



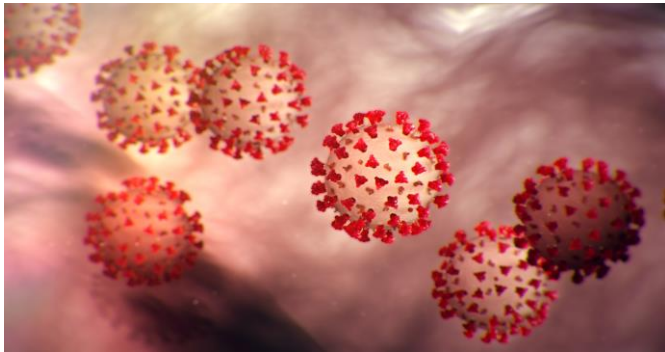
# Asia & Pacific PACIFIC ISLANDS MONITOR

April 2020

Issue 12

## *In this issue of the APD Pacific Islands Monitor:*

### ***COVID-19 Impact on Pacific Island Countries***



### ***Resident Representative Update***



### ***PFTAC News and Events***



**PACIFIC FINANCIAL TECHNICAL  
ASSISTANCE CENTRE**

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By APD Pacific Islands Division

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Yun He, Haopeng Xu & Francis Landicho (Project Coordinators) with inputs from Scott Roger, Robin Koepke, Vybhavi Balasundharam, David Kloeden, Leni Hunter, and APD Pacific Islands Mission Teams

The analysis and policy considerations discussed in this publication are those of the IMF staff and do not represent official IMF policy or the views of IMF Executive Directors or their national authorities.

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## Recent Developments

**Average real economic growth in Pacific Island Countries (PICs) remained low in 2019, while fiscal and external balances improved.** Average (unweighted) real GDP grew by an estimated 2.2 percent in 2019—down slightly from 2.4 percent in 2018. The modest decline in GDP growth masked a high degree of variance between countries. Papua New Guinea registered real growth of 5 percent, reflecting a recovery from the impact of the 2018 earthquake. Activity in Samoa benefitted from infrastructure and tourism spending for the Pacific Games in July 2019, which offset the tragic impact of the measles outbreak, while in Tuvalu activity was boosted by hosting the Pacific Islands Forum. In other PICs, growth was hampered by falling private investment and a pre-COVID slowing of tourism-related activities (notably in Nauru, Palau, and Fiji) as well as weaker logging exports (Solomon Islands). The Solomon Islands and Vanuatu were also affected by Cyclone Oma. Current account balances improved in most countries compared to the 2000-16 average and reserves coverage has been above minimum thresholds.

## COVID-19 and the Near-Term Outlook

**The onset of the COVID-19 pandemic has drastically changed the outlook for the Pacific Islands in 2020.** Compared to the October 2019 World Economic Outlook—which projected a modest increase

in the region’s average growth—eleven out of the twelve PICs are expected to record negative growth this calendar year. Average growth among the PICs is now projected at -2.7 percent in 2020, with the largest drops in activity (-6 to -13 percentage points relative to the October 2019 WEO) projected in Palau, Fiji, Samoa, and Vanuatu. More moderate drops in expected real GDP growth rates (in the -2 to -5 percentage point range relative to the October WEO) are expected in Tuvalu, the Solomon Islands, Tonga, Papua New Guinea, Nauru, the Marshall Islands, Kiribati, and Micronesia. The very recent destruction by

	Current WEO			Change vs. Oct WEO		
	2019	2020	2021	2019	2020	2021
<b>Pacific island countries</b>	<b>2.2</b>	<b>-2.7</b>	<b>3.9</b>	<b>-0.6</b>	<b>-5.3</b>	<b>1.5</b>
Fiji	0.5	-5.8	7.0	-2.2	-8.8	3.8
Kiribati	2.3	0.0	2.2	0.0	-2.3	0.2
Marshall Islands	2.4	-0.2	3.2	0.0	-2.5	1.2
Micronesia	1.2	-0.4	1.4	-0.3	-1.2	0.6
Nauru	1.0	-1.7	1.3	-0.6	-2.4	0.0
Palau	0.5	-11.9	14.4	0.2	-13.7	12.2
Papua New Guinea	5.0	-1.0	2.9	0.0	-3.5	0.4
Samoa	3.5	-3.7	0.5	0.1	-8.1	-1.7
Solomon Islands	1.2	-2.1	3.8	-1.5	-4.9	1.1
Tonga	-0.1	-1.2	1.2	-3.7	-4.9	-1.7
Tuvalu	6.0	-1.0	3.5	1.9	-5.3	-0.7
Vanuatu	2.9	-3.3	4.9	-0.9	-6.4	2.1

Source: IMF World Economic Outlook

Cyclone Harold is likely to further impact Vanuatu, Fiji, and Tonga to varying degrees.

