INTERNATIONAL MONETARY FUND

SAMOA

REQUEST FOR DISBURSEMENT UNDER THE RAPID CREDIT FACILITY—DEBT SUSTAINABILITY ANALYSIS

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This joint IMF-WB debt sustainability analysis (DSA) shows that Samoa has shifted from moderate to high risk of debt distress. This conclusion is based on the finding of a large and protracted breach of the present value (PV) of debt to GDP threshold in the baseline scenario. This elevated debt risk largely reflects the expected high levels of fiscal deficits during the post-cyclone reconstruction period and a lower discount rate used in calculating the present value of debt compared to the previous DSA (see the 2012 IMF Article IV Staff Report). The cyclone-related expenditures come on top of large fiscal outlays necessitated by the tsunami of 2009. Forceful fiscal consolidation in the post-reconstruction period and policies to raise growth will be needed to reduce Samoa's debt to more sustainable levels.

BACKGROUND

1. **Samoa is faced with lower growth in 2012/13 as a result of the impact of tropical cyclone Evan.** After more than two years of steady recovery from the devastating effect of the 2009 tsunami and the global financial crisis, GDP growth is likely to slow to about 1 percent in 2012/13, about one percentage point lower than the pre-cyclone forecast. The cyclone has caused wide-spread losses of output, most significantly in agriculture and tourism. Ensuing reconstruction activity is expected to boost growth in the next two years, but medium- and longer-term growth is likely to be moderate, at around 2½ percent.

2. **Samoa is in need of external assistance to meet the resource requirements for reconstruction.** Total resource requirements for reconstruction over the period

2012/13-2014/15 (July/June) are estimated at SAT 393 million, or 24½ percent of GDP. Preliminary estimates indicate that development partners may contribute an amount equivalent to 10 percent of GDP over the period, while expenditure reprioritization could create a fiscal space equivalent to 7½ percent of GDP, and insurance payments about 1½ percent of GDP. Taking into account the estimated losses of revenue of about ¾ percent of GDP, this leaves a financing gap of about 6½ percent of GDP. These additional resource requirements follow a period of high fiscal outlays necessitated by an earlier natural disaster, the tsunami of 2009, which had resulted in elevated debt levels.

3. **At the end of 2011/2012, the face value of public external debt was estimated at SAT 864.6 million (55.5 percent of GDP).** Multilateral creditors account for 63 percent of total external debt (including 27 percent owed to the World Bank, 34 percent to ADB, and 3 percent to OPEC, IFAD, EEC and EIB). Bilateral creditors account for approximately 37 percent of the total (China 30 and Japan 7). The non-concessional loans from OPEC attract interest rates ranging from 2.75 to 4.5 percent while other loans have interest rates ranging from 0.45 to 2.5 percent.

4. **As most of Samoa's external debt is concessional, the overall grant element of its debt stock is relatively high and the debt service burden is relatively low.** However, with the recent reduction of the Commercial Interest Reference Rate (CIRR) from 4 percent to 3 percent, the grant element of Samoa's debt stock has fallen significantly. This has led to a higher present value of future debt repayment streams.

5. **The central government's net domestic debt is small, totaling about SAT 42 million (2.7 percent of GDP)**. Treasury bonds outstanding are worth only SAT 0.4 million with interest rates ranging from 5 to 7 percent. The government has assumed responsibility for servicing a number of state-owned enterprise (SOE) loans that are in default with an outstanding balance of SAT 41.8 million at the end of 2011/12. SOE liabilities, although backed by their assets, represent a fiscal risk to the government. Total current liabilities are reported to be about SAT 100 million at the end of 2009/10 and non-current liabilities at SAT 270 million. Not all SOE balance sheets were available as of end-2010/11.

METHODOLOGY AND ASSUMPTIONS

6. **Debt sustainability is assessed in relation to policy-dependent debt burden thresholds**. Samoa is considered to have had strong governance in place and a strong policy reform environment since the mid-1990s;[1] therefore the country is assessed against a higher threshold compared to countries that have weaker governance and policy environment.[2]

[1] Three-year average CPIA rating for Samoa is 4.10.

[2] According to the 2012 review of the Debt Sustainability Framework for Low Income Countries, the thresholds for "strong performers" are: 50 percent for PV of debt to GDP; 200 percent for PV of debt to exports; 300 percent for PV of debt to revenues; 25 percent debt service to exports; and 22 percent debt service to revenues.

7. This DSA is based on updated data provided by the authorities and estimates by the staffs. The DSA uses non-reconciled debt data and a single discount rate of 3 percent, reduced recently from 4 percent based on global interest rate developments.

8. Key assumptions underlying the baseline DSA are consistent with the macroeconomic framework developed for the post-cyclone scenario during the 2013 mission. These assumptions are as follows:

- Annual real GDP growth is projected at 0.9 percent for 2012/13 and 3.1 percent for 2013/14. Growth is expected to decline to about 2½ in 2014/15 and remain at that level over the medium and longer term. This is considered to be the potential growth rate for Samoa, which is higher than the average GDP growth rate of 1.0 percent for 2005/06-2011/12, but lower than the average growth rate of 4.8 percent during the period 1997/98-2004/05. The lower potential growth rate reflects the adverse impact of a series of shocks over the past few years and the current policy environment.

- Average inflation of about 2.0 percent is projected for 2012/13 taking into account the high inflation of 6.2 percent in 2011/12. Price increases are expected to remain low, at about 1.5 percent, in 2013/14. Over the medium term, inflation is assumed to move back to the trend level of 4 percent before falling to 3 percent over the longer term, in line with the target of the Central Bank of Samoa.[3]

- The real exchange rate is assumed to remain unchanged, with exchange rate shocks taken into account in stress tests.

- Annual growth of goods and services exports is assumed to be broadly in line with GDP growth. The external non-interest current account deficit is projected to remain at around 12 percent of GDP over time.

- Fiscal projections are in line with the government's targets, which include fiscal consolidation over the medium term. Revenues and grants are assumed to remain constant as a share of GDP at about 39 percent, and development expenditure is expected to fall back to about 13 percent of GDP over the medium and long term, financed primarily by grants and concessional loans. Current expenditure is assumed to level off at about 26 percent of GDP over the medium term, following a gradual decline from 32 percent of GDP in 2012/13. The fiscal deficit is projected at about 7-8 percent of GDP over the period 2012/13-2014/15 and then gradually decline to 2 percent of GDP over the medium term and decline further to 1 percent of GDP over the long run.

