Kiribati: 2011 Article IV Consultation—Staff Report, Informational Annexes, Debt Sustainability Analysis, Public Information Notice on the Executive Board Discussion, and Statement by the Executive Director for Kiribati

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the Article IV consultation with Kiribati, the following documents have been released and are included in this package:

- The staff report, Informational Annexes, and Debt Sustainability Analysis for the 2011 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on February 22, 2011, with the officials of Kiribati on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 18, 2011. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its May 2, 2011 discussion of the staff report that concluded the Article IV consultation.
- A statement by the Executive Director for Kiribati.

The document(s) listed below have been or will be separately released.

Statistical Appendix.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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KIRIBATI

STAFF REPORT FOR THE 2011 ARTICLE IV CONSULTATION

April 18, 2011

KEY ISSUES:

Context and growth prospects. The economy has emerged from the 2008–09 recession with strong forward momentum. Key externally financed infrastructure projects are expected to spur growth over the next few years. The main challenge is to manage the investment boom that is underway without creating inflationary pressures. Downside risks are mainly external and relate to higher inflation pressures from a further escalation of international fuel and food prices and a stalled global recovery that would hit Kiribati's remittances and wealth funds. These are balanced by the potentially faster rebound in domestic demand driven by large public investments in the pipeline.

Impact of food and fuel prices. Further increases would pose a challenge for Kiribati, but there are some mitigating factors compared to the 2008 spike. The price of rice (the main food import) is still well below the 2008 peak. The strong appreciation of the Australian dollar has helped mitigate imported inflation pressures.

Achieving a sustainable growth path. Productivity gains from infrastructure investments will prove transitory if progress in fiscal and structural reforms lags behind. On the fiscal side, preserving the Revenue Equalization Reserve Fund (RERF) is key to ensure fiscal sustainability and intergenerational fairness through fiscal consolidation once key public projects in the pipeline are completed. Over the medium term, to better anchor fiscal plans, the government should aim to stabilize the real value of the RERF in per capita terms. To shift to a high growth path hinging on a vibrant private sector, the implementation of the structural reform agenda should be accelerated.

Safeguarding financial stability. Enhancing competition in the banking sector is crucial to boost private activity. The authorities' plans to revitalize the Development Bank of Kiribati (DBK) in the medium term are welcome.

Enhancing external competitiveness and stability. Securing grant financing and containing fiscal deficits are key to ensure external debt sustainability, as the joint IMF-WB Debt Sustainability Analysis (DSA) points out.

Data provision has some shortcomings, but is broadly adequate for surveillance. Significant progress has been made in the timeliness of core macroeconomic data since the 2009 Article IV. GDP and BOP data have been recently revised with Pacific Financial Technical Assistance Centre (PFTAC) assistance, but still suffer from shortcomings. The authorities have requested additional technical assistance in these areas.

Approved By

Kenneth Kang and Thomas Dorsey

Discussions took place in Tarawa from February 15–22, 2011. The staff team comprised Ms. Tumbarello (head), Ms. Maslova, Mr. Yi Xiong (all APD), Mr. Hague (World Bank), and Mr. Tora (AsDB). Ms. Tira (OED) participated in the discussions.

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INTRODUCTION

- Kiribati is a small Pacific island economy reliant on foreign aid and vulnerable to external shocks, particularly climate change. The export and production bases are narrow and limited to copra, seaweed and fishing. The country relies heavily on foreign aid to finance its structural trade deficit. Tourism accounts for less than 2 percent of GDP due to Kiribati's remoteness and poor infrastructure. Given its high import dependence, the economy is vulnerable to swings in commodity prices. The public sector dominates the economy, but private sector activity has picked up lately. Fishing license fees and remittances provide key sources of income as does Kiribati's wealth fund (derived) from phosphate deposits that were exhausted in 1979). The increasing costs of climate change and still large development needs also raise important policy challenges.
- 2. Against this background, the 2011 Article IV discussions tackled both short-
- term and longer-term questions. Discussions focused on policies to support sustainable growth and priorities for structural reforms. In the near term, the main challenge is to manage the investment boom that is without creating inflationary underway pressures. In the medium-term, economic prospects are contingent implementation of a critical mass of structural reforms. Lifting productivity growth and living standards depend on the scope and speed of government's own economic transformation program. The global crisis has led to a rethinking of Kiribati's development strategy, with the private sector playing a more vibrant role. The emerging view is that the country is now at a crossroads.
- **3. Political background.** The current government was elected in 2007. Parliamentary elections are scheduled for August 2011. The presidential election is to be held in October 2011.

RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

A. From Crisis to Recovery

- 4. The impact of the global crisis was stronger than anticipated at the time of the 2009 Article IV consultation. Kiribati has been affected by a fall in remittances and large declines in the value of its wealth and pension funds—the Revenue Equalization Reserve Fund (RERF) and the Kiribati Provident Fund. The spike in food and fuel prices in 2008 has already taken a toll on economic activity. Vulnerabilities to climate change, including coastline erosion, have also worsened, with recurring disruptions at two transportation lifelines (the main road in Tarawa and its airport). As a result, full achievement of the MDGs goals by 2015 is likely now out of reach (Table 1 and Box 1).
- 5. After two years of contraction, the economy recovered in the second half of

- **2010.** It is estimated to have grown by 1¾ percent for the year (Table 2). Despite a weather-related drop in copra production, private sector activity appears to have picked up, especially in retail. Tourist arrivals rebounded by 20 percent compared to 2009, although from a very low base.
- 6. Inflation pressures dissipated in 2010. Despite the rise in world food and fuel prices, inflation has plunged from 2008 crisis-highs into negative territory, reflecting the strong appreciation of the Australian dollar—which is used as the domestic currency—and a decline in the world price of rice (Box 2).
- 7. Credit growth in the overall economy declined in 2009 as economic activity stalled, but started to pick up in the second half of 2010 as the recovery gained traction.

Box 1. Poverty Trends in Kiribati ¹

The spike in food and fuel prices in 2008 and the global crisis have undermined past gains in poverty reduction. The UNDP and the authorities estimated that an additional 10 percent of population is likely to have fallen below the poverty line as a result, with the incidence of poverty increasing from 22 percent to 26 percent. Poverty is highly concentrated in urban areas (South Tarawa) and less in the outer islands where there is greater access to land and marine resources. However, the outer islands face higher transportation costs.

As a result, progress against the achievements of the MDGs has been set back. Five out of eight goals seem out of reach. Increased vulnerabilities to climate change have also slowed the achievement of poverty reduction goals. This reflects the need to divert resources from development expenditure toward building of seawalls.

The government's plan and development partners' assistance are expected to alleviate poverty going forward. The authorities' strategy toward poverty reduction is embedded in the Kiribati Development Plan (2008–11)—the government's overarching plan to "enhance economic growth and poverty reduction for sustainable development". The main pillars include supporting private sector development as a key engine of growth, especially in eco-tourism and in the domestic processing fishing industry, as well as creating employment opportunities both domestically and abroad.

Kiribati: Incidence of Poverty, 1/									
	1996	2006	2009 2/						
National Average	50.0	21.8	26.3						
South Tarawa	51.0	24.2	30.5						
Rest of Gilberts	50.0	22.0	25.4						
Line and Phoenix	50.0	8.9	9.0						

Sources: Kiribati National Statistics Office (NSO) and UNDP Pacific Center, 2009. 1/Defined as proportion of population below the (basic need) poverty line. 2/Kiribati National Statistics Office Estimates, and UNDP.

MDG 1. Eradicate extreme poverty and hunger. Halve between 1990 and 2015 the proportion of people whose income is less than \$1 per day.	Low food poverty, but off track that halve basic needs poverty
MDG 2. Achieve Universal Primary Education.	On track
MDG 3. Promote gender equality and empowerment Eliminate gender disparities in primary and secondary education.	On track, education equality, off track empowerment
MDG 4. Reduce child (Under 5) mortality by two thirds	Slightly off track
MDG 5. Improve maternal health Reduce maternal mortality by three quarters.	Off track
MDG 6. Reverse the spread of HIV/AIDS, malaria and TB	Off track
MDG 7. Ensure environmental sustainability Integrate principles of sustainable development into country policies.	Off track

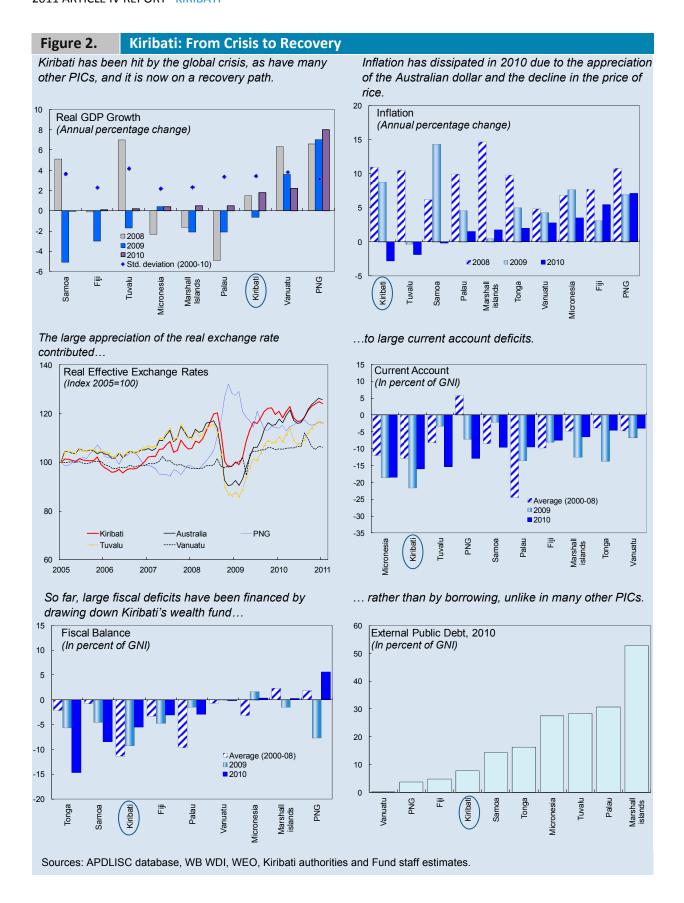
Sources: 2010 MDG Tracking Report, Pacific Islands Forum Secretariat, and 2011 World Bank CAS.

In March 2010, the government formulated a national framework for climate change and climate change adaptation and migration. Progress has been achieved so far in creating temporary employment opportunities abroad thanks to the engagement of development partners (in particular Australia and New Zealand).

1/ Prepared by Tobias Haque (World Bank).

Figure 1. Kiribati—The Setting in a Cross-Country Context Kiribati is one of the poorest islands in the Pacific... ... as subsistence agriculture-mainly copra-and fishing are core activities with tourism still relatively low. Contribution by Activity, 2009 GDP per Capita, 2010 Kiribati (In percent of GDP) (In U.S.dollars) 60 PNG 50 ■ Tourism Tuvalu ■Agriculture, forestry, fishing Micronesia 40 Pacific Islands Marshall 30 Islands (average) Tonga 20 Vanuatu 10 Samoa PNG Tonga Samoa Ē Fiji Kribati Palau 1,500 3,000 4,500 6,000 7,500 9,000 10,500 The country relies heavily on foreign aid... ...to finance its structural trade deficit and large development needs. 50 90 External Grants, 2010 Trade Balance, 2010 45 □ Exports (In percent of GNI) 80 ■ Imports 40 70 35 60 30 □ In percent of GDP 50 ■In percent of GNI 25 40 20 30 15 20 10 10 5 Kiribati 0 Tonga Palan Kiribati Ē /anuatu The economy is largely dominated by the public sector ...and constraints to private sector development. due its narrow production base... 6 Government Expenditure, 2010 Real GDP per Capita vs. Business Climate (In percent of GNI) 60 al GDP per Capita e growth rate,2000-10) Samoa □ Wage expenditure 50 Others 40 Pacific Marshall Islands Kiribati 30 Vanuatu Tonga_ Real (Average g 20 Micronesia 10 Palau 0 -2 Kiribati Marshall islands 臣 30 10 50 Starting a Business Rank, 2011 WB Doing Business (higher

Sources: APDLISC database, WB WDI, WEO, Kiribati authorities and Fund staff estimates.



B. Outlook and Risks

Staff's Views

8. Growth momentum in the near term is expected to strengthen. Under current policies, kev public projects—the rehabilitation of Tarawa's road, airport and port-financed with external assistance should support growth in the 3 percent range over the next few years, restoring prospects had been undermined by the that infrastructure failures. Growth would revert to 1½-2 percent in the medium to long term assuming that the impact of climate change will continue to negatively impact economic activity.

Summary of the Medium-term Baseline Macroframework										
	2011	2012	2013	2014	2015	2016				
Real GDP growth (%)	3.0	3.5	3.0	2.0	2.0	2.0				
Inflation (%)	7.7	5.0	3.3	2.5	2.5	2.5				
Fiscal balance (% of GDP)	-14.3	-18.1	-16.2	-14.7	-15.0	-13.7				
Current account (% of GDP)	-28.9	-29.2	-26.8	-23.0	-24.6	-23.9				
Source: IMF staff estimates.										

- 9. Risks to the near and medium-term outlook are balanced, but long-term challenges remain. On the upside, domestic public works in the pipeline may have largerthan-expected impact on output, despite their large import content. On the downside, if the global recovery stalls, Kiribati's remittances would be hit, while a surge in world food and oil prices could raise inflation pressures even further (Box 2) undermining past gains in poverty reduction. Higher than expected pressures from the upcoming investment boom could also arise. Over the long run, vulnerabilities to climate change could take a toll on economic activity undermining its long-run prospects.
- 10. However, the outlook for the medium term depends on the scope and speed of the

government's own reform agenda. With stepped-up reforms at a realistic pace, GDP growth could reach 3 percent over the medium and long term.

Summary of the Medium-term Reform Macroframework										
	2011	2012	2013	2014	2015	2016				
Real GDP growth (%)	3.0	3.5	3.5	3.0	3.0	3.0				
Inflation (%)	7.7	4.0	3.0	2.5	2.5	2.5				
Fiscal balance (% of GDP)	-14.3	-10.3	-7.5	-5.2	-5.3	-4.6				
Current account (% of GDP)	-27.2	-22.6	-20.2	-16.6	-17.4	-16.4				
Source: IMF staff estimates.										

Authorities' Views

11. The authorities agreed with staff's assessment of the economic outlook and risks. On the downside, they emphasized the potential spillovers from a potential further escalation of the food and fuel prices, with a negative impact especially on urban poverty. On the upside, improved prospects for employment driven by the investment boom could further spur domestic demand.

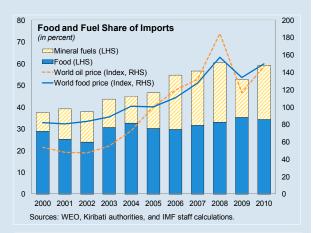
Box 2. Kiribati: The Impact of High Fuel and Food Prices

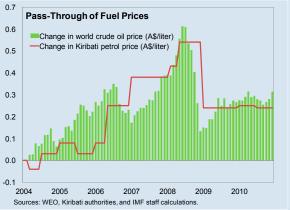
Kiribati is vulnerable to a surge in commodity prices. Food and fuel imports represent 30 percent of GDP. Their share in total imports increased from less than 40 percent to about 60 percent over the last decade as commodity prices trended up.

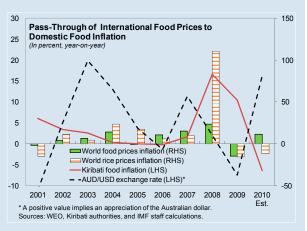
The pass-through of food—especially rice—and energy prices to domestic inflation is high. Rice accounts for 20 percent of the CPI food basket. An increase in international fuel prices historically has resulted in an equal increase in domestic prices, with a three-month lag.

However, there are some mitigating factors compared to 2008. Rice prices have fallen in 2010 and they are still well below the 2008 peak and the Australian dollar has appreciated significantly helping mitigate imported inflation pressures.

Yet, a further increase in commodity prices may eventually pass through to domestic inflation, worsening both the fiscal and **external positions**. This could occur through higher imports and public spending, especially in light of the large investment projects in the pipeline, and possibly through higher food and fuel subsidies, although they account for a very small part of GDP (1 percent). Under an adverse scenario with oil price increasing by 40 percent in 2011, the fiscal balance is expected to deteriorate by 2½ percentage points of GDP in 2011 compared to the baseline, and the current account balance by 3 percentage points of GDP, provided that the Australian dollar does not appreciate further.

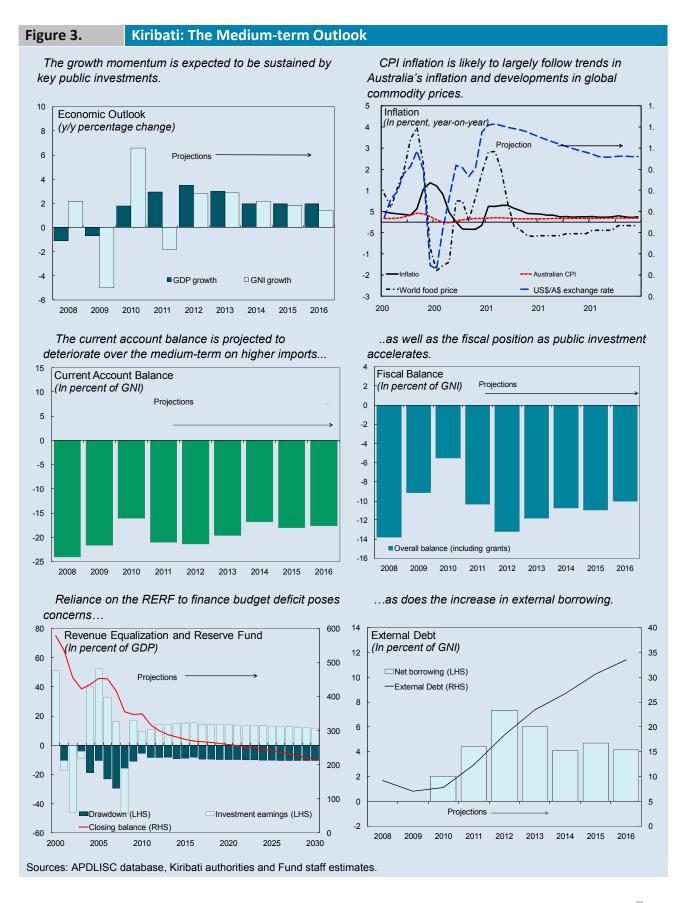






Adverse Oil-shock Scenario: Comparison with the Baseline 1/										
	201	11	20:	12						
	Baseline	Adverse	Baseline	Adverse						
Oil price (US\$/barrel)	107.2	149.2	109.3	110.9						
Real GDP growth (percent)	3.0	2.0	3.5	2.4						
Inflation (percent)	7.7	11.7	5.0	7.1						
Fiscal balance (percent of GDP)	-14.3	-16.8	-18.1	-20.2						
Current account (percent of GDP)	-28.9	-32.0	-29.2	-31.7						

1/ Assumes an increase in oil price of 40 percent in 2011 compared to the baseline.

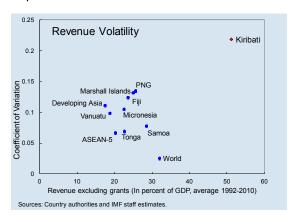


POLICIES TO ENSURE SUSTAINABLE GROWTH

A. Fiscal Policy

Background

12. The scope for countercyclical policy in Kiribati is limited. The revenue base is large but very volatile. Fishing license fees account for about half of government revenues (Box 3). The country depends on foreign aid to finance its large development needs. More extreme weather patterns related to global climate change are also putting strains on the budget. The only fiscal cushion against negative shocks has been provided by Kiribati's wealth fund (RERF), which in recent years has been severely depleted.



13. Fiscal policy has supported the economy during the economic downturn. Copra subsidies and civil servant wages have increased and have helped mitigate the impact of the output contraction on households. The fiscal deficit bottomed out at 20 percent of GDP in 2008 (Table 3), but narrowed substantially the following year as a result of expenditure compression and improved tax collection, with the introduction of a withholding tax at the source in March 2009.

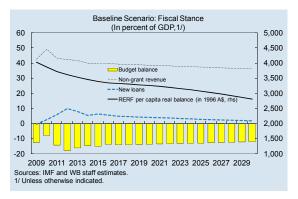
- **14.** However, the RERF suffered substantial losses. The RERF assets declined from A\$637 million (420 percent of GDP) in 2007 to A\$571 million (350 percent of GDP) in 2009. This drop reflected exposure to failed Icelandic banks (A\$40 million, or 25 percent of GDP), as well as continued drawdowns to finance budgetary shortfalls.
- 15. 2010 In the fiscal position strengthened and budget planning **improved.** The estimated fiscal deficit is 8 percent of GDP, down from 12½ percent in 2009. The narrowing deficit reflects a large increase in fishing licenses fees, as a result of an auction scheme introduced in September 2010 as well as temporary factors—such as fines collected from foreign fishing vessels. The 2010 budget introduced a three-year budget framework in line with previous IMF policy recommendations (Appendix 1), with the assistance of the AsDB.
- 16. The 2011 budget marks a return to fiscal expansion. The fiscal balance is expected to deteriorate to 14 percent of GDP in 2011 on the back of a large increase in development expenditure in infrastructure financed by a combination of external assistance and RERF draw-downs.
- 17. Over the medium term, fiscal deficits will remain in the double digits (Table 4). The current government's fiscal strategy is to target the RERF drawdown at A\$15 million per year during 2011–13. Given the expected external loans to finance infrastructure spending, this strategy would imply a deficit of 10–14 percent of GDP. In 2014, revenues are expected to drop by 2 percent of GDP

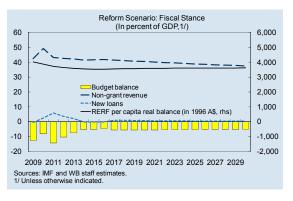
with lower tariffs following the implementation of Pacific Islands Countries Trade Agreement (PICTA).

Staff's Views

- 18. The fiscal stance for the next two years is appropriate, but fiscal adjustment will be required in the out years. The deterioration of the fiscal balance in the near term is warranted by key development expenditures that will spur productivity growth. However, going forward, the focus will need to shift to fiscal consolidation. In the last ten years, budget deficits (averaging 12 percent of GDP) have been financed by drawing down the RERF. If this trend continues, the RERF real per capita balance would reach one-third of its 2000 value by 2030 (DSA baseline scenario).
- 19. Should food and fuel prices escalate, the authorities should refrain from increasing universal subsidies and public wages. However, as income inequality is very low in Kiribati, it may be difficult to design a targeted subsidy program. Instead the mission supported the authorities' plan to take full advantage of the regional seasonal employment scheme offered by Australia and New Zealand to increase employment and income generating opportunities in the short term. Grant support from donors would also help limit the harm to real incomes and poverty. An increase in civil servant wages would not be an appropriate countercyclical policy because it is unlikely to be reversed when the economy recovers, as the increase introduced in early 2010 demonstrates.
- 20. Over the medium term, to help anchor fiscal plans, the mission suggested stabilizing the real value of the RERF in per capita

terms, once key public investments in the pipeline have occurred.¹ This would require limiting budget deficits to 5–6 percent of GDP over the long term (DSA reform scenario).² Fiscal sustainability requires preserving the value of the RERF as a buffer against external shocks. While this fiscal anchor would only be indicative, it could provide an internal consistency check to link fiscal decisions to a more intergenerationally equitable drawdown of sovereign wealth.