**The sharp disruption to tourism and the global drop in both commodity prices and demand are key transmission channels from the global pandemic to the PICs.** Tourism accounts for up to 20-30 percent of economic activity in several PICs (see newly developed monthly IMF [Tourism Tracker](#)). IMF staff project that foreign visitors to Pacific Islands as a group will fall by about 40 percent this year, with the largest declines expected in Kiribati, Papua New Guinea and Vanuatu (Figure 1). This projection assumes that inflows of foreign visitors will come to a near-standstill in 2020Q2, followed by a gradual recovery in the second half of the year as the pandemic subsides and domestic and international travel restrictions ease. There is significant downside risk to this assumption, however, as the dampening

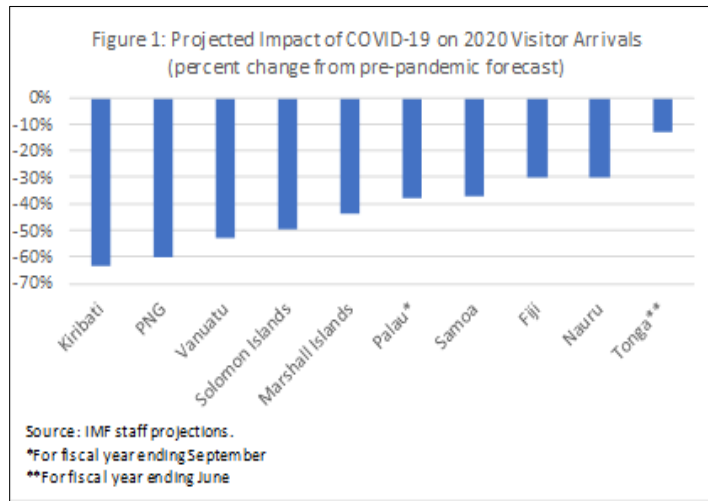
## Regional Developments and Outlook

effect on tourism from the pandemic could last longer—with negative ramifications for growth, incomes, and fiscal and external balances into 2021. Commodity prices are also a key channel affecting the PICs. Papua New Guinea’s dependence on natural gas exports is an illustrative case, with PNG now facing a projected 10 percent decline (in volume) and 24 percent decline in price for its LNG exports.

**Current account balances are also projected to deteriorate by substantial margins for many PICs.** As noted above, the

loss of tourism-related inflows is expected to have a significant negative impact on several of the PICs, particularly Palau, Fiji, and Samoa. Lower commodity prices and reduced global demand will also have a marked impact on Papua New Guinea (natural gas), and the Solomon Islands (timber). For some, the prospect of lower inward remittances may also impact the balance of payments. While reduced import prices offset some of the impact, along with lower demand (as a result of lower GDP growth), the net effect remains sharply negative. As a group, the average current account balance among the PICs is projected to deteriorate from a surplus of 7 percent of GDP in 2019 to a deficit of -5.7 percent in 2020. Foreign exchange reserve cover is also expected to decline, as external positions weaken.

**Fiscal positions will also witness a stark shift in 2020**—through lower revenues, a reduced denominator (GDP) and the need to address the impact of the pandemic through higher healthcare spending and support to vulnerable populations and hard-hit sectors. Several countries (notably Fiji, Samoa, Papua New Guinea, and Vanuatu) have already announced COVID-19 response packages, and more are expected to follow (see IMF COVID-19 Policy Tracker: <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19>).