[3] Historically inflation has averaged more than 4 percent. The authorities are targeting inflation of 3 percent over the longer term.

- New external borrowings to finance fiscal deficits are assumed to be mostly on concessional terms. These borrowings include possible budget support from multilateral development partners, which are preferred over other sources of less concessional borrowings. SOE borrowings are assumed to be on commercial terms.

- It is assumed that ADB and IDA financing will include a combination of grants and concessional loans.

- A constant level of nominal debt (in percent of GDP) is assumed for SOEs for the projection period.

EXTERNAL DEBT SUSTAINABILITY

9. **Based on these assumptions, Samoa is assessed to have shifted from moderate to high risk of debt distress.** The PV of Samoa's external debt is projected to exceed the policy-dependent threshold of 50 percent of GDP for a period of 9 years (Figure 1; Tables 1a and 1b). The PV of debt to GDP ratio is likely to breach the threshold in the current fiscal year and remain above the threshold for the next 8 years, with a peak value of over 58 percent in 2015/16. This is a qualitative departure from the result of the last DSA, which showed a breach of the threshold only in an exchange rate shock scenario. In addition to the effect of the reduction in the discount rate in calculating the PV of debt, this elevated debt risk reflects the additional borrowings required to finance post-cyclone reconstruction plans.

10. **A "historical" scenario, which replicates the past performance of key economic variables, yields debt ratios that are below the baseline projections (Figure 1).** Samoa has historically had sound macroeconomic policies supported by an array of structural reforms that had resulted in a period of strong growth and low fiscal deficits. However, there was a significant decline in economic growth in years just preceding the global financial crisis. Samoa also suffered major setbacks on growth and public finance when a tsunami hit in 2009, followed by the recent cyclone.

11. **Samoa's PV of debt to GDP ratio is vulnerable to exogenous shocks.** The most extreme stress test scenario of a 30 percent exchange rate depreciation, leads to the 50 percent threshold being breached for the entire forecast period.

12. **Measured by the PV of debt to exports ratio, Samoa's debt burden has also increased significantly.** Even in the baseline scenario, this ratio is projected to approach the policy-dependent threshold of 200 percent over the medium term. If loan terms and conditions are unfavorable to Samoa during the forecast period, the ratio could well exceed the threshold for a protracted period of time. A similar increase in the debt burden is observed when measured by the PV of debt to revenue ratio, although there is no breach of the threshold even in the shock scenarios. Samoa's strong performance in revenue collection makes it more resilient in this respect.

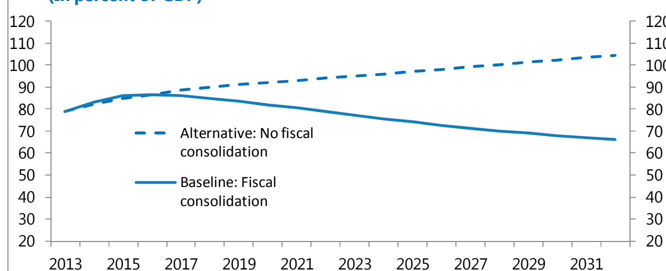
13. **Samoa's debt service burden is expected to remain relatively low.** As shown in Figure 1, even in the shock scenarios, Samoa remains well below the debt service to exports and debt service

to revenue thresholds. This clearly reflects the benefits of Samoa's strategy of minimizing non-concessional borrowings and its strong revenue efforts and the importance of the tourism industry in generating foreign exchange earnings. Samoa's debt service capacity is further supported by large inflows of remittances, which have been shown to be counter-cyclical.

PUBLIC SECTOR DSA

14. The public sector debt analysis supports the conclusions drawn from the external debt analysis (Figure 2; Tables 2a and 2b). The nominal value of public sector debt stock is estimated at 84 percent of GDP in 2011/12 (73 percent of GDP in PV terms) and is expected to rise to 99 percent of GDP (87 percent of GDP in PV terms) by 2015/16.[4] This rising burden of public debt is not surprising given that Samoa's public debt is dominated by external loans. Nevertheless, this assessment again highlights the central role of fiscal policy in determining Samoa's overall debt burden. Should Samoa fail to consolidate its fiscal position, as shown in the text graph above, public debt would increase rapidly and become unsustainable. Recent efforts to privatize some SOEs and to make all public enterprises more accountable for their financial performance are encouraging, but much more remains to be done.

NPV of Public Sector Debt under Different Alternatives
(In percent of GDP)



Source: IMF staff calculations.

CONCLUSION AND STAFF ASSESSMENT

15. Samoa is now faced with a high level of debt distress risk as a result of the sharp increases in external borrowings to deal with exogenous shocks. This underlines the importance of prudent borrowing even on concessional terms as well as the need to strengthen resilience to exogenous shocks. Samoa's experience also highlights the importance of building policy buffers in good times. The country's debt situation would have been much worse if it had not substantially reduced its debt prior to the recent shocks.

16. Samoa will need to develop a credible deficit-reduction strategy to bring its public debt to more sustainable levels over time. Central to this strategy is a commitment to a medium-term fiscal framework that spells out a path of declining fiscal deficits over time, supported by rigorous implementation of corresponding fiscal targets, including external borrowing targets, through the annual budgets. Further improvements in debt management will help minimize

[4] Public sector debt includes all external debt of the central government, including on-lent amounts, domestic debt of the central government, defaulted loans of SOEs and SOE current and non-current liabilities excluding government on-lent amounts and inter-SOE loans.

