Maldives: 2024 Article IV Consultation-Press Release; Staff Report; and Statement by the Executive Director for Maldives

INTERNATIONAL MONETARY FUND

INTERNATIONAL MONETARY FUND

IMF Country Report No. 24/106

MALDIVES

May 2024

2024 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR MALDIVES

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 2024 Article IV consultation with Maldives, 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 March 20, 2024 consideration of the staff report that concluded the Article IV consultation with Maldives.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on March 20, 2024, following discussions that ended on February 6, 2024, with the officials of Maldives on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on February 28, 2024.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staff of the International Monetary Fund (IMF) and the International Development Association (IDA).
- A **Statement by the Executive Director** for Maldives.

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PRESS RELEASE

PR 24/152

IMF Executive Board Concludes 2024 Article IV Consultation with Maldives

FOR IMMEDIATE RELEASE

Washington, DC – May 13, 2024: The Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Maldives.

Despite headwinds from the war in Ukraine, the Maldives' economic recovery from COVID-19 pandemic has shown resilience. The economy grew by 13.9 percent in 2022, with the tourism sector contributing to about one third of growth. Inflation has been contained at 1.9 percent y-o-y in December 2023, helped by falling food and energy prices and price subsidies.

The successful implementation of goods and services tax (GST) rate hikes has borne fruit, bringing sizable revenue windfalls in 2023. Nevertheless, the overall fiscal deficit is estimated to reach13.4 percent of GDP in 2023, with public debt to rise further to 118.7 percent of GDP in 2023. Reflecting surging capital goods imports, high import costs of food and fuel, and strong import demands associated with tourism activity, the current account deficit sharply widened to 22.8 percent of GDP in 2023. Gross international reserves declined to US$ 589 million at end-2023, covering about 1.4 months of prospective imports.

Real GDP growth is estimated to moderate to 4.4 percent in 2023, before gradually rising to 5.2 percent in 2024. Looking ahead, the Velana international airport terminal expansion and associated increase in hotel accommodation capacities is projected to further boost growth potential. Amid elevated commodity prices coupled with continued strong import demands, the current account deficit is projected to remain large albeit gradually narrow over the medium term. Without significant policy changes, the Maldives remains at high risk of external and overall debt distress. Uncertainty surrounding the outlook is high and risks are tilted to the downside, including from delayed fiscal consolidation and weaker growth in key sources markets for tourism. The Maldives is highly vulnerable to climate change risks, with potentially severe economic costs due to floods and rising sea level.

Executive Board Assessment[2]

Executive Directors welcomed the Maldives' strong post-pandemic recovery, but underlined that large fiscal and external vulnerabilities persist and risks are titled to the downside. Against this background, Directors stressed the need for immediate policy adjustments to safeguard macroeconomic and financial stability, restore debt sustainability, and support sustained strong and inclusive growth.

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[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.

[2] 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.

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Directors welcomed the authorities' commitment to advance their homegrown fiscal reforms. They underscored that strong and credible fiscal consolidation is urgently needed to restore debt sustainability and help rebuild international reserves. This should entail a combination of holistic expenditure rationalization and further domestic revenue mobilization. Strengthening public financial and debt management is also critical to enhance the effectiveness of fiscal policy.

Directors concurred that better fiscal and monetary policy coordination should facilitate necessary monetary policy actions to safeguard the exchange rate peg. To this end, they commended the authorities' decisive action to discontinue the exceptional use of the Maldives Monetary Authority advances, and underscored that this should be complemented by more active liquidity management over time. Directors also encouraged an acceleration of foreign exchange market reforms to enhance the credibility of the peg.

Directors urged the authorities to adopt macroprudential policies to help mitigate systemic risks stemming from the sovereign-bank nexus. They encouraged the authorities to swiftly introduce macroprudential institutional framework and instruments and further develop the systemic risk monitoring capacity. Directors considered that the financial safety net needs to be strengthened, along with enhancing financial sector oversight and crisis management. They emphasized that addressing gaps in the legal framework and implementing the AML/CFT framework remain a priority.

Directors encouraged the authorities to accelerate reform efforts to support inclusive and sustainable development. They emphasized that improving the business climate, strengthening governance and tackling corruption, and enhancing skill developments are crucial to boost growth potential and competitiveness. Given the Maldives's high vulnerability to climate change, Directors underscored that reforms to integrate climate considerations into the public financial and investment management processes and frameworks will help support climate adaptation and mitigation efforts and mobilize additional climate finance.

Maldives: Selected Economic Indicators 2021-2029

Population (2022): 523,787
GDP per capita (in U.S. dollars, 2022): 11,818
Poverty rate (in percent, $6.85 per day per person, 2019): 3.9
Quota (in million SDRs, as of December 2023): 21.2

	2021	2022	2023	2024	2025	2026	2027	2028	2029
			Est.			Projections			
Output and Prices (annual percentage change)									
Real GDP	37.3	13.9	4.4	5.2	6.5	5.0	4.8	4.5	4.5
Inflation (end-of-period) 1/	0.2	3.3	1.9	4.8	2.3	2.0	2.0	2.0	2.0
Inflation (period average) 1/	0.2	2.6	2.6	3.8	3.0	2.0	2.0	2.0	2.0
GDP deflator	4.7	1.6	2.6	2.4	3.0	2.0	2.0	2.0	2.0
Central Government Finances (in percent of GDP)									
Revenue and grants	25.7	30.5	32.3	30.0	29.3	29.2	29.2	29.1	29.1
Expenditure and net lending	39.5	41.5	45.7	42.2	38.6	36.1	34.6	33.9	33.3
Overall balance	-13.8	-11.0	-13.4	-12.2	-9.4	-6.9	-5.4	-4.8	-4.2
Overall balance excl. grants	-15.0	-12.1	-14.1	-13.3	-10.1	-7.6	-6.1	-5.4	-4.8
Financing	13.8	11.0	13.4	12.2	9.4	6.9	5.4	4.8	4.2
Of which:									
Financing gap 2/	…	…	…	2.9	…	…	…	…	…
Primary balance	-11.2	-7.4	-9.6	-7.6	-4.9	-2.9	-1.5	-1.0	-0.5
Public and publicly guaranteed debt	119.9	110.4	118.7	121.1	118.8	117.0	114.3	111.6	108.5
Monetary Accounts (annual percentage change)									
Broad money	26.2	6.0	7.9	7.7	9.7	7.1	6.9	6.6	6.6
Domestic credit	8.8	12.4	13.1	12.4	12.6	10.9	10.5	9.9	9.6
Balance of Payments (In percent of GDP, unless otherwise indicated)									
Current account	-8.4	-16.1	-22.8	-19.4	-13.9	-12.9	-10.0	-9.7	-9.9
Of which:									
Exports	5.3	6.4	6.6	6.1	5.8	5.6	5.4	5.2	5.1
Imports	-44.3	-53.2	-49.5	-48.2	-46.4	-44.9	-44.2	-44.0	-43.9
Tourism receipts (in nonfactor services, net)	65.1	72.1	60.8	60.8	60.8	60.8	60.8	60.8	60.8
Income (net)	-9.9	-11.4	-12.4	-10.3	-10.1	-9.7	-9.7	-9.6	-9.6
Current transfers	-7.8	-7.8	-8.3	-7.8	-8.3	-8.5	-6.4	-5.7	-6.0
Capital and financial account (including e&o)	5.1	16.5	19.2	18.3	14.7	12.6	13.3	12.1	11.0
Of which:									
General government, net	3.8	3.0	3.9	2.5	2.6	4.0	2.0	1.8	0.7
Banks and other sectors, net	-2.7	2.5	3.8	0.2	0.3	0.3	0.3	0.3	0.3
Overall balance	-3.3	0.4	-3.6	-1.1	0.7	-0.2	3.2	2.4	1.1
Gross official reserves (in millions of U.S. dollars, e.o.p.)	806	832	589	512	565	539	824	1,051	1,161
In months of GNFS imports	2.0	2.1	1.4	1.1	1.2	1.1	1.6	1.9	2.0
Exchange Rate (rufiyaa/U.S. dollars, e.o.p.)	15.4	15.4	15.4	15.4	15.4	15.4	15.4	15.4	15.4
Memorandum Items									
GDP (in millions of rufiyaa)	83,098	96,132	103,011	110,937	121,696	130,384	139,375	148,558	158,346
GDP (in millions of U.S. dollars)	5,392	6,238	6,685	7,199	7,897	8,461	9,044	9,640	10,276
Tourism bednights (000')	10,073	12,260	13,103	14,123	15,689	16,693	17,650	18,482	19,392
Tourist arrivals (000')	1,322	1,675	1,879	2,018	2,210	2,385	2,521	2,640	2,770
Tourism bednights (% change)	152.8	21.7	6.9	7.8	11.1	6.4	5.7	4.7	4.9
Tourist arrivals (% change)	137.8	26.7	12.1	7.4	9.5	7.9	5.7	4.7	4.9
Dollarization ratio (FC deposits in percent of broad money)	…	…	…	…	…	…	…	…	…

Sources: Maldivian authorities; World Bank; and IMF staff projections.
1/ CPI-Male definition.
2/ Including possible new sources of domestic financing or negotiated official bilateral financing as higher external financing costs are limiting options to tap international capital markets.

INTERNATIONAL MONETARY FUND

MALDIVES

STAFF REPORT FOR THE 2024 ARTICLE IV CONSULTATION

February 28, 2024

KEY ISSUES

Context. Despite headwinds from the war in Ukraine, the Maldives' economic recovery from the COVID-19 pandemic has shown resilience. The cyclical rebound and still favorable economic outlook provide an opportunity for the Maldives to address its large fiscal and external vulnerabilities. This calls for immediate policy actions to rebuild economic resilience and reduce debt to a sustainable level. Given that the Maldives is highly vulnerable to climate change, early actions to rein in debt vulnerabilities will help support the Maldives' efforts to scale up the much-needed climate adaptation investments in a resource constrained context.

Article IV consultation. The discussions focus on comprehensive policy reforms to address fiscal vulnerabilities, stem rising balance of payments pressures, and safeguard financial stability, while supporting sustained strong and inclusive growth.

Policy recommendations. Front-loaded fiscal adjustments, accompanied by tighter monetary and macroprudential policies, are urgently needed to reduce vulnerabilities and restore sustainability of public finances.

- **Fiscal policy**. Swift implementation of the strong and credible form of fiscal consolidation comprising expenditure rationalization and domestic revenue mobilization is urgently needed. Strengthening public financial, investment, and debt management is critical to enhance the credibility and effectiveness of fiscal policy.
- **Monetary and exchange rate policies**. Monetary policy needs to be tightened to ensure compatibility with the exchange rate peg. Foreign exchange market reforms should be accelerated to enhance the credibility of the peg.
- **Financial sector policy**. Adopting macroprudential policies will help mitigate systemic risks stemming from sovereign-bank nexus. Financial sector oversight and crisis management should be further enhanced.
- **Macro-structural policy**. Strengthening institutions to support climate adaptation and mitigation efforts and mobilize climate finance is crucial. Improving the business climate, addressing governance and corruption vulnerabilities, and enhancing skill developments will help support strong and inclusive growth.

Approved By
Anne-Marie Gulde-Wolf (APD) and Boileau Yeyinou Loko (SPR)

Discussions took place in Malé during January 23 – February 6, 2024. The IMF team comprised P. Sodsriwiboon (Head), Y. Ojima, Y. Xu (all APD), T. Wezel (MCM), and A. Remo (ICD). Anne-Marie Gulde-Wolf (APD) joined policy discussions and the concluding meeting. A. Abdul Raheem (OEDMI) joined the mission. Mr. Mohieldin (OEDMI) joined the concluding meeting. The team met with President M. Muizzu, Finance Minister M. Shafeeq, Maldives Monetary Authority Governor A. Hashim, other senior government and central bank officials, development partners, and representatives of the business community. G. Gamwalla-Khadivi and R. Yang (both APD) contributed to the preparation of this report.

