



Pacific Island Countries (PICs): Key Macro Challenges and Linkages to the Technical Assistance (TA) Program

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Outlook

- **Moderate growth**
- **Downside risks have increased:**
 - Weaker growth in the euro area, Japan, and some emerging markets
 - Potential financial market correction
 - Reduction in overseas development assistance
- **But important upside factors:**
 - Lower oil prices (for importers)
 - Stable regional growth backdrop in Asia
 - Stronger Fijian and PNG economies
 - Scope to expand: tourism, agriculture, fisheries

The global recovery continues...

WEO Real GDP Growth Estimates and Projections (Percentage change)

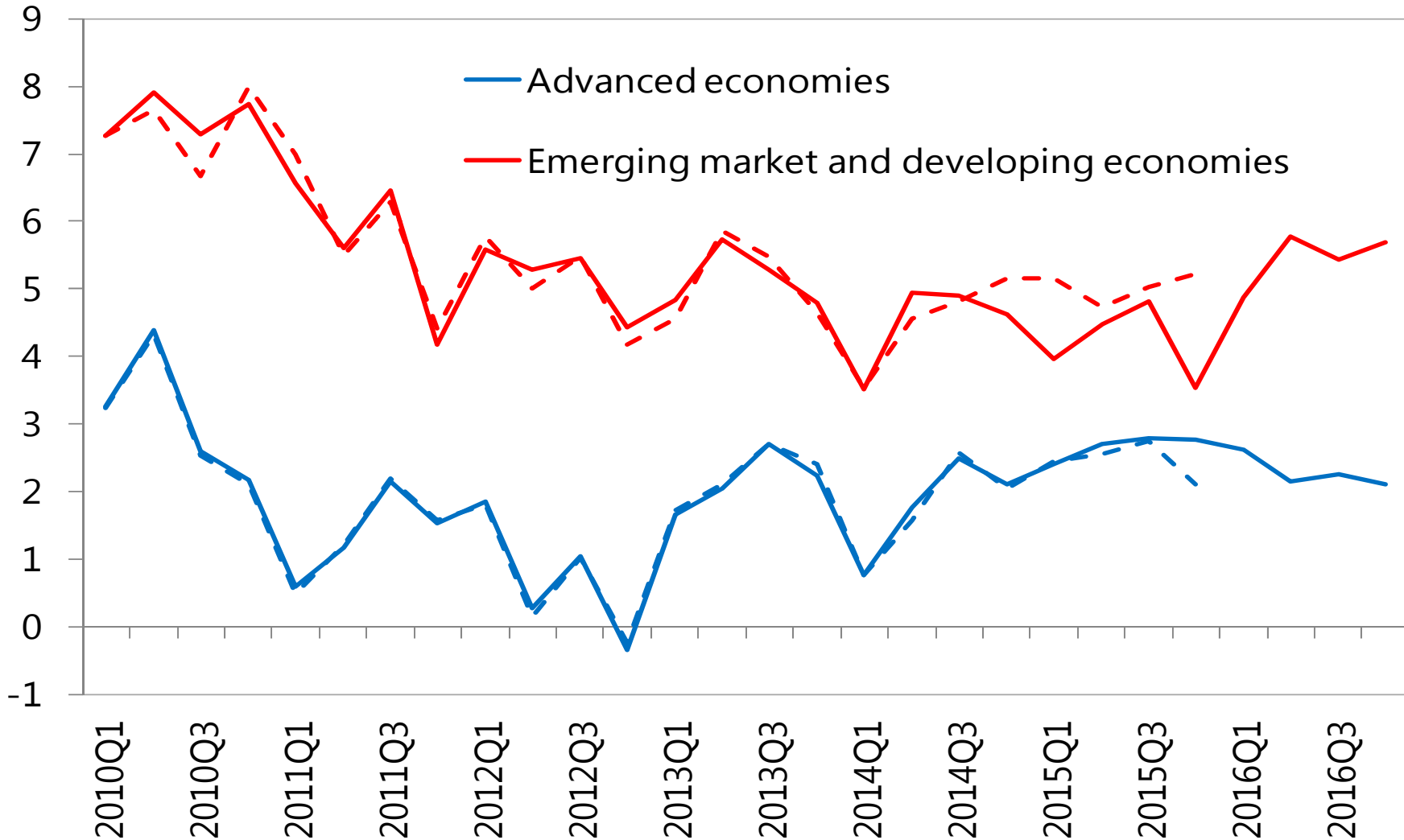


	World	U.S.	Euro Area	Japan	Brazil	Russia	India	China	PIC Small States	PIC Small States + PNG
2014	3.3	2.4	0.8	0.1	0.1	0.6	5.8	7.4	2.2	2.6
2015	3.5	3.6	1.2	0.6	0.3	-3.0	6.3	6.8	2.9	4.4

...although the pace is weak and uneven

Real GDP Growth

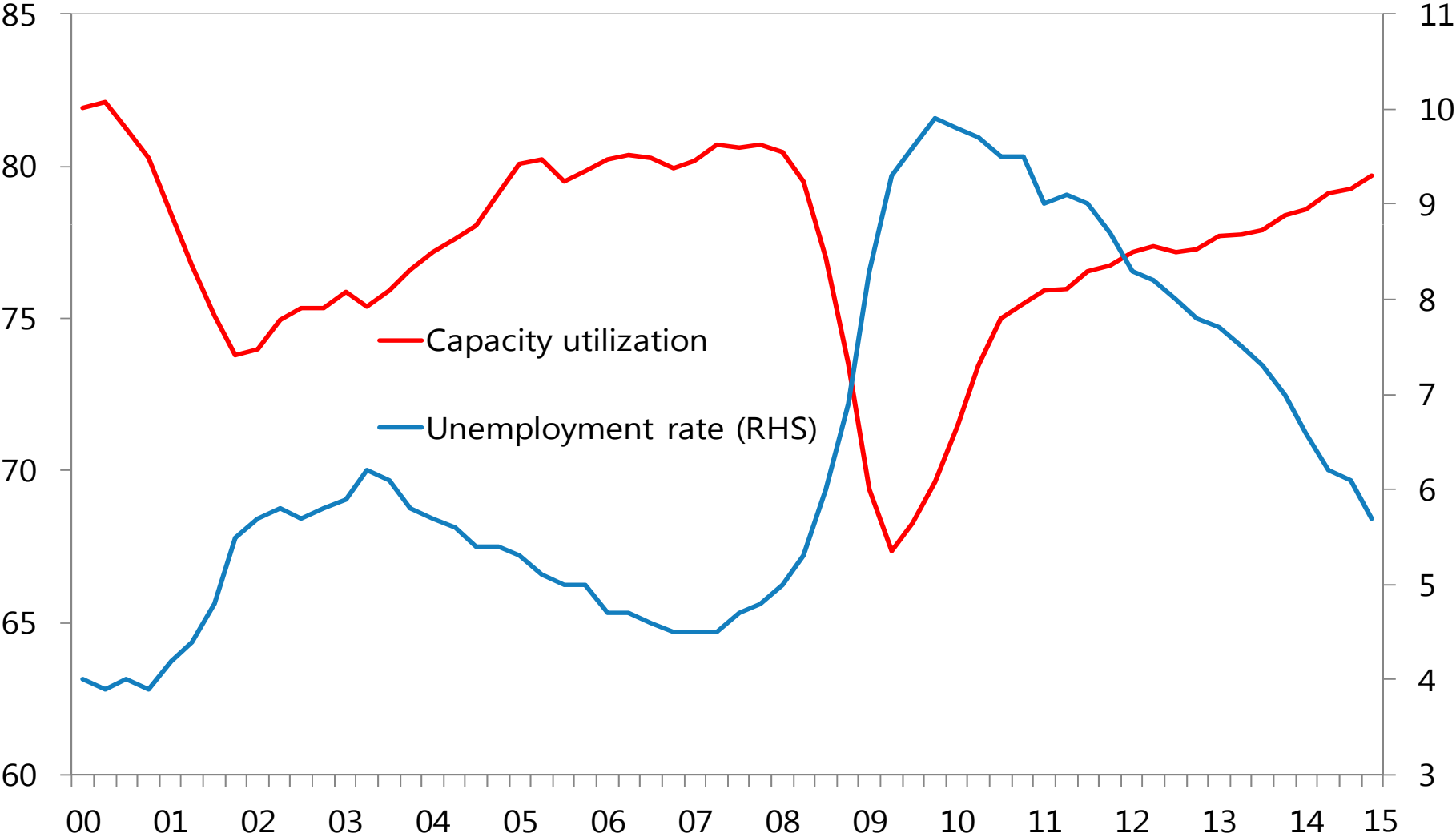
(annualized quarterly percent change; dashed lines are from October 2014 WEO)



