, e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3) 6/	-1.4	-2.5	1.6	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 2/	126.6	131.9	142.1	134.6	127.5			109.9	128.1	155.6	160.5	152.6	141.2	
Gross financing need 7/	21.7	24.5	25.8	24.5	19.4			27.6	38.0	29.1	27.1	24.4	21.6	
in billions of U.S. dollars	135.2	152.9	165.0	169.3	154.7			225.7	361.8	307.7	312.4	305.9	291.0	
Key macroeconomic and fiscal assumptions						10-year historical average	10-year standard deviation							Projected Average
Real GDP growth (in percent)	4.8	3.5	4.1	8.5	8.8	7.4	2.5	-3.6	10.2	7.0	6.5	6.0	5.0	5.2
Average nominal interest rate on public debt (in percent) 8/	3.8	3.9	4.1	3.8	3.8	3.8	0.2	6.0	6.0	6.0	6.0	6.0	6.0	6.0
Average real interest rate (nominal rate minus change in GDP deflator, in perc	2.7	3.2	1.1	4.5	-2.6	1.8	2.7	0.0	0.2	2.2	3.5	3.5	3.5	2.2
Nominal appreciation (increase in U.S. dollar value of local currency, in perce	0.0	-8.0	0.0	0.0	0.0	-0.8	2.5	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	1.1	0.6	3.0	-0.7	6.4	2.0	2.9	6.0	5.8	3.8	2.5	2.5	2.5	3.8
Growth of real primary spending (deflated by GDP deflator, in percent)	6.3	6.3	4.5	9.5	-1.2	8.2	7.7	69.8	19.2	-24.7	-7.1	0.9	-0.2	9.6
Primary deficit	2.9	3.2	3.2	1.7	0.1	2.3	1.6	9.8	14.2	3.6	0.2	-1.6	-3.5	3.8
										II. Stress Tests for Public Debt Ratio				**Debt-stabilizing primary balance 10/**
A. Alternative scenarios														
A1. Key variables are at their historical averages in 2006-10 9/								**53.7**	**53.1**	**52.6**	**52.1**	**51.7**	**51.2**	**-2.7**
A2. Primary balance under no policy change in 2006-10								**53.7**	**63.0**	**63.8**	**62.2**	**59.0**	**54.7**	**-0.8**
A3. Selected variables are consistent with market forecast in 2006-10								**53.7**	**63.0**	**63.8**	**62.2**	**59.0**	**54.7**	**-0.8**
B. Bound tests														
B1. Real interest rate is at historical average plus two standard deviations in 2006 and 2007								**53.7**	**66.3**	**69.9**	**68.1**	**64.8**	**60.3**	**-0.9**
B2. Real GDP growth is at historical average minus two standard deviations in 2006 and 2007								**53.7**	**71.5**	**80.3**	**83.0**	**83.9**	**83.5**	**-1.3**
B3. Primary balance is at historical average minus two standard deviations in 2006 and 2007								**53.7**	**54.3**	**57.4**	**56.0**	**53.0**	**48.7**	**-0.7**
B4. Combination of 1-3 using one standard deviation shocks								**53.7**	**57.2**	**60.8**	**59.3**	**56.2**	**51.9**	**-0.8**
B5. One-time 30 percent real depreciation in 2006 10/								**53.7**	**79.0**	**79.0**	**76.9**	**73.4**	**68.9**	**-1.0**
B6. 10 percent of GDP increase in other debt-creating flows in 2006								**53.7**	**73.0**	**73.4**	**71.4**	**68.1**	**63.6**	**-1.0**

1/ Based on the approved 2006 budget. Figures for 2005 are preliminary estimates.
2/ Total government debt, excluding state enterprise debt.
3/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in currency value of U.S. dollars.)
4/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi (1+g)$ and the real growth contribution as -g.
5/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.
6/ For projections, this line includes exchange rate changes.
7/ Defined as public sector deficit, plus amortization of medium-and long-term public sector debt, plus short-term debt at end of previous period.
8/ Derived as nominal interest expenditure divided by previous period debt stock.
9/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.
10/ Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).
11/ Assumes that key variables (real GDP growth, real interest rate, and primary balance) remain at the level in percent of GDP/growth rate of the last projection year.

