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Statement by the Hon. **AHMED NASEER,**
Governor of the Fund for **MALDIVES**

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Governor of the Fund for Maldives

Mr. Chairman, Mr. President, Fellow Governors, Distinguished Guests, Ladies and Gentlemen

Introduction

I am honored to represent the Republic of Maldives and address the international community in the 2017 International Monetary Fund (IMF) and the World Bank Group Annual Meeting. I would like to convey my earnest appreciation to the IMF and the World Bank for the warm welcome and excellent arrangements.

During the past 35 years the Maldives has achieved remarkable economic growth, led by the impressive growth of the tourism sector. However, as a Small Island Developing State (SIDs), the Maldives faces unique challenges that act as a hurdle in enhancing sustainable and inclusive growth. I take this opportunity to convey my heartfelt appreciation for the key role played by the IMF and the World Bank in bringing these issues into highlight and working closely with us to address these issues. We will continue to give our full cooperation to pave ways in curbing these challenges and stand at a better position to achieve the Sustainable Development Goals (SDGs) by 2030.

Recent Economic and Financial Developments

As a small and an open economy, global factors that are beyond our shores have a significant influence on the Maldivian economy. The changes to the global economic environment and the financial instability following the 2008 crisis had also been deeply felt by the Maldivian economy. After almost a decade of subdued growth, the global economy has started to show signs of strengthening. Despite several uncertainties and downside risks, outlook across many regions continues to improve. In line with these positive developments, the outlook for the Maldivian economy remains largely favorable in the medium term.

Following years of uneven and stagnant growth, the Maldivian economy has started to gain momentum since the latter part of 2016 and key economic sectors recorded a strong recovery in 2016. Looking at the developments of the first half of the year 2017, the growth projections for the year remain on track and more broad-based, with all key economic sectors showing upturns, thanks to the onset of renewed global growth momentum. Tourism sector–the single largest contributor to the gross domestic product– performed robustly, underpinned by the increased number of tourists from the European market. Concurrently, the construction sector remained buoyant due to improvements in the availability of finance together with the large-scale infrastructure projects, while fisheries sector showed notable improvements. Looking ahead, GDP growth for 2017 could be even stronger than expected if the remarkable performance seen in the tourism sector at the turn of the year continues. Furthermore, the strong domestic demand, largely stemming from the continued robust growth of the construction sector, is expected to provide additional impetus to growth in 2017.

After years of low and stable inflation, prices started to pick up during the latter part of 2016. The developments in prices have been largely influenced by domestic factors, particularly the base effect of the reduction in food subsidies effective from October 2016 and also the upward revision of import duties on cigarettes effective from March 2017. Inflation is, however, expected to return to pre-policy levels towards the end of the year as the base effect dissipates. Meanwhile, the overall public finance situation of the country continues to show signs of improvements, reflecting the concerted effort to streamline government current expenditure. Fiscal policy is largely focused on addressing infrastructure bottlenecks in the country, thus government capital expenditure remains high. However, these investments are expected to lead to significant fiscal savings in the future.

Against this backdrop, the monetary policy of the Maldives Monetary Authority (MMA) is aimed at catering the financing needs of the economy to foster growth through financial deepening. The MMA's decision to reduce the minimum reserve requirement of commercial banks in the latter half of 2015 has helped to lower the cost of financing while stimulating private sector credit which showed years of stagnant growth. With the positive synergy from both the current monetary policy and cyclical changes in the economy, the performance of the financial sector remains sound and strong. Banks continue to show significant profit growth and improved asset quality with remarkable drops in non-performing loans.

Despite these positive developments, the main risks for the Maldivian economy remain on the external front. The current account deteriorated significantly in 2016, primarily reflecting sizable growth in payments made abroad coupled with a surge in imports. In particular, a large one-off payment made abroad during the latter part of 2016 resulted in a significant drop in reserves of the country. Consequently, the MMA entered into short-term liquidity arrangements to prevent any shocks in the foreign exchange market. In addition, the MMA strengthened its intervention in the foreign exchange market to maintain confidence in the system. Although the swap agreements were paid back on maturity during the first half of 2017, the proceeds from the very first sovereign bond issued by the government in the international market helped to restore reserves to an adequate level.

Risks and Policy

Although the growth rate is likely to exceed expectations in the short term, substantial downside risks continue to cloud the medium term and long term growth prospects of the Maldivian economy. The unprecedented infrastructure scale up is transformational for the economy–adding to potential growth and helping to build resilience to climate change.

Further, these investments will also help to save foreign exchange outflows and boost reserves in the long term. However, higher imports related to these capital investments are expected to further deteriorate the current account deficit in the medium term. This leaves the country with low reserve position and vulnerable to external shocks. Therefore, holistic measures are needed to boost reserves and ensure the stability of the foreign exchange market.

Furthermore, the Maldivian economy depends solely on fuel imports for its energy requirement and the share of petroleum products in imports has been increasing considerably. With the growing population in the capital city Male' and nearby regions combined with the improved living standards have significantly increased energy consumption in the country. This has been putting pressure on the country's reserves, which makes the country more vulnerable to global oil shocks.

It is noteworthy that around the globe, renewable energy has become mainstream and the adoption of solar energy at private sector and household level has been increasing at a remarkable rate. However, being a geographically dispersed country, the deployment of renewable energy is relatively costly for the Maldives. While it will have a weighty negative impact on the trade balance in the short run, the unit cost of providing the service also tends to be higher due to the limited ability to exploit economies of scale, given the small population in each island. Hence, cost of such investments poses a heavy burden on the public as well as the private sector.

In this regard, accelerating the transition to a renewable-based energy system and saving on oil bills is crucial to enable positive structural changes to the country's balance of trade and boost potential economic growth in the long term. Renewable energy will not only help to reduce oil bills, but it will promote the country into a greener nation and reduce the risks associated with climate change, which is the center play in achieving SDGs.

IMF contributions

The IMF continues to play an important role for the stability of the international monetary system and provides innovative policy recommendations for its member countries to address critical macroeconomic issues. The Maldives has been a member of the IMF since 13 January 1978. Currently, the Maldives' quota in the IMF is 21.2 million special drawing rights, representing 0.004% of the total IMF quota. The IMF continues to maintain a close relationship with the MMA and provides technical assistance on issues relating to monetary policy, balance of payment, reserve management, corporate accounting and various other issues.

It is noteworthy that the Maldives embarked on IMF Stand-By Arrangement and Exogenous Shock Facility during the financial crisis. On 4th December 2009, The IMF Executive Board approved a blended financing arrangement for the Maldives amounting to a combined SDR 57.4 million (about US$92.5 million) for a period of 36 months. The financing arrangement was intended to help the country to smoothen its adjustments following the global downturn and the economic reform policies. However, SDR 10.3 million was drawn under the arrangement and the remaining amount was not disbursed due to challenges in bringing fiscal reforms.

Conclusion

Although the Maldivian economy has started gaining growth momentum, the daunting challenges of macro imbalances and imminent risks on the external front continue to cloud medium term growth prospects. While policies are aimed at addressing the infrastructure bottlenecks in the country and to make growth more inclusive, the higher imports related to these investments combined with growing debt are putting pressure on the external reserves and the country is becoming more vulnerable to external shocks. Therefore, holistic measures such as adopting renewable-based energy system would be most helpful to maintain an adequate reserve level in the country and stave off these downside risks. Meanwhile, credible fiscal consolidations and fiscal reforms remain salient in bringing down debt and to raise the potential growth.