In the US a solid recovery, closer to full capacity

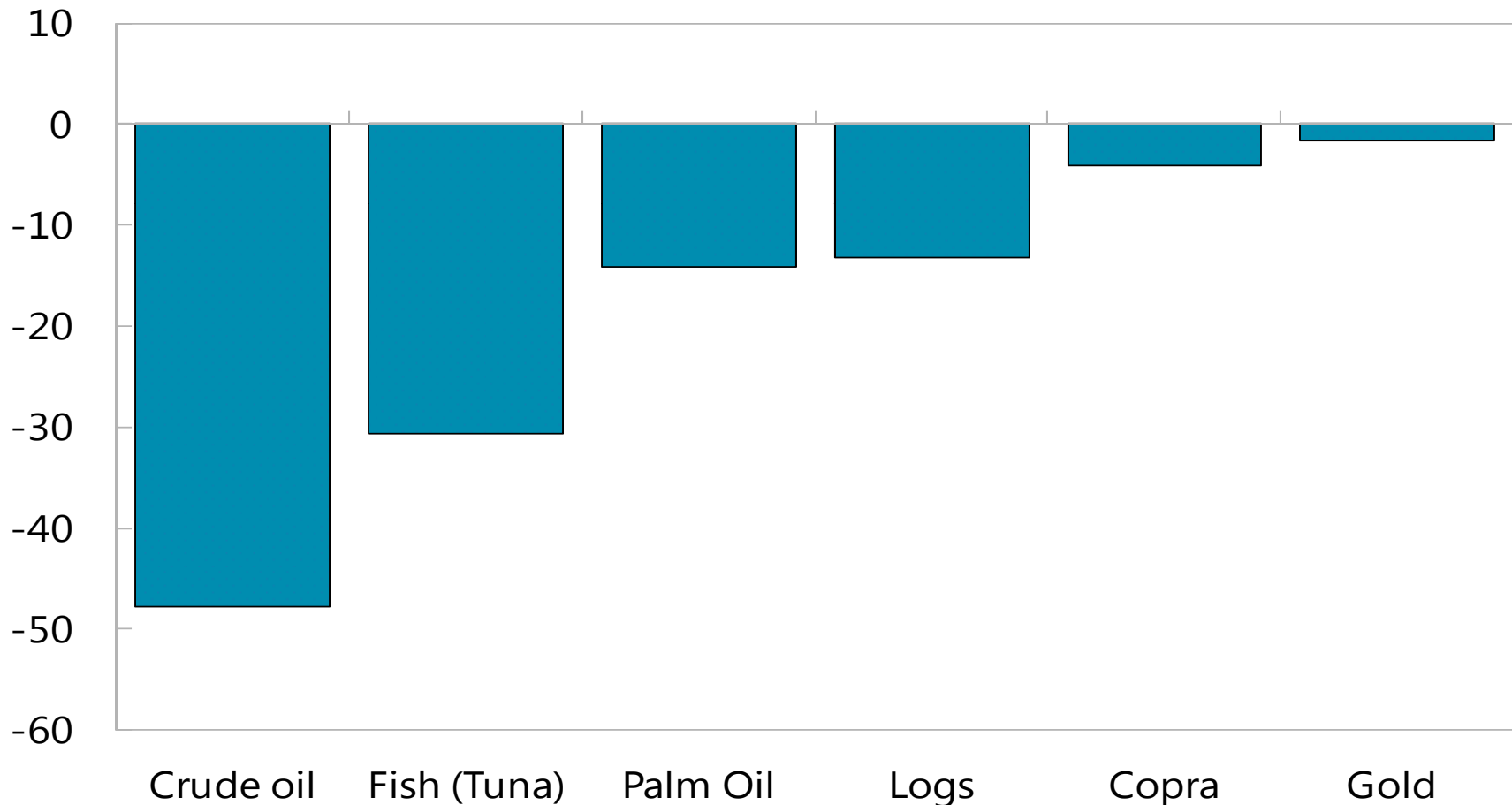
Capacity utilization and unemployment rate

(In percent)



Large drop in international oil prices and broad-based decline in commodity prices

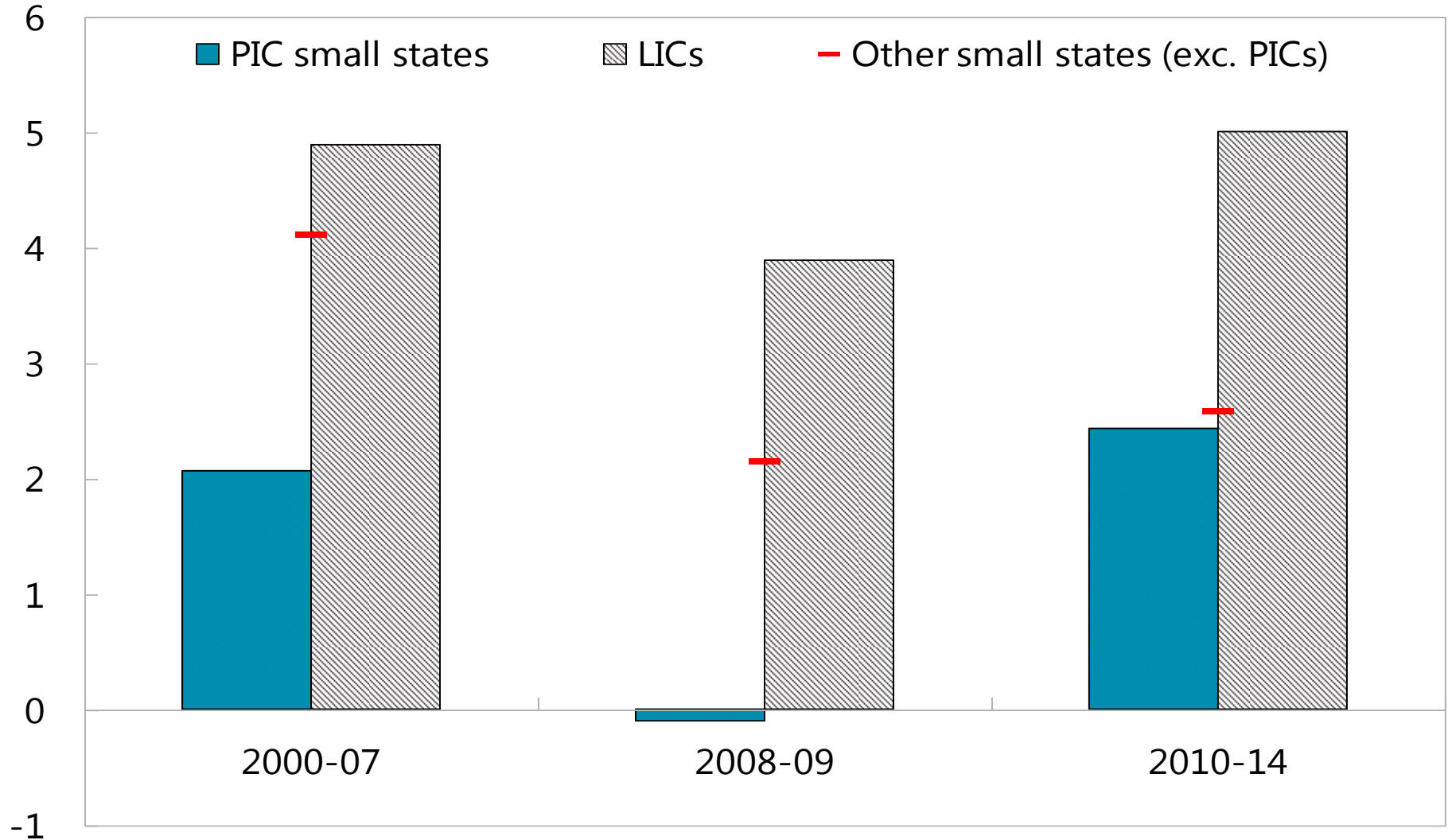
Change in Selected Commodity Prices, January 2015 (Year-on-year, in percent)



