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## Maldives: Enhancing Debt Sustainability

### Project Name

Enhancing Debt Sustainability

### Project Number

55263-001

### Country / Economy

- Maldives

### Project Status

Active

### Project Type / Modality of Assistance

- Technical Assistance

### Source of Funding / Amount

TA 6835-MLD: Enhancing Debt Sustainability

#### Source

#### Amount

Technical Assistance Special Fund US\$ 1.20 million

### Operational Priorities

- OP2: Accelerating progress in gender equality
- OP6: Strengthening governance and institutional capacity

### Sector / Subsector

- **Public sector management** / Public administration - Public expenditure and fiscal management

### Gender

Some gender elements

### Description

The knowledge and support technical assistance (TA) will support public debt sustainability in Maldives by focusing on institutional strengthening for sound fiscal policy framework, particularly domestic resource mobilization and public investment management. The TA is included in the country operations business plan, 2021-2023 for Maldives.

### Project Rationale and Linkage to Country/Regional Strategy

Coronavirus disease (COVID-19) has severely affected the economy. Gross domestic product (GDP) is estimated to have contracted by 33.6% in 2020 as travel and tourism, and construction activities got severely disrupted by restrictions imposed to contain the pandemic. Tourist arrivals hit an all-time low in 2020, collapsing by 67%. Poverty is estimated to have increased to 7.2% in 2020 from 2.1% before the pandemic. With travel and tourism activities and related services such as communication, real estate, and entertainment contributing over 40% of GDP, 80% of

exports and about 50% of total revenues, Maldives' economy is vulnerable to natural as well as global economic and health shocks.

The unprecedented pressure on public expenditure, especially to boost healthcare spending and social protection, amidst low revenue mobilization has heightened fiscal stress. Revenue mobilization contracted by 38.7% in 2020 while expenditure increased by 5.7%, resulting in fiscal deficit of 27.5% of GDP in 2020, up from just 6.6% of GDP in 2019. In 2020, public expenditure net lending, and total revenue including grants were 52.8% and 25.4%, respectively, of GDP. The government intends to scale up public sector investment programs (PSIPs) in 2021 and expects substantial increase in non-tax revenue, lowering fiscal deficit to 18.5% of GDP. Almost half of the investment required for PSIPs is financed by borrowing, often non-concessional external borrowing that potentially adds to external debt distress. Proper sequencing and prioritization of such projects are essential to ensure that well vetted investment project pipeline is consistent with fiscal and debt carrying capacities. In recent years, fiscal deficit and public debt have consistently overshoot 3.5% of GDP and 60% of GDP thresholds, respectively, specified in Fiscal Responsibility Act.

Challenging macroeconomic fundamentals narrow economic and taxpayer base, weak public financial management (PFM), high fiscal and current account deficits, and vulnerability to external and climatic shocks complicate debt distress vulnerabilities. The country was at a high risk of debt distress even before the pandemic. In its April 2020 Debt Sustainability Assessment, the International Monetary Fund (IMF) assessed Maldives' public debt as sustainable contingent on implementation of substantial fiscal consolidation strategies as promised in the recent budget and macroeconomic policy frameworks. However, the country remains at high risk of external debt distress and a high overall risk of debt distress. The country's debt carrying capacity is assessed to be weak by IMF. Maldives participated in the G-20 Debt Service Suspension Initiative. Public and publicly guaranteed (PPG) debt was estimated at 149.3% of GDP as of yearend 2020, a sharp increase from 78.3% of GDP at yearend 2019. The government estimated a total outstanding PPG debt to reach 124.1% of GDP in 2021.