MALDIVES: FUND RELATIONS

(As of December 31, 2005)

I. **Membership Status**: Joined 1/13/78; Article XIV

II. **General Resources Account**:

	SDR Million	**% Quota**
Quota	8.20	100.00
Fund holdings of currency	10.75	131.05
Reserve position in Fund	1.55	18.95

III. **SDR Department**:

	SDR Million	**% Quota**
Net cumulative allocation	0.28	100.00
Holdings	0.32	113.29

IV. **Outstanding Purchases and Loans**:

	SDR Million	**% Quota**
Emergency assistance	4.1	50.00

V. **Financial Arrangements**: None

VI. **Projected Obligations to Fund**:
(SDR million; based on existing use of resources and present holdings of SDR):

	Forthcoming			
	2006	2007	2008	2009
Principal			1.54	2.05
Charges/interest	0.17	0.17	0.16	0.08
Total	0.17	0.17	1.70	2.13

VII. **Exchange Arrangements**

From March 1, 1982 to June 30, 1985, the Maldivian rufiyaa was pegged to the U.S. dollar. Beginning in July 1985, the exchange rate of the rufiyaa was linked to a trade-weighted basket of currencies, but the exchange rate vis-à-vis the U.S. dollar remained relatively stable until February 1987. On March 1, 1987, the rufiyaa was devalued by 29 percent vis-à-vis the U.S. dollar. From 1987 to 1994, the exchange rate of the rufiyaa was adjusted periodically. Since October 1994, the exchange rate of the rufiyaa remained unchanged at Rf 11.77 per U.S. dollar, until July 25, 2001, when the rufiyaa was devalued to Rf 12.80 per U.S. dollar.

Maldives continues to avail itself of the transitional arrangements under the provisions of Article XIV, but no longer maintains restrictions under Article XIV. Under these circumstances, any exchange rate restriction that arises is subject to approval under Article VIII. Maldives' Post Office Exchange Counter (which existed until July 2000) did not by itself give rise to an exchange rate restriction.

VIII. **Last Article IV Consultation**

The 2004 Article IV consultation (SM/04/157, April 30, 2004) was concluded by the Executive Board on May 24, 2004 (EBM/04/50-2).

IX. **Technical Assistance**

FAD: In April 1994, Mr. Potter and Ms. Bédague visited Male to advise on budget management. This was followed by periodic assistance from Mr. Webber (consultant) over the period November 1994 to December 1995. In July 1994, Mr. Faria and Mr. Kambil (consultant) assisted in formulating a strategy for revenue reform. This was followed by a visit by Mr. Kambil in August/September 1995 to draft tax legislation. In October 1996, a tax administration mission visited Male to develop a strategy to establish an Inland Revenue Department and a follow-up mission by a consultant took place in June 1997.

LEG: In October 2003, Mr. Head provided assistance on the revision of the Maldives Monetary Authority Act (MMA Act).

MFD: In March 1993, a consultant provided assistance on the introduction of treasury bills. In November 1994, a mission headed by Mr. Taniguchi provided assistance on monetary management, foreign exchange operations, and bank supervision. In February/June 1995, a consultant provided assistance for the development of a treasury bill and MMA certificate market. In February/March 1996, a mission headed by Mr. Swinburne provided advice on the reform of monetary operations and exchange system. This was followed by a visit of a foreign exchange advisor in May 1997. In early 2001, two consultants provided assistance on foreign exchange and monetary management, of two missions each. In July 2001, a consultant provided assistance on monetary management following the lifting of credit ceilings and further impending changes in the monetary framework. In October 2002, a multi-purpose mission took stock of developments and provided recommendations in the areas of banking, foreign exchange operations, and foreign exchange reserves management. In October 2003, in cooperation with the legal consultant, Mr. Dornseif (Deutsche Bundesbank) provided assistance on the drafting of the amended MMA Act. Currently, Mr. Van de Walle and Mr. Nun are providing TA on monetary policy operations and banking supervision, respectively.