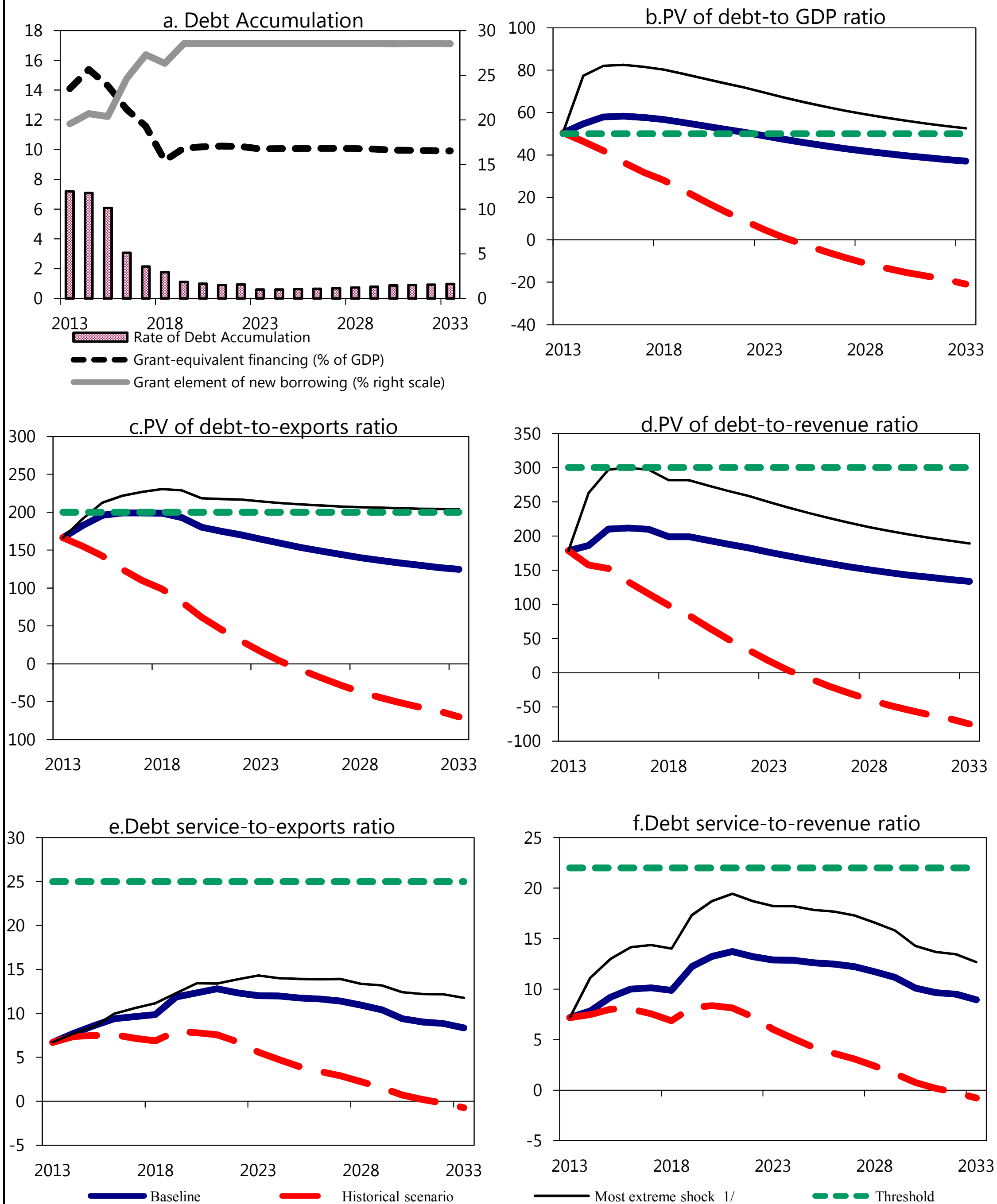
borrowing costs and reduce debt risks, as well as support fiscal consolidation by providing timely information on the country's debt burden.

17. Continued structural reforms will be important to reducing the debt burden. Faster economic growth based on a strong reform agenda should be part of the overall strategy to reduce public debt as well as to raise living standards and reduce poverty. In this regards, SOE reforms are particularly important, as they help reduce contingent liabilities, strengthen the government's fiscal position by generating more revenue and reducing subsidies, and release more resources for private sector development.

AUTHORITIES' VIEWS

18. The authorities recognize the risks posed by the high and rising level of public debt and are committed to bringing it down to more sustainable levels. They agreed that it is critical to formulate and implement a credible fiscal consolidation plan and to strengthen debt management. The authorities also attach great importance to structural reforms, and have agreed on a matrix of policy actions with key development partners toward this end.

Figure 1. Samoa: Indicators of Public and Publicly Guaranteed External Debt under Post - Cyclone Scenario, 2013-2033 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in 2023. In figure b. it corresponds to a One-time depreciation shock; in c. to a Terms shock; in d. to a One-time depreciation shock; in e. to a Terms shock and in figure f. to a One-time depreciation shock

