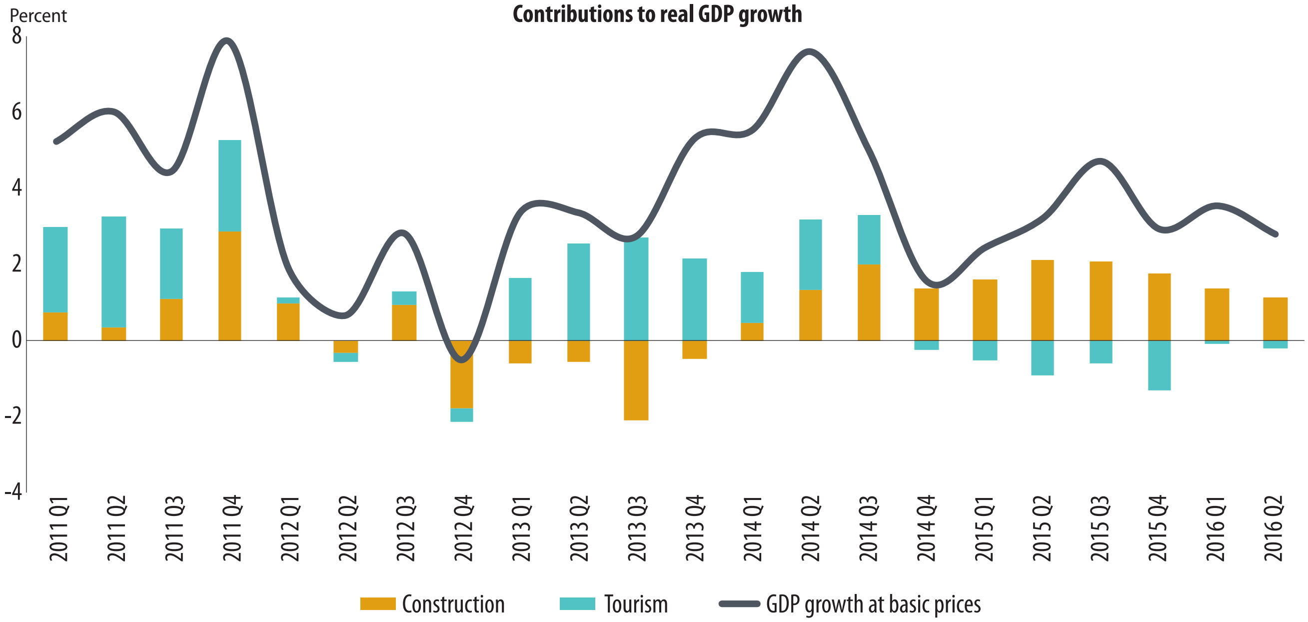
Maldives

The Government started a number of large infrastructure projects to allow the population to move from small, vulnerable islands to Greater Malé, one of the reasons why construction has overtaken tourism as the main driver of growth. To make space for these investments, the government is implementing a reduction in current expenditure. 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, current US$ billion	3.6
GDP per capita, current US$	8,620

Sources: World Bank WDI

Contributions to real GDP growth



Sources: Ministry of Finance and Treasury, and World Bank staff calculations

Recent developments

Overall GDP growth rebounded to an estimated 4.1 percent in 2016, compared to 2.8 percent in 2015.[3] 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.

The fiscal deficit in 2016 has widened slightly to an estimated 8.6 percent of GDP. Revenue and grants are estimated to have declined slightly to 32.2 percent of GDP. The expenditure side reflects a significant policy shift of around 4 percent of GDP away from recurrent expenditure, by abolishing electricity subsidies effectively, to capital expenditure into primarily population centers around Greater Malé and into the expansion of the main airport. Public debt grew from 63.4 to an estimated 69.5 percent of GDP. Thanks to concessional external debt and domestic debt issued at low, fixed

3 World Bank staff estimates. Official final estimates GDP have not yet been released.

rates, and relatively high revenue collection, the cost of debt service is low at 17 percent of revenue. In a sign of increased transparency, the Ministry of Finance and Treasury started to publish monthly fiscal outcomes on its website.