STA: In June 1993 and February 1994, assistance was provided on monetary and balance of payments statistics, respectively. In May 1995, a STA consultant provided assistance on the compilation of a new consumer price index, which was followed by further assistance in August 1996. TA on monetary and banking issues was provided by Mr. Martinez in 2005.

MALDIVES: RELATIONS WITH THE WORLD BANK GROUP[1]
(As of September 30, 2005)

IBRD/IDA Lending Operations

	Original Commitments		Disbursements	Undisbursed
Current portfolio (IDA)				
Integrated human development	15.6	1/	0.5	5.7
Emergency recovery credit and grant	14.0	2/	7.7	6.3
Sub-total	**29.6**		**8.2**	**12.0**
Closed projects (IDA)				
Fisheries I	3.2		2.48	
Fisheries II	5.0		5.75	
Fisheries III	10.0		9.42	
Male airport upgrading	7.5		8.04	
Education and training	8.19		8.12	
Education and training II	13.4		12.88	
Education and training III	17.6	3/	16.83	
Sub-total	**64.89**		**63.52**	
Total	94.49		71.72	12.0

1/ US$10 million cancelled to make IDA resources available under the Maldives Post-Tsunami Emergency Recovery Credit and Grant.
2/ Of this total, $8.4 million provided as credit and $5.6 million (40 percent of total financing) as grant.
3/ US$2 million cancelled to make IDA resources available under the Maldives Post-Tsunami Emergency Recovery Credit and Grant.

The World Bank's Country Assistance Strategy

The Country Assistance Strategy (CAS), discussed by the Board in FY2000 emphasizes increasing the frequency and scope of nonlending activities, and gradually shifting from sector-specific project lending to a more multisectoral and programmatic approach. The main objective is to help reduce poverty and regional disparities in access to social and infrastructure services. A new CAS will be prepared, most likely in early FY07, as soon as the country's PRSP is completed. It is intended that the PRSP be prepared as part of the next five-year plan, currently under preparation and due to be completed by the end of this calendar year.

[1]Prepared by World Bank staff.

Lending program

Historically, the Bank group has focused its assistance, totaling over US$80 million in net IDA commitments to date, on fisheries, tourism, human development, particularly education, and recently, emergency recovery. The first, second, and third fisheries projects helped boost production and exports, increasing the incomes of fishermen in the outer atolls. IDA promoted the development of tourism through the Male Airport upgrading project, which closed in 1994. IDA has also supported human resource development in the Maldives, by widening access to secondary education, improving the planning and management capacity of the Ministry of Education, providing overseas scholarships for critical skills acquisition, and training teachers in country. In line with the 2000 CAS, before the Tsunami disaster, the Bank had increased its nonlending services and initiated a shift from sector-specific lending to a more multisectoral and programmatic approach (reflected in the Integrated Human Development Project approved in early FY05).

In close coordination with other development partners, the Bank Group is concentrated presently in helping the government of Maldives implement its post-tsunami recovery program. The Bank approved the Maldives Post-Tsunami Emergency Recovery Credit/Grant (US$14 million) soon after the disaster, including US$12 million from funds reallocated from existing credits and US$2 million from additional IDA resources. More specifically, 40 percent (US$5.6 million) of the emergency operation was provided as grant, and the rest as credit. The grant portion has been fully disbursed. To facilitate coordination and provide advice to the government, the Bank has set up a temporary office in the Maldives managed by an experienced special representative.