Table 1a. Samoa: External Debt Sustainability Framework, Baseline Scenario, 2010-2033 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 6/	Standard Deviation 6/	Projections									
	2010	2011	2012			2013	2014	2015	2016	2017	2018	2013-2018 Average	2023	2033	2019-2033 Average
External debt (nominal) 1/	**49.5**	**50.1**	**55.5**			**61.8**	**66.8**	**70.6**	**70.9**	**70.2**	**69.0**		**61.1**	**48.7**	
o/w public and publicly guaranteed (PPG)	49.5	50.1	55.5			61.8	66.8	70.6	70.9	70.2	69.0		61.1	48.7	
Change in external debt	11.4	0.6	5.4			6.3	5.0	3.8	0.3	-0.7	-1.2		-1.8	-0.9	
Identified net debt-creating flows	4.4	1.7	5.6			10.8	13.1	12.7	10.9	9.2	7.8		10.0	11.4	
Non-interest current account deficit	**6.8**	**3.3**	**8.5**	**8.3**	**3.3**	**12.4**	**15.4**	**14.7**	**12.9**	**11.2**	**9.8**		**11.7**	**12.0**	11.8
Deficit in balance of goods and services	26.9	23.1	28.2			31.1	33.5	32.4	30.2	28.2	26.3		28.1	28.1	
Exports	32.8	33.5	32.9			30.4	29.9	29.6	29.3	29.0	28.6		29.8	29.8	
Imports	59.7	56.5	61.2			61.4	63.4	61.9	59.4	57.1	54.8		57.9	57.9	
Net current transfers (negative = inflow)	-22.5	-22.8	-23.6	-22.4	1.4	-23.3	-22.6	-22.2	-21.8	-21.6	-21.2		-21.1	-21.1	-21.1
o/w official	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other current account flows (negative = net inflow)	2.4	3.0	3.9			4.7	4.5	4.5	4.6	4.7	4.7		4.8	5.0	
Net FDI (negative = inflow)	**-0.2**	**-1.2**	**-1.4**	**-2.2**	**2.9**	**-1.9**	**-1.2**	**-1.3**	**-1.3**	**-1.3**	**-1.3**		**-1.1**	**0.0**	-1.0
Endogenous debt dynamics 2/	**-2.2**	**-0.4**	**-1.5**			**0.3**	**-1.0**	**-0.7**	**-0.7**	**-0.7**	**-0.7**		**-0.7**	**-0.6**	
Contribution from nominal interest rate	0.8	1.3	1.4			0.7	0.8	0.9	0.9	1.0	0.9		0.8	0.6	
Contribution from real GDP growth	-0.1	-1.0	-0.6			-0.5	-1.8	-1.6	-1.7	-1.7	-1.6		-1.5	-1.2	
Contribution from price and exchange rate changes	-2.9	-0.7	-2.4			…	…	…	…	…	…		…	…	
Residual (3-4) 3/	**7.0**	**-1.2**	**-0.2**			**-4.4**	**-8.2**	**-8.9**	**-10.6**	**-9.9**	**-9.0**		**-11.8**	**-12.3**	
o/w exceptional financing	-1.4	0.0	0.0			-1.3	0.0	0.1	0.1	0.1	0.2		0.0	0.0	
PV of external debt 4/	...	...	45.0			50.5	54.7	58.0	58.3	57.7	56.7		49.0	37.1	
In percent of exports	...	...	136.8			166.4	182.7	196.0	199.2	199.1	198.7		164.4	124.5	
PV of PPG external debt	**...**	**...**	**45.0**			**50.5**	**54.7**	**58.0**	**58.3**	**57.7**	**56.7**		**49.0**	**37.1**	
In percent of exports	**...**	**...**	**136.7**			**166.4**	**182.7**	**196.0**	**199.2**	**199.1**	**198.7**		**164.4**	**124.5**	
In percent of government revenues	**...**	**...**	**157.7**			**178.4**	**185.8**	**210.1**	**211.8**	**209.7**	**199.0**		**176.4**	**133.6**	
Debt service-to-exports ratio (in percent)	**2.3**	**3.6**	**4.5**			**6.7**	**7.7**	**8.6**	**9.4**	**9.6**	**9.9**		**12.0**	**8.4**	
PPG debt service-to-exports ratio (in percent)	**2.3**	**3.5**	**4.4**			**6.7**	**7.7**	**8.6**	**9.4**	**9.6**	**9.9**		**12.0**	**8.4**	
PPG debt service-to-revenue ratio (in percent)	**3.0**	**4.2**	**5.1**			**7.2**	**7.8**	**9.2**	**10.0**	**10.1**	**9.9**		**12.9**	**9.0**	
Total gross financing need (Millions of U.S. dollars)	45.8	21.3	58.6			88.3	121.8	124.1	116.9	108.4	100.7		159.8	257.3	
Non-interest current account deficit that stabilizes debt ratio	-4.6	2.7	3.1			6.1	10.4	10.9	12.6	11.9	11.0		13.6	12.9	
Key macroeconomic assumptions															
Real GDP growth (in percent)	0.4	2.0	1.2	2.2	3.2	0.9	3.1	2.6	2.5	2.5	2.5	2.3	2.5	2.5	2.5
GDP deflator in US dollar terms (change in percent)	8.3	1.4	5.0	7.9	8.4	2.0	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
Effective interest rate (percent) 5/	2.4	2.7	3.1	2.7	0.3	1.3	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.2	1.3
Growth of exports of G&S (US dollar terms, in percent)	5.3	5.5	4.5	10.9	10.6	-5.1	3.9	3.6	3.6	3.7	3.3	2.2	4.7	4.7	5.0
Growth of imports of G&S (US dollar terms, in percent)	11.7	-2.0	14.9	10.4	11.6	3.3	8.7	2.4	0.5	0.7	0.6	2.7	4.7	4.7	5.1
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	19.5	20.7	20.4	24.7	27.3	26.3	23.2	28.6	28.5	28.6
Government revenues (excluding grants, in percent of GDP)	25.6	28.0	28.5			28.3	29.4	27.6	27.5	27.5	28.5		27.8	27.8	27.8
Aid flows (in Millions of US dollars) 7/	65.4	60.9	61.1			94.3	113.2	108.8	108.0	103.3	86.0		117.7	182.6	
o/w Grants	65.4	60.9	61.1			86.1	99.2	97.5	92.5	88.3	73.5		100.8	159.5	
o/w Concessional loans	0.0	0.0	0.0			8.3	14.0	11.3	15.5	15.0	12.5		16.9	23.1	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			14.1	15.4	14.3	12.7	11.6	9.3		10.1	9.9	10.1
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			64.8	66.9	67.8	76.0	78.5	76.5		78.9	81.0	78.8
Memorandum items:															
Nominal GDP (Millions of US dollars)	621.5	643.1	683.3			703.2	740.7	776.4	813.1	851.7	892.2		1122.7	1777.0	
Nominal dollar GDP growth	8.7	3.5	6.2			2.9	5.3	4.8	4.7	4.8	4.8	4.6	4.7	4.7	4.7
PV of PPG external debt (in Millions of US dollars)			306.0			355.2	405.0	450.1	473.9	491.2	506.3		550.3	659.7	
(PVt-PVt-1)/GDPt-1 (in percent)						**7.2**	**7.1**	**6.1**	3.1	2.1	1.8	4.6	0.6	1.0	0.8
Gross workers' remittances (Millions of US dollars)	139.8	146.5	161.5			164.1	167.6	172.3	177.6	184.0	189.6		237.0	375.1	
PV of PPG external debt (in percent of GDP + remittances)	...	...	36.4			41.0	44.6	47.4	47.8	47.4	46.8		40.5	30.7	
PV of PPG external debt (in percent of exports + remittances)	...	...	79.6			94.1	104.0	112.0	114.0	114.0	113.9		96.2	72.9	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	2.6			3.8	4.4	4.9	5.4	5.5	5.7		7.0	4.9	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.
2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.
3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. The residual includes development partners' capital grant flows.
4/ Assumes that PV of private sector debt is equivalent to its face value.
5/ Current-year interest payments divided by previous period debt stock.
6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.
7/ Defined as grants, concessional loans, and debt relief.
8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 1b. Samoa: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2013-2033
(In percent)

