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March 2015

2014 ARTICLE IV CONSULTATION—STAFF REPORT; PRESS RELEASE; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE 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 2014 Article IV consultation with Maldives, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on February 11, 2015, following discussions that ended on November 20, 2014, 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 January 27, 2015.
- An **Informational Annex** prepared by the IMF.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- A **Press Release** summarizing the views of the Executive Board as expressed during its February 11, 2015 consideration of the staff report that concluded the Article IV consultation with Maldives.
- A **Statement by the Executive Director** for Maldives.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

MALDIVES

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION

January 27, 2015

KEY ISSUES

Context. Maldives has rapidly grown into a middle income country, driven by tourism development. Over the past decade, the economy has experienced persistent fiscal deficits, occasionally accompanied by a widening current account deficit and pressure on the stabilized exchange rate regime. At the time of the previous Article IV consultation, official data pointed to large current account and fiscal deficits. Staff recommended policy action, combining fiscal consolidation, exchange rate devaluation and an incomes policy. Some fiscal policy actions were taken. The exchange rate parity was maintained.

Recent economic developments. Two years on, the picture is different: a recovery in tourism is supporting growth; Maldives has performed well relative to peers; substantial data revisions paint less worrying picture of the external sector; and there is little pressure on the exchange rate. But the large and growing fiscal deficit remains the Achilles heel.

Policy recommendations:

- **Fiscal policy.** Fiscal consolidation is necessary to ensure sustainability. The 2015 Budget contains helpful measures but they do not seem sufficient to bring debt ratios down. With limited policy buffers, the risks of fiscal slippages are high and the economy is vulnerable to external shocks. Staff advise greater fiscal adjustment through expenditure restraint to place the debt ratio firmly on a downward path. Strengthened public financial management is critical to support fiscal goals.

- **Monetary, financial and external policies.** Support from monetary and financial policies would help build buffers. The external position is highly uncertain given data issues, but on balance looks modestly weaker than implied by fundamentals and desirable policies and the exchange rate modestly overvalued.

- **Medium term.** Care needs to be taken to ensure that medium term policies do not add substantially to public sector expenditures, that infrastructure spending adds to potential growth and does not run into capacity constraints

- **Data.** Statistics should be further strengthened to assist policy decisions.

Approved By
Rachel van Elkan and Catherine Pattillo

Discussions took place in Malé November 9–20 2014 Staff representatives comprised Ms. A Stuart (head), M Ghazanchyan (APD), K. Wijeweera (APD, and Resident Representatives Office), P. Xie (SPR) and Ms. E Kvintradze (Resident Representative, Sri Lanka and Maldives). Ms. W Abdelati (OED) joined the discussions.

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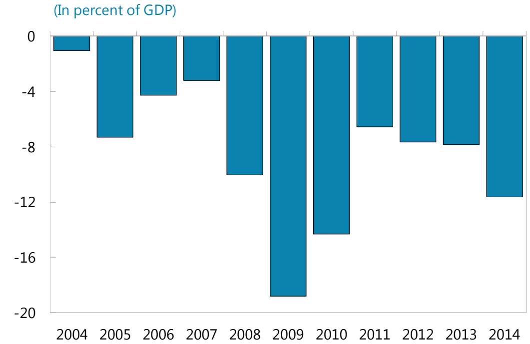
CONTEXT

1. Maldives has rapidly grown into a middle income country, driven by tourism development. Tourism activity—accounting directly and indirectly for around three-quarters of output—underpins the $6740 per capita GDP in 2013. The country's unique geography, with 200 inhabited islands covering around 90,000 sq.km, high import-intensity, and dollarization, pose policy challenges, alongside the detrimental impact of climate change. With tourist transactions mainly in U.S. dollars, the economy is highly dollarized. Given the weak fiscal position, monetary conditions (under the stabilized exchange rate regime and open capital account) are determined by fiscal policy and the supply of foreign exchange. Low population density (outside Malé) raises the cost of public service provision, results in a lack of employment opportunities and youth unemployment is high (only 40 percent of youth is in employment).

2. Over the past decade, the economy has experienced persistent fiscal deficits, occasionally accompanied by a widening current account deficit and pressure on the exchange rate. Since the 2004 tsunami, Maldives has faced fiscal deficits initially from reconstruction needs, but then from large increases in the public sector wage bill and social spending. These were financed mainly domestically—including through monetization—and led to intermittent pressure on official reserves and the exchange rate, especially since the global financial crisis.

Overall Fiscal Deficit
(In percent of GDP)



Source: MMA and IMF staff estimates.

3. By early 2013, official data pointed to large current account and fiscal deficits. At the conclusion of the previous Article IV consultation, the official data indicated a current account deficit of 26.5 percent of GDP and official reserves of $304mn (1.6 months imports) on a declining path. Difficulties financing the fiscal deficit led to some recourse to arrears. Consistent with these conditions, staff recommended policy action, combining fiscal consolidation, exchange rate devaluation and an incomes policy to curb import demand. Some fiscal policy actions were taken. The exchange rate parity was maintained.

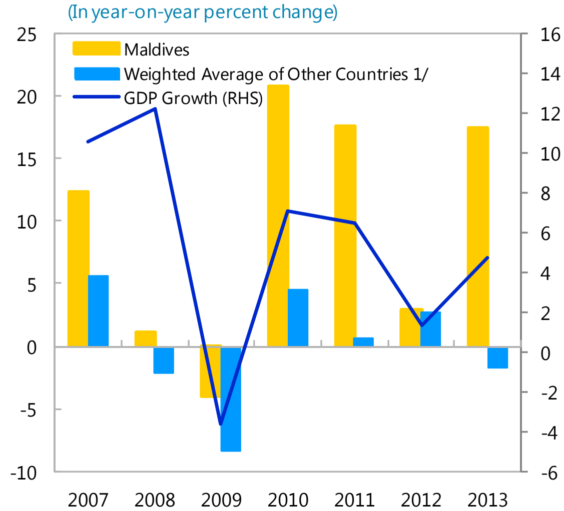
4. Two years on, the growth outlook is brighter, and significant data revisions paint a less worrying picture of the external sector position. A recovery in tourism activity has supported growth and exports; and there has been little apparent pressure on the exchange rate. Revisions to official statistics have resulted in a substantial reduction in the current account deficit (Box 1), and nominal GDP has been revised up (Annex 1). The puzzle of large current account deficits and low reserves but well stocked stores has been partly resolved by revised data. However, staff's analysis points to further underreporting of tourism exports suggesting that the current account deficit may still be somewhat overstated (Box 5). These revisions also imply a stronger private sector saving position than previously estimated. Nevertheless, the fiscal deficit and public debt remain very high and need to be addressed.

RECENT DEVELOPMENTS, OUTLOOK, AND RISKS

A. Recent Economic Developments

5. In 2013–14 growth rebounded, the current account deficit was in single digits and inflation was contained. Tourist activity picked up with a rapid expansion from Asian markets and a tepid recovery from Europe. Maldives performed well relative to other tourism dependent economies (text figure). Growth was 4.7 percent in 2013 and staff projects 5 percent in 2014 and 2015 (Table 1, Figure 2).[1] Higher tourism exports and subdued global food and fuel inflation helped reduce the current account deficit from its 2012 level to around 8.4 percent of GDP in 2014; and following significant data revisions, it is substantially smaller than previously estimated (Box 1). Inflation was contained at 1.1 percent in November. Lower oil prices have improved the outlook for the current account and inflation in 2015. An increased supply of dollars in the official market narrowed the parallel market premium (to 3–4 percent) and gross official reserves rose to $614 mn (2.8 months imports), though net reserves remained low.

Tourists Arrivals, 2007-2013
(In year-on-year percent change)



1/ Countries include Mauritius, Seychelles, Bahamas and Barbados.
Sources: Caribbean Tourism Organization; Authorities data and IMF staff estimates.

6. But the fiscal deficit is thought to have widened sharply in 2014, on the back of spending largesse. Staff estimates the deficit at 7.8 percent of GDP in 2013 compared with official data which report a deficit of 3.9 percent of GDP. The difference reflects higher staff estimates for interest payments, subsidies, and social welfare.[2] Maldives Monetary Authority (MMA) financing data also points to a higher deficit (see table). A sharp rise in recurrent expenditures (pensions, and wages) is likely to have widened the deficit to 11.6 percent of GDP in 2014. The 2015 Budget measures aim to rein in the deficit (Box 2).

Maldives: 2013-14 Authorities vs. Staff Projections

	2013 Authorities latest /1	2013 Staff Estimates 1/	2014 Staff Projection
Total Revenue & Grants	28.6	28.6	32.2
Revenue	28.3	28.3	31.2
Grants	0.3	0.3	0.9
Expenditure and Net Lending	32.6	36.5	43.7
Current Expenditure	27.8	31.7	36.3
Capital Expenditure	5.0	5.0	6.6
Net Lending	-0.3	-0.3	-0.3
Arrears clearance	0.0	0.0	1.1
Overall Balance	-3.9	-7.8	-11.6
Overall Balance Ex. Grants	-4.2	-8.1	-12.5
Financing			
Domestic o/w	2.8	4.4	
MMA		1.2	
Tbills		4.2	
banks & other		-1.0	
Foreign	1.1	3.4	
Memo: Outstanding Stock of arraers		6.3	

Sources: Maldives Authorities and IMF Staff estimates and projections
1/ The deficit is on a 'cash basis' and excludes the build up of arrears.

7. Public debt is correspondingly high. Sustained primary deficits placed public debt (including SOEs, excluding arrears) on a rising path from 52 percent in 2009 to 75 percent of GDP in 2014, above the 60 percent limit in the recently established Fiscal

[1] The real growth measure used throughout the report is gross value added at basic prices.
[2] Staff estimates for interest costs are in line with public debt levels and effective interest costs. Subsidy and welfare expenditures are in line with beneficiary numbers and benefit levels.

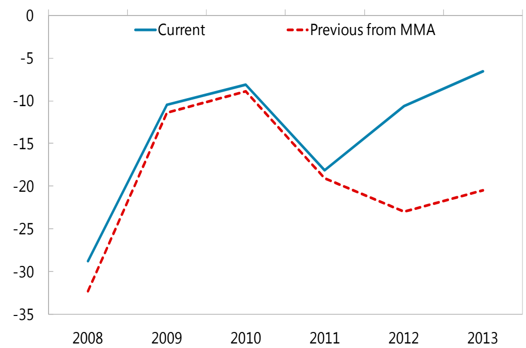
Responsibility Law. The stock of arrears estimated by staff would add 6.3 percent of GDP to the debt ratio. The arbitration ruling over the authorities' cancellation of the airport operating concession could pose a sizable contingent fiscal liability.[3]

Box 1. Data Revisions to the Balance of Payments

Significant revisions have been made to the balance of payments data in line with IMF technical assistance recommendations. Estimated current account deficits have been substantially reduced from rates of around 20 percent of GDP to single digits in 2012–13 (text figures). This reflects new data sources, better methods and new data.[1]

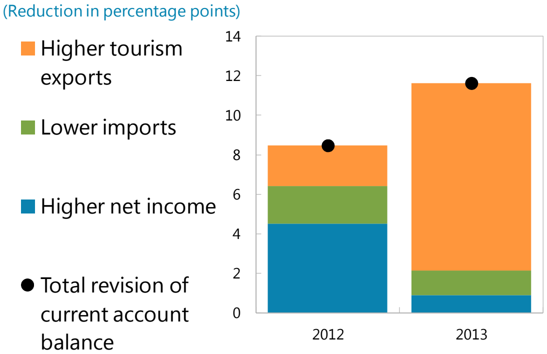
- **Higher tourism exports.** Data from the Tourism Goods and Services Tax (TGST) from the Maldives Inland Revenue Authority (MIRA) has been used to estimate total travel receipts (including new data for 2013) and the bed-nights tax has now been included in the estimate. *Net effect:* reduces the current account deficit by 2.1 and 9.5 percentage points of GDP in 2012 and 2013 respectively.
- **Lower imports of goods and services.** Two partially offsetting revisions were made. Double counting of the import of jet fuel was eliminated and imports of services were revised upwards (using withholding tax data). *Net effect*: reduces the current account deficit by 3.2 and 4.1 percentage points of GDP in 2012 and 2013 respectively.
- **Higher net income.** New improved methods have been used for estimating outward company profits and foreign workers' remittances. *Net effect*: reduces the current account deficit by 3.7 and 0.6 percentage points of GDP in 2012 and 2013 respectively.
- **The estimation of the financial account has been improved and gaps reduced using a variety of data sources:** (i) annual FDI survey; (ii) use of the MMA's monetary and financial statistics for bank flows; (iii) Bank of International Settlements data for non banks; and (iv) the IMF's Coordinated Portfolio Investment Survey database. Further improvement is expected with the new FDI survey launch in 2015. Previous estimates were incomplete.

Current Account Balance Comparison
(In percent of GDP)



Source: MMA and IMF staff estimates.

Breakdown of Current Account Balance Revision
(Reduction in percentage points)



Sources: MMA and IMF staff estimates.

Though large, the revisions are plausible and help partly resolve the external sector puzzle. They reduce the scale of errors and omissions in 2012 ($24mn), though these remain large in 2013 ($98 mn). They go some way to reconciling the puzzle of large deficits yet few signs of difficulty obtaining foreign exchange or imported goods.

[1]All data in the second text figure are ratios based on the new nominal GDP data (see Annex 1).

[3] In 2012 the authorities cancelled the airport concession contract with GMR and Malaysia Airports Berhad to upgrade and operate Malé airport. In June 2014 arbitration ruled in favor of GMR. Maldives Airport Company Limited (MACL) paid $4mn in immediate costs. Agreement on a final settlement between GMR and the authorities/MACL (has yet to be reached.

8. **Financial soundness indicators are slowly improving, monetary conditions are easy, but credit growth is subdued.** Bank profitability has increased and nonperforming loans in the tourism and construction sectors are falling back from high levels built up during the global financial crisis (Figure 4, Table 6). Base money and broad money have been growing rapidly financed by reserve accumulation and sharply higher NFA of the banks. But private sector credit growth is subdued (0.5 percent in November 2014 year on year) as banks appear to be cautious about lending to the tourism and construction sectors; and large investments are financed abroad (thought to include own funds of tourism operators held abroad). Instead funding is channeled into the MMA's Overnight Deposit Facility or directed into Treasury bills despite lower yields.

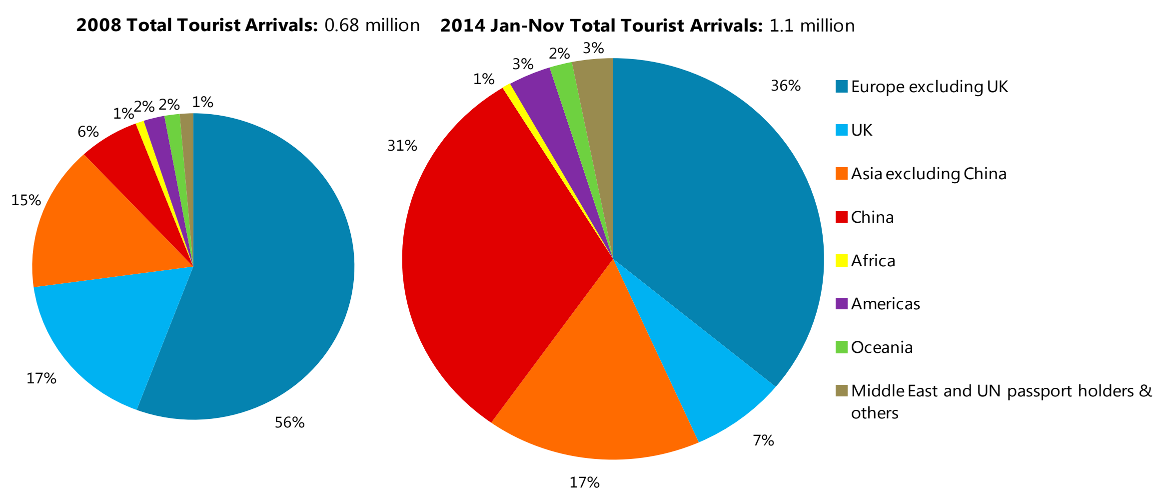
B. Outlook and Risks

Staff's Position

9. **Growth is forecast to remain fairly strong over the medium term, slowing a little as fiscal consolidation implied by the 2015 Budget takes hold.** However, there is upside potential if lower oil prices are sustained.

- Under the baseline scenario medium term growth is projected to be around 4½ percent, somewhat slower than the average of 6½ percent when tourism development was at its peak. Although the global recovery is uneven, Maldives has proved adept at attracting tourism from a variety of regions (see text figure), new resort openings and the development of the airport will add to capacity, and tourist activity is expected to grow moderately.[4] On the upside, if lower oil prices are sustained, and passed on in lower airline fares; this could provide a further boost to tourism.

Tourist Arrivals Composition: 2008 v.s. 2014 Jan-Nov
(In percent of total tourist arrivals)



Sources: MMA and IMF staff estimates.

[4] Around three quarters of activity is directly or indirectly linked to tourism. Maldives is a high end tourist destination with around 60 percent of resorts in the 5 star and plus category, and demand is relatively price and income inelastic. The authorities expect to lease five new resorts a year. A second runway at the airport will also add to capacity.

- If fully implemented, the authorities' fiscal adjustment plans would have a mildly negative effect on growth (around ¾ of a percentage point in 2016 17). Staff estimates the fiscal multiplier to be relatively low: Maldives is a high end destination for tourism, demand for which is likely relatively price inelastic; and other characteristics (high trade openness, low labor rigidities high public spending and debt) are consistent with a low multiplier.
- The recent drop in oil prices has improved the current account and inflation outlook. The current account is expected to narrow over the medium term to around 4.7 percent of GDP by 2019 as fiscal restraint and lower oil prices help constrain imports. Inflation is forecast to be just 0.3 percent in 2015 but to pick up with the increase in import duties and is expected to settle at around 4 percent in the medium term.

10. However, limited policy buffers suggest the economy is vulnerable to fiscal slippages and inward spillovers (Risk Assessment Matrix)**.** In the event of fiscal expenditure overruns relative to the authorities' targets, borrowing costs and monetization could increase, which could make the external position become fragile. Homegrown risks could also be triggered if there is a period of protracted low growth in advanced and emerging economies. In the face of a large external shock, foreign capital inflows (thought to be primarily inflows from tourism operators) may weaken as occurred during the global financial crisis. If risks materialize, an accelerated fiscal consolidation effort with tough expenditure control would be needed to restore sustainability and stem the erosion of reserves.

Authorities' Views

11. The authorities expect growth to be stronger than projected by staff with tourist arrivals rising robustly, especially as airport capacity is expanded. Real GDP growth is expected to average around 8 percent over the next three years. As a small open economy, Maldives is unavoidably vulnerable to external shocks. They were of the view that boosting growth potential, as has been done in the past with the development of the tourist industry, was the best way to manage shocks. Current plans to improve infrastructure and to develop Special Economic Zones (SEZs) (paragraph 27) would support growth and help build buffers.

POLICIES FOR FISCAL SUSTAINABILITY

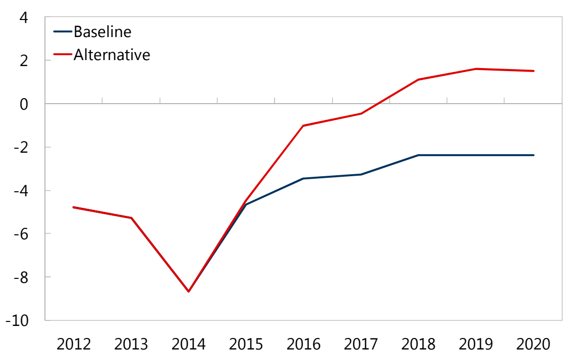
Background

12. The 2015 Budget aims to reverse the rise in the fiscal deficit, resulting from growing spending commitments. Public spending has risen by 9.9 percentage points of GDP since 2011 reflecting high spending on wages, subsidies and social welfare, and the spending-to-GDP ratio is high relative other tourism-based economies (Figures 1, 3). This reflects a combination of new spending initiatives and critical weaknesses in the governing framework for expenditure control. The Budget is largely aimed at revenue raising measures (imposing a green tax, acquiring fees from SEZs and raising import duties), supplemented by some expenditure restraint through a temporary public employment freeze and better targeting of subsidies (Box 2).

Staff's Position

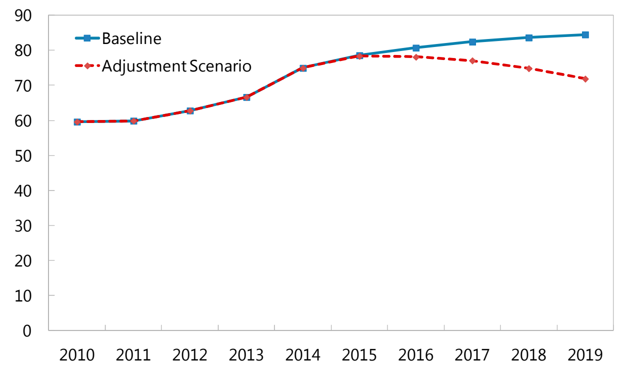
13. The fiscal consolidation implied by the 2015 Budget is commendable and significant but may not deliver sufficient savings to place the debt ratio on a sustainable path. Based on baseline forecasts, staff expects the Budget to deliver a significant improvement in the primary deficit of around 4.1 percentage points in 2015, (see Box 2, Table 2), containing the primary deficit to 2.4 percent of GDP over the medium term (consistent with an overall deficit of 7.6 percent in the medium term). Public debt would continue to increase, though at a slower pace and would remain well above the debt anchor of 60 percent of GDP in the Fiscal Responsibility Law (text figure and Debt Sustainability Analysis, Supplement 1). This contrasts with the authorities' fiscal projections, where they assume additional revenues (in particular from fees related to the acquisition of Special Economic Zones), earlier realization of some measures, and faster GDP and tourism growth.

Primary Balance
(In percent of GDP)



Source: MMA and IMF staff estimates.

Public Debt: Baseline vs. Adjustment Scenarios, 2010–2019
(In percent of GDP)



Sources: Maldives authorities; and IMF staff estimates.

14. Staff's view is that an additional and more permanent consolidation, amounting to around 3 percentage points of GDP is needed over 2015-19 to bring debt ratios down. If the authorities' ambitious capital spending plans are fully realized (see Box 2), then further adjustment would also be needed to offset the fiscal impact. Additional consolidation could be achieved through politically feasible structural measures that build on the 2015 Budget and deliver a more permanent improvement in the fiscal position. Gradually lowering the debt ratio would reduce pressure for monetary financing, strengthen the external position by cutting import demand and reduce crowding out, albeit at some cost to near-term growth.[5]

[5] The 2009 fiscal consolidation plan targeted a 30 percentage points of GDP reduction in the deficit in a year was not implemented as essential political support for large scale measures dissipated, especially given a recession that year.

Box 2. Maldives 2015 Budget Fiscal Adjustment Measures

The 2015 Budget passed in December includes measures to reduce the fiscal deficit. Measures are weighted to revenues and include some expenditure restraint (see tables). Staff estimates that the package could help reduce the primary deficit by 4.1 percentage points in 2015.

- **Revenues**. Measures are directed at the tourism sector and imports. The green tax (replacing the bednights tax) is an important source of income from the tourism sector. Import duties on some consumer items are being raised from zero and excises are being increased. The authorities expect significant revenues from the acquisition of land for SEZs and licenses for new resorts.

2015 Budget Measures

	Description of Measure	Authorities savings estimate Change from 2014 pps of GDP
Revenues		
Green Tax	A tourism "green tax" ($6 per night) replaces the bednights tax ($ 8 per night).	0.7
Import Duties	Rise in duties on some zero rated consumer items; vehicles duties and tobacco excises.	1.2
Resort Development	Ten new resorts a year to come on stream generating resort license income.	1.1
SEZ plus land reclamation	$100 mn from the acquisition of land for a Special Economy Zone in 2015	4
Expenditures		
Subsidies	Targeting electricity and food subsidies.:40 percent cut in subsidies in 2015.	-2.1
Wage bill	The public employment freeze.	1.1

- **Expenditures.** Measures aim to contain current spending, including a public employment freeze. Stricter control over public sector employment and the wage bill, and targeting subsidies, are both important goals. Previous work by the World Bank found that subsidies could be much better targeted—half the electricity subsidy goes to the highest two income quintiles, and food subsidies were similarly poorly targeted (with subsidies also benefiting the tourist resorts).

- **Capital expenditures.** The authorities plan a large increase in capital expenditures (for a Malé-airport road bridge and for airport development) financed by bilateral official loans.

Staff project the deficit will be higher than the official target for a number of reasons: the delayed introduction of some measures, uncertainty over revenue realization from the acquisition of land for SEZs, the need for targeting of subsidies to be accompanied by measures to secure safety nets (this will take time, although some conditions are in place for proxy means testing); possible slippage on wages, and a different base, given 2013 estimates. In the other direction, staff expect capital spending to come on stream more gradually than envisaged by the authorities (as feasibility studies for these projects have yet to be completed) reducing the overall deficit.