PICs growth continues to be moderate

Average Real GDP Growth

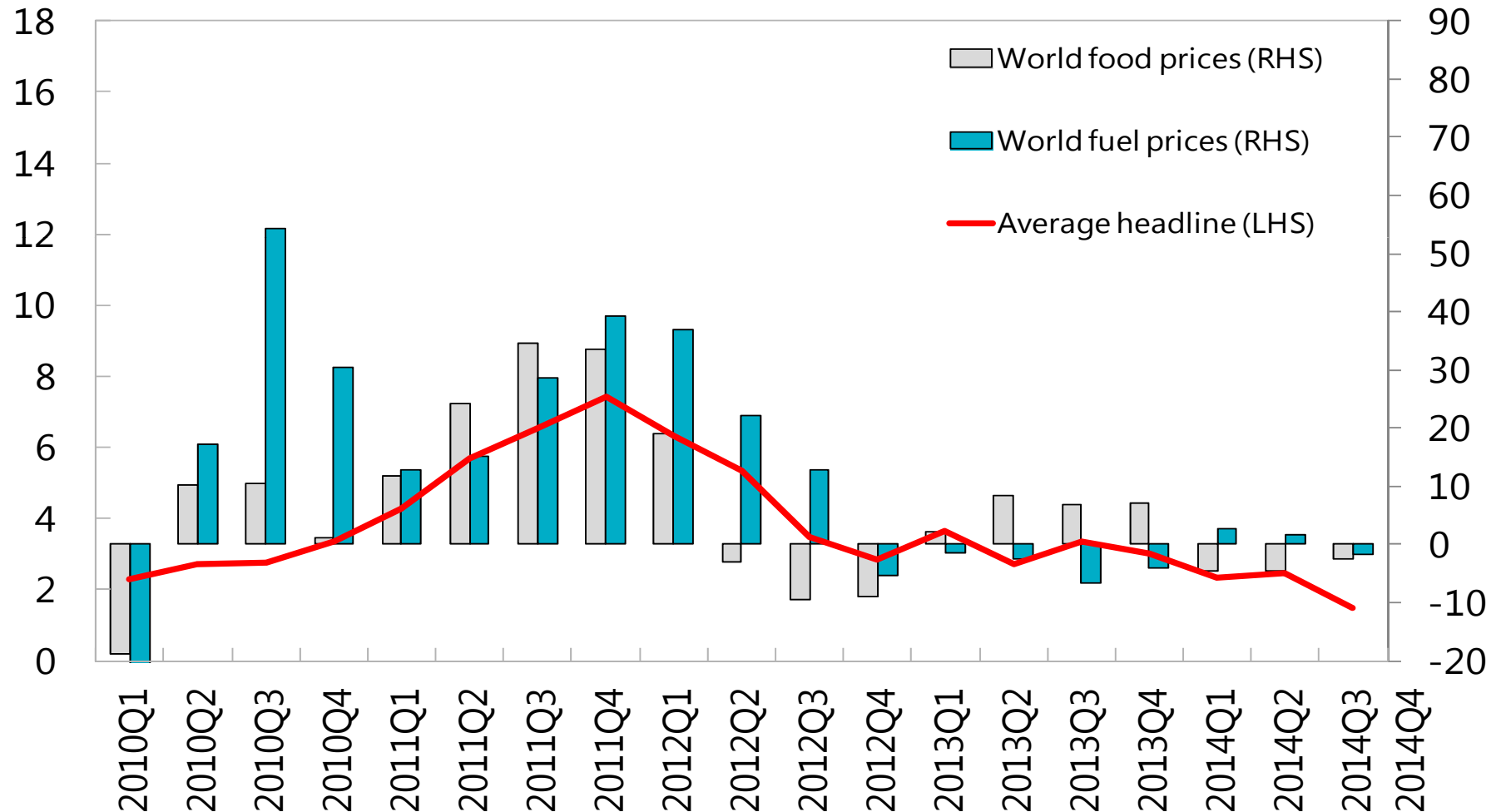
(In percent)



Lower inflation has eased the monetary policy trade off...

Pacific Islands: Inflation and Global Commodity Prices

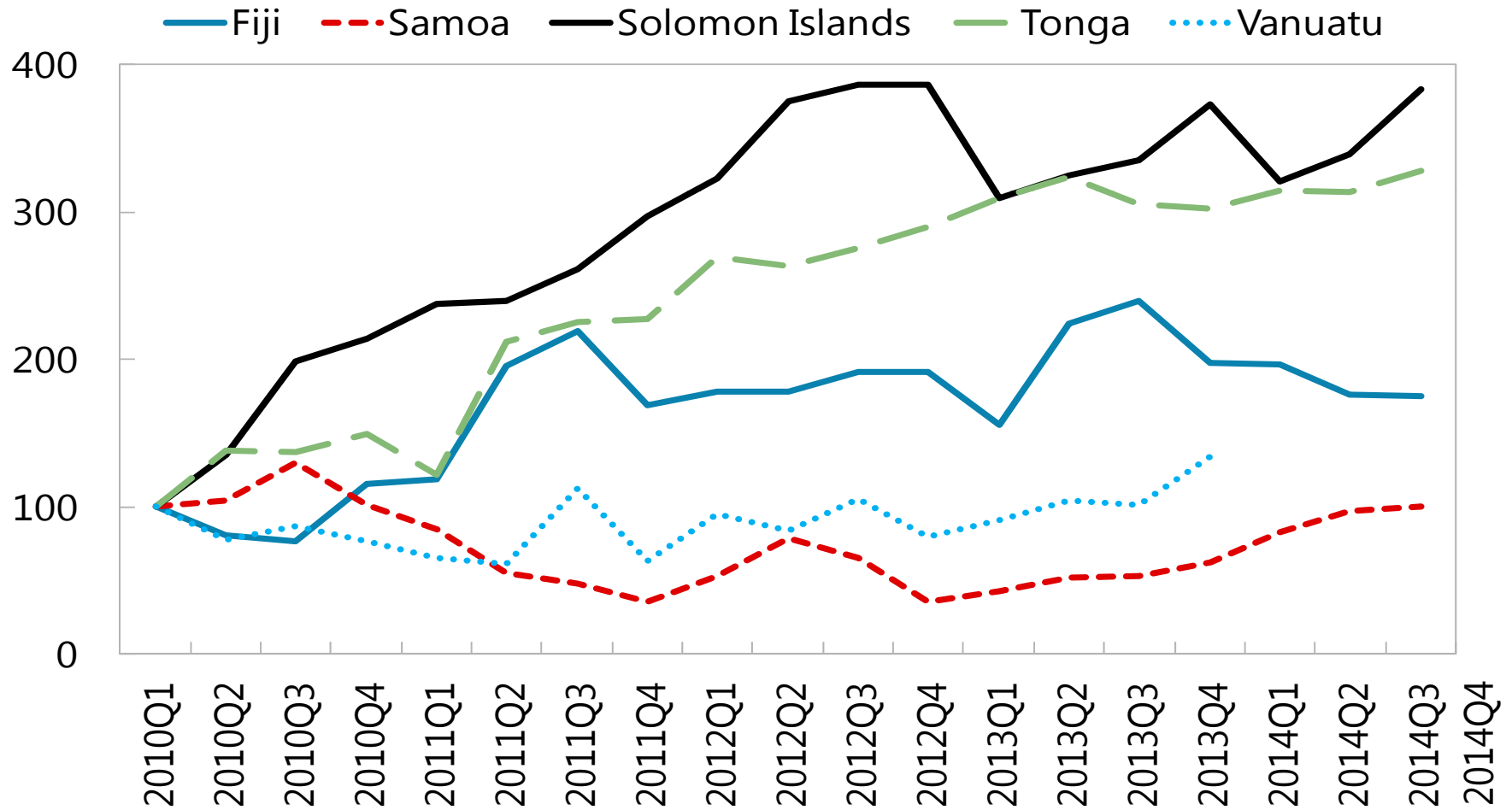
(In percent)



...although high excess reserves in the banking system because of weak monetary transmission mechanism weak