**APD Pacific Island Countries: Current Account Balance**  
(In percent of GDP)

	2019	2020 Proj.	2021 Proj.
Fiji	-7.2	-8.2	-6.0
Kiribati	44.9	1.5	5.5
Marshall Islands	3.7	-0.9	-3.7
Micronesia	17.1	3.4	5.3
Nauru	5.0	5.2	2.7
Palau	-23.6	-30.7	-27.6
Papua New Guinea	24.1	19.8	23.1
Samoa	2.3	-6.4	-4.4
Solomon Islands	-6.4	-15.0	-14.7
Tonga	-8.9	-14.8	-15.7
Tuvalu	25.6	-11.2	-24.0
Vanuatu	7.2	-10.9	-5.6
Average	7.0	-5.7	-5.4

Source: World Economic Outlook

**APD Pacific Island Countries: Fiscal Account Balance**  
(In percent of GDP)

	2019	2020 Proj.	2021 Proj.
Fiji	-4.9	-10.6	-4.5
Kiribati	8.8	-18.7	1.0
Marshall Islands	2.0	0.3	-0.3
Micronesia	16.4	5.7	5.2
Nauru	16.1	5.3	2.5
Palau	1.9	-5.0	-2.5
Papua New Guinea	-4.1	-5.0	-3.9
Samoa	2.7	-9.1	-5.9
Solomon Islands	-2.7	-7.3	-7.8
Tonga	1.0	-2.4	-1.5
Tuvalu	-8.6	-25.5	-18.5
Vanuatu	5.3	-13.7	-4.8
Average	2.8	-7.1	-3.4

Source: World Economic Outlook

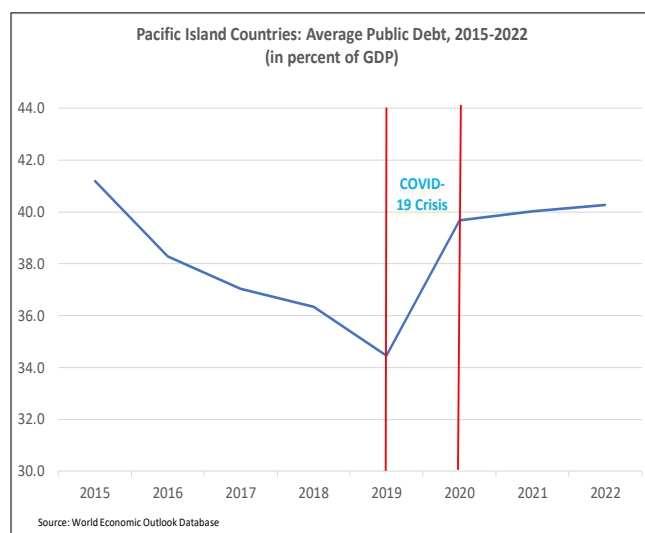
## Medium-Term Outlook and Risks

**COVID-19 will leave a deep impact on the global economy, the Pacific Islands, and low income and developing economies in general.** Looking ahead to the post-crisis environment, policy makers in the Pacific Islands may want to consider how to best place their economies for the eventual recovery and be mindful of the following issues that may remain after the pandemic recedes:

**Lower global integration and breaks in trade and value chains.** The prolonged disruption to global economic activity will have some lasting (but not permanent) impact on trade and supply/demand chains. This will mean both challenges and opportunities for the private sector in the aftermath of COVID-19 and the reestablishment (or creation of new) business relationships and supply chains.

**Lower potential growth.** The sharp reduction in economic activity as a result of the current pandemic has potential implications for potential output, depending on the depth and length of the crisis, and sector-specific effects (such as on tourism flows and trade/value added chains). Short-term shocks are generally manageable without a decrease in potential output. But the COVID-19 crisis may cause more permanent damage to selected industries. This is particularly the case if the effects of the pandemic extend into and beyond 2021.

**Higher public debt.** Given the shock to fiscal balances, the need for counter-cyclical and counter-COVID short-term spending, and uncertainty regarding the timing and speed of the recovery, many Pacific Islands (and small states in general) will face higher debt-to-GDP levels in the future. With a number of PICs already in elevated or moderate risk of debt distress, new thinking will be needed about how to address the debt run-up and potential solutions that do not impede a durable improvement in living standards over time.



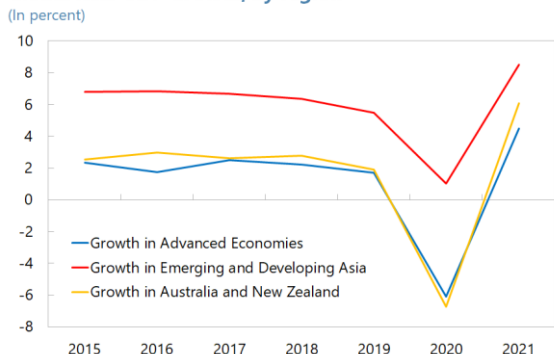
**Lower foreign exchange reserves.** The expected sharp deterioration in external balances in 2020 are expected to put a dent in PIC's foreign exchange buffers. A fresh look at reserve adequacy after the COVID crisis, may be warranted in some cases. In light of expected balance of payments needs, several PICs have accessed support under the IMF's emergency financing facilities.

