



# REPUBLIC OF THE MARSHALL ISLANDS

May 2021

## 2021 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR REPUBLIC OF THE MARSHALL ISLANDS

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 2021 Article IV consultation with Republic of the Marshall Islands, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its May 21, 2021 consideration of the staff report that concluded the Article IV consultation with Republic of the Marshall Islands.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on May 21, 2021, following discussions that ended on March 18, 2021, with the officials of Republic of the Marshall Islands on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 6, 2021.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the International Development Association.
- A **Statement by the Executive Director** for Republic of the Marshall Islands.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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## IMF Executive Board Concludes 2021 Article IV Consultation with the Republic of the Marshall Islands

FOR IMMEDIATE RELEASE

**Washington, DC – May 21, 2021:** The Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation<sup>1</sup> with the Republic of the Marshall Islands.

The economy of the Marshall Islands was performing well prior to the COVID-19 outbreak, but the pandemic and containment measures have strained the economy. Real GDP is estimated to have increased by around 6.5 percent in FY2019 (October 1-September 30), driven by strong fishery and construction activities. The COVID-19 travel restrictions have significantly impacted fisheries, construction, transportation, and tourism related activities. As a result, GDP is expected to have contracted by 3.3 percent in FY2020.

Economic activity is expected to continue declining in FY2021 and rebound only in FY2022. RMI is leading in the vaccine roll-out in the Pacific Island region but faces challenges in inoculating the outer island population. As a result, containment measures are expected to be in place through end-FY2021, weighing on economic activity. A rebound in activity is expected in FY2022, assuming gradually easing health restrictions. In the medium term, economic growth is projected at around 1.6 percent due to continued emigration to the US, while inflation should be converging to U.S. levels of around 2 percent. The fiscal and external balances are expected to be in surplus in the near term, benefiting from higher grants, but to move to deficits from FY2023, assuming expiring Compact grants and stagnant fishing revenues.

Uncertainty around the economic outlook is exceptionally high, and risks are tilted to the downside. A worsening of the pandemic, locally or elsewhere, could adversely impact economic activity. The issuance of the digital currency SOV as a second legal tender would raise risks to macroeconomic and financial stability as well as financial integrity. Establishing a Digital Economic Zone (DEZRA) would introduce additional financial integrity risks. These combined with anti-money laundering and combatting the financing of terrorism (AML/CFT) risks (including those related to the SOV and DEZRA) could jeopardize the RMI's last USD corresponding banking relationship (CBR), resulting in a significant drag on the economy. Climate change and related natural disasters are other sources of downside risks. Without enough fiscal consolidation, the country will face increased fiscal risks of a fiscal cliff if the Compact financial provisions between RMI and the United States expire in FY2023. Alternatively, the potential renewal of the expiring Compact grants on favorable terms presents an upside risk.

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<sup>1</sup> 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.

## Executive Board Assessment<sup>2</sup>

Executive Directors commended the authorities for their strong and swift containment measures that successfully prevented a domestic outbreak of the pandemic, and for implementing a policy package that helped to support the economy. Directors noted that risks to the outlook are tilted to the downside and underscored the importance of policy measures to ensure long-term fiscal sustainability, safeguard financial stability, and promote a green, inclusive, and sustainable post-COVID recovery.

Directors agreed that the supportive fiscal responses should continue in the near-term, complemented by governance safeguards to promote fiscal transparency. Once the recovery has firmed, Directors emphasized that a gradual fiscal consolidation is necessary to support long-term fiscal self-reliance. They encouraged adopting a multipronged strategy focused on reducing recurrent spending, implementing the tax reforms, strengthening the PFM, and establishing a medium-term fiscal framework.

Directors emphasized the importance of preserving financial stability and integrity. They welcomed the authorities' cautious approach on the Sovereign initiative which, if repealed, would eliminate related macroeconomic, financial stability, and financial integrity risks from the issuance of a decentralized digital currency as a second legal tender. Directors, however, cautioned against the new initiative of establishing a Digital Economic Zone, which could potentially also pose significant financial stability and integrity risks that would not be easily managed, given the country's limited capacity. In this regard, Directors emphasized the importance of strengthening the AML/CFT framework in line with international standards. Moreover, they recommended to strengthen the capacity of relevant agencies to ensure proper oversight of offshore activities and effective mitigation of related risks to financial integrity. These are critical to improve correspondent banking relationship.

Directors noted that Republic of Marshall Islands is vulnerable to climate change shocks. They welcomed the authorities' commitment to finalize the National Adaptation Plan in 2021 and called for steadfast actions to address immediate disaster risks, prioritize key adaptation investments, and integrate resilience and disaster risk costs in the budget.

Directors emphasized that structural reforms are needed to promote sustainable and inclusive growth. They recommended accelerating the momentum of SOE reforms to help reduce fiscal pressures and improve economic efficiency. Directors also encouraged reforming land registration, building skilled workforce, closing infrastructure gaps, and enhancing access to finance for the private sector.

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<sup>2</sup> 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 summing up can be found here: <http://www.IMF.org/external/np/sec/misc/qualifiers.htm>.