The Bank participated in the recent Joint Economic Mission, which also included staffs from IMF and the Asian Development Bank (AsDB). Maldives is facing severe budget and balance of payments problems, triggered by the tsunami and aggravated by higher oil prices and several fiscal policies. Accordingly, in addition to supporting the government's effort to develop a sound fiscal plan, particularly for 2006 and 2007, the Bank will provide a second emergency recovery credit (indicative amount of $8 million) to help finance imports necessary for the country's recovery. Moreover, the Bank is discussing with the government the possibility of providing budget support in FY07.

Implementation of the Integrated Human Development Project ($5.6 million) continues, although the project was restructured after US$10 million of credit funds were cancelled to make room for post-tsunami support (see above). This project has an inter-sectoral focus, encompassing education, health, social protection, and improved development management at the atoll and island level. The development objective of the project is to improve social service provision and economic opportunities in selected ecologically viable focus islands, helping to provide an alternative to Male and the capital region. In early FY07, the Bank plans to provide about $7 million in additional financing to help meet the objectives originally established for this project.

Advisory and analytical support

The Bank Group has promoted a better understanding of poverty and vulnerability in Maldives and completed a Country Economic Update (which will be valuable inputs into the PRSP); provided technical advice and training on public expenditure management and pension reform; and supported the development of a strategy and action plan in critical areas such as urban development, land management, land administration and housing markets/finance. Following the December 2004 tsunami disaster, the Bank, in partnership with AsDB and the UN agencies, and in coordination with the IMF, prepared an assessment of damage and needs, which helped guide the government's reconstruction efforts, as well as international support.

During FY06, the Bank will help the government develop a Fisheries Sector Development Strategy and conduct an Investment Climate Assessment (ICA) and a Social Security Study, while continuing to build capacity in public expenditure management through an Institutional Development Fund grant. The Social Security Study will explore various options and provide input into the national debate on social security reform. The ICA is underway and should provide new information on the environment for private sector growth.

Another key priority of the government is strengthening and deepening the financial sector, and the authorities have sought legal and technical assistance from the Bank in this area. Efforts in the near future will focus on reforming the provident fund and spurring the development of housing finance (contributing to improved land management). The IFC has begun providing assistance with insurance and leasing, and help is needed to introduce Anti-Money Laundering legislation.

MALDIVES: RELATIONS WITH THE ASIAN DEVELOPMENT BANK[1]
(As of June 30, 2005)

The Asian Development Bank (AsDB) has provided 15 Special Fund loans for a total of $92.5 million (net loan amount) to Maldives since 1981. Energy was the largest sector accounting for 33.9 percent of the total net loan amount, followed by transport and communications, 28.5 percent, education, 13.1 percent, multisector, 12.4 percent, water supply, sanitation and waste management, 6.1 percent, and law, economic management and public policy, 6 percent. As of June 30, 2005 cumulative disbursements of ongoing projects amounted to $24.7 million, or 68 percent of the amount available for withdrawal. In addition, as of June 30, 2005, the AsDB has provided 36 advisory technical assistance (TA) grants for $14.6 million and 15 TA grants amounting to $2.9 million for preparation of loan projects.

List of Loans

Loan Name	Year of Loan Approval	Net Loan Amount	Of which: Disbursed 1/
	(In millions of U.S. dollars)		
Inter-island Transport Project (closed)	1981	0.8	0.8
Multi-project (closed)	1984	2.9	2.9
Power System Development Project (closed)	1987	6.5	6.5
Male Port Development Project (closed)	1988	6.7	6.7
Second Power System Development Project (closed)	1991	9.2	9.2
Second Male Port Development Project (closed)	1993	7.9	7.9
Third Power System Development Project (closed)	1997	6.5	6.5
Post Secondary Education Development Project	1998	6.4	4.4
Regional Development Project I	1999	6.8	6.7
Information Technology Development	2001	10.9	1.2
Outer Islands Electrification	2001	9.2	1.3
Strengthening Public Accounting System	2002	5.5	0.0
Employment Skills Training	2003	5.7	0.2
Regional Development Phase II	2005	5.7	-
Tsunami Emergency Assistance Project	2005	1.8 2/	1.8
Total		92.5	56.1

1/ Data as of June 30, 2005.
2/ Excluding $20 million grant from Asian Tsunami Fund.