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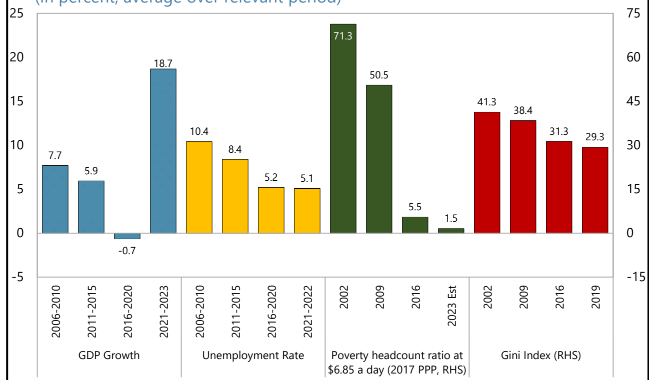
TABLES

ANNEXES

CONTEXT

1. **The Maldives' economic recovery from COVID-19 pandemic has shown resilience**. Despite headwinds from Russia's war in Ukraine, tourist arrivals have steadily increased and are set to reach a historic high in 2023. Amid a buoyant tourism sector, real GDP surpassed its pre-pandemic level in 2022. Nevertheless, economic scars remain, particularly related to losses in education opportunities[1]. Robust growth has also contributed to sustained poverty and inequality reduction, with poverty level[2] falling to an estimate of about 1.5 percent of total population in 2023 from 3.9 percent in 2019.



Sources: MMA; ILO; World Bank's World Development Indicators; and IMF Staff Calculations and Estimates.

2. **The cyclical rebound and still favorable economic outlook provide a narrow window of opportunity for the Maldives to fix its large fiscal and external imbalances**. Over the years, sizeable infrastructure spending push and generous social assistance programs have led to a sharp rise in public debt. Large external financing requirements to support public spending have added pressures on external stability. This calls for immediate policy actions to tackle these long-standing vulnerabilities, importantly for the Maldives to rebuild its economic resilience, regain financial market access when needed, and avoid any forced disruptive adjustments. Being one of the lowest lying nations in the world, the Maldives' vulnerability to natural disasters and climate change is paramount. Early actions to rein in debt vulnerabilities will help support the Maldives' efforts to scale up the much-needed climate adaptation investments in a resource constrained context.

3. **The new government is committed to restore macroeconomic stability, while sustaining growth**. Past Fund policy advice gained traction, importantly the implementation of the tourism and domestic goods and services tax (TGST and GST respectively) rate hikes among others (Annex I). The current administration sees the urgency of reducing debt and putting public finances on a more sustainable footing. The Presidential address in February 2024 laid out fiscal adjustment measures, including subsidy reforms that phase out existing subsidies and replace them with targeted direct income transfers, healthcare reform, capital expenditure rationalization, and reforms of state-owned enterprises (SOEs), and the authorities are committed to urgently implement them. Given tourism sector's dominant role in the Maldivian economy, the government prioritizes policies to further expand tourism activities, including to expedite the completion of Velana International

[1] Losses in education opportunities remain significant, with secondary school enrollment rates still lower than pre-pandemic levels (https://www.moe.gov.mv/assets/upload/STAT_BOOK_2021_2022_V2.1_ready.pdf).

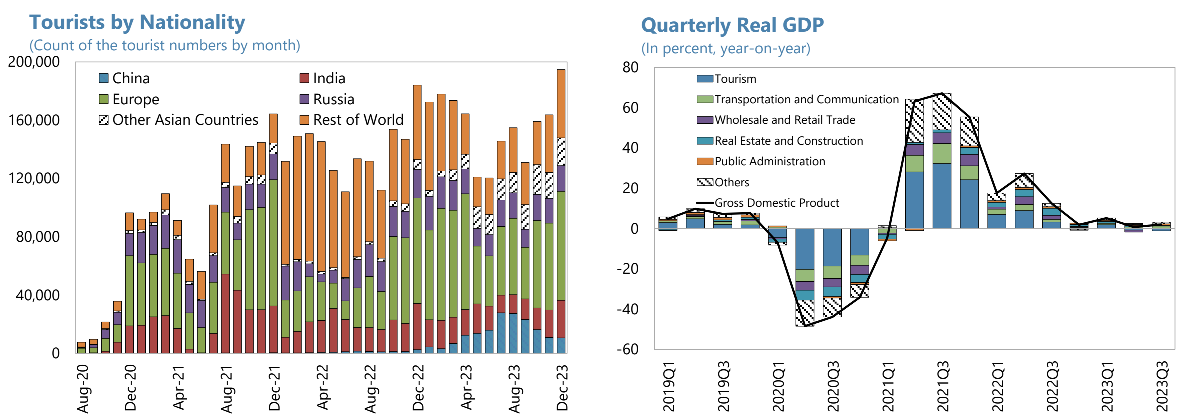
[2] Based on World Bank's *Maldives Economic Update* (October, 2023), data are measured at the US$6.85 poverty line in 2017 purchasing power parity.

Airport (VIA) terminal expansion. The government also emphasizes policies to reduce spatial disparities between Malé and other atolls and support sustainable development.

RECENT DEVELOPMENTS

4. The Maldives' post pandemic growth has been strong, but recently normalized. After a brief contraction of tourist arrivals following the war in Ukraine, the tourism sector was quickly back to a strong footing, benefited from the Maldives' diversified source countries and China's re-opening at end-2022 (Text Figure 1). The economy grew by 13.9 percent in 2022, with the tourism sector contributing to about one third of real GDP growth. Tourist arrivals in 2023 reached a historic high of 1.88 million. Nevertheless, real GDP growth in 2023 is estimated to moderate to 4.4 percent. The airport terminal capacity constraints and increased diversification of tourist arrivals, shifting in part toward shorter stay and guesthouse-based travelers, despite their contribution to the overall increase in tourism revenue, led to growth slowdown (Box I).

Text Figure 1. Maldives: Tourist Arrivals and Economic Activity



Sources: Maldives Monetary Authority, Maldives Bureau of Statistics, and IMF Staff Calculations.

5. Inflation has been contained, amid price subsidies. Reflecting the base effect due to the GST rate hikes—effective in January 2023—and high commodity prices, headline inflation in Malé rose in the first half of 2023, peaking at 3.8 percent year-on-year (y-o-y) in April. Nevertheless, vast existing price subsidies have limited the pass-through from GST rate hikes and global commodity price pressures to headline inflation. Helped by falling food and energy prices, Malé inflation declined to 1.9 percent y-o-y in December 2023.

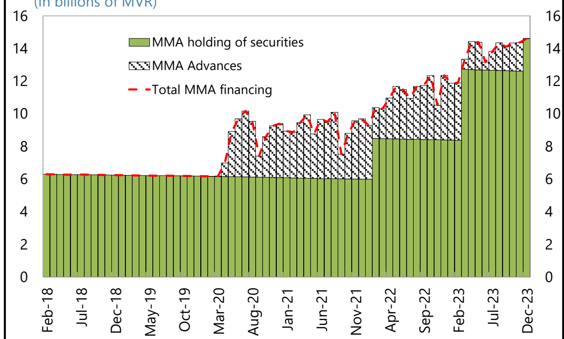
6. Fiscal vulnerabilities remain elevated. The successful implementation of GST rate hikes is estimated to yield tax revenue gains of about 3.2 percent of GDP in 2023[3]. Nevertheless, the overall fiscal deficit is estimated to reach 13.4 percent of GDP in 2023, up from 7.8 percent of GDP envisaged in the initial budget. The widened fiscal deficit was due to spending pressures from

[3] GST rate hikes are expected to yield GST revenue collections of 12.9 percent of GDP in 2023, compared with a counterfactual analysis without GST reforms that would yield GST revenue collections of 9.7 percent of GDP.

significant increases in capital spending, rising interest costs amid increased debt stock and tight global financial conditions, increased subsidies related to medical services, fuel and electricity, and election-related expenditure. Support to state-owned enterprises (SOEs) are also added risks to fiscal sustainability, as they often require large and ad-hoc budget support to address their solvency and liquidity issues (Annex IV).

7. Public debt rose further. Total public and publicly guaranteed (PPG) debt is estimated to increase to MVR 122 billion, about 118.7 percent of GDP in 2023. While robust recovery in tourism and growth has helped suppress debt-to-GDP ratio in recent years, gross financing needs are substantial, due to large fiscal deficits and increased debt services repayments. Amid limited access to external financing, rising fiscal financing needs are being met by domestic debt issuance and monetary financing, with bank financing through purchases of government securities continued to underpin most of domestic financing in 2023. The authorities discontinued monetary financing at the end of 2023 and securitized the outstanding Maldives Monetary Authority (MMA) advances into 30-to-40-year government bonds in early 2022, then February and December 2023, with face values of MVR 2.5 billion, 4.4 billion, and 1.9 billion, respectively.

Maldives: Central Bank Fiscal Financing
(In billions of MVR)



Source: Maldives Monetary Authority.

8. The current account deficit sharply widened. Despite robust tourism revenues, the current account deficit is estimated to further deteriorate to 22.8 percent of GDP in 2023, due to surging capital goods imports, high import costs of food and fuel, and strong import demands associated with tourism activity. This has led to persistent foreign exchange (FX) shortages with significant spread of around 10-15 percent between the official and parallel market rates. Real effective exchange rate marginally appreciated in the first eight months of 2023, and stayed well above its long-term historical average. Gross international reserves steadily declined to US$589 million at end-December 2023, covering about 1.4 months of prospective imports. The overall external position in 2023 is assessed to be substantially weaker than the level implied by fundamentals and desirable policies, which urgently requires upfront fiscal consolidation to contain external financing needs and rebuild FX reserve buffers to reduce vulnerabilities and risks (Annex II).

OUTLOOK AND RISKS

9. Growth is projected at 5.2 percent in 2024 (Table 1-5). Tourist arrivals are expected to rise further and the authorities forecast 2 million tourist arrivals for 2024. The resilience in the tourism sector and associated spillovers to other sectors will continue to drive economic activity, although the pace is moderating. The VIA terminal expansion and associated increase in hotel accommodation capacities is projected to further boost growth potential, upon the expected completion in 2025[4] and over the medium term. The planned phasing out of subsidies is expected to add inflationary pressures, with inflation projected to rise to 3.8 percent in 2024 then gradually decline to 3 percent in 2025.

10. Despite reform measures to recurrent expenditure, fiscal sustainability without additional strong policy measures will remain at risk. Long-standing subsidy reforms are expected to take off in July 2024, which entails phasing out subsidies on fuel, electricity, and food staples by end of the year and rolling out direct income transfers targeting vulnerable households. Rationalization on health insurance scheme, *Aasandha*, and other medical expenditures, which encompasses facilitating bulk procurement to generate cost savings and imposing revised coverage prices, is expected to be implemented in the latter half of 2024. Complete enactment of the expected subsidy and medical expenditure reforms will help reduce total fiscal expenditure by 1.9 percent of GDP in 2024. The overall fiscal deficit is projected to narrow marginally to 12.2 percent of GDP in 2024, and public debt would stay above 110 percent of GDP over the medium term. Without policy changes, SOEs are expected to remain vulnerable, as liquidity and solvency risks persist.

11. The external sustainability hinges critically on fiscal adjustments. Given high commodity prices and continued public investment, imports of food, fuel, and capital goods will weigh on trade balance, leading to persistently high current account deficit of 19.4 percent of GDP in 2024. While the completion of airport terminal expansion will help ease up import demands, the expected rise in external debt services payments and profit remittance associated with FDI will continue to weigh on the current account balance to remain at around 10 percent of GDP over the medium term. In absence of corrective policies, FX reserves are projected to remain suppressed in the near term, covering about 1 month of prospective imports, before gradually rising over the medium term.