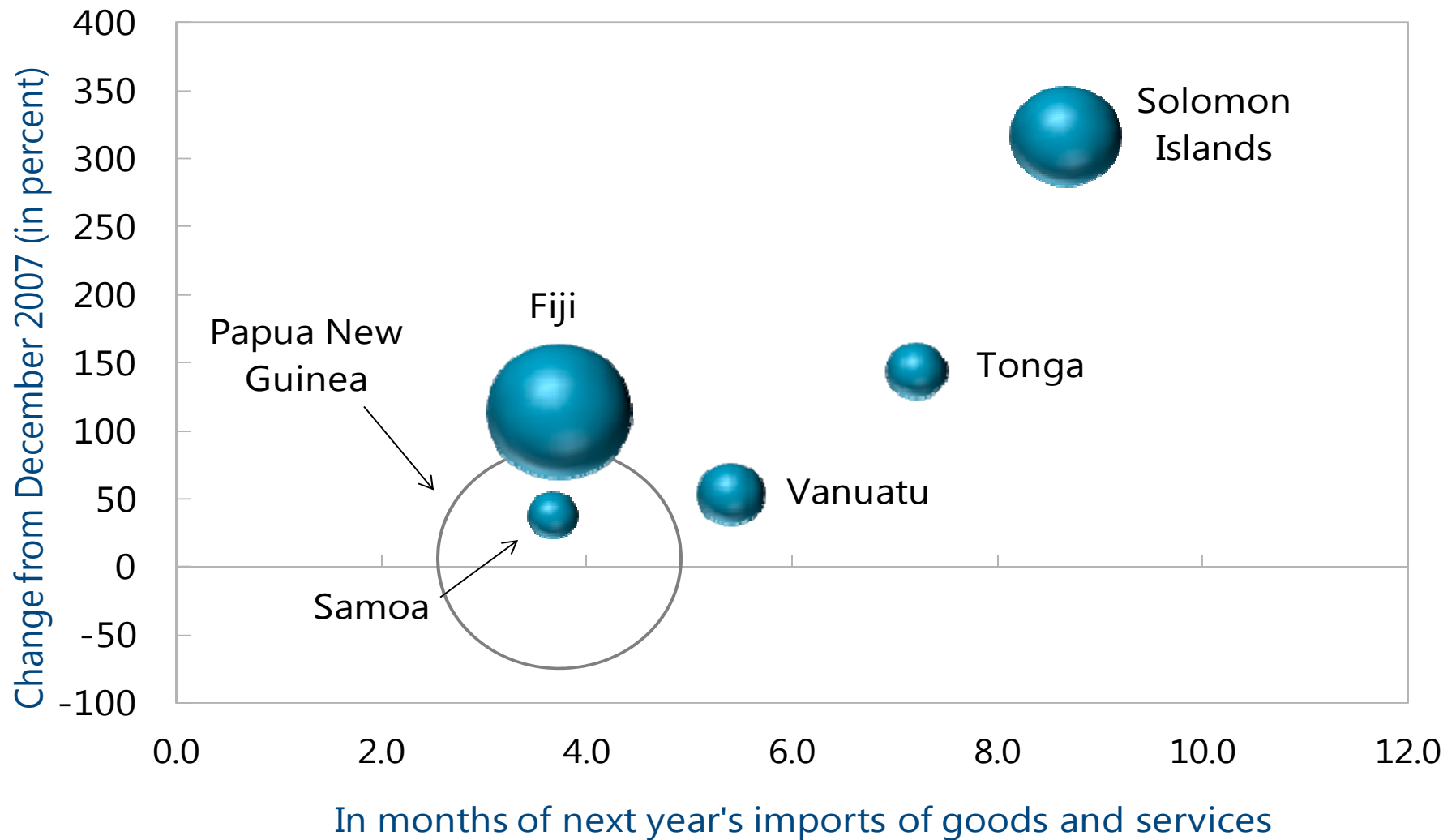
Selected APD Small States: Excess Reserves

(2010Q1=100)



On the upside, reserve buffers are at comfortable levels...

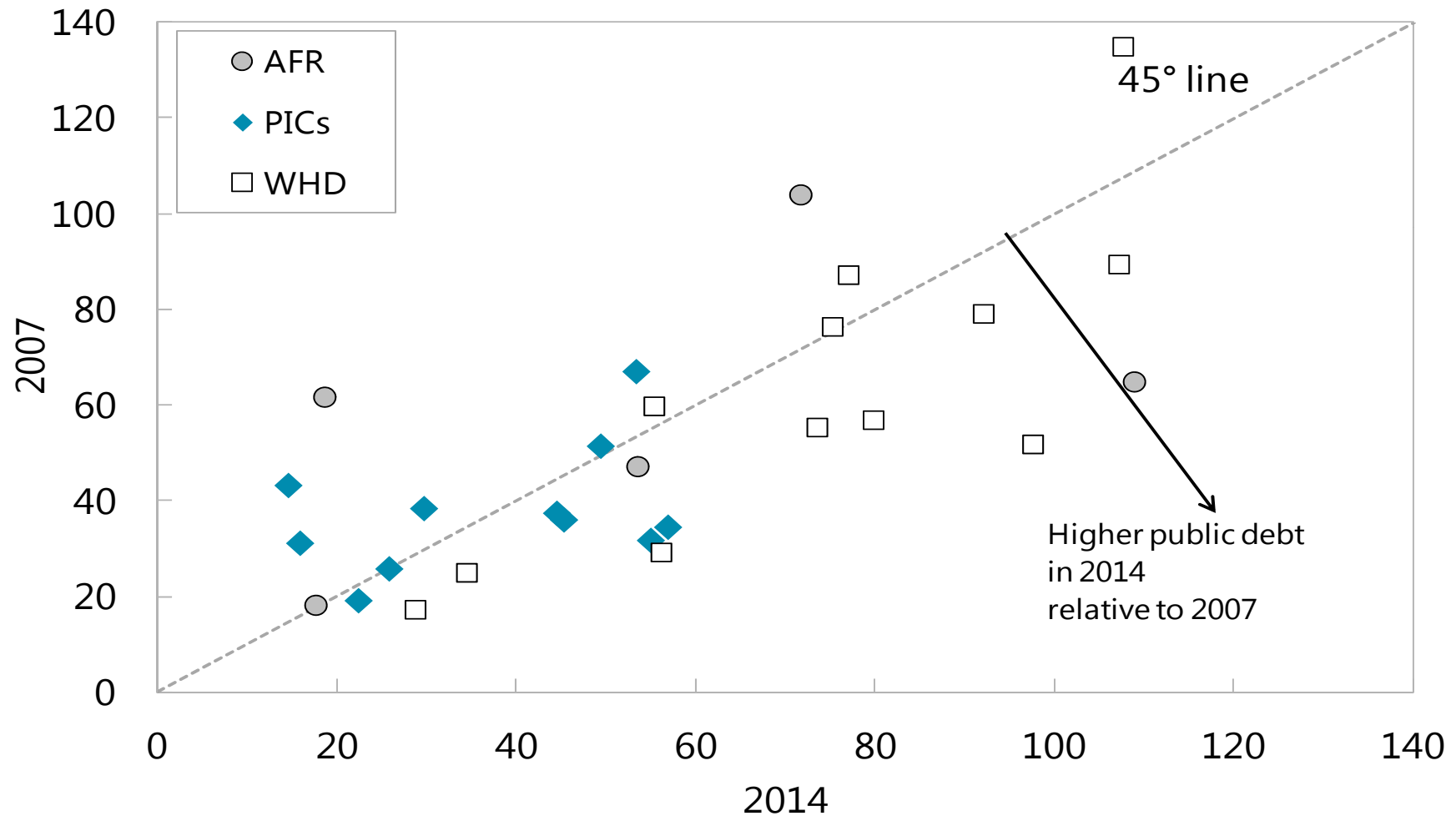
APD Small States and PNG: International Reserves, November 2014



...but some still need to rebuild fiscal space and deal with growing public debt

Small States: Gross Public Debt

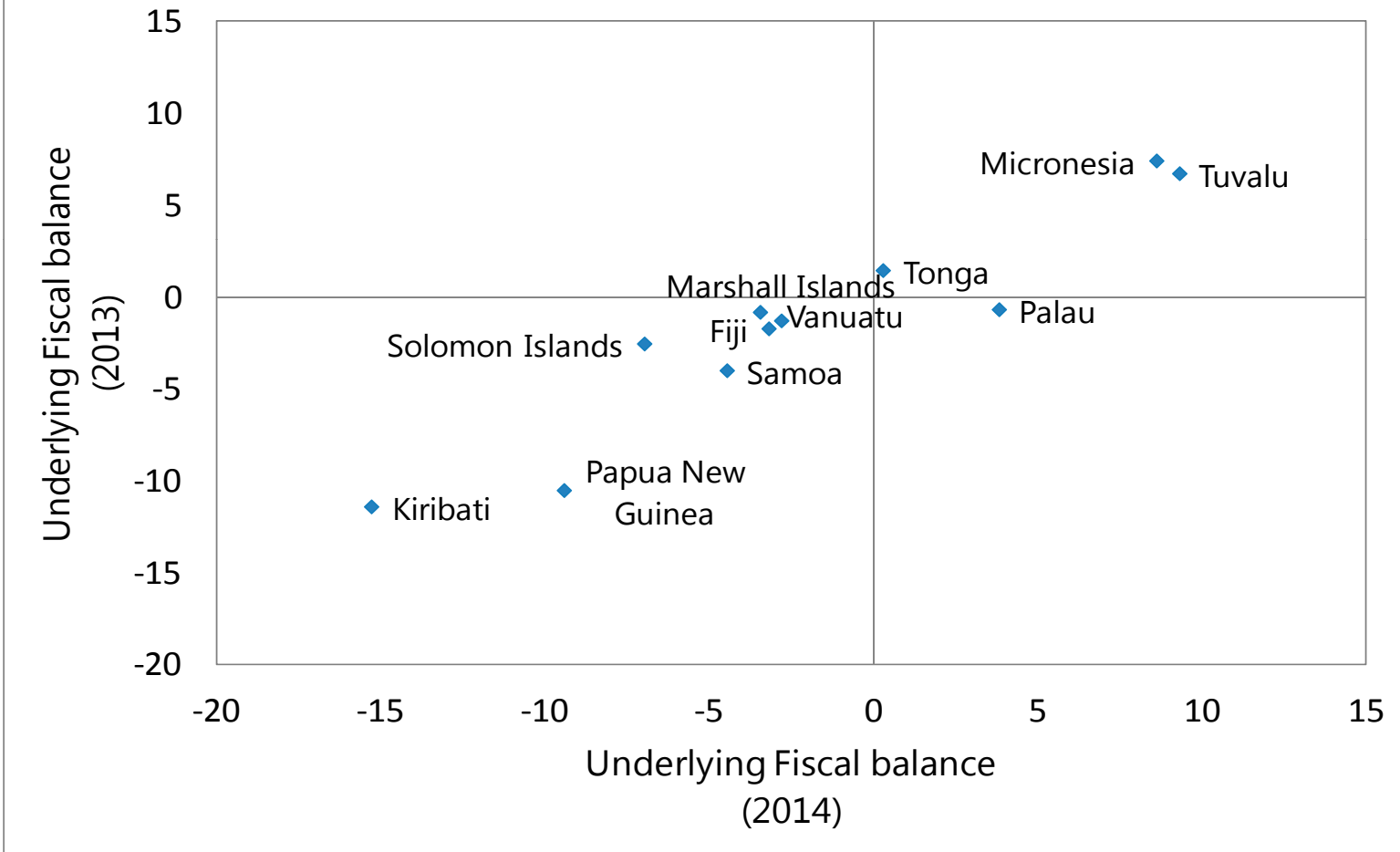
(In percent of GDP)