[1] Prepared by the Asian Development Bank.

Maldives: Social and Demographic Indicators

	Latest single year	
	1980–85	1995–2004
GDP per capita (U.S. dollars)	469	2,670
Land area (sq. km.)	298	298
Population		
Total population	180,088	299,520
Rate of growth (percent per annum)	2.8	2.2
Density in Male (persons per sq. km.)	42,000	70,000
Population characteristics		
Infant mortality at birth (per 1,000)	115.0	55.0
Crude birth rate (per 1,000)	41.6	28.9
Crude death rate (per 1,000)	11.8	7.3
Life expectancy at birth (years)	57.1	69.5
Labor force (in percent of working-age population)		
Labor force participation rate (2000)	52.1	54.8
Male	77.7	71.7
Female	23.8	37.4
Unemployment rate (2000)	...	2.0
Health care		
Access to safe water	17	100
Immunization (DPT, percent of children under age one)	28	98
Physicians (per 1,000 people)	0.07	0.78
Population per nurse	10,080	651
Population per hospital bed	1,500	503
Education		
School enrollment, primary (gross, 2002)	…	118.0
School enrollment, secondary (gross, 2002)	…	66.7
Adult illiteracy rate (percent, ages 15 and above, 2002)	…	97.2

Sources: Data provided by the Maldivian authorities; *Statistical Yearbook of Maldives* , various years; *World Development Indicators 2005* ; and IMF staff estimates and projections.

MALDIVES: STATISTICAL ISSUES

While data provision for surveillance purposes is adequate overall, staff's analysis was affected by shortcomings in certain areas. The Maldives has improved its macroeconomic statistics in recent years, with technical assistance from STA and the Asian Development Bank. However, remaining shortcomings affect the balance of payments, government finance and national accounts statistics. The authorities have requested assistance from the Fund in the areas of balance of payments and government finance, in addition to the ongoing assistance on monetary statistics. Also, the authorities are receiving assistance from other agencies to improve the national accounts. The main official statistical publication is the *Statistical Yearbook of Maldives*, which contains some data series up to 2004. APD also receives, albeit with a lag, the *Quarterly Economic Bulletin* and the *Annual Report* of the Maldives Monetary Authority (MMA).

Real sector

National accounts statistics are available only on an annual basis and with a considerable lag, and there are inconsistencies between GDP data from the production and expenditure sides. The AsDB is assisting the authorities in setting up a framework for compiling more comprehensive national accounts. The CPI has been compiled since June 1995 based on the 1993 income and expenditure survey. In 1996, a STA consumer price statistics mission recommended that the authorities develop additional price indices for a more comprehensive analysis of inflation. As 1995 is still used as the base year, the CPI may not reflect current consumer spending patterns.

Fiscal sector

General government data are reported for publication in the *GFS Yearbook* and the latest published data are for 2005. Data on the operations of state enterprises are limited.

Monetary sector

Comprehensive data on the monetary sector are published in the *Quarterly Economic Bulletin* and the *Annual Report*, with a significant lag. Data for the accounts of the MMA, commercial banks, and interest rates are reported to the Fund for publication in *IFS* on a regular and timely basis. There are inconsistencies between monetary and fiscal data regarding the financing of the fiscal deficit which involve issues of timing and coverage. The STA monetary and financial statistics mission that visited Maldives in November 2005 completed the new standardized reporting forms for the central bank, which provide more detailed classification of certain items, fuller sectoral and instrument breakdown, and currency disaggregation. It is expected that similar reporting forms will be completed for other depository corporations (ODCs) in a follow-up mission.

External sector

Following a 1994 STA mission, a number of measures were taken to improve data coverage and quality for the balance of payments. However, problems of coverage remain. Travel receipts are still estimated on the basis of a small-sample survey of resorts/hotels to determine daily average expenditure by tourists. Estimates of profit remittances and reinvested earnings in the tourism sector are still unsatisfactory and information on private capital flows is incomplete.

