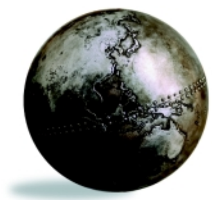

# Maldives

*The Maldives continued its strong economic growth in 1999, mainly because of favorable developments in the tourism and fisheries sectors. To continue sustainable economic growth, the country will need to expedite structural reforms, including fiscal consolidation and human resource development.*

## RECENT TRENDS AND PROSPECTS

During 1996-1998, the Maldives' economy grew by 8-9 percent. This strong performance resulted from favorable developments in transportation, communications, utilities, tourism, fisheries, and manufacturing, particularly garments. For 1999, growth was an estimated 8.5 percent, with tourist arrivals increasing about 10 percent to more than 400,000. Increased growth in tourism continued to facilitate the expansion of construction, the growth of transportation subsectors, and the development of basic infrastructure facilities. Although the fisheries sector remained buoyant, fish export earnings declined because of a fall in fish prices in the international market. Because fish is the principal food item in the Maldives, the increase in fish production favorably affected inflation, with the annual average inflation rate estimated at about 3 percent in 1999.

The fiscal deficit worsened slightly in 1999 to 6 percent of GDP, in contrast to 5.3 percent of GDP the previous year. The deteriorating fiscal position partly resulted from higher expenditures on wages of public sector employees, which increased about 30 percent on average.

The unemployment rate is low in the Maldives. Estimates suggest that more than 20 percent of the labor force are expatriates and this share is growing. Rapid economic development and the reluctance of Maldivians to work in unskilled occupations have resulted in increased recruiting of expatriate workers to fill these vacancies. Simultaneously, there is a shortage of high-skilled and professional labor. These positions are also being filled by overseas recruitment.

In the external sector, the current account deficit deteriorated further to 10 percent of GDP, compared with about 7 percent in 1998. This was primarily due to increased imports associated with tourism sector investments. The current account deficit, however, was more than offset by private capital inflows, which increased the official reserves to the equivalent of more than four months of imports. External debt as a percent of GDP reached 51.5 percent in 1998 and increased slightly to 52 percent in 1999. The debt-service ratio remained below 4 percent for the past five years except in 1997, when it increased to 7.2 percent because a $15 million loan from the Kuwait Fund for balance-of-payment support was repaid fully. This low level of debt service was possible because most of the debt consisted of concessional foreign assistance.

While the country remains potentially vulnerable to economic shocks because of its dependence on tourism and fishing, the economic outlook for the medium term remains promising. Growth should be around 7 percent in 2000, mainly strengthened by a continued increase in tourist arrivals. Inflation is expected to average about 3 percent in 2000 and beyond, because of a prudent macroeconomic policy stance and favorable external conditions. The current account deficit is expected to fall slightly to 6 percent of GDP in 2000 and 2001 because of strong growth in the tourism and fisheries sectors.

## ISSUES IN ECONOMIC MANAGEMENT

Deterioration of the fiscal balance in 1999, coupled with the declining trend in concessional external assistance such as grants, highlights the need to strengthen the government's narrow revenue base. On average, nontax revenue consists of more than half of total revenue, and combined tax receipts from tourism and import duties amounted to 60 percent of tax revenue during 1995-1998. In this regard, tax reform is needed to broaden the tax base and enhance public sector efficiency. The government is preparing to introduce a business profit tax and a property rental value tax to broaden the current tax base, and intends to upgrade the institutional capacity and valuation system of the customs service to improve import duty collections.

The administrative capacity of the government in key agencies also needs improvement. This includes enhancing public sector management, introducing legal and judicial reforms, and restructuring state-owned enterprises. Furthermore, financial sector development is needed to enhance economic efficiency, including promoting competition in the banking sector, increasing the availability of long-term finance, developing capital markets, and strengthening the Maldives Monetary Authority.

## POLICY AND DEVELOPMENT ISSUES

Human resource development (HRD) is a high priority, with two distinct goals: to sustain higher economic growth and to address regional disparities between the outer islands and the main urban centers. The dearth of sufficiently skilled workers is a serious obstacle to achieving national development objectives, and continued efforts in HRD will be required to reduce the dependence on expatriate labor and save foreign exchange. Institutional development of the education sector is important to further enhance HRD. An important government strategy is to pool resources; unify the management function; and improve the range, quality, and comprehensiveness of the courses offered at training institutes. This initiative also provides for staff training and institutional development. The HRD strategy should further target quality improvement through curriculum development, expansion of secondary education and distance learning, and skill development through vocational training.

With regard to regional disparities, government estimates indicate that 22 percent of the country's population has a daily income of less than Rf10 ($0.84), and most of them reside in the outer islands. Regional development, including basic social and physical infrastructure and institution-building in the outer islands, is essential for medium- to long-term HRD.

Greater emphasis on HRD, particularly education, is necessary to improve skills in the labor force that are required to help the private sector to become an engine of economic development. To sustain a higher rate of economic growth, these efforts must be complemented by capacity building of government agencies, financial sector reform, and legal and judicial reform.