Summary of Fiscal Projections 2015-17: Authorities and Staff (in percent of GDP) [1]

	2015		2016		2017	
	Auth	Staff	Auth	Staff	Auth	Staff
Total Revenue & Grants	45.9	35.3	43.4	35.9	41.2	35.4
o/w Tax Revenue	27.5	23.8	31.3	26.0	31.5	26.1
Import Duties	5.2	4.6	6.3	5.6	6.1	6.0
Green Tax	0.7	0.4	2.7	1.5	2.6	1.5
Tourism GST	10.4	8.1	10.9	8.0	11.3	7.8
o/w Non-tax revenue	13.7	10.4	8.9	9.0	8.0	8.6
Resort Lease Rentals/SEZ acquisition	10.1	5.7	5.4	4.3	4.3	3.9
Total Expenditure & net lending	47.6	43.4	46.2	43.1	40.0	43.3
o/w Current Expenditure	32.4	36.0	29.8	35.8	27.0	36.0
Wages Costs	13.6	13.3	12.3	12.8	11.4	12.3
Interest Costs	2.9	3.5	3.5	3.8	2.3	4.6
Social Welfare Contributions	3.5	5.6	3.0	6.0	2.8	6.4
Subsidies & Transfers	3.0	6.3	2.9	5.9	2.7	5.4
o/w Capital Expenditure	15.1	6.7	16.5	6.7	13.1	6.7
Primary Balance	1.3	(4.6)	0.7	(3.5)	3.5	(3.4)
Overall Balance	(1.7)	(8.1)	(2.8)	(7.3)	1.2	(7.9)

1/ Staff estimates are based on the baseline scenario; authorities estimates (presented relative to staff's nominal GDP projections, authoriteis project higher nominal GDP).

15. To ensure successful implementation, the size and phasing of fiscal adjustment needs to be relatively gradual and calibrated to avoid a sharp growth slowdown (although fiscal multipliers are likely low). Evidence from other small economies illustrates the importance of sustaining an adjustment effort over a number of years and focusing on expenditure control (Box 4). To return the debt ratio to the level of 2013 and bring it within reach of the 60 percent limit (text figure and table 5), staff proposes additional savings of 3 percentage points of GDP, beginning in 2016, with just over half of the additional savings deriving from the spending side:

- *Expenditure measures:* spending restraint over 2016–19 with structural measures to durably contain the wage bill (by establishing a pay body to set consistent rules across the public sector, by reducing the number of paid local councilors, and by embarking on the public service reform already envisaged by the authorities), by containing rising healthcare costs and savings on transport and communications.[6] *Saving 1.7 percentage points of GDP*.
- *Revenue measures*: an increase in the TGST rate from 12 to 15 percent in 2016 would help underpin revenues*. Increased revenues: 1.3 percentage points of GDP*.

16. Better public financial management is a prerequisite for fiscal sustainability. The recent Public Expenditure and Financial Accountability assessment identified deep rooted problems with greater fiscal discipline and better prioritization needed across government. Difficulties include: unrealistic budgets with spending allocations insufficient to meet commitments, reshuffling of spending between activities/ministries, and unenforced spending ceilings. Reforms were suggested in many areas, including a baseline review of expenditures (Box 3). Better methods are needed to track payments, including subsidies, in order to design targeting and monitor savings. Compliance with the Fiscal Responsibility Law (which came into force in May 2014) would also support longer term fiscal goals. The Law includes positive features that can helpfully discipline fiscal policy—including debt and deficit limits and strict limits on MMA credit to government (preventing monetization). It could also be used to help anchor a targeted primary balance path.

Authorities' Views

17. The 2015 Budget includes significant measures, expected to result in a larger fiscal consolidation than estimated by staff. The set up of Special Economic Zones would generate fee income from their acquisition and could significantly supplement revenues with no need for further revenue measures. Expenditure restraint, in particular through the public sector employment freeze has political backing and, together with the review of local government pay structures, this would generate sizeable permanent cost savings. They also agreed that a public sector wide pay body could be helpful to ensure consistency of wages and salaries across public service and drive forward public service reform. Strengthening public financial management is a key government priority, and continued technical assistance on the fiscal chart of accounts and budget execution would be valuable.

[6] The universal healthcare insurance scheme, Aasandha was introduced in 2012 and covers the whole population. Costs have risen rapidly and the announcement in 2014 of unlimited health insurance will escalate costs. According to the World Bank, savings could be achieved through bulk procurement of essential and generic drugs and by reducing expenditure on overseas treatment through negotiation of close-ended package rates with providers.

Box 3. Public Financial Management Reform Plan (2015–2018)

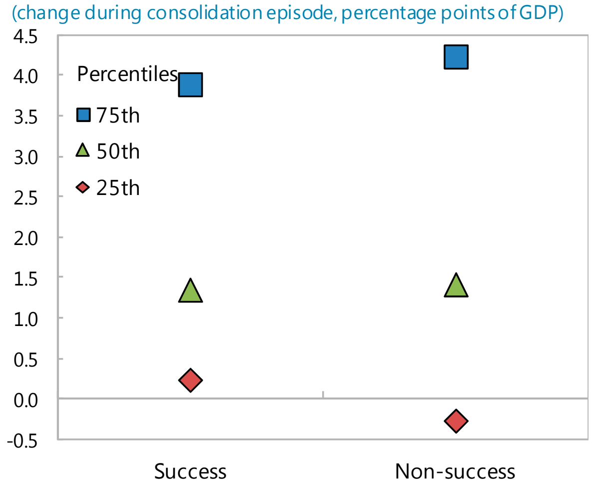
Goal	Actions
Clear responsibilities between agencies should be established to enable successful reform.	• Convene high level discussion among public financial management agencies to establish agreement on the reform plan, monitoring, priorities and responsibilities. • Develop capacity for analysis of budget, fiscal framework and audit reports.
Strengthened Budget formulation policies and procedures and establish more realistic Budgets.	• Improve policies for setting expenditure ceilings, including identifying multi-year expenditure commitments. Gain commitment to realistic expenditure ceilings at line ministry and agency level at the beginning of the budget process. • Strengthen information provision for line ministries and agencies on actual, priority and committed expenditures. • Closer coordination between recurrent and capital budgets including unified expenditure plans together with financing plans for capital expenditures.
Better cash management.	• Review baseline expenditures as an input for cash management. • Improve reporting and monitoring of budget execution, including commitments. All line ministries to implement commitment control. • Develop policy on payment of arrears and preventing their recurrence • Strengthen capacity and coordination to improve cash flow forecasting
A medium term fiscal framework should be put in place once macro-fiscal analysis and forecasting capacity is developed.	• Develop a medium term fiscal plan in line with the fiscal Responsibility Law. • Strengthen capacity and develop the analytical information for a medium term framework including projecting credible aggregate fiscal parameters. Develop a simple medium term model. • Improve information flow on fiscal policy within and among ministries and agencies..
A medium term debt strategy should be established once the information base has improved.	• Update the debt strategy in line with the Fiscal Responsibility Law and ensure it is based on clear risk minimization policies. • Gather reliable data, including on guarantees, arrears and domestic securities. Improve procedures for recording information on external grants. • Make debt data available to the public • Increase capacity for debt sustainability analysis. • Expand primary domestic debt market through the provision of longer term instruments and develop a secondary market.
Better accounting, fiscal reporting, internal and external audit and monitoring across local government agencies and SOEs.	• Document the accounting and reporting frameworks and introduce streamlined reporting requirements and formats. • Use the Chart of Accounts in consultation with key data users • Roll out the remainder of the Public Accounting System. • Fuller reporting including of major deviations in budget and financial statement • For both internal and external audit, review legislation, clarify responsibilities and develop capacity. Make external audits timelier.
Commitment at the political level by the Majlis (Maldives' parliament) to the spending envelope and the composition of spending in addition to the budget aggregate would be important.	

Box 4. Episodes of Large Fiscal Consolidation in Smaller States

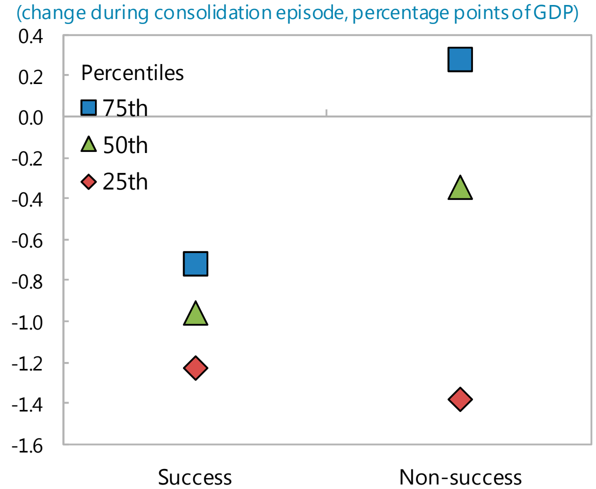
Recent IMF research for the Jamaica Article IV shows that expenditure adjustment measures offer the greatest likelihood of success for durable fiscal consolidation.

- Work on "Smaller Countries and Large Fiscal Adjustments" by Simard, Lonkeng and Lindow looked at 35 cases of large fiscal consolidation for smaller countries since the 1990s.[1] The analysis focused on countries which reduced public debt through improvements in the primary balance (and did not benefit from a reduction in debt through a HIPC or a debt exchange). Successful fiscal consolidations were defined as those where the debt ratio remained lower four years following the fiscal consolidation episode.[2]
- Out of the 35 cases: 14 successfully reduced their debt ratio four years out and 11 of these featured a cumulative improvement in the primary balance over a 5 year period.
- Most countries managed to raise tax revenues during the adjustment period. However, what distinguished the successful cases was a larger reduction in the wage bill (see Charts).
- The findings are similar to those in earlier work by Tsibouris, Horton, Flanagan and Maliszewski on a wider set of countries.[3] They found that expenditure adjustment was associated with durable adjustment but also that it was best done in a multi-year framework.

Tax Revenue
(change during consolidation episode, percentage points of GDP)



Wage Bill
(change during consolidation episode, percentage points of GDP)



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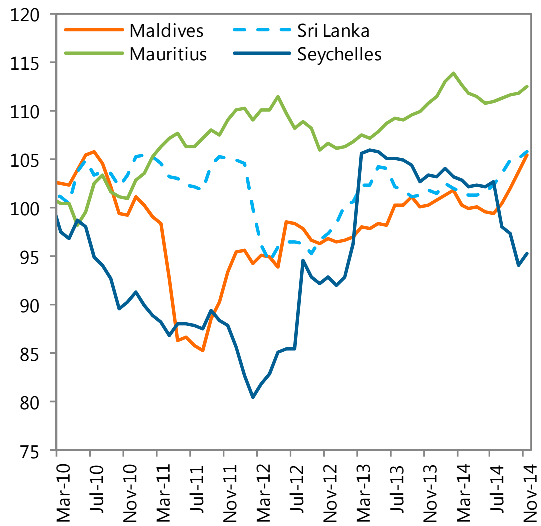
[1] See also Jamaica – Staff Report for the 2014 Article IV consultation and Fourth Review Under the Extended Arrangement Under the EFF. Working Paper forthcoming.
[2] A consolidation is defined as an improvement in the primary fiscal balance by one percentage point of GDP or more and lasts as long as the primary fiscal balance does not deteriorate compared to the previous year.
[3] "Experience with Large Fiscal Adjustments" Occasional Paper 246, 2006.

EXTERNAL SECTOR ASSESSMENT

Background

18. The real exchange rate quickly appreciated by around 20 percent following the 2011 devaluation as rapid inflation pass through more than offset the exchange rate devaluation. Since the April 2011 devaluation, Maldives has retained a de facto stabilized exchange rate regime.[7] Although the band is wide at 20 percent either side of Rf 12.85 per dollar, the exchange rate has remained at the weakest end of the band (Rf 15.42 per dollar) and operates like a de facto peg. The benefits of the devaluation were quickly eroded by higher inflation in Maldives relative to trading partners. But over the past eighteen months Maldives inflation performance has improved and the real exchange rate has been broadly flat (text figure).

Real Effective Exchange Rate, 2010–14
(Index, 2010 Jan=100)



19. External indicators and the current account deficit (following data revisions) look somewhat healthier.

- The estimated current account deficit, though still quite high, is much smaller than previously reported and is expected to be 8.1 percent of GDP in 2014 (up a little from 2013). Lower oil prices will help narrow the current account deficit in 2015.
- The MMA has been able to increase its supply of foreign exchange to the market, likely reflecting higher dollar inflows. Gross official reserves have risen to $614mn, but are low compared to standard reserve adequacy indicators (around 2.8 months imports) and usable reserves are just $132mn (0.6 months imports).

Staff's Position

20. The external sector assessment is difficult given the large turnover in the parallel fx market and data issues—but on balance the external sector position seems modestly weak.

- *Standard indicators* would point to an external sector position that is moderately weaker than fundamentals and desirable policies and a real exchange that that is moderately overvalued. The Fund's empirical approaches for smaller countries (EBA lite and a CGER-type methodology) applied to the revised official data point to a current account gap of around 3 percent of GDP and a real exchange rate overvaluation of around 5 percent (Box 5). Low reserves levels also indicate external sector weakness.

[7] The de jure exchange rate regime is a pegged exchange rate within horizontal bands.

- *Other considerations*, point to less of an imbalance (i.e. only modestly weaker). With a low level of reserves, the MMA is only able to supply only a small fraction of foreign exchange demand with the excess satisfied in the parallel market (Box 6), and the premium has remained stable and low for an extended period. Surveys and anecdote suggest that—even after revisions—tourism exports likely remain underestimated; but by how much is uncertain within a wide range from US$100mn-2bn (3-75 percent of GDP), (Box 5). Though if under-recording was very high, imports would also likely be under-reported, significantly offsetting the effect on the current account. Nonetheless, underestimation of tourism revenues could easily be sufficient to eliminate the current account gap.
- *Fiscal consolidation*. The loose fiscal stance explains two thirds of the current account gap.[8] Undertaking the fiscal adjustment implied by the 2015 Budget will help halve the gap.

Overall, the external sector position looks modestly weaker than fundamentals and desirable policies and the exchange rate modestly overvalued. No exchange rate adjustment is warranted at present. The stabilized exchange rate regime is suitable for Maldives in view of the very high openness of its goods and services market, the dollarized nature of the economy, and the large seasonal variation in tourism revenues.

Authorities' Views

21. The authorities are committed to maintaining the exchange rate within the current band and agree that a stabilized regime suits their needs. They view past exchange rate devaluations as being unsuccessful. In particular, the April 2011 devaluation did not achieve a durable impact on imbalances. Without an effective incomes policy, wages in the public and private sectors rose quickly back to previous real levels and the parallel market premium reappeared. Improving the fiscal position is viewed as the best way to sustain the exchange rate within its current band. The parallel foreign exchange market has been in place for a long time and appeared with the rapid development of tourism in the economy. The premium has fallen back to around 3 to 4 percent but it is structural in nature and unlikely to be eliminated completely. The authorities agreed that there would likely be no change on Article VIII issues until official reserves levels had increased and the fiscal position improved, the data revisions to the current account are based on substantial improvements in methodologies and the new data are much more consistent with other indicators and developments in the economy. The extent of any under-recording of tourism expenditures is likely to be small.

[8] Work on microstates suggests an improvement in the cyclically adjusted primary balance of 1 percent of GDP can improve the current account by around 0,4 percent of GDP Endeganew, Amo-Yartey and Turner Jones" Fiscal Policy and the Current Account. Are Microstates Different? WP/12/51.

Box 5. The Operation of Maldives Parallel Foreign Exchange Market

Maldives has a de-facto stabilized exchange rate regime, while the foreign exchange regime is very open, there is a long history of an active parallel foreign exchange market, and the premium is relatively stable. The tourist industry appears to be a key supplier and driver of the parallel market. The scale of the premium has ranged from around 5 to 15 percent, and during 2014 it fell back to just 3 to 4 percent. The relatively steady premium may reflect the oligopolistic nature of the market.

- There are only a few large suppliers of foreign exchange who are able to adjust supply to the parallel foreign exchange market—based on the observed premium and where marginal costs equal marginal revenue.
- There is a positive relationship between the premium and supply given the profit motive to benefit from an increased spread. If the suppliers of foreign exchange formed a cartel they could behave as monopolists and drive up the premium. But in practice, as each supplier's total holdings of foreign currency (in Maldives and abroad) is large and the ability to supply foreign exchange to benefit from any change in the premium is high, the cartel appears unstable and the premium remains bounded within a narrow stability range but it is not arbitraged away.
- The relationship between the supply of dollars and the premium may be non-linear. Occasional hikes in premia can occur with expectations of a potential devaluation and heightened macroeconomic risk.

Since the global financial crisis, the appearance of a parallel market premium and a shortage of foreign exchange at the official rate has continued to give rise to exchange restrictions and a multiple currency practice (MCP). Maldives is an Article XIV member but maintains exchange restrictions and a MCP under Article VIII Sections 2 (a) and 3 which have been in place since 2009.[1/] These arise from the MMA's foreign exchange rationing and greater than 2 percent parallel market premium. Although these measures are non discriminatory, Fund approval is not recommended as they are unlikely to be temporary and would be eliminated only once official reserves levels are higher and the fiscal position has improved. The existing restriction arising from rationing has eased, with the MMA increasing the foreign exchange provided to commercial banks from $3 million to $4 million a week from September 2013.[2/]

[1/] See Informational Annex.

[/2] Staff continues to engage with the authorities in order to finalize its assessment of Maldives' exchange system.

Box 6. Estimates of Tourism Spending and External Sector Assessment

Anecdotal evidence suggests that tourist spending in Maldives may be underestimated (and the current account deficit overestimated). Unfortunately it is not possible to check the official data against partner countries as these data are not collected for tourism services. To come up with ball park estimates of actual tourism expenditures, staff used three approaches:

a) Using the *Ministry of Tourism survey* to estimate expenditures (from arrivals and individuals' reported spending habits) points to an estimate as high as $4.3bn (double official estimates). But the survey has drawbacks. It only asks about ranges of spending, it may indistinguishably include airfares and spending in nearby economies such as Sri Lanka, it is conducted for one month in February (high season) each year and the response rate is low (25 percent). Given these caveats, the survey is likely an overestimate of tourist spending.

Estimates of Tourist Spending Per Arrival

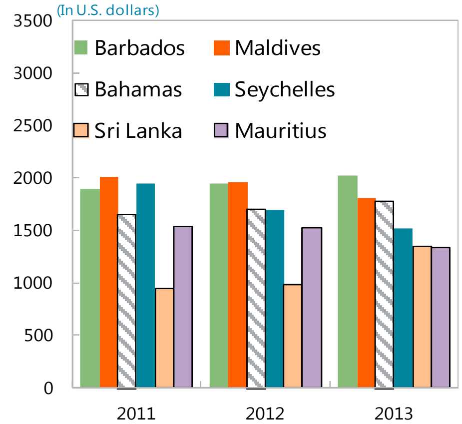
	Spending Per Arrival	Annual Revenue Estimate	Difference from official data
	US Dollars	$ Millions	Percent
Official data	1,877	2,112	
Survey of tourists spending habits (conducted peak season)	3,873	4,357	106
Back of the Envelope based on internet prices	3,703	4,166	97
Estimate that would reduce errors and omissions in the BoP	2,065	2,323	10

b) *A sample of internet pricing* from a range of resorts also points to spending roughly double the recorded estimates.

c) *Errors and omissions* in the BoP statistics might also indicate the extent to which flows are mis-recorded. In 2013 (after data revisions) errors and omissions were $97mn. This would point to receipts of $2.4bn. However, this estimate would not capture flows kept offshore by residents (that return later as FDI).

Tourism Receipts per Arrival

(In U.S. dollars)



Sources: World Travel and Tourism Council; Authories data and IMF staff estimates.

Cross-country comparisons with tourism-dependent small islands suggests that the discrepancy could be relatively small. Comparisons do not point to Maldives as being a big outlier—only Barbados recorded higher spending per tourist in 2013.

The range of possible under-recording of receipts is very large from around $100mn to up to $2bn. But if under-recording of receipts was at the high end of these estimates, outflows such as imports would also likely be under-recorded—with a smaller net effect on the current account.

Quantified approaches. Using the official data (and an estimate for under-recording of $100mn) staff looked at the standard quantified approaches to assess the external position.

- The approaches estimate the current account norm to be between -4.8 to -5.7 percent of GDP.
- The resulting current account gap is estimated to be in the range from 0.2 to -3.6 percent of GDP. EBA lite, suggests the fiscal policy gap can explain 2 percent of GDP of the current account gap.
- The corresponding REER estimates range from a small undervaluation to an overvaluation of up to 5 percent.

External Sector Position: Baseline Scenario1/ (Percent of GDP)

	EBA Lite Approach		ES Approach	
	Official data	Staff estimate2/	Official data	Staff estimate
Current Account Norm	-4.8		-5.7	
Current Account Balance (underlying)	-8.4	-5.5	-8.4	-5.5
Current Account Gap	**-3.6**	**-0.7**	**-2.7**	**0.2**
Elasticity 3/	-0.70		-0.70	
REER overvaluation estimate (percent)	**5.1**	**1.1**	**3.8**	**-0.3**

Source: IMF staff estimates and projections.

1/ All figures are based on the projection for 2014. Macrobalance approach is the new EBA lite approach. External Sustainabiity Approach based on Vitek 2010.

2/ Staff estimate based on a conservative assumption of underestimation of tourist revenues and partly offset by income flows: that revenues are underestimated by around $100mn.

3/ The trade elasiticity comes from Tokarick 2010 and takes into account exports are likely to be price inelastic

SUPPORTING MONETARY AND FINANCIAL POLICIES

Background

22. **The policy stance has eased since the start of 2014 with measures that staff view as being aimed at facilitating government financing.** The high minimum reserve requirement was cut; the MMA took steps to convert the government's overdraft (6.8 percent of GDP) into a non tradable long-term bond; administered yields on Treasury bills were lowered; and the MMA halted liquidity absorbing open market operations. Despite lower yields, banks (and Maldives Pension Fund) have continued to purchase Treasury Bills, given limited market development, and in preference to lending. Recently, banks have found it difficult to access correspondent banking services, as overseas banks reassessed their business models; this has made it difficult to obtain letters of credit and process remittances.

Staff's Position

23. **Staff did not support the monetization of the fiscal deficit and welcomes the authorities' commitment to resist this going forward.** This would help direct monetary policy at supporting the current exchange rate band. In addition, the MMA should charge rates on government advances and long-term bonds that exceed T-bill yields. As the fiscal position improves, greater use should be made of market based financing of government debt. To promote nonbank participation, the government securities market could be developed, with longer term instruments, primary dealers, and a secondary market.

24. **Fuller information on the operation of the foreign exchange market would support policy making.** More comprehensive information on money changer activities, with regular data collection, analysis and closer supervision of large fx operators would assist policy decisions.

25. **A firmer approach to supervision remains necessary.** Banks are broadly in compliance with prudential regulations, though one bank has breached single borrower limits and another foreign currency exposure limits. Nonetheless, the accuracy of financial soundness indicators deserves close scrutiny. The MMA has rightly resisted pressure to count capital held offshore when calculating compliance with single borrower limits. Standards for financial institutions that may in the future set up in SEZs should be equivalent to those onshore, with similar prudential, supervisory and reporting requirements, including with regard to AML/CFT.

Authorities' Views

26. **The authorities were of the view that the MMA measures taken earlier in the year had helped tackle the large government overdraft legacy.** This had helped put policy on a firmer footing and would make Fiscal Sustainability Law targets attainable going forward. They agreed that public debt market development was a high priority and were working on ways to open up the Treasury Bill market to the non-bank private sector and to develop longer term instruments. Since the beginning of 2014, the MMA had begun to collect more regular information on money changer

activities. The MMA is also continuously working to strengthen supervision and regulations are being developed to supplement the legislation on SEZs.

MEDIUM TERM AND OTHER ISSUES

A. Economic Diversification and Service Provision

Background

27. Maldives' geography—while a central attribute for the tourism industry—imposes high costs in terms of public service provision. Over the longer term, the government is considering ways to develop regional hubs and improve transport connectivity which could also encourage voluntary resettlement. This would enable higher quality service provision at lower cost in key areas such as education. However, putting in place such a change will take many years as it requires a broad national consensus, adequate incentives, and compensation. The government is also planning two large infrastructure projects—airport expansion and a road bridge between Male and the airport financed by official bilateral loans. There are environmental challenges from tourism and infrastructure development. The UN is encouraging the development of a comprehensive long-term national climate change adaptation strategy for Maldives which could help mobilize grants and concessional loans. An increased share of renewable energy will help reduce reliance on oil imports.

28. The SEZs are a key part of government's strategy for diversification into labor intensive sectors such as off-port shipping services, IT and financial services. Youth unemployment is high in Maldives and education attainment at upper secondary level lags behind other economies (Table 6); and consequently the tourism industry typically recruits many workers from abroad rather than from Maldives (due to skills mismatch).[9] The SEZ scheme which will have mixed activity (with a 40 percent limit on activity devoted to tourism) will aim at providing job opportunities for Maldivian workers. However, the details of specific SEZs have yet to be worked out.

Staff's Position

29. Careful planning of infrastructure investment scale up will help ensure it adds to growth. To help maximize the future growth benefits of the planned infrastructure projects and keep down costs, it will be necessary to avoid over-stretching the economy's construction capacity. Financing arrangements should be carefully assessed so that only quality projects with high social and growth impact are undertaken, with adequate social and environmental safeguards also in place.

30. Economic diversification into new sectors is welcome but public sector support for these initiatives needs to be contained, given debt sustainability challenges. Strict ring-fencing of SEZ tax exemptions is necessary to limit foregone tax revenue and preserve the current relatively

[9] Maldives is on track to meet most Millennium Development Goals (MDGs), and has already met many of them (Table 6). Efforts on gender equality and empowering women as well as ensuring environmental sustainability and effective adaptation to climate change will need to be sustained to reach these MDGs.

simple tax system (which has few exemptions), with adequate reporting of tax expenditures. Beyond the SEZs, there is scope to reduce the reliance of tourism on imported foodstuffs by developing links between tourism, traditional fisheries, and small-scale agriculture, in order to raise the domestic value added from tourism and spread the economic benefits more widely. Boosting access to financial services and raising connectivity of renewables-generated electricity for small and medium-size businesses would enhance the business climate and substantially reduce the cost of electricity generation (among the highest in South Asia) and related subsidies.