A faster growth of public expenditure relative to revenue growth together with high cost of borrowing pose a binding constraint to a stable macrofiscal framework and debt sustainability. High public expenditure is partly due to the inclusion of mega infrastructure projects as well as other ad hoc projects sans cost benefit analysis and proper due diligence, implying weak public investment management process. Sequencing, screening, and prioritization of PSIPs are important to ensure that capital spending surge is consistent with available fiscal space and high debt distress situation. Meanwhile, higher revenue mobilization is constrained by weak taxpayer compliance and audit capacities of the authorities. Non-compliance in the case of goods and services tax was as high as 32% in 2019. Tax revenue stagnated at around 19% of GDP before the pandemic but is projected to decline to 16.5% of GDP in 2021. The 2020 Public Expenditure and Financial Accountability (PEFA) assessment shows that the country has scored low (C+ and below) in public investment management, fiscal risk reporting, fiscal strategy, medium-term perspective in expenditure budgeting, revenue administration and accounting, and internal and external audit.

The TA is aligned to the government's priority to lower debt distress and improve fiscal management to support implementation of Strategic Action Plan 2019-2023. The TA support aligns with the country partnership strategy's objective of enhancing public sector efficiency and fiscal sustainability, is included in country operations

business plan 2021-2023, and is consistent with Medium-term Fiscal Strategy 2021-2023 and the upcoming PFM Reform Strategy 2021-2025. It prioritizes capacity building on areas where Maldives' PEFA 2020 score is C+ and below and will support adherence to International Development Association's Sustainable Development Finance Policy. The proposed TA activities are designed in close coordination with development partners.

## Impact

Debt vulnerabilities and overall debt reduced

## **Project Outcome**

### Description of Outcome

Fiscal policy framework improved

### Progress Toward Outcome

Ongoing implementation.

## **Implementation Progress**

### Description of Project Outputs

Domestic resource mobilization and revenue administration policies and strategies strengthened

Public investment and expenditure management policies and strategies strengthened

Identification and implementation of the SDFP PPAs supported

### Status of Implementation Progress (Outputs, Activities, and Issues)

Output 1: Ongoing

Output 2: Ongoing

Output 3: Ongoing

### Geographical Location

Nation-wide

## **Summary of Environmental and Social Aspects**

### Environmental Aspects

Involuntary Resettlement

Indigenous Peoples

## **Stakeholder Communication, Participation, and Consultation**

During Project Design

During Project Implementation

## **Business Opportunities**

Consulting Services

ADB will engage the consultants and carry out procurement following the ADB Procurement Policy (2017, as amended from time to time) and its associated project administration instructions and/or staff instructions

Procurement

Request for quotation on computers, software, and other small office equipment to be procured by ADB.

## **Contact**

Responsible ADB Officer

Seyama, So

Responsible ADB Department

Sectors Group

Responsible ADB Division

Public Sector Management and Governance Sector Office (SG-PSMG)

Executing Agencies

*Ministry of Finance (formerly Ministry of Finance and Treasury)*

## **Timetable**

Concept Clearance

20 Oct 2021

Fact Finding

15 Nov 2021 to 16 Nov 2021

MRM

-

Approval

22 Nov 2021

Last Review Mission

-

Last PDS Update

14 Dec 2022

## **Funding**

**TA 6835-MLD**

Milestones

| Approval    | Signing Date | Effectivity Date | Closing     |             |        |
|-------------|--------------|------------------|-------------|-------------|--------|
|             |              |                  | Original    | Revised     | Actual |
| 22 Nov 2021 | 14 Dec 2021  | 14 Dec 2021      | 30 Nov 2024 | 30 Nov 2026 | -      |

Financing Plan/TA Utilization

| ADB          | Cofinancing | Counterpart |               |                 |        | Total        |
|--------------|-------------|-------------|---------------|-----------------|--------|--------------|
|              |             | Gov         | Beneficiaries | Project Sponsor | Others |              |
| 1,200,000.00 | 0.00        | 0.00        | 0.00          | 0.00            | 0.00   | 1,200,000.00 |

Cumulative Disbursements

| Date        | Amount     |
|-------------|------------|
| 18 Jul 2024 | 605,153.00 |

Project Page <https://www.adb.org/projects/55263-001/main>

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