

INTERNATIONAL MONETARY FUND ASSESSMENT LETTER

SAMOA—ASSESSMENT LETTER FOR THE ASIAN DEVELOPMENT BANK

September 14, 2011

Recent Developments and Outlook

1. **The Samoan economy is recovering steadily from the devastating 2009 tsunami and the global financial crisis.** Following declines of 5 percent in 2008/09 (July/June) and 0.2 percent in 2009/10, real GDP is expected to have grown by about 2 percent in 2010/11. Despite the completion of major reconstruction work, the effects of the tsunami and the crisis are still lingering, as reflected in a moderate recovery of tourism and remittances. The phasing out of post-tsunami reconstruction will also take some steam out of economic activity. We project GDP growth at 2–2½ percent over the next couple of years before returning to the medium-term trend of 2½–3 percent.

2. **Inflation remains at a moderate level and there is little upward pressure at present.** During the last price surge in 2008/09, annual average inflation reached 14.4 percent, but with the retreat of world food and fuel prices and slow economic activity, the CPI fell marginally in 2009/10 and increased by about 3 percent in 2010/11. Inflation is projected to be 3 percent over the current fiscal year.

3. **The fiscal deficit fell significantly in 2010/11 after a sharp increase in the previous year as a result of post-tsunami reconstruction.** The government is targeting an overall deficit below 5 percent of GDP for 2011/12 and 3 percent of GDP over the medium term. The deficit has been predominantly financed with external concessional resources and is likely to remain so for a foreseeable future. The external current account deficit is likely to remain elevated due to a lagging recovery in tourism and remittances, but continued strong donor support (grants and loans) will likely keep foreign reserves at a comfortable level equivalent to about 5 months of imports. The Tala exchange rate has been stable in both real and nominal effective terms.

4. **The main risk to the outlook is a sharper-than-anticipated slowdown of the global economy.** Although Australia and New Zealand, Samoa's key trading partners, are expected to grow strongly in 2012, the slowing US economy will be a drag on growth as remittances and trade (including tourism) will be adversely affected. Samoa is currently affected by drought conditions which may affect the recovery of the agricultural sector.

Issues and Challenges

5. **Medium-term fiscal consolidation is essential to ensure debt sustainability.** The fiscal response to the economic downturn and the need for reconstruction has exhausted much of the country's fiscal space, with public debt expected to reach almost 60 percent of GDP (in nominal

value) this fiscal year, compared to just 30 percent in 2007/08. The government is committed to reducing the fiscal deficit to 3 percent of GDP and bringing debt down to 40 percent of GDP (in present value terms) over the medium term, a goal that strikes the right balance between the need to support short-term economic activity and to ensure medium-term debt sustainability. To achieve this goal, the government will need to maintain its revenue effort and to reprioritize its expenditure should revenue fall short of expectations. A number of reforms are under way to strengthen the revenue base and compliance, including through a review of tax concessions, an upgrade of the information technology, and a community education program. Continued donor support in grants or highly concessional terms will be important for achieving the medium-term fiscal targets.

6. Prudent fiscal policy to achieve these targets is essential to maintain the favorable debt outlook, as is adherence to the current debt management strategy. The current trajectory of public debt is broadly in line with the projections of the last joint IMF/World Bank debt sustainability analysis (DSA). That DSA suggested that even after taking into account the large deficits envisaged during the post-tsunami reconstruction, the debt outlook remains favorable. However, economic recovery has since been slower than anticipated, and the downside risks to the global economy have increased for the near term.

7. The Central Bank of Samoa (CBS) is committed to keeping inflation at the moderate level while supporting short-term economic activity. With little anticipated demand pressure and to support economic activity, CBS has substantially reduced the policy rate to lower lending rates. However, credit growth has been weak due to a lack of demand. Nevertheless, CBS should not hesitate to tighten the policy stance if the outlook for inflation worsens. CBS should also make use of the exchange rate flexibility (a ± 2 percent band around the basket peg) afforded by the current arrangements to absorb external shocks and manage aggregate demand.

8. Considerable progress has been made in structural reforms, but continued efforts will be needed to sustain the momentum. The privatization of Samoa Tel (the sole telecom company for landline services) early this year and the establishment of the Independent Selection Committee for state-owned enterprise board directors were major steps in SOE reform. A Customary Land Advisory Commission has been set up to guide and promote the productive use of customary land. Meanwhile, public financial management reforms have entered the second phase, which will be aimed at strengthening fiscal discipline and improving performance monitoring linked to the three-year rolling medium-term expenditure framework. Continued reforms in these and other key areas, if sustained, would help create a more enabling environment for private-sector-led growth.

