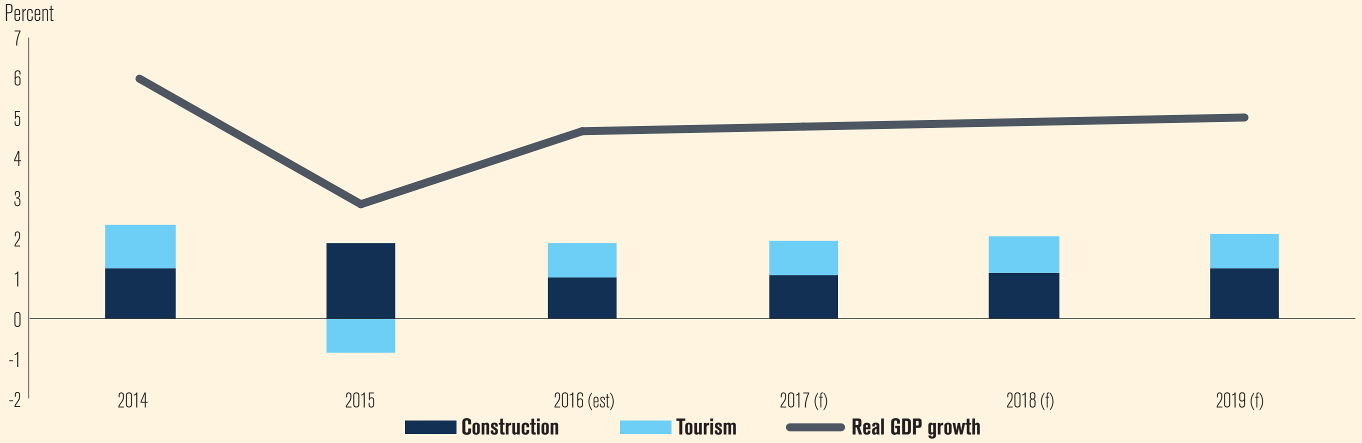
Maldives

The Government started several large infrastructure projects to allow the population to move from small, vulnerable islands to Greater Malé. To make space for these investments, the government is reducing current expenditure. As a result, in the medium term, construction is expected to remain the main driver of growth with large current account deficits financed by investment and infrastructure loans.

	2016
Population, million	0.4
GDP, US$ billion[(a)]	3.6
GDP per capita, current US$[(a)]	8,695

Note: (a) GDP with 2003 base year. It is expected that the Government will release GDP numbers with 2014 base year shortly, which would increase nominal GDP
Source: World Bank WDI.

Contributions to real GDP growth



Source: National Bureau of Statistics, World Bank staff estimates.

Recent developments

Overall GDP growth remained around an estimated 4.7 percent in 2016. Construction for housing and large investment projects has taken over as the main driver of growth since late 2014, while tourism has been slowing down due to an economic slowdown in key countries. Inflation fell further to 0.5 percent in 2016, thanks to continued low global food and fuel prices and a stable exchange rate, as most products are imported.

Foreign reserves dropped in late 2016 due to the settlement of a long-running court case between the state-owned airport and an Indian engineering company in the amount of USD 271 million. Despite a modest recovery in tourism income and fish exports and the continued low global commodity prices, the current account deficit widened sharply from 8.6 percent in 2015 to 23.2 percent of GDP in 2016, driven by the large increase in investment and the one-off impact of the settlement. FDI inflows were not sufficient to cover the current account deficit unlike in previous years. Gross official reserves fell to USD 467 million towards the end of 2016, although usable reserves – after netting out short-term foreign currency liabilities to the banking sector – were only USD 200 million (1.1 months of imports). The exchange rate to the USD remains at 15.4, the low end of the currency band.

The fiscal deficit in 2016 widened to 11.2 percent of GDP, after accounting for unpaid bills. New revenue measures proposed in the budget did not materialize and existing revenue sources underperformed slightly, as tourism was lower than projected. Total expenditure was 44.3 percent of GDP due to the sharp increase in public infrastructure investment around Malé, while electricity subsidy cuts were offset by higher than expected expenditure on health care. Public debt grew from 63.3 to 69.2 percent of GDP in 2016, driven by the wide primary deficit. In 2017 the Government issued a USD 200 million Eurobond.