**Financial sector stress.** Banks may face losses on their loan portfolios due the impact of the crisis. The overall impact will depend on the severity of the virus spread as well as the magnitude of the economic and financial impact on the bank. It will be critical to measure NPL and potential losses as accurately as possible, and banks should not be encouraged to hide losses (creating moral hazard and transparency issues). Banks' capital and liquidity buffers should be the first line of defense, but in some cases additional financing or extending further credit to impacted firms could be part of the loan restructuring process in line with prudent risk management principles.

# Regional Developments and Outlook

Global growth is set to take a major shock from the COVID-19 pandemic.

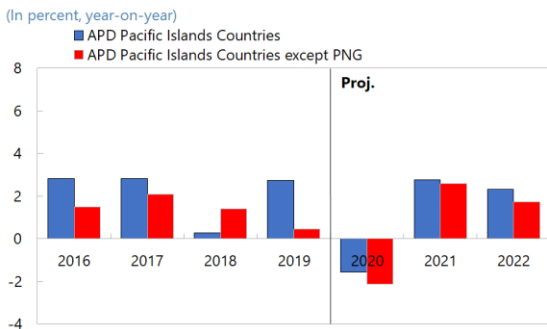
## Global Real GDP Growth, by region



Sources: World Economic Outlook

Pacific Island Countries also to register significant decline in GDP growth in 2020.

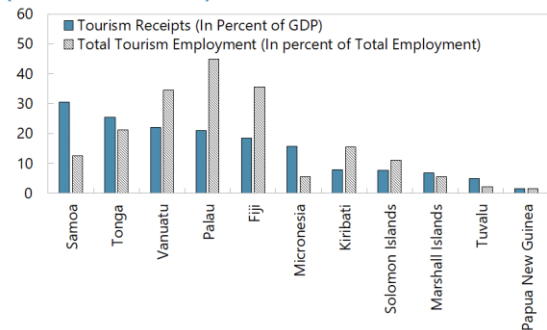
## Real GDP Growth in Pacific Island Countries



Sources: IMF, World Economic Outlook, and staff calculations.

For several PIC countries, tourism accounts for substantial part of growth and employment

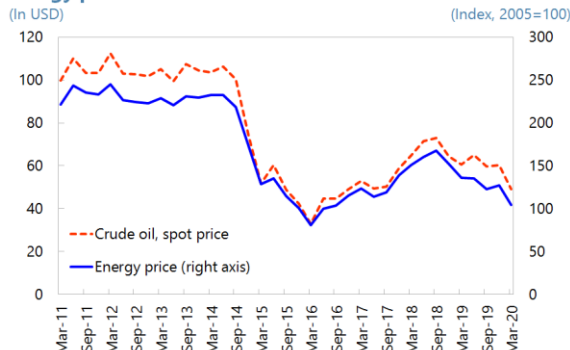
## Pacific Island Countries- Tourism Receipts and Employment (Latest available data)



Sources: NTOs, NSOs, and SPTO.

Commodity prices reflect downward shift in demand (as well as supply issues)

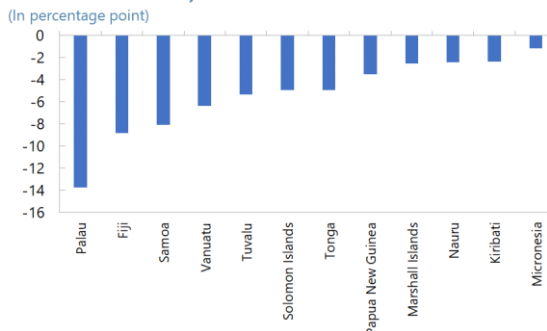
## Energy prices



Sources: World Economic Outlook Database.