12. Debt vulnerability persists. The joint IMF-World Bank Debt Sustainability Analysis (DSA) assesses that, without significant policy changes, the Maldives remains at high risk of external and overall debt distress, and protracted breaches in several debt indicators over the medium term make the assessment of debt unsustainable. Gross external financing needs are expected to rise in the coming years, reflecting persistently large fiscal deficits and repayments and rollovers of non-concessional debt, mainly global sukuk. External refinancing pressures are expected to peak in 2026. Increasingly higher amortizations and large interest payments would trigger protracted breaches in several debt indicators by 2026, similar to the previous DSA. The debt dynamics will remain vulnerable to adverse shocks in growth, interest rates, and fiscal position in the near term.

13. Uncertainty surrounding the outlook remains high and risks are tilted to the downside (Annex III). Delayed fiscal consolidation and failure to reduce public debt will risk economic stability. Weaker growth in key source markets for Maldives' tourism could adversely affect tourism revenue, with spillovers on to the rest of the economy. In particular, as China is expected to remain one of the largest tourist source markets for the Maldives, growth could be weighed down by China's structural

[4] The authorities are expediting the VIA terminal expansion to be completed in the last quarter of 2024, which could potentially provide an upside risk to growth.

deceleration, which may lower Chinese tourist arrivals in the medium term (Box II). A renewed uptick in global energy and food prices could widen current account deficit, further drawn on the already-thin FX reserve buffers. Tighter global financial conditions could add to interest costs and reduce options for market financing to the government. The Maldives is highly vulnerable to climate change risks, with potentially severe economic costs due to floods and rising sea level.

Authorities' Views

14. The authorities broadly agreed with staff's assessment on the outlook and risks and highlighted several upside risks. They concurred that the return to normal growth rates was faster than anticipated, supported by the expansion of new source markets and connectivity despite some compositional changes in tourists' average stay and spending preferences. The authorities emphasized that the guesthouse sector is a segmented market and could help diversify the products offered by the tourism industry. At the same time, they underscored several upside risks to the tourism sector outlook. First, the new terminal of VIA could be operational sooner-than-expected, thus augmenting the airport capacity to accommodate tourists considerably in the near term. Second, diversification of resorts and guesthouses offerings can appeal to tourists with different preferences when the bottleneck on airport capacity is lifted, which will further expand tourism revenue. Third, upside risks to the outlook of key source markets (e.g., China) could help generate additional revenue in the tourism sector.

KEY POLICY ISSUES

Comprehensive policy reforms will be paramount to urgently reduce fiscal vulnerabilities, stem rising balance of payments pressures, and safeguard financial stability, while supporting sustained strong and inclusive growth.

15. Policy mix. With limited policy space and growing balance of payments pressures, the authorities should swiftly implement front-loaded fiscal adjustments, accompanied by tighter monetary and macroprudential policies, to reduce vulnerabilities, restore sustainability of public finances, and lessen FX pressures. This will help avoid disruptive adjustments and lay the foundation for strong, inclusive, and sustainable growth.

- Under staff's baseline scenario (Table 1-5), which reflects the authorities' established policies and implementations of some expenditure reforms[5], elevated near-term fiscal spending push will continue to put substantial pressures on the domestic economy and the current account. In the face of a prolonged period of over-expansionary macroeconomic policy mix, limited access to market financing has been followed by declining official financing. The resulting decline in FX reserves would continue to weigh on economic stability and confidence, crowd out private

[5] In the baseline forecast, the subsidy reform measures on energy, electricity, and other items and Aasandha reforms will be implemented since July 2024, as currently envisaged in the 2024 budget. However, expensive medical services will remain covered by Aasandha and rationalization on capital expenditure is limited.

investment to support growth, expose macro-financial risks, and risk disruptive adjustments down the road.

- Under staff's proposed policy adjustment scenario (Text Table 1), public spending is further scaled back, while domestic revenue mobilization continues to progress, and monetary policy is tightened. These measures would promote economic stability and address the overall macroeconomic risks by limiting further public debt creation, containing the current account deficit, thus rebuilding FX reserves to more sustainable levels. Adopting macroprudential policies to rein in sovereign-bank nexus would also help limit financial sector risks. Although near-term growth is slightly more measured in this scenario, a prudent policy stance and the stronger external balance of payments would reduce macroeconomic risks and provide a sounder basis for sustained strong growth in the medium-term.

Text Table 1. Maldives: Medium-Term Macro-Fiscal Outlook

(In percent of GDP, unless otherwise indicated)

		Baseline Scenario					Policy Adjustment Scenario 1/				
	2023	2024	2025	2026	2027	2028	2024	2025	2026	2027	2028
Real GDP growth	4.4	5.2	6.5	5.0	4.8	4.5	5.0	6.3	5.5	5.2	5.0
Inflation (period average)	2.6	3.8	3.0	2.0	2.0	2.0	3.8	3.0	2.0	2.0	2.0
Revenue	32.3	30.0	29.3	29.2	29.2	29.1	30.0	29.3	30.5	30.5	30.4
o/w tax revenue	23.4	22.9	22.9	22.9	22.9	22.9	22.9	22.9	24.2	24.2	24.2
Expenditure	45.7	42.2	38.6	36.1	34.6	33.9	41.6	37.2	35.0	33.5	32.9
o/w social contributions and subsidies	11.1	9.5	8.2	8.0	8.0	8.0	9.5	8.0	7.8	7.8	7.8
capital expenditure	13.6	10.4	8.8	6.9	5.9	5.3	9.9	7.8	6.4	5.4	5.0
Central government balance	-13.4	-12.2	-9.4	-6.9	-5.5	-4.8	-11.6	-7.9	-4.5	-3.0	-2.5
Primary balance	-9.6	-7.6	-4.9	-2.9	-1.5	-1.0	-7.0	-3.5	-0.6	0.7	1.0
Public and publically guarantee (PPG)											
debt-to-GDP ratio	118.7	121.2	118.8	117.1	114.4	111.7	120.8	117.2	112.6	107.4	102.3
Gross international reserves											
in millions of US dollars	589	512	565	539	824	1,051	557	710	968	1,592	2,250
in months of prospective imports	1.4	1.1	1.2	1.1	1.6	1.9	1.3	1.6	2.0	3.0	4.1

Source: IMF Staff Projections.

1/ The policy adjustment scenario assumes a fiscal multiplier of 0.2, in line with literatures on small islands states that suggest a relatively low fiscal multipliers (see, for instance, Dodzin and Bai (2016), Alichi and others (2021) and Balasundharam and others (2023).

A. Fiscal Policy

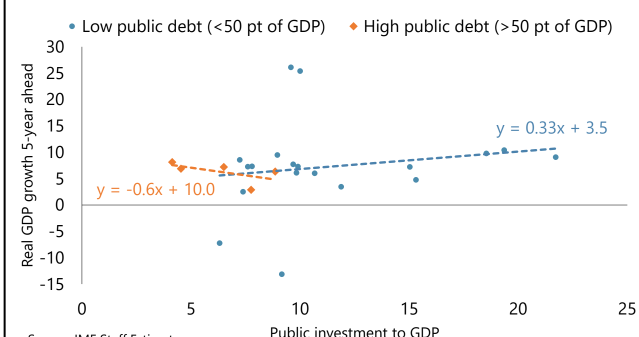
16. The successful implementation of GST rate increases is a welcome step, but additional strong and credible form of fiscal consolidation will be needed. The authorities' homegrown revenue mobilization plan that stems from GST rate hikes has borne fruit, bringing sizable revenue windfalls in 2023. The authorities' medium-term fiscal strategy (MTFS) for 2024-2026 has laudable anchors, including (i) reducing public debt to less than 95 percent of GDP by 2026, (ii) reducing primary budget deficit to less than 5 percent of GDP by 2024, (iii) maintaining PPG debt-to-GDP ratio on a downward trend, and (iv) reducing recurrent expenditure to levels that do not exceed government revenue by 2024. The 2024 budget envisages the implementation of fuel and electricity subsidy reforms in the second half of 2024, after a delay from initial announcement in January 2023, as well as some reduction in capital expenditure. Nevertheless, in staff's view, the fiscal consolidation plan envisaged under the current policies will not be sufficient to achieve these ambitious targets. The following discussion (¶17-¶20) lays out a set of recommended fiscal adjustments aiming for faster debt reduction to increase the chance of meeting such targets. To increase the chance of meeting these targets, this critically requires swift implementation of a strong and credible form of fiscal consolidation that comprises both expenditure rationalization and domestic revenue mobilization, while avoiding political temptation to spend and borrow more.

17. Holistic expenditure rationalization is a priority to narrow fiscal deficit and bring debt down.

- *Subsidy reforms* should be implemented without further delay. The 2024 budget presents a reform plan to phase out fuel, electricity, and other existing subsidies and replace them with targeted cash transfers toward low-income households, which will be implemented starting in the second half of 2024. The authorities, with the help from the World Bank, are developing a direct cash transfer mechanism that emphasizes on the vulnerable population. In the policy adjustment scenario, efforts to further rationalize and streamline health subsidies[6], *Aasandha*, could be adopted.

- *Rationalizing capital spending*. The authorities should heavily reprioritize, rationalize, and scale back capital spending, including through SOEs. Staff's analysis suggests that the Maldives' capital spending push since 2014 appears to have passed its peak economic gains, and at current high debt level, its incremental growth benefit has diminished. Hence, infrastructure development projects need to be realistically costed, appraised, and subject to transparent and rigorous project selection process for inclusion in the annual budget. Enhancing fiscal institutions and the public financial framework would enable the authorities to conduct more effective project appraisals and costings. The authorities should safeguard capital expenditure that supports growth potential, while rationalizing projects that are costly but less essential.

Maldives: Public Investment and Future Real GDP Growth 1/
(In percent)



Source: IMF Staff Estimates.
1/ Correlation between public investment and future real GDP growth was positive when public debt was below 50 percent of GDP, but turned negative when public debt was above 50 percent of GDP. Data are from 1991 to 2019. Data for COVID-19 years are excluded, due to large volatility of real GDPgrowth rates.

[6] Based on the World Bank's Maldives Public Expenditure Review (2022), spending on Aasandha health insurance scheme grew at 18 percent annually, on average between 2014 and 2019. In absence of robust procurement and purchasing system, the average drug prices under Aasandha scheme were 15 to 75 times higher than international benchmarks.

- *Public wage and pension reforms.* The continuation of pay harmonization measures, which aim to raise compensation of all public servants, is expected to add an additional MVR 3 billion (2 percent of GDP) to total government expenditure by 2026. Comprehensively reviewing the public sector wage bill and assessing the target for pay harmonization in the context of both civil service efficiency and budget sustainability is necessary to address fiscal spending pressures. This should be followed by measures to reduce unnecessary cost associated with pay harmonization in order to mitigate fiscal burden. In addition, the new pension schemes covering the public sector and state-owned enterprises are proliferated, fragmented, and costly. Early actions to streamline such schemes and phase out overly generous, tax-financed pension benefits will help reduce pension expenditures in the long term.

- *SOE reforms* are warranted to reduce additional fiscal burdens caused by SOE vulnerabilities (Annex IV). As identified by IMF technical assistance (TA), the authorities should undertake reforms to address these risks in a strategic manner, including to triage SOE portfolio, then restructure weak SOEs to ensure their financial viability and reduce the number of SOEs, particularly those either non-commercial in their operations or do not have sufficient operations to justify being classified as an SOE. In addition, reforms to develop new SOE legislation, strengthen fiscal risk and oversight framework, and improve performance management of SOEs are critical.

18. Further domestic revenue mobilization would help ensure fiscal sustainability. The medium-term revenue strategy (MTRS) presents options for revenue mobilization, including to lower the personal income tax (PIT)[7] thresholds and personal allowance, raise the top marginal PIT rate, increase the statutory rate of corporate income tax, rationalize import duty exemptions, apply excises on tobacco, fuels, alcoholic products, and motor vehicles, and impose carbon levy on fuels. Adopting additional measures to raise tax revenues, along with strengthening customs and tax administration, would yield sustained fiscal savings to increase the probability of approaching and achieving fiscal and debt sustainability.