IMF Relations

9. On December 7, 2009, the IMF approved Samoa's request for disbursement of SDR 5.8 million (50 percent of quota) under the Rapid Access Component of the Fund's Exogenous Shocks Facility to assist the country in responding to the balance of payment impact of the

tsunami. The fund was subsequently disbursed. The IMF's last Article IV consultation with Samoa was concluded on May 7, 2010 and the next consultation is expected to take place in March 2012. A staff team visited Samoa during April 5-11, 2011.

Samoa: Selected Economic and Financial Indicators, 2004/05–2011/12 ^{1/}

Population (2008): 0.18 million
 Main Exports: Tourism, Fish
 GDP per capita (2009/10): US\$ 2,889
 Quota: SDR 11.6 million

	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11 Est.	Proj. 2011/12
(12-month percent change)								
Output and inflation								
Real GDP growth	7.0	2.1	2.3	4.9	-5.1	-0.2	2.0	2.1
Nominal GDP	11.2	8.6	9.4	10.1	-2.4	1.6	5.1	5.1
Change in CPI (end period)	1.0	2.2	8.5	8.2	10.0	-0.3	2.9	3.0
Change in CPI (period average)	7.8	3.2	4.8	6.2	14.3	-0.2	2.9	3.0
(In percent of GDP)								
Central government budget								
Revenue and grants	36.3	31.8	36.4	30.9	34.3	39.7	35.7	35.1
Of which: grants	11.2	5.9	7.4	5.2	7.7	15.3	8.1	7.9
Expenditure and net lending	36.1	32.3	35.8	32.8	38.4	50.9	44.0	40.1
Of which: Development	13.1	7.1	9.3	6.5	12.7	17.6	16.4	12.9
Overall balance	0.3	-0.5	0.6	-1.8	-4.1	-11.3	-8.2	-5.1
External financing	1.4	0.5	-1.1	0.8	3.1	12.0	8.3	5.4
Domestic financing	-1.7	0.0	0.4	1.0	1.0	-0.7	-0.1	-0.3
(12-month percent change)								
Money and credit								
Broad money (M2)	15.0	13.0	8.7	12.3	7.6	11.1
Net foreign assets	34.4	-20.2	7.8	14.4	9.0	46.9
Net domestic assets	-0.7	79.8	-0.5	1.3	6.7	-9.0
Private sector credit	6.8	28.2	11.7	6.5	5.2	5.1
(In millions of U.S. dollars)								
Balance of payments								
Current account balance	-39.1	-46.5	-83.2	-32.6	-16.1	-42.9	-70.5	-78.0
(In percent of GDP)	-9.6	-10.2	-15.9	-6.4	-3.1	-7.7	-12.7	-13.3
Merchandise exports, f.o.b.	12.8	11.0	12.2	11.2	10.2	11.0	11.1	10.1
Merchandise imports, c.i.f.	-168.2	-204.6	-241.1	-204.3	-227.6	-236.4	-257.6	-249.6
Services (net)	59.7	73.7	79.3	85.8	92.1	85.3	66.8	64.2
Income (net)	-34.1	-36.2	-37.5	-38.0	-17.2	-21.6	-17.6	-22.7
Current transfers	90.8	109.6	103.9	112.8	126.5	118.7	126.8	120.1
External reserves and debt								
Gross official reserves	84.2	64.4	80.9	87.6	96.6	150.1	155.5	155.4
(In months of next year's imports of GNFS)	3.7	2.4	3.6	3.5	3.7	5.2	5.5	5.2
External debt (in percent of GDP)	39.5	40.1	37.1	30.3	38.1	49.5	54.4	58.2
Public external debt-service ratio (in percent)	9.3	9.8	5.2	3.9	5.0	5.6	5.1	4.8
Exchange rates								
Market rate (tala/U.S. dollar, period average)	2.7	2.8	2.6	2.6	2.8	2.8	2.8	2.8
Market rate (tala/U.S. dollar, end period)	2.8	2.7	2.6	2.9	2.8	2.8	2.8	2.8
Nominal effective exchange rate (2000 = 100) ^{2/}	100.0	98.9	97.3	94.9	97.6	98.1	98.0	98.9
Real effective exchange rate (2000 = 100) ^{2/}	100.0	99.6	101.0	105.5	116.1	111.6	112.4	114.4
<i>Memorandum items:</i>								
Nominal GDP (in millions of tala)	1,124	1,221	1,336	1,470	1,435	1,458	1532	1611
Nominal GDP (in millions of U.S. dollars)	407	455	522	506	522	526	556	586
GDP per capita (U.S. dollars)	2,276	2,537	2,901	2,800	2,876	2,889	3,050	3,194

Sources: Data provided by the Samoan authorities and Fund staff estimates.

1/ Fiscal year beginning July 1.

2/ IMF, Information Notice System (calendar year).