Authorities' Views

31. Maldives faces unique challenges as small island nation with a dispersed population across many islands. The tourism sector will remain the growth engine, propelled by private sector innovation which has successfully capitalized on the natural beauty of the islands, adapted to new markets and put Maldives on the global destination map. Addressing diversification and climate adaptation requires unorthodox thinking. The SEZs will help link tourism to other industries and services. The authorities noted staff's concerns about the development of SEZs and emphasized that tax exemptions would be ring-fenced; and regulations would be developed to safeguard offshore financial sector standards and data provision.

B. Data Issues

Background

32. Statistics have been strengthened in recent years. Maldives is a member of GDDS and substantial improvements have been made to price, national accounts and balance of payments statistics, supported by technical assistance (see Informational Annex).

Staff's Position

33. Notwithstanding this improvement, data gaps complicate policymaking. The reliability of the balance of payments data is uncertain—in part as it is inherently difficult to capture full data with many transactions occurring outside the country and with no international counterparty data on tourism services to validate revenue estimates. GDP methodology can be updated, including finalizing the expenditure measure. The fiscal chart of accounts (under development) is crucial for budget accuracy. A statistics law providing the legal authority to collect data from the nonfinancial corporate sector and households would greatly enhance data provision.

Authorities' Views

34. Further work is underway to improve the balance of payments and national accounts statistics and a fiscal chart of accounts is being put in pl ace. The authorities intend to submit a revised draft statistics law to the Majlis but no timetable has yet been set for this.

STAFF APPRAISAL

35. Maldives has rapidly grown into a middle income country, driven by tourism development. Over the past two years, the real economy has picked up. Tourist activity has recovered, driven by a rapid expansion of new Asian markets and Maldives has performed well relative to peers. The external sector has broadly stabilized and inflation is contained.

36. Public debt is elevated, the fiscal deficit has widened and consolidation is necessary to ensure sustainability. The authorities' 2015 Budget is an important step toward adjustment, containing revenue raising measures, better targeting of subsidies and a public employment freeze. But this may be insufficient to bring debt ratios down and some measures are only temporary. With limited policy buffers, the risks of fiscal slippages are high and the economy is vulnerable to external shocks.

37. Greater and more durable fiscal adjustment through additional expenditure restraint would place the debt ratio firmly on a downward path. Staff recommend additional adjustment of 3 percentage points of GDP by 2019, focusing on spending restraint. Establishing a public sector wage body would help ensure consistency in pay setting across the public sector and restrain the wage bill. It should be accompanied by firmer control of other current spending. A further rise in TGST would underpin revenues and help reduce debt. Stronger public financial management, preceded by a review of baseline expenditures, and compliance with the Fiscal Responsibility Law, would raise the probability of successful fiscal adjustment.

38. The assessment of the external position is highly uncertain given data issues, but on balance it looks modestly weaker than implied by fundamentals and desirable policies. Following revision, the reported current account deficit is substantially narrower than previously estimated. And tourism expenditures may still be underestimated and the current account deficit overstated. The real exchange rate has been broadly stable recently and the parallel market premium has narrowed. Overall, the external position appears modestly weaker than fundamentals and desirable policies, and the real exchange rate modestly overvalued (within a large uncertainty range). The stabilized exchange rate regime remains suitable for Maldives. However, with low levels of official reserves, the MMA continues to ration foreign exchange to commercial banks and the parallel market premium is greater than 2 percent leading to a multiple currency practice and exchange restrictions. Without a timetable for removal of these measures, Fund approval is not sought at this time.

39. Support from monetary and financial policies would help build buffers. The authorities' determination to resist monetization is welcome. Work strengthening financial supervision should continue, including ensuring consistent and high standards for institutions that choose to operate in SEZs.

40. Public service delivery and economic diversification are key medium-term challenges. Encouraging regional hubs and better connectivity would help support service provision but will take many years. Careful planning of infrastructure investment scale up will help ensure it adds to growth.

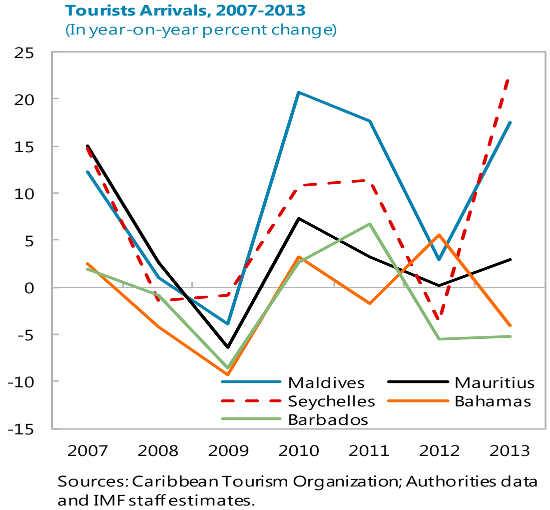
Diversification of economic activity into new sectors—such as through SEZs—is welcome but strict ring-fencing of SEZ tax exemptions is needed to preserve the tax base.

41. Statistics should be further strengthened. Work should continue on national accounts, balance of payments and a chart of accounts. A statistics law would greatly improve data provision.

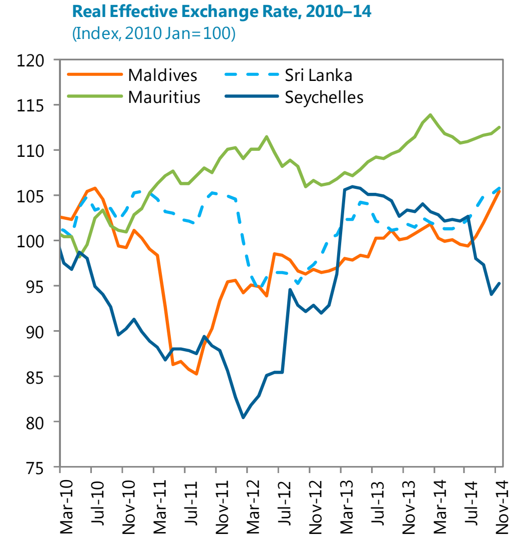
42. It is recommended that the next Article IV consultation be held on the standard 12 month cycle.

Figure 1. Comparison with Other Tourist Dependent Economies

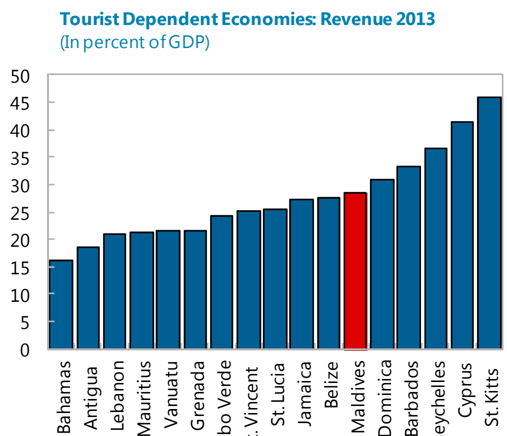
Tourism has performed well compared to competitors



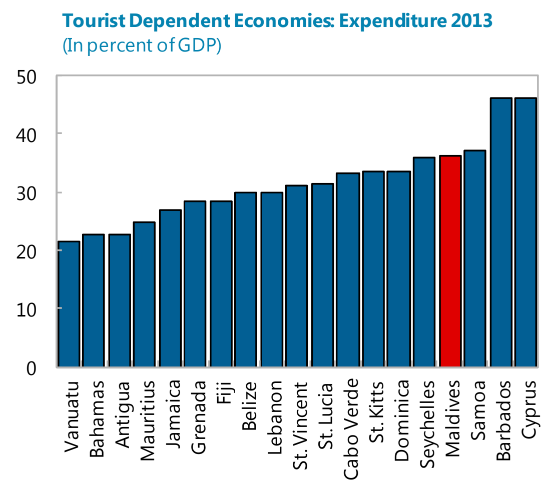
...and the real exchange rate is broadly stable.



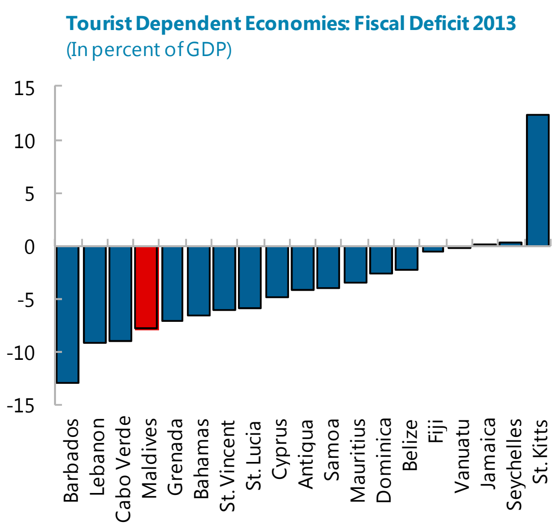
Fiscal Revenues are high compared to others



...but expenditures are high and increasing.



The overall fiscal deficit is large...



...despite relatively high indirect tax rates and good revenue performance.

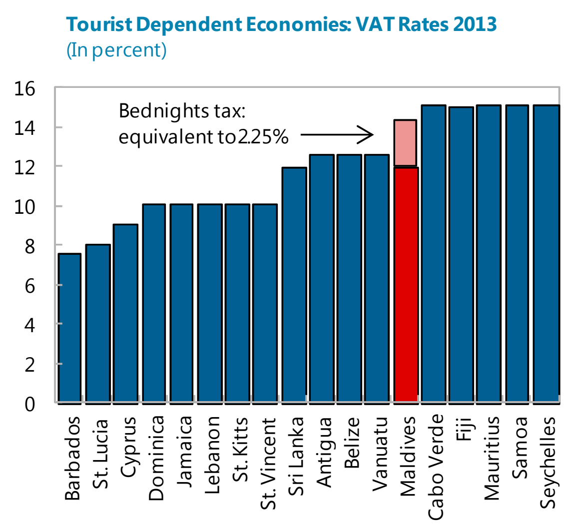
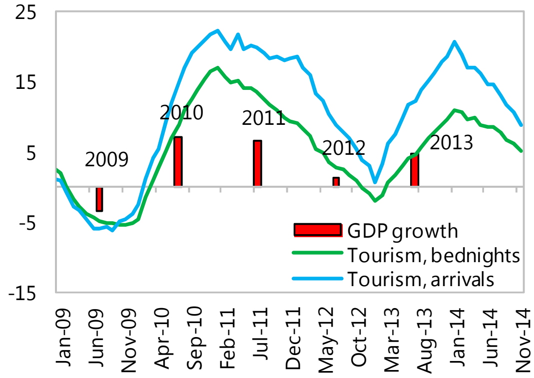


Figure 2. Maldives: Real and External Sector Developments

Tourism growth has picked up from a 2012 trough.

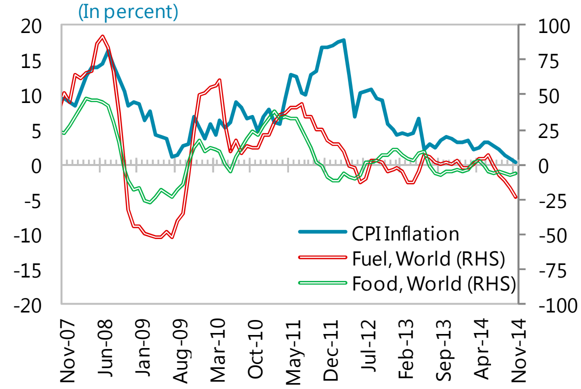
Tourism
(12-mo moving average growth, in percent)



Sources: Maldivian authorities; and IMF staff estimates.

Inflation is contained by low import price inflation.

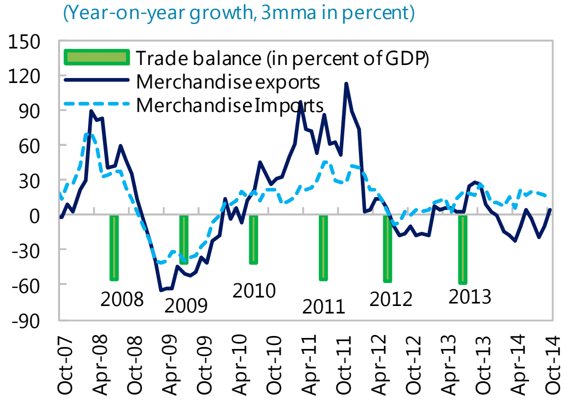
Inflation
(In percent)



Sources: Maldivian authorities; and IMF staff estimates.

Goods trade is a little weaker with a drop in volatile fish exports.

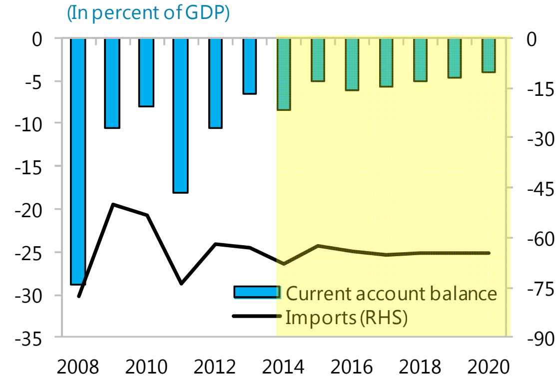
Merchandise Exports and Total Imports
(Year-on-year growth, 3mma in percent)



Sources: Maldivian authorities; and IMF staff estimates.

Current account data have been revised and the deficit is substantially smaller than in earlier years

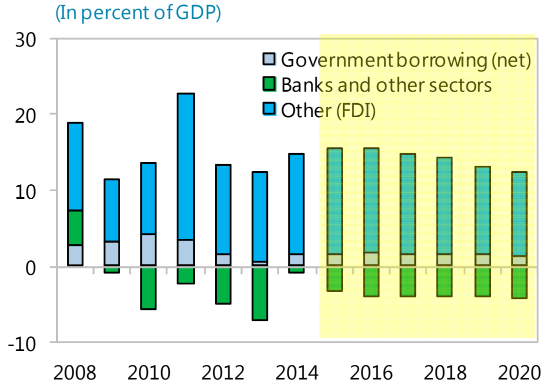
External Current Account
(In percent of GDP)



Sources: Maldivian authorities; and IMF staff estimates.

FDI inflows are offsetting other outflows

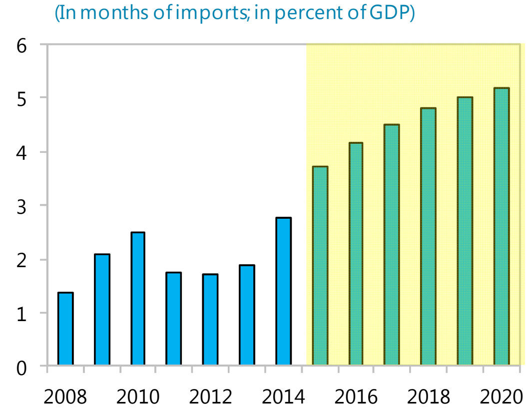
Capital Account
(In percent of GDP)



Sources: Maldivian authorities; and IMF staff estimates.

…Reserve cover has increased but is still low….

International Reserves
(In months of imports; in percent of GDP)

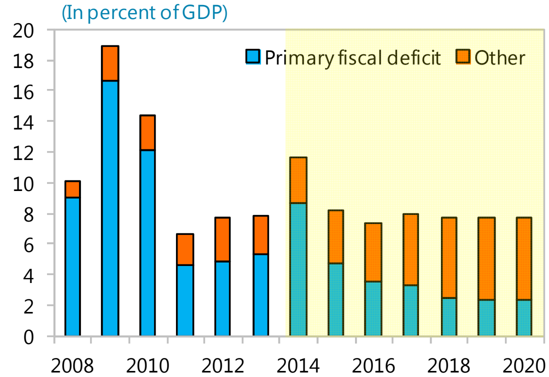


Sources: Maldivian authorities; and IMF staff estimates.

Figure 3. Maldives: Fiscal Developments

High primary deficits drive the weak fiscal position…the 2015 Budget will rein in the deficit

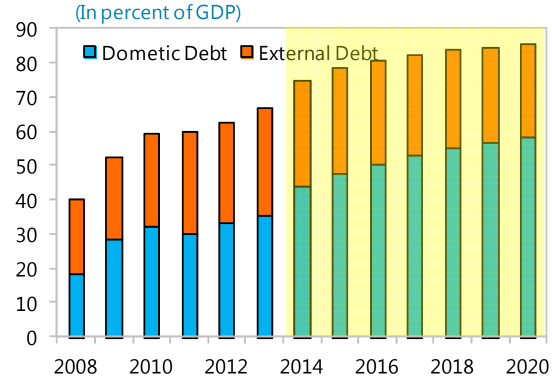
Overall Fiscal Deficit
(In percent of GDP)



Sources: Maldivian authorities; and IMF staff estimates.

… but not sufficiently to stop public debt rising

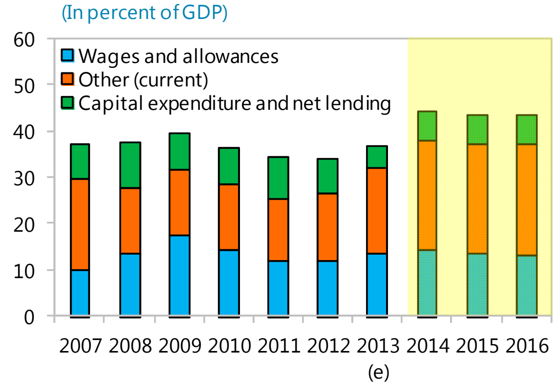
Public Debt
(In percent of GDP)



Sources: Maldivian authorities; and IMF staff estimates.

The spending structure is rigid—wages, pensions, subsidies and social welfare at close to 30% of GDP

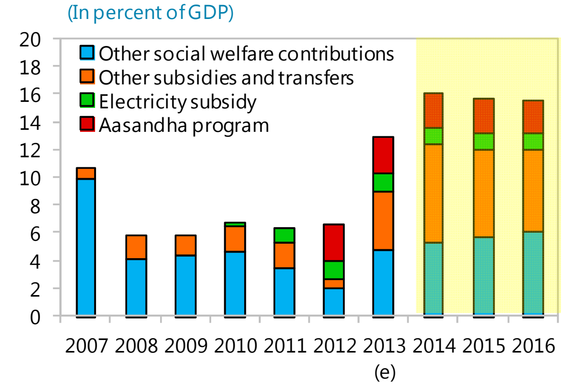
Central Government Expenditure
(In percent of GDP)



Sources: Maldivian authorities; and IMF staff estimates.

…with subsidies and social welfare schemes being poorly targeted.

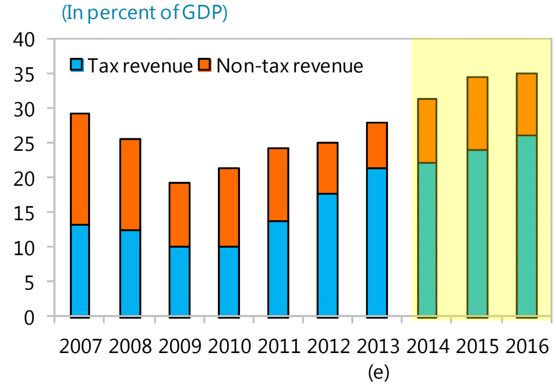
Social Welfare, Subsidies and Transfers
(In percent of GDP)



Sources: Maldivian authorities; and IMF staff estimates.

New and sustainable tax measures have helped raise the revenue ratio since 2009

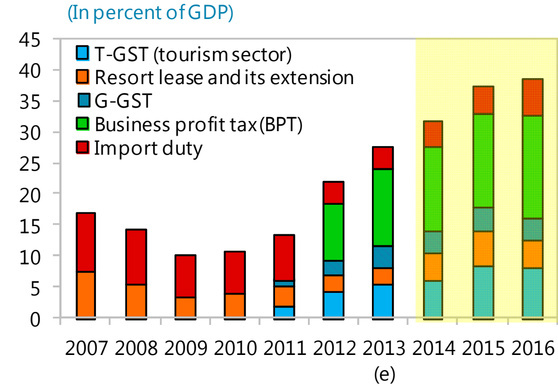
Central Government Revenue
(In percent of GDP)



Sources: Maldivian authorities; and IMF staff estimates.

Overall revenue buoyancy, together with that of main tax items remains positive.

Major Tax and Non-tax Receipts
(In percent of GDP)

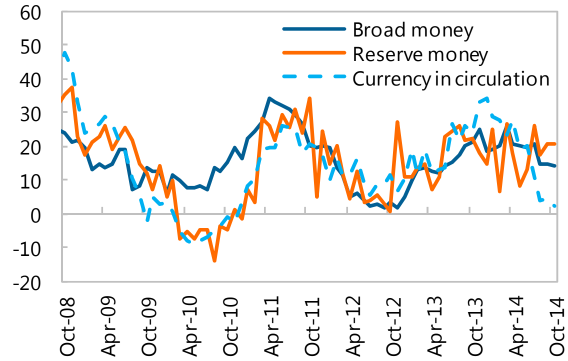


Sources: Maldivian authorities; and IMF staff estimates.

Figure 4. Maldives: Monetary and Financial Sector Developments

Monetary aggregates have picked up reflecting larger fiscal deficits and monetization

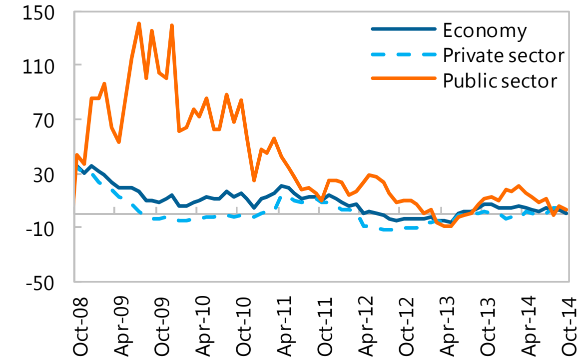
Monetary Variables
(Year-on-year growth, in percent)



Sources: Maldivian authorities; and IMF staff estimates

........But credit is subdued.

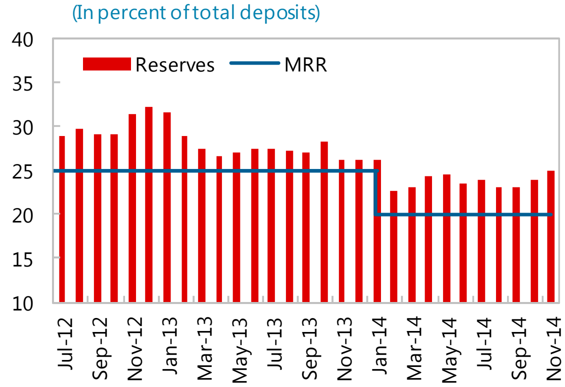
Credit
(Year-on-year growth, in percent)



Sources: Maldivian authorities; and IMF staff estimates.

The recent cut in reserve requirements has boosted commercial bank excess reserves

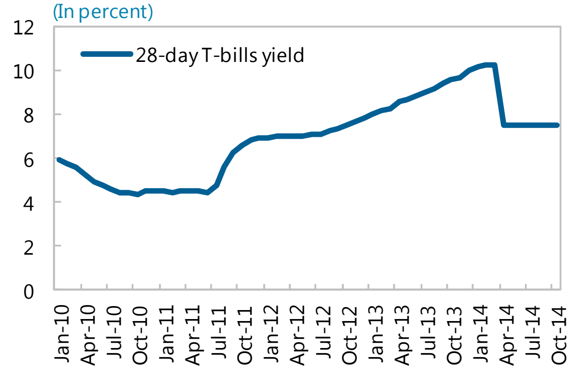
Commercial Banks' Reserves
(In percent of total deposits)



Sources: Maldivian authorities; and IMF staff estimates.

..........Cuts in treasury bill yields have not dampened purchases

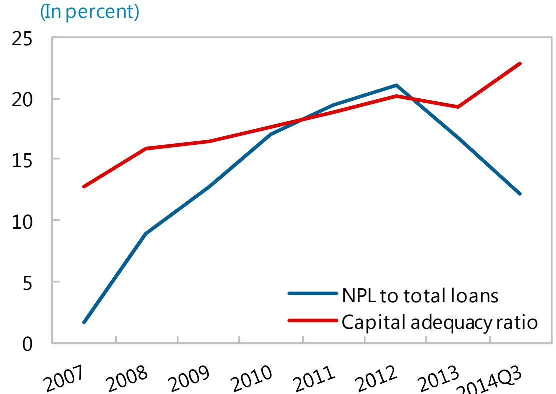
T-Bills Yields 1/
(In percent)



Sources: Maldivian authorities; and IMF staff estimates.
1/ Monthly average of weighted average yields.

The decline in NPLs is a result of better performance in the tourism sector

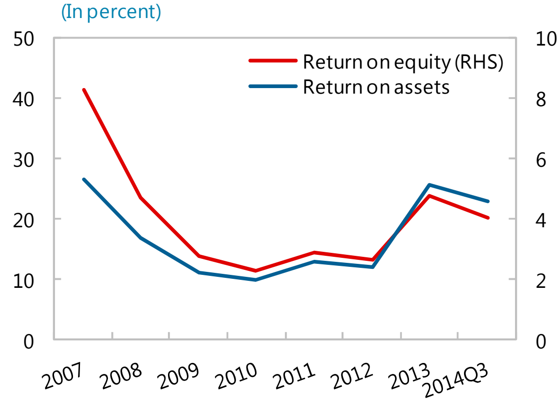
Commercial Banks' Capital and Credit Quality Indicators
(In percent)



Source: Maldivian authorities.

..........with increased profitability on receivables from investments in resorts.

Commercial Banks' Profitability Indicators
(In percent)



Source: Maldivian authorities.