Official reserves are reported monthly with a (variable) two-week lag. Predetermined outflows on foreign currency assets (mainly debt service payments) are known and reported at the time of the annual consultation missions, while other movements of foreign currency assets have not been identified. Quarterly data on external debt and debt service are available for the government and the monetary authority, and to some extent for the banking sector and state enterprises, at the time of the annual consultation missions, but no data are reported for the nonfinancial private sector.

MALDIVES: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE
As of January 23, 2006

	Date of latest observation	Date received	Frequency of data[6]	Frequency of reporting[6]	Frequency of publication[6]
Exchange Rates	8/31/05	9/26/05	M	M	M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	8/31/05	9/26/05	M	M	M
Reserve/Base Money	12/31/05	1/17/06	M	M	M
Broad Money	11/30/05	12/19/05	M	M	M
Central Bank Balance Sheet	12/31/05	1/17/06	M	M	M
Consolidated Balance Sheet of the Banking System	11/30/05	12/19/05	M	M	M
Interest Rates[2]	11/30/05	12/19/05	M	M	M
Consumer Price Index	Dec 2005	1/18/06	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2004	9/26/05	A	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	2004	9/26/05	A	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2004	9/26/05	A	M	M
External Current Account Balance	2004	9/26/05	A	M	M
Exports and Imports of Goods and Services	Aug. 2005	9/26/05	M	M	M
GDP/GNP	2004	9/26/05	A	M	M
Gross External Debt	2004	9/26/05	A	I	I

[1]Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes, and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).

INTERNATIONAL MONETARY FUND

MALDIVES

Staff Report for the 2005 Article IV Consultation

Supplementary Information

Prepared by the Asia and Pacific Department
(In consultation with PDR)

Approved by Daniel Citrin and Michael Hadjimichael

February 16, 2006

I. INTRODUCTION

1. Based on information that has become available since the issuance of the staff report (SM/06/47, 2/8/06), this supplement presents the government's announced intension to reduce substantially the risk of an overly expansionary fiscal stance in 2006 which could lead to general macroeconomic instability. The information in this supplement does not change the overall analysis and staff appraisal contained in the staff report.

II. THE 2006 BUDGET IMPLEMENTATION

2. **Recognizing the serious risks associated with the 2006 budget, the authorities have formed a Multi-Agency Macroeconomic Technical Committee (MMTC) to devise measures that can help contain the serious risks inherent in the 2006 budget**.[1] The MMTC comprises representatives of the Ministry of Finance and Treasury, Ministry of Planning and National Development, Department of Inland Revenue, and the Maldives Monetary Authority. Its tasks are to identify the risks; monitor macroeconomic developments closely; and recommend to the Minister of Finance measures to prevent significant deterioration.

3. **The MMTC has identified the following three risks**:

- **Revenues envisaged in the budget appear optimistic.** While the authorities are making strenuous efforts to tender 35 islands for resort development and collect advance lease payments from winning bidders (including by simplifying tender procedures), the Department of Inland Revenue projects that collection from this source within 2006 may

[1] See paragraphs 17-18 of the staff report.

likely be only about a half of the budgeted Rf 537 million (4½ percent of GDP).[2] In addition, the MMTC foresees legal problems in fully implementing elimination of duty waivers as envisaged in the budget with a possible shortfall of up to Rf 200 million (1⅔ percent of GDP).

- **There may be a need for additional subsidy spending**. The budget envisages a removal of the subsidy to the State Electricity Company (STELCO). STELCO estimates that tariffs would need to be raised by 45 percent for it to avoid losses; with tariffs at current levels, a subsidy of Rf 225 million (2 percent of GDP) would be required. The government has not made any decision on tariff adjustments, and if decisions are delayed further, there is a risk that some subsidy would be necessary.

- **Envisaged foreign financing may fail to materialize**. The committee mentions this risk without elaboration.