¹ Given the assumed rate of return on the RERF assets (5½ percent per year), population growth (1.6 percent per year) and inflation (2½ percent per year), to preserve the real per capita balance of the RERF, the nominal RERF balance would need to grow by about 4 percent per year (2½ percent inflation plus a 1.6 percent increase in population). This implies a yearly nominal draw-down of about 1½ percent of the RERF total balance. See paragraph 12 of the Supplement DSA.

² Part of the difference in the size of fiscal deficits in the baseline scenario and in the reform scenario is due to the assumption that development expenditure is fully funded by grants over the medium term in the latter.

- 21. Staff commended the authorities for adopting a multi-year budget framework as it would provide more fiscal discipline. Realistic fiscal plans would be more easily designed and fiscal sustainability safeguarded. Given the uncertainty surrounding revenue and aid flows, revenue projections should be conservative assumptions. Downside scenarios should also be fleshed out, with revenue shortfalls, as a result of a temporary shock, and the prospective costs of climate change mitigation, explicitly considered. Overall, lower fiscal deficits (and a stronger sovereign balance sheet) are needed to reconstitute room for countercyclical fiscal maneuver, as well as scope to meet the longterm spending pressures arising from a rising sea level.
- 22. As the recovery proceeds, stronger than anticipated revenues should be saved. To help moderate pro-cyclical fiscal policies driven by volatile revenues, windfalls should be saved during upswings and used only during downturns to support the economy. This will help create fiscal space by safeguarding the RERF against external shocks and support a smooth path of expenditure.
- 23. Savings can also be achieved by rationalizing expenditure and tax structures. Poorly targeted and distortionary subsidies to copra producers and other state-owned-enterprises (SOEs), amounting to some 5 percent of GDP, should be phased out. The restructuring of loss-making SOEs should also proceed apace. Customs administration—which reportedly has worsened in the last few years—should be shored up and exemptions reduced. The introduction of a VAT tax should also be considered.
- 24. Staff welcomed the introduction of an auction scheme on fishing licenses. This

- would provide scope for increasing fishing license revenues over the medium term.
- 25. The authorities should reconsider RERF investment strategies in line with the recent MCM TA recommendations. The report suggested reviewing current strategic asset allocation to reflect more closely the currency composition of Kiribati's imports. The report also recommended strengthening the governance of the RERF by increasing inhouse expertise over the medium term through training or secondment at other wealth fund institutions, hiring a long-term consultant to improve the investment framework, closer monitoring investment risks and returns, and publishing annual reports to increase transparency.
- Kiribati is at high risk of debt distress. 26. Fiscal risks have been exacerbated by the crisis as RERF assets—the primary source of deficit financing—dropped significantly. The uncertainty about aid flows and the impact of climate change will add to pressures on Kiribati's fiscal position over the long term. The joint IMF-WB debt sustainability analysis shows that despite low external public debtcurrently estimated at about 10 percent of GDP—the debt outlook is projected to worsen in the years ahead as Kiribati undertakes infrastructure investment (partly financed borrowing from development through partners) and the fiscal costs of climate change. Improving debt dynamics will require borrowing, prudent continued grant financing, fiscal consolidation, and a step up in structural reforms.

Authorities' Views

27. The authorities reiterated their strong commitment to preserve the value of the RERF. They saw merit in staff's advice to save

stronger-than-anticipated revenues in the upswing, as well as in maintaining the real per capita balance of the RERF constant once the large public investments have occurred. They noted that their nominal drawdown rule, while imperfect, is simple to communicate and is the first step toward a fiscal anchor. Should the increase in commodity prices be persistent they may consider increasing the import levy and then using the proceeds to reimburse the freight costs for goods transported to the outer islands, where transportation costs are higher. While they agreed that the increase in civil servant wages effective in January 2010 was not a countercyclical policy measure given its permanent nature, they noted that the previous increase dated back to 2006 and thus was overdue.

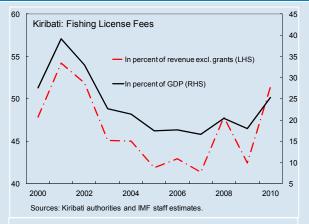
28. On technical assistance, they requested assistance from PFTAC on the macroframework and tax administration. They also expressed concerns about the volatility in fishing revenues as they are collected in U.S. dollars and are currently looking at options for hedging exchange rate risk through financial derivatives and for denominating fishing license fees using a basket of currencies. Officials would welcome technical assistance from development partners. They highly appreciated the TA on the RERF provided by MCM.

Box 3. Kiribati: Prospects for Fishing License Revenues

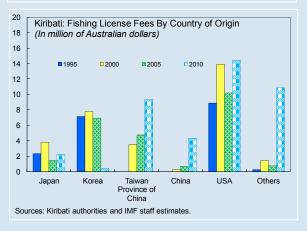
Fishing license fees are a key source of income for Kiribati. Over the last ten years they represented on average 45 percent of government revenues. They are the highest (in terms of GDP) among regional peers reflecting the largest marine resource endowment across the Pacific.

Kiribati has still untapped potential to exploit its fishing resources and reduce the volatility of fishing revenues and some steps have been recently taken.

- September 2010, the authorities introduced an auction scheme for fishing rights. replacing bilateral access agreements-in line with previous IMF recommendations. Bilateral agreements specified a fixed fee per vessel and were renegotiated on a yearly basis, regardless of the value of fish catches. Thanks to the introduction of the auction scheme, as well as some other temporary factors (paragraph 15) in 2010 fishing license fees surged by almost 40 percent (year-on- year) to 52 percent of GDP.
- The authorities are seeking options to reduce the volatility of license fees due to exchange rate movements of the U.S. dollar through financial derivatives or by denominating fishing license fees using a basket of currencies. They are currently evaluating pros and cons of moving away from the current U.S. dollar denomination as it provides a natural hedge against U.S. dollar-denominated imports.
- Recent initiatives to encourage investment in domestic marine processing would increase proceeds from fishing resources. The recent agreement among the government of Kiribati and Chinese and Fijian fishing companies to set up a joint venture for marine processing could provide a significant boost to the economy. The FDI involved is expected to reach A\$50 million.







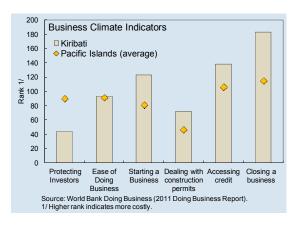
Further improvements can be expected. Participation in the Pacific Islands Forum Fisheries Agency and negotiation of a comprehensive Economic Partnership Agreement with the European Union may strengthen control over marine resources and create new opportunities for increasing revenue. Adopting cooperative sub-regional measures may strengthen bargaining power of license-issuing countries.

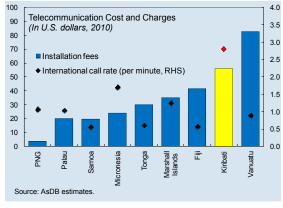
B. Structural Reforms—Supporting Private Sector Growth

Background

- 29. Weak private sector development is an impediment to sustainable growth. Participation of the private sector in the economy is tenuous although it has increased over the last few years. According to the 2011 WB Doing Business Report, procedures for starting and closing a business, and dealing construction permits cumbersome than in other Pacific islands. Also, access to credit is limited and costly, while poor infrastructure continues to hold back long-term growth. The government's Development Plan (KDP), spanning 2008-11, correctly recognized the need to rotate the sources of growth toward the private sector in areas such as tourism and marine resources—including the development of niche tourism in Kiritimati (Christmas) Island—and identified key weaknesses of the current system. The outstanding issue remains the slow pace of implementation in key areas:
- Land reform. Limited land availability and weak enforcement of land property rights are problematic. Two thirds of the land is owned by the government and the remaining third by families rather than individuals, making property rights unclear. Most transactions are contested, and court settlement procedures are very long. Lease procedures are lengthy and perceived as arbitrary with the Minister of Land responsible for final approval.
- **SOEs reform.** Despite little progress in recent years, momentum in the SOE reforms seems finally to have gained traction. An SOE will be privatized by May 2011 and five additional SOEs have been identified for

reform. The KDP calls for cutting back government guarantees on SOEs' borrowing. The contingent liabilities from SOEs amounted to about 20 percent of GDP in 2010.





Staff's Views

30. With a shift to a higher growth path hinging on a vibrant private sector, the implementation of the structural reform agenda should be accelerated. Private sector development is crucial to improve growth prospects, especially in tourism and fish processing.³ While there was agreement that

³ Kiribati's extensive marine resource endowment of Kiritimati and Tabuaeran Islands, and the Phoenix Islands Protected Area—the largest world heritage marine protected area—could provide substantial opportunities for eco-tourism. However, basic infrastructure is needed.

the pace of reforms needs to be calibrated to political realities, staff advised the authorities to bring the current structural reform momentum forward and take measures to improve the business climate. A critical mass of reform is needed to continue attract foreign assistance and increase opportunities for foreign investment. Reforms aimed at streamlining starting up businesses, and construction permits, obtaining and expanding access to credit are key. A new land law that improves access to land by strengthening administrative systems for transferring property rights and improves the legal framework for land usage ownership is also urgent. The authorities' interest to liberalize telecommunication with the assistance of the World Bank is a welcome step.

- 31. Staff supported the SOE reform underway with the assistance of the AsDB. Reforming the SOEs would create space for private sector development and reduce the drain on the budget. As advocated by the Fund in past consultations, it is important to limit SOEs to areas where the private sector operations are not viable such as in public utilities (water, electricity, and fuel distribution to the outer islands).
- **32.** Strengthening public financial management (PFM) is crucial. PFM in Kiribati is weak, and characterized by poor data quality and expenditure controls, outdated legislation and regulations, limited

information about fiscal risks from nonperforming SOEs, and poor links between capital investments and recurrent budgets. These weaknesses weight on business activity. The PFM Reform Plan, which sets out the government's reform priorities based on the findings of the 2010 Public Expenditure and Financial Accountability, provides a good platform for policy dialogue and more focused technical assistance.

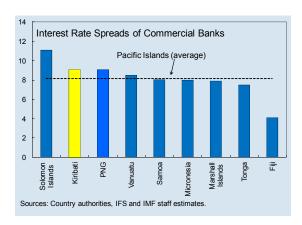
Authorities' View

The authorities shared the view that a meaningful uplift in trend growth requires structural reforms on a broad front. The authorities have reiterated in the 2011 budget speech their commitment to SOE reform. While they pointed out that the pace of reforms may slow down in the second half of the year ahead of elections, the need for the private sector to support the economy has gained consensus among policymakers and the public. They are considering a law to ease constraints to the use of land as collateral. To streamline the red tape for business they are planning on instituting a "one-stop shop" to ease procedures for opening a business. They also stressed that a review of the investment regulatory framework should take place with the assistance of development partners to increase interest of foreign investors. In their view, one of main impediments to private sector development is the difficulty in accessing credit. However, they agreed that this in turn reflects the absence of clear property rights.

C. Safeguarding Financial Sector Stability

Background

34. Kiribati's financial sector is undercut by structural impediments and a lack of competition. It consists of two banks, one insurance company, and a pension fund. ANZ Bank (Kiribati) Limited is the only commercial bank.⁴ Restrictions on land ownership by foreign entities tilt the bulk of its lending toward public enterprises. ANZ Bank NPLs are less than 1 percent of total loans. The Development Bank of Kiribati (DBK), wholly government-owned, has a larger share of loans to the private sector but its loan book is marred by high NPLs and secured lending remains underdeveloped. Insurance coverage is provided by another government financial institution, the Kiribati Insurance Corporation. Finally, the Kiribati Provident Fund (KPF) manages the assets of the pension system, about 60 percent of GDP in 2010 (Box 4). Overall, access to credit by the private sector remains restricted and expensive. The interest rate spread is slightly above the Pacific Islands average. The private sector has regularly complained about high charges and fees, including on remittances.



The authorities have tried to bolster competition and intermediation. Entry into the insurance industry was liberalized at end-2008, although the incumbent insurer remains unchallenged to date. The KPF introduced a lending scheme in July 2010, which allows short-term borrowing (i.e., one year) for any purpose of up to 14 percent of a member's balance in the pension fund, using his pension entitlements as collateral⁵. In 2010, loans under this scheme totaled A\$3 million (about 3½ percent of the fund's portfolio). There are also plans afoot to strengthen the commercial orientation of the DBK through a foreign partnership.

Staff's Views

More competition in the banking sector would help to spur private sector's **development.** The authorities' efforts are appropriately focused but other steps could be considered. These include: (i) expanding micro-credit with the development of village banks as done in other Pacific islands; (ii) containing NPLs at the DBK by

⁴ It is 25 percent government-owned. Until August 2009 it was known as the Bank of Kiribati.

⁵ Loans could amount up to 20 percent of a member's collateral, the latter being defined as 70 percent of the member's balance.

tightening lending standards and improving risk management; and (iii) introducing a long-overdue land law to ease access to credit and improve collateral recovery. Bank regulation and supervision need to be strengthened before an expansion of the DBK's lending activity is considered. Staff also stressed the need to enact and implement the draft law on anti-money laundering and combating the financing of terrorism (AML/CFT).

37. The new lending scheme of the pension fund could prove problematic. Although collateralization limits credit risks to the KPF, contingent liabilities to the government could build up if members exhaust their pension wealth ahead of retirement. Thus the size of the scheme should not be increased. If this were the case, asset allocation may be adversely affected by the need to ensure greater liquidity of the assets, if draw-downs under the scheme increase. If members were to use the loans for consumption or improper investments, they might compromise their future pension income. Hence, the government and/or KPF should invest in financial education. Technical assistance, including from the IMF, could help the authorities improve the design of the lending program.

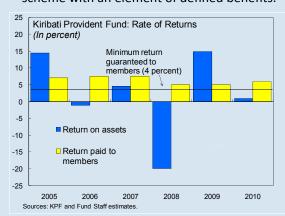
Authorities' Views

- 38. The officials broadly shared staff's views on the challenges facing the financial sector and requested IMF technical assistance in this area. They agreed that greater competition would improve the private sector's access to credit and reduce credit costs. Fund technical assistance on financial supervision and regulation would strengthen the underpinning of the reforms underway, including the restructuring of the Development Bank.
- **39.** The authorities noted that the new KPF lending scheme is an initial step to improve households' access to credit. Since lending is a relatively small fraction of the accumulated individual assets and collateralized, the solvency of the pension fund or its exposure to credit risk are not at issue. Nonetheless, the authorities requested IMF technical assistance in reviewing the asset allocation strategy of the KPF as well as an assessment of its long-term viability.

Box 4. Financial Sector Developments: The Provident Fund and Kiribati Development Bank

Kiribati Provident Fund (KPF) is Kiribati's government-managed pension fund.

 The 2008 crisis hit the KPF hard. Assets values dropped by 20 percent, but rebounded in 2009-10, reaching pre-crisis value. Its assets totaled A\$100 million (60 percent of GDP) at end-2010. Employers and employees each contribute 71/2 percent of the employee's salary. At the retirement age (50 years), participants receive a lump-sum payment. However, at the age of 45, members have the option of withdrawing 50 percent of their accrued balance while continuing working until age 50, or 100 percent of their balance if they retire at 45 for medical reasons. With a minimum yearly rate of return guaranteed at 4 percent, the fund is a defined-contribution scheme with an element of defined benefits.



• The KPF has built a buffer fund to accumulate "surpluses" when rate of return on assets exceed rate of return accrued to members (decided by the KPF board). Through the years, this buffer has, however, been depleted in the wake of losses during the crisis resulting in a gap between assets and projected liabilities. Additionally, earlier losses related to lending operations to the DBK (amounting to A\$1½ million) to allow households to borrow funds for education

fees at terms below market rates in 2007 have further deteriorated its financial position.

Recognizing these risks, the KPF management has committed to a more active asset allocation strategy, increasing asset diversification in mid-2010 and hiring an additional portfolio manager.¹

The Development Bank of Kiribati (DBK) is a government-owned banking institution.

- About 40 percent of loans are for business purposes. The interest rate charged is close to market rates. Loans of all types are collateralized (by land or pension contributions for borrowers older than 45 years). Loans are funded by a revolving government fund.
- Although NPLs declined since 2008, they were still high at 24 percent of total loans in 2010.
- DBK lending activity has started to pick up in the second half of 2010 as the economy recovered. In spite of the 60 percent provisions for NPLs, poor prospects for loan recovery due to issues with land titling and poor risk management undermine the soundness of the bank.

DBK: Financial Soundness Indicators (in percent)

			(1	-7
	2007	2008	2009	2010 1/
NPL to total loans	23.7	25.6	24.7	23.6
Provisions-NPL ratio	48.9	56.4	56.9	58.2
Loans-capital ratio	220	246	201	202
Capital-assets ratio	41.5	39.3	48.6	51.7
Return on assets (ROA)	2.7	-3.0	1.5	1.3
Return on equity (ROE)	6.4	-7.3	3.3	2.6

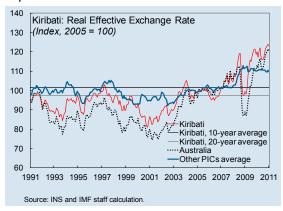
1/ September 2010.

Sources: DBK and Fund Staff estimates.

¹In mid-2010, the KPF asset allocation strategy changed from a 60–40 split between risky assets and fixed income assets to a more diversified asset class allocation.

ADDRESSING EXTERNAL COMPETITIVENESS AND SAFEGUARDING EXTERNAL STABILITY

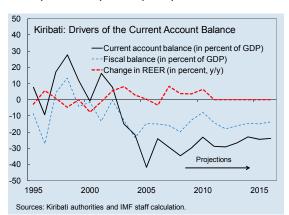
- **40. The Australian dollar circulates as legal tender.** Kiribati has accepted the obligations of Article VIII, Sections 2, 3, and 4 and maintains an exchange system free of restrictions on payments and transfers for current international transactions.
- 41. The real effective exchange rate has appreciated by 20 percent since 2008, driven by the strong Australian dollar and appears to be overvalued compared to its long-run level. However, the current account balance has improved over the last few years, reflecting strong income from fishing license fees. Looking ahead, the current account deficit is expected to deteriorate in the near term as Kiribati undertakes large public investment, and to narrow again by the end of the projection period to 24 percent of GDP (from 29 percent in 2011) in line with an improvement in the fiscal position (Tables 5 and 6). In the short term, large deficits are likely manageable as they are driven by key investment in infrastructure and financed by capital transfers.



Staff's Views

42. The use of the Australian dollar as the official currency remains appropriate given Kiribati's close linkages with Australia and has provided a strong nominal anchor.

- 43. While it is desirable to maintain the dollar as nominal Australian pursuing structural reforms is crucial to regaining competitiveness following strong real appreciation. As (paragraph 29), competitiveness based on institutional indicators suggests that the business environment needs be significantly improved.
- 44. Continuing to secure grant financing, instead of loans, and containing fiscal deficits are key to ensure external stability. From a macro balance perspective, the sustainability of the current account in the medium-term is totally driven by fiscal policy.



Authorities' Views

45. The authorities agreed that there is no scope to have an independent monetary policy. They also stressed that the fluctuation of the Australian dollar makes the economy vulnerable to exchange rate risks, given the RERF assets are mostly held in Australian dollars, while imports are not, resulting in a currency mismatch. They noted that the large current account deficit reflects to a large extent the surge in commodity prices, not only a loss in competitiveness and a large structural component—low public saving driven by large developments spending.

STAFF APPRAISAL

- Kiribati is at a crossroads. The economy has recovered from the crisis with strong forward momentum. Large public investment in key infrastructures financed by foreign assistance underpins its favorable mediumterm growth prospects. Yet gains will prove transitory if a broader agenda of fiscal and structural reforms remains unfinished. Further reforms are necessary to bolster the economy's resilience and to ensure sustainable growth. The increasing costs of climate change and still large development needs raise important policy challenges.
- 47. Preserving the real per capita value of the RERF is key to ensure fiscal sustainability and intergenerational fairness. Once key public projects in the pipeline are underway, the focus should shift to fiscal consolidation. Lower fiscal deficits and a stronger sovereign balance sheet are necessary to rebuild fiscal space and help cope with long-term spending pressures arising from climate change.
- 48. The authorities have taken steps to bolster the public finances by introducing a multi-year budget framework. Casting budget decisions in a multi-year perspective will help design realistic fiscal plans. Positive windfall revenues compared to the budget should be saved during upswings and used only during downturns to support the economy. Continuing strengthening the medium-term fiscal framework is important to facilitate public planning and help guard against pro-cyclical policies.
- **49.** The implementation of the structural reform agenda should be accelerated. Reforming the SOEs is key to creating space

for private sector development and reducing the drain on the budget.

- **50.** Competition in the banking sector is crucial to boost private activity. The authorities' plans to revitalize the DBK in the medium term are welcome. In the meantime any further expansion of the DBK's activity should be postponed until a regulatory and supervisory framework is in place. Expanding micro-credit schemes would also help ease credit constraints.
- **51.** The use of the Australian dollar remains appropriate. To preserve external stability, continuing to secure grant financing would be key to supporting the country's large development need, as indicated in the joint IMF-World Bank debt sustainability analysis.
- **52.** The quality of macroeconomic data should continue to improve. The authorities should press ahead with PFTAC recommendations on the compilation and dissemination of economic data.
- 53. It is recommended that the next Article IV consultation take place on a 24-month cycle. This recommendation is in accordance with the Decision on Article IV Consultation Cycles (Decision No. 14747-(10/96) (9/28/2010),

http://www.imf.org/external/pp/longres.aspx?id=4515.