Table 1. Maldives: Selected Economic Indicators, 2011–19 (Staff's Baseline Scenario)

Population (in 1,000; 2012 est.)	331
GDP per capita (in U.S. dollars; 2012 est.):	6,675
Quota (in million SDRs):	10.0

	2011	2012	2013	2014	2015	2016	2017	2018	2019
			Est.			Proj.			
Output and prices	(Annual percentage change)								
Real GDP	6.5	1.3	4.7	5.0	5.0	3.9	4.2	4.4	4.6
Inflation (end-of-period) 1/	16.7	5.4	3.1	1.2	0.4	2.8	4.0	4.5	4.5
Inflation (period average) 1/	11.3	10.9	4.0	2.5	0.3	2.1	3.5	4.3	4.3
GDP deflator	8.6	6.8	-0.9	0.7	1.5	3.0	4.1	4.2	4.1
Central government finances									
Revenue and grants	27.6	26.0	28.6	32.4	35.3	35.9	35.4	35.2	34.9
Expenditure and net lending	34.1	33.7	36.5	44.0	43.4	43.1	43.3	42.9	42.6
Overall balance	-6.6	-7.6	-7.8	-11.6	-8.1	-7.3	-7.9	-7.7	-7.6
Overall balance excl. grants	-8.6	-8.6	-8.1	-12.6	-8.8	-7.9	-8.4	-8.1	-8.0
Primary balance	-4.5	-4.8	-5.3	-8.7	-4.6	-3.5	-3.3	-2.4	-2.4
Public and publicly guaranteed debt	59.9	62.8	66.7	75.0	78.6	80.7	82.5	83.7	84.5
Monetary accounts	(Annual percentage change, unless otherwise indicated)								
Broad money	20.1	6.4	16.8	17.9	6.6	8.5	8.5	8.7	9.0
Domestic credit	11.3	-2.4	3.9	5.4	5.0	7.0	8.5	8.7	9.0
Balance of payments	(In percent of GDP, unless otherwise indicated)								
Current account	-18.1	-10.6	-6.5	-8.4	-5.0	-6.2	-5.6	-5.1	-4.7
Of which:									
Exports	14.9	12.4	12.3	12.9	10.3	9.5	9.7	10.3	10.6
Imports	-73.6	-62.2	-63.1	-68.0	-62.4	-64.3	-65.4	-64.9	-64.7
Tourism receipts and nonfactor services, net	64.2	60.4	68.6	72.1	73.8	74.7	76.0	75.3	75.2
Income (net)	-13.2	-11.0	-13.7	-14.7	-15.2	-14.9	-14.6	-14.6	-14.4
Current transfers	-10.4	-10.2	-10.6	-10.9	-11.5	-11.3	-11.3	-11.4	-11.4
Capital and financial account (including e&o)	17.5	9.4	8.9	17.0	12.2	11.6	10.8	10.1	8.9
Of which:									
General government, net	3.4	1.6	0.7	1.4	1.7	1.7	1.5	1.6	1.5
Banks and other sectors, net	-2.1	-5.0	-7.0	-0.8	-3.2	-4.0	-4.0	-4.1	-4.1
Overall balance	-0.7	-1.2	2.4	8.6	7.2	5.3	5.2	4.9	4.3
Gross international reserves (in millions of US$; e.o.p.) 2/	335	305	368	614	832	1,005	1,188	1,377	1,555
In months of GNFS imports	1.7	1.7	1.9	2.8	3.7	4.1	4.5	4.8	5.0
Memorandum items:									
GDP (in millions of rufiyaa)	35,931	38,943	41,569	43,971	46,863	50,177	54,427	59,189	64,488
GDP (in millions of U.S. dollars)	2,332	2,534	2,699	2,855	3,043	3,258	3,534	3,843	4,188
Tourism bednights (000')	6,529	6,451	7,045	7,503	7,916	8,311	8,311	8,810	9,899
Tourism bednights (% change)	9.1	-1.2	9.2	6.5	5.5	5.0	6.0	6.0	6.0
Dollarization ratio (FC deposits in percent of broad money) 3/	49.5	49.2	50.2	51.8					

Sources: Maldivian authorities; and IMF staff estimates and projections.
1/ CPI-Male definition.
2/ MMA liabilities, include allocation of SDR 7.4 million, equivalent to US$11.7 million, made available in Q3 2009, see http://www.imf.org/external/np/tre/sdr/proposal/2009/0709.htm. These are treated as long term liabilities of the MMA.
3/ For the first 9 months of the year 2014.

Table 2a. Maldives: Central Government Finances, 2011–19 (Staff's Baseline Scenario)
(In millions of rufiyaa)

	2011	2012	2013		2014	2015	2016	2017	2018	2019
			Budget	Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	9,905	10,138	12,609	11,900	14,240	16,535	18,000	19,261	20,840	22,529
Revenue (excluding privatization receipts)	9,172	9,771	12,049	11,783	13,825	16,195	17,701	19,009	20,594	22,255
Tax revenue	4,893	6,803	8,469	8,771	9,723	11,174	13,051	14,179	15,249	16,342
Import duties	2,587	1,369	1,642	1,576	1,827	2,133	2,835	3,245	3,587	3,894
Airport service charge	338	300	392	350	394	500	525	556	589	625
Business profit tax (BPT)	35	1,401	1,594	1,881	2,113	2,331	2,562	2,779	2,943	3,116
Goods and services tax (GST)	908	2,559	3,877	3,693	4,178	5,559	5,859	6,240	6,651	7,096
Of which: General GST	243	1,006	1,029	1,538	1,568	1,746	1,856	1,996	2,153	2,328
Tourism GST	665	1,554	2,848	2,155	2,610	3,813	4,003	4,244	4,498	4,768
Tourism tax ($8 bed tax) 1/	751	805	434	862	770	183	768	814	885	965
Other	275	369	249	410	440	469	503	545	593	646
Nontax revenue	3,745	2,920	3,572	2,743	3,976	4,887	4,506	4,675	5,175	5,729
SOE profit transfers	974	633	675	476	785	836	895	971	1,056	1,151
Royalties, land, and resort rent	1,312	1,187	1,878	1,287	2,065	2,851	2,326	2,310	2,603	2,927
Other	1,459	1,100	1,019	981	1,126	1,200	1,285	1,393	1,515	1,651
Capital revenue	534	48	7	268	126	134	144	156	169	185
Grants	733	367	560	118	415	340	299	252	247	274
Expenditure and net lending	12,265	13,110	13,973	15,153	19,350	20,338	21,647	23,563	25,395	27,442
Current expenditure	9,076	10,317	10,265	13,195	16,054	16,858	17,955	19,601	21,512	23,083
Of which: Salaries and allowances	4,281	4,559	5,363	5,606	6,152	6,242	6,403	6,691	7,061	7,454
Transportation, communication, and utilities	991	1,035	616	1,226	1,296	1,354	1,464	1,588	1,814	2,035
Social welfare contributions	1,231	1,903	1,433	1,954	2,292	2,647	3,034	3,478	3,961	4,316
Repairs and maintenance	128	195	15	371	393	419	448	486	529	576
Subsidies and transfers	998	690	1,327	1,774	3,115	2,960	2,972	2,961	2,971	3,106
Interest	726	1,107	1,049	1,058	1,295	1,626	1,909	2,528	3,144	3,381
Other	721	826	463	1,206	1,510	1,609	1,723	1,869	2,033	2,215
Capital expenditure	3,588	2,884	3,819	2,093	2,940	3,133	3,355	3,639	3,957	4,312
Net lending	-399	-90	-111	-136	-143	-153	-164	-177	-75	48
Overall balance	-2,360	-2,972	-1,364	-3,253	-5,111	-3,803	-3,647	-4,302	-4,555	-4,914
Overall balance, excluding grants	-3,093	-3,339	-1,924	-3,370	-5,526	-4,143	-3,946	-4,553	-4,802	-5,188
Financing 2/	2,360	2,972	1,364	3,253	5,111	3,803	3,647	4,302	4,555	4,914
Privatization	377	0	...	0	0	0	0	0	0	0
External	968	772	...	1,425	638	775	877	835	944	944
Domestic	1,015	2,200	...	1,828	4,473	3,028	2,770	3,467	3,611	3,970
MMA					537	303	277	347	361	397
Commericial banks					2,908	1,817	1,662	2,080	2,167	2,382
Other					1,029	908	831	1,040	1,083	1,191

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

1/ The bed tax will be eliminated from November 2014.

2/ Includes unidentified financing.

Table 2b. Maldives: Central Government Finances, 2011–19 (Staff's Baseline Scenario)

(In percent of GDP, unless otherwise specified)

	2011	2012	2013		2014	2015	2016	2017	2018	2019
			Budget	Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	27.6	26.0	33.0	28.6	32.4	35.3	35.9	35.4	35.2	34.9
Revenue (excluding privatization receipts)	25.5	25.1	31.6	28.3	31.4	34.6	35.3	34.9	34.8	34.5
Tax revenue	13.6	17.5	22.2	21.1	22.1	23.8	26.0	26.1	25.8	25.3
Import duties	7.2	3.5	4.3	3.8	4.2	4.6	5.6	6.0	6.1	6.0
Nontax revenue	10.4	7.5	9.4	6.6	9.0	10.4	9.0	8.6	8.7	8.9
SOE profit transfers	2.7	1.6	1.8	1.1	1.8	1.8	1.8	1.8	1.8	1.8
Royalties, land, and resort rent	3.7	3.0	4.9	3.1	4.7	6.1	4.6	4.2	4.4	4.5
Other	4.1	2.8	2.7	2.4	2.6	2.6	2.6	2.6	2.6	2.6
Capital revenue	1.5	0.1	0.0	0.6	0.3	0.3	0.3	0.3	0.3	0.3
Grants	2.0	0.9	1.5	0.3	0.9	0.7	0.6	0.5	0.4	0.4
Expenditure and net lending	34.1	33.7	36.6	36.5	44.0	43.4	43.1	43.3	42.9	42.6
Current expenditure	25.3	26.5	26.9	31.7	36.5	36.0	35.8	36.0	36.3	35.8
Of which: Salaries and allowances	11.9	11.7	14.1	13.5	14.0	13.3	12.8	12.3	11.9	11.6
Transportation, communication, and utilities	2.8	2.7	1.6	2.9	2.9	2.9	2.9	2.9	3.1	3.2
Social welfare contributions	3.4	4.9	3.8	4.7	5.2	5.6	6.0	6.4	6.7	6.7
Repairs and maintenance	0.4	0.5	0.0	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Subsidies and transfers	2.8	1.8	3.5	4.3	7.1	6.3	5.9	5.4	5.0	4.8
Interest	2.0	2.8	2.7	2.5	2.9	3.5	3.8	4.6	5.3	5.2
Other	2.0	2.1	1.2	2.9	3.4	3.4	3.4	3.4	3.4	3.4
Capital expenditure	10.0	7.4	10.0	5.0	6.7	6.7	6.7	6.7	6.7	6.7
Net lending	-1.1	-0.2	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.1	0.1
Overall balance	-6.6	-7.6	-3.6	-7.8	-11.6	-8.1	-7.3	-7.9	-7.7	-7.6
Overall balance, excluding grants	-8.6	-8.6	-5.0	-8.1	-12.6	-8.8	-7.9	-8.4	-8.1	-8.0
Financing 2/	6.6	7.6	3.6	7.8	11.6	8.1	7.3	7.9	7.7	7.6
Privatization	1.0	0.0	…	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External	2.7	2.0	…	3.4	1.4	1.7	1.7	1.5	1.6	1.5
Domestic	2.8	5.6	…	4.4	10.2	6.5	5.5	6.4	6.1	6.2
MMA	1.1	2.3			1.2	0.6	0.6	0.6	0.6	0.6
Commericial banks	1.1	2.3			6.6	3.9	3.3	3.8	3.7	3.7
Other	0.6	1.1			2.3	1.9	1.7	1.9	1.8	1.8
Memorandum items:										
Current balance	0.3	-1.4	…	-3.4	-5.1	-1.4	-0.5	-1.1	-1.6	-1.3
Primary balance	-4.5	-4.8	…	-5.3	-8.7	-4.6	-3.5	-3.3	-2.4	-2.4
Public and publicly guaranteed debt 3/	59.9	62.8	…	66.7	75.0	78.6	80.7	82.5	83.7	84.5
Domestic	29.9	33.2	…	35.5	44.1	47.9	50.4	52.9	54.9	56.7
External (excluding IMF and currency swaps by MMA)	30.0	29.6	…	31.2	30.9	30.7	30.4	29.6	28.8	27.9
GDP (in millions of rufiyaa)	35,931	38,943	38,153	41,569	43,971	46,863	50,177	54,427	59,189	64,488

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

1/ The green tax will be effective late 2015, it replaces the bednights tax (eliminated November 2014).

2/ Includes unidentified financing.

3/ Arrears are not included.

Table 2c. Maldives: Statement of General Government Operations, 2011–19 (Staff's Baseline Scenario)

(In millions of rufiyaa)

	2011	2012	2013	2014	2015	2016	2017	2018	2019
							Proj.		
Revenue	9,370	10,090	11,632	14,114	16,401	17,856	19,105	20,671	22,344
Tax revenue	4,893	6,803	8,771	9,723	11,174	13,051	14,179	15,249	16,342
Taxes on income, profits, and capital gains	35	1,401	1,881	2,113	2,331	2,562	2,779	2,943	3,116
Payable by individuals	0	0	0	0	0	0	0	0	0
Payable by corporations and other enterprises	35	1,401	1,881	2,113	2,331	2,562	2,779	2,943	3,116
Taxes on goods and services	908	2,559	3,693	4,178	5,559	5,859	6,240	6,651	7,096
General GST	243	1,006	1,538	1,568	1,746	1,856	1,996	2,153	2,328
Tourism GST	665	1,554	2,155	2,610	3,813	4,003	4,244	4,498	4,768
Taxes on international trade and transactions	2,587	1,369	1,576	1,827	2,133	2,835	3,245	3,587	3,894
Taxes not elsewhere classified	1,363	1,474	1,622	1,605	1,152	1,795	1,915	2,067	2,235
Airport service charges	338	300	350	394	500	525	556	589	625
Tourism ($8 bed tax) 1/	751	805	862	770	183	768	814	885	965
Other	275	369	410	440	469	503	545	593	646
Grants	733	367	118	415	340	299	252	247	274
Other revenue	3,745	2,920	2,743	3,976	4,887	4,506	4,675	5,175	5,729
Administrative fees and charges	1,387	1,028	930	1,080	1,151	1,233	1,337	1,454	1,584
Interest income	72	72	51	46	49	52	56	61	67
Resort lease rent 2/	1,152	1,031	1,106	1,881	2,665	2,136	2,114	2,399	2,714
SOEs dividend payments	974	633	476	785	836	895	971	1,056	1,151
Other	160	155	180	185	185	189	196	204	213
Total expenditure	12,129	13,152	15,020	18,868	19,857	21,167	23,084	25,300	27,210
Expense	9,076	10,317	13,195	16,054	16,858	17,955	19,601	21,512	23,083
Compensation of employees	4,281	4,559	5,606	6,152	6,242	6,403	6,691	7,061	7,454
Goods and services	1,823	2,241	3,203	4,213	4,155	4,414	4,679	5,060	5,539
Interest	726	1,107	1,058	1,295	1,626	1,909	2,528	3,144	3,381
Subsidies	749	226	884	1,137	1,084	1,052	1,034	1,024	1,068
Social benefits	1,480	2,151	2,420	3,230	3,723	4,147	4,638	5,188	5,604
Miscellaneous other expense	17	32	25	26	28	30	32	35	38
Net acquisition of nonfinancial assets	3,054	2,836	1,825	2,814	2,999	3,211	3,483	3,788	4,127
Domestically financed	1,726	1,704	648	1,825	1,945	2,082	2,259	2,456	2,676
Capital expenditure (domestically financed)	2,260	1,752	916	1,951	2,079	2,226	2,415	2,626	2,861
Capital revenue	-534	-48	-268	-126	-134	-144	-156	-169	-185
Externally financed	1,328	1,132	1,177	989	1,054	1,129	1,224	1,332	1,451
Capital expenditure (foreign financed)	1,328	1,132	1,177	989	1,054	1,129	1,224	1,332	1,451
Gross operating balance	294	-227	-1,563	-1,940	-457	-99	-496	-841	-739
Net lending/borrowing (overall balance)	-2,759	-3,062	-3,388	-4,754	-3,456	-3,311	-3,979	-4,629	-4,866
Net financial transactions	-2,759	-3,062	-3,388	-4,754	-3,456	-3,311	-3,979	-4,629	-4,866
Net acquisition of financial assets	-616	90	136	143	153	164	177	75	-48
Domestic	-616	90	136	143	153	164	177	75	-48
Currency and deposits	-751	0	0	0	0	0	0	0	0
Loans	399	90	136	143	153	164	177	75	-48
Account payable	113	0	0	0	0	0	0	0	0
Equity and investment fund shares	-377	0	0	0	0	0	0	0	0
Foreign	0	0	0	0	0	0	0	0	0
Currency and deposits	0	0	0	0	0	0	0	0	0
Loans	0	0	0	0	0	0	0	0	0
Equity and investment fund shares	0	0	0	0	0	0	0	0	0
Net incurrence of liabilities	1,705	3,368	6,523	8,010	8,943	8,943	8,943	8,943	8,947
Domestic	220	3,498	7,009	7,372	8,168	8,168	8,168	8,168	8,169
Currency and deposits	0	0	0	0	0	0	0	0	1
Debt securities	220	3,498	7,009	7,372	8,168	8,168	8,168	8,168	8,168
Treasury bills	220	4,132	7,326	7,689	8,485	8,485	8,485	8,485	8,485
Commercial banks	0	0	0	0	0	0	0	0	0
Non banks	0	0	0	0	0	0	0	0	0
Other	0	0	0	0	0	0	0	0	0
Treasury bonds (ways and means account)	0	-634	-317	-317	-317	-317	-317	-317	-317
Loans	0	0	0	0	0	0	0	0	0
Equity and investment fund shares	0	0	0	0	0	0	0	0	0
Foreign	1,485	-130	-487	638	775	775	775	775	778
Debt securities	260	-770	-770	0	0	0	0	0	1
Loans	1,225	640	283	638	775	775	775	775	776
Statistical discrepancy	*438*	*-215*	*-2,999*	*-3,112*	*-5,334*	*-5,469*	*-4,787*	*-4,239*	*-4,129*
Memorandum items:									
Primary balance	-2,033	-1,955	-2,330	-3,460	-1,830	-1,401	-1,452	-1,485	-1,485
Overall balance excluding grants	-2,027	-2,696	-3,270	-4,340	-3,116	-3,011	-3,728	-4,383	-4,592
Net privatization proceeds	377	0	0	0	0	0	0	0	0
Public and publicly guaranteed debt	21,518	24,455	27,707	32,968	36,816	40,515	44,883	49,512	54,508
Domestic	10,754	12,919	14,746	19,370	22,443	25,264	28,797	32,483	36,535
External (excluding IMF and currency swaps by MMA)	10,764	11,536	12,961	13,598	14,373	15,250	16,086	17,029	17,973
GDP at market prices	35,931	38,943	41,569	43,971	46,863	50,177	54,427	59,189	64,488

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

1/ Bed-tax was removed w.e.f. December 2014. A green tax in its place will come into effect from November 2015.

2/ Includes lease extension fees for 2011, 2012, 2014, 2015 and 2016.

Table 3. Maldives: Monetary Accounts, 2007–19 (Staff's Baseline Scenario)

	2011	2012	2013	2014	2015	2016	2017	2018	2019
			Est.			Proj.			
				(In millions of rufiyaa, e.o.p.)					
Net foreign assets	2,873	5,141	8,813	13,739	17,180	19,806	22,576	25,439	28,119
Maldives Monetary Authority, net	4,725	4,241	5,308	8,956	12,435	15,104	17,920	20,834	23,571
Assets	5,170	4,690	5,685	9,450	12,806	15,474	18,290	21,205	23,942
Liabilities	-445	-448	-377	-494	-371	-371	-371	-371	-371
Commercial banks, net	-1,852	900	3,505	4,783	4,745	4,703	4,656	4,605	4,548
Net domestic assets	16,088	15,138	14,863	11,265	12,515	13,972	15,428	16,920	18,384
Domestic credit	24,505	23,908	24,850	26,204	27,517	29,397	31,468	33,677	35,890
Public sector	8,415	9,242	10,212	10,716	11,963	13,405	14,838	16,304	17,740
Central government (net)	6,735	7,664	8,638	8,700	9,939	11,324	12,673	14,042	15,378
Public enterprises	1,680	1,578	1,574	2,016	2,025	2,082	2,165	2,262	2,363
Private sector	16,090	14,505	14,638	15,488	15,554	15,992	16,630	17,373	18,149
Other items (net)	-8,417	-8,770	-10,096	-14,939	-15,002	-15,425	-16,040	-16,757	-17,506
Broad money	19,057	20,280	23,677	27,032	28,810	30,847	33,460	36,387	39,645
Narrow money	8,187	8,429	10,416	12,111	12,259	12,591	13,657	14,852	16,182
Currency	1,857	2,117	2,802	2,635	3,514	3,514	3,514	3,514	3,514
Public enterprise and local government d	60	1	2	1	0	0	0	0	0
Demand deposits	6,270	6,311	7,612	9,475	8,746	9,077	10,143	11,338	12,668
Quasi-money	10,870	11,851	13,261	14,921	16,550	18,256	19,803	21,535	23,463
				(Annual percentage change, unless otherwise indicated)					
Broad money	20.1	6.4	16.8	14.2	6.6	7.1	8.5	8.7	9.0
Narrow money	8.7	3.0	23.6	16.3	1.2	2.7	8.5	8.7	9.0
Domestic credit, net	11.3	-2.4	3.9	5.4	5.0	6.8	7.0	7.0	6.6
Central government	25.1	13.8	12.7	0.7	14.2	13.9	11.9	10.8	9.5
Public enterprises	14.7	-6.1	-0.2	28.1	0.4	2.8	4.0	4.5	4.5
Private sector	7.1	-9.8	0.9	5.8	0.4	2.8	4.0	4.5	4.5
				(In percent of GDP)					
Broad money	53.0	52.1	57.0	61.5	61.5	61.5	61.5	61.5	61.5
Narrow money	22.8	21.6	25.1	27.5	26.2	25.1	25.1	25.1	25.1
Domestic credit, net	68.2	61.4	59.8	59.6	58.7	58.6	57.8	56.9	55.7
Central government	18.7	19.7	20.8	19.8	21.2	22.6	23.3	23.7	23.8
Public enterprises	4.7	4.1	3.8	4.6	4.3	4.1	4.0	3.8	3.7
Private sector	44.8	37.2	35.2	35.2	33.2	31.9	30.6	29.4	28.1
				(In millions of U.S. dollars)					
Gross foreign assets of MMA	335	305	368	614	832	1,005	1,188	1,377	1,555
Usable reserves	150	99	93	120	347	443	543	647	745
Commercial banks NFA	-120	59	228	311	308	305	302	299	295
Commercial banks forex open position, net	142	155	221	280	n.a.	n.a.	n.a.	n.a.	n.a.
Memorandum items:									
Velocity	1.6	1.9	1.8	1.6	1.6	1.6	1.6	1.6	1.6
Money multiplier	2.5	2.4	2.5	2.5	2.3	2.4	2.5	2.5	2.5
Reserve money (in millions of rufiyaa, e.o.p.	7,551	8,368	9,629	10,727	12,259	12,591	13,657	14,852	16,182

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

Table 4. Maldives: Balance of Payments, 2011–18 (Staff's Baseline Scenario)

(In millions of U.S. dollars, unless otherwise indicated)

	2011	2012	2013	2014	2015	2016	2017	2018	2019
			Est.			Proj.			
Current account	-423	-270	-176	-241	-152	-202	-199	-198	-196
Balance of goods and nonfactor services	127	269	480	489	662	649	717	798	885
Trade balance	-1,370	-1,261	-1,372	-1,572	-1,585	-1,786	-1,970	-2,097	-2,265
Exports (f.o.b.)	346	314	331	369	313	308	342	396	445
Domestic exports	127	162	167	202	200	168	178	209	238
Re-exports	219	153	164	167	113	140	164	187	207
Imports (f.o.b.)	-1,717	-1,576	-1,703	-1,941	-1,899	-2,094	-2,312	-2,493	-2,711
Tourism-related	-251	-252	-302	-334	-362	-380	-413	-449	-488
Other	-1,466	-1,324	-1,401	-1,607	-1,536	-1,714	-1,899	-2,044	-2,222
Nonfactor services, net	1,498	1,530	1,852	2,060	2,247	2,435	2,687	2,896	3,150
Of which: Travel receipts	1,942	1,951	2,333	2,584	2,821	3,026	3,289	3,575	3,887
Income, net	-308	-280	-370	-419	-463	-485	-517	-560	-604
Current transfers, net	-242	-259	-286	-310	-351	-367	-399	-436	-477
Receipts	18	20	4	27	22	18	18	18	18
Payments	-260	-279	-290	-337	-373	-385	-418	-454	-495
Capital and financial account	478	215	142	398	372	376	382	388	374
Of which: 1/									
Foreign direct investment, net	424	228	361	380	418	450	471	483	484
Other investment, net	26	-83	-175	18	-46	-74	-88	-95	-110
Monetary authorities 2/	-4	0	-5	0	0	0	0	0	0
General government	79	42	18	41	50	57	54	61	61
Of which: Disbursements of loans	137	111	71	108	123	129	130	144	146
Amortization	-58	-69	-53	-66	-72	-72	-75	-83	-85
Banks	99	179	-153	-128	-156	-167	-182	-197	-215
Additional donor financing catalyzed by an SMP	0	0	0	0	0	0	0	0	1
Other sectors 3/	95	61	-36	105	60	37	39	41	44
Errors and omissions	-71	24	98	88	0	0	0	0	0
Overall balance	-15	-30	64	245	219	174	183	190	178
Gross international reserves (increase: -)	15	30	-64	-242	-218	-173	-183	-189	-178
Use of Fund credit, net	0	0	0	-3	-1	-1	-1	-1	0
Financing gap 4/	0	0	0	0	0	0	0	0	0
Memorandum items:									
Gross international reserves (stock; e.o.p.) 2/	335	305	368	614	832	1,005	1,188	1,377	1,555
In months of GNFS imports	1.7	1.7	1.9	2.8	3.7	4.1	4.5	4.8	5.0
In percent of short-term debt at remaining maturity	114	128	174	233	322	374	463	531	574
Usable reserves (stock; e.o.p.) 2/	137	99	93	132	347	443	543	647	745
In percent of short-term debt at remaining maturity	47	42	44	50	135	165	212	250	275
Current account (in percent of GDP)	-18.1	-10.6	-6.5	-8.4	-5.0	-6.2	-5.6	-5.1	-4.7
GNFS balance (in percent of GDP)	5.5	10.6	17.8	17.1	21.7	19.9	20.3	20.8	21.1
Exports (volume, percent change)	59.0	-8.2	6.3	12.6	-11.5	-0.9	11.0	15.6	12.2
Imports (volume, percent change)	21.2	-7.8	9.6	16.8	11.0	7.3	8.6	6.4	8.1
Tourism: bednights (percent change)	9.1	-1.2	9.2	6.5	5.5	5.0	6.0	6.0	6.0
Tourism: travel receipts (percent change)	13.4	0.4	19.6	10.8	9.2	7.3	8.7	8.7	8.7
External debt (in percent of GDP) 5/	42.6	34.3	32.2	34.5	33.9	33.7	32.9	32.0	31.1
Medium- and long-term	38.0	32.3	30.7	32.2	31.8	31.8	31.0	30.3	29.4
Short-term	4.6	2.0	1.4	2.3	2.1	1.9	1.9	1.7	1.6
Debt service (in percent of domestic GNFS exports)	9.7	9.3	7.6	6.8	7.3	6.8	6.5	5.6	5.2
Exchange rate (rufiyaa per U.S. dollar; average)	15.4	…	…	…	…	…	…	…	…
GDP (in millions of U.S. dollars)	2,332	2,534	2,699	2,855	3,043	3,258	3,534	3,843	4,188

Sources: Maldivian authorities; and IMF staff estimates and projections.
1/ There are no capital transfers or portfolio investments.
2/ MMA liabilities, include allocation of SDR 7.4 million, equivalent to US$11.7 million, made available in Q3 2009, see http://www.imf.org/external/np/tre/sdr/proposal/2009/0709.htm. These are treated as long term liabilities of the MMA.
3/ These flows are treated as non-debt creating, as they mainly reflect intra-company financing for tourism-related projects.
4/Assumes financing to keep GIR from falling below end-2012's months of import coverage.
5/ Public and private external debt includes IMF, but excludes domestic foreign-currency denominated debt.