4. **The MMTC plans to monitor monthly indicators, including revenues, expenditures, foreign exchange reserves, and borrowing from the MMA, and proposes thresholds that would trigger remedial actions**. In particular, the MMTC recommends that the levels of gross official reserves and MMA borrowing by the government be two key thresholds—each having an "emerging risk" threshold and a "high risk" threshold, and contingency measures be taken when these thresholds are reached.

- For foreign reserves, the "emerging risk" threshold is set at US$170 million (2⅓ months of imports of goods and services) and corrective action would be needed if the reserves fell below this threshold (reserves at end-2005 amounted to US$187 million). More urgent remedial measures would be required if reserves fell to the "high risk" threshold of US$140 million.

- The thresholds for MMA borrowing are defined in terms of the size of overdraft from the government's Ways and Means account at the MMA. Risks would "emerge" if the government were to borrow Rf 120 million in 2006 (1 percent of GDP) and become "high" with additional borrowing of Rf 300 million.

5. **The Minister of Finance intends to implement a set of contingency measures if risks materialize.** The Minister of Finance has asked the MMTC to prepare contingency plans to forestall an impending fiscal crisis and guide him on how best to contain expenditures and increase revenues. Measures that would likely be involved are the following: (i) delaying capital projects that have not been started and are not absolutely critical for immediate development purposes; (ii) delaying ongoing projects as appropriate; (iii) restricting local and foreign travel of government officials; (iv) minimizing discretionary

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[2] There was a tendering out of three islands in January. The government intends to tender seven more islands by March, and a further ten before July.

allowances; (v) reducing budget allocations for repair and maintenance; (vi) delaying all new recruitment except the ones that the cabinet considers essential; (vii) not introducing any new subsidies and phasing out existing subsidies except those specifically targeted to the poor or those directly affected by natural disasters. The letter, however, does not explicitly state which measures should be employed to which intensity when macroeconomic risks emerge or become high—it appears that these decisions are left to key policymakers' judgments at the time, as circumstances warrant.

6. **The authorities' willingness to take action as needed is encouraging, but early implementation is critical for containing the crisis risk**. While the staff welcomes the proposed contingency measures together with the serious efforts being made to closely monitor the situation, the potential quantitative impact of these measures on the budget balance remains uncertain. The staff stresses the need to implement corrective measures early to reduce the deficit and contain the risk of a potential crisis.

Statement by Mr. Shaalan on the Maldives
Executive Board Meeting
March 4, 2005

At the outset, I would like to convey the Maldives authorities' sincere gratitude for the Board's decision to extend post-conflict emergency assistance to those PRGF-eligible countries hit by natural disasters and their appreciation for staff's valuable and prompt follow up. This decision and the staff's recent mission assessing economic developments in the wake of the tsunami disaster have not only paved the way for a request for emergency assistance but provided necessary information for potential donors.

Regarding the staff report, the authorities are in broad agreement with the analysis and the thrust of the policy recommendations contained in the well-balanced and concise report.

As highlighted in the recent briefing note on the preliminary assessment of the macroeconomic impact of the tsunami disaster, circulated to Executive Directors on February 4th, the Maldives is one of three countries that was most seriously affected by the disaster. In this regard, it is important to note that although the absolute financial loss was smaller than other affected countries, relative to its GDP, the Maldives was by far the hardest hit. Moreover, the tidal waves have seriously affected the two top economic activities of the country, namely, tourism and fisheries.

Pre-Tsunami Economic Performance

For a number of years the Maldives made significant progress on many fronts while maintaining a stable macro environment. Growth rates were consistently high, averaging 8 percent over the last three years, contributing to a doubling in per capita income over a decade, while inflation was generally kept under control. Economic projections indicate that these favorable developments were expected to continue into 2005.