	1990	1995	2000	2005	2008	2009
Goal 1: Halve the rates for extreme povetry and malnutrition						
Income share held by lowest 20%						
Malnutrition prevalence, weight for age (% of children under 5)						
Poverty gap at \$1.25 a day (PPP) (%)						
Poverty headcount ratio at \$1.25 a day (PPP) (% of population)						
ioal 2: Achieve universal primary education						
·						
Literacy rate, youth female (% of females ages 15-24)						
Literacy rate, youth male (% of males ages 15-24) Persistence to last grade of primary, total (% of cohort)		••	••			•
Primary completion rate, total (% of relevant age group)		••	 99	 125	••	•
Secondary school enrollment (% gross)	••	••	99	88	••	•
Total enrollment, primary (% net)	••	••	97			•
	••		37		••	•
ioal 3: Promote gender equality and empower women						
Proportion of seats held by women in national parliaments (%)	0	0	5	5	4	4
Ratio of female to male enrollments in tertiary education					••	
Ratio of female to male primary enrollment			99	101	••	•
Ratio of female to male secondary enrollment			161	114		
Share of women employed in the nonagricultural sector						
(% of total nonagricultural employment)			37	39	••	•
ioal 4: Reduce child mortality by two-thirds						
Immunization, measles (% of children ages 12-23 months)	75	47	80	85	72	82
Mortality rate, infant (per 1,000 live births)	65	56	49	42	38	37
Mortality rate, under-5 (per 1,000)	89	75	63	53	48	46
oal 5: Improve maternal health						
Births attended by skilled health staff (% of total)		72	89			
Contraceptive prevalence (% of women ages 15-49)	••		21	••		
Maternal mortality ratio (modeled estimate, per 100,000 live births)					•	
oal 6: Combat HIV/AIDS, malaria, and other diseases	540	460	420	200	260	
Incidence of tuberculosis (per 100,000 people)	510	460	420	380	360	
Prevalence of HIV, total (% of population ages 15-49)						•
Tuberculosis case detection rate (all forms)	18	92	71	95	97	•
oal 7: Halve the proportion of people without sustainable access to basic needs						
CO2 emissions (kg per PPP \$ of GDP)	0.2	0.2	0.2	0.1		
CO2 emissions (metric tons per capita)	0.3	0.3	0.4	0.3		
Forest area (% of land area)	2.7	2.7	2.7	2.7		
Improved sanitation facilities (% of population with access)	26	28	33	31		
Improved water source (% of population with access)	48	54	62	61	65	
Terrestrial protected areas, (% of surface area)					55.0	
oal 8: Develop a global partnership for development						
Debt service (PPG and IMF only, % of exports, excluding workers' remittances)						
Internet users (per 100 people)			1.8	2.2	2.1	
Mobile cellular subscriptions (per 100 people)	0.0	0.0	0.4	0.7	1.0	
Personal computers(per 100 people)			1.0		1.1	
Telephone lines (per 100 people)	1.7	2.6	4.0	4.6	4.1	
ther	4.0	4.5	2.0	2.4		
Fertility rate, total (births per woman)	4.0	4.5	3.8	3.4	1.060	1 020
GNI per capita, Atlas method (current US\$)	730	1,160	1,380	1,780	1,960	1,830
GNI, Atlas method (current US\$) (billions)	0.1	0.1	0.1	0.2	0.2	0.2
Gross capital formation (% of GDP)	93.1					
Life expectancy at birth, total (years)	56.8	59.4	59.5	60.9		
Literacy rate, adult total (% of people ages 15 and above)						
Population, total (millions)	0.1	0.1	0.1	0.1	0.1	0.1
Trade (% of GDP)	158.9	83.5	53.7			

Table 2. Kiribati: Selected Economic Indicators, 2007–12

Nominal GDP (2010): US\$146.7 million Nominal GNI (2010): US\$209.6 million Main export products: fish and copra GDP per capita (2010): US\$1,420 Population (2010): 103,280 Quota: SDR 5.6 million

	2007	2008	2009	2010	2011 rojections	2012
				Г	rojections	
Real GDP (percent change)	0.4	-1.1	-0.7	1.8	3.0	3.5
Real GNI (percent change)	-0.9	2.2	-5.0	6.6	-1.8	2.8
Consumer prices (percent change, average)	4.2	11.0	8.8	-2.8	7.7	5.0
Consumer prices (percent change, end of period)	3.7	18.6	0.1	-1.4	8.0	4.0
Central government finance (percent of GNI)						
Revenue and grants	47.3	48.9	58.1	57.6	58.6	58.8
Total domestic revenue	28.8	29.6	32.0	34.1	31.3	30.8
Grants	18.5	19.3	26.1	23.5	27.3	28.0
Expenditure and net lending	58.7	62.7	66.0	63.1	69.0	72.0
Current	40.3	43.4	39.9	38.0	37.4	36.9
Of which: wages and salaries	19.5	19.8	19.1	18.5	18.5	18.5
Development	18.5	19.3	26.1	25.1	31.6	35.1
	10.0	10.0	20.1	20.1	01.0	
Overall balance	-11.4	-13.8	-7.9	-5.5	-10.4	-13.2
Financing	11.4	13.8	7.9	5.5	10.4	13.2
Revenue Equalization and Reserve Fund (RERF)	21.1	11.0	11.6	3.9	6.1	6.1
Other	-9.7	2.8	-3.7	1.7	4.2	7.2
RERF						
Closing balance (in millions of U.S. dollars)	562	389	512	572	515	518
Closing balance (in millions of \$A)	637	562	570	576	580	590
Per capita value (in 1996 \$A)	5,052	4,185	4,020	3,868	3,717	3,614
Commercial banks (in millions of U.S. dollars)	,	,	·		·	·
Foreign assets	30.0	11.3	17.2			
Private sector claims	22.9	45.6	36.4		•••	•••
Total deposits	38.8	43.4	36.8		•••	
· · · · · · · · · · · · · · · · · · ·	00.0	70.7	00.0	•••		
Balance of payments (in millions of U.S. dollars)	27.6	46.0	20.4	24.4	47.4	E0 E
Current account including official transfers	-37.6	-46.0	-38.1	-34.1	-47.1	-50.5 -29.2
(In percent of GDP)	-29.4	-34.7	-29.8	-23.1	-28.9	-29.2 -116.7
Current account excluding official transfers (In percent of GDP)	-70.6 -55.2	-78.9 -59.6	-84.2 -65.8	-84.0 -57.0	-108.4 -66.5	-116. <i>1</i> -67.4
(III percent of GDF)	-55.2	-59.0	-05.0	-57.0	-00.5	-07.4
External debt (in millions of U.S. dollars)	13.7	14.5	14.3	18.4	27.6	43.5
(In percent of GDP)	10.2	13.3	9.7	11.3	17.0	25.1
External debt service (in millions of U.S. dollars)	2.2	0.6	1.0	0.6	0.6	0.7
(In percent of exports of goods and services)	11.9	5.0	7.9	3.0	2.6	2.7
, , , , , , , , , , , , , , , , , , , ,					2.0	,
Exchange rate (\$A/US\$ period average) 1/	1.2	1.2	1.3	1.1		
Real effective exchange rate (period average) 2/	99.8	115.0	125.9	129.4		
Memorandum item:						
Nominal GDP (in millions of Australian dollars)	152.8	158.0	164.1	164.8	183.2	197.2
(in millione of Australian dollars)	102.0	100.0	104.1	104.0	100.2	.07.2

Sources: Data provided by the Kiribati authorities; and Fund staff estimates and projections.

^{1/} The Australian dollar circulates as legal tender.

^{2/} Index, 2005=100.

Table 3. Kiribati: Summary of Central Government Operations, 2007–12

	2007	2008	2009	201	.0	201	.1	2012
				Budget	Outturn	Budget	Proj.	Proj.
			(In m	illions of A	ustralian	dollars)		
Total revenue and grants	100.9	111.3	128.7	124.4	136.9	139.3	147.8	158.5
Revenue	61.5	67.3	69.6	68.6	81.0	70.4	78.9	83.1
Tax revenue	29.9	29.6	28.7	30.3	30.4	30.8	33.9	36.0
Nontax revenue	31.6	37.7	40.8	38.3	50.6	39.6	45.0	47.1
Of which: Fishing license fees	25.4	32.2	29.5	30.5	41.7	31.5	35.0	36.4
External grants	39.4	44.0	59.1	55.8	55.8	68.9	68.9	75.4
Total expenditure	125.2	142.7	149.4	143.3	150.1	168.9	173.9	194.2
Current expenditure	85.8	98.7	90.3	87.5	90.3	89.4	94.3	99.5
Of which: Wages and salaries	41.5	45.0	43.2	42.4	44.1	46.6	46.6	49.9
Subsidies to public enterprises 1/	7.2	8.1	7.3	7.9	7.9	7.9	7.9	7.5
Other current expenditure	37.1	45.5	39.8	37.2	38.3	34.9	39.8	42.1
Development expenditure 2/	39.4	44.0	59.1	55.8	59.8	79.6	79.6	94.7
Overall balance 3/	-24.4	-31.4	-20.7	-18.9	-13.2	-29.7	-26.1	-35.7
Financing	24.4	31.4	20.7	18.9	13.2	29.7	26.1	35.7
Revenue Equalization and Reserve Fund	45.0	25.0	18.0	15.0	9.2	15.0	15.5	16.4
Consolidated Fund	-20.5	6.4	-8.3	0.0	0.0	0.0	0.0	0.0
Development Fund	4.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External loans (net)	-2.3	-0.7	-0.9	4.0	4.0	10.7	10.7	19.3
Other sources	-2.1	0.7	12.0	0.0	0.0	4.0	0.0	0.0
					nt of GDF			
Total revenue and grants	66.0	70.4	78.4	75.5	83.1	76.0	80.7	80.4
Revenue	40.2	42.6	42.4	41.6	49.2	38.4	43.0	42.2
Tax revenue	19.6	18.8	17.5	18.4	18.5	16.8	18.5	18.3
Nontax revenue	20.7 16.6	23.8 20.4	24.9 18.0	23.3 18.5	30.7 25.3	21.6 17.2	24.5 19.1	23.9 18.5
Of which: Fishing license fees External grants	25.8	27.8	36.0	33.9	33.9	37.6	37.6	38.2
•								
Total expenditure	81.9	90.3	91.0	87.0	91.1	92.2	94.9	98.5
Current expenditure Of which: Wages and salaries	56.2 27.1	62.5 28.5	55.0 26.3	53.1 25.8	54.8 26.8	48.8 25.4	51.5 25.4	50.5 25.3
Subsidies to public enterprises 1/	4.7	5.2	4.4	4.8	4.8	4.3	4.3	3.8
Other current expenditure	24.3	28.8	24.3	22.6	23.3	19.0	21.7	21.3
Development expenditure	25.8	27.8	36.0	33.9	36.3	43.4	43.4	48.0
Overall balance	-15.9	-19.9	-12.6	-11.5	-8.0	-16.2	-14.3	-18.1
Financing RERF	15.9 29.5	19.9 15.8	12.6 11.0	11.5 9.1	8.0 5.6	16.2 8.2	14.3 8.4	18.1 8.3
Consolidated Fund	-13.4	4.1	-5.1	0.0	0.0	0.0	0.0	0.0
Development Fund	2.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External loans (net)	-1.5	-0.4	-0.6	2.4	2.4	5.8	5.8	9.8
Other sources	-1.4	0.4	7.3	0.0	0.0	2.2	0.0	0.0
Memorandum items:								
RERF balance (in millions of Australian dollars)	637.3	561.6	570.5		576.1		579.7	590.0
RERF: Accrued income	30.0	34.2	21.6		20.8		21.8	22.8
Valuation changes	-5.5	-83.5	6.5		-4.9		-1.8	4.9
Government drawings	-45.0	-25.0	-18.0		-9.2		-15.5	-16.4
RERF balance (in percent of GDP)	423.3	417.5	347.6		349.7		316.4	299.2
Current fiscal balance (in percent of GDP, excl. grants)	-15.9	-19.9	-12.6	-11.5	-5.6	-10.4	-8.4	-8.3
Real GNI (percentage change)	-0.9	2.2	-5.0		6.6		-1.8	2.8
Real GDP (percentage change)	0.4	-1.1	-0.7	1.8	1.8	3.0	3.0	3.5

Sources: Data provided by the Kiribati authorities; and Fund staff estimates and projections.

^{1/} Includes subsidies to copra production.

^{2/} Development expenditure equals grants plus loans for development projects.

^{3/} Overall balance in the table is different from official budget because loans are classified as financing.

	2009_	2010	2011	2012	2013	2014	2015	201
				Pr	ojection	s		
aseline scenario								
Real sector								
Real GDP (percentage change)	-0.7	1.8	3.0	3.5	3.0	2.0	2.0	2.
Inflation (period average)	8.8	-2.8	7.7	5.0	3.3	2.5	2.5	2.
Nominal GDP at market prices (in millions of AU\$)	164.1	164.8	183.2	197.2	208.2	217.6	227.4	237
Government finance			(Ir	percent	t of GDP)		
Total revenue and grants	78.4	83.1	80.7	80.4	78.5	, 75.7	69.8	72
Revenue	42.4	49.2	43.0	42.2	41.6	39.7	39.6	39
External grants	36.0	33.9	37.6	38.2	36.9	36.0	30.2	33
Total expenditure and net lending	91.0	91.1	94.9	98.5	94.7	90.5	84.8	86
Current expenditure	55.0	54.8	51.5	50.5	49.7	49.1	48.4	47
Of which: Wages and salaries	26.3	26.8	25.4	25.3	25.2	25.1	25.0	24
Development expenditure	36.0	36.3	43.4	48.0	44.9	41.4	36.4	38
Overall balance	-12.6	-8.0	-14.3	-18.1	-16.2	-14.7	-15.0	-13
RERF balance (end of period; in millions of AU\$)	570.5	576.1	579.7	590.0	601.2	611.9	625.4	641
Real per capita balance (in 1996 AU\$)	4,020	3,868	3,717	3,614	3,531	3,450	3,386	3,33
, , , , , , , , , , , , , , , , , , , ,	4,020	3,000		1	1		3,300	3,30
Balance of payments	00.0	20.4		percent		•	04.0	00
Current account balance	-29.8	-23.1	-28.9 -51.2	-29.2	-26.8	-23.0	-24.6	-23
Trade balance	-47.1	-48.0		-55.4	-53.4	-50.5	-50.5	-49
Balance on services	-35.3 37.8	-32.0 44.3	-28.8	-26.9	-25.9	-25.1	-24.3	-23 35
Balance on factor income Balance on current transfers	37.8 14.8	12.5	37.6 13.4	36.7 16.4	36.5 16.0	36.7 15.9	36.6 13.7	აი 13
	14.0	12.5	13.4	10.4	10.0	15.9	13.7	13
External debt (in millions of US\$; end of period)								
External debt	14.3	18.4	27.6	43.5	57.2	66.8	78.4	89
(In percent of GDP)	9.7	11.3	17.0	25.1	32.0	36.6	41.9	45
External debt service	1.0	0.6	0.6	0.7	0.8	1.0	1.1	1
(In percent of exports of goods and services)	7.9	3.0	2.6	2.7	3.2	3.5	3.7	3
eform scenario								
Real sector								
Real GDP (percentage change)	-0.7	1.8	3.0	3.5	3.5	3.0	3.0	3.
Inflation (period average)	8.8	-2.8	7.7	4.0	3.0	2.5	2.5	2
Nominal GDP at market prices (in millions of AU\$)	164.1	164.8	183.2	197.2	209.2	220.9	233.2	246
Government finance			(Ir	percent	t of GDP)		
Total revenue and grants	78.4	83.1	80.7	86.8	84.8	82.6	76.2	77
Revenue	42.4	49.2	43.0	42.5	42.1	41.4	41.5	41
External grants	36.0	33.9	37.6	44.3	42.6	41.2	34.7	35
Total expenditure and net lending	91.0	91.1	94.9	97.1	92.3	87.8	81.5	81
Current expenditure	55.0	54.8	51.5	49.2	47.5	46.8	47.0	46
Of which: Wages and salaries	26.3	26.8	25.4	24.3	23.2	23.1	23.0	22
Development expenditure	36.0	36.3	43.4	47.9	44.8	41.0	34.4	35
Overall balance	-12.6	-8.0	-14.3	-10.3	-7.5	-5.2	-5.3	-4
RERF balance (end of period; in millions of AU\$)	570.5	576.1	579.7	593.2	610.3	630.0	651.6	678
Real per capita balance (in 1996 AU\$)	4,020	3,868	3,717	3,634	3,584	3,552	3,528	3,53
Total per capita balance (III 1000 AOW)	7,020	5,500	0,7 17	0,007	0,007	0,002	0,020	0,00
Balance of payments			•	percent		•		
Current account balance	-29.8	-22.5	-27.2	-22.6	-20.2	-16.6	-17.4	-16
Trade balance	-47.1	-48.0	-50.7	-50.8	-49.0	-46.3	-45.4	-45
Balance on services	-35.3	-31.4	-27.6	-25.2	-24.2	-23.3	-22.4	-21
Balance on factor income	37.8	44.3	37.6	37.1	37.1	37.5	37.5	37
Balance on current transfers	14.8	12.5	13.4	16.4	15.9	15.6	13.0	12
External debt (in millions of US\$; end of period)								
External debt	14.3	18.4	27.6	33.5	37.2	36.8	36.4	36
(In percent of GDP)	9.7	11.3	17.0	19.4	20.7	19.9	19.0	17
External debt service	1.0	0.6	0.6	0.7	0.7	8.0	8.0	0
(In percent of exports of goods and services)	7.9	2.9	2.3	2.3	2.3	2.3	2.2	2

Tab	le 5. Kir	ibati: B	alance	of Payr	nents, 2	2007-16	5			
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
						Pr	ojections			
				(In r	millions of	US dollars)			
Current account balance	-37.6	-46.0	-38.1	-34.1	-47.1	-50.5	-47.9	-42.0	-45.9	-46.7
Trade balance	-58.9	-65.1	-60.3	-70.6	-83.4	-95.8	-95.4	-92.3	-94.6	-97.5
Exports, f.o.b.	11.2	8.6	6.3	9.6	11.8	12.9	13.7	14.5	15.5	16.9
Imports, f.o.b.	70.0	73.7	66.6	80.2	95.2	108.7	109.1	106.8	110.1	114.4
Balance on services	-41.2	-53.2	-45.2	-47.1	-46.9	-46.6	-46.3	-45.8	-45.5	-46.0
Credit	6.1	5.1	4.8	7.5	10.2	11.7	12.2	12.7	13.2	14.0
Debit	47.3	58.3	50.0	54.6	57.0	58.3	58.5	58.5	58.7	60.0
Balance on factor income 1/	50.5	58.5	48.4	65.2	61.3	63.5	65.2	67.1	68.5	70.1
Credit	59.6	63.8	52.8	70.3	66.5	69.0	70.9	72.9	74.3	76.1
Fishing license fees	21.3	27.0	23.0	37.2	31.1	32.0	32.5	33.0	33.7	35.0
Investment income	28.4	31.0	19.2	20.9	21.8	22.5	23.3	24.0	24.1	23.4
Remittances	10.6	9.7	9.0	10.5	11.8	12.7	13.4	14.1	14.9	16.0
Debit	9.1	5.3	4.4	5.1	5.2	5.4	5.6	5.7	5.8	6.0
Balance on current transfers	11.9	13.8	18.9	18.4	21.9	28.3	28.7	29.0	25.6	26.7
Credit	16.8	18.8	23.5	24.0	28.1	34.9	35.4	35.9	32.7	34.1
Of which: Government	16.1	18.1	22.6	23.0	27.1	33.9	34.5	35.0	31.7	33.2
Debit	4.9	4.9	4.6	5.6	6.2	6.6	6.8	6.9	7.1	7.4
Of which: Government	1.3 25.8	1.2 12.1	1.1 22.1	1.4 31.2	1.6 54.0	1.7 57.6	1.7 55.5	1.8 48.0	1.8 52.7	1.9 53.2
Financial and capital account balance Government	25.8 14.9	18.2	22.1	30.8	43.7	49.2	55.5 45.8	48.0	36.4	42.0
Capital transfers	14.9	18.2	23.5	26.9	43.7 34.2	32.3	45.8 31.6	30.9	24.8	31.4
Loans (net)	-1.9	-0.6	-0.7	3.9	9.5	16.9	14.3	9.8	11.6	10.6
Direct investment	0.3	0.3	0.3	0.3	1.2	2.1	2.9	3.1	3.3	3.7
Financial institutions	10.5	-6.5	-0.9	0.0	9.1	6.3	6.8	4.2	13.0	7.6
Errors and omissions	11.4	35.1	24.3	14.4	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-0.4	1.2	8.3	11.4	6.9	7.1	7.7	6.0	6.7	6.5
Change in external assets (increase -) 2/	0.4	-1.2	-8.3	-11.4	-6.9	-7.1	-7.7	-6.0	-6.7	-6.5
Revenue Equalization Reserve Fund	14.0	-6.6	-1.8	-9.4	-4.8	-4.8	-5.3	-3.4	-4.0	-3.5
Government funds 3/	-13.6	5.4	-6.5	-2.0	-2.1	-2.3	-2.4	-2.5	-2.7	-2.9
Memorandum items:				(In percent	of GDP)				
Official external assets	435.0	368.7	365.4	368.7	334.9	317.7	307.6	300.7	295.1	290.6
(In years of imports)	4.7	3.7	4.0	4.0	3.6	3.3	3.3	3.3	3.3	3.3
Foreign reserve assets	26.0	21.0	25.3	26.6	25.2	24.7	24.8	25.1	25.4	25.8
(In months of imports of G&S)	3.4	2.5	3.3	3.5	3.2	3.1	3.2	3.3	3.4	3.5
Other assets	409.0	347.7	340.0	342.2	309.7	293.0	282.9	275.6	269.6	264.8
External debt	10.2	13.3	9.7	11.3	17.0	25.1	32.0	36.6	41.9	45.5
External debt service 4/	1.6	0.5	0.7	0.4	0.3	0.4	0.5	0.5	0.6	0.6
(In percent of exports of G&S)	11.9	5.0	7.9	3.0	2.6	2.7	3.2	3.5	3.7	3.8
Real GDP (percentage change)	0.4	-1.1	-0.7	1.8	3.0	3.5	3.0	2.0	2.0	2.0

 $Sources: \ Data\ provided\ by\ the\ Kiribati\ authorities;\ and\ Fund\ staff\ estimates\ and\ projections.$

^{1/} Includes fishing license fees, which would be shown as current transfers under conventional international guidelines.

^{2/} Excludes valuation changes.

^{3/} Comprises the Consolidated Fund, Development Fund, and STABEX Fund.

^{4/} An increase in the debt service in 2007 reflects maturity of certain external borrowing including from Japan.