Table 5. Maldives: Selected Economic and Vulnerability Indicators, 2011–19 (Staff's Recommended Adjustment Scenario) 1/

Population (in 1,000; 2012 est.)	331
GDP per capita (in U.S. dollars; 2012 est.):	6,675
Quota (in million SDRs):	10.0

	2011	2012	2013	2014	2015	2016	2017	2018	2019
			Est.			Proj.			
Output and prices				(Annual percentage change)					
Real GDP (gross value added at basic prices)	6.5	1.3	4.7	5.0	5.0	3.9	4.2	4.4	4.6
Inflation (end-of-period) 1/	16.7	5.4	3.1	1.2	0.4	2.8	4.0	4.5	4.5
Inflation (period average) 1/	11.3	10.9	4.0	2.5	0.3	2.1	3.5	4.3	4.3
GDP deflator	8.6	6.8	-0.9	0.7	1.5	3.0	4.1	4.2	4.1
Central government finances									
Revenue and grants	27.6	26.0	28.6	32.4	35.3	37.8	37.3	37.2	37.0
Expenditure and net lending	34.1	33.7	36.5	44.0	43.2	42.6	42.3	41.0	40.0
Overall balance	-6.6	-7.6	-7.8	-11.6	-7.9	-4.8	-5.0	-3.8	-3.1
Overall balance excl. grants	-8.6	-8.6	-8.1	-12.6	-8.7	-5.4	-5.4	-4.3	-3.5
Primary balance	-4.5	-4.8	-5.3	-8.7	-4.5	-1.0	-0.5	1.1	1.6
Public and publicly guaranteed debt	59.9	62.8	66.7	75.0	78.4	78.1	77.1	74.9	71.9
Monetary accounts				(Annual percentage change, unless otherwise indicated)					
Broad money	20.1	6.4	16.8	14.2	6.6	7.1	8.5	8.7	9.0
Domestic credit	11.3	-2.4	3.9	5.4	5.0	6.8	8.5	8.7	9.0
Balance of payments				(In percent of GDP, unless otherwise indicated)					
Current account	-18.1	-10.6	-6.5	-8.4	-5.0	-5.5	-4.9	-4.4	-3.9
Of which:									
Exports	14.9	12.4	12.3	12.9	10.3	9.5	9.7	10.3	10.6
Imports	-73.6	-62.2	-63.1	-68.0	-62.4	-63.5	-64.7	-64.1	-64.0
Tourism receipts and nonfactor services, net	64.2	60.4	68.6	72.2	73.9	74.8	76.1	75.4	75.3
Income (net)	-13.2	-11.0	-13.7	-14.7	-15.2	-14.9	-14.6	-14.6	-14.4
Current transfers	-10.4	-10.2	-10.6	-10.9	-11.5	-11.3	-11.3	-11.4	-11.4
Capital and financial account (including e&o)	17.5	9.4	8.9	17.0	12.2	11.5	10.8	10.1	8.9
Of which:									
General government, net	3.4	1.6	0.7	1.5	1.7	1.7	1.5	1.6	1.5
Banks and other sectors, net	-2.1	-5.0	-7.0	-0.8	-3.2	-4.0	-4.0	-4.1	-4.1
Overall balance	-0.7	-1.2	2.4	8.6	7.2	6.1	6.0	5.7	5.0
Gross international reserves (in millions of US$; e.o.p.) 2/	335	305	368	614	832	1,030	1,240	1,458	1,668
In months of GNFS imports	1.7	1.7	1.9	2.8	3.7	4.3	4.8	5.1	5.4
Memorandum items:									
GDP (in millions of U.S. dollars)	2,332	2,534	2,699	2,854	3,042	3,257	3,533	3,842	4,186
Tourism bednights (000')	6,529	6,451	7,045	7,503	7,916	8,311	8,311	8,810	9,899
Tourism bednights (% change)	9.1	-1.2	9.2	6.5	5.5	5.0	6.0	6.0	6.0
Dollarization ratio (FC deposits in percent of broad money) 3/	49.5	49.2	50.2	54.5					

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

1/ CPI-Male definition.

2/ MMA liabilities, include allocation of SDR 7.4 million, equivalent to US$11.7 million, made available in Q3 2009, see http://www.imf.org/external/np/tre/sdr/proposal/2009/0709.htm. These are treated as long term liabilities of the MMA.

3/ For the first 11 months of the year 2014.

Table 6. Maldives: Selected Financial Soundness Indicators
(In percent, unless otherwise specified)

	2007	2008	2009	2010	2011	2012	2013	2014Q1	2014Q2	2014Q3
Capital										
Regulatory capital to risk-weighted assets	15.4	21.0	24.7	28.9	30.3	35.8	34.0	39.4	31.7	31.2
Tier 1 capital to risk-weighted assets	24.8	15.4	20.82	24.8	26.3	30.1	30.0	36.5	26.8	26.3
Capital to total assets	12.8	15.9	16.4	17.7	18.8	20.2	19.3	20.1	21.6	22.8
Asset quality										
Nonperforming loans (gross) to total loans (gross)	1.7	8.9	12.7	17	19.4	21	16.7	15.9	15.6	12.2
Nonperforming loans (net of provisioning) to regulatory capital	-1.7	31.8	33	34.9	35.2	16.5	2.4	4.1	0.5	-3.3
Loan loss provisions to nonperforming loans	118.4	24.2	34.4	39.8	41.5	77.1	95.0	88.0	98.4	112.8
Earnings and profitability										
Return on assets	5.3	3.4	2.2	2.0	2.6	2.4	5.1	4.0	3.8	4.6
Return on equity	41.2	23.4	13.8	11.5	14.4	13.2	23.8	18.9	17.0	20.2
Liquidity										
Ratio of net loans to total deposits	130.6	141.9	112.6	97.6	86.3	70.7	62.6	62.9	63.7	71.2
Liquid assets to total assets	11.4	9.6	20.7	25.9	27.9	28.3	34.1	41.8	42.9	40
Assets of Banks (rufiyaa billions)	18.3	22.7	25.1	25.9	28.7	27.6	32.7	38.9	37.1	37.6
Deposits of banks (rufiyaa billions)	10.2	12.2	14.3	15.5	18.3	19.2	22.6	27.7	26.4	25.6

Source: Maldives Monetary Authority

Table 7. Maldives: Millennium Development Goals

Goals	1990	1995	2000	2005	2012
Goal 1: Eradicate extreme poverty and hunger					
Employment to population ratio, 15+, total (%) (modeled ILO estimate)	45	46	49	54	59
Employment to population ratio, ages 15-24, total (%) (modeled ILO estimate)	32	29	30	39	40
GDP per person employed (constant 1990 PPP $)	..	..	..	..	..
Income share held by lowest 20%	..	..	1	7	..
Malnutrition prevalence, weight for age (% of children under 5)	..	39	26	..	..
Poverty gap at $1.25 a day (PPP) (%)	..	..	13	0	..
Poverty headcount ratio at $1.25 a day (PPP) (% of population)	..	..	26	1	..
Vulnerable employment, total (% of total employment)	46	54	50	30	..
Goal 2: Achieve universal primary education					
Literacy rate, youth female (% of females ages 15-24)	98	98	98	99	..
Literacy rate, youth male (% of males ages 15-24)	98	98	98	99	..
Persistence to last grade of primary, total (% of cohort)	..	..	..	..	83
Primary completion rate, total (% of relevant age group)	..	122	184	144	..
Adjusted net enrollment rate, primary (% of primary school age children)	..	96	99	98	..
Goal 3: Promote gender equality and empower women					
Proportion of seats held by women in national parliaments (%)	6	6	6	12	7
Ratio of female to male primary enrollment (%)	100	97	100	98	..
Ratio of female to male secondary enrollment (%)	..	106	108	113	..
Ratio of female to male tertiary enrollment (%)	..	..	..	159	..
Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	15.8	32.4	40.6	30	40.5
Goal 4: Reduce child mortality					
Immunization, measles (% of children ages 12-23 months)	96	96	99	97	98
Mortality rate, infant (per 1,000 live births)	68	53	35	19	9
Mortality rate, under-5 (per 1,000 live births)	94	70	44	23	11
Goal 5: Improve maternal health					
Adolescent fertility rate (births per 1,000 women ages 15-19)	136	79	38	17	4
Births attended by skilled health staff (% of total)	..	90	70	84	..
Contraceptive prevalence (% of women ages 15-49)	29	..	42	39	..
Maternal mortality ratio (modeled estimate, per 100,000 live births)	430	210	110	57	31
Pregnant women receiving prenatal care (%)	..	..	81	95	..
Unmet need for contraception (% of married women ages 15-49)	..	..	..	..	..
Goal 6: Combat HIV/AIDS, malaria, and other diseases					
Children with fever receiving antimalarial drugs (% of children under age 5 with fever)	..	..	..	..	..
Condom use, population ages 15-24, female (% of females ages 15-24)	..	..	..	..	..
Condom use, population ages 15-24, male (% of males ages 15-24)	..	..	..	..	..
Incidence of tuberculosis (per 100,000 people)	150	118	60	51	41
Prevalence of HIV, female (% ages 15-24)	0.1	0.1	0.1	0.1	0.1
Prevalence of HIV, male (% ages 15-24)	0.1	0.1	0.1	0.1	0.1
Prevalence of HIV, total (% of population ages 15-49)	0.1	0.1	0.1	0.1	0.1
Tuberculosis case detection rate (%, all forms)	47	80	80	80	80
Goal 7: Ensure environmental sustainability					
CO2 emissions (kg per PPP $ of GDP)	..	..	0	0	0
CO2 emissions (metric tons per capita)	1	1	2	2	3
Forest area (% of land area)	3	3	3	3	3
Improved sanitation facilities (% of population with access)	68	70	79	89	99
Improved water source (% of population with access)	93	94	95	97	99
Marine protected areas (% of territorial waters)	..	..	..	..	..
Goal 8: Develop a global partnership for development					
Net ODA received per capita (current US$)	97	236	70	255	171
Debt service (PPG and IMF only, % of exports of goods, services and primary income)	4	3	4	7	3
Internet users (per 100 people)	0	0	2.2	6.9	38.9
Mobile cellular subscriptions (per 100 people)	0	0	3	68	166
Telephone lines (per 100 people)	3	6	9	11	7
Other					
Fertility rate, total (births per woman)	6.1	4.6	3.3	2.5	2.3
GNI per capita, Atlas method (current US$)	..	..	..	3,420	5,430
GNI, Atlas method (current US$) (billions)	..	..	..	1	1.8
Gross capital formation (% of GDP)	..	31.3	26.3	40.4	..
Life expectancy at birth, total (years)	61	65	69	74	78
Literacy rate, adult total (% of people ages 15 and above)	96	96	96	98	..
Population, total (billions)	0	0	0	0	0
Trade (% of GDP)	168.1	169.9	161.1	136.3	223.6

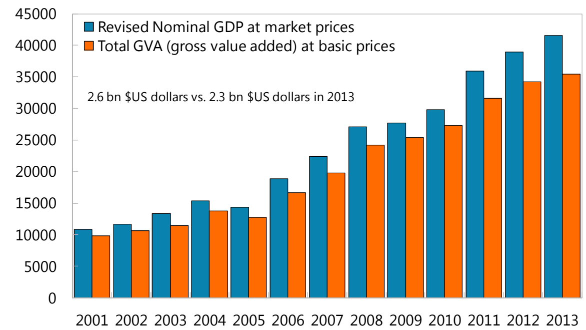
Source: World Development Indicators

Note: Figures in blue refer to periods other than those specified.

Annex I. Revisions to Nominal GDP

The authorities have also made significant changes to their GDP figures. They have adopted the methodology of using a market price GDP as their aggregate—instead of the previous approach of presenting gross value added figures at basic prices (which exclude taxes and subsidies on products from the estimation of gross output). The adjustment from basic to market prices is consistent with the purchasers' price valuation of the components of the expenditure measure of GDP. This change is in line with international practice and enables more consistent cross-country comparisons. It was important to make the change, given the introduction of TGST, a Goods and Services Tax and changes to import duties in recent years. The revised calculation of nominal GDP, is consistent with the expenditure measure of GDP, and is being used by staff to replace previously published nominal GDP figures. The effect is to revise up the level of nominal GDP by 13 percent in 2013 (see chart).

Maldives: Nominal GDP at market and basic prices
(mn Rf, 2001-13)



The revisions also affect sectoral contributions to GDP and economic aggregates commonly calculated as ratios to nominal GDP. Ratios for the fiscal deficit, public debt and the current account all are all a little lower than previously reported. Looking forward, the authorities and staff agree on the importance of the credibility in final revisions of the GDP data and are collaborating closely. Technical assistance is being provided by the Fund to support some necessary further revisions to real GDP data and to more broadly support improvements in GDP methodology.

Annex II. Maldives: Risk Assessment Matrix

Nature/ Source of Risk	Likelihood/ Direction	Expected Impact on the Economy and Policy Response
Potential External Shocks		
Protracted period of slower growth in advanced and emerging economies • **Advanced economies**: lower than anticipated potential growth and persistently lower inflation due to failure to fully address legacies of financial crisis, leading to secular stagnation and a further decline in commodity prices. • **Emerging markets**: maturing of the cycle, misallocation of investment and incomplete structural reforms leading to prolonged slower growth.	**High**	**High** The pickup in tourist activity would prove short-lived negatively affecting activity, denting fiscal revenue and widening the deficit. If combined with fiscal slippage, this could also place pressure on the parallel market premium and erode the level of MMA official reserves. Policy actions: Fiscal adjustment would need to be accelerated. To restore stability tough expenditure control would need to be in place.
An abrupt surge in global financial market volatility, as investors reassess underlying risk.	**High**	**High** Would likely dent global tourist activity with adverse consequences for Maldives fiscal and external accounts—similar to those traced out in the scenarios above.
Growth slowdown and financial risks in China over the medium term • Continued buildup and eventual unwinding of excess capacity, eventually resulting in a sharp growth slowdown and large financial and fiscal losses.	**Medium**	**Medium** Tourist activity has benefited from increased arrivals from new markets such as China and other Asian economies that are part of China's supply chain. A sharper than expected slowdown in China would dent tourism from these destinations. Indirectly any impact on the euro area would also dent tourism arrivals from core markets. The effects are milder than for protracted lower growth in advanced and emerging economies. Policy recommendations as above.
Persistent strengthening of the US dollar, reflecting asymmetric exit and relative fundamentals.	**Medium**	**Medium** Maldives exchange rate behaves like a defacto dollar peg, a sustained appreciation in the dollar could reduce competitiveness .
Further fall in commodity prices (particularly oil).	**Medium**	**Medium** If sustained, lower oil prices would improve Maldives net export position through lower import costs. If lower costs are passed on in airfares, tourism demand could increase and as a remote destination with high travel costs Maldives could gain. But, these effects would be partly offset if weaker global demand is driving lower prices.
Potential Domestic Shocks: mild external shocks could trigger these domestic vulnerabilities		
Implementation of proposal on SEZs could undermine the tax base and GMR arbitration adds to contingent costs.	**High**	**High** Market appetite for government debt could weaken if the fiscal position deteriorates. Policy response: accelerate fiscal adjustment.
Financial stability risks in a domestic bank come to the fore.	**Medium**	**Medium** Though financial soundness indicators have improved in recent years, it might reflect unsound accounting practices. In the event of strains in a bank a range of resolution options would need to be considered and should include independent external assessment.

Annex III. Follow Up on Past Fund Advice

2013 Article IV Policy Recommendations	Policy Actions
Fiscal Policy Substantial fiscal consolidation plan is needed to bring the deficit down and alleviate pressures on the monetary and external fronts. Measures to adopt are: to raise tourism GST (TGST) to 15 percent by mid-2013 while not allowing the bed tax to expire by end 2013; freeze salaries and wages; selectively reverse duty reductions; further rationalize universal health insurance scheme (Aasandha) and better target electricity subsidies.	The TGST was increased from 6 to 8 percent in January 2013 and to 12 percent with effect from November 2014. The bed-night tax was eliminated in December 2014 (but the 2015 Budget will replace it with the Green tax from late 2015). Import duties were raised, but policy measures were insufficient to offset the increase in spending. Targeting of subsidies and a public employment freeze are included in the 2015 Budget. However, the Aasandha has been broadened, limits removed, and it functions more like an administered rather than an insurance scheme.
Monetary Policy To eliminate the long-standing fiscal dominance, further monetization of the fiscal deficit (daily monetization limits need to be introduced and the MMA should charge interest greater than the T-bill yield on advances to the government) and pressures by the government to limit OMOs should be avoided.	Fiscal policy continues to dominate monetary policy. In May 2014 the MMA took steps to monetize the outstanding government overdraft by converting it into a non negotiable long term bond. The measures to adopt daily monetization limits and charge higher than T-bill interest rate on government advances were not implemented. The MMA has eliminated liquidity absorbing OMOs. With the advent of the Fiscal Responsibility Law from May 2014, strict limits have been imposed on monetary accommodation. However, there has been no recourse to monetary financing since that time.
Financial Policies A more forward-looking and risk-based supervisory regime was needed. In addition, removing forbearance granted on provision requirements, the AML/CFT bill should be adopted. The introduction of the deposit insurance (DI) scheme should be considered later in the reform time-plan, when macroeconomic conditions are met. Independent assessment of one bank's compliance with prudential requirements and recapitalization strategy should be conducted.	The MMA is improving the collection of information for prudential supervision. The authorities received MCM TA on effective stress testing framework in May 2014. The AML/CFT bill was adopted by parliament. The authorities have prioritized deposit insurance in their agenda. The overall conditions of banks and their compliance with prudential requirements have improved though there has yet to be an independent professionally-qualified external opinion regarding the validity of the accounting treatment and valuations of banks asset sales.
External Policy To support fiscal and monetary policy a 20 percent devaluation of the exchange rate was recommended to be accompanied by wage and subsidy restraint.	The exchange rate parity and band was maintained.

INTERNATIONAL MONETARY FUND

MALDIVES

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

January 27, 2015

Prepared By

Asia and Pacific Department
(In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of November 30, 2014)

Membership Status: Joined: January 13, 1978; Article XIV

General Resources Account:	**SDR Million**	**Percent Quota**
Quota	10.00	100.00
Fund holdings of currency (exchange rate)	9.53	95.34
Reserve Tranche Position	2.00	20.04

SDR Department:	**SDR Million**	**Percent Allocation**
Net cumulative allocation	7.69	100.00
Holdings	6.78	88.12

Outstanding Purchases and Loans:	**SDR Million**	**Percent Quota**
Stand-By Arrangements	1.54	15.38
ESF Arrangements	2.05	20.50

Latest Financial Arrangements:

Type	**Arrangement Date**	**Expiration Date**	**Amount Approved (SDR million)**	**Amount Drawn (SDR Million)**
Stand-By	12/04/2009	12/3/2012	49.20	8.20
ESF	12/04/2009	12/3/2011	8.20	2.05

Projected Payments to Fund[1]
(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming			
	2014	**2015**	**2016**	**2017**
Principal	1.03	0.82	0.41	0.41
Charges/Interest		0.01	0.00	0.00
Total	**1.03**	**0.83**	**0.41**	**0.41**

[1]When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

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. Since April 2011, the rufiyaa has floated in a band of 20 percent on either side of Rf 12.85 per dollar. In practice, however, the rufiyaa has been virtually fixed at the band's weaker end of Rf 15.42 per dollar. The de jure exchange rate arrangement is a pegged exchange rate within horizontal bands and the de facto exchange rate arrangement is classified as a stabilized exchange rate arrangement. Maldives continues to avail itself of the transitional provisions of Article XIV, and has not yet accepted the obligations of Article VIII, Sections 2, 3, and 4. It maintains an exchange restriction subject to IMF approval under Article VIII, Section 2(a) of the IMF's Articles of Agreement arising from a shortage of foreign exchange at the official rate which leads to the MMA rationing its supply of foreign exchange to commercial banks. This results in a channeling of foreign exchange transactions for current international transactions to the parallel market where transactions take place at an exchange rate that deviates by more than 2 percent from the official exchange rate. The greater-than-2-percent exchange-rate spread gives rise to a multiple currency practice subject to IMF approval under Article VIII, Section 3 and also to exchange restrictions, given the additional cost involved for obtaining foreign exchange. The extent of rationing has been eased with an increase in amounts provided to commercial banks.

Last Article IV Consultation

The 2013 Article IV consultation was concluded by the Executive Board on February 4, 2013.

Technical Assistance

FAD: FAD main areas of engagement were in Public Expenditure and Financial Accountability (PEFA) assessment and providing TA for cash management. A joint IMF/WB Public Expenditure and Financial Accountability (PEFA) assessment was carried out in February 2014 to gauge progress made since the last PFM Action Plan for 2009-2011, identify remaining weaknesses and future direction. As a follow-up to the PEFA, the FAD team together with the World Bank also developed a Public Financial Management Reform Plan (PFMRP) for the GoM in June 2014. This was a broad PFM reform and consolidation plan aimed at improving the overall policy-making, coordination, implementation and monitoring framework in PFM. Altogether 3 missions on cash management TA were carried out in FY14. This mainly focused on developing a cash management manual for the GoM and related activities. On request from the authorities, the FAD in September 2014 also carried out a review of Chart of Accounts (CoA) at the ministry of finance and proposed structure for a revised CoA and an action plan to achieve same. In addition, there was a coordinated FAD/STA mission around the same time to review the mapping of the government COA to GFSM 2014.

LEG: In October 2003 provided technical assistance on the revision of the Maldives Monetary Authority Act (MMA Act). A series of missions (March and September 2005, and April 2006) were provided to revamp the banking law. In August 2009, a mission provided assistance on the MMA Act (jointly with MCM). A follow-up mission in February 2011 focused on payments law. LEG conducted an AML/CFT assessment in October 2010 and conducted a desk-based review of the draft AML/CFT law in May 2012. In 2014 LEG provided advice on the Special Economic Zones Law, offshore banking legislation and deposit insurance.

MCM: Two missions visited in 2006 on monetary operations, financial market development, and banking issues. In 2007, a series of mission were provided on debt management, monetary policy and financial supervision. In 2008, three missions visited on monetary operations and liquidity management, monetary policy and financial supervision issues. In November 2008 and March/May/August 2009, a series of mission were provided on research capacity building, bank supervision, monetary policy and the MMA act. Two missions visited Malé to advise on monetary operations, liquidity management, and the development of a crisis management framework. In December 2010, MCM conducted a TA mission on crisis preparedness and management, bank restructuring, and monetary operations. In May and September 2011, MCM consecutively conducted missions on the development of debt markets, and on on-site banking supervision. In February 2012, MCM undertook a TA mission on assessing the foreign exchange operations framework. In 2014, MCM conducted a series of TA missions on banking supervision in early February and late May. Also, together with APD another joint mission on developing foreign exchange market was carried out. MCM also provided advice on deposit insurance schemes.