... while the underlying fiscal position deteriorated in some countries

Underlying Fiscal Balance

(In percent of GDP)



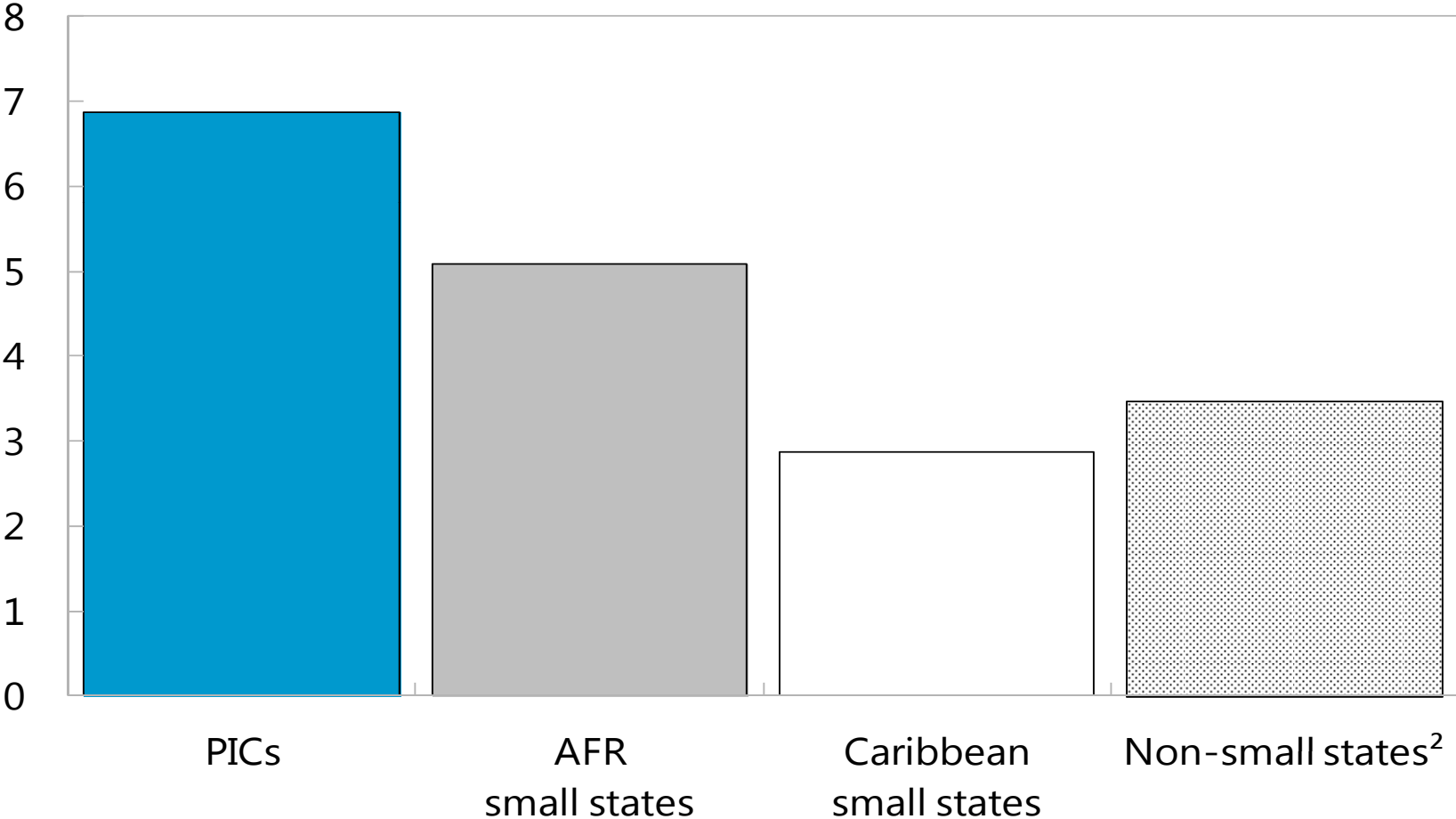
Underlying fiscal balance = overall fiscal balance – (commodity revenue – long term average of commodity revenue)

Structural Issues: Policy Challenges and TA Priorities

PICs face several structural challenges: fiscal revenue is more volatile than in other comparators

Volatility of Revenue¹

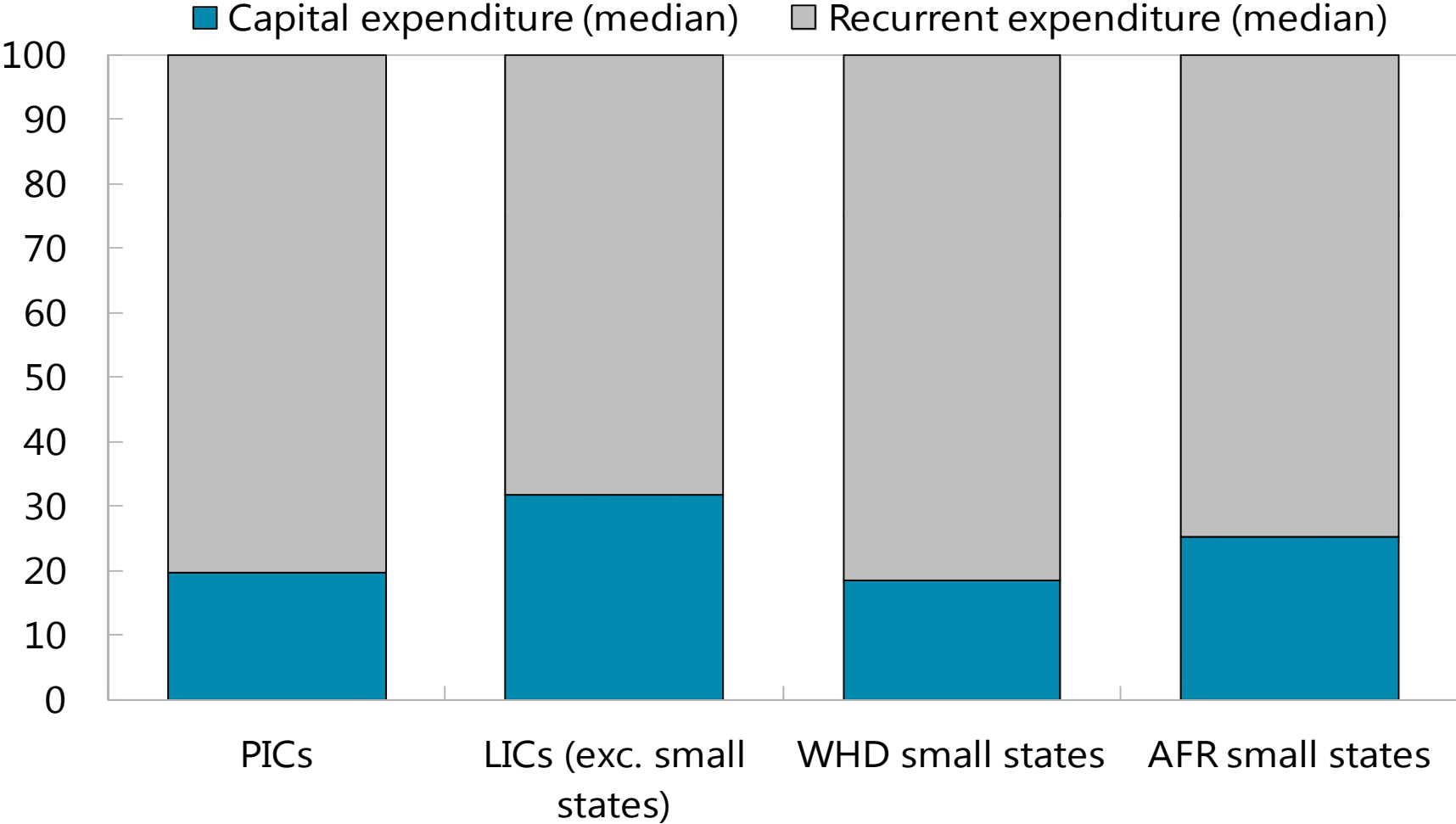
(Standard deviation of revenue-to-GDP ratio; 1990-2013)



... the large share of recurrent spending introduces rigidities to the budget ...