Despite the highly successful tourism sector, youth unemployment remains high, as the sector attracts many migrant workers. More than a quarter of women are either unemployed or not looking for a job and the share of unemployed among young females is even higher. Almost a quarter of Maldivian youth is not in employment, education, or training (NEET). The NEET rate is particularly high for the female youth because of inactivity mostly due to family reasons, while the driver for the high male NEET rate is (involuntary) unemployment. Moreover, the employment share of Maldivians in construction, the other main driver of growth, is relatively low as this sector employs mainly migrant workers as well.

Outlook

Maldives is expected to continue to expand the number of resorts, attracting substantial FDI inflows of around 9 percent of GDP a year. Construction is expected to remain a key growth driver, while tourism sector growth is likely to recover slowly.

As food subsidies are being gradually phased out in 2017, inflation is expected to spike due to a direct impact and knock-on effects on other food items. The Government has put in place a targeted cash transfer program to protect vulnerable households from its impact. This program will be revised in the coming months as the take-up of the cash transfers has been limited so far.

The current account deficit is likely to become narrower gradually but to remain well above 10 percent of GDP, financed by FDI, external loans and one-off income sources. Usable reserves are expected to gradually increase, assuming a recovery of exports and further income from leasing out new lagoons and islands for development.

The World Bank projects a fiscal deficit of 9.4 percent of GDP for 2017, gradually narrowing until 2020, reflecting high capital expenditure of around 15 percent of GDP on average and decreasing current expenditure relative to GDP. The level of public debt is expected to increase but taper off towards 2020, as the large investment projects will have been completed. Despite mostly concessional external debt and domestic debt issued at low, fixed rates, and relatively high revenue collection, the risk of external debt distress is high, reflecting the refinancing risk from the Eurobond with a low level of reserves and fiscal risks through guarantees, while the vulnerability of the overall debt portfolio remains elevated, due to its short maturity.

Risks and challenges

The main macroeconomic risks are shocks to tourism, a faster than expected recovery of global commodity prices, fiscal slippages, especially delays to controlling current expenditure, and the realization of contingent liabilities through guarantees.

The immediate challenge is to improve fiscal sustainability and budget credibility. It is important to contain current expenditure while implementing the large and necessary infrastructure program. The following measures are crucial: seeking efficiency improvements in the health system, updating and strengthening its targeted social protection system replacing the food and electricity subsidies, avoiding large hikes in wages and pensions, and improving investment project selection, maintenance budgeting and implementation to increase the value-for-money of public investment. These measures would also make the budget more flexible and reduce the exposure to global commodity price shocks. Maldives needs to preserve its tax base and avoid relying on unrealistic revenue sources in the budget. To preserve debt sustainability and reduce fiscal risks, it is important to increase the maturity of domestic debt, seek the most concessional terms from external lenders and issue guarantees prudently.

While construction and resort tourism are expected to drive growth in the medium term, these sectors do not create sufficient jobs for Maldivians. The consolidation of population from vulnerable islands and atolls to larger islands in Greater Malé, while also reducing pressure on Malé is a country priority. If successful, it may eventually allow for new forms of economic activity in line with the aspirations of Maldivian youth and provide employment, improve the quality of public services such as health and education, and make the country more resilient to climate change.

	2014	2015	2016 (est)	2017 (f)	2018 (f)	2019 (f)
Real GDP growth, at constant market prices	6.0	2.8	4.7	4.8	4.9	5.0
Real GDP growth, at constant factor prices	5.5	3.8	4.7	4.8	4.9	5.0
Agriculture	0.2	-0.5	2.6	2.6	2.6	2.7
Industry	12.9	18.3	8.5	8.7	8.9	9.1
Services	4.6	1.6	4.1	4.1	4.2	4.2
Inflation (CPI)	2.1	1.0	0.5	2.4	2.8	3.0
Current Account Balance (percent of GDP)	-3.8	-8.6	-23.2	-21.1	-15.3	-13.8
Net Foreign Direct Investment (percent of GDP)	10.8	9.0	12.4	9.5	9.0	8.6
Fiscal Balance (percent of GDP)	-8.2	-8.5	-11.2	-9.4	-7.3	-6.4
Debt (percent of GDP)[a]	65.9	63.4	69.2	74.0	75.9	76.6
Primary Balance (percent of GDP)	-4.6	-5.9	-9.0	-6.9	-4.8	-3.9

Note: GDP with 2003 base year. It is expected that the Government will release GDP numbers with 2014 base year shortly, which would increase nominal GDP
(a) Excluding outstanding guarantees and arrears
Source: Ministry of Finance and Treasury, National Bureau of Statistics, Maldives Monetary Authority, World Bank staff estimates