***STA*:** In May 2007, STA conducted a mission on money and banking statistics. In February and April 2011, STA offered TA on multiple topics covering improvements in balance of payments statistics, government financial statistics (GFS), monetary and financial statistics (MFS) and national accounts. In June and September 2011, STA conducted TA missions on improving price statistics and on the General Data Dissemination System (GDDS). In February, May, and October 2012 STA continued providing TA on improving price statistics. Similarly, in April 2012, a TA mission on improving national accounts covered constructing GDP from the expenditure side and compiling quarterly national accounts. Further advice on improving GDP and developing quarterly GDP was provided in November 2012, January and July, 2014. Between March 2013 and November 2014, STA field five TA missions on balance of payments statistics, in the context of a project funded by the Government of Japan. Another TA mission on balance of payments statistics is scheduled for March 2015.

Safeguards Assessment

In line with the Fund's safeguards assessments policy, an assessment of the Maldives Monetary Authority was concluded in March 2010. In addressing recommendations, the MMA appointed an external auditor and strengthened controls over foreign payments through the automation of the authorization process. A Chief Internal Auditor has also been appointed, while capacity in the internal audit function continues to be improved. In addition, to strengthen the legal framework, amendments to the MMA Act were drafted in 2011 in consultation with the Fund, and have yet to be enacted.

IMF–WORLD BANK JOINT MANAGEMENT ACTION PLAN[1]

(As of December 2014)

In view of the macroeconomic challenges facing Maldives and in the wake of a period of political volatility, the World Bank Group Interim Strategy Note (ISN) for FY14-FY16, presented to its Board in June 2014, proposes a selective program of engagement focused on deepening dialogue and support on macro-fiscal issues while strengthening the analytical foundations that would underpin a future program. To this end, a Systematic Country Diagnostic (SCD) is under preparation to shed light on the country's challenges and opportunities for achieving more inclusive growth, reduced poverty and enhanced prosperity of the Maldivian people. The SCD will inform policy dialogue and provide the analytical basis for scoping out the next Country Partnership Framework (CPF). While the ISN is planned to span over a 24-month period, the preparation of the next CPF could be brought forward if opportunities emerge to support a full-fledged medium-term government program for macroeconomic stability and sustainable growth. Under the current ISN, support is being provided in the areas of: fiscal management, public financial management and debt management; sustainable growth; social inclusion and service delivery; and environment and natural resource management.

The teams have been holding, and will continue to hold, joint missions and regular briefing meetings on macroeconomic developments. Public financial management is a key area of collaboration for these operations as is universal subsidies and social protection reform, where the Bank is taking the lead on a number of initiatives aimed at improving targeting. The World Bank has carried out a technical assistance project on fiscal policy in FY 14, and has launched a Public Financial Management Systems strengthening project for FY 15-20, with the objective to enhance budget credibility, transparency, and financial reporting of central government finances. It will focus on strengthening the PFM environment (including enhancing the medium-term fiscal framework and strengthening debt and cash management) and strengthening budget execution. This work is carried out in close collaboration with the IMF providing considerable TA assistance in the areas of PFM and PEFA. The Bank, Fund and Government have jointly undertaken a Public Expenditure and Financial Accountability (PEFA) assessment in mid-2014, followed by a PFM action plan. The Bank is also providing technical assistance to forecasting tourism flows. The Appendix details the macro-critical activities that the Bank and IMF will work on over the coming year.

Appendix I. Maldives IMF-World Bank Joint Management Action Plan		
Title	**Products/Activity**	**Expected Date of Delivery**
Bank Work Program in the next 12 months	**I. Mutual Information on Relevant Work Program A. Lending (IDA, Trust Fund)** A. Strategy and Analytical Work Systematic Country Diagnostic Sustainable Fisheries Support Gender Study Youth Engagement Poverty and Shared Prosperity in Maldives B. Lending Program Environmental Management Project Pension and Social Protection Administration Climate Change Trust Fund I (three projects) Statistical Capacity Building Enhancing Education Development Project Public Financial Management Systems Strengthening Project Accelerating Sustainable Private Investments in Renewable Energy (ASPIRE) Project Climate Change Trust Fund II C. Technical Assistance Forecasting Tourism Flows TA	 FY2015 FY2015 FY2015 FY2015 FY2016 **Approval Date** June 2008 May 2009 December 2009 November 2012 April 2013 June 2014 June 2014 FY2015 FY2015
IMF Work Program in the next 12 months	**A. Missions** Staff visit and Article IV consultation **B. Analytical Work** drivers of inflation, fiscal sustainability and tourism competitiveness. **C. Technical Assistance Fiscal issues** Public finance management, developing a fiscal Chart of Accounts and support for cash management. **Financial sector issues** training for supervisors and deposit insurance. **Statistics** continuing assistance on balance of payments statistics and national accounts.	April 2015, December 2015.
IMF Request to Bank	**II. Request for Work Program Inputs (as needed)** Poverty and social impact analysis of the electricity tariff increases Request for assistance in targeting subsidies	FY2010 Ongoing
Joint Products	**III. Agreement on Joint Products** Debt sustainability analysis[1]	Jan. 2015

[1] Prepared jointly by IMF and World Bank staff

RELATIONS WITH THE ASIAN DEVELOPMENT BANK

(As of November 30, 2014)

Asian Development Bank

ADB's interim country partnership strategy (CPS) for 2014–2015 was endorsed by its Board of Directors in October 2014. The interim CPS continues the partnership strategy and focus on ADB's prioritized areas and sectors of operations that were inherent in the interim CPS for 2012-2013; these include: energy, transport, and finance (in particular, micro, small, and medium-sized enterprises). In support of investments in these areas, ADB is providing capacity building support to strengthen institutional capacity in various sectors such as tax administration, operations management, and MSME development; and in agencies such as Maldives Energy Authority and the Ministry of Finance and Treasury.

Work on the full CPS will commence in early 2015.

Loans and Grants

Since ADB started lending to the Maldives in 1981 and up to 2014-end, it has provided 24 loan and grant projects to the country with a total approved amount of $209.91 million. As of November-end, 2 loans and grants (in the MSME and energy sectors) were active with a net amount of $45.350 million (Table 1). In October 2014, the ADB Board of Directors approved the Outer Island Sustainable Energy Development Project; of its total cost, $38.08 million came from Asian Development Fund (ADF).

Table 1. Ongoing Loan and Grant Portfolio

(As of November-end 2014, in $ million)

Project Name	Amount	Closing Date
Inclusive Micro, Small and Medium-Sized Enterprise Development (Grant)	4.450	31 Dec 2016
Inclusive Micro, Small and Medium-Sized Enterprise Development (Loan)	2.820	31 Dec 2016
Outer Island Sustainable Energy Development	38.080	20 June 2020
TOTAL	**45.350**	

Technical Assistance

As of November-end 2014, ADB had approved 68 TA projects to the Maldives, with a total amount of $26.90 million. Of the ongoing 4 TA projects (Table 2), 2 are in the energy sector ($1.9 million altogether), and 2 in public sector management ($1.175 million altogether) for a total of $3.075 million.

Table 2. Ongoing TA Portfolio

(As of November-end 2014, in $ million)

Capacity Development for the Maldives Energy Authority	Energy	0.800	30 Sept 2017
Outer Islands Sustainable Energy Development	Energy	1.100	31 Dec 2014
Strengthening Capacity for Operations Management	PSM	0.325	31 Dec 2015
Enhancing Tax Administration Capacity	PSM	0.850	31 Dec 2015
TOTAL		**3.075**	

PSM= public sector management

Contract Awards/Commitments

As a result of the closure of the Economic Recovery Program (ERP) loan as well as two other projects, the level of contract awards for all of 2013 was reduced significantly as compared to 2012 (Table 3).

Table 3. Contract Awards/Commitment Performance

(Without program loans as of September 30, 2014)[a]

A	Contract Awards/Commitment				
	1	Projected ($ million)[b]	7.1	6.5	-
	2	Achieved ($ million)	3.8	6.0	0.3
	3	Achieved (Percent)	53.5	92.3	-
B	Contract Awards/Commitment Ratio (%)		40.9	26.6	5.9

[a] No contract awarded for 2014

[b] Refers to full year projection.

Disbursements

Total disbursements in 2012 were high due to the ERP; since its closure, and that of two other projects, the level of disbursements has declined. The disbursement ratio in 2013 was 7.8 percent both with and without program loans (Table 4).

Table 4. Disbursement Performance
(As of September 30, 2014)

A.	Disbursements					
	1	***Projected ($ million)***				
		- With Program Loans	10.1	18.2	0.1	0.8
		- Without Program Loans	10.1	1.8	0.1	0.8
	2	***Achieved ($ million)***				
		- With Program Loans	7.0	20.0	0.6	0.8
		- Without Program Loans	7.0	3.5	0.6	0.8
	3	***Achieved (Percent)***				
		- With Program Loans	69.3	109.9	600.0	99.1
		- Without Program Loans	69.3	194.4	600.0	99.1
B.	Disbursement Ratio (%)					
		- With Program Loans	14.1	3.7	7.8	n/a
		- Without Program Loans	42.5	12.2	7.8	n/a

Partnerships and Cofinancing

In addition to the ADF funds for the Outer Island Sustainable Energy Development Project, approved in October 2014, it had cofinancing resources of $72 million, comprising $50 million from the European Investment Bank, $12 million from the Scaling Up Renewable Energy Program in Low Income Countries (SREP), and $10 million from the Islamic Development Bank.

By the end of 2013, cumulative direct value-added official cofinancing for Maldives amounted to $14.2 million for four investment projects and $2.3 million for four technical assistance projects.

Private Sector Operations

In 2008, ADB approved a direct loan of $7.5 million and an equity investment of $4.5 million in the Housing Development Finance Corporation, which provided funding for critically needed housing in the country. As of year-end 2013, cumulative approvals in 2 projects amounted to $16.5 million (including $4.5 million equity investment in loan 7274/2418). Total outstanding balances and undisbursed commitments to nonsovereign projects in the Maldives amount to $5.7 million, representing 0.1% of ADB's total nonsovereign portfolio as of 31 December 2013.

Regional Cooperation

ADB is supporting the Maldives through the study on Regional Economics of Climate Change (RECCSA), which identifies adaptation measures to climate change impact and recommends cleaner technologies and options for the country and for the region. ADB-supported studies also focus on strengthening and promoting regional cooperation on climate change by analyzing regional climate change risks and addressing the issues associated with climate change at the cross-sectoral and cross-country levels, which are of importance to the Maldives.

ADB also provided assistance in the preparation of the study on Indian Ocean Cargo and Passenger Ferry to analyze the feasibility of launching subregional passenger and cargo services, connecting the Maldives to India (Tuticorin and Cochin) and Sri Lanka (Colombo). This will help the Maldives to increase accessibility and mobility; facilitate trade and regular cargo movement; and improve logistics, which can consequently open new opportunities for tourism development.

The Maldives also receives capacity building support for customs modernization under the South Asia Subregional Economic Cooperation (SASEC) program. In May 2014, the Maldives (together with Sri Lanka), became full members of SASEC (original members were Bangladesh, Bhutan, India, and Nepal). SASEC focuses on planning, preparing, and implementing regional projects in energy, trade facilitation, and transport.

STATISTICAL ISSUES

(As of January 22, 2015)

I. Assessment of Data Adequacy for Surveillance

General: Macroeconomic statistics have improved in recent years, with technical assistance from STA and the Asian Development Bank (AsDB). While data are broadly adequate for surveillance (Category B) there are nonetheless significant data gaps that complicate policy making and aspects of surveillance. Remaining shortcomings affect the balance of payments, government finance, and national accounts statistics. The main official statistical publication is the *Statistical Yearbook of Maldives*. APD receives a monthly electronic statistical report, covering a broad range of economic and financial statistics. It also receives the *Quarterly Economic Bulletin* (*QEB*) and the *Annual Report* (*AR*), albeit with a lag, of the Maldives Monetary Authority (MMA).

Real sector: National accounts statistics are available only on an annual basis and with a considerable lag, though the authorities are working on quarterly GDP. While GDP estimates are made using both the production and expenditure approaches, these estimates are inconsistent. Furthermore, the base year for constant price estimates is 2003, so that recent changes in the structure of the economy are not reflected by the base period weights. The AsDB has assisted the authorities in setting up a framework for compiling more comprehensive national accounts and STA has provided substantial assistance for improving the annual production and expenditure GDP measures, and for developing quarterly GDP series.

The CPI was rebased to June 2012=100, with assistance from STA. Weights are based on the 2012 household income and expenditure survey.

Fiscal sector: General government data are reported for publication in the *GFS Yearbook* and the latest published data are for 2011. Monthly data on revenue and expenditure are available, but the reporting system is new, and its reliability is as yet untested. In particular, the consistency of these data with below-the-line financing numbers provided by the monetary authorities is weak. Data on external debt are subject to reconciliation with creditors. Data on the operations of state enterprises are limited.

Monetary sector: APD receives a weekly electronic report on monetary statistics, covering the balance sheets of the MMA and the commercial banks. Current summary data are published in the MMA's *Monthly Statistics* publication as well as in its *QEB* and *AR*. There are inconsistencies between monetary and fiscal data regarding the financing of the fiscal deficit due to issues of timing and coverage. An April 2007 STA monetary and financial statistics mission completed the standardized report forms for the central bank and other depository corporations, and developed an integrated monetary database that meets the needs of the MMA, STA, and APD. It became operational in 2010.

<table>
<tr><td colspan="2">External sector: The MMA compiles balance of payments data on an annual basis. Coverage has improved but is still limited in some areas. Travel credits (receipts) are estimated on the basis of tourism GST receipts and the use of the withholding tax on services provided by nonresidents improved the coverage of other services (debits). Inward foreign direct investment, including distributed and reinvested earnings, is estimated with a survey and administrative data. Other private financial flows are estimated on the basis of the CPIS and BIS data, but coverage needs to improve. Data on the international investment position are still incomplete as private sector data are not available. 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. A STA technical assistance mission is planned in March 2015 to improve data on private financial flows, International Investment Position, and a range of other specific items.

Notwithstanding recent improvements in the balance of payments statistics, the reliability of the data is uncertain—in part as it is inherently difficult to capture full data with many transactions occurring outside the country and no international counterparty data on tourism services to validate revenue estimates.

Official reserves assets are reported weekly with a (variable) one-week lag. Predetermined foreign currency outflows (mainly debt service payments) are known and reported to APD at the time of annual Article IV consultation missions, while other movements of foreign currency assets are not identified.</td></tr>
<tr><td colspan="2" align="center">II. Data Standards and Quality</td></tr>
<tr><td>Maldives has participated in the General Data Dissemination System (GDDS) since October 14, 2011.</td><td>No data ROSC available.</td></tr>
<tr><td colspan="2" align="center">III. Reporting to STA (Optional)</td></tr>
<tr><td colspan="2">The authorities report macroeconomic data to the IMF on a regular and generally timely basis for publication in the IFS, BOPSY, and GFSY.</td></tr>
</table>

Maldives: Table of Common Indicators Required for Surveillance

(As of January 7, 2015)

	Date of Latest Observation	Date Received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	01/19/2015	01/20/2015	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	01/19/2015	01/20/2015	D	D	D
Reserve/Base Money	01/15/2015	01/20/2015	W	W	M
Broad Money	01/15/2015	01/22/2015	W	W	M
Central Bank Balance Sheet	01/15/2015	01/22/2015	W	W	M
Consolidated Balance Sheet of the Banking System	01/15/2015	01/22/2015	W	W	M
Interest Rates[2]	01/19/2015	01/20/2015	W	W	M
Consumer Price Index	11/30/2014	12/31/2014	W	W	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2013	11/30/2014	A	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	2013	11/30/2014	A	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2013	11/30/2014	A	M	M
External Current Account Balance	2013	11/30/2014	A	M	M
Exports and Imports of Goods and Services	11/30/2014	12/31/2014	M	M	M
GDP/GNP	2013	11/30/2014	A	M	M
Gross External Debt	2013	11/30/2014	A	M	M
International investment Position[6]	2013	12/31/2013	A	A	A

[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. Interest rates on bank deposits are not provided.
[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] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).

MALDIVES

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION—DEBT SUSTAINABILITY ANALYSIS

January 27, 2015

Approved By
Rachel Van Elkan and Catherine Pattillo (IMF) and Satu Kahkonen (IDA)

Prepared by the staffs of the International Monetary Fund (IMF) and the International Development Association (IDA)

Public debt is already very high by international standards and without fiscal adjustment would be on an unsustainable path. The 2015 Budget, included in the baseline, puts in place fiscal measures to reduce the primary deficit but these are not sufficient to stabilize the debt ratio. And there is a risk of expenditure overruns. Maldives public debt problem is largely a domestic one—total public and publicly guaranteed debt is expected to have reached 74.6 percent of GDP in 2014 while public external debt is 27.7 percent of GDP (mainly with multilateral and bilateral creditors). Under the authorities' current policies, public debt continues to rise (104 percent of GDP in 2034) and domestic financing reaches 76 percent of GDP in 2034. A staunch fiscal adjustment effort is needed; otherwise Maldives would face a high risk of overall debt distress driven largely by domestic debt vulnerabilities.[1]

Fiscal policy mistakes and shocks to tourism exports or foreign direct investment are key risks that could trigger debt distress. To place public debt on a firmly downward path, staff proposes an additional focus on expenditure restraint and public financial management reforms which, together with a further rise in Tourism Goods and Services Tax (TGST), would place debt ratios on a sustainable path. Overall Maldives is judged to face a moderate risk of external debt distress, based on an assessment of public external debt, but a heightened overall risk of public debt distress, reflecting the significant and high vulnerabilities related to domestic debt. There are also potential additional risks to external debt if the increase in public debt is financed to a greater extent from external sources than currently assumed.

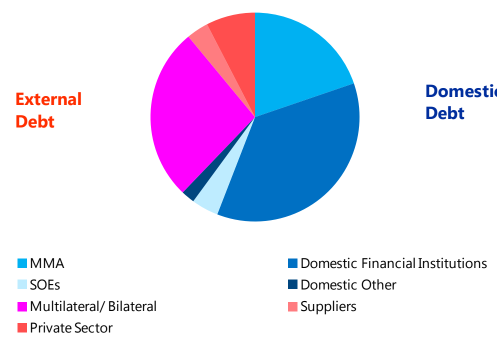
[1] In 2011, Maldives was classified as a medium performer in terms of policies and institutions by the World Bank's Country Policy and Institutional Assessment (CPIA), averaging 3.28 over 2011–13. The indicative thresholds for medium performers are 40 percent for the PV of the debt to GDP ratio, 150 percent for the debt to exports ratio, 250 percent for the PV of the debt to revenue ratio, 20 percent for the debt service to exports ratio and 20 percent for the debt service to revenue ratio. Thresholds are applicable to public and publicly guaranteed (PPG) external debt (not to total PPG debt).Previously Maldives was rated as a high risk of external debt distress, the change in risk rating reflects net repayments of private external debt since the previous assessment and a much lower private external debt stock.

RECENT DEBT DEVELOPMENTS

Total public debt has risen rapidly since the 2004 tsunami from around 36 percent of GDP in 2004 to 74.6 percent of GDP in 2014, excluding domestic arrears, above the 60 percent limit in the Fiscal Responsibility Law (Figure 2 and Table 3).[1,2] The increase initially reflected additional expenditure needs in the aftermath of the tsunami but more recently additional recurrent spending on wages, social welfare, and subsidies. Under the baseline scenario, public debt would remain on a rising path over the medium term.

Public debt is held mainly by domestic banks, the Maldives Monetary Authority (MMA) and official multilateral and bilateral creditors (text figure)**.**

Public Debt Holdings by Sector
(Percent distribution)



The economy has relied heavily on the issuance of treasury bills and monetization as well as external borrowing to finance deficits. There has also been a buildup in domestic arrears which are estimated at 6.3 percent of GDP in 2013. The DSA baseline assumes the authorities clear these arrears going forward over a period of five years.

The stock of external debt is substantially lower than previously projected but has been on a rising trajectory. Between 2011 and 2013, net repayments of external public and publicly guaranteed external debt and revised data for the private external debt have reduced the estimated level of external debt in 2013 from 98 percent of GDP projected in the 2013 debt sustainability analysis to 32 percent of GDP; PPG external debt is now estimated at 27.6 percent in 2013 down from 44 percent of GDP in the 2013 DSA. Private external debt is now estimated to be just 5 percent of GDP in 2013 substantially lower than the projection of 53 percent in the previous DSA—this reflects revisions to the external accounts which have also reduced the scale of the current account deficit and lower net flows than projected in the past two years. However, these data are still estimates and remain uncertain. With an open capital account and little reporting private sector external debt data are subject to large errors and there are likely to be further revisions to debt estimates.

Taken together private external debt and total public debt are estimated at about $ 1.8 bn (67 percent of GDP) in 2013.

[1] Public debt is defined as the net debt of the non-financial public sector comprising central government, State Owned Enterprises, publicly guaranteed debt and net of government deposits. It does not include domestic arrears.

[2] Since the 2013 Article IV Staff Report nominal GDP has been revised upwards. The authorities have adopted market price GDP as their aggregate (instead of gross value added at basic prices). The revision raises the level of nominal GDP by 13 percent in 2013.

MACROECONOMIC ASSUMPTIONS

The macroeconomic assumptions underlying this DSA have been updated based on developments in 2013 and 2014. At the time of the IMF's 2013 Article IV consultation, official data pointed to very large current account and fiscal deficits. Two years on, the picture is somewhat different: a recovery in tourism is supporting real growth and Maldives is performing well compared to peers; substantial data revisions paint a less worrying picture of the current account (with deficits of 10.6 percent of GDP in 2012 and 6.5 percent of GDP in 2013); external debt estimates are lower; and while the large fiscal deficit has continued to widen following increases in recurrent spending, measures in the 2015 Budget and earlier increases in taxes, including the Tourism Goods and Services Tax (TGST) should help to rein in the deficit. The primary deficit is therefore projected to narrow–but not sufficiently to bring debt ratios down.

Consistent with these developments, the main changes in the macroeconomic assumptions in the 2014 DSA compared to those contained in the IMF's 2013 Article IV Staff Report are: (i) a lower non-interest current account deficit; (ii) a smaller but still sizeable primary deficit; (iii) a lower starting point for external debt; and (iv) a somewhat stronger growth path (accompanied by slightly higher FDI) reflecting a stronger tourism performance and a somewhat lower probability attached to a twin deficit crisis (which would hit confidence and permanently damage growth prospects).

The baseline scenario is built on current policies, including the Authorities 2015 Budget measures. This includes the green tax on tourism (replacing the bednights tax), increases in import duties, better targeting of subsidies, and a public employment freeze. The baseline does not include estimates for revenues from the Special Economic Zones (SEZs). It also does not include any compensation amount from the arbitration ruling over the airport concession.[3]

Debt SustainabilityAnalysis: Macroeconomic Assumptions 2014-2034

IMF 2013 and 2014 Article IV Reports	2013	2014
(Annual percentage change)		
Real growth	4.1	4.5
Inflation	4.6	3.5
(In percent of GDP)		
Current Account (non interest)	25.5	4
FDI	8.4	8.6
Primary Deficit	8.9	2.4

Key assumptions: Overall, the baseline macroeconomic assumptions are a little stronger than the previous DSA.[4] The baseline macro scenario includes significant fiscal adjustment but the primary balance does not improve sufficiently to prevent a rising debt profile.

- *Real GDP growth.* Fiscal adjustment has a mild negative effect on growth in the short run, slowing to 4–4¼ percent in 2016–17 and averages 4.5 percent over 2020–34 a slower pace than the average of the past ten years (around 6.5 percent) which included the initial rapid

[3] In 2012 the authorities cancelled the airport concession contract with GMR and Malaysia Airports Berhad to upgrade and operate Malé airport. Arbitration ruled in favor of GMR. Maldives Airport Company Limited (MACL) paid $4mn in immediate costs. Agreement on a final settlement has yet to be reached.

[4] The baseline scenario in the DSA assumes that the stabilized exchange rate regime holds.

development of the tourism sector; estimates of potential output growth (are around 5 percent).[5] The tourism sector initially continues to experience a recovery driven by expansion from new markets (especially China) and a gradual pick up in core markets. New resorts are likely to be developed and the development of the airport could substantially add to capacity, sustaining growth into the medium term.[6]

- *Inflation.* GDP deflator inflation remains low over the next two years reflecting lower oil prices and generally weaker global commodity prices partly offset by higher import duties and then rises to around 3.5 percent—close to its long run average.

- *The current account.* Substantial data revisions have reduced current account deficit compared to the previous DSA.[7] The non interest current account deficit narrows in 2015 to 3.7 percent of GDP with lower oil prices and narrows a little to 3.4 percent of GDP in 2019 with improving tourist receipts and some restraint on import demand from the authorities' planned fiscal adjustment. Thereafter the current account deficit widens a little. Reserves levels strengthen by 2019.

- *The fiscal deficit.* The primary deficit (under the baseline), improves by 3.7 percentage points in 2015 significantly boosted by the temporary impact of bringing forward the timing of extension of resort licenses; and in 2016 revenues strengthen with the full year effect of higher import duties and the imposition of the green tax. Further consolidation is expected thereafter from gradual expenditure restraint, lowering the primary deficit to around 2.4 percent of GDP. But this is less than the stabilizing primary deficit (0.8 percent of GDP) and public debt ratios still continue to drift upwards—reaching 104 percent of GDP in 2034.

- *Financing.* In the recent past, the bulk of the deficit financing has been met from domestic sources, in particular through the domestic banking system and the pension fund. Interest rates had risen sharply in the primary market for T-bills in 2012 and 2013. But, from mid 2014 the government has replaced the auction system with a 'tap system' (of fixed interest rates) which lowered interest costs by about 200bp on average across maturities. This temporarily stabilized interest cost on domestic debt. And thus far demand for T-bills has been sustained by the banking sector, against a backdrop of weak lending conditions (with banks reluctant to lend to sectors where NPLs built up during the crisis). However if debt rises, lower yields may not be sustained and with global interest rates expected to rise, Maldives yields are assumed to remain high over the forecast period. In the debt sustainability analysis it is

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[5] The real growth measure used in this report is gross value added at basic prices.