Despite this strong performance, the country remains vulnerable to external shocks on account of its high dependence on tourism and tuna exports. Significant private sector credit, including new lending for investment by tourist resorts, reflects the country's focus on expanding the main productive sectors, so as to lessen the need for concessional resources to make further social and economic strides. Supported by concurrent structural reforms such as the Land Act, the new investments, as well as increased consumption, led to a sharp acceleration in imports, widening the current account deficit to 12 percent of GDP despite the strong growth in exports. The stock of debt has edged up slightly on account of lower concessional financing and growing investment needs. International reserves, though in our view small, given the vulnerabilities the economy is subject to, increased to just over US$200 million (equivalent to 3½ months of 2004 imports).

Fiscal performance in 2004 was strong. Despite falling grants, the current revenue base increased by 1 percent of GDP. This pick up was on account of an expansion in tourism and revenue measures, thus resulting in halving the deficit of recent years in spite of growing current expenditures. The revenue increase was associated with rising current expenditures of equal magnitude, predominantly due to the first increase since 1999 in civil servant salaries, but was offset by lower spending on other items.

In the case of other structural reforms, and as recommended by staff, the proposed amendment of the Maldives Monetary Authority (MMA) Act is likely to increase central bank independence by separating the functions of the Minister of Finance and Governor of the MMA. In addition, a financial intelligence unit has been set up at the MMA and the proposed legal limits on lending to government are now in parliament. The latter will necessitate finding new sources of financing without burdening debt sustainability. Other financial sector reforms are underway.

Recent Developments since the Tsunami

The steady course of progress set last year was brought to, hopefully, a short halt by the tsunami disaster, which hit on December 26, wrecking havoc to vulnerable groups while damaging the infrastructure supporting the two main productive sectors. About a quarter of tourist resorts were affected and closed, resulting in a sharp fall from previously full occupancy rates. About one-tenth of the fishing fleet and some processing facilities were damaged or lost. Consequently GDP growth is likely to fall from the pre-tsunami projection of 6½ percent to only 1 percent this year, as these key productive sectors are not expected to recover to their pre-tsunami levels until the mid-year or toward year-end.

In addition to the virtual collapse in major economic activities, the international community has estimated reconstruction costs at about US$400 million (about 50 percent of GDP), of which US$110 million are needed immediately for budgetary needs. While the government is taking all measures possible to close the budget financing needs through revenue measures and already pledged donor grants, the balance of payments gap cannot be closed.

The balance of payments shortfall due to losses in export receipts and tourism earnings is estimated at about US$160 million and cannot be fully covered by identified inflows. Therefore, a request for a purchase of an amount equivalent to SDR 4.1 million (50 percent of quota) under the Fund’s policy for emergency and natural disaster assistance is being made given that international reserves are low. This purchase is intended to leverage in the remainder of US$91 million shortfall in the balance of payments thus obviating a precipitous fall in reserves. Given the current debt level and fiscal tightness, the authorities have requested the provision of subsidies to reduce the rate of charge down to 0.5 percent per annum on this Fund purchase.

Although the authorities have acted promptly in managing the losses and associated relief efforts, and are very grateful for the international support received so far from the Asian Development Bank, the World Bank, the United Nations, and Japan, more is needed. For their part, in consultation with staff and as set out in their letter, they will refrain from granting import duty waivers for tourism, reorient capital and non-wage spending toward reconstruction needs, and refrain from awarding any new wage increases. In addition, the "bed tax" was increased late last year as planned, which should further contribute to an enhancement of revenues once tourism picks up.

The authorities are now awaiting the outcome of a meeting at the Asian Development Bank in Manila on March 18th before considering a call for a consultative group meeting to seek donor pledges to close the US$91 million balance of payments gap this year. In the meantime, the country is at risk of losing the already low level of international reserves given the increased vulnerability. I would, therefore, encourage colleagues to approve this small request of SDR 4.1 million, and convey the country's request for additional concessional support to facilitate a rebound this year and in years to come thus contributing measurably to debt sustainability. Finally, I would like to confirm that the Maldives will not be seeking any debt rescheduling from the Paris Club, as most debt is to multilaterals and non-Paris Club countries.