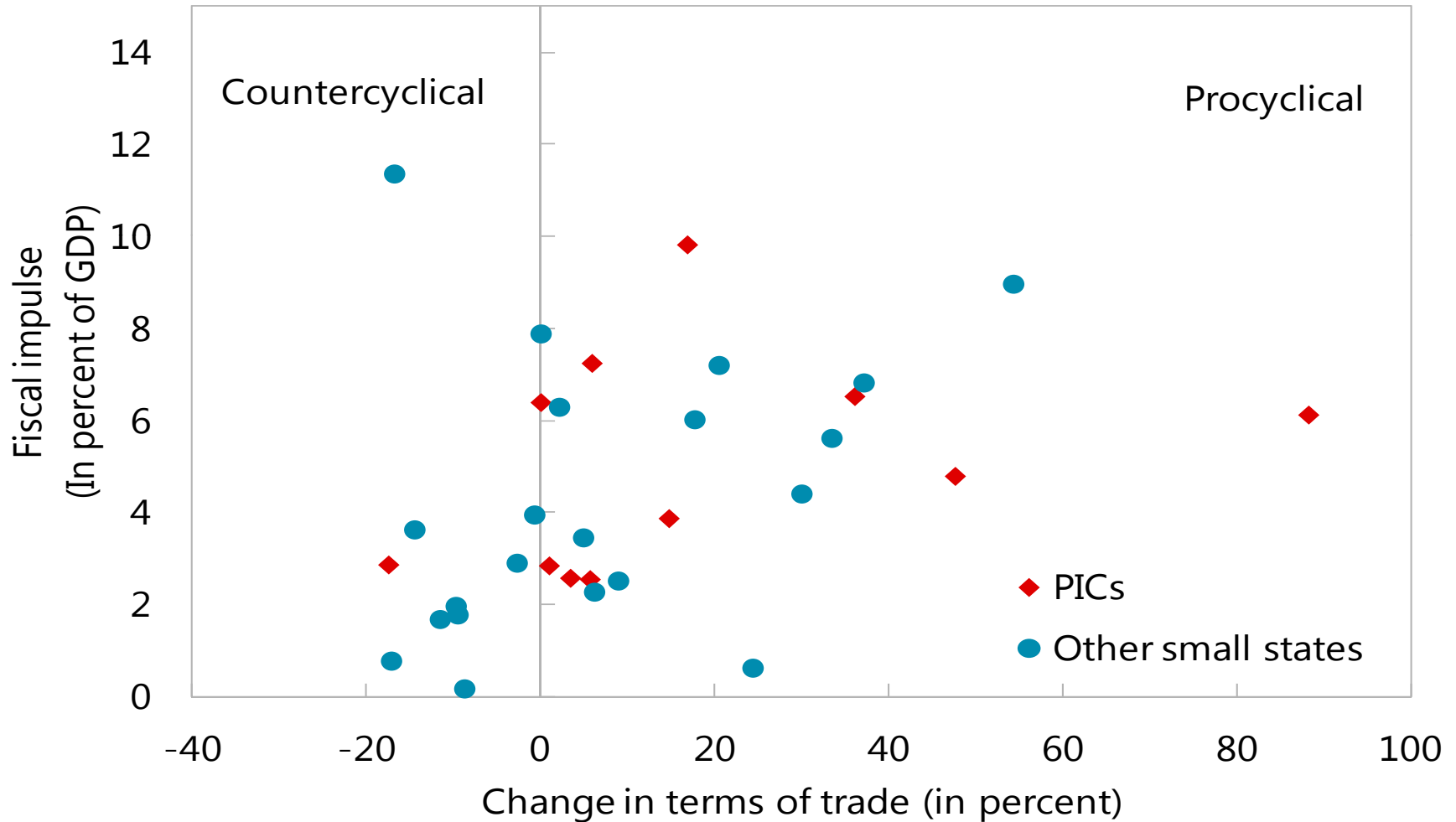
Government Expenditure, 2003-13

(In percent of total government expenditure)



...which make fiscal policy procyclical...

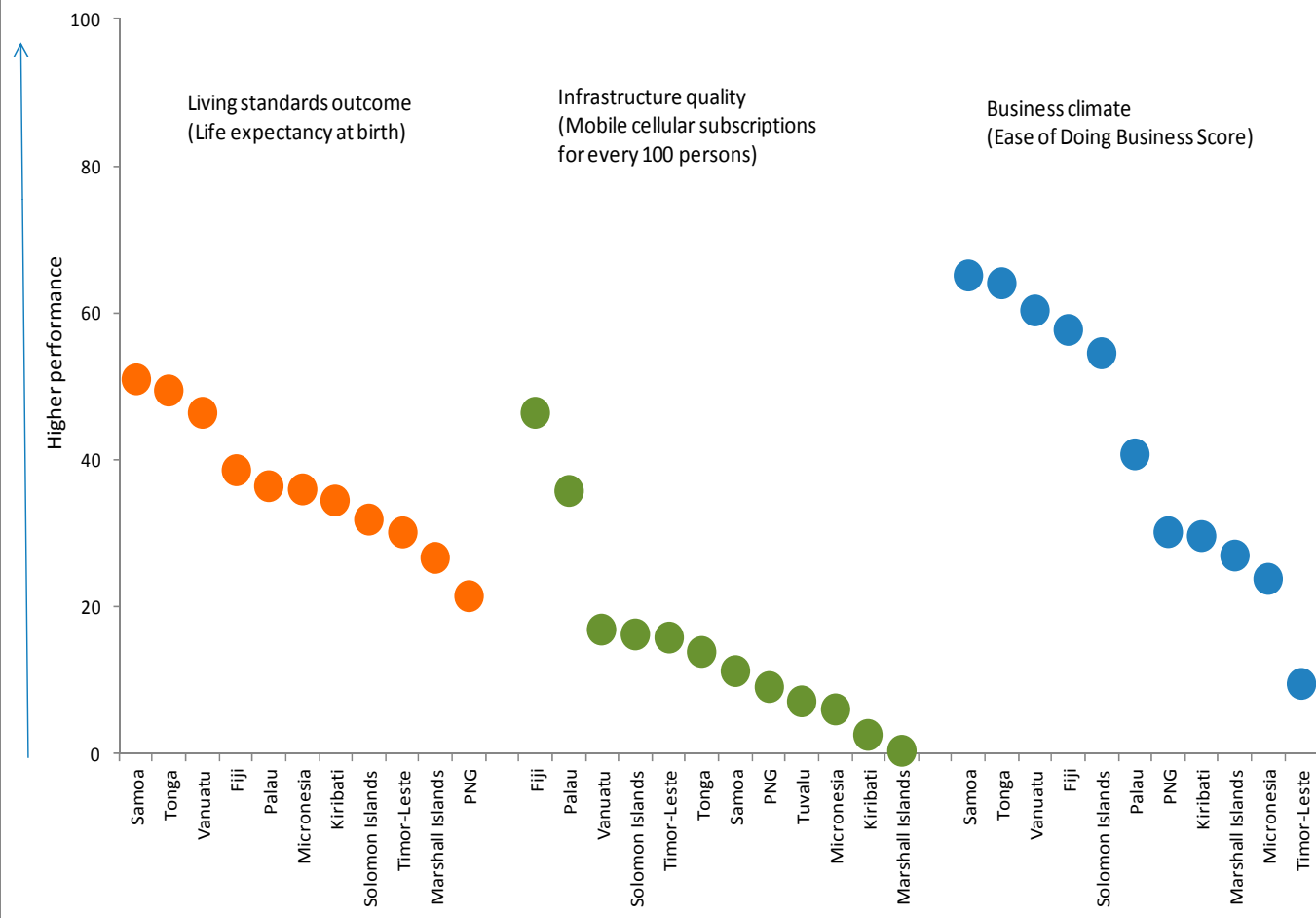
Fiscal Impulse and Terms of Trade, 2005-12



Limited capital spending weak structural indicators relative to peers...