19. Strengthening fiscal institutions and the public financial framework is critical to enhance the credibility and effectiveness of fiscal policy. IMF's Public Investment Management Assessment (PIMA) identified several weaknesses in public investment and financial management, importantly related to budget credibility and budget execution. In this regard, infrastructure development projects need to be realistically costed, appraised, and subject to transparent and rigorous project selection process for inclusion in the annual budget. Enhancing fiscal institutions and the public financial framework would enable the authorities to conduct more effective project appraisals and costings. In particular, reforms to develop a strategic and focused Public Sector Investment Program (PSIP) and a costed medium-term national development strategy should be expedited. The authorities should strengthen strategic guidance and budget ceilings for public investment, in line with the fiscal strategy statement. A ceiling for the PSIP budget included in the

[7] The PIT exemption threshold is current set at more than three times GDP per capita and the maximum of PIT rates is at 15 percent.

budget circular at the start of the budget process based on a binding resource envelope should be respected.

20. Improving debt management will help better manage financial costs and reduce debt-related risks. The authorities should urgently develop a realistic and credible multi-year debt management strategy to systemically reduce rollover and solvency risks. Finalizing the Public Debt Management Law and completing the reform of the Fiscal Responsibility Act (FRA) should be part of a broader credible plan that puts debt on a sustainable path, including by setting and disclosing realistic numerical targets for the fiscal deficit and public debt in a subsequent Charter of Fiscal Responsibility to support compliance and accountability. Rising interest burdens could be limited by avoiding non-concessional financing of non-priority spending, particularly capital spending. Deepening domestic debt markets would not only help release resources for priority spending, but also broaden investor base and reduce foreign currency risks. The authorities are taking a welcome step to develop a law for the sovereign development fund (SDF), in which it could earmark the airport development fee for crediting to the SDF along with one-off windfall revenues from resort leases, privatization proceeds, among others. The accumulation and investment of SDF in FX instruments that match the loan portfolio will also help manage external debt or servicing such debt. Given imminent climate change vulnerability to the Maldives, the authorities may continue to explore innovative financing options such as debt-for-nature swaps as part of an overall fiscal strategy.

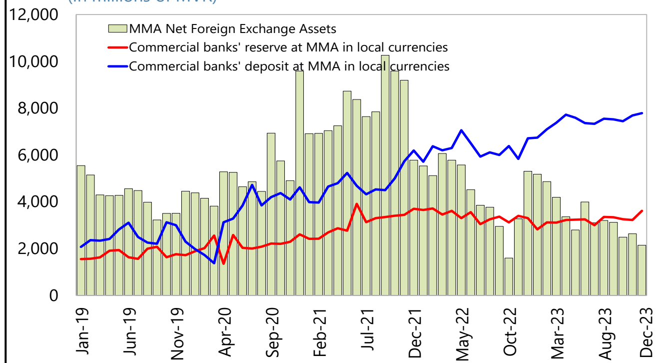
Authorities' Views

21. The authorities emphasized their readiness to undertake the necessary fiscal adjustments. They stressed that subsidy reforms will be executed from July 2024, and the preparatory work is underway while collaborating with various stakeholders. They instructed the line ministries to reprioritize the investment projects under PSIP, by appraising benefits over costs and ensuring future revenue generation. Nevertheless, the authorities cautioned against trade-offs of the impending fiscal consolidation measures, as miscalibration of subsidies reforms and capital expenditure rationalization could induce unintended growth and welfare impacts. The authorities also agreed that SOE reforms are warranted to reduce additional fiscal burdens, arising from SOE vulnerabilities. In this regard, the cabinet has endorsed an SOE reform plan, and the authorities are currently developing the reform plans for individual SOEs to ensure operational efficiency and financial viability. They underscored strengthening coordination with domestic stakeholders and multilateral donors could help pave the way for the successful implementation of fiscal policy adjustments. The authorities also highlighted that the recent resumption of the accumulation of inflows to the SDF in foreign currency would increase the debt servicing capacity in the future.

B. Monetary and Exchange Rate Policies

22. Excess structural liquidity continues to pose risks to economic stability. The peg to U.S. dollar continues to serve as a transparent nominal anchor for monetary policy. Nevertheless, the current stance of monetary policy is too accommodative, where increased MMA advances and subsequent securitization of monetary financing have translated into central bank liquidity injection and large excess structural liquidity in the system (about 7 percent of GDP or 8.1 percent of banking system's assets). The size and conditions of the past and recent securitization of MMA advances to the Government of Maldives have compromised the MMA balance sheet and impacted the MMA's ability to conduct an independent and active liquidity management to support the exchange rate peg.

Maldives: Net Foreign Exchange Assets and Excess Liquidity 1/
(In millions of MVR)



Source: Maldives Monetary Authority.
1/ Excess liquidity refers to bank deposits in excess of required reserves at the central bank.

23. Monetary policy, in concertation with other policy levers, can contribute more effectively to addressing macroeconomic vulnerabilities. Discontinuing exceptional use of MMA advances based on a temporary suspension of limits on MMA advances under the FRA is a welcome first step. [8] Raising minimum reserve requirements (MRR) rate on Rufiyaa, while ensuring policy coordination between monetary and fiscal policies, would help absorbing some excess liquidity and signal monetary tightening.[9] Going forward, more active liquidity management in domestic currency would be needed, in which MMA could rely on periodic open market operations (OMOs) to steer interest rate on commercial banks' liquidity toward an appropriate level within the interest rate corridor given by Standing Deposit and Lending Facility interest rates. Should inflationary pressures increase or the parallel market exchange rate premium widen, MMA should stand ready to further tighten monetary policy stance. In line with IMF TA, it is recommended that the MMA gradually undertakes liquidity absorbing operation to address excess structural liquidity resulted from the securitized monetary financing, initially with a maturity of one-year.

24. Accelerating long-overdue reforms of FX markets, alongside the needed macroeconomic adjustments, will enhance the credibility of the peg. The MMA, under the 2017 MMA's FX-Intervention Policy, provides weekly allocation to commercial banks based on their foreign currency asset position and net open position for import payments and telegraphic transfers

[8] Under the existing rules specified in the FRA, MMA may provide advances for liquidity management purposes only which shall not exceed 1 percent of average of the government revenues in the last three years.

[9] Based on staff's analysis, increasing MRR when commercial banks' excess liquidity is high would likely not lead to significant changes in commercial banks' interest rates. The private sector lending and deposit rates were stable in the past and have not changed significantly even after changes in MRR. This holds for MRR and commercial banks rates in both MVR and USD.

payments. In addition, the MMA, through banks, provides FX allocations to Maldivians traveling abroad for medical and education purposes and provides a maximum of US$500 per person/trip in cash for Maldivian traveling abroad, as well as to SOEs, mainly for foreign loans obligations, import payments of fuel. The rationing of foreign exchange and its allocation to certain priority items give rise to an exchange restriction[10]. The authorities are working on a comprehensive FX reform strategy through enhancing the use of Rufiyaa (e.g., for payrolls and transactions), promoting alternative financial instruments that are denominated in Rufiyaa and satiate risk appetites and liquidity preferences of large investors (e.g., SOEs), and streamlining licensing regulation on money changing businesses. The discussion with key stakeholders in the private and public sectors on the reform strategy should be expedited. The MMA should then apply the regulations on the use of the MVR as widely as possible including for all salaries and taxes. The new digital instant payment system will act as a facilitator to this process. An overhaul of the current system of money changer licenses should be directed toward channeling the FX supply through the domestic banking system.

Authorities' Views

25. The authorities agreed with the need to gradually tighten monetary policy, though it needs to be accompanied by fiscal consolidation to reduce external balance and FX pressures. The authorities noted that the temporary suspension of clauses 32 a), d) and e) of the Fiscal Responsibility Act (FRA) 2013 has expired at end-December 2023, effectively ending use of MMA advances to finance government deficits. As the first step to deal with the existing excess liquidity, the MMA considered gradually increasing MRR rate on Rufiyaa deposits to absorb up to MVR 1.5 billion of excess liquidity. They cautioned that OMOs could potentially complicate domestic financing through government securities in the near term. Over time, the MMA is looking into conducting structural/long-term OMOs to absorb the remaining excess liquidity and more regular OMOs afterward as needed. Since the MMA has not been conducting OMOs since 2014, it is seeking IMF TA on liquidity forecasting and on conducting OMOs to support such operations. The authorities also stressed on the need for close coordination between monetary and fiscal policies, especially during the rollout of the fiscal reforms.

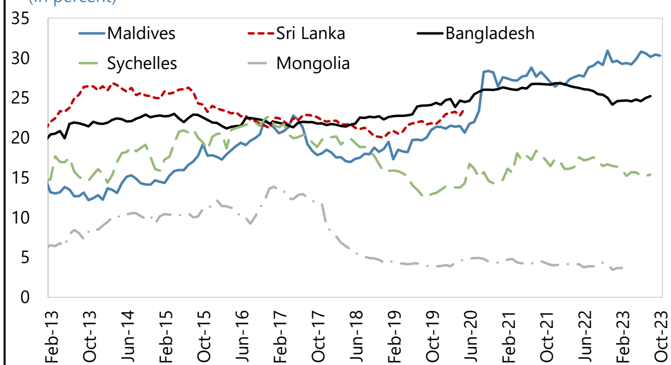
26. The MMA underscored the peg continues to serve as an appropriate policy anchor, while recognizing challenges under conditions of limited foreign exchange reserves. The MMA continued to provide FX supply to commercial banks through its regular allocations prioritizing specific priority needs. Meanwhile, the MMA has developed a package of measures to reform FX markets and shared the draft with government for technical consultation. The measures include regulating licensing criteria and conditions for money changers, encouraging the use of the Maldivian Rufiyaa in domestic monetary transactions, and limiting the types of transactions allowed through FX accounts. The MMA noted that these reforms would help improve functioning of FX markets going forward.

[10] The exchange restriction previously found has been modified due to the prioritization of FX.

C. Financial Sector Policies

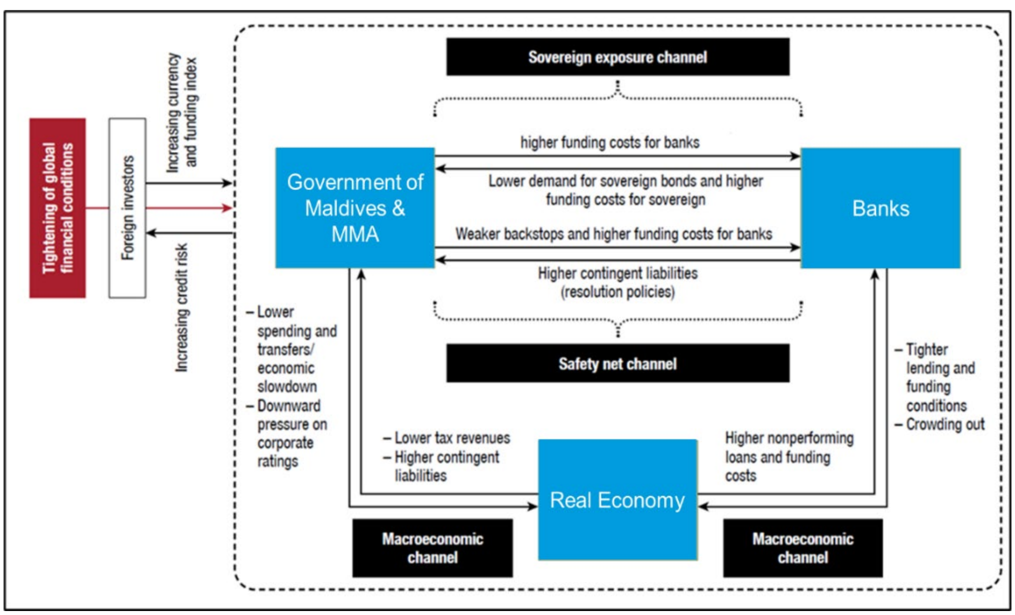
27. Systemic risks have increased, stemming largely from a growing sovereign-bank nexus, high dollarization, and a shortage of foreign exchange (Text Figure 2 and Annex V). The overall banking sector remains sound, with high capital and liquidity buffers and strong profitability (Table 6). Credit to private sector continued to recover in line with tourism-related activity, and non-performing loans ratio declined to a historic low of 5.2 percent of gross loans in September 2023. Nevertheless, macro-financial vulnerabilities in the Maldives primarily related to the sovereign-bank nexus have increased, where banking sector exposure to sovereign debt continues to rise above 30 percent of total assets, well above peer countries in the region, and sovereign exposure as share of total bank capital breaches 400 percent in some banks. The application of a zero risk-weight on domestic sovereign exposures has in part contributed to the banking sector's sizable sovereign exposures. Significant maturity mismatch also poses liquidity risk including from runs on callable foreign currency deposits. The Maldives' vulnerability to natural disasters and climate change could have repercussions on the financial sector in the longer run.