	Projections							
	2013	2014	2015	2016	2017	2018	**2023**	2033
PV of debt-to GDP ratio								
Baseline	51	55	58	58	58	57	**49**	37
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	51	46	42	37	32	28	**5**	-21
A2. New public sector loans on less favorable terms in 2013-2033 2	51	57	63	65	66	66	**64**	61
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	51	55	58	58	58	57	**49**	37
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	51	55	60	60	60	59	**51**	38
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	51	56	61	62	61	60	**52**	39
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	51	57	63	63	63	62	**53**	39
B5. Combination of B1-B4 using one-half standard deviation shocks	51	56	60	60	60	59	**51**	38
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	51	77	82	82	82	80	**69**	53
PV of debt-to-exports ratio								
Baseline	166	183	196	199	199	199	**164**	125
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	166	155	142	125	110	99	**16**	-70
A2. New public sector loans on less favorable terms in 2013-2033 2	166	192	213	222	227	231	**214**	204
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	166	183	196	199	199	199	**164**	125
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	166	192	218	221	221	220	**182**	136
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	166	183	196	199	199	199	**164**	125
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	166	192	213	216	216	215	**179**	131
B5. Combination of B1-B4 using one-half standard deviation shocks	166	183	193	196	195	195	**161**	121
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	166	183	196	199	199	199	**164**	125
PV of debt-to-revenue ratio								
Baseline	178	186	210	212	210	199	**176**	134
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	178	158	152	133	116	99	**17**	-75
A2. New public sector loans on less favorable terms in 2013-2033 2	178	195	228	236	239	231	**230**	219
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	178	186	210	212	210	199	**176**	134
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	178	188	218	220	217	206	**183**	137
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	178	191	222	224	221	210	**186**	141
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	178	195	229	230	227	216	**192**	140
B5. Combination of B1-B4 using one-half standard deviation shocks	178	191	218	219	217	206	**182**	137
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	178	263	297	300	297	282	**250**	189

Table 1b. (continued) Samoa: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2013-2033

(In percent)

				Debt service-to-exports ratio				
Baseline	7	8	9	9	10	10	**12**	8
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	7	7	7	8	7	7	**6**	-1
A2. New public sector loans on less favorable terms in 2013-2033 2	7	8	8	10	11	11	**14**	12
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	7	8	9	9	10	10	**12**	8
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	7	8	9	10	10	11	**13**	9
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	7	8	9	9	10	10	**12**	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	7	8	9	10	10	10	**13**	9
B5. Combination of B1-B4 using one-half standard deviation shocks	7	8	8	9	9	10	**12**	8
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	7	8	9	9	10	10	**12**	8
				Debt service-to-revenue ratio				
Baseline	7	8	9	10	10	10	**13**	9
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	7	7	8	8	8	7	**6**	-1
A2. New public sector loans on less favorable terms in 2013-2033 2	7	8	9	11	11	11	**15**	13
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	7	8	9	10	10	10	**13**	9
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	7	8	9	10	10	10	**13**	9
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	7	8	10	11	11	10	**14**	9
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	7	8	9	10	10	10	**14**	10
B5. Combination of B1-B4 using one-half standard deviation shocks	7	8	9	10	10	10	**13**	9
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	7	11	13	14	14	14	**18**	13
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	24	24	24	24	24	24	**24**	24

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

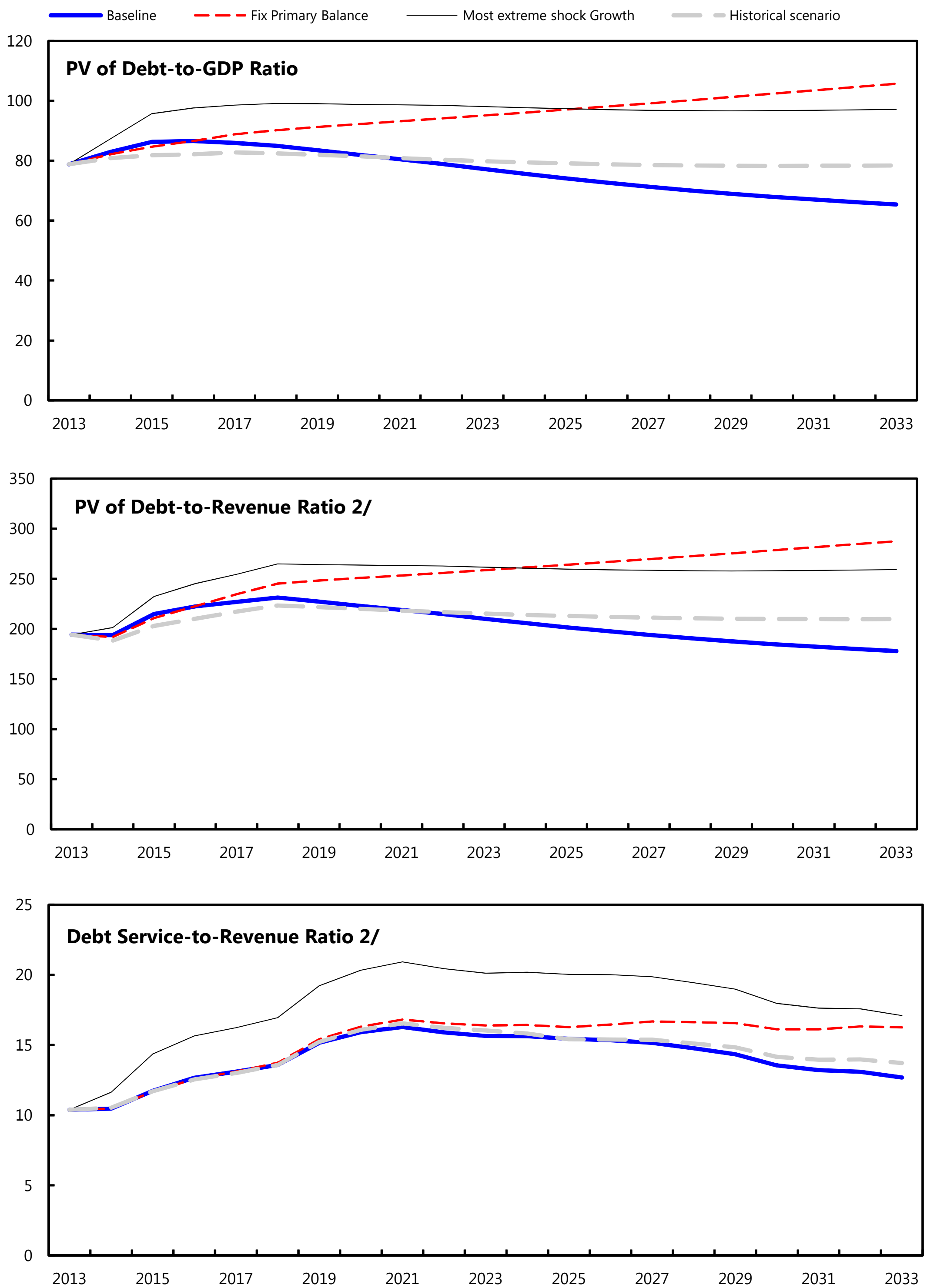
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Figure 2. Samoa: Indicators of Public Debt Under Alternative Scenarios, 2013-2033 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2023.