Revisions vary across countries, with heaviest impact on those with reliance on tourism

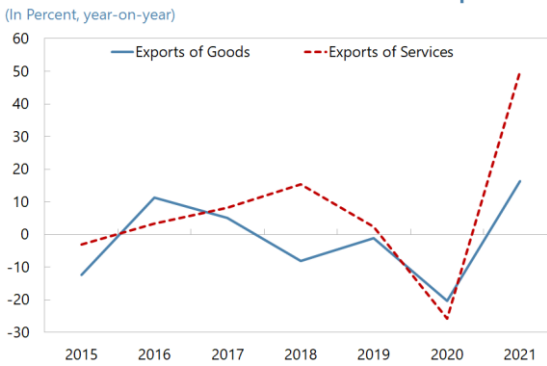
## WEO Revisions to PIC GDP Growth Projections (versus October 2019 WEO)



Sources: World Economic Outlook database.

But both goods and services exports will be affected by current crisis.

## Pacific Islands Countries' Goods and Services Exports

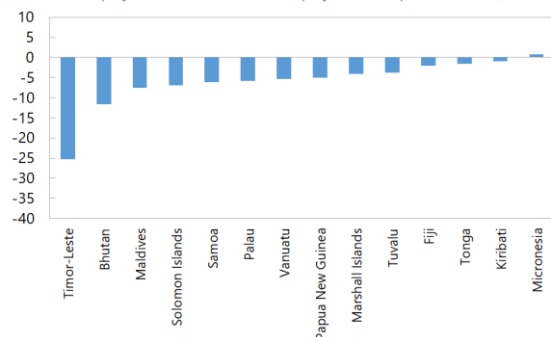


Sources: World Economic Outlook Database.

External accounts will bear heavy brunt of COVID-19 pandemic impact

## Change in Current Account Balances

(Current WEO projections v.s. October WEO projections; in percent of GDP)

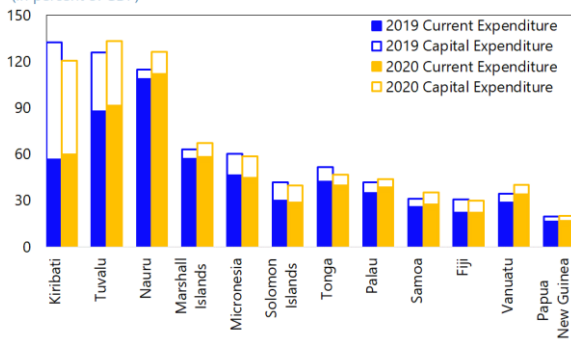


Sources: World Economic Outlook Database.

COVID-19 crisis and need for policy response will also have a fiscal impact.

## Current and Capital Expenditure

(In percent of GDP)

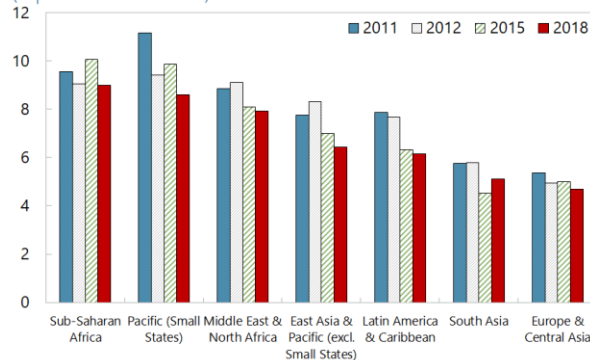


Sources: Countries authorities; and IMF staff estimates and projections.

The Pacific region continues to grapple with correspondent banking relation issue and cost of remittances.

## Cost of Remittance by Destination Region

(In percent of amount sent)

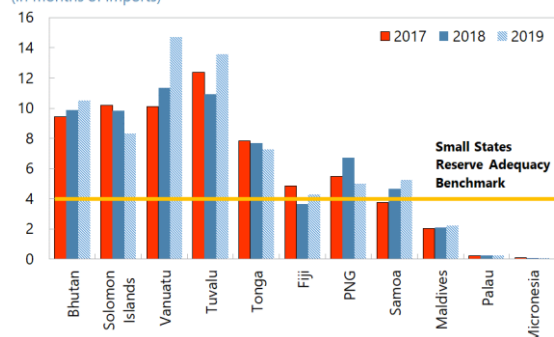


Sources: World Bank, Remittance Prices Worldwide; and IMF staff calculations.

Impact on reserves will be material for some PICs, and a potential concern for reserve adequacy in some cases

## Official Reserves

(In months of imports)



Sources: World Economic Outlook Database.

Fiscal response will eventually impact public debt levels, and potentially level of debt risk.