Banking Sector Sovereign Debt Holding to Total Asset Ratio
(In percent)



Sources: Haver Analytics; and IMF staff calculations.

Text Figure 2. Maldives: Macro-Financial Linkages of the Sovereign-Bank Nexus



Source: IMF Financial Sector Stability Assessment on the Maldives (2023).

28. Macroprudential policies should be adopted to mitigate systemic risks. As identified by the joint IMF-World Bank Financial Sector Assessment Program (FSAP), banks are found to be relatively resilient to economic shocks, thanks to ample interest margins. Nevertheless, an unraveling of the sovereign-bank nexus, where further stress on public finance could elevate sovereign risks leading to valuation losses on sovereign papers, would rapidly deplete bank capital. In this regard, the authorities plan to gradually phase in a 100 percent risk weight on bank holdings of Maldives government securities in foreign currency and introduce liquidity requirements. A macroprudential institutional framework and instruments should be swiftly introduced, and systemic risk monitoring capacity should be further strengthened (Table 7).

29. Financial sector oversight and crisis management need to be enhanced. Addressing weaknesses in the regulatory and supervisory frameworks through strengthening MMA independence, redefining off-site monitoring, and enhancing enforcement is crucial. With the help of IMF TA, MMA should perform a comprehensive review of the regulations and supervisory processes for loan loss provisioning with the focus on loan classifications and the transition to international financial reporting standards 9 (IFRS9). Improvements are also required in financial safety net and crisis management arrangements. Priorities include (i) making early intervention and resolution triggers forward-looking; (ii) introducing recovery and resolution planning; (iii) overhauling the use of public funds in resolution; and (iv) enhancing the deposit insurance system. An effective emergency liquidity assistance framework is needed to address challenges from the high dollarization and FX shortages. Interagency arrangements and crisis preparedness should also be strengthened.

30. The authorities should swiftly address gaps in the legal framework and enhance implementation of the AML/CFT framework. The authorities are preparing for the Maldives' mutual evaluation by the Asia/Pacific Group on Money Laundering (APG), against the Financial Action Task Force (FATF) international standards on anti-money laundering and combatting the financing of terrorism (AML/CFT) in 2024-2025. The authorities' current and planned steps include mitigating risks identified in the national risk assessment (NRA), addressing gaps in the legal framework, issuing regulations for remaining sectors (e.g., payment service providers and financing businesses). The NRA's findings which were shared with the financial sector should enable it to factor these in their own institutional risk assessment and mitigation plans, including enhancing suspicious transactions reporting. Regulation of the financial sector and service providers needs to be improved, and supervision should be conducted on a risk-based approach, also to address risks related to non-resident inflows. Such reforms would assist the authorities to mitigate domestic and foreign ML/TF risks safeguarding the financial sector integrity and its cross-border business.

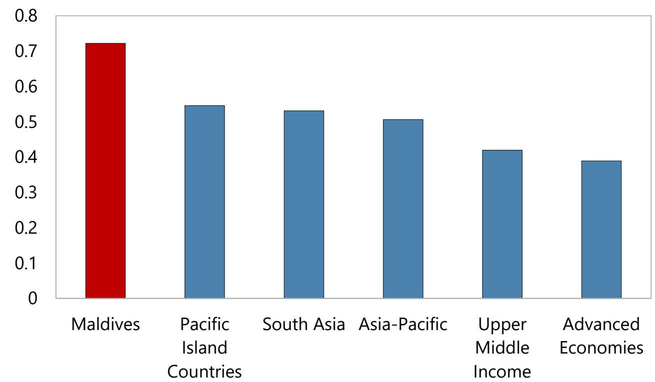
Authorities' Views

31. The authorities generally agreed with the FSAP findings and recommendations, including on the strong sovereign-bank nexus. They flagged some concerns about the recommended a 100 percent risk weight on domestic sovereign securities in foreign currency, likely making sourcing of FX from banks more difficult or costly. Therefore, the authorities agreed with the proposed gradual phasing-in of the risk weight over the medium term, while more details are being discussed with stakeholders. The authorities also mentioned that upcoming amendments to the AML framework would address technical deficiencies identified by FATF toward the upcoming mutual assessment in 2025.

D. Climate Change and Other Structural Reforms

32. The Maldives is highly vulnerable to the climate change and natural disasters. Climate change poses an existential threat to the low-lying islands of the Maldives through sea level rise and flood. The country is also vulnerable to ocean warming and resulting coral bleaching events, potentially affecting tourism activity over the longer term. The fiscal and climate vulnerabilities together have magnified posing significant risks to the economy, livelihoods, and food security, where the atolls outside of Malé are particularly vulnerable.

Maldives: Exposure to Climate Change Index
(Range 0-1, higher score means more vulnerable to climate change)



Source: Notre Dame Global Adaption Initiative, 2021; and IMF staff calculations.

33. Given the Maldives' climate vulnerabilities, strengthening institutions to support climate adaptation and mitigation efforts and mobilize climate finance is critical. The authorities set the ambitious goal of reducing emissions by 26 percent by 2030 through increased use of renewable energy sources, as articulated in the Nationally Determined Contribution (NDC). They have also started to take actions to reap benefits from a green and blue transition, such as developing a comprehensive set of development and climate policies and plans and initiating an ambitious infrastructure program prioritizing resilience[11]. In this regard, the integration of climate sensitivity into public financial management and public investment management processes can be a key contributor to government's strategies to combat the climate change (see Annex VI). Priority actions include the introduction of climate budget tagging and a Climate Budget Statement into the budget process alongside more in-depth periodic assessment of the fiscal costs and risks of climate change. The authorities could also provide a new guidance to the public sector on how to incorporate climate sensitivity into investment plans, with a stronger role for the Ministry of Finance and the Ministry of Climate Change, Environment and Energy. Adding climate dimensions to project appraisal and selection processes as well as systems for asset management and maintenance could

[11] The climate adaptation and mitigation costs are estimated at US$8.8 billion (159 percent of 2022 GDP) and US$1 billion (18 percent of 2022 GDP) respectively. The cost of adaptation is based on some sectoral assessments mainly covering the cost of coastal protection in all inhabited islands. Both adaptation and mitigation costs are provided by the Ministry of Environment, Climate Change, and Technology. Some specific and limited revenue measures are in place to fund the climate mitigation and adaptation strategies such as the Maldives Green Tax and the Baa Atoll Conservation Fund. The 2022 budget approved a potential issuance of green/blue bonds. The Maldives has developed a pipeline of projects totaling US$500 million for the Green Climate Fund (GFC), which are part of the Public Sector Investment Program.

be considered. Such policies will facilitate scaling-up of climate adaptation and additional climate finance from concessional sources.

34. Improving the business climate, strengthening governance and tackling corruption, and enhancing skill developments will help support strong and inclusive growth. Improvement in governance will reduce risks of corruption and cost of doing business, improve economic efficiency, and attract more FDI inflows. While the Maldives performs well relative to its South Asian peers on voice and accountability and rule of laws, there is room to further strengthen its regulatory quality (Figure 6). Asset Declaration Bill is being drafted to enhance the declaration process. The Anti-Corruption Commission has stepped up their efforts on their investigation activities under its strategic action plan 2020-2024. Policy priorities should include enhancing public disclosures of financial transactions of government and SOEs operations and strengthening the procurement procedures through the harmonization of procurement guidelines for SOEs and adopting a more competitive procurement process. Further efforts to align the legal framework of foreign investment to protect property rights, support FDI facilitation, and address skill gaps including through improving the quality of education and equal opportunity to education across gender will help boost investment, productivity and competitiveness.

35. IMF capacity development (CD) will continue to support the authorities' efforts to expedite macro-critical reforms. The Maldives is one of the intensive IMF CD recipients amongst countries in Asia and the Pacific. CD priorities are closely aligned with IMF surveillance policy recommendations that include revenue mobilization, expenditure rationalization, public financial and debt management, financial sector reforms, and monetary and exchange rate policies (Annex VII).

Authorities' Views

36. The authorities have advanced its climate reform agenda. The authorities are developing the National Development Strategy that lays out the country's 20-year development vision, which will include a new National Adaptation Plan (NAP) and associated implementation strategies. They are also committed to scaling up their mitigation efforts, by developing renewable energy systems, jointly with development partners, toward its COP28 commitment to expand renewables to reach 33 percent of the nation's electrical supply within the next five years. In addition, the government has recently completed budget tagging for the Sustainable Development Goals (SDGs) and already begun work on climate budget tagging. This will be followed by a climate budget statement, which will incorporate the costs and risks of climate change into the budgeting process. The government is also working to formulate an environmental, social, and governance (ESG) framework. Given the immediate threats of climate change to the Maldives, the authorities highlighted the importance of greater and more flexible access to concessional climate financing, which has been either difficult to access due to strict procedural requirements, or limited as the access levels are constrained by the country's quota or the size of the economy regardless of the extent of climate vulnerabilities and hence climate financing needs.

37. The authorities highlighted their strategy to expand trade and investment through diversification and competitiveness enhancement. The authorities underscored their continued efforts to further strengthen the tourism sector through enhancing overall capacity and diversified market segments within the sector. In addition, the authorities aim to increase the competitiveness of tuna fishery by modernizing it with new and environmental-friendly vessels. While sustainable pole and line tuna fishing in the Maldives has helped conserve ocean resources, this has weighed significant costs on the Maldivian tuna fishery as global tuna prices are not necessarily fair enough for such sustainable catches. The authorities are considering ways to garner preferential market access from key tuna exports markets toward sustainable fishery. The authorities noted that they would continue to improve governance, including by passing a draft bill on asset declaration, and to strengthen their asset recovery process with a new bill on asset recovery.

STAFF APPRAISAL

38. The Maldives' economy recovered strongly from COVID-19 pandemic but now faces challenges. Following the pandemic-induced contraction and strong post-COVID rebound, the Maldivian economy is estimated to have grown by 4.4 percent in 2023. Achieving projected growth of 5.2 percent in 2024 will require significant policy adjustments to address existing vulnerabilities. Inflation is expected to rise further, reflecting price pressures from the phasing-out of subsidies. Risks to the outlook are tilted to the downside.

39. Large fiscal and debt vulnerabilities persist. Without significant policy changes, the overall fiscal deficit is projected to narrow marginally but remain elevated at 12.2 percent of GDP in 2024. Continued support to SOEs is adding to fiscal vulnerabilities. Gross external financing needs are expected to rise in the coming years, reflecting persistently large fiscal deficits and repayments and rollovers of non-concessional debt, mainly global sukuk. The Maldives remains at high risk of external and overall debt distress, with debt assessed as unsustainable.

40. The external positions remain under pressures. Reflecting high import costs of food and fuel, and strong import demands associated with tourism activity and capital investment, large current account deficits would persist even over the medium term, weighing on FX reserves. The overall external position in 2023 is assessed to be substantially weaker than the level implied by fundamentals and desirable policies.