2/ Revenues are defined inclusive of grants.

Table 2a. Samoa: Public Sector Debt Sustainability Framework, Baseline Scenario, 2010-2033

(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2010	2011	2012	Average 5/	Standard Deviation 5/	2013	2014	2015	2016	2017	2018	2013-18 Average	2023	2033	2019-33 Average
Public sector debt 1/	78.8	78.9	83.8			90.1	95.1	98.9	99.2	98.5	97.3		89.4	77.0	
o/w foreign-currency denominated	49.5	50.1	55.5			61.8	66.8	70.6	70.9	70.2	69.0		61.1	48.7	
Change in public sector debt	10.1	0.1	4.9			6.3	5.0	3.8	0.3	-0.7	-1.2		-1.8	-0.9	
Identified debt-creating flows	3.0	0.0	2.9			4.3	3.7	3.3	0.1	-1.6	-0.7		-1.3	-0.7	
Primary deficit	4.7	3.1	2.5	1.4	1.6	4.0	5.1	5.1	1.9	0.3	0.9	2.9	0.0	0.3	0.2
Revenue and grants	36.2	37.5	37.5			40.5	42.8	40.2	38.9	37.9	36.8		36.8	36.8	
of which: grants	10.5	9.5	8.9			12.2	13.4	12.6	11.4	10.4	8.2		9.0	9.0	
Primary (noninterest) expenditure	40.8	40.5	40.0			44.6	47.9	45.2	40.8	38.2	37.7		36.8	37.0	
Automatic debt dynamics	-1.8	-3.1	0.3			0.3	-1.4	-1.8	-1.8	-1.8	-1.5		-1.3	-0.9	
Contribution from interest rate/growth differential	1.7	0.2	0.8			0.8	-1.0	-1.6	-1.7	-1.8	-1.5		-1.3	-0.9	
of which: contribution from average real interest rate	2.0	1.8	1.8			1.5	1.7	0.8	0.7	0.6	0.8		0.9	0.9	
of which: contribution from real GDP growth	-0.3	-1.6	-0.9			-0.7	-2.7	-2.4	-2.4	-2.4	-2.4		-2.2	-1.9	
Contribution from real exchange rate depreciation	-3.5	-3.3	-0.5			-0.5	-0.4	-0.2	-0.1	-0.1	0.0		...	...	
Other identified debt-creating flows	0.1	0.1	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.1	0.1	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	
Debt relief (HIPC and other)	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	7.0	0.1	2.0			2.1	1.2	0.5	0.3	0.8	-0.5		-0.5	-0.2	
Other Sustainability Indicators															
PV of public sector debt	...	...	73.3			78.8	83.0	86.3	86.6	86.0	85.0		77.3	65.4	
o/w foreign-currency denominated	...	...	45.0			50.5	54.7	58.0	58.3	57.7	56.7		49.0	37.1	
o/w external	...	...	45.0			50.5	54.7	58.0	58.3	57.7	56.7		49.0	37.1	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	13.9	13.1	12.0			14.6	15.9	16.0	13.0	11.5	12.2		12.0	11.2	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	195.7			194.4	193.8	214.8	222.6	227.0	231.4		210.3	178.0	
PV of public sector debt-to-revenue ratio (in percent)	...	...	256.9			278.4	282.0	312.7	314.6	312.6	298.3		278.2	235.4	
o/w external 3/	...	...	157.7			178.4	185.8	210.1	211.8	209.7	199.0		176.4	133.6	
Debt service-to-revenue and grants ratio (in percent) 4/	7.8	9.0	8.2			10.4	10.5	11.7	12.7	13.1	13.6		15.7	12.7	
Debt service-to-revenue ratio (in percent) 4/	11.0	12.0	10.8			14.9	15.2	17.1	17.9	18.1	17.5		20.7	16.8	
Primary deficit that stabilizes the debt-to-GDP ratio	-5.4	3.0	-2.3			-2.3	0.1	1.3	1.5	1.0	2.1		1.8	1.2	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	0.4	2.0	1.2	2.2	3.2	0.9	3.1	2.6	2.5	2.5	2.5	2.3	2.5	2.5	2.5
Average nominal interest rate on forex debt (in percent)	2.4	2.7	3.1	2.7	0.3	1.3	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.2	1.3
Average real interest rate on domestic debt (in percent)	5.2	5.4	4.0	4.9	0.8	5.8	6.4	4.0	4.1	4.0	5.0	4.9	5.0	5.0	5.0
Real exchange rate depreciation (in percent, + indicates depreciation)	-9.1	-6.8	-1.0	-6.6	5.7	-1.0	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	1.5	2.2	1.7	3.9	2.0	1.9	1.5	4.0	3.9	4.0	3.0	3.0	2.9	2.9	2.9
Growth of real primary spending (deflated by GDP deflator, in percent	0.1	0.0	0.0	0.0	0.1	0.1	0.1	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Grant element of new external borrowing (in percent)	...	...	...	...	...	19.5	20.7	20.4	24.7	27.3	26.3	23.2	28.6	28.5	...

Sources: Country authorities; and staff estimates and projections.

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.]