A long-running court case between the airport SOE and an Indian engineering company was settled for USD 271 million in November 2016, partly through selling a bond to the central bank, which used a USD 100 million 6-month currency swap with the Reserve Bank of India to replenish reserves. The current account deficit has widened sharply from 9.5 percent in 2015 to 25.7 percent of GDP in 2016, on the back of reduced tourist services income, further declines in fish exports and increased imports of construction materials, and the one-off impact of the settlement on the current account, while commodity imports fell thanks to low global prices. FDI inflows were not sufficient to cover the current account deficit unlike previous years. Gross official reserves fell to USD 467 million at end-2016, although usable reserves[4] were only USD 200 million (1.2 months of imports). The exchange rate to the USD remains at 15.4, the low end of the currency band.

Outlook

Maldives is expected to continue to expand the number of resorts, attracting substantial FDI inflows of around 9-10 percent of GDP a year. Construction is also likely to remain a key growth driver, while the tourism sector growth is likely to remain below previous growth rates, reflecting lower growth expectations in key countries, despite an expected recovery in Russia.

As food subsidies are being gradually phased out in 2017, inflation is expected to spike due to the direct impact and knock-on effect on other food items. The Government has put in place a targeted cash transfer program to protect vulnerable households from the impact, even if take-up of the cash transfer has been limited so far.

The Government has projected a budget deficit for 2017 of 1 percent of GDP. While acknowledging the effort to phase out food subsidies, it may be difficult to meet the deficit target unless new revenue measures and further expenditure savings are realized, and the World Bank projects a fiscal deficit of 6.1 percent of GDP instead, which would still be the lowest deficit since 2007. Efficiency gains in the universal health system could make the budget more flexible and subsidies reduction make it less exposed to global commodity price shocks. However, the level of public debt is expected to remain elevated as long as the investment boom continues.

The current account deficit is likely to remain around 20 percent of GDP, financed by FDI, external loans, an expected Eurobond issuance and one-off income sources. Usable reserves are expected to remain low, as the currency swap and other foreign loans will be due for repayment.

Risks and challenges

It is important that Maldives preserves its tax base and efficient tax system, as it prepares to develop Special Economic Zones offering tax concessions. On the expenditure side, the World Bank encourages the Government to continue to seek efficiency improvements in the health system, while updating and strengthening its targeted social protection system to avoid a return of food and electricity subsidies once commodity prices rise again. Improved project selection, planning and budgeting for construction, maintenance and operations could increase the value-for-money for public investment. A Sovereign Development Fund set up to receive the newly introduced Airport Development Charge and dividends from the airport SOE will ring-fence funds to repay the loans to finance the airport expansion.

The level of reserves at the central bank is structurally low, but large economic actors are typically able to supply dollars to the market to keep the parallel market premium low.

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.

4 After netting out short-term foreign currency liabilities to the banking sector.

TABLE: Maldives macro outlook indicators (annual percent change unless indicated otherwise)

	2014	2015	2016 (est)	2017 (f)	2018 (f)	2019 (f)
Real GDP growth, at constant market prices	6	2.8	4.1	4.5	4.6	4.6
Private Consumption	..	..	..	..	..	..
Government Consumption	..	..	..	..	..	..
Gross Fixed Capital Investment	..	..	..	..	..	..
Exports, Goods and Services	..	..	..	..	..	..
Imports, Goods and Services	..	..	..	..	..	..
Real GDP growth, at constant factor prices	6	2.8	4.1	4.5	4.6	4.6
Agriculture	0.2	-0.5	1.9	2.3	2.5	2.4
Industry	12.9	18.3	6.6	6.7	6.8	6.9
Services	4.6	1.6	3.3	3.8	4	3.9
Inflation (Consumer Price Index)	2.1	1	0.5	2.4	2.8	3
Current Account Balance (percent of GDP)	-3.8	-9.5	-25.7	-21.9	-21	-19.4
Net Foreign Direct Investment (percent of GDP)	10.8	8.7	10.7	10.4	9.9	9.4
Fiscal Balance (percent of GDP)	-8.2	-8.2	-8.6	-6.1	..	..
Debt (percent of GDP)	65.9	63.4	69.5	71.2	..	..
Primary Balance (percent of GDP)	-4.6	-5.6	-5.6	-2.7	..	..

Sources: World Bank, Macroeconomics and Fiscal Management Global Practice.
Notes: est = estimate, f = forecast