41. A strong and credible form of fiscal consolidation is urgently needed to reduce debt and restore the sustainability of public finances. Subsidy reforms should be implemented without delay and further efforts to rationalize and streamline healthcare subsidies could be subsequently adopted. The authorities should rationalize and scale back capital spending, including through SOEs. Assuming additional measures to mobilize domestic revenue, along with strengthening customs and tax administration, would help ensure fiscal sustainability. Strengthening fiscal and debt management is critical to enhance the effectiveness of fiscal policy.

42. Better fiscal-monetary policy coordination should facilitate necessary monetary policy actions to safeguard the exchange rate peg. Discontinued using of MMA advances is a welcome first step and should over time be complemented by a more active liquidity management. Should inflationary pressures increase or the parallel market exchange rate premium widen, the MMA should stand ready to further tighten monetary policy stance. FX market reforms should be accelerated to enhance the credibility of the peg. Fiscal adjustment will avoid renewed excessive burden on monetary policy.

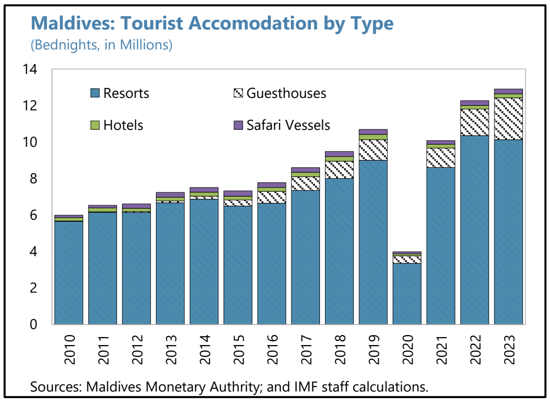
43. **Adopting macroprudential policies will help mitigate systemic risks stemming from the sovereign-bank nexus**. The authorities should amend capital regulation to gradually phase in a non-zero risk weight on bank holdings of Maldives government securities in foreign currency and introduce liquidity requirements. Macroprudential institutional framework and instruments should be swiftly introduced, and systemic risk monitoring capacity could be further enhanced. Together with enhancing financial sector oversight and crisis management, the financial safety net needs to be strengthened. Addressing gaps in the legal framework and implementing the AML/CFT framework should also be prioritized.

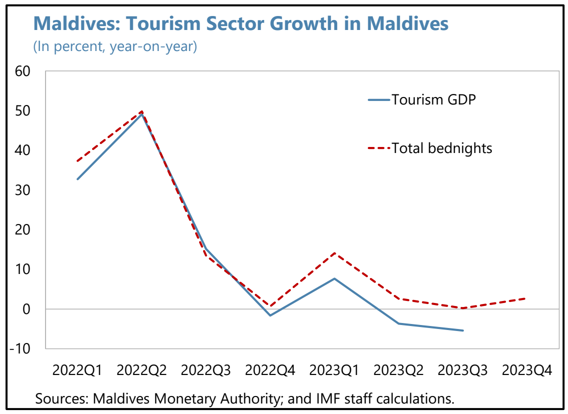
44. **Accelerating reforms to support inclusive and sustainable development remains crucial**. Given the Maldives' climate vulnerabilities, reforms to integrate climate considerations into the public financial and investment management processes and frameworks will help support climate adaptation and mitigation efforts, and facilitate scaling-up of climate finance from concessional sources. Improving the business climate, strengthening governance and tackling corruption, and enhancing skill developments will help support strong, inclusive, and sustainable growth.

45. **It is recommended that the next Article IV consultation take place on the standard 12-month cycle.**

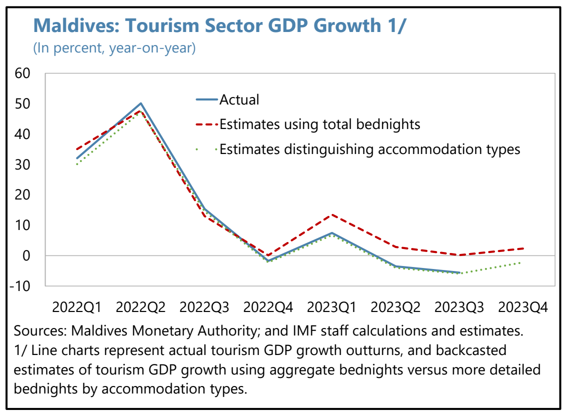
Box 1. Sectoral Analysis of Maldives' Tourism Industry[1]

Resorts and guesthouses are the two largest segments in the Maldives' tourism industry. While resorts are dominant segment in the tourism industry representing about 80 percent of total bednights, share of guesthouses, the second largest segment, has grown over time with notable increase in 2023 and reached almost 18 percent of total bednights (see text charts). Moreover, due to substantially lower night rates, the increasing share of guesthouses is associated with arrivals of lower-cost tourists.





Contribution of the guesthouses segment to the value added per one bednight is likely much smaller than contribution of the resorts. Based on estimates using seasonally adjusted quarterly tourism real GDP data and number of bednights for different segments, the average value added generated by one bednight in a guesthouse is about 15 percent of the average value added generated by one bednight in a resort.[2] Considering the difference in value added together with the increase in number of guesthouses bednights in 2023, could explain lower-than-expected growth of the tourism sector GDP despite the solid growth in total bednights and tourist arrivals (see text chart).



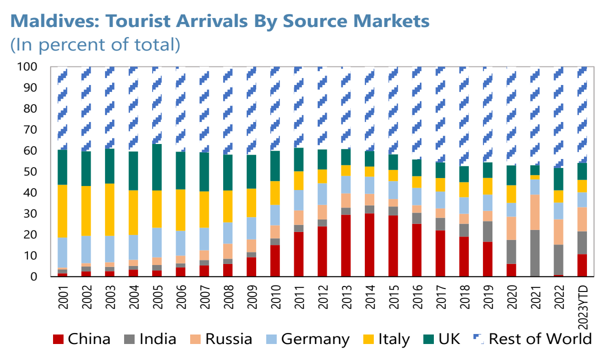
Provided that tourist arrivals are expanding and the management of tourism segments are well-balanced, growth of the guesthouses segment will continue to contribute positively to overall economic activity and growth. Expansion of the guesthouses segment could be complemented to higher-value-added resorts, where the guesthouses segment may help broaden tourist base by catering to a group of different—likely lower-cost—tourists. This would help grow the size of tourism GDP and contribute positively to economic inclusion in the Maldives.

1/ Prepared by Adam Remo (ICD).

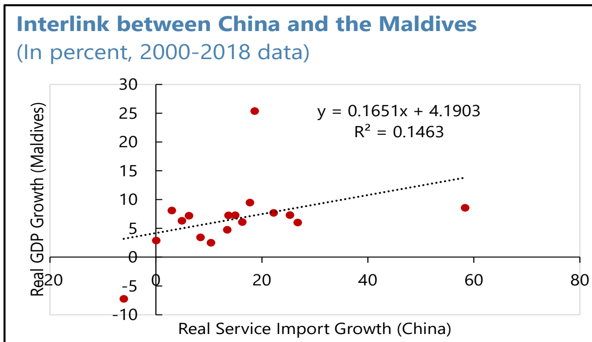
2/ The estimate was done on data starting from 2016Q1 as guesthouses represented only a small share before 2016. The periods from 2020Q1 to 2021Q4 were excluded from estimation due to COVID-19 pandemic disruption to the tourism sector.

Box 2. China Structural Slowdown and the Maldivian Economy[1]

Since the early 2010s, China has become the leading source of tourists for the Maldives' tourism industry. China overtook Germany, Italy, and the UK in tourist arrivals to the Maldives in 2010 (text figure). The Chinese market share reached its highest level in 2014, when the Maldives welcomed 363.6 thousands visitors from China, accounting for more than 30 percent of the total arrivals. However, the COVID-19 pandemic and the border restrictions imposed by the Chinese authorities have severely affected the tourist arrivals from China. In 2021 and 2022, the Chinese market share in the Maldives' tourism industry dropped sharply to only 0.2 and 0.9 percent, respectively.

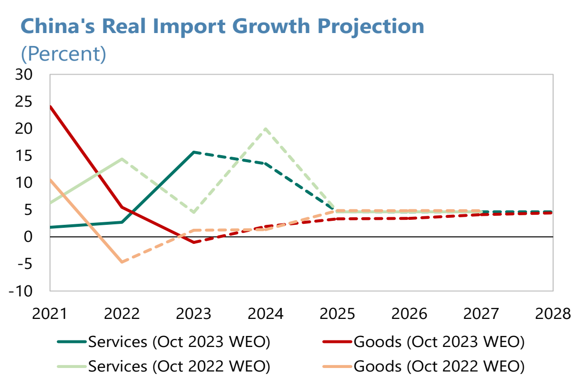


Source: Authorities' Data and IMF Staff Caclculations.



Source: IMF *World Economic Outlook*, October 2023 and IMF Staff Calculations.

The Maldives' real GDP growth is strongly correlated with China's demand for service imports, indicating that the Chinese market will remain a key driver of the Maldives' growth. Historical data from the two decades before the pandemic show a positive relationship between China's service imports and the Maldives' real GDP growth (text figure). After China reopened in early 2023, the Maldives saw a recovery in Chinese tourist arrivals and market share. In the third quarter of 2023, China accounted for 19 percent of the total arrivals to the Maldives. The resilience of the Chinese market suggests that China's travel imports will continue to support the Maldivian economy.



Source: IMF *World Economic Outlook*, October 2023.

China's trend slowdown could, nevertheless, pose downside risks to the Maldives' medium-term growth. According to the October 2023 IMF's *World Economic Outlook* (WEO), the growth of China's real service imports is expected to sharply slow from 13.5 percent in 2024 to around 4.6 percent annually until 2028.[2] While service imports from China would remain relatively strong over the medium term, the spillover effects of China's medium-term slowdown on the Maldives are likely to be very limited under the baseline scenario and further growth slowdown in China could create a headwind to the Maldivian economy.

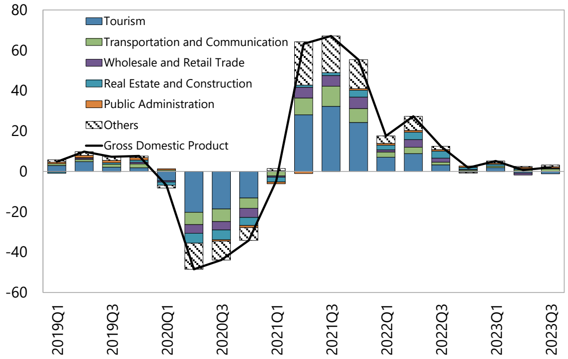
1/ Prepared by Yizhi Xu (APD).

2/ Despite China's structural slowdown, the downward revision of China's medium-term growth since the April 2023 WEO mostly affect the growth of its goods imports and its demand for service imports is expected to hold up.

Figure 1. Maldives: Key Economic Developments

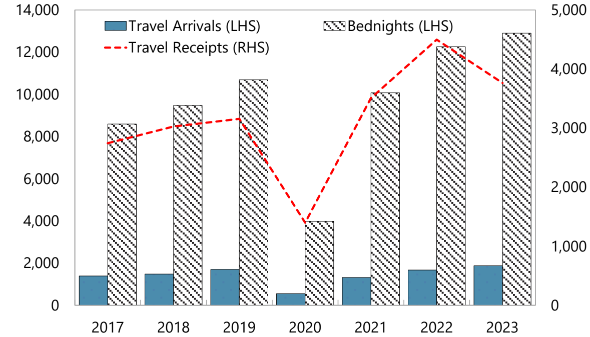
The economic recovery continued,.. .

Quarterly Real GDP
(In percent, year-on-year)



...supported by robust tourism rebound.

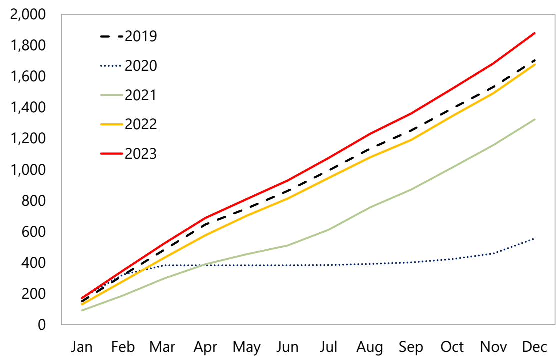
Tourism indicators
(In thousands (LHS), in USD millions (RHS))



Note: Data for 2023 travel receipts are as of Jan-Nov.