Pacific Island Countries: Structural Indicators

(Percentile ranks)

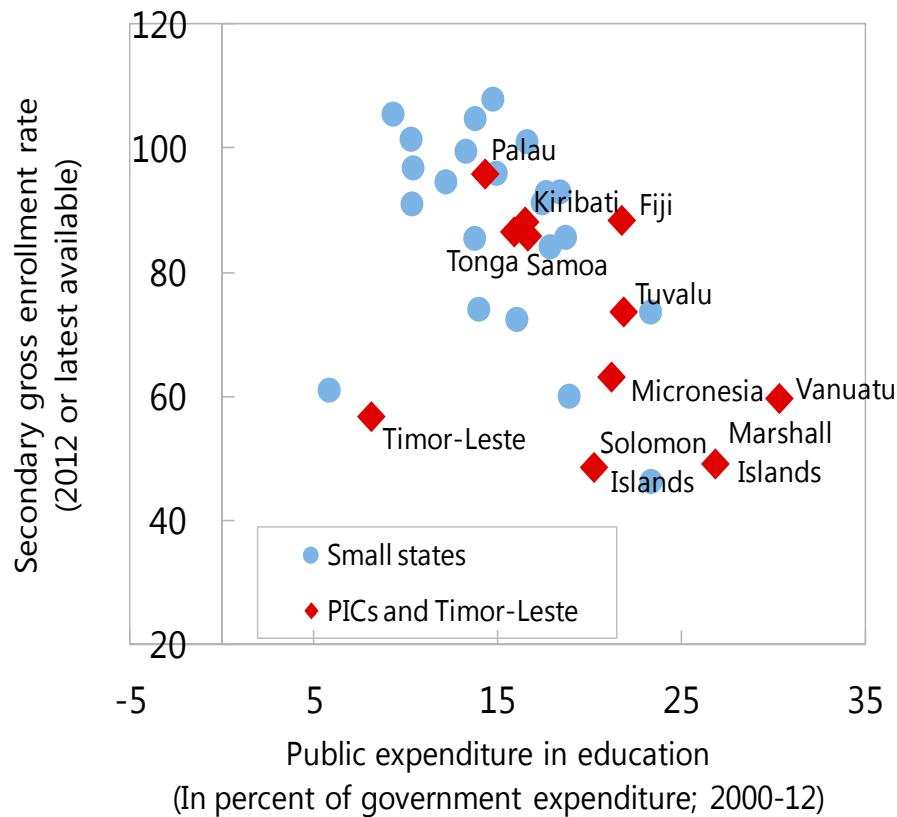


Priorities are country-specific, but generally include:

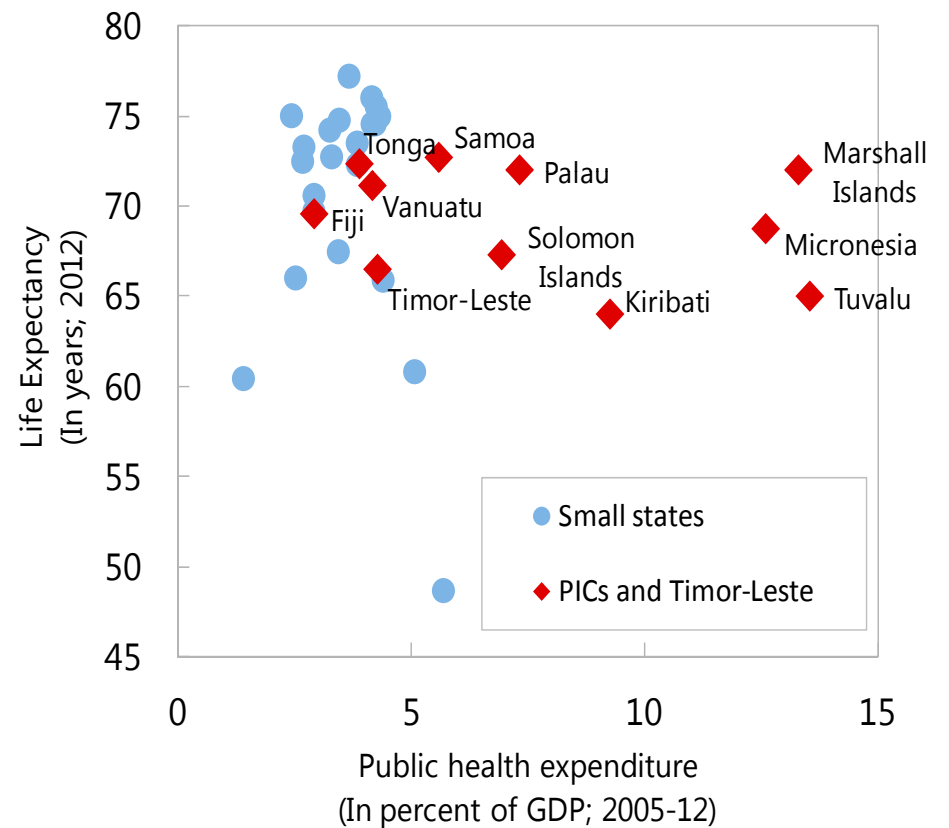
- Addressing the infrastructure bottleneck
- Increasing living standards
- Improving the business climate

More efficient spending through PFM reforms is required to improve living standards...

Public Expenditure in Education and Secondary Enrollment



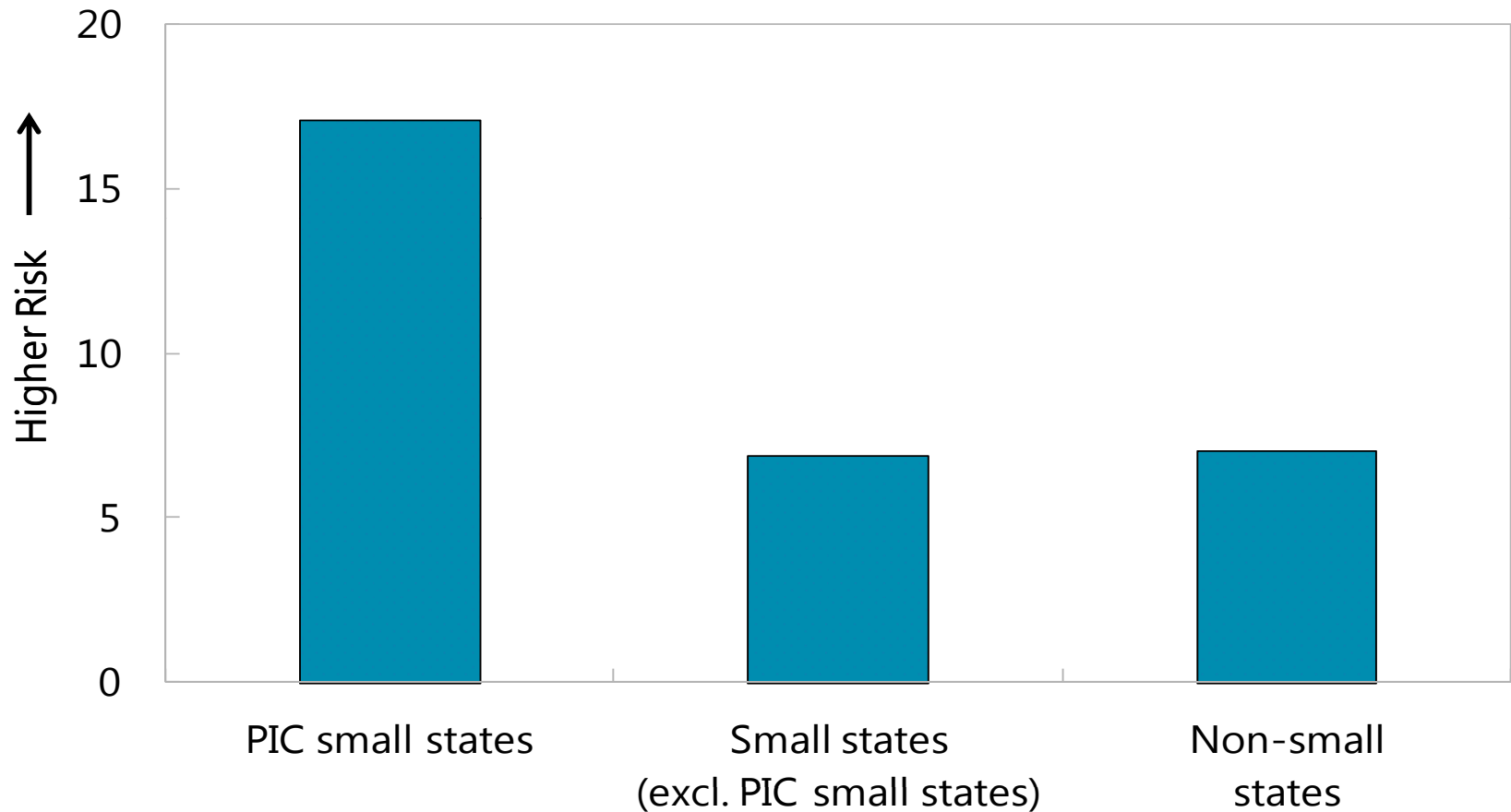
Life Expectancy and Public Health Expenditure



Continue to build buffers against shocks, including natural disasters

Natural Disaster Risks - World Risk Index, 2013

(In percentage points)