	2007	2008	2009	2010	2011	2012 Pro	2013 ojections	2014	2015	2016
				,			5,000,0115			
Current account balance	-21.1	-24.1	-21.6	-16.0	In percent -21.0	-21.3	-19.6	-16.8	-18.0	-17.6
Trade balance	-33.0	-34.1	-34.2	-33.2	-37.2	-40.5	-39.1	-36.9	-37.0	-36.7
Exports, f.o.b.	6.3	4.5	3.6	4.5	5.3	5.4	5.6	5.8	6.1	6.3
Imports, f.o.b.	39.3	38.6	37.7	37.8	42.5	45.9	44.7	42.8	43.1	43.1
Balance on services	-23.1	-27.8	-25.6	-22.2	-20.9	-19.7	-19.0	-18.4	-17.8	-17.3
Credit	3.4	2.7	2.7	3.5	4.5	4.9	5.0	5.1	5.2	5.3
Debit	26.5	30.5	28.3	25.7	25.4	24.6	24.0	23.4	22.9	22.6
Balance on factor income 1/	28.3	30.6	27.5	30.7	27.3	26.9	26.7	26.9	26.8	26.4
Credit	33.4	33.4	29.9	33.1	29.7	29.1	29.1	29.2	29.1	28.6
Fishing license fees	11.9	14.1	13.0	17.5	13.9	13.5	13.3	13.2	13.2	13.2
Investment income	15.9	16.2	10.9	9.8	9.7	9.5	9.5	9.6	9.4	8.8
Remittances	5.9	5.1	5.1	4.9	5.3	5.4	5.5	5.6	5.8	6.0
Debit	5.1	2.8	2.5	2.4	2.3	2.3	2.3	2.3	2.3	2.3
Balance on current transfers Credit	6.7 9.4	7.2 9.8	10.7 13.3	8.7 11.3	9.8 12.5	12.0	11.7 14.5	11.6 14.4	10.0	10.1 12.8
Debit	9.4 2.7	9.8 2.6	2.6	2.6	2.8	14.7 2.8	2.8	2.8	12.8 2.8	2.8
Financial and capital account balance	14.4	6.3	12.5	14.7	24.1	24.3	2.8	19.2	20.6	20.0
Government	8.4	9.6	12.9	14.7	19.5	20.8	18.8	16.3	14.2	15.8
Capital transfers	9.4	9.8	13.3	12.7	15.3	13.6	12.9	12.4	9.7	11.8
Loans (net)	-1.1	-0.3	-0.4	1.9	4.2	7.2	5.9	3.9	4.5	4.0
Direct investment	0.2	0.2	0.2	0.2	0.5	0.9	1.2	1.2	1.3	1.4
Financial institutions	5.9	-3.4	-0.5	0.0	4.1	2.7	2.8	1.7	5.1	2.8
Errors and omissions	6.4	18.4	13.8	6.8	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-0.2	0.6	4.7	5.4	3.1	3.0	3.1	2.4	2.6	2.4
Change in external assets (increase -) 2/	0.2	-0.6	-4.7	-5.4	-3.1	-3.0	-3.1	-2.4	-2.6	-2.4
Revenue Equalization Reserve Fund	7.9	-3.4	-1.0	-4.4	-2.1	-2.0	-2.2	-1.4	-1.6	-1.3
Government funds 3/	-7.6	2.8	-3.7	-0.9	-1.0	-1.0	-1.0	-1.0	-1.1	-1.1
					n percent	of GDP)				
Current account balance	-29.4	-34.7	-29.8	-23.1	-28.9	-29.2	-26.8	-23.0	-24.6	-23.9
Trade balance	-46.1	-49.1	-47.1	-48.0	-51.2	-55.4	-53.4	-50.5	-50.5	-49.9
Exports, f.o.b.	8.7	6.5	4.9	6.5	7.3	7.4	7.7	8.0	8.3	8.6
Imports, f.o.b.	54.8	55.6	52.0	54.5	58.5	62.8	61.1	58.5	58.8	58.5
Balance on services	-32.2	-40.1	-35.3	-32.0	-28.8	-26.9	-25.9	-25.1	-24.3	-23.5
Credit	4.8	3.9	3.7	5.1	6.2	6.8	6.8	6.9	7.1	7.2
Debit	37.0	44.0	39.0	37.1	35.0	33.7	32.7	32.0	31.3	30.7
Balance on factor income 1/	39.5	44.1	37.8	44.3	37.6	36.7	36.5	36.7	36.6	35.8
Credit	46.6	48.1	41.3	47.8	40.8	39.8	39.7	39.9	39.7	38.9
Fishing license fees	16.6	20.4	18.0	25.3	19.1	18.5	18.2	18.1	18.0	17.9
Investment income	22.2	23.4	15.0	14.2	13.4	13.0	13.0	13.2	12.9	12.0
Remittances	8.3	7.3	7.1	7.1	7.3	7.4	7.5	7.7	8.0	8.2
Debit	7.1	4.0	3.4	3.5	3.2	3.1	3.1	3.1	3.1	3.1
Balance on current transfers	9.3	10.4	14.8	12.5	13.4	16.4	16.0	15.9	13.7	13.7
Credit	13.1	14.2	18.4	16.3	17.2	20.2	19.8	19.7	17.5	17.4
Debit	3.8	3.7	3.6	3.8	3.8	3.8	3.8	3.8	3.8	3.8
inancial and capital account balance	20.1	9.1	17.3	21.2	33.2	33.3	31.1	26.3	28.2	27.2
Government	11.7	13.8	17.8	20.9	26.8	28.4	25.7	22.3	19.4	21.5
Capital transfers	13.2	14.2	18.3	18.3	21.0	18.6	17.7	16.9	13.2	16.0
Loans (net)	-1.5	-0.4	-0.6	2.7	5.8	9.8	8.0	5.4	6.2	5.4
Direct investment	0.2	0.2	0.2	0.2	0.7	1.2	1.6	1.7	1.8	1.9
Financial institutions	8.2	-4.9	-0.7	0.0	5.6	3.7	3.8	2.3	6.9	3.9
Errors and omissions	8.9	26.5	19.0	9.7	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-0.3	0.9	6.5	7.8	4.3	4.1	4.3	3.3	3.6	3.3
Change in external assets (increase -) 2/	0.3	-0.9	-6.5	-7.8	-4.3	-4.1	-4.3	-3.3	-3.6	-3.3
Revenue Equalization Reserve Fund	11.0	-49	-1 /	-6.4	-2 9	-2 S	-2 9	-1 9	-2.2	-1 2

Sources: Data provided by the Kiribati authorities; and Fund staff estimates and projections.

11.0

-10.6

-4.9

4.1

-1.4

-5.1

-6.4

-2.9

-1.3

-2.8

-1.3

Revenue Equalization Reserve Fund

-1.8

-1.5

-2.9

-1.3

-1.9

-1.4

-2.2

-1.4

^{1/} Includes fishing license fees, which would be shown as current transfers under conventional international guidelines.

^{2/} Excludes valuation changes.

^{3/} Comprises the Consolidated Fund, Development Fund, and STABEX Fund.

APPENDIX 1: MAIN RECOMMENDATIONS OF THE 2009 ARTICLE IV CONSULTATION

Fund Recommendations 1

Fiscal policy: Staff noted that there was scope for fiscal policy to mitigate the impact of the global shocks through deficit neutral options, such as expediting or bringing forward project implementation and through well targeted social expenditure to ease the impact on the poor.

Staff suggested introducing some tax and revenue measures: strengthening the administration and merging the tax and custom offices, and establish a single tax payer identification number, as well as the adoption of a broad –based consumption tax and the introduction of excises to counterbalance the drop in custom revenues under the upcoming regional trade agreement (PICTA). Staff advised to increase fishing license fees through the use of auctions and/or collective agreements. It also advised to control expenditure by reducing wage bills.

Staff also recommended introducing a multi-year budget framework as well as a well-defined target or rule for the RERF draw-downs.

Structural reforms: Staff suggested limiting SOE operation to areas where the private sector was not viable and improving SOE performance, improving investment climate, and land tilting.

Financial sector policy: Staff recommended more competition in the financial sector to facilitate access to credit and decrease its cost. Given DBK's large NPLs, staff recommended to limit its expansion until an appropriate risk management framework is in place. Staff advised Kiribati Provident Fund (KPF) to review its investment strategy and limit dividends until its capital position is strengthened.

1/ Board Meeting of May 1, 2009.

Sources: IMF staff.

Policy Actions

Fiscal policy supported the economy during the crisis. The impact of the global crisis was stronger than anticipated at the time of the 2009 Article IV consultation as was the global recession. Consequently, deficit-neutral measures were not applicable. Copra subsidies and civil servant wages have increased.

The authorities introduced a withholding tax at the source in March 2009 (retroactive to January 2009). A PFTAC mission on tax administration will be discharged in 2011. The implementation of PICTA commitments has been postponed to 2014. To increase license fishing fees, the government introduced an auction scheme in September 2010.

A three-year budget framework was introduced in October 2009. It targets the RERF drawdown at A\$15 million per year during 2011–13.

An SOE will be privatized by May 2011 and five additional SOEs have been identified for reform later in 2011. The authorities are considering a law to ease constraints to the use of land as collateral.

The KPF introduced a lending scheme in July 2010. It also revised its investment strategy in mid-2010. There are also plans afoot to strengthen the commercial orientation of the DBK through a foreign partnership. DBK's lending activities were contained and NPLs reduced by 2 percentage points of total loans over the last two years.



INTERNATIONAL MONETARY FUND

KIRIBATI

STAFF REPORT FOR THE 2011 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

The Asia and Pacific Department (In Consultation with Other Departments)

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ANNEX I. KIRIBATI: FUND RELATIONS

(As of March 1, 2011)

Membership Status

Joined: June 3, 1986; Article VIII

General Resources Account

	SDR	Percent
	Million	Quota
Quota	5.60	100.00
Fund holdings of		
currency	5.60	100.02
Reserve position in		
Fund	0.00	0.08

SDR Department

	SDR Million	Percent Allocation
Net cumulative		
allocation	5.32	100.00
Holdings	5.34	100.21

Outstanding Purchases and Loans

None

Financial Arrangements

None.

Projected Obligations to the Fund

None.

Implementation of HIPC Initiative

Not Applicable.

Implementation of Multilateral Debt Relief Initiative (MDRI)

Not Applicable.

Exchange Rate Arrangement

The Australian dollar circulates as legal tender.

Article IV Consultation

The 2009 Article IV consultation discussions with Kiribati were held in Tarawa during February 20–28, 2009. Kiribati is on a 24–month consultation cycle.

Technical Assistance (TA), 1995–2011

STA, LEG, MCM and PFTAC have provided TA on statistics, tax administration and policy, budget management, Revenue Equalization Reserve Fund (RERF) management, financial sector reform and supervision, and combating financial crime and financial system abuse.

Resident Representative

The resident representative office in the Pacific Islands was opened in September 2010 in Suva, Fiji. Mr. Yongzheng Yang is the Resident Representative.

ANNEX II. KIRIBATI: RELATIONS WITH THE PACIFIC FINANCIAL TECHNICAL ASSISTANCE CENTRE (PFTAC)¹

(As of March, 2011)

During the current funding cycle (May 2008 to May 2011), PFTAC assistance to Kiribati has included eight advisory missions. Kiribati also sent 15 officials to regional seminars and workshops.

Tax Administration and Policy

In 2003, PFTAC recommended several reforms. These included: a value-added tax (VAT); a presumptive tax; and a single ad valorem tax on imports from non Pacific countries; simplified personal income tax (PIT); single rate of corporate income tax (CIT). A steering committee was established to manage the introduction of the reforms. In 2009, a subsequent review mission was provided to update tax recommendations.

The domestic revenue issues require to be addressed with some urgency. Compliance levels are low and the impact of trade liberalization (PICTA and the Pacific Agreement on Closer Economic Relations) is expected to reduce trade revenues by up to 15 percent. PFTAC provided support and training in customs procedures in 2009.

Although agreed to in principle little progress has been made to introduce the reforms.

¹The Pacific Financial Technical Assistance Centre (PFTAC) in Suva, Fiji is a multi-donor technical assistance (TA) institution, financed by IMF, AsDB, AusAID, and NZAID, with the IMF as Executing Agency. The Centre's aim is to build skills and institutional capacity for effective economic and financial management that can be sustained at the national level. Member countries are: Cook Islands, Federated States of Micronesia, Fiji, Kiribati, Marshall Islands, Nauru, Niue, Palau, Papua New Guinea, Samoa, Solomon Islands, Tokelau, Tonga, Tuvalu, and Vanuatu.

However, in February 2009, the cabinet approved the introduction of legislation to treat income tax deductions from salary and wages (PAYE) as a final tax.

PFTAC stands ready to assist the authorities implement the wider reforms including introduction of automated processes once the cabinet has made a firm commitment to proceed.

Public Financial Management

AusAid maintains a long-term TA program aimed at improving public sector financial and economic management. A joint PFTAC mission with Asian Development Bank (AsDB) on public financial management reform was undertaken in August 2006. Following this mission, a multi-donor mission of AusAID, PFTAC, and AsDB visited Kiribati from December 12-15, 2006. AusAID and AsDB the have taken lead in supporting implementation of the recommendations. PFTAC is ready to provide additional technical support, such as the review of IFMIS procedures undertaken in late 2009.

Financial Sector Regulation and Supervision

In August 2003, the PFTAC advisor and an IMF legal expert visited Kiribati to conduct consultations with industry and government officials on a Financial Institutions Bill that had been drafted in July 2002. No major concerns arose from the discussions. Proposed responses to comments raised in the meeting, together with appropriately amended draft legislation, were forwarded to the authorities in December 2003 for action.

In 2005, the advisor was invited to attend a government and industry workshop to discuss aspects of the Financial Institutions Bill. The mission did not proceed. However, the advisor provided authorities with papers, which highlighted the need for such legislation. To date there has been no further progress on the draft Financial Institutions Bill or the previously drafted Anti-money Laundering Legislation. The PFTAC advisor makes periodic contact with the Ministry of Finance regarding the status of the draft legislation.

Economic and Financial Statistics

GDDS metadata was published on the IMF website in April 2004, following assistance

with drafting by PFTAC. A brief mission was undertaken in August 2006 to assess TA needs. The BOP compiler benefited from training provided in regional courses in 2005 and 2010. PFTAC provided TA on balance of payments in 2008 and 2010, improving compilation methods and use of source data, as well as providing training, and helping with the transition to BPM6. PFTAC provided TA on national accounts 2008, 2009, and 2010; and assisted the authorities in making significant improvements in methodology and use of source data. The NA compiler benefited from a regional course in 2009. PFTAC also sponsored a one-month attachment for the BOP compiler with Statistics New Zealand in May 2009.

ANNEX III. KIRIBATI: BANK-FUND COLLABORATION

A. WORLD BANK-IMF COLLABORATION

The Fund Kiribati mission chief—Ms. Tumbarello—met with the World Bank team ⁷ in March 2010, in Tarawa, at the Development Partner Forum, to exchange views on the recent economic developments, identify macro structural challenges ahead and discuss a work plan to prepare the first joint debt sustainability analysis.

In September 2010, the IMF and World Bank teams held two phone conferences to coordinate the teams' work plan for the period September 2010–August 2011 (see below). Since then the teams consulted very frequently, especially on issues related to the debt sustainability analysis and the economic outlook. Bank staff joined the 2011 IMF Article IV mission in February for the first time.

There has been close cooperation on the following issues:

Macroeconomic developments and economic updates. There has been close dialogue throughout the year on macro policies and economic developments with regular sharing of information.

External debt and debt sustainability analysis. The teams have engaged very closely on discussions around government plans to borrow. Despite the existence of a wealth fund, going forward the fiscal costs of climate are expected to be substantial. They produced two joint DSAs.

The teams agreed that Kiribati's main macroeconomic challenges include:

Striking a balance between the need to preserve Kiribati's wealth fund through fiscal consolidation and the need to address the large infrastructure, health and education needs;

High vulnerability to climate change and rising sea level. An important first step is to recognize the fiscal risks involved and start building a fiscal buffer—with the assistance of international donors—and to consider the implications for expenditure programs.

The teams have indentified the reform of the state-owned enterprises as s a macro-critical structural reform.

The teams agreed to continue the close cooperation going forward. The following table details the specific activities planned by the two country teams over the period September 2010–August 2011. The Fund will continue to lead on macro issues, and the Bank will continue to lead on macro critical structural reform issues. The Bank and the Fund closely cooperated in preparing a joint DSA, also in consultation with the Asian Development Bank and in the run-up of the IMF 2011 Article IV.

Structural reform. The Bank program will support reforms related to telecoms liberalization, strengthening road maintenance arrangements, improving returns from fisheries resources, the operation of the import levy fund given the liberalization of food import arrangements. The Bank agreed to update the Fund on developments in these areas as needed.

⁷ The World Bank team was represented by Mr. Jauncey. The World Bank Country Director is Mr. Belhaj.

Kiribati: World Bank-Fund Planned Activities in Macro-critical Areas (September 2010–August 2011)					
Title	Products	Provisional Timing	Expected Delivery		
1. Bank Work	Adaptation to climate		Ongoing		
Program	change		FY11 ongoing		
	Road maintenance project		1111011501115		
	Ministrum asti Ainm and		FY11 ongoing		
	Kiritimati Airport Rehabilitation		Ongoing		
	Support for temporary migrant labor schemes		FY11 ongoing		
	illigiant labor schemes		1 111 Oligoliig		
	Telecoms regulatory				
	support for market liberalization		Ongoing		
	Country Assistance Strategy		Board meeting March 2011		
2. Fund Work	2011, Article IV Consultation	February 2011	(accomplished) Board May 2, 2011		
Program	2011, Article IV Consultation	rebluary 2011	Board May 2, 2011		
, and the second	Strengthening the Financial	September 7-17	October 2010 (report finalized)		
	Management of the				
	Revenue Equalization Reserve Fund				
			FY 2011		
		FY 2011			
	TA BOP mission				
3. Joint Work Program	First DSA	October-December 2010	Issuance to the board February 2011 (accomplished)		
Hogiani	Updated DSA	March 2011 for the 2011	Issuance to the board (April		
	•	IMF Article IV	2011)		

B. RELATIONS WITH THE WORLD BANK GROUP¹ (As of March 1, 2011)

Kiribati became a member of the World Bank Group in 1986.

On March 1, 2011, the World Bank's Board of Executive Directors discussed the first Country Assistance Strategy (CAS) for Kiribati, which had previously been covered by a Pacific Islands Regional Engagement Framework. The CAS is structured around the themes of: (i) addressing the existential threat

posed by climate change; and, (ii) mitigating the effects of geographic isolation.

The CAS anticipates a significantly expanded program of advisory and financial support for Kiribati. Consistent with Kiribati's limited repayment capacity highlighted in the DSA, it is anticipated that IDA financing will be provided on 100-percent grant terms. IDA grants and trust fund investments of as much as US\$50 million are anticipated over the four year CAS period from FY11 to FY14. Such a program of investments is intended to build a

¹ Prepared by World Bank staff.

foundation for the World Bank to play a more substantive role, in close collaboration with the IMF and other donor partners, in a coordinated economic policy dialogue with the Government of Kiribati.

Key components of proposed World Bank Group engagement include:

Climate change adaptation and building resilience against shocks is at the core of Bank engagement in Kiribati. The Bank, with trust fund has been financing, supporting climate change mitigation since 2003 through the Kiribati Adaptation Program (KAP). Staff anticipates seeking Board agreement in mid-2011 to enlarge and extend activities under KAP Phase 3. Trust fund financing of US\$7-10 million has been agreed in principle for KAP 3 from GEF, GFDRR, Australia, and, potentially, Zealand. This will involve a significant scale up compared to previous phases. Activities will focus on seawalls, mangrove planting, and water conservation and supply. In addition to KAP, the Bank is proposing to work with the government and other donors to consider options for an integrated program in the water sector, which is the key issue where the climate change and development agendas intersect in Kiribati. Kiribati's already limited supply of fresh water adversely affects development outcomes, and population growth and the impact of climate change is likely to put further pressure on this critical resource. Beyond climate change adaptation, the Bank is committed to accelerating efforts to address wider issues of vulnerability in Kiribati, including accessing trust

fund resources to improve renewable energy generation to reduce reliance on volatile imported diesel, and to support the transport of food to remote outer islands.

- Mitigating the effects of geographic isolation. Given Kiribati's remoteness, the Bank anticipates scaling up support for climate friendly infrastructure investments. A South road improvement Tarawa investment of US\$24m in IDA and TF financing—to be undertaken jointly with the AsDB—was approved by the Board on March 1, 2011, with the Kiribati CAS. The Bank is also considering options, in collaboration with New Zealand and other partners, to help bring Kiribati airports – a vital link with the outside world - up to international safety standards.
- Supporting economic reform and regional integration. An expanded program of investments will provide a foundation for a more substantive engagement by the Bank Group in a coordinated economic policy dialogue in Kiribati. Bank staff, for instance, joined the IMF Article IV mission in 2011 for the first time. Reform of the large and inefficient state owned enterprise sector will be especially important to improve services and to reduce the fiscal costs to the budget from such enterprises. The AsDB, with support from Australia, has to date led efforts to support the government to develop a legal and regulatory framework for reforming SOEs. Building on this, the Bank Group anticipates supporting government efforts to open the telecoms market

to new private investments. As well as the direct benefits, telecoms reform has elsewhere in the Pacific proven to be especially successful in building public support and momentum for reform more broadly. The Bank and IFC will cooperate closely in supporting telecoms reform, in providing advisory services more broadly, and on other potential SOE transactions. As well as domestic

reform, the Bank Group continues to support efforts by Kiribati and other Pacific Island Countries to gain benefits from greater regional integration, including participation in temporary labor migration schemes established by New Zealand and Australia and anticipated analytical support to help countries improve management and returns from the pelagic fishery.

ANNEX IV. KIRIBATI: RELATIONS WITH THE ASIAN DEVELOPMENT BANK ¹

(As of February, 2011)

The Asian Development Bank has approved seven project loans to Kiribati amounting to US\$27.14 million, all from Asian Development Fund (ADF) resources since Kiribati joined the AsDB in 1974. In addition, TA amounting to US\$13.9 million has been provided for 41 projects. The latest AsDB loan to Kiribati, for a road rehabilitation project, was approved in December 2010. The AsDB most recently approved an US\$0.85 million TA grant for Tarawa Sanitation Improvement in October 2009 and a supplementary of US\$0.2 million for the same TA in December 2010.

The strategy of the AsDB in Kiribati directly supports the government's Kiribati Development Plan (KDP) 2008–11. Further, AsDB's approach is anchored in the mid-term review of the Pacific Strategy, which put a stronger emphasis on issues of supporting a conducive environment for private sector development, good governance, and capacity

development. Rapid population growth and urban migration has left Kiribati with overcrowded urban areas, and its most pressing development challenges are social and environmental concerns, including the impacts of climate change, access to clean water and sanitation, and the spread of HIV/AIDS. AsDB supports the government's efforts to balance growth more evenly throughout the country through TA for the Integrated Land and Population Development Program on Kiritimati Island. AsDB supports also efforts to improve the government's financial management through TA for Economic Management and Public Sector Reform recognizing the sizeable constraint the poor performance of public enterprises is placing on government ability to fund needed goods and services.

Kiribati: Loan, Grant ar	nd Technical .	Assistance A	pprovals, (2	005–10)		
	2005	2006	2007	2008	2009	2010
Loan approvals						
Number	0	0	0	0	0	1
Amount (US\$m)	0	0	0	0	0	12
Grant approvals						
Number	0	0	0	0	0	0
Amount (US\$m)	0	0	0	0	0	0
TA approvals						
Number	0	1	0	1	1	1
Amount (US\$m)	0	0.63	0	0.8	0.85	0.2

^{1/} Prepared by Asian Development Bank Staff.

ANNEX V. KIRIBATI—STATISTICAL ISSUES

(Assessment of Data Adequacy for Surveillance, as of April 4, 2011)

General: Data provision has some shortcomings, but is broadly adequate for surveillance. Balance of Payments data are the most affected area.

National Accounts: With PTFAC assistance, GDP estimates have been significantly improved. Three TA missions from STA took place in January 2009 and 2010 and in April 2011 to improve national account data and revised estimates through 2009. However, further capacity building would be needed to continue to improve the quality of GDP estimates. So far, estimates are limited to Gross Domestic Product (GDP) at current and constant 2006 prices, using the production approach. There are no expenditure-based GDP estimates. Also, unemployment indicators are not regularly available. PFTAC has also recommended that the statistics authorities work more closely with other agencies (e.g., tax authorities, public enterprises).

Price statistics: The monthly retail price index (1996=100) is produced with a short lag (about a month), based on a survey in the capital (a national index is not available). There are no producer, wholesale, or trade price indices.

Government finance statistics: The budget outcome is available with a lag of about a year. Currently, a provisional budget outcome for 2008 is available. There are misclassifications in the current statistics, which have been identified by PFTAC. Audited financial statements of public enterprises are not available.

Monetary statistics: The balance sheets of all the financial institutions (Bank of Kiribati,

Development Bank of Kiribati, Kiribati Provident Fund, and Kiribati Insurance Corporation) are available with lags, but the consolidated balance sheet of the financial sector is not available. Data on interest rates are reported with a long lag.