## Pacific Island Countries' Public Debt

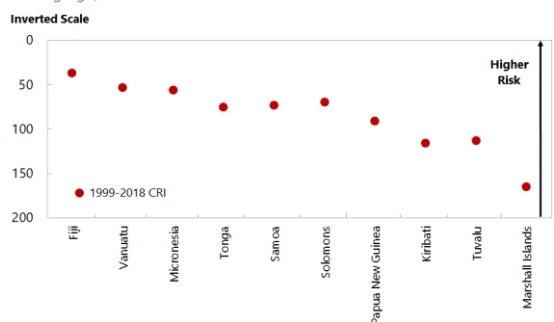
	2019 (In percent of GDP)
<b>Pacific island countries</b>	34.5
Fiji	48.0
Kiribati	21.2
Marshall Islands	21.9
Micronesia	17.0
Nauru	62.1
Palau	35.3
Papua New Guinea	38.4
Samoa	47.6
Solomon Islands	11.7
Tonga	40.9
Tuvalu	19.5
Vanuatu	49.9

Source: World Economic Outlook database.

As well as ongoing risk from natural disasters and climate-induced risks.

## Long-Term Climate Risk Index for Pacific Island Countries

(Countries with lower CRI scores are more impacted and should consider the CRI as a warning sign)



Source: Global Climate Risk Index 2020.

## Resident Representative's Corner

**By Leni Hunter, Resident Representative of Pacific Island Countries Pacific**

Bula Vinaka, Kia Orana,



Greetings to all at this challenging time, due to both the coronavirus and also the devastating impacts of TC Harold. We are glad that covid-19 has not reached several Pacific Island countries and hope that remains the case. Nonetheless, the Pacific has been deeply affected, with confirmed cases in two member countries. In Fiji we currently have 17 cases, and the authorities are making strong efforts to keep the virus contained.

With borders closed for now, I am finally catching up to the rest of the Res Rep office team, on learning how to use video conferencing. In that sense the crisis has improved our ability to work closely with country authorities and colleagues in Washington. I think and hope that many of the changes we are making now will lead us to work more efficiently in the post-covid environment.

During the second half of 2019 and early 2020 our office participated in several missions. Reshika Singh and I joined the Nauru Article IV in September 2019, and Jacinta Hesaie joined the PNG team in Port Moresby in late October. The Samoa AIV consultation occurred in February 2020, one of the last Fund missions to occur before travel restrictions tightened. I joined the Article IV in Apia, and Reshika participated from Suva.

In November 2019, I travelled to Vanuatu with mission chief Dirk Muir for a staff visit, and to attend the second South Pacific Central Bank Research Conference, with Alison Stuart. Alison discussed the Fund's work with Pacific island countries, including on climate change and correspondent bank relationships, and I spoke about the region's success in increasing fishing license revenues.

Two new economists started in late 2019, Devendra Narain and Seruwaia Cagilaba, giving us a team of three local economists along with Reshika, as well as our admin team Pule and Peter. Devendra and Seruwaia have joined the PNG and Vanuatu teams, respectively. Jacinta has returned to the Reserve Bank of Fiji in a management role, and we thank her again for her highly valued contribution.

For the time being we are all working from home here in Suva. We will see you at the next conference call and look forward to when we can meet again in person.

With best wishes, Leni Hunter



Nauru.



Participants from the South Pacific Central Bank Research Conference, Port Vila.

By David Kloeden, PFTAC Coordinator



## **PFTAC was on track to a record level of CD delivery in FY2020 until COVID-19 restrictions began in February.**

Through technology, innovation, and the patience of PFTAC member countries, some missions were delivered remotely with more innovation to come. Nevertheless, the late postponement of 22 missions reduced the projected FY2020 CD delivery from 90 percent outturn to 78 percent. Projected budget utilization is 85 percent given fewer postponed training events, non-CD related expenses such as the external evaluation, and prepaid travel costs for postponed missions. The draft 2020 PFTAC Annual Report is available at: <https://www.pftac.org/content/PFTAC/en1/reports.html> along with the detailed FY2020 workplans and their projected outturn plus the proposed FY2021 workplans pending lapse of time (LoT) Steering Committee (SC) endorsement given the unavoidable cancellation of the 2020 SC meeting that Niue was to host in late March.