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 2b. Samoa: Sensitivity Analysis for Key Indicators of Public Debt 2013-2033

		Projections						
	2013	2014	2015	2016	2017	2018	2023	2033
PV of Debt-to-GDP Ratio								
Baseline	79	83	86	87	86	85	77	65
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	79	81	82	82	83	83	80	78
A2. Primary balance is unchanged from 2013	79	82	85	87	89	90	95	106
A3. Permanently lower GDP growth 1/	79	84	88	89	90	90	91	104
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	79	87	96	98	99	99	98	97
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	79	81	83	84	83	82	75	64
B3. Combination of B1-B2 using one half standard deviation shocks	79	83	86	87	87	87	84	80
B4. One-time 30 percent real depreciation in 2014	79	103	105	105	103	102	91	75
B5. 10 percent of GDP increase in other debt-creating flows in 2014	79	91	94	94	93	92	84	70
PV of Debt-to-Revenue Ratio 2/								
Baseline	194	194	215	223	227	231	210	178
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	194	188	203	210	217	223	215	210
A2. Primary balance is unchanged from 2013	194	192	211	223	235	245	259	288
A3. Permanently lower GDP growth 1/	194	195	218	228	235	243	242	273
A4. Alternative Scenario :[Costumize, enter title]	194	681	658	613	585	522	544	477
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	194	201	233	245	255	265	262	259
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	194	190	207	215	219	224	203	173
B3. Combination of B1-B2 using one half standard deviation shocks	194	192	210	221	228	235	226	215
B4. One-time 30 percent real depreciation in 2014	194	241	262	269	273	277	247	205
B5. 10 percent of GDP increase in other debt-creating flows in 2014	194	211	233	241	246	250	227	190
Debt Service-to-Revenue Ratio 2/								
Baseline	10	10	12	13	13	14	16	13
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	10	11	12	13	13	14	16	14
A2. Primary balance is unchanged from 2013	10	10	12	13	13	14	16	16
A3. Permanently lower GDP growth 1/	10	11	12	13	13	14	17	16
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	10	11	12	13	14	15	17	16
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	10	10	12	13	13	13	16	12
B3. Combination of B1-B2 using one half standard deviation shocks	10	11	12	13	13	14	16	14
B4. One-time 30 percent real depreciation in 2014	10	12	14	16	16	17	20	17
B5. 10 percent of GDP increase in other debt-creating flows in 2014	10	10	12	13	13	14	16	13

Sources: Country authorities; and staff estimates and projections.
1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.
2/ Revenues are defined inclusive of grants.

INTERNATIONAL MONETARY FUND EXTERNAL RELATIONS DEPARTMENT

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FOR IMMEDIATE RELEASE
May 16, 2013

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$8.6 Million Disbursement Under Rapid Credit Facility for Samoa

The Executive Board of the International Monetary Fund (IMF) yesterday approved a disbursement of an amount equivalent to SDR 5.8 million (about US$8.6 million) under the Rapid Credit Facility (RCF) for Samoa to help the country manage the economic impact of Cyclone Evan. The Board's approval enables the immediate disbursement of the full amount, which represents 50 percent of Samoa's quota in the IMF.

The December 2012 cyclone inflicted damages and losses across the whole spectrum of economic activity on the main island of Upolu, home to 70 percent of the population. The total estimated cost of damages and production losses could amount to almost 30 percent of GDP. Though small relative to the overall impact of the cyclone on the budget and balance of payments, Fund assistance to Samoa under the RCF will help catalyze support from development partners.

The RCF provides rapid financial assistance with limited conditionality to low-income countries with an urgent balance of payments need. In this context, the economic policies of a member receiving RCF financing are expected to address the underlying balance of payments difficulties and support policy objectives including macroeconomic stability and poverty reduction. Financing under the RCF carries zero interest (until end 2014), has a grace period of 5 ½ years, and a final maturity of 10 years. The Fund reviews the level of interest rates for all concessional facilities every two years.

Following the Executive Board's discussion of Samoa's request for assistance under the RCF, Mr. Naoyuki Shinohara, Deputy Managing Director and Acting Chair, stated:

"The macroeconomic impact of the tropical cyclone that struck Samoa in December 2012 has been especially significant coming just three years after the devastation caused by a tsunami. Economic growth will be adversely affected for some time, but there are encouraging signs of early recovery, and the authorities are to be commended for their swift response to the disaster.

“The main challenge in the short run is to secure sufficient resources for reconstruction with minimal additional borrowing. Planned public expenditure should be reprioritized and grant financing from development partners should be sought. However, as soon as the recovery takes hold, fiscal consolidation anchored in a medium-term fiscal framework should resume to bring public debt to more sustainable levels.

“Given low inflation and the need to support activity in the period ahead, monetary policy should remain accommodative, although the Central Bank of Samoa should continue to monitor domestic liquidity closely. With the aftermath of the cyclone posing risks to bank balance sheets, heightened prudential oversight of the financial system is necessary.

“Continued efforts will be needed to improve Samoa’s competitiveness and raise potential growth. The authorities are encouraged to build on their past successes and make further progress in improving the business environment, and in the areas of public enterprise reform, land use, and public financial management.

“The disbursement under the Fund’s Rapid Credit Facility is intended to help Samoa cope with its immediate balance of payments needs as well as catalyze critical donor support for the recovery.”

Statement by Jong-Won Yoon, Executive Director for Samoa
and Craig Fookes, Advisor
May 15, 2013

Cyclone Evan comes just three years after the tragic 2009 tsunami and was the largest cyclone to strike Samoa in twenty two years with an economic damage assessment equivalent to almost 30 percent of GDP. The cyclone created significant economic disruption and affected most parts of the economy on the main island, which is home to 70 percent of the population. GDP growth is expected to decline to 0.9 percent over 2012/13.

A strong track record of prudent economic management provided policy headroom, but successive crises have unwound ten years of prudent macroeconomic management. Samoa was widely viewed as a model economy with a strong track record of careful economic management. A period of structural reforms, beginning 1996, was supported by prudent fiscal management aimed at building resilience over time. Public debt declined from 66 percent of GDP in the late nineties to around 35 percent of GDP in 2007/08. The advent of the financial crisis and the cost of relief for the 2009 tsunami created a significant setback for the authorities. Debt rose to nearly 60 percent of GDP by 2011/12, leaving government finances vulnerable to further shocks.

The arrival of Cyclone Evan and its associated costs have pushed the economy over into a high risk of debt distress under the joint IMF/WB debt sustainability analysis. The RCF will be used to ease immediate cyclone related pressures on fiscal resources and foreign reserves, given current projections suggest debt, which is largely concessional, could reach 70 percent of GDP by 2014/15. In addition to providing such financial assistance and advising on macroeconomic frameworks, the Fund involvement will help catalyze support from development partners.

Over the medium term, our authorities have highlighted their continued commitment to implementing sound macro policy aimed at rebuilding resilience through stronger growth and macroeconomic stability. The post-crisis response was proactive and utilized a range of innovative and unconventional policy tools to provide immediate policy support within Samoa's shallow domestic markets. The rapid response has reduced economic disruption, but the authorities are now looking to normalize policy to guide the economy back to growth. The intention is to return debt to a more prudent level given an ongoing exposure to economic shocks and further natural disaster.

