Economic recovery continued in 2022 with border reopening in the second half. Inflation accelerated, and higher global commodity prices drove the current account balance into deficit. Growth is expected to slow in 2023 because of cyclone and earthquake damage to crops and infrastructure, which is seen to keep inflation elevated and the current account in deficit. Facing labor shortages, the new government needs to balance competing demand for skilled workers in tourism at home and for seasonal worker schemes abroad.

**Economic Performance**

**Gradual economic recovery continued in 2022 as growth doubled from 1.0% in 2021 to 2.0%**. Despite domestic transmission of COVID-19 early in the year, international borders reopened in July. Growth was restored in much of the economy but particularly in such tourism-related areas as trade, real estate, and restaurants and accommodation (Figure 2.36.1). Public services rose as spending increased on COVID-19 response and support. Stalled infrastructure projects resumed, boosting construction.

**International borders reopened, but to considerably fewer tourists than before the pandemic.** Visitor arrivals in July 2022 were only 30% of the average in July 2017–2019, and visitors in the second half of 2022 from Australia and New Zealand, the two biggest markets, were about 48% of that baseline (Figure 2.36.2). Cruise ships resumed operations in November, but data on arrivals aboard them are not available.

**Figure 2.36.1  Supply-Side Contributions to Growth**

*Damage to agriculture and infrastructure is expected to lead to slower growth in 2023.*

<table>
<thead>
<tr>
<th>Percentage points</th>
<th>Agriculture</th>
<th>Industry</th>
<th>Other services</th>
<th>Gross domestic product</th>
</tr>
</thead>
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<td>-5.0</td>
<td>1.0</td>
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<tr>
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<td>1.0</td>
<td>2.0</td>
<td>1.0</td>
<td>4.2</td>
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<tr>
<td>2024</td>
<td></td>
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</tr>
</tbody>
</table>

*Forecast*

*Sources:* Vanuatu National Statistics Office; Asian Development Bank estimates.

**Figure 2.36.2  Arrivals by Air from Australia and New Zealand**

*The inflow of tourists in 2022 from the two biggest source markets was below pre-pandemic levels.*

*Sources:* Australian Bureau of Statistics; Statistics New Zealand.
The fiscal deficit returned with higher spending on COVID-19 response and lower nontax revenue. A fiscal surplus equal to 2.7% of GDP in 2021 turned into a 3.3% deficit in 2022 (Figure 2.36.3). Import duties and value-added tax collections rose, reflecting increased consumer demand and higher prices. However, nontax revenue—mainly from honorary citizenship programs (HCPs)—fell by more than a fifth, while grants also declined. Revenue from HCPs has provided about 30% of all revenue in recent years. Along with other problems, HCP revenue continued to decline with the suspension in March 2022 of a European Union visa waiver program. Current expenditure rose, driven by higher spending on goods and services and employee compensation in response to domestic COVID-19 transmission in the first half of 2022. Capital spending also increased as projects stalled due to COVID-19 restrictions resumed.

The current account fell into deficit with higher global commodity prices. Increases in remittances, exports of goods, and tourism receipts were insufficient to offset the rise in imports. Higher global prices pushed fuel import bill up by 150%, while imports of manufactured goods and of machine and transport equipment also rose substantially. Lower HCP revenue helped push the current account from a surplus equal to 0.8% of GDP into a 5% deficit (Figure 2.36.4). Gross international reserves were little changed from 2021, still enough to cover 21 months of imports.

Economic Prospects

Economic growth is forecast to slow to 1.0% in 2023 following multiple disasters. Vanuatu was battered in March 2023 by two category 4 cyclones and by earthquakes that massively damaged agriculture and infrastructure. The damage may be as bad as from Cyclone Pam in 2015, for which estimates ranged as high as 60% of GDP. Economic recovery will partly depend on revival in tourism, but frequent disasters have made that more risky, as the country’s focus frequently shifts to reconstruction. These developments compound the challenges faced by a new government elected in November 2022. That said, continued remittance inflows and the gradual return of tourists in the second half of the year will likely sustain consumer spending. Growth is forecast to accelerate to 4.2% in 2024 (Table 2.36.1), driven by agriculture, trade and tourism services, and reconstruction.

Inflation doubled from 2.3% in 2021 to 4.8% in 2022 on higher global prices. Price increases for food, transportation, housing and utilities, education, and alcoholic drinks and tobacco were the main drivers of inflation. With higher global fuel prices, bus fares soared by 33% in November. Despite inflation exceeding its 1%–4% target, the Reserve Bank of Vanuatu, the central bank, kept its key policy rate at 2.25%, unchanged since March 2020.
Reconstruction and recovery costs are expected to tighten fiscal space further. The latest disasters are expected to lower tax collections and increase expenditure for recovery and reconstruction, widening the fiscal deficit. The 2023 budget, delayed by the early dissolution of Parliament in August 2022, was passed in March and included additional allocations and borrowing for disaster relief and recovery.

Infrastructure rehabilitation and upgrading after Cyclone Pam in 2015 pushed external debt from the equivalent of 14% of GDP in 2014 to 39% in 2020, almost breaching the 40% ceiling (Figure 2.36.5). In January 2023, the International Monetary Fund reconfirmed that Vanuatu’s debt remained sustainable but with limited space to absorb further shocks like disasters.

The need to rebuild damaged facilities and infrastructure will delay recovery in tourism.

Cyclone devastation of agriculture and damage to infrastructure will crimp supply chains, offsetting lower international prices for food and fuel. Rising demand from tourists in 2024 may sustain inflation slightly higher than the long-term average. The current account deficit is expected to expand to the equivalent of 6.7% of GDP in 2023. Higher imports of food and materials for relief and reconstruction are expected to counter increased receipts from tourism, remittances, and grants.

Policy Challenge—Shortage of Skilled Labor

Increase in remittances lent resilience to the economy during the pandemic. Official remittance inflow increased from $50 million in 2015 to $208 million in 2021, or 21.2% of GDP (Figure 2.36.6). These figures do not include cash carried in or money sent through other informal channels. Remittances are sent mainly by Vanuatu nationals employed in seasonal worker schemes in Australia and New Zealand. Since these schemes started, Vanuatu has been the largest sending country, providing 32% of Pacific seasonal workers in 2022. The schemes employed about 14% of Vanuatu’s working-age men and 2% of women. Further, the 11,118 seasonal workers in mid-2022 outnumbered government employees—a rare feat in the Pacific, where the public sector usually dominates.
Demand for seasonal workers is likely to increase with changes introduced by Australia and New Zealand in 2022. When the pandemic forced tourism businesses in Vanuatu to close, many of their staff applied for seasonal worker openings. As tourism businesses reopen, they struggle to find workers with the required skills, hampering tourism industry revival.

Balancing these two growth drivers is expected to be difficult. By halting the issuance of new passports to prospective seasonal workers until July 2023, the government effectively capped the supply of new workers at 6,000, the number provided with passports from November 2022 to January 2023. This aligns with a government review of labor mobility programs to refocus on national needs. Yet frequent disasters in Vanuatu highlight the importance of remittances as a safety net supported by external sources. A longer-term challenge is how to increase labor participation, especially by women. In 2020, only 51% of working age men and 42% of women were in the labor force. Also needed are training and better education to raise the number of skilled workers.

**Figure 2.36.6 Remittance Inflow and Tourism Receipts**

While tourism receipts dried up with COVID-19, remittances remained strong.

GDP = gross domestic product.

Sources: International Monetary Fund; Haver Analytics; Asian Development Bank estimates.