[6] Around three quarters of activity is directly or indirectly linked to tourism. Maldives is a high end tourist destination with around 60 percent of resorts in the 5 star and plus category, and demand is relatively price and income inelastic. The authorities expect to lease ten new resorts a year. A second runway at the airport will also add to capacity.

[7] Revisions to the balance of payments data are consistent with IMF technical assistance advice. Revisions substantially reduced the current account deficits from around 20 percent of GDP to single digits in 2012 and 2013.

assumed that the bulk of financing is sourced domestically.[8] However, as the debt ratio rises this may not be sustainable—and raising external financing may become difficult.

- Non debt creating financial flows. With limited lending opportunities, Maldives banks have paid down debt and increased assets abroad since the global financial crisis, leading to a steady financial account outflow (of around 4 percent of GDP). These outflows are expected to continue and contribute to the residual in the external DSA.

EXTERNAL AND PUBLIC DEBT SUSTAINABILITY

External debt sustainability. Under the baseline scenario, with a smaller current account deficit to be financed, the present value of external debt falls back a little to 26.7 percent of GDP and the external burden remains comfortably below the thresholds. However, the improvement is in part because it is assumed that the authorities continue to finance public debt predominantly from domestic sources—a shift in financing mix towards greater external borrowing is an upside risk to the external DSA. Furthermore, the external debt path is vulnerable to export shocks, a combined shock to exports, GDP growth, US dollar GDP deflator and non-debt creating flows, and a scenario where data reverts to historical averages (of a larger current account deficit and slightly weaker growth). In the historical averages scenario two thresholds would be breached, and a third rises close to the threshold.

Public debt sustainability. Public debt is already at a very high level and, even if the measures in the 2015 Budget are effectively implemented, debt ratios continue to rise and are in breach of the benchmark. Under the baseline, the PV of public debt rises from 70 percent of GDP in 2014 to 99 percent of GDP in 2034. Domestic debt is also highly vulnerable to shocks to the primary balance and to growth (and there are downside risks to non tourism activity for example if domestic arrears continue to build). Shocks to public debt or fiscal slippage or a lower growth trajectory than expected easily push debt onto an unsustainable path.

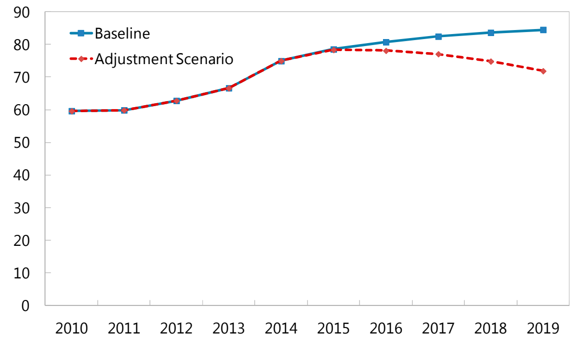
ASSESSMENT

Current policies still lead to rising public debt levels and further adjustment is needed to build buffers and reduce the risk of public debt distress. The DSA therefore points to the need for additional fiscal consolidation measures in the near term.

[8] In Maldives while such large domestic financing may have a small effect crowding out domestic activity, it is unlikely to affect tourism (which accounts for around three-quarters of activity in Maldives directly and indirectly), since the resorts typically obtain their financing from abroad. The impact on growth is not as adverse as for other economies.

IMF staff's view is that further fiscal measures are needed to firmly place debt on a downward path and this should entail better expenditure control and public financial management reforms. Staff would recommend a further fiscal adjustment effort of around 3 percent of GDP over five years. This could be accomplished through greater expenditure restraint, focusing on control of the wage bill, containing rising healthcare costs, and finding savings on transport and communications. A further rise in the TGST rate from 12 to 15 percent would also help to underpin revenues. Such an adjustment path would help to stabilize debt by 2016 and then begin to bring the debt ratio down (see text figure).

Public Debt: Baseline vs. Adjustment Scenarios, 2010–2019
(In percent of GDP)



Sources: Maldives authorities; and IMF staff estimates.

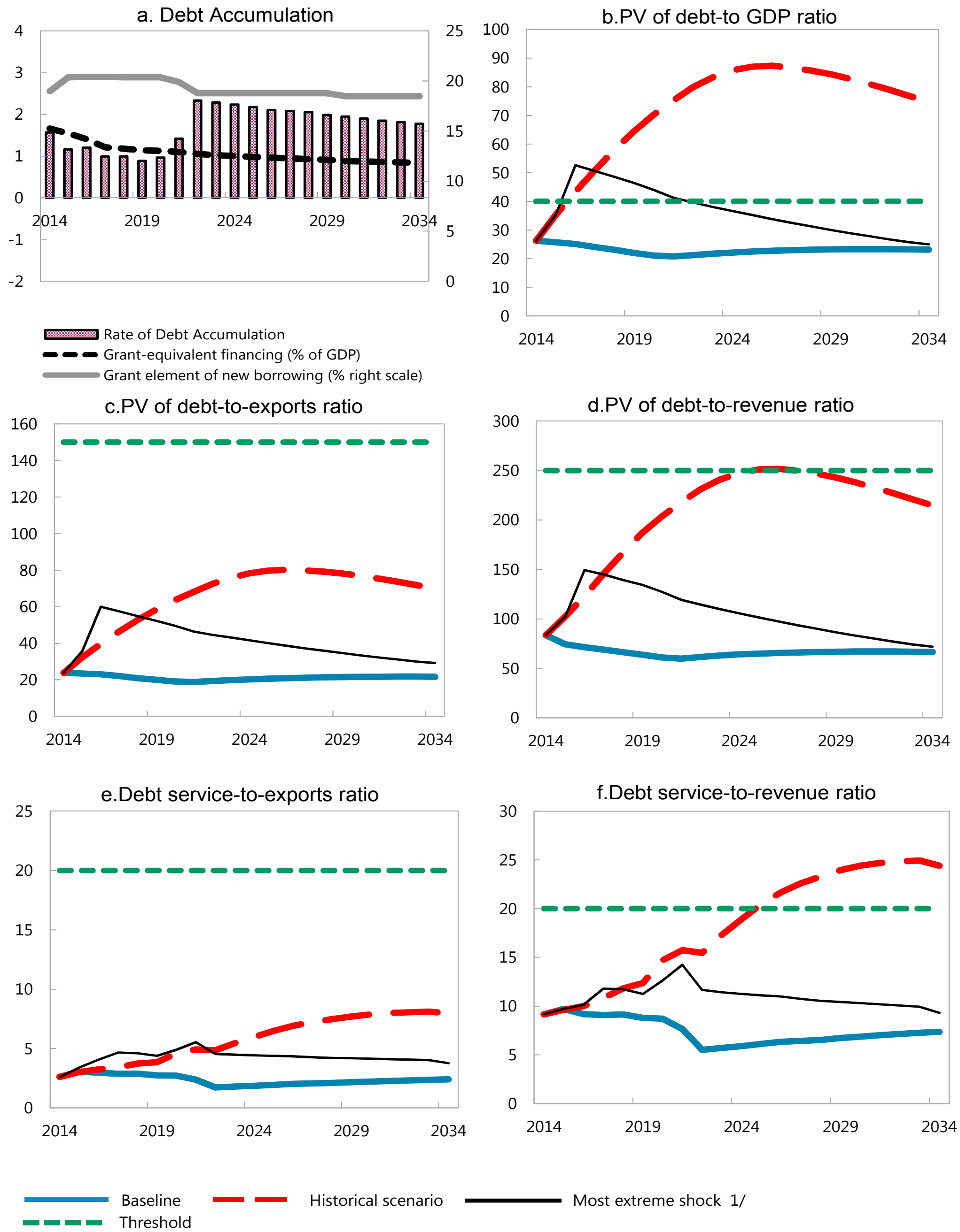
Even with a sustained fiscal consolidation effort, Maldives has a high level of public debt and would remain vulnerable for a number of years. A deterioration of public finances, or external shocks to tourism earnings and foreign direct investment, or a dent to confidence against a backdrop of rising fiscal pressure are all important risks.

External risk rating. Overall, Maldives is judged to face a moderate risk of external debt distress, based on an assessment of public external debt, but a heightened overall risk of debt distress, reflecting the significant and high vulnerabilities related to domestic debt. In addition, as public debt rises there is a risk that domestic financing sources become sated and financing has to be sought from external sources, thus worsening the external debt outlook. The lowering of the risk rating from high to moderate largely reflects data revisions and the much lower private external debt stock in the current DSA compared to projections of the previous DSA—there were significant net repayments of private external debt during 2011–13.

AUTHORITIES' VIEWS

The authorities were of the view that the measures in the 2015 Budget would deliver bigger savings and larger revenue increases than projected by staff (especially related to revenues from the acquisition of SEZs and resort licenses). They expected the public employment freeze would generate substantial savings on the wage bill. They expected these to be sufficient to bring debt ratios down without the need for further revenue raising or other measures. Nonetheless, they concurred with the external risk rating, though they judged the risks from the shock scenarios to be lower than assessed by staff.

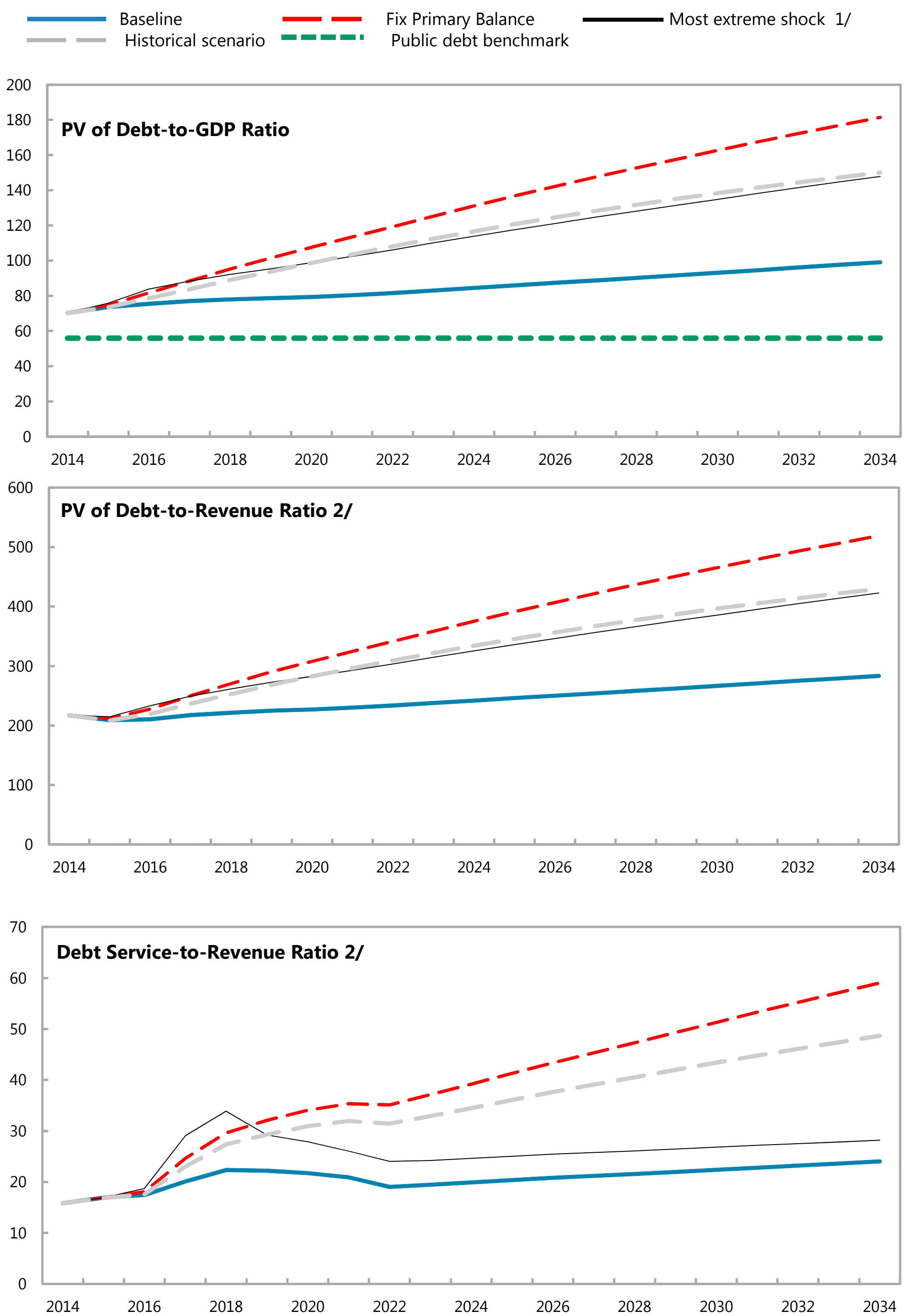
Figure 1. Maldives Baseline Scenario: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios , 2014–2034 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2024. In figure b. it corresponds to a Exports shock; in c. to a Exports shock; in d. to a Exports shock; in e. to a Exports shock and in figure f. to a Exports shock

Figure 2. Maldives Baseline Scenario: Indicators of Public Debt Under Alternative Scenarios, 2014–2034 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio on or before 2024.
2/ Revenues are defined inclusive of grants.

Table 1. Maldives: External Debt Sustainability Framework, Baseline Scenario, 2011–34 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical 6/ Average	Standard 6/ Deviation	Projections									
	2011	2012	2013			2014	2015	2016	2017	2018	2019	2014-2019 Average	2024	2034	2020-2034 Average
External debt (nominal) 1/	**42.6**	**34.3**	**32.2**			**34.3**	**33.8**	**33.6**	**32.8**	**32.0**	**31.0**		**31.2**	**32.0**	
of which: public and publicly guaranteed (PPG)	29.6	28.5	27.6			27.7	27.6	27.5	26.9	26.4	25.7		26.9	28.5	
Change in external debt	-2.7	-8.3	-2.2			2.1	-0.5	-0.2	-0.8	-0.8	-1.0		0.3	-0.1	
Identified net debt-creating flows	0.0	-1.8	-8.9			-6.4	-10.3	-8.8	-9.0	-8.8	-8.2		-6.0	-3.0	
Non-interest current account deficit	**16.8**	**9.7**	**5.9**	**14.0**	**7.3**	**7.4**	**3.7**	**4.8**	**4.2**	**3.8**	**3.4**		**3.6**	**5.0**	4.0
Deficit in balance of goods and services	-5.5	-10.6	-17.8			-17.1	-21.7	-19.9	-20.3	-20.8	-21.1		-20.7	-17.8	
Exports	104.4	95.5	105.0			110.1	109.8	109.2	109.6	110.2	110.3		109.5	106.6	
Imports	98.9	84.9	87.3			93.0	88.1	89.2	89.3	89.4	89.1		88.8	88.8	
Net current transfers (negative = inflow)	10.4	10.2	10.6	5.8	7.4	10.9	11.5	11.3	11.3	11.4	11.4		11.5	11.5	11.5
of which: official	-2.0	-0.9	-0.3			-1.4	-1.0	-0.6	-0.5	-0.4	-0.4		-0.3	-0.1	
Other current account flows (negative = net inflow)	11.9	10.1	13.0			13.6	13.9	13.5	13.2	13.2	13.1		12.7	11.4	
Net FDI (negative = inflow)	**-18.2**	**-9.0**	**-13.4**	**-8.7**	**4.3**	**-13.3**	**-13.7**	**-13.8**	**-13.3**	**-12.6**	**-11.6**		**-9.3**	**-7.8**	-8.6
Endogenous debt dynamics 2/	**1.4**	**-2.5**	**-1.4**			**-0.5**	**-0.2**	**0.1**	**0.1**	**0.0**	**0.0**		**-0.3**	**-0.3**	
Contribution from nominal interest rate	1.3	0.9	0.7			1.1	1.4	1.4	1.4	1.4	1.3		1.0	1.0	
Contribution from real GDP growth	-2.9	-0.5	-1.5			-1.5	-1.6	-1.2	-1.3	-1.3	-1.4		-1.3	-1.3	
Contribution from price and exchange rate changes	2.9	-2.9	-0.6			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**-2.7**	**-6.5**	**6.8**			**8.5**	**9.8**	**8.6**	**8.2**	**7.9**	**7.3**		**6.3**	**3.0**	
of which: exceptional financing	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	30.8			32.9	32.0	31.3	30.0	28.7	27.4		26.5	26.7	
In percent of exports	...	...	29.4			29.9	29.1	28.6	27.4	26.1	24.8		24.2	25.0	
PV of PPG external debt	**...**	**...**	**26.2**			**26.3**	**25.7**	**25.2**	**24.1**	**23.1**	**22.0**		**22.2**	**23.1**	
In percent of exports	**...**	**...**	**25.0**			**23.9**	**23.4**	**23.1**	**22.0**	**20.9**	**19.9**		**20.3**	**21.7**	
In percent of government revenues	**...**	**...**	**92.6**			**83.6**	**74.5**	**71.3**	**69.0**	**66.3**	**63.7**		**64.1**	**66.5**	
Debt service-to-exports ratio (in percent)	**8.9**	**8.7**	**7.2**			**6.2**	**7.2**	**6.7**	**6.5**	**5.7**	**5.4**		**3.8**	**3.7**	
PPG debt service-to-exports ratio (in percent)	**3.1**	**3.1**	**2.8**			**2.6**	**3.1**	**3.0**	**2.9**	**2.9**	**2.7**		**1.9**	**2.4**	
PPG debt service-to-revenue ratio (in percent)	**12.7**	**11.8**	**10.5**			**9.2**	**9.7**	**9.2**	**9.1**	**9.1**	**8.8**		**5.9**	**7.4**	
Total gross financing need (Millions of U.S. dollars)	337.5	334.2	52.7			65.8	-3.0	9.9	-3.9	-29.1	-29.6		-17.0	298.3	
Non-interest current account deficit that stabilizes debt ratio	19.5	18.0	8.0			5.3	4.1	5.0	5.1	4.6	4.3		3.2	5.1	
Key macroeconomic assumptions															
Real GDP growth (in percent)	6.5	1.3	4.7	6.2	8.3	5.0	5.0	3.9	4.2	4.4	4.6	4.5	4.5	4.4	4.5
GDP deflator in US dollar terms (change in percent)	-6.1	7.2	1.8	3.9	4.8	0.7	1.5	3.0	4.1	4.2	4.1	2.9	3.5	3.5	3.5
Effective interest rate (percent) 5/	3.0	2.4	2.1	3.5	1.7	3.5	4.2	4.4	4.5	4.5	4.5	4.3	3.6	3.4	3.6
Growth of exports of G&S (US dollar terms, in percent)	21.0	-0.6	17.1	8.5	13.1	10.9	6.3	6.4	8.9	9.3	9.1	8.5	7.8	7.8	8.0
Growth of imports of G&S (US dollar terms, in percent)	36.4	-6.7	9.5	8.5	23.4	12.7	0.9	8.5	8.5	8.9	8.6	8.0	8.1	8.1	8.2
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	19.0	20.4	20.4	20.4	20.4	20.4	20.2	18.8	18.5	18.9
Government revenues (excluding grants, in percent of GDP)	25.5	25.1	28.3			31.4	34.6	35.3	34.9	34.8	34.5		34.7	34.8	34.7
Aid flows (in Millions of US dollars) 7/	88.0	51.9	-14.2			26.9	24.8	29.8	26.7	27.4	29.4		29.8	41.3	
of which: Grants	47.5	23.9	7.6			26.9	22.1	19.4	16.3	16.0	17.8		17.8	17.8	
of which: Concessional loans	40.5	28.1	-21.8			0.0	2.7	10.3	10.4	11.4	11.6		12.0	23.5	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			1.7	1.5	1.4	1.2	1.2	1.1		1.0	0.8	1.0
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			35.2	32.5	30.8	29.3	28.3	29.0		24.4	21.2	23.6
Memorandum items:															
Nominal GDP (Millions of US dollars)	2332	2534	2699			2855	3043	3258	3534	3843	4188		6267	13664	
Nominal dollar GDP growth	0.0	8.7	6.5			5.8	6.6	7.1	8.5	8.7	9.0	7.6	8.1	8.1	8.2
PV of PPG external debt (in Millions of US dollars)			708.2			750.5	783.4	819.9	852.0	886.9	920.8		1392.2	3162.7	
(PVt-PVt-1)/GDPt-1 (in percent)						1.6	1.2	1.2	1.0	1.0	0.9	1.1	2.2	1.8	1.9
Gross workers' remittances (Millions of US dollars)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of PPG external debt (in percent of GDP + remittances)	...	...	26.2			26.3	25.7	25.2	24.1	23.1	22.0		22.2	23.1	
PV of PPG external debt (in percent of exports + remittances)	...	...	25.0			23.9	23.4	23.1	22.0	20.9	19.9		20.3	21.7	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	2.8			2.6	3.1	3.0	2.9	2.9	2.7		1.9	2.4	

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 (for Maldives bank placements abroad 4 percent of GDP); and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

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 6 years-- the years surrounding the 2004 Tsunami are excluded as it is a one off exceptional event.

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 2. Maldives: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2014–34

(In percent)

	Projections							
	2014	2015	2016	2017	2018	2019	**2024**	2034
PV of debt-to GDP ratio								
Baseline	26	26	25	24	23	22	**22**	23
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	26	35	43	51	58	65	**86**	75
A2. New public sector loans on less favorable terms in 2014-2034 2	26	27	27	26	26	26	**29**	35
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	26	27	28	27	26	24	**25**	26
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	26	35	53	51	49	46	**37**	25
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	26	27	28	26	25	24	**24**	25
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	26	31	36	34	33	31	**28**	24
B5. Combination of B1-B4 using one-half standard deviation shocks	26	34	46	45	43	41	**34**	27
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	26	37	36	34	33	31	**32**	33
PV of debt-to-exports ratio								
Baseline	24	23	23	22	21	20	**20**	22
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	24	32	40	47	53	59	**78**	70
A2. New public sector loans on less favorable terms in 2014-2034 2	24	24	25	24	24	23	**27**	33
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	24	23	23	22	21	20	**20**	22
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	24	36	60	57	55	52	**42**	29
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	24	23	23	22	21	20	**20**	22
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	24	28	33	31	30	28	**25**	22
B5. Combination of B1-B4 using one-half standard deviation shocks	24	31	42	41	39	37	**31**	25
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	24	23	23	22	21	20	**20**	22
PV of debt-to-revenue ratio								
Baseline	84	74	71	69	66	64	**64**	67
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	84	102	123	146	167	187	**247**	215
A2. New public sector loans on less favorable terms in 2014-2034 2	84	77	76	76	75	74	**84**	102
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	84	79	79	76	73	71	**71**	74
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	84	102	149	145	139	134	**106**	72
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	84	78	78	76	73	70	**70**	73
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	84	89	101	98	94	90	**80**	69
B5. Combination of B1-B4 using one-half standard deviation shocks	84	98	132	128	123	118	**99**	76
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	84	106	101	98	94	90	**91**	94

Table 2. Maldives: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2014–34 (continued)

(In percent)

Debt service-to-exports ratio								
Baseline	3	3	3	3	3	3	**2**	2
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	3	3	3	3	4	4	**6**	8
A2. New public sector loans on less favorable terms in 2014-2034 2	3	3	3	3	3	3	**2**	3
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	3	3	3	3	3	3	**2**	2
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	3	3	4	5	5	4	**4**	4
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	3	3	3	3	3	3	**2**	2
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	3	3	3	3	3	3	**3**	3
B5. Combination of B1-B4 using one-half standard deviation shocks	3	3	3	4	4	4	**3**	3
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	3	3	3	3	3	3	**2**	2
Debt service-to-revenue ratio								
Baseline	9	10	9	9	9	9	**6**	7
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2014-2034 1/	9	10	10	11	12	12	**19**	24
A2. New public sector loans on less favorable terms in 2014-2034 2	9	10	9	9	9	9	**7**	10
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2015-2016	9	10	10	10	10	10	**7**	8
B2. Export value growth at historical average minus one standard deviation in 2015-2016 3/	9	10	10	12	12	11	**11**	9
B3. US dollar GDP deflator at historical average minus one standard deviation in 2015-2016	9	10	10	10	10	10	**6**	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2015-2016 4/	9	10	10	10	10	10	**8**	8
B5. Combination of B1-B4 using one-half standard deviation shocks	9	10	11	12	12	11	**10**	9
B6. One-time 30 percent nominal depreciation relative to the baseline in 2015 5/	9	14	13	13	13	12	**8**	10
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	15	15	15	15	15	15	**15**	15

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.