## **Phase V fundraising is secure with the generous contribution of CA\$1.5million when Canada joined the PFTAC community in November 2019 as the sixth and newest donor partner.**

The first contribution was also received from the Marshall Islands following their signature of a Letter of Understanding leaving only two member countries yet to financially pledge support to PFTAC operations. Funding certainty through April 2022 enabled the SC to provide LoT endorsement to a one-year extension of the Government Finance Statistics (GFS) program that members requested as well as secretariat support that PFTAC is providing to a time-bound Know Your Client (KYC) initiative for the Pacific Central Bank governors against the loss of Correspondent Banking Relationships (CBR).

## **PFTAC's public financial management (PFM) program has been innovatively at the forefront of several key initiatives.**

Tonga benefited from two new approaches under the Public Expenditure and Financial Accountability (PEFA) framework with the streamlined use of an 'agile' assessment methodology along with the first application of gender responsive PFM module. PFTAC contributed to Tonga's Climate Change Policy Assessment (CCPA) in February 2020, and is working with regional partners and the Pacific Island Forum Secretariat (PIFS) towards a PEFA climate change module. In December 2019, Pacific, Caribbean, and Indian Ocean small island states came together in Washington for a joint PFTAC/CARTAC seminar on Public Finance and Climate Resiliency seminar hosted by the Fiscal Affairs Department (FAD) and financed by the Government of Japan. Finally, a FAD review of the PFTAC PFM program since 2010 is making good progress towards a Working Paper due by mid-2020.

**Recent PFTAC staff changes include a new Macro advisor, Mr. Andrew Beaumont** (pictured left) succeeding Ms. Iris Claus after a five-year assignment. After more than 25 years PFTAC service, Ms. Nina Samuela was promoted to the newly created position of Office Manager, and Ms. Pretti Lata was recruited to replace Mr. Josaia Nakete. The intended April transfers of two PFTAC advisors (Financial Sector Supervision expert Benjamin Stefanou and PFM advisor Celeste Kubasta) to other CD centers and recruitment of their successors is on hold until after the COVID-19 crisis. Meanwhile, all PFTAC staff have been working remotely from their homes since late March, and stand ready to respond flexibly and innovatively to the changing needs of the PFTAC membership during these challenging times.





### **Strategy for Fintech Applications in the Pacific Island Countries**

*Prepared by Sonja Davidovic, Elena Loukoianova, Cormac Sullivan, and Hervé Tourpe*

The Bali Fintech Agenda highlighted 12 principles for policymakers to consider when formulating their approaches to new financial technology (fintech). The agenda aims to harness the potential of fintech while managing associated risks. This paper looks at how some elements of the Bali Fintech Agenda could be used in Pacific island countries, which face significant financial-structural challenges.

<https://www.imf.org/en/Publications/Departmental-Papers-Policy-Papers/Issues/2019/08/21/Strategy-for-Fintech-Applications-in-the-Pacific-Island-Countries-46862>

### **Fiscal Buffers for Natural Disasters in Pacific Island Countries**

*Prepared by Hidetaka Nishizawa, Scott Roger, Huan Zhang*

Pacific island countries (PICs) are vulnerable to severe natural disasters, especially cyclones, inflicting large losses on their economies. In the aftermath of disasters, PIC governments face revenue losses and spending pressures to address post-disaster relief and recovery efforts. This paper estimates the effects of severe natural disasters on fiscal revenues and expenditure in PICs. These are combined with information on the frequency of large disasters to calculate the rate of budgetary savings needed to build appropriate fiscal buffers. Fiscal buffers provide self-insurance against natural disaster shocks and facilitate quick disbursement for recovery and relief efforts, and protection of spending on essential services and infrastructure. The estimates can provide a benchmark for policymakers and should be adjusted to take into account other sources of financing, as well as budget risks from less severe as well as more frequent disasters.

<https://www.imf.org/en/Publications/WP/Issues/2019/07/12/Fiscal-Buffers-for-Natural-Disasters-in-Pacific-Island-Countries-47011>

### **Report on the Pacific Roundtables: Actions to Address Correspondent Banking and Remittances Pressure**

*Prepared by Alison Stuart, Jihad Alwazir, Yan Liu, Scott Roger, Si Guo, Chau Nguyen, Emmanuel Mathias, and Jonathan Pampolina*

The paper looks at feasible concrete action that can be taken by correspondent and respondent banks, money transfer operators, the Pacific authorities, the Australian and New Zealand authorities, and international organizations.

<https://www.imf.org/en/Publications/Departmental-Papers-Policy-Papers/Issues/2019/05/01/Report-on-the-Pacific-Roundtables-Actions-to-Address-Correspondent-Banking-and-Remittances-46734>