Balance of payments: The quality of the data has been improved with recent PFTAC assistance. However, there still remain some shortcomings: i) external statistics are reported with a long delay (about a year or more), ii) there are large errors and omissions in some years, which appear to partly reflect the underestimation of private transfers, iii) and there are some inconsistencies between the balance of payments data and budget data. A PFTAC mission took place in April 2010. The mission revised the BOP estimates up to 2007, and updating estimates to end 2009. As in the case of GDP data, PFTAC has suggested the need for further statistical capacity building.

Data Standards and Quality

Kiribati has been a participant in the General Data Dissemination System (GDDS) since 2004.

No data ROSC are available.

Reporting to STA (Optional)

No data are currently reported to STA for publication in the *Government Finance Statistics Yearbook*, the *Balance of Payments Statistics Yearbook* or in the *IFS*.

Kiribati: Table of Common Indicato	ors Required f	or Surveill	ance		
	Date of latest observation	Date Received	Frequency of Data ⁷	Frequency of Reporting ⁷	Frequency of Publication ⁷
Exchange Rates	4/04/11	4/04/11	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities	12/31/10	02/18/11	М	Α	NA
Reserve/Base Money	NA	NA	NA	NA	NA
Broad Money	NA	NA	NA	NA	NA
Central Bank Balance Sheet	NA	NA	NA	NA	NA
Consolidated Balance Sheet of the Banking System	NA	NA	NA	NA	NA
Interest Rates ²	12/31/09	1/3/2011	Α	Α	I
Consumer Price Index	12/10	2/19/11	M	Q	Q
Revenue, Expenditure, Balance and Composition of Financing ³ – General Government ⁴	12/31/10	2/19/11	Α	Α	I
Revenue, Expenditure, Balance and Composition of Financing ³ – Central Government	12/31/10	2/19/11	Α	Α	I
Stocks of Central Government and Central Government-Guaranteed Debt ⁵	12/31/10	2/19/11	Α	А	I
External Current Account Balance	12/31/09	2/18/11	Α	Α	1
Exports and Imports of Goods and Services	12/31/10	3/11	Α	Α	1
GDP/GNP	12/31/09	2/18/11	Α	Α	ı
Gross External Debt	12/31/10	2/18/11	Α	Α	1
International Investment Position ⁶	12/31/10	2/18/11	Α	Α	1

¹ Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

2 Both market-based and officially-determined, including discounts rates, money market rates, rates on treasury bills, notes and bonds.

³ Foreign, domestic bank, and domestic nonbank financing.

⁴ The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

Including currency and maturity composition.

⁶ Includes external gross financial asset and liability positions vis-à-vis nonresidents.

⁷ Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).



INTERNATIONAL MONETARY FUND

KIRIBATI

April 18, 2011

JOINT IMF/WORLD BANK DEBT SUSTAINABILITY ANALYSIS 2011¹

Approved By

Kenneth Kang and Thomas Dorsey (IMF) Vikram Nehru and Jeffrey D. Lewis (WB)

Prepared By

The International Monetary Fund and The World Bank

Kiribati continues to be at high risk of debt distress according to this new debt sustainability analysis (DSA). Containing the risk of debt distress will require prudent financing by continuing to secure grants to support the country's large development needs, fiscal consolidation, and stepping up the implementation of the structural reform agenda to raise long-term growth.

-

¹ This DSA has been produced in consultation with the Asian Development Bank (AsDB). It is based on the common standard LIC DSA framework. Under the Country Policy and Institutional Assessment (CPIA), Kiribati is rated as a weak performer, and the DSA uses the indicative threshold indicators on the external public debt for countries in this category: 30 percent for the present value (PV) of debt-to-GDP ratio; 100 percent for the PV of debt-to exports ratio; 200 percent for the PV of debt-to-revenue ratio; 15 percent for the debt service-to-exports ratio; and 25 percent for the debt service-to-revenue ratio.

I. BACKGROUND

- 1. This DSA reflects Kiribati's latest external financing arrangements, economic outlook, and revisions of historical data. Key changes in assumptions from the DSA issued in February 2011 are: 1) access to World Bank grant financing from IDA (US\$20 million) for the 2011 fiscal year, whereas in early 2011 all IDA financing was assumed to be offered as concessional loans; 2) an increase in IDA loan allocation compared to the previous DSA by US\$25 million. This reflects IDA's recent decision to double the base allocation to all IDA countries which has resulted in an increased IDA envelope of an additional SDR 3 million annually for Kiribati. It also incorporates an anticipated US\$11million in regional IDA funds for a regional aviation safety investment; 3) improved economic prospects over the next 2-3 years taking into account new projects, including Tarawa's port rehabilitation financed with grants (US\$45 million) and a fish processing joint-venture; and 4) a slightly improved fiscal outlook due to higher fishing license fees following the introduction of an auction scheme in 2010. In addition, this analysis adopts the latest authorities' balance of payment (BOP) series revised with the assistance of Pacific Financial Technical Assistance Centre (PFTAC).
- The fiscal stance has deteriorated in the last few years and the value of Kiribati's wealth fund has declined substantially. Large fiscal

- deficits over the last decade (about 12 percent of GDP on average) have resulted in substantial draw downs of the Revenue Reserve Equlization

 Fund (RERF)—the main source of deficit financing.² The value of RERF assets dropped to AU\$570 million or 350 percent of GDP in 2009, and interest income and dividends have also fallen from 20 percent of GDP in 2008 to only 12 percent in GDP in 2009.
- 3. The medium-term macroeconomic outlook has improved compared to the previous DSA, although risks to the outlook remain. Early reading of 2010 data suggests that the recovery is underway. The economy is estimated to have grown by about 2 percent in 2010. The fiscal deficit is estimated to have narrowed to 8 percent of GDP in 2010 driven by stronger than anticipated revenue, following the introduction of a fisheries license auction scheme as well as some temporary factors. Going forward, key public projects—the rehabilitation of Tarawa's road, airport and port-financed with external assistance should support growth in the 2–3 percent range over the medium term. However, the economy is still vulnerable to rising international food and fuel prices in the short term and climate change in the long term. Further

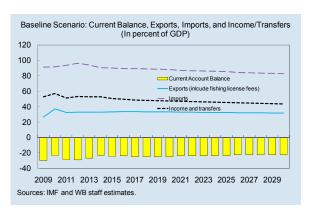
² The RERF is a wealth fund established in 1956 and was capitalized using phosphate mining proceeds. Phosphate deposits were exhausted in 1979.

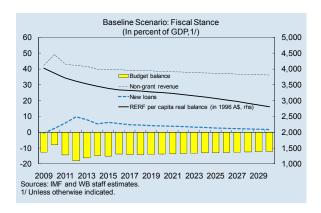
fiscal and structural reforms are necessary going forward.

- 4. As of end-2009, domestic debt accounted for about 20 percent of GDP, while gross external debt was estimated at less than 10 percent of GDP (Table 1). Domestic debt includes the publicly guaranteed debt of the SOEs. As of end-
- 2009, all external public debt consisted of concessional loans from the AsDB.
- 5. Yet fiscal risks are likely to increase in the upcoming years. Uncertainty about aid flows and fiscal costs associated with climate change are likely to impose further pressures on Kiribati's fiscal position.

II. EXTERNAL AND PUBLIC DEBT SUSTAINABILITY ANALYSIS

6. Under the baseline scenario, Kiribati is drawing down its financial resources. The fiscal balance, after deteriorating initially, is projected to improve somewhat in the longer term. The fiscal deficit is projected to be about 12 percent of GDP by 2030, taking into account costs of climate change of about 1½ percent of GDP. The deficit is assumed partly financed through an US\$10 million of loans, on average, each year, with the remaining financing gap closed through draw-downs of RERF. Annual drawdown from the RERF is projected to be 10 percent of GDP on average. As a result, the real per capita RERF balance would decline, reaching only about two thirds of its 2009 per capita value in 2030 (or onethird of its 2000 per capita value). macroeconomic assumptions underlying the baseline scenario are presented in Box 1.





External Debt Sustainability Analysis

high risk of debt distress. Under the baseline scenario (Table 3a), although Kiribati does not face a liquidity problem (Figure 1, d and e) with the debt service indicators remaining low, a breach of the thresholds of the present value (PV) of debt-to-exports ratio and of the PV of the debt to GDP ratio takes place starting around 2020 (Figure 1, b and c). This outcome is the result of the large increase in PV of external debt in the next few years due to disbursements from both multilateral and bilateral partners. This will raise the PV of external debt from about 7 percent of

GDP in 2009 to above 30 percent of GDP starting in 2019, and the PV of external debt reaching over 100 percent of exports (including fishing license fees) starting in 2020.³

8. Sensitivity analysis suggests that debt path is particularly vulnerable to shocks to exports and to financing terms (Table 3b, and Figure 1). The exports shock, defined as a lower exports growth at about one standard deviation less than the historical average in 2011-12, would take the PV of debt to exports ratio to about 210 percent in 2030 (Table 3b). Kiribati's debt path is also very sensitive to the assumption on the terms of new borrowing. A 200-basis point increase in the interest rate on new borrowing would result in a severe breach of the thresholds on both PV of debt to GDP ratio and PV of debt to exports ratio (Figure 1).

9. Continuing to avoid new borrowing is necessary for Kiribati to prevent external debt distress. The economy does not have sufficient sources of external income to afford large amounts of concessional loans.

Public Debt Sustainability Analysis

10. Public debt analysis paints a similar picture. In addition to the external debt, public debt includes guaranteed loans for state-owned enterprises of about 20 percent of GDP as of end-2009. Under the baseline scenario, the net present value of total public debt will reach above 40 percent of GDP, driven by external borrowings. Public debt sustainability is vulnerable to shocks as well. Under the most extreme stress test scenario—real GDP growth being one standard deviation temporarily lower in 2011–2012—the present value of debt reaches 87 percent of GDP by 2030 (Table 2, scenario B1).

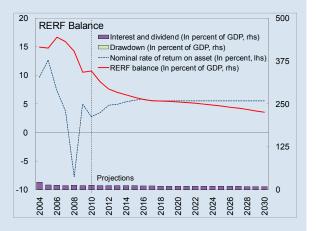
³ As a measure of sustainability, fishing license fees are included in the export ratio.

Box 1 Macroeconomic Assumptions Under the Baseline Scenario

- **GDP growth and population**. Large infrastructure investments supported by external loans are expected to boost real growth to about 2–3½ percent in the medium term. Growth will moderate to 1½ percent over the longer term. Population growth (net of migration) is projected to increase by 1.6 percent per year.
- New loan disbursements are assumed to amount to about US\$50 million—27 percent of GDP—over the next four years. This amount includes lending on concessional terms from the World Bank and non-concessional lending from other development partners. These loans will finance the rehabilitation of Tarawa's main road and airport, as well as projects to adapt to the adverse impacts of climate change. Over the longer term, additional concessional borrowing amounting to US\$10 million per year related to climate change expenditure is assumed starting in 2015.
- Aid flows and FDI. Aid flows are expected to pick up over the medium term with main donors increasing ODA allocations. In the long term, aid flows decline slightly in terms of GDP, assuming that the main donors (AusAID, NZAID, Japan, EU, and Taiwan Province of China) do not reduce their envelopes (Table 5). FDI will slowly increase over the next twenty years, reflecting foreign equity participation in fish processing projects.
- The fiscal deficit after widening to 14.3 percent of GDP in 2011 is expected to narrow under current policies (Table 6). The deterioration in the near term reflects the loan-financed increase in infrastructure spending and a decline of fishing license fees from 2010. Over the longer term, the fiscal balance is projected to revert to historical averages (about 12–13 percent of GDP) once the

key infrastructure projects have occurred. However, fiscal costs of climate change, assumed to be roughly 1½ percent of GDP each year in the long term will continue to put pressure on the budget. Fiscal deficits are expected to be financed by a combination of RERF draw-downs and external loans.

- The current account deficit is projected to deteriorate in 2011, mainly reflecting large imports related to infrastructure projects in the pipeline. Over the medium and long term, the balance is expected to improve compared to 2009 due to a narrowing fiscal deficit.
- The average nominal return on the RERF assets is projected at 5½ percent. The drawdown from RERF (i.e., flow) each year equals the fiscal deficit net of external financing. Under current policies, the RERF balance is projected to decline to 216 percent of GDP by 2030 (down from 350 percent of GDP in 2009).

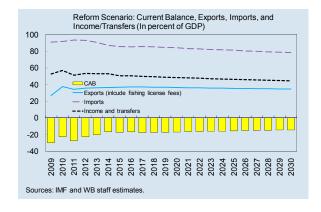


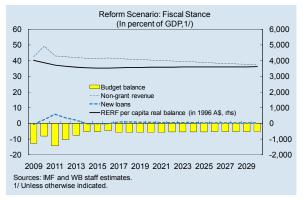
^{1/} Nicholls and Toll estimated coastal protection costs at 1–2 percent of GDP per year in some of the most affected PICs. See, 2006, "Impacts and Responses to Sea-Level Rise," *Philosophical Transactions of the Royal Society."*

III. THE REFORM SCENARIO

- 11. The risk of debt distress could be reduced to "low" under the reform scenario (Figure 3 and Table 4). The reform scenario envisages fiscal consolidation, grant financing, and the implementation of structural reforms.
- 12. To better anchor fiscal plans, under this scenario, an explicit fiscal rule is applied: preserving the real per capita value of the RERF at its 2014 level (once the infrastructure projects are completed). This would require limiting fiscal deficits to 5–6 percent of GDP, on average, starting in 2014.
- 13. The underlying assumptions underpinning the fiscal policy advice to stabilize the value of the RERF in real per capita terms are as follows: the nominal rate of return on the RERF is about 5½ percent in the long term; population growth is 1.6 percent per year and inflation is 2½ percent. Thus, to preserve the real per capita balance of the RERF the nominal RERF balance would have to grow by about 4 percent per year (2½ percent inflation plus 1.6 percent population growth), implying a yearly nominal draw-down of about 1½ percent of the **RERF** total

balance.⁵ Current expenditure would also be reduced, mainly through cuts in wage bill and subsidies.





14. A greater proportion of Kiribati's development financing needs are projected to be met by grants rather than loans (Tables 5a and 6a). Over the medium term, the reform scenario assumes that the World Bank would only offer grants. Over the long term, external loan financing is assumed to be about US\$21/2 million each year compared to US\$10 million in the baseline scenario.

⁴ SOE guaranteed debt is assumed to be constant in nominal terms over the projection period. It implies that SOE fiscal losses are assumed to be equivalent to the amount of SOE debt following falling due each year.

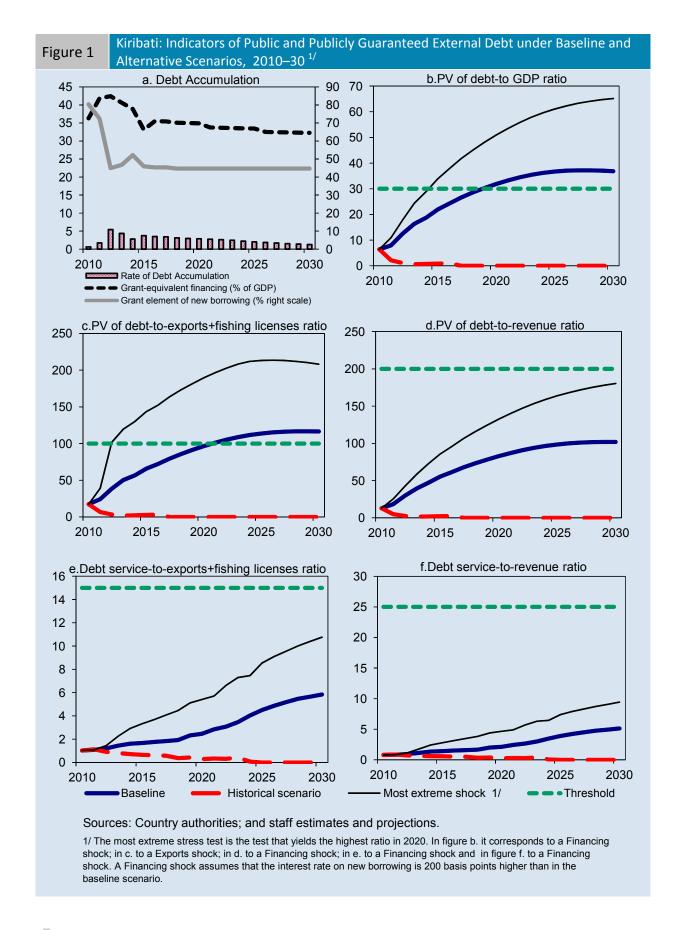
⁵ Because nominal GDP growth is about 5 percent per year over the long run (2½ real growth plus 2½ inflation rate), the RERF balance as a percentage of GDP declines over the long term, despite remaining constant in real per capita value.

15. The implementation of the structural reform agenda is accelerated under the reform scenario. Public enterprise reform would be combined with reforms to increase private sector opportunities. There would be a better utilization

of marine resources that would result in higher fiscal revenue and higher economic growth. As a result of these assumptions none of the thresholds are breached in this scenario.

IV. CONCLUSIONS

- 16. Kiribati is at high risk of debt distress. Continuing to secure grant financing instead of loans as well as substantial fiscal adjustment is key to ensuring debt sustainability. While the RERF assets mitigate the risks of debt distress in the medium term, given the large uncertainties regarding the fiscal costs of climate change, the RERF should be continued to be used as a buffer against substantial external shocks.
- **17.** Narrowing fiscal deficits will also be **necessary.** A simple fiscal rule capping the real per capita value of the RERF at the end of the medium term would be key to ensure fiscal sustainability and appropriate for intergenerational fairness as the RERF was established with royalties from a nonrenewable resource. In light of continued pressures from climate change and large infrastructure needs, keeping current expenditures in check and improving customs administration to broaden the tax base will be important. Continued efforts to strengthen the multi-year budget framework with the assistance of the AsDB and the IMF would also provide fiscal discipline and help ensure debt sustainability.
- 18. Growth-supporting structural reforms can mitigate the downward pressure of fiscal tightening and enhance sustainability in the long term. These include: improving the business environment by streamlining the process of starting a business and expanding access to credit; improving access to land through improved administration; and reforming state—owned enterprises to create space for private sector development and reduce the drain on the budget.
- with this assessment. They are fully committed to continuing taking steps to preserve the value of the RERF. On the revenue side, they plan to improve tax administration (merging tax and custom offices) and introduce the VAT over the medium term. On the expenditure side, they are committed to control expenditure by reforming state-owned enterprises (SOEs). Reform of SOEs will reduce their burden on the budget while supporting private sector development.



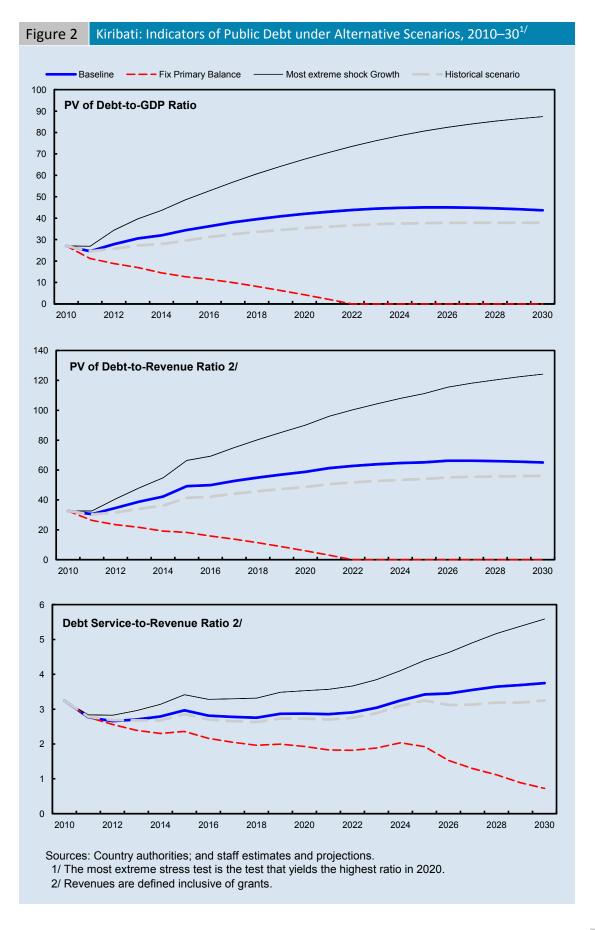


Table 1. Kiribati: Public Sector Debt Sustainability Framework, Baseline Scenario, 2007–30 1/

(In percent of GDP, unless otherwise indicated)

		Actual				Estimate					Projectio	ons			
				Average 6/	Standard							2010-15			2016-30
	2007	2008	2009	Average of	Deviation 6/	2010	2011	2012	2013	2014	2015	Average	2020	2030	Average
Public sector debt 1/	32.5	34.8	30.5			31.9	33.6	40.4	46.2	49.8	54.3		66.0	66.2	
o/w foreign-currency denominated	10.2	13.3	9.7			11.3	17.0	25.1	32.0	36.6	41.9		55.8	59.4	
Change in public sector debt	-2.3	2.3	-4.4			1.5	1.7	6.8	5.7	3.7	4.5		1.6	-0.9	
Identified debt-creating flows	13.2	21.5	8.4			6.9	12.2	15.9	14.6	13.4	13.5		11.2	9.5	
Primary deficit	13.2	17.2	9.8	11.8	6.9	5.6	12.3	16.2	14.3	12.8	13.1	12.4	12.0	10.9	11.6
Revenue and grants	66.0	70.4	78.4			83.1	80.7	80.4	78.5	75.7	69.8		71.4	67.1	
of which: grants	25.8	27.8	36.0			33.9	37.6	38.2	36.9	36.0	30.2		32.9	30.9	
Primary (noninterest) expenditure	79.2	87.7	88.2			88.6	92.9	96.6	92.8	88.6	82.9		83.4	78.0	
Automatic debt dynamics	0.0	4.3	-1.4			1.4	-0.1	-0.3	0.3	0.6	0.4		-0.7	-1.4	
Contribution from interest rate/growth differential	1.3	1.8	2.0			2.1	-0.6	-0.1	0.0	0.1	0.0		-0.4	-1.0	
of which: contribution from average real interest rate	1.5	1.5	1.7			2.6	0.4	1.1	1.2	1.0	0.9		0.5	0.0	
of which: contribution from real GDP growth	-0.1	0.4	0.2			-0.5	-0.9	-1.1	-1.2	-0.9	-1.0		-1.0	-1.0	
Contribution from real exchange rate depreciation	-1.3	2.5	-3.4			-0.7	0.5	-0.2	0.3	0.4	0.5				
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes 2/	-15.5	-19.2	-12.8			-5.5	-10.5	-9.1	-8.8	-9.8	-9.0		-9.7	-10.5	
Other Sustainability Indicators															
PV of public sector debt	22.3	21.6	27.3			27.1	24.6	27.8	30.5	32.0	34.4		42.0	43.7	
o/w foreign-currency denominated	0.0	0.0	6.6			6.4	7.9	12.5	16.4	18.7	21.9		31.9	36.8	
o/w external			6.6			6.4	7.9	12.5	16.4	18.7	21.9		31.9	36.8	
PV of contingent liabilities (not included in public sector debt)															
Gross financing need 3/	17.4	20.3	13.2			8.3	14.5	18.3	16.4	14.9	15.2		14.0	13.4	
PV of public sector debt-to-revenue and grants ratio (in percent)	33.8	30.6	34.9			32.6	30.5	34.6	38.9	42.2	49.2		58.8	65.1	
PV of public sector debt-to-revenue ratio (in percent)	55.4	50.6	64.5			55.0	57.2	66.0	73.4	80.6	86.7		109.2	120.8	
o/w external 4/			15.5			13.0	18.4	29.8	39.4	47.2	55.4		82.9	101.9	
Debt service-to-revenue and grants ratio (in percent) 5/	6.5	4.4	4.3			3.2	2.8	2.7	2.7	2.8	3.0		2.9	3.7	
Debt service-to-revenue ratio (in percent) 5/	10.6	7.2	7.9			5.5	5.2	5.1	5.1	5.3	5.2		5.3	7.0	
Primary deficit that stabilizes the debt-to-GDP ratio	15.5	14.9	14.2			4.1	10.6	9.4	8.5	9.2	8.6		10.4	11.8	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	0.4	-1.1	-0.7	1.8	3.7	1.8	3.0	3.5	3.0	2.0	2.0	2.5	1.5	1.5	1.5
Average nominal interest rate on forex debt (in percent)	1.1	1.0	1.1	1.0	0.1	1.3	1.0	1.0	1.0	1.0	1.0	1.1	1.0	1.0	1.0
Average real interest rate on domestic debt (in percent)	7.1	7.1	7.9	7.4	0.5	12.7	1.9	7.0	8.7	8.9	9.2	8.1	9.4	7.0	8.2
Real exchange rate depreciation (in percent, + indicates depreciation)	-11.6	24.4	-25.5	-1.7	17.5	-7.5									
Inflation rate (GDP deflator, in percent)	4.5	4.5	4.6	2.5	3.7	-1.4	8.0	4.0	2.5	2.5	2.5	3.0	2.5	2.5	2.5
Growth of real primary spending (deflated by GDP deflator, in percent)	-0.1	0.1	0.0	0.0	0.1	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grant element of new external borrowing (in percent)						80.4	72.4	45.0	46.8	52.2	46.0	57.1	44.7	44.7	

Sources: Country authorities; and staff estimates and projections.