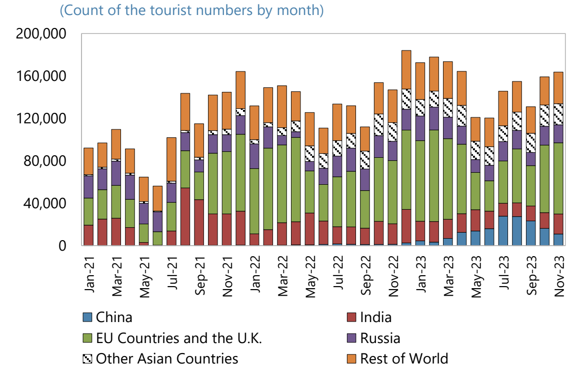
Tourist arrivals in 2023 have surpassed the pre-pandemic level,..

Tourist Arrivals (Cumulative)
(In thousands)



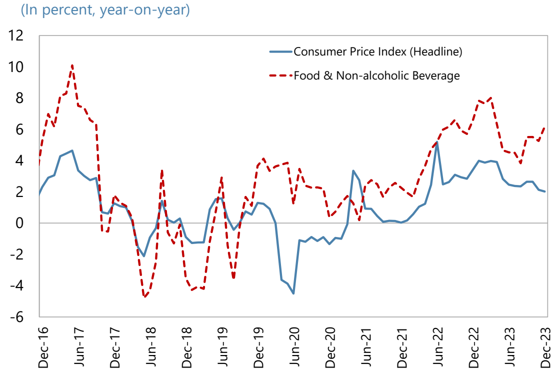
..., benefited from strong tourist inflows from India, Europe, and China.

Tourists by Nationality
(Count of the tourist numbers by month)



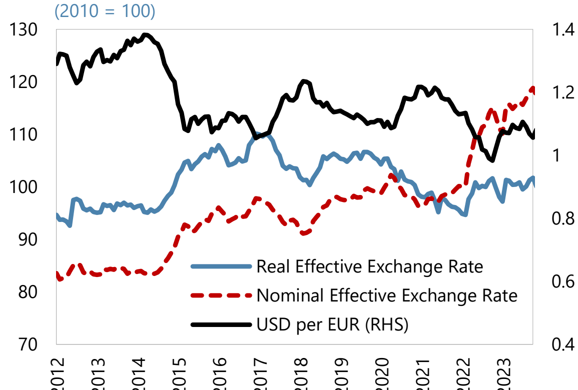
Despite an increase in food price and GST rate hike, headline inflation further declined.

CPI Inflation
(In percent, year-on-year)



Real exchange rate appreciated somewhat.

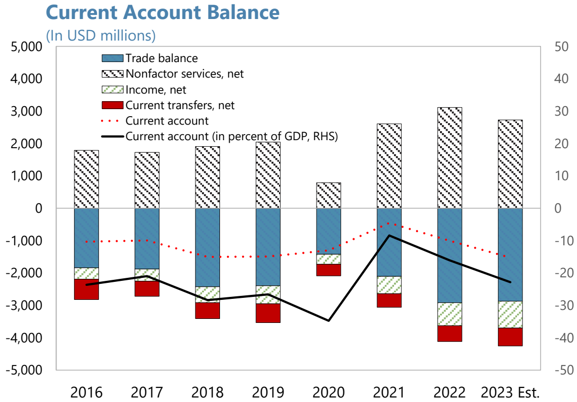
Exchange Rate Movements
(2010 = 100)



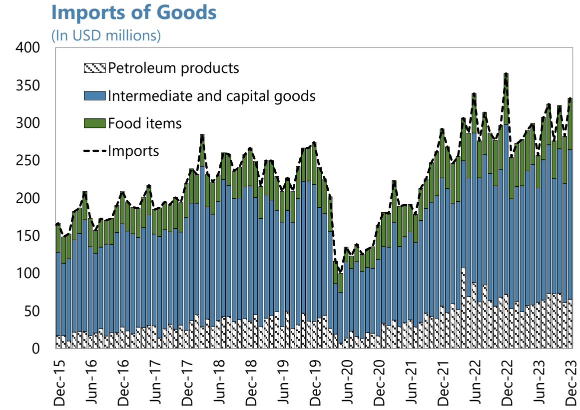
Source: Maldives Bureau of Statistics, Ministry of Finance, Maldives Monetary Authority (MMA); and IMF staff calculations

Figure 2. Maldives: External Sector Developments

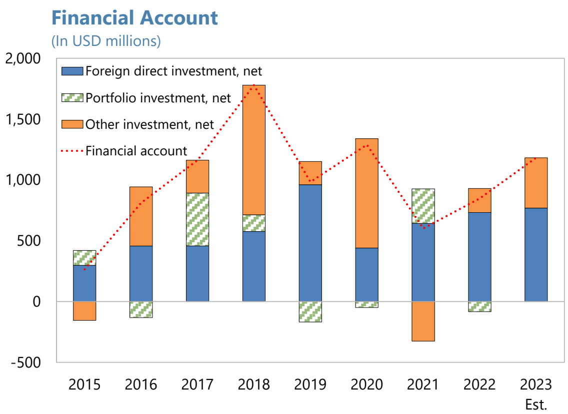
Large current account deficits (CAD) persist,..



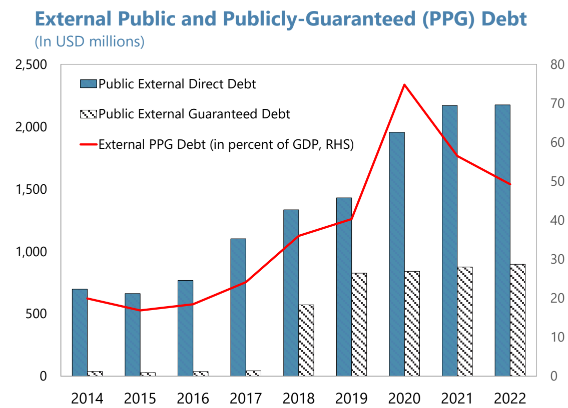
...amid rising import bills for petroleum and capital goods.



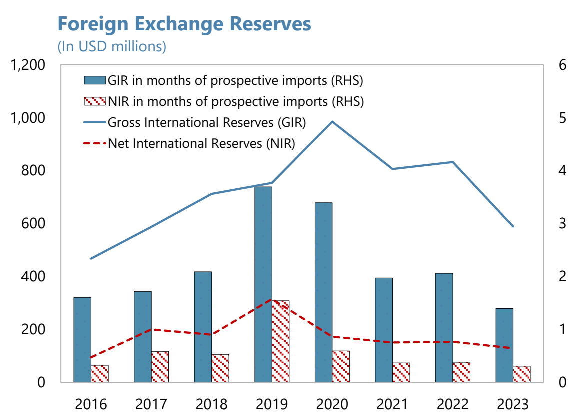
The CAD has been mainly financed by FDI and debt.



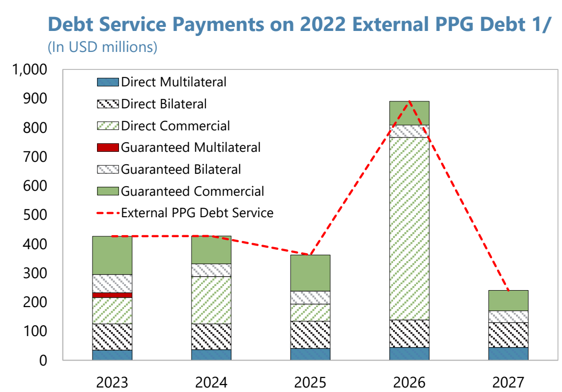
Government external debt surged.



Foreign exchange reserves have fallen.



External debt service payments are projected to rise.

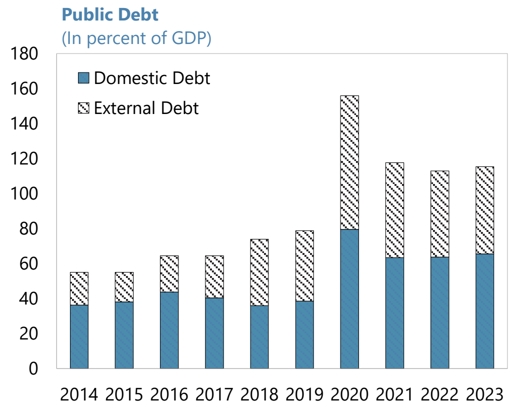


1/ Includes outstanding as of end-2022 (inclusive of IMF creidt and Sukuk).

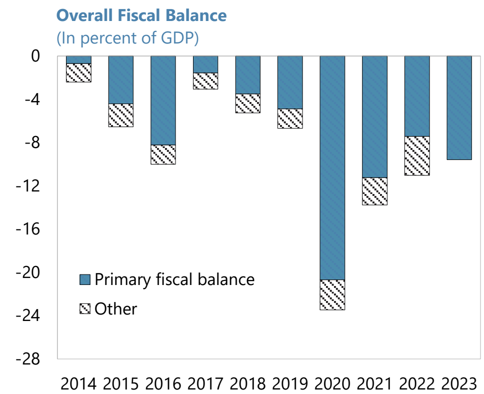
Source: Maldives Monetary Authority (MMA); Ministry of Finance; and IMF staff projections.

Figure 3. Maldives: Fiscal Sector Developments

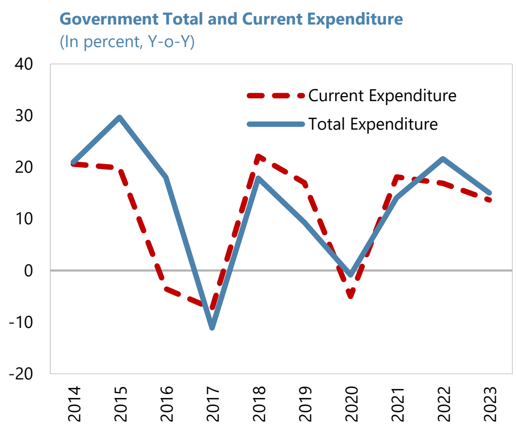
Public debt remains elevated since the pandemic,...



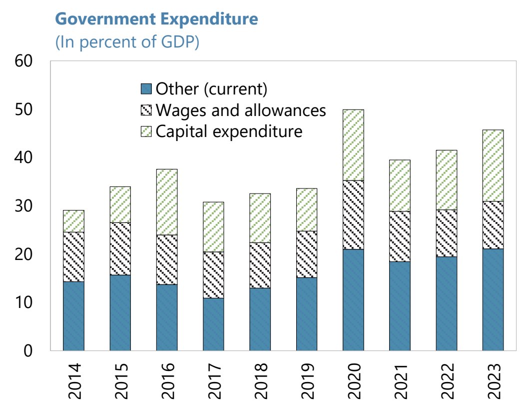
amid large fiscal deficits.



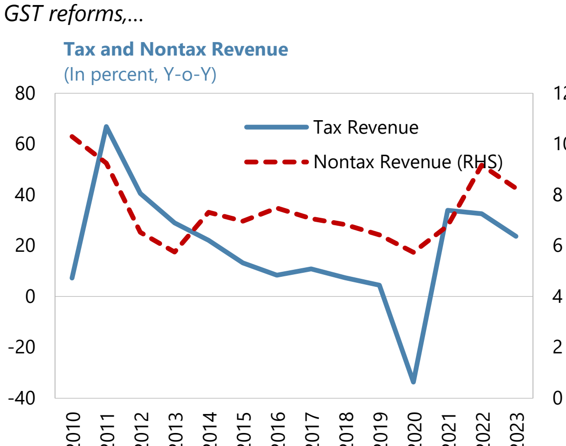
Government expenditure continues to rise,...