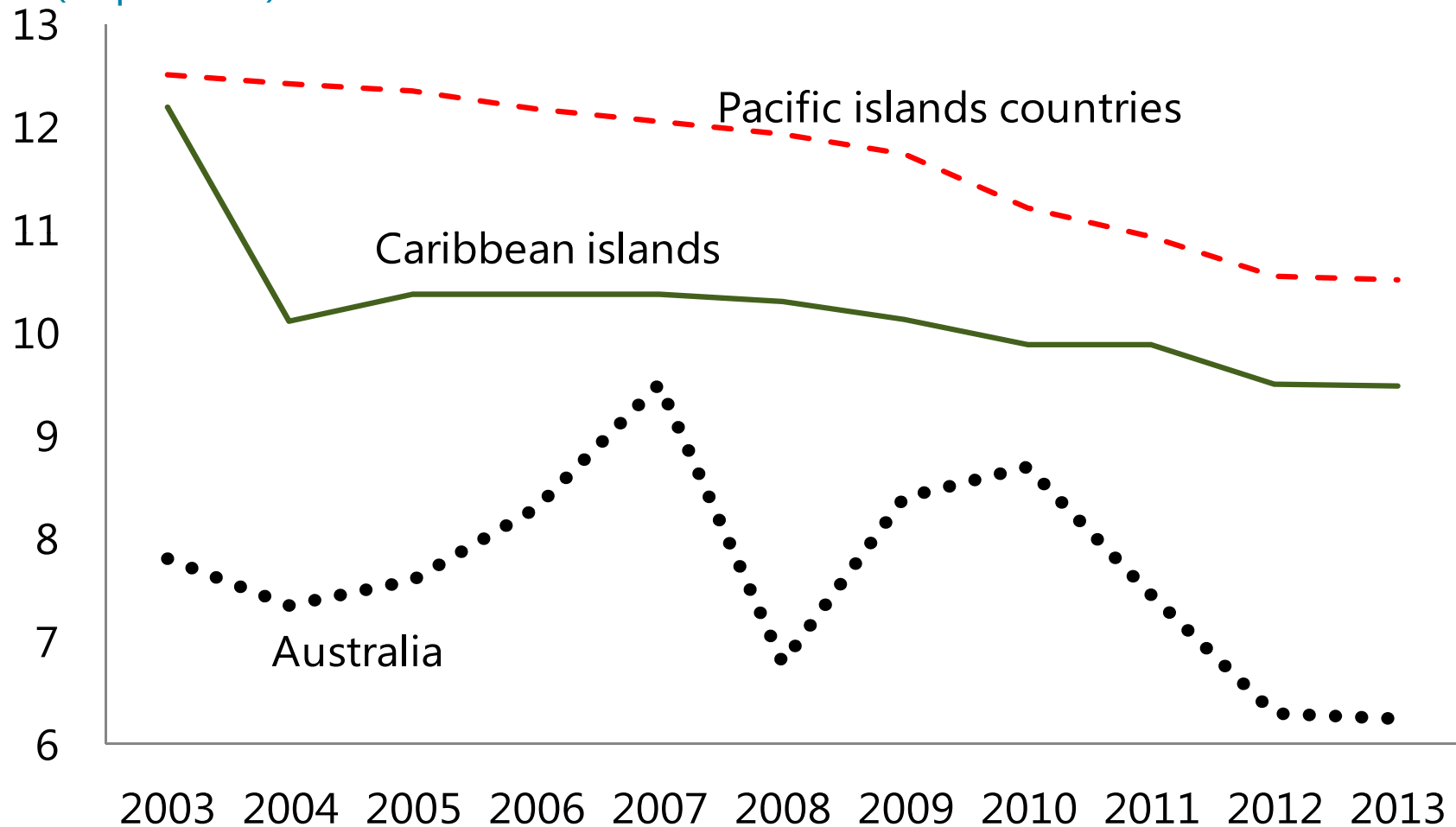


Note: High value indicates high risk. Maximum risk country = 36 percentage points.

Cost of financing is high relative to the Caribbean islands...

Average Lending Rates

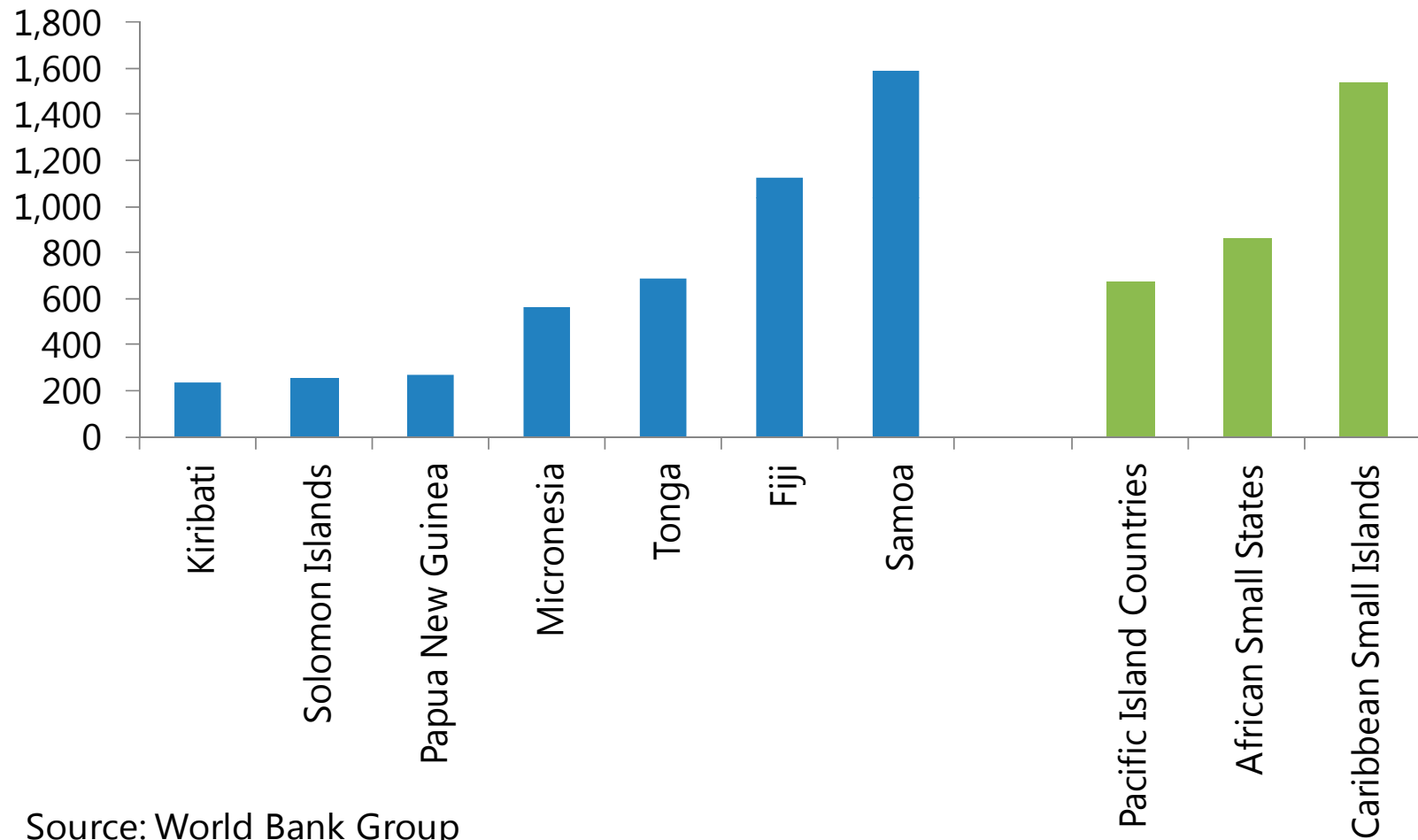
(In percent)



... and financial access lower

PICs: Commercial Bank Accounts per 1,000 Adults, 2013

(Number of accounts)



Source: World Bank Group

Policy Actions

- **Continue rebuilding policy space for rainy days**
- **Enhance fiscal frameworks**
 - Use fiscal anchor to manage revenue volatility
 - Strengthen medium-term orientation of fiscal policy
- **Improve spending mix to close infrastructure gap**
- **Implement PFM to improve quality of spending**
- **Enhance financial supervision/regulation**
- **Improve quality of statistics**

Mapping Policy Actions to TA Program

- Fiscal space/buffers => TA on revenue administration and PFM to raise revenue collection and improve spending efficiency
- Fiscal anchors => TA on macroeconomic economic analysis and PFM to design and implement fiscal anchor
- Medium-term budgeting => TA on PFM to develop the budget framework
- Spending mix => TA on PFM to improve spending quality
- Financial sector stability => TA on financial supervision and regulation including credit union
- Statistics => TA on macroeconomic statistics (national accounts, prices, balance of payments, government financial statistics, etc.)

Issues for discussions

- Are policy actions appropriate?
- Are TA priorities aligned to challenges?

Thank you