^{1/} Public sector includes central government and nonfinancial public sector. Gross debt is used. Inloudes AUD\$34 million of public enterprise loans guaranteed by the government.

^{2/} Large residuals reflect RERF drawdowns, and capital transfers to the government.

^{3/} Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

^{4/} Revenues excluding grants.

^{5/} Debt service is defined as the sum of interest and amortization of medium and long-term debt.

^{6/} Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

				Project	ions			
	2010	2011	2012	2013	2014	2015	2020	2030
PV of Debt-to-GDP Ratio	27							
Baseline	27	25	28	31	32	34	42	44
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages A2. Primary balance is unchanged from 2010	27	21	19	17	14	13	35 4	38
A3. Permanently lower GDP growth 1/	27	25	29	32	35	38	55	86
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012				40			68	87
B2. Primary balance is at historical average minus one standard deviations in 2011-2012							46	47
B3. Combination of B1-B2 using one half standard deviation shocks							56	69
B4. One-time 30 percent real depreciation in 2011							35	36
B5. 10 percent of GDP increase in other debt-creating flows in 2011	27	30	33	35	37	39	47	48
PV of Debt-to-Revenue Ratio 2/								
Baseline	33	31	35	39	42	49	59	65
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	33	30	32	34	36	41	49	56
A2. Primary balance is unchanged from 2010	33	26	23	22	19	18	6	(
A3. Permanently lower GDP growth 1/	33	31	36	41	45	54	74	119
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	33	33	41	48	55	66	90	124
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	33	35	40	45	48	56	65	71
B3. Combination of B1-B2 using one half standard deviation shocks							76	100
B4. One-time 30 percent real depreciation in 2011							49	54
B5. 10 percent of GDP increase in other debt-creating flows in 2011	33	37	41	45	49	56	66	71
Debt Service-to-Revenue Ratio 2	1							
Baseline	3.2	2.8	2.7	2.7	2.8	3.0	2.9	3.7
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	3.2	2.8	2.7	2.7	2.7	2.9	2.7	3.2
A2. Primary balance is unchanged from 2010							1.9	0.7
A3. Permanently lower GDP growth 1/	3.2						3.2	5.1
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	3.2	2.8	2.8	3.0	3.1	3.4	3.5	5.6
B2. Primary balance is at historical average minus one standard deviations in 2011-2012							3.0	4.1
DE. I filliary balance is at historical average fillings one standard deviations in 2011-2012							3.2	4.8
B3. Combination of B1-B2 using one half standard deviation shocks	3.2	7 X	/ ~	/ ~				
B3. Combination of B1-B2 using one half standard deviation shocks B4. One-time 30 percent real depreciation in 2011							3.5	5.3

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

Table 3a. External Debt Sustainability Framework, Baseline Scenario, 2007–30 ¹

(In percent of GDP, unless otherwise indicated)

		Actual		Historical	Standard			Project	ions						
				Average 6/	Deviation 6/							2010-2015			2016-2030
	2007	2008	2009			2010	2011	2012	2013	2014	2015	Average	2020	2030	Average
External debt (nominal) 1/	10.2	13.3	9.7			11.3	17.0	25.1	32.0	36.6	41.9		55.8	59.4	
o/w public and publicly guaranteed (PPG)	10.2	13.3	9.7			11.3	17.0	25.1	32.0	36.6	41.9		55.8	59.4	
Change in external debt	-1.2	3.1	-3.6			1.5	5.7	8.2	6.9	4.6	5.3		2.0	-0.7	
Identified net debt-creating flows	27.6	34.1	30.1			22.8	27.9	27.4	24.4	20.7	22.1		27.0	22.4	
Non-interest current account deficit	29.3	34.6	29.7	17.3	19.1	23.0	28.8	29.0	26.5	22.7	24.2		29.6	26.8	27.9
Deficit in balance of goods and services	61.6	68.9	64.4			54.7	60.9	63.8	61.1	57.5	56.8		55.2	51.3	
Exports	30.1	30.8	26.7			36.9	32.6	32.6	32.6	33.0	33.3		33.0	31.6	
Imports	91.8	99.6	91.1			91.6	93.5	96.5	93.8	90.5	90.2		88.2	82.9	
Net current transfers (negative = inflow)	-9.3	-10.4	-14.8	-16.6	4.8	-12.5	-13.4	-16.4	-16.0	-15.9	-13.7		-13.7	-13.7	-13.7
o/w official	-11.6	-12.8	-16.8			-14.7	-15.7	-18.6	-18.3	-18.2	-16.0		-16.0	-16.0	
Other current account flows (negative = net inflow)	-23.0	-23.8	-20.0			-19.1	-18.6	-18.4	-18.6	-19.0	-18.9		-11.9	-10.8	0.0
Net FDI (negative = inflow)	-0.2	-0.2	-0.2	-0.2	0.4	-0.2	-0.7	-1.2	-1.6	-1.7	-1.8		-2.4	-4.1	-2.9
Endogenous debt dynamics 2/	-1.5	-0.3	0.6			0.0	-0.2	-0.4	-0.5	-0.3	-0.4		-0.3	-0.3	
Contribution from nominal interest rate	0.1	0.1	0.2 0.1			0.1 -0.2	0.1	0.2	0.3	0.3	0.3		0.5	0.6	
Contribution from real GDP growth	0.0	0.1	0.1				-0.3	-0.6	-0.7	-0.6	-0.7		-0.8	-0.9	
Contribution from price and exchange rate changes	-1.6 -28.8	-0.5 -31.0	-33.6			24.2	-22.2	40.2	47.6	46.4	-16.7		25.0	-23.1	
Residual (3-4) 3/	0.0	0.0	0.0			-21.2 0.0	0.0	-19.3 0.0	- 17.6 0.0	-16.1 0.0	0.0		-25.0 0.0	0.0	
o/w exceptional financing	0.0	0.0													
PV of external debt 4/			6.6			6.4	7.9	12.5	16.4	18.7	21.9		31.9	36.8	
In percent of exports			24.7			17.3	24.4	38.4	50.1	56.8	65.7		96.5	116.4	
PV of PPG external debt			6.6			6.4	7.9	12.5	16.4	18.7	21.9		31.9	36.8	
In percent of exports			24.7			17.3	24.4	38.4	50.1	56.8	65.7		96.5	116.4	
In percent of government revenues			15.5			13.0	18.4	29.8	39.4	47.2	55.4		82.9	101.9	
Debt service-to-exports ratio (in percent)	5.3	1.7	2.6			1.0	1.1	1.2	1.4	1.6	1.7		2.5	5.9	
PPG debt service-to-exports ratio (in percent)	5.3	1.7	2.6			1.0	1.1	1.2	1.4	1.6	1.7		2.5	5.9	
PPG debt service-to-revenue ratio (in percent)	4.0	1.2	1.6			0.8	0.8	0.9	1.1	1.3	1.4		2.1	5.1	
Total gross financing need (Millions of U.S. dollars)	39.2	46.2	38.6			34.1	46.3	48.8	45.4	39.3	43.0		64.4	83.7	
Non-interest current account deficit that stabilizes debt ratio	30.5	31.5	33.2			21.5	23.1	20.9	19.6	18.1	18.9		27.7	27.5	
Key macroeconomic assumptions															
Real GDP growth (in percent)	0.4	-1.1	-0.7	1.8	3.7	1.8	3.0	3.5	3.0	2.0	2.0	2.5	1.5	1.5	1.5
GDP deflator in US dollar terms (change in percent)	16.1	4.8	-2.8	4.8	10.4	13.0	7.4	2.7	0.2	0.3	0.5	4.0	2.5	2.5	2.5
Effective interest rate (percent) 5/	1.1	1.0	1.1	1.0	0.1	1.3	1.0	1.0	1.0	1.0	1.0	1.1	1.0	1.0	1.0
Growth of exports of G&S (US dollar terms, in percent)	46.5	5.8	-16.3	1.6	19.5	59.4	-2.4	6.5	3.2	3.3	3.6	12.3	3.5	3.6	3.7
Growth of imports of G&S (US dollar terms, in percent)	24.1	12.5	-11.7	8.6	17.0	15.7	12.9	9.7	0.4	-1.4	2.1	6.6	3.6	3.6	3.5
Grant element of new public sector borrowing (in percent)						80.4	72.4	45.0	46.8	52.2	46.0	57.1	44.7	44.7	44.8
Government revenues (excluding grants, in percent of GDP)	40.2	42.6	42.4			49.2	43.0	42.2	41.6	39.7	39.6		38.5	36.1	37.8
Aid flows (in Millions of US dollars) 7/	32.9	36.9	46.1			54.4	69.2	76.2	76.0	75.8	64.5		81.5	111.4	
o/w Grants	32.9	36.9	46.1			49.9	61.3	66.2	66.0	65.8	56.5		75.5	105.4	
o/w Concessional loans	0.0	0.0	0.0			4.5	8.0	10.0	10.0	10.0	8.0		6.0	6.0	
Grant-equivalent financing (in percent of GDP) 8/						36.3	41.9	42.5	40.6	38.9	33.1		34.9	32.3	33.7
Grant-equivalent financing (in percent of external financing) 8/						98.4	96.3	89.1	90.6	93.7	90.5		93.5	95.2	93.9
Memorandum items:															
Nominal GDP (Millions of US dollars)	127.9	132.5	128.0			147.2	162.9	173.1	178.7	182.6	187.1		229.1	340.4	
Nominal dollar GDP growth	16.6	3.6	-3.4			15.0	10.6	6.3	3.2	2.2	2.5	6.6	4.0	4.0	4.1
PV of PPG external debt (in Millions of US dollars)			9.7			10.4	12.9	21.7	29.2	34.2	41.0		73.1	125.4	
(PVt-PVt-1)/GDPt-1 (in percent)						0.6	1.7	5.7	4.3	2.8	3.7	3.1	2.9	1.2	2.4
Gross workers' remittances (Millions of US dollars)	10.6	9.7	9.0			10.5	11.8	12.7	13.4	14.1	14.9		19.6	29.1	
PV of PPG external debt (in percent of GDP + remittances)			6.1			6.0	7.4	11.7	15.2	17.4	20.3		29.4	33.9	
PV of PPG external debt (in percent of exports + remittances)			19.5			14.5	19.9	31.4	40.8	46.0	53.1		76.7	91.6	
Debt service of PPG external debt (in percent of exports + remittances)			2.0			0.9	0.9	1.0	1.2	1.3	1.4		2.0	4.6	

Sources: Country authorities; and staff estimates and projections.

^{1/} Includes both public and private sector external debt.

^{2/} Derived as $[r - g - \rho(1+g)]/(1+g+\rho+g\rho)$ times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and $\rho =$ growth rate of GDP deflator in U.S. dollar terms.

^{3/} Large residuals reflect RERF drawdowns; government capital transfers; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

^{4/} Assumes that PV of private sector debt is equivalent to its face value.

^{5/} Current-year interest payments divided by previous period debt stock.

^{6/} Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

^{7/} Defined as grants, concessional loans, and debt relief.

^{8/} Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 3b. Kirib

Kiribati: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2010–30

(In percent)

				Project				
	2010	2011	2012	2013	2014	2015	2020	2030
PV of debt-to GDP rat	tio							
Baseline	6	8	13	16	19	22	32	37
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/ A2. New public sector loans on less favorable terms in 2010-2030 2/	6 6	2 11	1 18	1 24	1 29	1 34	0 51	0 65
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012 B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/ B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012 B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/ B5. Combination of B1-B4 using one-half standard deviation shocks B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	6 6 6 6	8 11 9 9 11 11	14 22 16 17 24 17	18 25 20 21 29 23	21 28 23 23 32 26	24 31 27 27 36 30	35 41 39 36 47 44	41 43 46 40 50 51
PV of debt-to-exports+fishing li	censes r	atio						
Baseline	17	24	38	50	57	66	97	116
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/ A2. New public sector loans on less favorable terms in 2010-2030 2/	17 17	7 34	3 55	2 75	2 88	3 102	0 154	0 206
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012 B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/ B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012 B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/ B5. Combination of B1-B4 using one-half standard deviation shocks B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	17 17 17 17 17 17	24 39 24 29 32 24	38 102 38 52 78 38	50 120 50 64 92 50	57 130 57 71 100 57	66 144 66 80 111 66	97 190 97 110 148 97	116 208 116 126 164 116
PV of debt-to-revenue	atio							
Baseline	13	18	30	39	47	55	83	102
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/ A2. New public sector loans on less favorable terms in 2010-2030 2/	13 13	5 25	3 43	2 59	2 73	2 86	0 132	0 180
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012 B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/ B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012 B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/ B5. Combination of B1-B4 using one-half standard deviation shocks B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	13 13 13 13 13	19 25 21 22 25 26	33 51 37 41 58 41	44 61 49 50 70 55	52 70 58 59 80 66	61 78 69 67 90	92 105 103 94 123 115	113 118 126 110 138 141
50. One time to personal norminal depreciation relative to the passine in 2011 of	13	20	71	- 55	- 00	- ' '	113	141

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Company Comp								
Company Comp								
Baseline	Continued Cont				6			
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	1	1	1	1	1	1	0	0
								11
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	1	1	1	1	2	2	2	6
					3			11
	1	1	1	1	2	2	2	6
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	1	1	1		2	2	3	7
	1						-	9
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	1	1	1	1	2	2	2	6
Debt service-to-revenue	ratio							
Baseline	1	1	1	1	1	1	2	5
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	1	1	1	1	1	1	0	0
			1					9
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	1	1	1	1	1	2	2	6
	1	1	1					6
	-	-	-					6
		-		-				6
								7
Bb. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	1	1	1	2	2	2	3	7
	46	46	46	46	46	46	46	46
Craft Comen assumed on residual intaneing (i.e., intaneing required above baseline) of	70	70	70	70	70	70	70	70

Sources: Country authorities; and staff estimates and projections.

^{1/} Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows. Under this scenario PV of debt reduces to zero due to increases in reserve assets.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the

shock (implicitly assuming an offsetting adjustment in import levels).

^{4/} Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

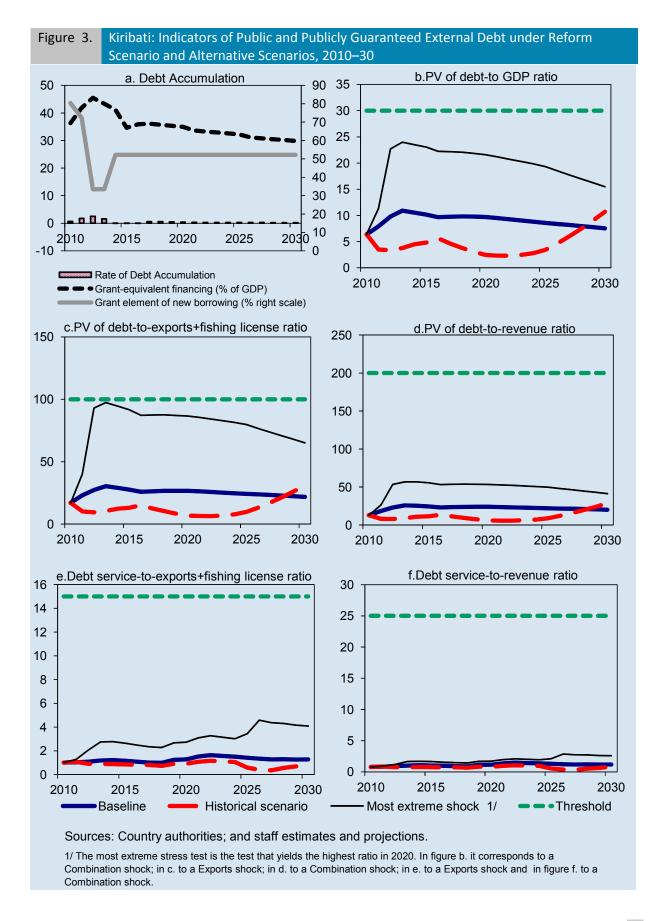


Table 4. External Debt Sustainability Framework, Reform Scenario, 2007-30 1/

(In percent of GDP, unless otherwise indicated)

		Actual		Historical	Standard			Projecti	ons						
	2007	2008	2009	Average 6	/ Deviation 6/	2010	2011	2012	2013	2014	2015	2010-2015 Average	2020	2030	2016-2030 Average
Fudamal dabé (naminal) 4/												Average			Average
External debt (nominal) 1/	10.2	13.3	9.7			11.3	17.0	19.4	20.7	19.9	19.0		17.9	14.4	
o/w public and publicly guaranteed (PPG)	10.2	13.3	9.7			11.3	17.0	19.4	20.7	19.9	19.0		17.9	14.4	
Change in external debt	-1.2	3.1	-3.6			1.5	5.7	2.4	1.4	-0.9	-0.9		-0.1	-0.4	
Identified net debt-creating flows	27.6	34.1	30.1	47.0	40.4	22.1	26.2	20.9	17.9	14.3	15.1		18.1	13.0	10.0
Non-interest current account deficit Deficit in balance of goods and services	29.3 61.6	34.6 68.9	29.7 64.4	17.3	19.1	22.4 54.1	27.1 59.2	22.5 57.2	20.0 54.5	16.3 50.8	17.2 48.9		20.6 47.7	17.4 43.8	19.0
· ·	30.1	30.8	26.7			37.5	34.3	35.7	36.0	36.4	36.8		36.4	34.6	
Exports Imports	91.8	99.6	91.1			91.6	93.5	93.0	90.4	87.1	85.7		84.2	78.4	
Net current transfers (negative = inflow)	-9.3	-10.4	-14.8	-16.6	4.8	-12.5	-13.4	-16.4	-15.9	-15.6	-13.0		-13.0	-13.0	-13.0
o/w official	-9.3 -11.6	-10.4	-14.8	-10.0	4.0	-12.5 -14.7	-15.4 -15.7	-18.6	-18.2	-17.9	-15.0		-15.0	-15.3	-13.0
Other current account flows (negative = net inflow)	-11.0	-12.8	-20.0			-14.7	-13.7	-18.4	-18.5	-17.9	-13.3		-13.3	-13.4	
Net FDI (negative = inflow)	-23.0 - 0.2	-23.6 - 0.2	-20.0 - 0.2	-0.2	0.4	-19.1 - 0.2	-10.0 - 0.7	-10.4 - 1.2	-16.5 - 1.6	-10.0 - 1.7	-10.7 - 1.7		-14.1	-13.4 - 4.2	-2.9
Endogenous debt dynamics 2/	-1.5	-0.2	0.6	-0.2	0.4	0.0	-0.7	-0.4	-0.4	-0.4	-1.7 -0.4		-0.2	-4.2	-2.9
Contribution from nominal interest rate	0.1	0.1	0.0			0.0	0.1	0.2	0.2	0.2	0.2		0.2	0.1	
Contribution from real GDP growth	0.0	0.1	0.2			-0.2	-0.3	-0.6	-0.7	-0.6	-0.6		-0.4	-0.4	
Contribution from price and exchange rate changes	-1.6	-0.5	0.1												
Residual (3-4) 3/	-1.0 -28.8	-0.5 - 31.0	-33.6			-20.6	-20.5	-18.5	-16.6	-15.2	-16.0		-18.2	-13.4	
o/w exceptional financing	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
, v	0.0	0.0													
PV of external debt 4/			6.6			6.4	7.9	9.8	10.9	10.5	10.2		9.7	7.5	
In percent of exports			24.7			17.0	23.2	27.4	30.3	29.0	27.6		26.6	21.8	
PV of PPG external debt			6.6			6.4	7.9	9.8	10.9	10.5	10.2		9.7	7.5	
In percent of exports			24.7			17.0	23.2	27.4	30.3	29.0	27.6		26.6	21.8	
In percent of government revenues			15.5			13.0	18.5	23.0	25.9	25.4	24.5		24.0	20.1	
Debt service-to-exports ratio (in percent)	5.3	1.7	2.6			1.0	1.0	1.1	1.2	1.2	1.2		1.3	1.3	
PPG debt service-to-exports ratio (in percent)	5.3	1.7	2.6			1.0	1.0	1.1	1.2	1.2	1.2		1.3	1.3	
PPG debt service-to-revenue ratio (in percent)	4.0	1.2	1.6			0.8	0.8	0.9	1.0	1.1	1.0		1.2	1.2	
Total gross financing need (Millions of U.S. dollars)	39.2	46.2	38.6			33.2	43.5	37.5	33.8	28.0	30.5		46.1	54.8	
Non-interest current account deficit that stabilizes debt ratio	30.5	31.5	33.2			20.9	21.4	20.1	18.6	17.2	18.1		20.8	17.8	
Key macroeconomic assumptions															
Real GDP growth (in percent)	0.4	-1.1	-0.7	1.8	3.7	1.8	3.0	3.5	3.5	3.0	3.0	3.0	2.5	2.5	2.5
GDP deflator in US dollar terms (change in percent)	16.1	4.8	-2.8	4.8	10.4	13.0	7.4	2.7	0.2	0.3	0.5	4.0	2.5	2.5	2.5
Effective interest rate (percent) 5/	1.1	1.0	1.1	1.0	0.1	1.3	1.0	1.0	1.1	1.2	1.2	1.1	1.1	0.9	1.0
Growth of exports of G&S (US dollar terms, in percent)	46.5	5.8	-16.3	1.6	19.5	62.0	1.1	10.7	4.4	4.4	4.7	14.5	4.4	4.6	4.6
Growth of imports of G&S (US dollar terms, in percent)	24.1	12.5	-11.7	8.6	17.0	15.7	12.9	5.7	0.9	-0.5	1.8	6.1	4.5	4.5	4.4
Grant element of new public sector borrowing (in percent)						80.4	72.4	33.5	33.5	52.2	52.2	54.0	52.2	52.2	52.2
Government revenues (excluding grants, in percent of GDP)	40.2	42.6	42.4			49.2	43.0	42.5	42.1	41.4	41.5		40.4	37.4	39.5
Aid flows (in Millions of US dollars) 7/	32.9	36.9	46.1			54.4	69.2	76.7	76.5	76.3	66.5		87.1	121.3	
o/w Grants	32.9	36.9	46.1			49.9	61.3	76.7	76.5	76.3	66.5		84.6	118.8	
o/w Concessional loans	0.0	0.0	0.0			4.5	8.0	0.0	0.0	0.0	0.0		2.5	2.5	
Grant-equivalent financing (in percent of GDP) 8/						36.3	41.9	45.5	43.4	41.2	34.7		35.0	29.8	33.0
Grant-equivalent financing (in percent of external financing) 8/						98.4	96.3	95.0	96.6	100.0	100.0		98.6	99.0	98.8
Memorandum items:															
Nominal GDP (Millions of US dollars)	127.9	132.5	128.0			147.2	162.9	173.1	179.5	185.4	191.9		245.7	402.5	
Nominal dollar GDP growth	16.6	3.6	-3.4			15.0	10.6	6.3	3.7	3.3	3.5	7.1	5.1	5.1	5.1
PV of PPG external debt (in Millions of US dollars)			9.7			10.4	12.9	16.9	19.6	19.5	19.5		23.8	30.4	
(PVt-PVt-1)/GDPt-1 (in percent)						0.6	1.7	2.5	1.5	0.0	0.0	1.0	0.4	0.2	0.3
Gross workers' remittances (Millions of US dollars)	10.6	9.7	9.0			10.5	11.8	12.7	13.4	14.1	14.9		20.5	33.6	
PV of PPG external debt (in percent of GDP + remittances)			6.1			6.0	7.4	9.1	10.1	9.8	9.4		8.9	7.0	
PV of PPG external debt (in percent of exports + remittances)			19.5			14.3	19.1	22.7	25.1	24.0	22.8		21.6	17.6	
Debt service of PPG external debt (in percent of exports + remittances)			2.0			0.9	0.9	0.9	1.0	1.0	1.0		1.0	1.0	

Sources: Country authorities; and staff estimates and projections.