Monetary policy

The Central Bank of Samoa's (CBS) will retain its accommodative monetary policy stance, which will support stronger growth of around 3 percent through 2013/14. To maintain the real value of the fixed peg, the authorities aim to keep inflation on par with inflation rates observed in key trading partners, such as Australia. The inflation outlook remains benign with headline inflation expected to average 2 percent through 2012/13, falling to 1.5 percent alongside projected declines in global commodity prices.

Past Article IV reports have highlighted the weak pass-through from changes in monetary policy. Samoan banks remain constrained in their ability to lend and tend to suffer from excess cash reserves. The most recent monetary policy statement noted that banks' excess reserves remain at over three times the monthly minimum excess levels of WST 20.5 million. The CBS has reintroduced credit facilities for commercial banks' use and are working to encourage an active interbank market as liquidity returns to more desirable levels. The authorities highlighted that the Central Bank credit lines provided to the Development Bank remain temporary and were only used twice in the wake of the tsunami and Cyclone Evan. The loans served a similar purpose to the quantitative easing in advanced economies, in that they aimed to overcome structural impediments creating a blockage in the credit channel for monetary policy. The CBS credit lines funded emergency loans to solvent businesses facing a temporary loss of income. The authorities remain conscious of the risks to the central bank balance sheet and have issued a government guarantee to protect the CBS from loss.

Fiscal Policy

Reconstruction expenditure will remain elevated over the next couple of years, but should moderate as crisis-related spending starts to tail away. Reconstruction and social spending will provide stimulus over the short-term, although debt will need to be lowered over the medium term given that the 2012/13 deficit will rise to 6.4 percent of GDP. Grant funding and a reprioritization of planned development projects will help minimize the projected increase in debt. To further aid consolidation, a joint working group has been formed to improve policy coordination between the CBS and Ministry of Finance and the medium-term fiscal framework will be revised. The World Bank will provide assistance through a review of expenditure and debt management policy.

Notwithstanding this, Samoa continues to face significant pressures for investment to support future growth. The Government has a stated policy to "build back better". Improvements will have a nominal upfront cost. However, the authorities expect that stronger building standards will help reduce crisis-related expenditures should further natural disasters occur over the medium term. New building projects should come under increased scrutiny and, as the staff noted, would ideally be grant funded.

Financial Sector

Samoa's financial sector is profitable, but markets remain shallow and relatively underdeveloped. Four registered banks provide basic financial services. The two largest banks are foreign owned, but are limited in the lending opportunities they can purse given a need to comply with their parent banks' prudential guidelines. Thus, even in the wake of the cyclone, banks report excess reserves and a lack of lending opportunities given difficulties around the use of collateral. The CBS is responsible for supervision and is monitoring non-performing loans in the wake of Cyclone Evan.

Our Samoan authorities are investigating ways to encourage financial deepening by addressing issues such as an inability to use land as collateral, which has acted as brake on investment. Box 4 discusses the new Customary Land Advisory Commission (CLAC).

Communal ownership has complicated the sale, lease, or development of nearly 80 percent of the country's land. CLAC will identify ways to encourage land use within traditional ownership structures. Clearer land rights and an ability to post collateral under the recently passed *Personal Property Security Act* should facilitate financial deepening and a more efficient pass through from changes in monetary policy.

The Government has also sought to expand access to financial services as a way to encourage saving. The National Provident Fund provides a retirement savings vehicle and the Unit Trust of Samoa (UTOS) provides access to a broader and more diversified investment portfolio than simple bank deposits. The decision to invest savings abroad has contributed to a reduction in excess liquidity, but the situation will need to be carefully monitored. In light of the developments, the authorities are fully supportive of undertaking an FSAP update. UTOS is relatively new (2008), while other financial entities are undergoing change through product redesign or evolutionary amendments to their mandate. An FSAP update could highlight the implications that these changes have had and identify ways to encourage development in private markets. Public financial entities are currently supervised by the SOE unit in the Ministry of Finance. However, the authorities agree that supervision could be streamlined through increased involvement from the Central Bank. An FSAP update could facilitate this transition and the Central Bank currently has staff seconded at the Bank of Fiji to develop specialist experience in the regulation of unit trusts.

External Sector

The authorities are monitoring reserves and are committed to maintaining external stability. Samoa has limited short-term debt as banks are funded by domestic deposits and most external debt is public debt owed to the ADB and WB. The current account deficit will increase for the time being, but will remain predominantly funded by official flows and remittances. IMF projections suggest that reserves will increase to around 4 months import cover, provided that donor support plays out as expected. While reserves are expected to exceed the standard 3 month reserve adequacy guideline, they do start to decline to around 3.8 months in 2014/15. Our authorities are aware of the risks of allowing reserves to dwindle and will act to prevent any depletion that could risk a more disruptive devaluation down the track. To prevent drains on CBS reserves, the authorities have highlighted the need for development partners to target funding towards boosting domestic activity through grant financing (upfront rather than on a reimbursable basis).

Our authorities have requested technical assistance (TA) to strengthen monitoring and analysis of exchange rate developments. They do not consider a devaluation at this point in time as desirable. Large uncertainties around equilibrium exchange rate levels would suggest a need for caution in interpreting the estimation results. The pace of post-cyclone recovery in Samoa remains uncertain and there is significant concern as to how a devaluation would affect the poor at the current juncture. Samoa is still adjusting to higher food prices as result of global food price inflation, the local drought, and the loss of agricultural production through Cyclone Evan. For these reasons, the authorities share the staff advice that an exchange rate devaluation be delayed until after the recovery starts to take hold.

The ongoing Fund technical assistance will provide useful input to guide future decisions by the Central Bank. The decision to devalue would need to carefully consider the effectiveness of monetary policy and its ability to control the pass through to inflation. A more gradual process of adjustment would allow monetary policy time to respond. Given that Samoa's debt is mainly denominated in foreign currency, the Samoan authorities remain concerned about an increase in debt at a time when the country has just been placed at high risk of debt distress.

Finally, our Samoan authorities would like to express their gratitude to Management and the mission team for their swift response to our request for the RCF and their dedication in helping Samoa overcome the tremendous hardships caused by the cyclone.