Table 3. Maldives: Public Sector Debt Sustainability Framework, Baseline Scenario, 2011–34

(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2011	2012	2013	Average 5/	Standard Deviation 5/	2014	2015	2016	2017	2018	2019	2014-19 Average	2024	2034	2020-34 Average
Public sector debt 1/	59.5	61.7	63.0			74.6	75.5	77.9	79.8	81.2	82.1		89.2	104.4	
of which: foreign-currency denominated	31.7	29.8	28.2			30.6	27.6	27.5	26.9	26.4	25.7		26.9	28.5	
			34.9			44.1	47.9	50.4	52.9	54.9	56.5	0.0	62.3	75.9	
Change in public sector debt	0.1	2.2	1.4			11.6	0.9	2.4	1.9	1.4	0.9		1.6	1.5	
Identified debt-creating flows	0.7	3.0	4.0			8.2	3.6	2.3	1.8	1.3	0.9		1.5	1.4	
Primary deficit	4.5	4.8	5.3	7.8	5.1	8.7	4.5	3.2	2.9	2.0	1.9	3.9	2.4	2.4	2.4
Revenue and grants	27.6	26.0	28.6			32.4	35.3	35.9	35.4	35.2	34.9		34.9	34.9	
of which: grants	2.0	0.9	0.3			0.9	0.7	0.6	0.5	0.4	0.4		0.3	0.1	
Primary (noninterest) expenditure	32.1	30.8	33.9			41.0	39.8	39.1	38.3	37.2	36.8		37.3	37.4	
Automatic debt dynamics	-2.8	-1.8	-1.3			-0.5	-0.9	-0.9	-1.1	-0.7	-0.9		-0.9	-1.0	
Contribution from interest rate/growth differential	-5.3	-0.2	-1.2			-0.7	-0.9	-0.6	-0.6	-0.2	-0.4		-0.5	-0.6	
of which: contribution from average real interest rate	-1.7	0.6	1.5			2.4	2.6	2.2	2.6	3.2	3.2		3.2	3.7	
of which: contribution from real GDP growth	-3.6	-0.8	-2.8			-3.0	-3.5	-2.9	-3.2	-3.4	-3.6		-3.8	-4.3	
Contribution from real exchange rate depreciation	2.5	-1.6	-0.1			0.2	0.0	-0.3	-0.5	-0.5	-0.5		...	...	
Other identified debt-creating flows	-1.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	-1.0	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	
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	-0.6	-0.8	-2.6			3.4	-2.7	0.1	0.1	0.1	-0.1		0.1	0.1	
Other Sustainability Indicators															
PV of public sector debt	...	...	61.7			70.3	73.6	75.5	77.0	78.0	78.6		84.5	99.0	
of which: foreign-currency denominated	...	...	26.9			26.3	25.7	25.2	24.1	23.1	22.0		22.2	23.1	
of which: external	...	...	26.2			26.3	25.7	25.2	24.1	23.1	22.0		22.2	23.1	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	36.5	37.8	41.5			47.1	51.8	54.2	56.5	58.5	60.0		66.0	79.6	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	215.6			217.2	208.7	210.5	217.6	221.4	225.1		241.9	283.5	
PV of public sector debt-to-revenue ratio (in percent)	...	...	217.7			223.7	213.1	214.1	220.5	224.1	227.9		243.9	284.6	
of which: external 3/	...	...	92.6			83.6	74.5	71.3	69.0	66.3	63.7		64.1	66.5	
Debt service-to-revenue and grants ratio (in percent) 4/	17.6	20.8	18.0			15.8	16.9	17.5	20.1	22.4	22.2		19.9	24.0	
Debt service-to-revenue ratio (in percent) 4/	19.0	21.6	18.1			16.3	17.3	17.8	20.3	22.6	22.5		20.1	24.1	
Primary deficit that stabilizes the debt-to-GDP ratio	4.5	2.6	3.9			-2.9	3.6	0.8	1.0	0.6	1.0		0.8	0.9	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	6.5	1.3	4.7	5.5	5.4	5.0	5.0	3.9	4.2	4.4	4.6	4.5	4.5	4.4	4.5
Average nominal interest rate on forex debt (in percent)	1.3	1.4	1.3	2.0	0.9	2.7	3.8	4.0	4.1	4.2	4.1	3.8	3.1	3.1	3.2
Average nominal interest rate on domestic debt (in percent)	6.8	9.5	7.3	6.8	2.7	6.8	6.3	6.8	8.5	9.6	9.4	7.9	8.7	8.5	8.6
Average real interest rate (in percent)	-3.1	1.0	2.6	0.6	2.5	3.9	3.7	3.1	3.4	4.2	4.1	3.7	3.8	3.8	3.8
Average real interest rate on foreign-currency debt (in percent)	-2.1	-1.6	-1.4	-1.7	0.7	-1.3	-1.4	-1.7	-1.9	-1.9	-1.9	-1.7	-1.9	-1.9	-1.9
Average real interest rate on domestic debt (in percent)	-5.5	2.4	5.2	0.6	5.2	6.0	4.7	3.6	4.2	5.3	5.0	4.8	5.0	4.8	4.9
Real exchange rate depreciation (in percent, + indicates depreciation)	8.8	-5.2	-0.3	-1.5	5.2	0.6	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	13.0	7.0	2.0	6.3	4.1	0.7	1.5	3.0	4.1	4.2	4.1	2.9	3.5	3.5	3.5
Growth of real primary spending (deflated by GDP deflator, in percent)	0.7	-2.7	15.2	1.9	5.9	27.1	1.8	2.1	2.2	1.3	3.6	6.4	4.5	4.4	4.6
Grant element of new external borrowing (in percent)	...	...	...	...	...	19.0	20.4	20.4	20.4	20.4	20.4	20.2	18.8	18.5	...

Sources: Country authorities; and staff estimates and projections.

1/ Public debt is defined here as the net debt of the non-financial public sector comprising the central government, SOEs, and publicly guaranteed debt. It is net of government deposits (3 percent of GDP). It does not include domestic arrears.

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 6 years-- the years around the 2004 Tsunami are excluded as they are a one off exceptional event.

Table 4. Maldives: Sensitivity Analysis for Key Indicators of Public Debt, Baseline Scenario, 2014–34

		Projections						
	2014	2015	2016	2017	2018	2019	2024	2034
PV of Debt-to-GDP Ratio								
Baseline	70	74	76	77	78	79	85	99
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	70	74	79	84	89	94	117	150
A2. Primary balance is unchanged from 2014	70	75	82	88	95	101	131	181
A3. Permanently lower GDP growth 1/	70	72	76	79	83	86	113	196
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-2016	70	76	84	88	92	95	114	148
B2. Primary balance is at historical average minus one standard deviations in 2015-2016	70	79	89	91	91	91	95	107
B3. Combination of B1-B2 using one half standard deviation shocks	70	78	87	89	91	92	102	121
B4. One-time 30 percent real depreciation in 2015	70	82	83	84	85	85	90	106
B5. 10 percent of GDP increase in other debt-creating flows in 2015	70	80	82	83	84	84	90	103
PV of Debt-to-Revenue Ratio 2/								
Baseline	217	209	211	218	221	225	242	284
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	217	208	219	237	253	269	334	430
A2. Primary balance is unchanged from 2014	217	212	228	250	271	290	375	519
A3. Permanently lower GDP growth 1/	217	204	211	224	235	247	322	559
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-2016	217	215	233	250	262	273	326	423
B2. Primary balance is at historical average minus one standard deviations in 2015-2016	217	223	249	256	259	261	273	306
B3. Combination of B1-B2 using one half standard deviation shocks	217	220	242	252	258	264	291	347
B4. One-time 30 percent real depreciation in 2015	217	232	232	238	241	243	259	302
B5. 10 percent of GDP increase in other debt-creating flows in 2015	217	227	229	235	239	242	257	295
Debt Service-to-Revenue Ratio 2/								
Baseline	16	17	17	20	22	22	20	24
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	16	17	18	23	27	29	34	49
A2. Primary balance is unchanged from 2014	16	17	18	25	30	32	39	59
A3. Permanently lower GDP growth 1/	16	17	18	21	24	25	30	59
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2015-2016	16	18	19	24	28	29	31	43
B2. Primary balance is at historical average minus one standard deviations in 2015-2016	16	17	19	29	34	29	25	28
B3. Combination of B1-B2 using one half standard deviation shocks	16	17	19	27	32	29	27	34
B4. One-time 30 percent real depreciation in 2015	16	19	21	25	28	28	26	33
B5. 10 percent of GDP increase in other debt-creating flows in 2015	16	17	19	29	26	26	23	26

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.

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International Monetary Fund
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Washington, D. C. 20431 USA

IMF Executive Board Concludes 2014 Article IV Consultation with Maldives

On February 11, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Maldives.

The Maldives real economy has picked up. Growth is estimated to have reached 5 percent in 2014 with stronger tourism activity driven by a rapid expansion from Asian markets and a tepid recovery from Europe. Staff expects growth to be around 5 percent in 2015. Weaker import prices have pushed down inflation to low levels (1.1 percent in November 2014). Higher tourism exports and subdued global food and fuel inflation have helped reduce the current account deficit to around 8.4 percent of GDP in 2014; and following significant data revisions, the current account is now substantially smaller than previously estimated. Lower oil prices have improved the outlook for the current account and inflation in 2015. Gross official reserves have risen to around $614mn (2.8 months imports). Financial soundness indicators are slowly improving, monetary conditions are loose, but credit growth is subdued at just 0.5 percent year on year to November 2014.

However, persistent and growing fiscal deficits have driven up the public debt ratio to a high level. The fiscal deficit increased to an estimated 7.8 percent of GDP in 2013 and, following increases in recurrent spending, the deficit is likely to have widened further in 2014. Sustained primary deficits have led to an increase in the public debt level from 52 percent in 2009 to 75 percent of GDP in 2014.

The 2015 budget includes a number of important measures to rein in the fiscal deficit through revenue raising measures (imposing a green tax, acquiring fees from Special Economic Zones and raising import duties) and expenditure restraint through a public employment freeze and better targeting of subsidies. However, further fiscal adjustment measures would be needed to place debt ratios firmly on a downward path.

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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.

Growth is expected to remain relatively strong in the near term, though the fiscal adjustment envisaged in the 2015 Budget will have a mildly negative effect on growth. There is also some upside potential if lower oil prices are sustained. However, with limited policy buffers, the economy is vulnerable to fiscal slippages and inward spillovers. In the event of large fiscal overruns relative to the authorities' targets, borrowing costs and monetization could increase, which would weaken the external position.

Over the medium term, while the tourism sector is expected to remain the locomotive for growth in Maldives, economic diversification to reduce youth unemployment, and improving the efficiency of public service provision remain key issues. The government has several long run strategies: (i) developing regional hubs and improving transport connectivity which could also encourage voluntary resettlement, and would enable higher quality service provision (though such a change will take many years); (ii) developing Special Economic Zones to diversify jobs into off-port shipping services, IT, financial services industries and tourism-support activities such as traditional fisheries and small-scale agriculture; (iii) undertaking infrastructure development, in particular of the airport, to add to capacity; and (iv) reducing the environmental impact of tourism and reliance on oil imports by developing renewable energy.

Executive Board Assessment[2]

Executive Directors welcomed that Maldives has reached middle-income status, with a pickup in the real economy driven by tourism activity, a moderation in inflation, a marked lowering of the fiscal deficit from its peak in 2009 aided by tax measures, and a stronger reserves position. Although Maldives's outlook is favorable, it shares many of the challenges of other small states, and risks remain, particularly in the fiscal sector.

Directors welcomed the authorities' commitment to fiscal consolidation and the plans contained in the 2015 budget, including raising revenues, improving the targeting of subsidies, and a temporary halt in public sector hiring. Nevertheless, they noted that some of these measures will have only a temporary effect, and that further, durable fiscal adjustment, with a focus on expenditure restraint, will be needed to place the public debt-to-GDP ratio on a downward path over the medium term, consistent with the Fiscal Responsibility Law. Improvements in public financial management and addressing domestic arrears need to support the fiscal consolidation efforts.

[2] 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. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Directors welcomed the improvements to the external sector statistics, in line with IMF technical assistance recommendations, which point to significantly smaller current account deficits than previously estimated. They considered the stabilized exchange rate regime as appropriate for Maldives. Directors welcomed the increase in official reserves, and recommended continued strengthening of the official reserves position.

Directors welcomed the authorities’ commitment to avoiding the monetization of the fiscal deficit, which will help direct monetary policy at supporting the exchange rate regime and build buffers. They supported plans to make greater use of market-based financing for government debt, including by developing the government securities market. Directors welcomed the improvement in financial soundness indicators, and called for continued efforts to strengthen financial supervision, including measures to ensure uniform high standards for institutions that decide to operate in special economic zones.

Directors agreed that public service delivery and economic diversification are key medium-term objectives. They welcomed the proposals for establishing regional hubs and improving inter-island connectivity. Directors stressed that strict ring-fencing of tax exemptions for special economic zones will be necessary to preserve the tax base. They also emphasized that scaling up infrastructure investment should be implemented efficiently in order to boost growth potential.

Directors welcomed the significant recent improvements in macroeconomic statistics, and encouraged the authorities to continue to strengthen data quality and availability, including adopting a statistics law to enhance data provision, to assist policy decisions.

Table. Maldives: Selected Economic Indicators, 2011–15

Population (in 1,000; 2012 est.)	331				
GDP per capita (in U.S. dollars; 2012 est.):	6,675				
Quota (in million SDRs):	10.0				
	2011	2012	2013	2014	2015
			Est.	Proj.	
Output and prices	(Annual percentage change)				
Real GDP (gross value added at basic prices)	6.5	1.3	4.7	5.0	5.0
Inflation (end-of-period) 1/	16.7	5.4	3.1	1.2	0.4
Inflation (period average) 1/	11.3	10.9	4.0	2.5	0.3
GDP deflator	8.6	6.8	-0.9	0.7	1.5
Central government finances					
Revenue and grants	27.6	26.0	28.6	32.4	35.3
Expenditure and net lending	34.1	33.7	36.5	44.0	43.4
Overall balance	-6.6	-7.6	-7.8	-11.6	-8.1
Overall balance excl. grants	-8.6	-8.6	-8.1	-12.6	-8.8
Primary balance	-4.5	-4.8	-5.3	-8.7	-4.6
Public and publicly guaranteed debt	59.9	62.8	66.7	75.0	78.6
Monetary accounts	(Annual percentage change, unless otherwise indicated)				
Broad money	20.1	6.4	16.8	14.2	6.6
Domestic credit	11.3	-2.4	3.9	5.4	5.0
Balance of payments	(In percent of GDP, unless otherwise indicated)				
Current account	-18.1	-10.6	-6.5	-8.4	-5.0
Of which:					
Exports	14.9	12.4	12.3	12.9	10.3
Imports	-73.6	-62.2	-63.1	-68.0	-62.4
Tourism receipts and nonfactor services, net	64.2	60.4	68.6	72.1	73.8
Income (net)	-13.2	-11.0	-13.7	-14.7	-15.2
Current transfers	-10.4	-10.2	-10.6	-10.9	-11.5
Capital and financial account (including e&o)	17.5	9.4	8.9	17.0	12.2
Overall balance	-0.7	-1.2	2.4	8.6	7.2
Gross international reserves (in millions of US$; e.o.p.) 2/	335	305	368	614	832
In months of GNFS imports	1.7	1.7	1.9	2.8	3.7
Memorandum items:					
GDP (in millions of rufiyaa)	35,931	38,943	41,569	43,971	46,863
GDP (in millions of U.S. dollars)	2,332	2,534	2,699	2,855	3,043

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

1/ CPI-Male definition.

2/ MMA liabilities, include allocation of SDR 7.4 million, equivalent to US$11.7 million, made available in Q3 2009, see http://www.imf.org/external/np/tre/sdr/proposal/2009/0709.htm. These are treated as long term liabilities of the MMA.

Statement by Hazem Beblawi, Executive Director for Maldives and Wafa F. Abdelati, Senior Advisor February 11, 2015

At the outset, we would like to thank staff for their insightful analysis, constructive discussions, and well-written reports. The Maldives' authorities highly value the expert advice of the Fund, much of which they agree with, and the effective technical assistance, which they have consistently implemented. They consider the report to reflect positively on developments in the Maldives and particularly appreciate staff's recognition of the specific structural challenges that Maldives faces due to its small population disbursed among so many different islands. This Article IV discussion comes at a time of large data revisions, which places the country in a much better position compared with the alarming assessment in the last report. The authorities fully appreciate staff's difficult position of working with substantial data revisions. However, it is important to underscore that these data revisions are due only to improvements in compilation and coverage, which are based on the recommendations of technical assistance provided by the Fund. The authorities are grateful for the Fund's continued support in improving macroeconomic statistics as well as other areas of technical assistance.

Background. The Maldivian economy is heavily dependent on fisheries and tourism, which have been the major sources of growth, foreign exchange earnings and government revenues. Maldives' economy grew rapidly in the two decades prior to the December 2004 Tsunami, powered by successful development of its tourism sector. Per capita incomes rose to upper middle income levels and social conditions improved commensurately. However, the country was severely hit by a series of natural disasters and external shocks — the tsunami, the 2007-2008 food and fuel crisis, and the subsequent global financial crisis. As a result, the pace of economic activity has been uneven in the past decade and macroeconomic management has been somewhat complicated by the process of political transition to democracy. A sharp slump in tourist activity in 2009 and then again in 2012 reflected the slowdown in Europe, whose share fell from two thirds to one third of tourist arrivals to the Maldives. The picture is more positive now. The real economy is picking up driven by a recovery in tourism activity[1] due to the expansion of new Asian markets, the fiscal position has improved, inflation is very low, and banking soundness has improved.

Fiscal revenue, which is highly dependent on tourism, declined by about 10 percentage points of GDP between 2007 and 2009, and the public sector wage bill surged following the 2008 elections, which prompted the authorities to seek a Stand-By Arrangement in December 2009. At that time, the central government fiscal deficit was estimated at around 30 percent of GDP and a drastic fiscal consolidation was targeted under the program. In the event, the program was interrupted after the first review, mainly because staff was uncertain that the

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[1] More recently, Chinese tourists have continued to grow and now constitute the largest single source country for the Maldives. See "Changing Dynamics in the Maldivian Tourism Industry: Chinese Tourists and Average Length of Stay" by: Azeema Adam and Aishath Zara Nizar, *MMA Research Papers,* Volume 1 Number I, June 2014.

authorities' policies could deliver the envisaged reduction in the fiscal deficit. Nevertheless, the objectives of the 2009 program were largely achieved, particularly with respect to raising sustainable budget revenues, reducing the overall and primary fiscal deficit, and significantly raising international reserves. This experience underscores the authorities' commitment to implement significant reforms, even without a program and while going through political transitions. Moreover—as aptly highlighted in the staff report—the recent balance of payments revisions point to a considerably lower current account deficit than previously believed.

Fiscal Policy. The authorities intend to build on the recent fiscal consolidation. The primary fiscal deficit was reduced from 17 percent of GDP in 2009 to 5½ percent of GDP in 2013 according to staff's estimates (or 2½ percent according to preliminary estimates of the Ministry of Finance), which is a remarkable achievement by any measure. It also far surpasses the episodes of large fiscal consolidation presented by staff in Box 4. This was achieved by introducing a General Sales Tax in 2011 and later broadening its base and raising the rate, a new Business Profits Tax in July 2011, as well as raising duties and some charges. However, the introduction of the universal health program and other social welfare contributions, which were considered a social priority, have since then contributed to rising current spending and crowding out capital expenditures.

The 2015 Budget targets an ambitious further consolidation. Revenue measures include a "green tax" to be levied tourists instead of the bednights tax, raising import duties on some zero rated items, new resorts licenses and land acquisition fees from the Special Economic Zones. Meanwhile, a public employment freeze will be implemented and electricity and food subsidies will be cut, seizing the opportunity of low global oil and food prices and identifying steps to improve targeting. The authorities expect this package to eliminate the primary deficit and set debt on a downward and sustainable path as stipulated in the Fiscal Responsibility Act, introduced in 2013, which aims to limit public debt to 60 percent of GDP, down from the current level of 75 percent of GDP.

In any case, the authorities are keen to review local government pay structures, and they view a public pay body as potentially helpful to ensure consistency of wages and salaries across public service and to move in the direction of public service reform. The authorities consider strengthening public financial management a key priority that will contribute to achieving fiscal sustainability. They attach high importance to reducing the long-standing stock of government arrears and preventing further accumulation. They are accordingly requesting additional technical assistance from the Fund, particularly in the area of the fiscal chart of accounts and budget execution. Additional revenue measures *could* be considered, if needed. The staff suggests that the authorities undertake additional fiscal measures equivalent to 3 percent of GDP, which would be manageable. The authorities may out-perform staff's fiscal projections as has been the case in the past[2].

[2]The authorities targeted an overall fiscal deficit of 4 percent in 2013, and the last staff report had projected a deficit exceeding 16 percent of GDP, but staff's latest estimate places it at under 8 percent.

External Sector Assessment. The authorities welcome staff's revised external sector assessment. They view the current exchange rate regime to be suitable for Maldives given the high degree of openness and seasonality of tourism revenues. Past exchange rate devaluations have been unsuccessful (of which the latest is the 2011 experience) as the rapid inflation pass-through offset the impact of the nominal exchange rate devaluation. Continuing to improve the fiscal position is seen as the best way to sustain the exchange rate within its current band. The authorities particularly appreciate the additional background work prepared by staff to better understand the functioning of the foreign exchange market and revise balance of payments estimates, consistent with the authorities' previous requests. For their part, the authorities have begun to collect more regular information on the operations of exchange bureaus.

Monetary and Financial Policies. The Maldives Monetary Authority (MMA) remains committed to its objectives of maintaining price stability and an adequate level of international reserves, while promoting non-inflationary economic growth. Although monetary aggregates have been growing rapidly as the MMA accumulates reserves, private sector credit growth has remained subdued as banks are cautious in extending new credit. The authorities consider the reduction of the minimum reserve requirement necessary given its unusually high level[3] and the handling of the government's overdraft the best way to facilitate achievement of the targets under the Fiscal Sustainability Law. The policy stance was eased in 2014 in response to macroeconomic conditions, including very low inflation. The MMA stopped monetizing the deficit since April 2014, and monetary policy decisions have not been influenced by government finance considerations. The MMA continues to absorb liquidity through its overdraft facility while it has only temporarily stopped conducting Open Market Operations. Steps are being considered to deepen and develop the Treasury bill market and to introduce longer term instruments. Financial soundness indicators continue to improve as the strengthening of loan portfolios reflects a revival in the tourism and construction sectors.

Medium term prospects. The authorities are optimistic that medium-term growth will pick up following the development of the new airport, implementation of current plans to improve infrastructure, and investments in the Special Economic Zones. Diversifying the economy beyond tourism and creating employment opportunities is a high priority. These plans are intended to boost growth potential and will help build buffers against external shocks. The authorities are well aware of the external vulnerabilities faced by all small open tourist-dependent states. The risks outlined in the Matrix are plausible but appear to be over-stated. The tourism sector has out-performed other peers and Maldives has a broad spectrum of source countries and still substantial unmet demand by international visitors.

In closing, we welcome the shift to a more positive staff assessment, which reflects important policy achievements, favorable economic developments, and data revisions as recommended

[3] Effective from 20th February 2014, the Minimum Reserve Requirement was reduced from 25 percent to 20 percent of the average local and foreign currency deposits, excluding interbank liabilities and L/C margin deposits.

by the Fund. We look forward to continued close engagement with the Fund as the authorities tackle remaining challenges.

Table 1. Maldives--Staff's Data Revisions Since the Last Article IV Report
(in Percent, Million Rufiya, Million $, or Percent of GDP as indicated)

	2008	2009	2010	2011	2012	2013 Est.	2014 Est.	2015 Proj.
Real GDP growth - Jan 2013	12.2	-3.6	7.1	7.0	3.5	3.8	4.0	4.1
Real GDP growth - Jan 2015	12.2	-3.6	7.1	6.5	1.3	4.7	5.0	5.0
Old GDP (million of Rufiya)- 2013	24,213	25,403	27,316	31,447	34,012	36,774	40,640	44,560
New GDP (million of Rufiya)- 2015	27,108	27,729	29,855	35,931	38,943	41,569	43,971	46,863
CG Fiscal deficit in Rufiya mn-2013	-2719	-5219	-4275	-3547	-4555	-5994	-5194	-5547
CG Fiscal deficit in Rufiya mn-2015	-2719	-5219	-4275	-2360	-2972	-3253	-5111	-3803
CG Deficit as % GDP - Jan 2011	17.1	-29.0	-17.9	-21.3	-18.8			
CG Deficit as % GDP - Jan 2013	-11.2	-20.5	-15.7	-11.3	-13.4	-16.3	-12.8	-12.4
CG Deficit as % GDP - Jan 2015	-10.0	-18.8	-14.3	-6.6	-7.6	-7.8	-11.6	-8.1
Primary balance as %GDP-Jan 2013	-10.1	-18.1	-13.2	-9.0	-10.7	-12.4	-9.0	-8.7
Primary balance as %GDP-Jan 2015	-9.0	-16.6	-12.1	-4.5	-4.8	-5.3	-8.7	-4.6
BoP Current account-in $ mn -Jan 2013	-612	-221	-197	-437	-585	-646	-700	-743
BoP Current account-in $ mn -Jan 2015	-610	-226	-190	-423	-270	-176	-241	-152
Current account as % of GDP -Jan 2013	-32.4	-11.1	-9.2	-20.5	-26.5	-27	-26.5	-25.7
Current account as % of GDP-Jan 2015	-28.8	-10.4	-8.1	-18.11	-10.6	-6.5	-8.4	-5.0
GDP $ - Jan 2013	1892	1985	2134	2132	2209	2388	2639	2893
GDP $ - Jan 2015	2118	2166	2332	2332	2534	2699	2855	3043
Total domestic public debt-Ruf mn-2013	5,036	7,972	10,175	12,220	14,218	15,590	17,899	20,268
Total domestic public debt --2015	5,036	7,833	9,666	10,754	12,919	14,746	19,370	22,443
External PPG debt ($mn) 2013	472	555	630	703	866	1,064	1,252	1,462
External PPG debt ($mn) 2015	456	538	630	689	722	744	790	841
Private external debt $ mn - 2013	516	501	600	800	1,023	1,271	1,562	1,867
Private external Debt $ mn - 2015	616	517	426	304	148	124	189	189
Public+external private debt $ mn 2013	1,381	1,679	2,025	2,363	2,812	3,347	3,977	4,645
% of GDP	73.0	84.6	94.9	110.8	127.3	140.2	150.7	160.5
Public+external private debt $ mn 2015	1,466	1,667	1,812	1,691	1,709	1,826	2,238	2,487
% of GDP	69.2	76.9	77.7	72.5	67.4	67.7	78.4	81.7