^{1/} Includes both public and private sector external debt.

^{2/} Derived as $[r \cdot g - \rho(1+q)]/(1+q+\rho+q\rho)$ times previous period debt ratio, with r = nominal interest rate; q = real GDP growth rate, and $\rho =$ growth rate of GDP deflator in U.S. dollar terms.

^{3/} Large residuals reflect RERF drawdowns; government capital transfers; and valuation adjustments. The size of residuals in 2011-2015 is close to baseline, but the composition has changed: drawdowns from RERF are smaller, but capital transfers are larger due to increased grants.

^{4/} Assumes that PV of private sector debt is equivalent to its face value.

^{5/} Current-year interest payments divided by previous period debt stock.

^{6/} Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

^{7/} Defined as grants, concessional loans, and debt relief.

^{8/} Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 5. Kiribati: Balance of Pay	/ments	, Base	line S	cenari	o, 200	7-30												
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017 rojections	2018	2019	2020	2022	2025	2027	2030
										PI	ojections							
								(1	n percent	of GDP)								
Current account balance	-29.4	-34.7	-29.8	-23.1	-28.9	-29.2	-26.8	-23.0	-24.6	-23.9	-24.3	-24.3	-24.3	-24.3	-23.3	-23.3	-22.6	-22.6
Trade balance Exports, f.o.b.	-46.1 8.7	-49.1 6.5	-47.1 4.9	-48.0 6.5	-51.2 7.3	-55.4 7.4	-53.4 7.7	-50.5 8.0	-50.5 8.3	-49.9 8.6	-49.4 8.7	-49.1 8.8	-48.8 8.9	-48.5 9.0	-47.2 9.2	-46.2 9.4	-45.1 9.6	-44.1 9.9
Imports, f.o.b.	54.8	55.6	52.0	54.5	58.5	62.8	61.1	58.5	58.8	58.5	58.1	57.9	57.7	57.4	56.3	55.7	9.6 54.7	9.9 54.0
Balance on services	-32.2	-40.1	-35.3	-32.0	-28.8	-26.9	-25.9	-25.1	-24.3	-23.5	-23.3	-23.2	-23.1	-23.0	-22.4	-22.1	-21.6	-21.3
Credit	4.8	3.9	3.7	5.1	6.2	6.8	6.8	6.9	7.1	7.2	7.2	7.2	7.2	7.2	7.2	7.2	7.2	7.2
Debit	37.0	44.0	39.0	37.1	35.0	33.7	32.7	32.0	31.3	30.7	30.5	30.4	30.3	30.2	29.6	29.3	28.8	28.5
Balance on factor income 1/ Credit	39.5 46.6	44.1 48.1	37.8 41.3	44.3 47.8	37.6 40.8	36.7 39.8	36.5 39.7	36.7 39.9	36.6 39.7	35.8 38.9	34.8 38.0	34.3 37.6	33.9 37.2	33.5 36.8	32.6 35.9	31.3 34.7	30.4 33.8	29.1 32.4
Fishing license fees	16.6	20.4	18.0	25.3	19.1	18.5	18.2	18.1	18.0	17.9	17.7	17.4	17.1	16.9	16.4	15.7	15.2	14.5
Investment income	22.2	23.4 7.3	15.0	14.2 7.1	13.4 7.3	13.0 7.4	13.0 7.5	13.2 7.7	12.9	12.0 8.2	11.8 8.6	11.6 8.6	11.5 8.6	11.3 8.6	11.0 8.6	10.4 8.6	10.0 8.6	9.3
Remittances Debit	8.3 7.1	7.3 4.0	7.1 3.4	3.5	3.2	3.1	7.5 3.1	3.1	8.0 3.1	3.1	3.2	3.2	3.2	3.3	3.3	3.3	3.3	8.6 3.3
Balance on current transfers	9.3	10.4	14.8	12.5	13.4	16.4	16.0	15.9	13.7	13.7	13.7	13.7	13.7	13.7	13.7	13.7	13.7	13.7
Credit	13.1	14.2	18.4	16.3	17.2	20.2	19.8	19.7	17.5	17.4	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5
Of which: Government Debit	12.6 3.8	13.7 3.7	17.7 3.6	15.6 3.8	16.6 3.8	19.6 3.8	19.3 3.8	19.1 3.8	17.0 3.8	17.0 3.8	17.0 3.8	17.0 3.8	17.0 3.8	17.0 3.8	17.0 3.8	17.0 3.8	17.0 3.8	17.0 3.8
Of which:G overnment	1.0	0.9	0.9	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Financial and capital account balance	20.1	9.1	17.3	21.2	33.2	33.3	31.1	26.3	28.2	27.2	28.5	28.3	27.9	27.6	26.0	24.9	23.5	22.6
Government Capital transfers	11.7 13.2	13.8 14.2	17.8 18.3	20.9 18.3	26.8 21.0	28.4 18.6	25.7 17.7	22.3 16.9	19.4 13.2	21.5 16.0	19.8 16.0	19.6 16.0	19.3 16.0	19.2 16.0	17.7 14.9	16.9 14.9	15.6 14.0	15.1 14.0
Loans (net)	-1.5	-0.4	-0.6	2.7	5.8	9.8	8.0	5.4	6.2	5.4	3.7	3.6	3.4	3.2	2.8	2.0	1.6	1.1
Direct investment	0.2 8.2	0.2 -4.9	0.2	0.2	0.7 5.6	1.2 3.7	1.6 3.8	1.7 2.3	1.8	1.9 3.9	2.0	2.1 6.6	2.2 6.3	2.4	2.6 5.7	3.1	3.5	4.1
Financial institutions and others Errors and omissions	8.9	26.5	-0.7 19.0	9.7	0.0	0.0	0.0	0.0	6.9 0.0	0.0	6.8 0.0	0.0	0.0	6.1 0.0	0.0	4.9 0.0	4.4 0.0	3.4 0.0
Overall balance	-0.3	0.9	6.5	7.8	4.3	4.1	4.3	3.3	3.6	3.3	4.2	3.9	3.6	3.3	2.7	1.6	0.0	-0.1
Change in external assets (increase -) 2/	0.3	-0.9	-6.5	-7.8	-4.3	-4.1	-4.3	-3.3	-3.6	-3.3	-4.2	-3.9	-3.6	-3.3	-2.7	-1.6	-0.9	0.1
Revenue Equalization Reserve Fund	11.0	-4.9	-1.4	-6.4	-2.9	-2.8	-2.9	-1.9	-2.2	-1.8	-4.2	-3.9	-3.6	-3.3	-2.7	-1.6	-0.9	0.1
Government funds 3/	-10.6	4.1	-5.1	-1.4	-1.3	-1.3	-1.3	-1.4	-1.4	-1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items: Official external assets	435.0	368.7	365.4	368.7	334.9	317.7	307.6	300.7	295.1	290.6	286.1	282.9	279.5	276.0	268.1	254.4	244.1	227.2
(In years of imports of goods and services)	4.7	3.7	4.0	4.0	3.6	3.3	3.3	3.3	3.3	3.3	3.2	3.2	3.2	3.2	3.1	3.0	2.9	2.8
Foreign reserve assets (In months of imports of goods and services)	26.0 3.4	21.0 2.5	25.3 3.3	26.6 3.5	25.2 3.2	24.7 3.1	24.8 3.2	25.1 3.3	25.4 3.4	25.8 3.5	23.4 3.2	22.5 3.1	21.6 2.9	20.8 2.8	19.2 2.7	17.0 2.4	15.7 2.3	14.0 2.0
(In months of imports of goods and services) Other assets	409.0	347.7	340.0	342.2	309.7	293.0	282.9	275.6	269.6	264.8	262.7	260.5	257.9	255.2	248.9	237.4	228.4	213.3
External debt 4/	10.2	13.3	9.7	11.3	17.0	25.1	32.0	36.6	41.9	45.5	49.0	51.6	53.9	55.8	58.8	60.9	60.9	59.4
External debt service 5/ (In percent of exports of goods and services)	1.6 11.9	0.5 5.0	0.7 7.9	0.4 3.0	0.3 2.6	0.4 2.7	0.5 3.2	0.5 3.5	0.6 3.7	0.6 3.8	0.6 3.9	0.6 4.0	0.8 4.8	0.8 5.1	1.0 6.2	1.5 8.8	1.7 9.9	1.9 10.8
Real GDP Growth	0.4	-1.1	-0.7	1.8	3.0	3.5	3.0	2.0	2.0	2.0	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5

Sources: Data provided by the Kiribati authorities; and Fund staff estimates and projections.

1/ Includes fishing license fees, which would be shown as current transfers under conventional international guidelines.

2/ Excludes valuation changes.

3/ Comprises the Consolidated Fund, Development Fund, and STABEX Fund.

4/ External debt at end–2002 is adjusted by \$A 3.2 million reflecting forgiven debt.

5/ An increase in the debt service in 2007 reflects maturity of certain external borrowing including from Japan.



INTERNATIONAL MONETARY FUND

Table 5a Kiribati: Balance of P	aymen	ts, Re	form S	Scenar	io, 20	007–3	0											
	2007	2008	2009_	2010	2011	2012	2013	2014	2015	2016 Pr	2017 ojections	2018	2019	2020	2022	2025	2027	2030
								(1	n percent	of GDP)								
Current account balance	-29.4	-34.7	-29.8	-22.5	-27.2	-22.6	-20.2	-16.6	-17.4	-16.4	-17.6	-17.4	-17.3	-17.1	-16.2	-15.7	-14.9	-14.4
Trade balance	-46.1	-49.1	-47.1	-48.0	-50.7	-50.8	-49.0	-46.3	-45.4	-45.4	-45.6	-45.2	-44.8	-44.4	-43.3	-42.2	-41.2	-40.1
Exports, f.o.b. Imports, f.o.b.	8.7 54.8	6.5 55.6	4.9 52.0	6.5 54.5	7.8 58.5	8.5 59.3	8.7 57.8	9.0 55.3	9.2 54.7	9.5 54.9	9.7 55.2	9.8 55.0	9.9 54.7	10.0 54.4	10.2 53.5	10.5 52.7	10.7 51.8	11.0 51.1
Balance on services	-32.2	-40.1	-35.3	-31.4	-27.6	-25.2	-24.2	-23.3	-22.4	-21.6	-21.7	-21.5	-21.3	-21.1	-20.4	-19.8	-19.2	-18.6
Credit	4.8	3.9	3.7	5.7	7.4	8.4	8.4	8.5	8.6	8.6	8.7	8.7	8.7	8.7	8.7	8.7	8.7	8.7
Debit	37.0	44.0	39.0	37.1	35.0	33.7	32.7	31.8	31.0	30.2	30.4	30.2	30.0	29.8	29.1	28.5	27.8	27.3
Balance on factor income 1/ Credit	39.5 46.6	44.1 48.1	37.8 41.3	44.3 47.8	37.6 40.8	37.1 40.2	37.1 40.2	37.5 40.5	37.5 40.4	37.5 40.4	36.8 39.7	36.3 39.3	35.9 38.8	35.4 38.4	34.6 37.5	33.3 36.2	32.5 35.4	31.3 34.2
Fishing license fees	16.6	20.4	18.0	25.3	19.1	18.8	18.8	18.9	18.9	19.0	18.8	18.4	18.1	17.8	17.2	16.3	15.7	14.9
Investment income	22.2	23.4	15.0	14.2	13.4	13.0	13.0	13.1	12.9	12.7	12.6	12.5	12.4	12.2	12.0	11.6	11.3	11.0
Remittances Debit	8.3 7.1	7.3 4.0	7.1 3.4	7.1 3.5	7.3 3.2	7.4 3.1	7.5 3.1	7.6 3.1	7.8 3.0	7.9 2.9	8.3 3.0	8.3 2.9						
Balance on current transfers	9.3	10.4	14.8	12.5	13.4	16.4	15.9	15.6	13.0	12.9	13.0	13.0	13.0	13.0	13.0	13.0	13.0	13.0
Credit	13.1	14.2	18.4	16.3	17.2	20.2	19.7	19.4	16.8	16.7	16.8	16.8	16.8	16.8	16.8	16.8	16.8	16.8
Of which: Government Debit	12.6 3.8	13.7 3.7	17.7 3.6	15.6 3.8	16.6 3.8	19.6 3.8	19.2 3.8	18.9 3.8	16.3 3.8	16.3 3.8	16.3 3.8	16.3 3.8	16.3 3.8	16.3 3.8	16.3 3.8	16.3 3.8	16.3 3.8	16.3 3.8
Of which:G overnment	1.0	0.9	0.9	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Financial and capital account balance	20.1	9.1	17.3	21.2	31.5	28.3	27.3	23.8	24.3	24.0	24.9	24.6	24.3	24.0	22.6	21.9	20.9	20.2
Government Capital transfers	11.7 13.2	13.8 14.2	17.8 18.3	20.9 18.3	26.8 21.0	28.3 24.7	25.6 23.4	22.1 22.3	18.2 18.4	19.2 19.4	20.2 19.2	19.8 18.9	19.3 18.5	18.9 18.2	17.0 16.5	16.0 15.5	14.6 14.2	13.6 13.3
Loans (net)	-1.5	-0.4	-0.6	2.7	5.8	3.6	2.1	-0.2	-0.2	-0.2	1.0	1.0	8.0	0.7	0.5	0.4	0.4	0.3
Direct investment Financial institutions and others	0.2 8.2	0.2 -4.9	0.2 -0.7	0.2 0.0	0.7 3.9	1.2 -1.2	1.6 0.1	1.7 0.0	1.7 4.4	1.8 2.9	1.9 2.7	2.1 2.8	2.2 2.8	2.3 2.8	2.6 3.0	3.1 2.8	3.5 2.8	4.2 2.4
Errors and omissions	8.9	26.5	19.0	9.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-0.3	0.9	6.5	7.8	4.3	5.7	7.1	7.2	6.9	7.5	7.4	7.2	7.0	6.9	6.5	6.2	6.0	5.7
Change in external assets (increase -) 2/	0.3	-0.9	-6.5	-7.8	-4.3	-5.7	-7.1	-7.2	-6.9	-7.5	-7.4	-7.2	-7.0	-6.9	-6.5	-6.2	-6.0	-5.7
Revenue Equalization Reserve Fund	11.0	-4.9	-1.4	-6.4	-2.9	-4.4	-5.7	-5.9	-5.5	-6.1	-7.4	-7.2	-7.0	-6.9	-6.5	-6.2	-6.0	-5.7
Government funds 3/	-10.6	4.1	-5.1	-1.4	-1.3	-1.3	-1.3	-1.4	-1.4	-1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items: Official external assets	435.0	368.7	365.4	368.7	334.9	319.3	310.5	304.4	299.0	295.7	293.4	291.1	288.7	286.2	281.0	272.9	267.6	259.7
(In years of imports of goods and services)	4.7	3.7	4.0	4.0	3.6	3.4	3.4	3.5	3.5	3.5	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.3
Foreign reserve assets	26.0	21.0	25.3	26.6	25.2	24.7	24.6	24.7	24.8	24.9	22.5	21.4	20.3	19.4	17.5	15.1	13.7	11.8
(In months of imports of goods and services) Other assets	3.4 409.0	2.5 347.7	3.3 340.0	3.5 342.2	3.2 309.7	3.2 294.6	3.3 285.8	3.4 279.7	3.5 274.2	3.5 270.8	3.1 270.9	3.0 269.7	2.9 268.4	2.8 266.9	2.6 263.4	2.2 257.8	2.1 253.9	1.8 247.8
External debt 4/	10.2	13.3	9.7	11.3	17.0	19.4	20.7	19.9	19.0	17.8	18.0	18.1	18.0	17.9	17.3	16.2	15.5	14.4
External debt service 5/ (In percent of exports of goods and services)	1.6 11.9	0.5 5.0	0.7 7.9	0.4 2.9	0.3 2.3	0.4 2.3	0.4 2.3	0.4 2.3	0.4 2.2	0.4 2.1	0.4 2.1	0.4 2.0	0.5 2.5	0.5 2.5	0.6 3.1	0.5 2.6	0.5 2.3	0.4 2.2
Real GDP Growth	0.4	-1.1	-0.7	1.8	3.0	3.5	3.5	3.0	3.0	3.0	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5

Sources: Data provided by the Kiribati authorities; and Fund staff estimates and projections.

^{1/} Includes fishing license fees, which would be shown as current transfers under conventional international guidelines.

^{2/} Excludes valuation changes.

^{3/} Comprises the Consolidated Fund, Development Fund, and STABEX Fund.

^{4/} External debt at end–2002 is adjusted by \$A 3.2 million reflecting forgiven debt.

^{5/} An increase in the debt service in 2007 reflects maturity of certain external borrowing including from Japan.