**Table 1. Marshall Islands: Selected Economic Indicators, FY 2016-26 1/**

Nominal GDP: US\$ million 239(FY 2019)

GDP per capita: US\$4,073 (FY 2019)

Population: 58,791 (FY 2019)

Quota: SDR 3.36 million

	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
							Proj.				
<b>Real sector</b>											
Real GDP (percent change)	1.4	3.3	3.1	6.5	-3.3	-1.5	3.5	2.5	2.0	1.8	1.6
Consumer prices (percent change)	-1.5	0.1	0.8	-0.5	0.6	1.1	1.5	2.0	2.0	2.0	2.0
<b>Central government finances (in percent of GDP)</b>											
Revenue and grants	60.7	68.7	62.6	62.0	66.5	85.7	71.0	70.2	66.9	63.0	64.5
Total domestic revenue	31.4	37.9	32.2	31.9	32.3	30.4	31.2	31.3	41.0	40.7	40.4
Grants	29.3	30.8	30.4	30.0	34.2	55.3	39.8	38.9	25.8	22.3	24.1
Expenditure	56.8	64.2	60.0	63.7	66.4	85.1	72.3	71.7	70.1	66.5	68.5
Expense	53.8	58.1	55.5	61.2	60.2	76.9	59.8	59.8	59.9	60.0	60.1
Net acquisition of nonfinancial assets	3.1	6.1	4.5	2.5	6.2	8.2	12.4	11.9	10.2	6.5	8.4
Net lending/borrowing	3.9	4.4	2.5	-1.8	0.0	0.6	-1.3	-1.5	-3.3	-3.5	-3.9
Compact Trust Fund (in millions of US\$; end of period)	294.5	356.9	402.4	434.7	480.0	525.7	574.5	626.7	631.4	635.7	620.8
<b>Balance of payments (in percent of GDP)</b>											
Current account balance	13.5	5.2	4.0	-25.4	2.2	2.6	0.4	-0.2	-0.5	-1.7	-2.7
Goods and services balance	-42.2	-46.3	-46.6	-72.9	-50.3	-57.0	-60.0	-57.8	-56.0	-56.7	-57.2
Primary income	29.4	27.8	26.0	22.2	27.1	27.9	29.0	29.0	38.5	38.0	37.6
<i>Of which: fishing license fee</i>	12.5	12.5	11.9	10.5	11.5	9.5	10.0	10.2	10.1	10.0	9.9
Secondary income	26.3	23.7	24.6	25.3	25.5	31.7	31.4	28.5	17.0	17.1	16.9
<i>Of which: compact current grants</i>	16.0	14.7	14.3	15.4	14.3	14.3	13.5	12.8	3.5	3.4	3.4
<i>Of which: other budget and off-budget grants</i>	8.8	7.6	9.5	9.7	10.2	16.4	17.1	15.1	13.0	13.2	13.2
Current account excluding current grants	-11.4	-17.1	-19.8	-50.5	-22.3	-28.1	-30.2	-28.1	-4.0	-5.1	-6.0
External PPG debt (Percent of GDP; end of period) 2/	41.4	36.8	32.7	27.8	27.5	26.2	25.3	25.1	26.7	28.8	31.3
Exchange rate											
Real effective exchange Rate (2010 =100)	120.3	120.7	121.5	97.2	...	...	...	...	...	...	...
Memorandum item:											
Nominal GDP (in millions of US\$)	201.5	211.9	221.6	239.5	234.1	234.1	247.1	258.3	268.8	279.1	289.2

Sources: RMI authorities; and IMF staff estimates and projections.

1/ Fiscal year ending September 30.

2/ Assumption is that RMI will continue to receive 100 percent of its MDBs financial assistance in the form of grants.



# REPUBLIC OF THE MARSHALL ISLANDS

## STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION

May 6, 2021

### KEY ISSUES

**Context.** Strong and timely containment measures have successfully prevented a domestic COVID-19 outbreak but have also weighed on economic activity. The real GDP is estimated to have contracted by 3.3 percent in FY2020 and is projected to further decline by another 1.5 percent in FY 2021 due to continued travel restrictions. Economic activity is expected to pick up in FY2022, as COVID-related restrictions will be relaxed gradually. The government is currently negotiating the renewal of Compact of Free Association (COFA) financial provisions with the United States, but terms remain uncertain. The government is considering to repeal the SOV Act and a bill on establishing a Digital Economic Zone was submitted to the Parliament recently.

**Policy recommendations:** Policies should focus on ensuring a durable recovery in the short term and maintaining fiscal sustainability in the long term, while strengthening financial stability and tackling structural challenges. Specifically:

- **COVID-19 response.** The COVID-19 pandemic responses in train should continue, with well targeted measures, to enable a strong economic recovery.
- **Fiscal.** A gradual fiscal consolidation is needed once the recovery is firmly underway to mitigate the risks of a fiscal cliff and support long-term fiscal self-reliance. Multipronged policies are needed to implement the required adjustment measures.
- **Financial stability.** Safeguarding financial stability requires a cautious approach to the SOV and the proposed Digital Economic Zone, strengthening the AML/CFT framework and institutional capacity, including with respect to the “offshore” sector, and strengthening financial sector oversight.
- **Structural reforms.** Promoting a green, inclusive, and sustainable post-COVID recovery requires timely adoption of a National Adaptation Plan to climate change, steadfast implementation of planned SOE reforms, and reforms to promote a dynamic private sector.

Approved By  
**Thomas Helbling and  
 Martin Sommer**

Discussions took place by video conference during March 1–18, 2021. The staff team comprised Yong Sarah Zhou (head), Mouhamadou Sy, Jermy Mudong, Sang mok Lee, Biying Zhu (all APD), Kathleen Kao (LEG), and Sonja Davidovic (MCM and ITD). Byung Hee Yoo (OED), Andrew Blackman (World Bank), and Mark Sturton and Glenn Mckinlay (both US Graduate School) participated in the mission. Thomas Helbling (APD) and Chang Huh (OED) attended the Concluding Meeting. The team met with Finance Minister Alfred Alfred Jr, Secretary of Finance Patrick Langrine, Banking Commissioner Sultan Korean, other government officials, representatives of the private sector, and development partners. Seble Abebe (APD) provided excellent editorial assistance for the preparation of this report.

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