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2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020 2022 2025 2027																		
	2007	2008	2009_	2010	2011	2012	2013	2014	2015		2017 rojection		2019	2020	2022	2025	2027	2030
								(In milli	one of A	ustralian								
otal revenue and grants	100.9	111.3	128.7	136.9	147.8	158.5	163.5	164.8	158.7	172.3	178.6	185.1	191.9	198.9	210.6	234.6	249.0	27
Revenue	61.5	67.3	69.6	81.0	78.9	83.1	86.6	86.4	90.1	93.9	97.0	100.3	103.7	107.1	114.5	126.5	135.2	14
Tax revenue	29.9	29.6	28.7	30.4	33.9	36.0	37.4	35.2	36.8	38.4	40.0	41.6	43.3	45.0	48.7	54.9	59.4	6
Nontax revenue Of which: Fishing license fees	31.6 25.4	37.7 32.2	40.8 29.5	50.6 41.7	45.0 35.0	47.1 36.4	49.2 37.9	51.2 39.4	53.3 40.9	55.5 42.6	57.1 43.6	58.7 44.7	60.4 45.9	62.1 47.0	65.8 49.4	71.6 53.2	75.8 55.9	6
External grants	39.4	44.0	59.1	55.8	68.9	75.4	76.9	78.4	68.7	78.4	81.6	84.8	88.2	91.7	96.1	108.1	113.8	12
Fotal expenditure and net lending	125.2	142.7	149.4	150.1	173.9	194.2	197.1	196.9	192.8	204.8	211.7	219.2	227.0	235.1	249.0	276.4	293.3	32
Current expenditure	85.8	98.7	90.3	90.3	94.3	99.5	103.6	106.7	110.1	113.5	120.4	124.7	129.1	133.6	143.1	158.6	169.8	18
Of which: Wages and salaries	41.5	45.0 8.1	43.2 7.3	44.1	46.6	49.9 7.5	52.5 7.5	54.6	56.8 7.5	59.0 7.5	62.1 8.2	64.3 8.5	66.6 8.8	68.9 9.1	73.8 9.8	81.8 10.8	87.6	9
Subsidies to public enterprises 1/ Other current expenditure	7.2 37.1	45.5	39.8	7.9 38.3	7.9 39.8	42.1	43.6	7.5 44.7	45.8	47.0	50.1	51.9	53.7	9.1 55.6	59.6	66.0	11.6 70.7	7
Development expenditure	39.4	44.0	59.1	59.8	79.6	94.7	93.5	90.1	82.8	91.3	91.3	94.5	97.9	101.5	105.8	117.8	123.5	13
Net lending	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Overall balance	-24.4	-31.4	-20.7	-13.2	-26.1	-35.7	-33.6	-32.1	-34.1	-32.5	-33.1	-34.1	-35.1	-36.2	-38.4	-41.9	-44.3	-4
Financing	24.4	31.4	20.7	13.2	26.1	35.7	33.6	32.1	34.1	32.5	33.1	34.1	35.1	36.2	38.4	41.9	44.3	4
Revenue Equalization and Reserve Fund Consolidated Fund	45.0 -20.5	25.0 6.4	18.0 -8.3	9.2 0.0	15.5 0.0	16.4 0.0	17.0 0.0	20.4	20.0	19.6 0.0	23.8	24.8 0.0	26.2 0.0	27.3 0.0	30.0	35.1 0.0	38.5 0.0	4
Development Fund	4.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
STABEX Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
External loans (net)	-2.3	-0.7	-0.9	4.0	10.7	19.3	16.6	11.7	14.1	12.9	9.3	9.3	9.0	8.9	8.4	6.8	5.8	
Other sources	-2.1	0.7	12.0	0.0	0.0	0.0	0.0	0.0	0.0 In percer	0.0 nt of GDF	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Fotal revenue and grants	66.0	70.4	78.4	83.1	80.7	80.4	78.5	75.7	69.8	72.5	72.2	72.0	71.7	71.4	69.9	69.1	67.8	6
Revenue	40.2	42.6	42.4	49.2	43.0	42.2	41.6	39.7	39.6	39.5	39.3	39.0	38.7	38.5	38.0	37.3	36.8	3
Tax revenue	19.6	18.8	17.5	18.5	18.5	18.3	18.0	16.2	16.2	16.2	16.2	16.2	16.2	16.2	16.2	16.2	16.2	1
Nontax revenue Of which: Fishing license fees	20.7 16.6	23.8 20.4	24.9 18.0	30.7 25.3	24.5 19.1	23.9 18.5	23.6 18.2	23.5 18.1	23.4 18.0	23.4 17.9	23.1 17.7	22.8 17.4	22.6 17.1	22.3 16.9	21.8 16.4	21.1 15.7	20.6 15.2	2
External grants	25.8	27.8	36.0	33.9	37.6	38.2	36.9	36.0	30.2	33.0	33.0	33.0	33.0	32.9	31.9	31.9	31.0	3
Fotal expenditure and net lending	81.9	90.3	91.0	91.1	94.9	98.5	94.7	90.5	84.8	86.2	85.6	85.2	84.8	84.4	82.6	81.5	79.9	7
Current expenditure	56.2	62.5	55.0	54.8	51.5	50.5	49.7	49.1	48.4	47.8	48.7	48.5	48.2	48.0	47.5	46.7	46.2	2
Of which: Wages and salaries	27.1	28.5	26.3	26.8	25.4	25.3	25.2	25.1	25.0	24.8	25.1	25.0	24.9	24.7	24.5	24.1	23.8	2
Subsidies to public enterprises 1/ Other current expenditure	4.7 24.3	5.2 28.8	4.4 24.3	4.8 23.3	4.3 21.7	3.8 21.3	3.6 20.9	3.4 20.5	3.3 20.1	3.2 19.8	3.3 20.3	3.3 20.2	3.3 20.1	3.3 20.0	3.2 19.8	3.2 19.5	3.2 19.2	1
Development expenditure	25.8	27.8	36.0	36.3	43.4	48.0	44.9	41.4	36.4	38.4	36.9	36.8	36.6	36.4	35.1	34.7	33.6	3
Net lending	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Overall balance	-15.9	-19.9	-12.6	-8.0	-14.3	-18.1	-16.2	-14.7	-15.0	-13.7	-13.4	-13.3	-13.1	-13.0	-12.7	-12.3	-12.1	-1
Financing	15.9	19.9	12.6	8.0	14.3	18.1	16.2	14.7	15.0	13.7	13.4	13.3	13.1	13.0	12.7	12.3	12.1	1
RERF	29.5	15.8	11.0	5.6	8.4	8.3	8.2	9.4	8.8	8.2	9.6	9.7	9.8	9.8	10.0	10.3	10.5	1
Consolidated Fund Development Fund	-13.4 2.8	4.1 0.0	-5.1 0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
STABEX Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
External loans (net)	-1.5	-0.4	-0.6	2.4	5.8	9.8	8.0	5.4	6.2	5.4	3.7	3.6	3.4	3.2	2.8	2.0	1.6	
Other sources	-1.4	0.4	7.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Memorandum items RERF balance (in milllions of Australian dollars;end of period)	637.3	561.6	570.5	576.1	579.7	590.0	601.2	611.9	625.4	641.4	661.8	682.3	702.5	722.8	762.4	817.9	851.1	89
RERF: Interest and dividend Income	30.0	34.2	21.6	20.8	21.8	22.8	24.1	25.5	25.9	24.9	25.5	26.3	27.2	28.0	29.6	31.8	33.2	3
Valuation changes	-5.5	-83.5	6.5	-4.9	-1.8	4.9	5.0	6.7	8.5	11.8	10.0	10.3	10.6	11.0	11.6	12.5	13.0	1
Government drawings	45.0	25.0	18.0	9.2	15.5	16.4	17.0	20.4	20.0	19.6	14.1	15.1	16.4	17.6	20.3	25.4	28.8	3
Overall balance + RERF income (in percent of GDP) Current fiscal balance (in percent of GDP, exclud. grants)	3.7 -15.9	1.8 -19.9	0.5 -12.6	4.6 -5.6	-2.3 -8.4	-6.5 -8.3	-4.6 -8.2	-3.0 -9.4	-3.6 -8.8	-3.2 -8.2	-3.1 -9.4	-3.0 -9.5	-3.0 -9.5	-3.0 -9.5	-2.9 -9.5	-3.0 -9.5	-3.0 -9.4	
Nominal GDP at market prices	-15.9 152.8	-19.9 158.0	-12.6 164.1	-5.6 164.8	-8.4 183.2	-8.3 197.2	-8.2 208.2	-9.4 217.6	-8.8 227.4	-8.2 237.6	-9.4 247.2	-9.5 257.2	-9.5 267.6	-9.5 278.4	-9.5 301.4	-9.5 339.3	-9.4 367.3	41
Real GDP Growth	0.4	-1.1	-0.7	1.8	3.0	3.5	3.0	2.0	2.0	2.0	1.5	1.5	1.5	1.5	1.5	1.5	1.5	-

Sources: Data provided by the Kiribati authorities; and Fund staff estimates and projections. 1/ Includes subsidies to copra production.

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DEBT SUSTAINABILITY ANALYS

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ARTICLE IV REPORT-

Table 6a Kiribati: Summary of Central Government Operations, Reform Scenario, 2007–30 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020 2022 2025 2027 2030 Projections (In millions of Australian dollars) Total revenue and grants 100.9 111 3 128 7 136.9 147.8 171.2 177.3 182 5 177.6 190.3 197.8 206.0 214 4 223.3 239.0 270.0 289 8 327 6 Revenue 61.5 69.6 81.0 91.5 102.4 106.4 110.9 115.6 120.5 130.9 148.4 161.4 183.2 67.3 78.9 83.8 88.2 96.8 Tax revenue 29 9 29 6 28.7 30.4 33.9 36.0 37.5 37.8 39 9 42 2 44 1 46.3 48 7 51.1 56.4 65.5 72.2 83.8 31.6 37.7 40.8 50.6 45.0 47.8 50.7 53.7 56.9 60.2 62.3 64.6 66.9 69.3 74.5 99.4 Nontax revenue 83.0 89.2 Of which: Fishing license fees 25.4 32 2 29.5 417 35.0 37.1 39.3 417 44 2 46.8 48.3 499 51.5 53.1 56.6 62 2 66.2 72 8 39.4 44.0 59.1 55.8 68.9 89.1 90.9 80.8 87.9 91.4 95.1 98.9 102.8 108.1 144.4 External grants 87.4 121.6 128.4 125.2 Total expenditure and net lending 142.7 149.4 150.1 173.9 191.5 193.0 193 9 190.0 201.5 212.3 221.1 230.3 239 9 257.1 290.5 312 0 352 5 98.7 90.3 103.4 109.7 117.9 128.4 134.0 165.9 Current expenditure 85.8 90.3 94.3 97.0 99.4 114.1 123.0 146.0 180.6 205.1 Of which: Wages and salaries 41.5 45.0 43.2 44.1 46.6 47.9 48.6 51.1 53.7 56.4 57.7 60.2 62.9 65.6 71.4 81.2 88.4 100.4 Subsidies to public enterprises 1/ 7.2 8.1 7.3 7.9 7.9 7.0 7.0 7.0 7.0 7.0 7.5 7.9 8.2 8.6 9.3 10.6 11.5 13.1 Other current expenditure 44.4 53.7 47 1 46.2 47 7 49.1 50.8 454 49 0 50.7 52 7 55.0 57.4 59.9 65.2 74.1 80.7 91.6 39.4 44.0 59.1 59.8 90.5 80.3 87.4 94.4 98.1 105.9 131.4 Development expenditure 79.6 94.5 93.6 101.9 111.1 124.6 147.4 Net lending 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 Overall balance -24.4 -31.4 -20.7 -13.2 -26.1 -20.3 -15.7 -11.4 -12.4 -11.3 -14.5 -15.2 -15.9 -16.6 -18.1 -20.5 -22.2 -25.0 Financing 24.4 31.4 20.7 13.2 26.1 20.3 15.7 11.4 12.4 11.3 14.5 15.2 15.9 16.6 18.1 20.5 22.2 25.0 Revenue Equalization and Reserve Fund 45.0 18.0 13.2 11.9 12.9 11.9 25.0 9.2 15.5 11.2 11 7 12.6 13.6 14.4 16.4 18.8 20.5 23.5 Consolidated Fund -20.5 6.4 -8.3 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 Development Fund 4.3 0.0 0.0 0.0 0 0 0.0 0.0 0.0 0.0 0.0 0 0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 STABEX Fund 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 -0.7 -0.5 -0.5 -2.3 -0.9 4.0 10.7 45 -0.5 2.6 2.6 2.3 2.2 1.7 External loans (net) 7 1 17 1.8 1.5 Other sources -2.1 0.7 12.0 0.0 0.0 0.0 0.0 0.0 0.0 1.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 0.0 (In percent of GDP) Total revenue and grants 66.0 70.4 78.4 83.1 80.7 86.8 84 8 826 76.2 77.3 76.9 76.2 75.5 74.8 72.5 70.7 68.7 67.0 Revenue 40.2 42.6 42.4 49.2 43.0 42.5 42.1 41.4 41.5 41.6 41.3 41.0 40.7 40.4 39.7 38.8 38.3 37.4 18.5 Tax revenue 19.6 18.8 17.5 18.5 18.3 17.9 17.1 17.1 17.1 17.1 17.1 17.1 17.1 17.1 17 1 17.1 17.1 Nontax revenue 20.7 23.8 24.9 30.7 24.5 24.2 24.2 24.3 24.4 24.5 24.2 23.9 23.6 23.2 22.6 21.7 21.1 20.3 Of which: Fishing license fees 16.6 20.4 18.0 25.3 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Sources: Data provided by the Kiribati authorities; and Fund staff estimates and projections. 1/ Includes subsidies to copra production.



INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 11/56 FOR IMMEDIATE RELEASE May 17, 2011

International Monetary Fund 700 19th Street, NW Washington, D. C. 20431 USA

IMF Executive Board Concludes 2011 Article IV Consultation with Kiribati

On May 2, 2011, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Kiribati.¹

Background

Kiribati has been affected by the global crisis through a fall in remittances and large decline in the value of its wealth and pension funds—the Revenue Equalization Reserve Fund (RERF) and the Kiribati Provident Fund. The spike in food and fuel prices in 2008 has already taken a toll on economic activity. Vulnerabilities to climate change, including coastline erosion, have also worsened.

After two years of contraction, the economy recovered in the second half of 2010 and inflation pressure dissipated. It is estimated to have grown by 1¾ percent for the year. Despite a weather-related drop in copra production, private sector activity appears to have picked up, especially in retail. Tourist arrivals rebounded by 20 percent compared to 2009, although from a very low base. Despite the rise in world food and fuel prices, inflation has bounced from 2008 crisis-highs into negative territory, reflecting the strong appreciation of the Australian dollar, which is used as the domestic currency, and a decline in the world price of rice. Credit growth in the overall economy declined in 2009 as economic activity stalled. But it started to pick up in the second half of 2010 as the recovery gained traction.

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Fiscal policy has supported the economy during the economic downturn. Copra subsidies and civil servant wages have increased and have helped mitigate the impact of the output contraction on households. The fiscal deficit bottomed out at 20 percent of GDP in 2008, but narrowed substantially the following year as a result of expenditure compression and improved tax collection, with the introduction of a withholding tax at the source in March 2009. However, the RERF suffered substantial losses, with its assets declining from 420 percent of GDP in 2007 to 350 percent of GDP in 2009.

In 2010, the fiscal position strengthened and budget planning improved. The estimated fiscal deficit is 8 percent of GDP, down from 12½ percent in 2009. The narrowing deficit reflects a large increase in fishing licenses fees, as a result of an auction scheme introduced in September 2010. The authorities introduced a three-year budget framework with the 2010 budget. Structural reform momentum, especially in privatizing SOEs gained traction at end 2010.

The Development Bank of Kiribati's (DBK) non-performing loans (NPLs) have been reduced by 2 percentage points as a share of total loans in the last two years, but they remain high. A new lending scheme was introduced by the Provident Fund in July 2010 to ease access to credit.

Executive Board Assessment

Executive Directors noted that the economy has recovered from the global crisis and that growth in the next few years is expected to strengthen owing to key public infrastructure projects financed by foreign assistance. Nevertheless, as a small island economy, Kiribati faces many policy challenges and is also vulnerable to external shocks, particularly climate change. A further escalation of food and fuel prices could result in higher inflation and erode past gains in poverty reduction. Directors concurred that ensuring sustainable growth and poverty reduction over the medium term and bolstering the economy's resilience necessitates timely implementation of comprehensive structural reforms.

Directors stressed the importance of preserving the real per capita value of the Revenue Equalization Reserve Fund to ensure fiscal sustainability and intergenerational fairness. Once key public projects in the pipeline are completed, the focus should shift to fiscal consolidation, with a view to rebuilding fiscal space and addressing the long-term spending pressures arising from climate change.

Directors commended the authorities for introducing a multi-year budget framework, which should help in designing realistic fiscal plans. They looked forward to further strengthening

of the medium-term fiscal framework to facilitate public planning and help guard against procyclical policies.

Directors stressed that accelerating structural reforms, especially reforming the state-owned enterprises and developing the private sector are critical to ensure sustainable growth and reduce the drain on the budget. Welcoming the steps taken by the authorities to boost competition, Directors called for further efforts toward enhancing the business climate and increasing competition in the banking sector. Strengthening bank regulation and supervision and introducing a new law to improve access to land and collateral recovery are also important.

Directors noted the joint IMF-World Bank debt sustainability analysis and encouraged the authorities to continue to secure grant financing to support the country's large development needs. They also noted that containing fiscal deficits will be essential for maintaining external stability.

Directors encouraged the authorities to continue improving the quality of macroeconomic data.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Kiribati: Selected Economic Indicators, 2007–12

Nominal GDP (2010): US\$146.7 million Nominal GNI (2010): US\$209.6 million Main export products: fish and copra GDP per capita (2010): US\$1,420 Population (2010): 103,280 Quota: SDR 5.6 million

	2007	2008	2009	2010	2011	2012
				Projections		
Real GDP (percent change) Real GNI (percent change) Consumer prices (percent change, average) Consumer prices (percent change, end of period)	0.4	-1.1	-0.7	1.8	3.0	3.5
	-0.9	2.2	-5.0	6.6	-1.8	2.8
	4.2	11.0	8.8	-2.8	7.7	5.0
	3.7	18.6	0.1	-1.4	8.0	4.0
Central government finance (percent of GNI) Revenue and grants Total domestic revenue Grants	47.3	48.9	58.1	57.6	58.6	58.8
	28.8	29.6	32.0	34.1	31.3	30.8
	18.5	19.3	26.1	23.5	27.3	28.0
Expenditure and net lending Current Of which: wages and salaries Development	58.7	62.7	66.0	63.1	69.0	72.0
	40.3	43.4	39.9	38.0	37.4	36.9
	19.5	19.8	19.1	18.5	18.5	18.5
	18.5	19.3	26.1	25.1	31.6	35.1
Overall balance	-11.4	-13.8	-7.9	-5.5	-10.4	-13.2
Financing Revenue Equalization and Reserve Fund (RERF)	11.4	13.8	7.9	5.5	10.4	13.2
	21.1	11.0	11.6	3.9	6.1	6.1
Other	-9.7	2.8	-3.7	1.7	4.2	7.2
RERF Closing balance (in millions of U.S. dollars) Closing balance (in millions of \$A) Per capita value (in 1996 \$A)	562	389	512	572	515	518
	637	562	570	576	580	590
	5,052	4,185	4,020	3,868	3,717	3,614
Balance of payments (in millions of U.S. dollars) Current account including official transfers (In percent of GDP) Current account excluding official transfers (In percent of GDP)	-37.6	-46.0	-38.1	-34.1	-47.1	-50.5
	-29.4	-34.7	-29.8	-23.1	-28.9	-29.2
	-70.6	-78.9	-84.2	-84.0	-108.4	-116.7
	-55.2	-59.6	-65.8	-57.0	-66.5	-67.4
External debt (in millions of U.S. dollars) (In percent of GDP)	13.7	14.5	14.3	18.4	27.6	43.5
	10.2	13.3	9.7	11.3	17.0	25.1
External debt service (in millions of U.S. dollars) (In percent of exports of goods and services)	2.2	0.6	1.0	0.6	0.6	0.7
	11.9	5.0	7.9	3.0	2.6	2.7
Exchange rate (\$A/US\$ period average) 1/ Real effective exchange rate (period average) 2/	1.2 99.8	1.2 115.0	1.3 125.9	1.1 129.4		
Memorandum item: Nominal GDP (in millions of Australian dollars)	152.8	158.0	164.1	164.8	183.2	197.2

Sources: Data provided by the Kiribati authorities; and Fund staff estimates and projections.

^{1/} The Australian dollar circulates as legal tender.

^{2/} Index, 2005=100.

Statement by Christopher Y. Legg, Executive Director for Kiribati and Teea Tira, Advisor to Executive Director May 2, 2011

The Kiribati authorities welcome and endorse the Staff's frank and objective assessment of Kiribati's current economic conditions and its future outlook.

Managing the impact of increases in future food and fuel prices and pick-up in economic activity from the upcoming major infrastructure investments will occupy the authorities over the short term. The longer-term concern is achieving the increasing growth path amidst the challenges posed by Kiribati remoteness, geographical dispersion, and climate change effects. The authorities' development and policy initiative directions are broadly consistent with Staff's advice.

Managing Near-term Pressures

In the near term, the authorities agree that fiscal consolidation will need to be managed with the inflationary pressures from increases in food and fuel prices and the pickup in economic activity from the upcoming major infrastructure investments.

A further escalation of fuel and food prices is a concern to the authorities, given the limited policy instruments available to cushion the adverse impact on the population. Targeted subsidies are not easy to implement, given the relatively low income differential. A mechanism is currently in place that subsidizes the transportation cost of goods to the outer islands aimed at equalizing the price of goods across the nation. The mechanism is basically self-sustaining through a levy on all imports. However, the import levy rate has remained constant since its introduction more than 10 years ago. With the recent hike in fuel prices resulting in the increase in transportation costs, the import levy fund balance has been consistently eroded. Recognizing the need to adequately manage the import levy in the face of further hikes in fuel and food prices, the authorities welcome the grant assistance from the World Bank towards this mechanism. They are also very appreciative of the assistance (both, in-kind and financial) from their other development partners in cushioning the impact of the fuel and food price hikes.

Urban poverty is a complex issue. Given the lack of policy instruments to address the impact of hikes in the food and fuel prices, the authorities are very active in seeking employment opportunities for their people in external labor markets. They agree with Staff that an increase in civil servant wages is not an appropriate countercyclical policy measure, given its permanent nature, as well as its potential spill-over effects to the nation as a whole. The authorities have generally noted that the SOEs and the private sector usually follow the trends in the civil service wages. Given the low level of competition, costs are then passed on to the consumers, adding to inflation pressures. In this context the authorities are generally very cautious about awarding increases in civil service wages. However, the authorities consider that the recent increase in civil service wages in 2010 was long overdue, with the last increase in 2006, and with real wages remaining below 2006 levels.

In terms of the drawdown from the Revenue Equalization Reserve Fund (RERF), as an initial step towards fiscal restraint, the authorities have set a cap on the drawdown from the RERF for this fiscal year and three years forward at a nominal value of \$15 million per annum. This is a reduction of \$5 million as compared to the average drawdown in prior years. This rule is simple to implement and to manage. However, the authorities recognize the need to reduce further the drawdown to preserve the value of the RERF as a buffer against external shocks and for the benefit of future generations. In this context they are very appreciative of the recent MCM TA on the RERF, with key components of the TA mission outcomes currently under consideration for implementation. The authorities also expect to build on their current collaboration with MCM in maximizing the use and value of the RERF. The authorities are also committed to saving windfall earnings whenever possible.

Medium-term Fiscal Policy Settings

Over the medium term, the authorities agree that reining in the fiscal deficit will be crucial once key public investments have been addressed. Drawdowns from the RERF will continue to be anchored by the long-term objective of preserving the per capita value of the RERF.

As part of reining in the fiscal deficit, the authorities are pursuing improvements in revenue collection and have requested technical assistance (TA) to support their tax reform agenda. They have also taken steps to reduce the volatility of the fishing license revenues (the main source of government income) and are working towards further maximizing returns from their marine resources.

On the expenditure side, the authorities consider that an overall rationalization of government operations and services will be necessary. This includes the SOE reforms currently in progress. The authorities are also currently working on strengthening PFM and have initiated a multi-year budget framework. However, the authorities are conscious that the robustness and effectiveness of multi-year budgeting is constrained by the lack of a relevant macroeconomic policy framework. In this context the authorities have requested TA from PFTAC on setting up a credible macro-economic policy framework that should be complemented with strengthening the capacity for fiscal forecasting.

Lifting Sustainable Growth

To achieve a sustained growth path, the authorities underscore the importance of a vibrant private sector as an engine of growth. The authorities also concur with the Staff that productivity gains from infrastructure investments will prove transitory if progress in fiscal and structural reforms lags. Overarching structural reforms will be key to addressing the impediments to private sector growth as well as recognizing the benefits from the infrastructure investments.

As part of the structural reform process, the SOE reform is in progress, with the privatization of one SOE recently concluded. The recent successful conclusion of the privatization exercise has given the authorities confidence to move forward with four more SOEs, currently targeted for extensive reform measures. We consider this particularly noteworthy,

given that this is an election year with the authorities moving forward despite the political challenges.

The authorities are also targeting measures that will be relatively easy to implement and at the same time, will have a significant positive impact on the business environment, drawing from successful initiatives around the region. In this context, the authorities have targeted liberalization of the telecommunication sector with the World Bank's assistance. They aim to build on their success in such initiatives to address other impediments to private sector development.

Other measures which the authorities are considering include streamlining the business startup process, addressing the long-standing land tenure issue, and improving households' access to credit. As part of improving access to credit, micro-credit schemes such as village banks have been initiated with negative and positive experiences. The village banks appear to work better in the rural areas whilst in the urban areas, credit consumers tend to look more to the services of the mainstream financial institutions', whose lending products include relatively small scale loans.

The lending schemes offered by the Development Bank and the Kiribati Provident Fund are initial steps to improve the urban households' access to credit. However, the authorities agree with Staff that such schemes need to be managed carefully. In this context the authorities have requested TA from MCM to review the asset allocation of both, the Kiribati Provident Fund (KPF) and the Kiribati Insurance Corporation, which will include a review of the current credit schemes managed by the KPF. The authorities have also requested TA from MCM to assist in formulating a financial supervision and regulation framework in the event that further expansion of the financial sector, particularly through the Development Bank of Kiribati (DBK) is possible.

Conclusion

The authorities are very appreciative of the lead taken by the Fund Mission Chief and her team in strengthening collaboration with both, the World Bank and the Asian Development Bank, in particular in the context of Kiribati's DSA. A tangible outcome has been the stance taken by the World Bank to provide assistance through grants, as underlined in the recently approved Kiribati Country Assistance Strategy (CAS) covering the period 2011 to 2014. With limited fiscal space and balancing the need to preserve the per capita value of the RERF, such assistance to address the infrastructure gaps is welcome. However, the authorities are conscious of absorptive capacity constraints and will endeavor to ensure that they work closely with their development partners to manage implementation of these investment projects.

More generally, the authorities are well aware of the challenges that they face. They would like to stress their commitment to moving the economy forward and greatly appreciate the assistance from their development partners. In addition, the authorities would like to put on record their appreciation of the constructive efforts of the mission chief and her team. They look forward to maintaining this strong relationship as they navigate the challenges ahead.