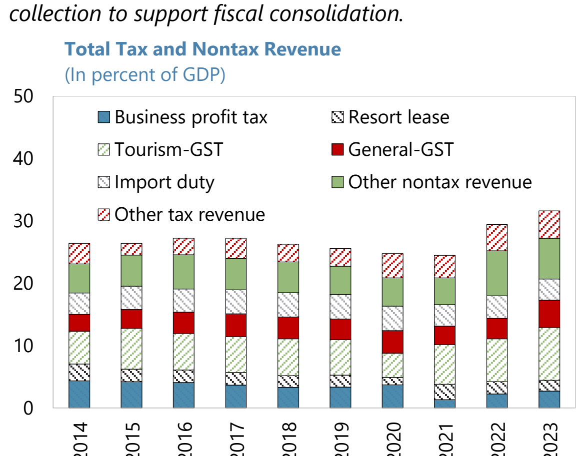
.... mainly driven by spending pressures from persistently large public investment and subsidies.



While progress has been made to raise revenue through GST reforms,...



.... there is still ample room to further improve tax revenue collection to support fiscal consolidation.



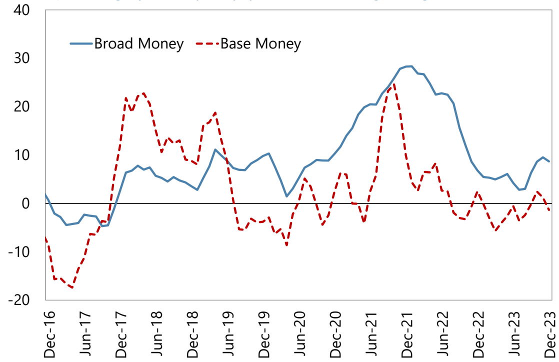
Source: Maldives Monetary Authority (MMA); and Ministry of Finance.

Figure 4. Maldives: Monetary and Credit Developments

Broad money has moderated post-pandemic.

Broad and Base Money

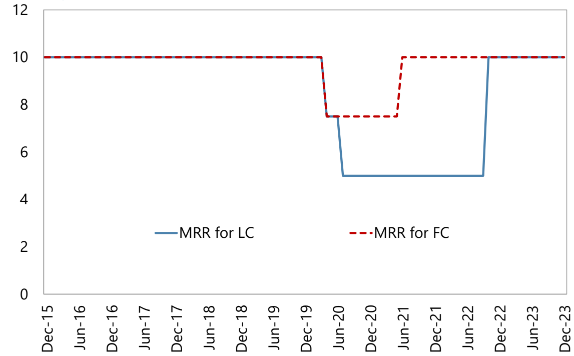
(In percentage, year-on-year (yoy), 3-month moving average)



MMA unwound the COVID support measures, including a temporary relaxation of minimum reserve requirements.

Minimum Reserve Requirement (MRR)

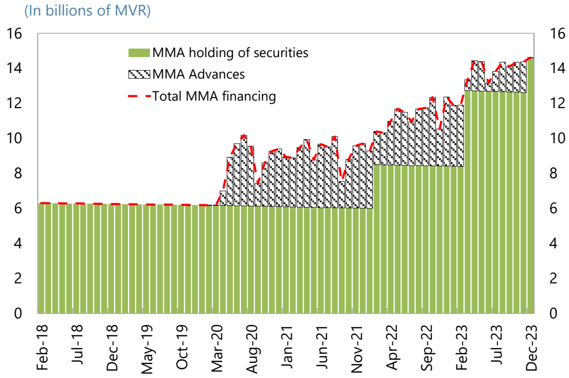
(In percent)



Central bank financing of fiscal deficits increased substantially…

Central Bank Fiscal Financing

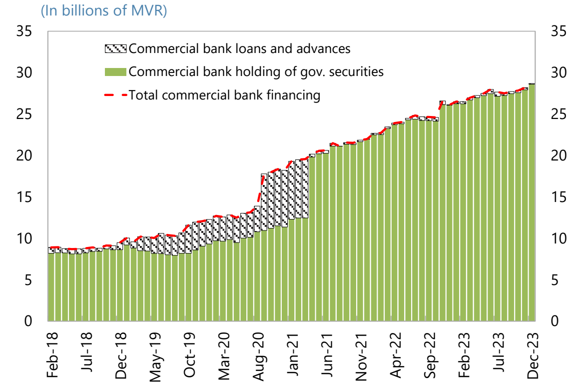
(In billions of MVR)



…so as commercial bank lending to government.

Government Borrowing from Banking System

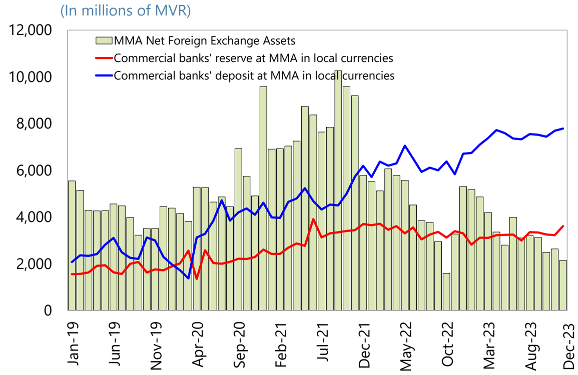
(In billions of MVR)



With the increase in MMA's advances to the government, excess liquidity has been observed…

Net Foreign Exchange Assets and Excess Liquidity 1/

(In millions of MVR)

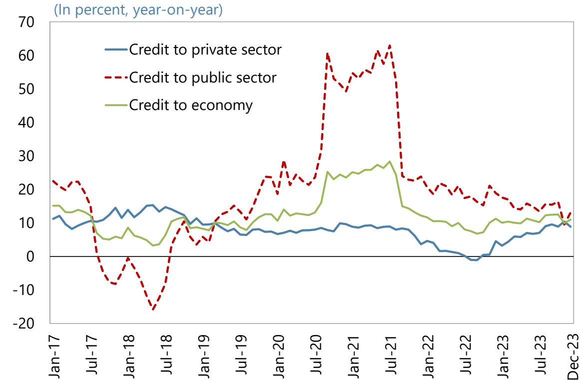


1/ Excess liquidity refers to bank deposits in excess of required reserves at the central bank.

…credits to private sector have been softened.

Credit Growth

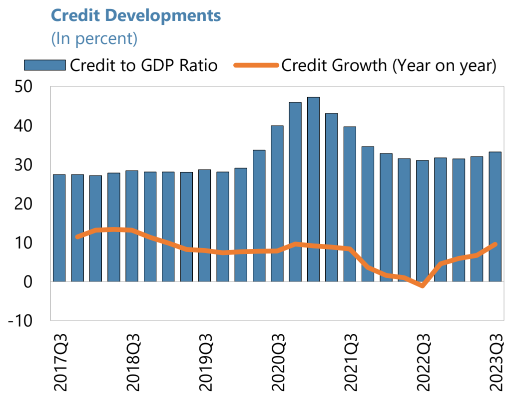
(In percent, year-on-year)



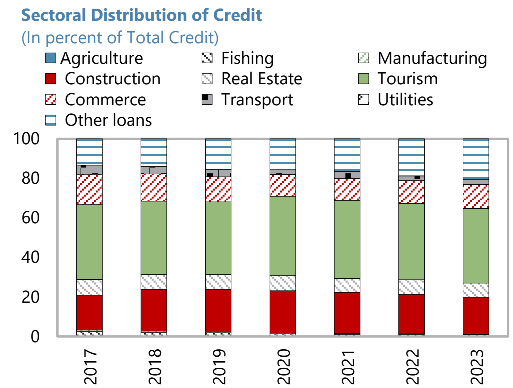
Sources: Maldives Monetary Authority (MMA); and IMF staff calculations.

Figure 5. Maldives: Financial Sector Developments

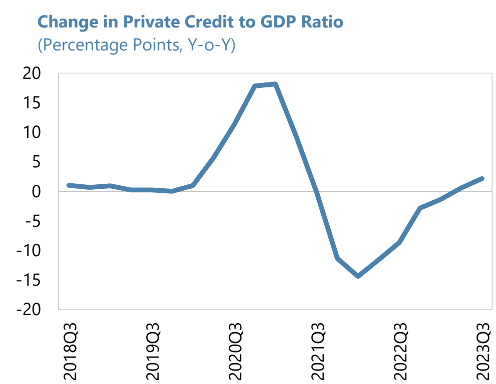
Credit to the economy has recovered from the trough during the pandemic…



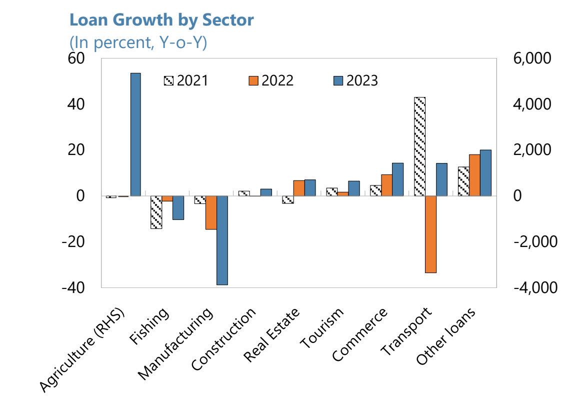
…. fueled by strong recovery in the tourism sector.



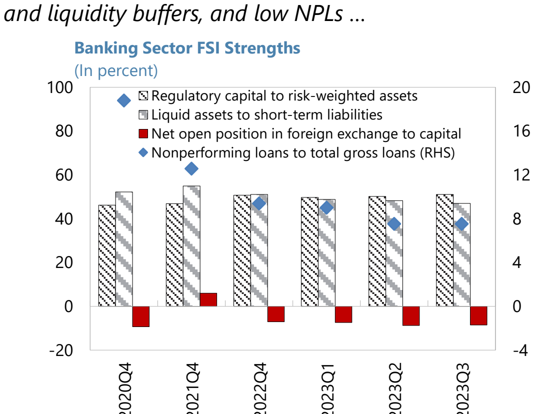
Credit-to-GDP ratio increased recently;…



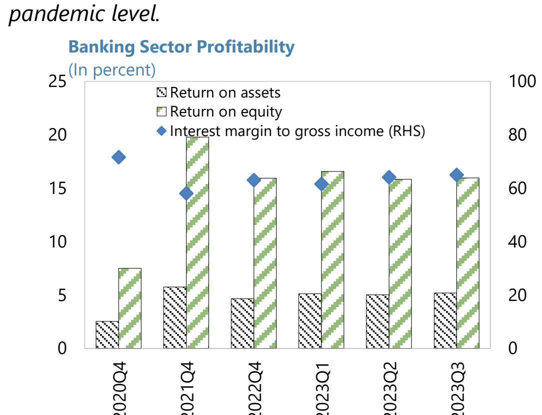
….however, credit growth across sectors remains imbalanced.



Banking sector resilience is supported by strong capital and liquidity buffers, and low NPLs …



…. and bank profitability continues to stay above the pre-pandemic level.



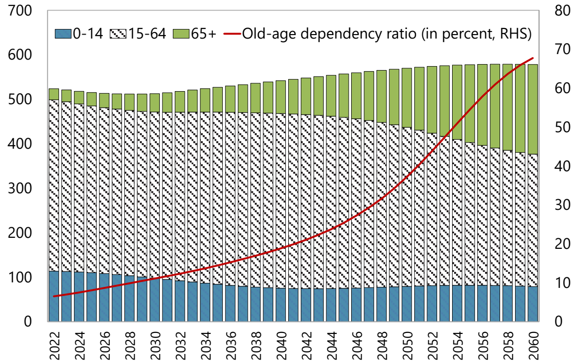
Sources: Maldives Monetary Authority (MMA); and IMF staff calculations.

Figure 6. Maldives: Macro-Structural and Climate Change Indicators

Maldives continues to benefit from its relatively young and dynamic population.

Population Dynamics of the Maldives

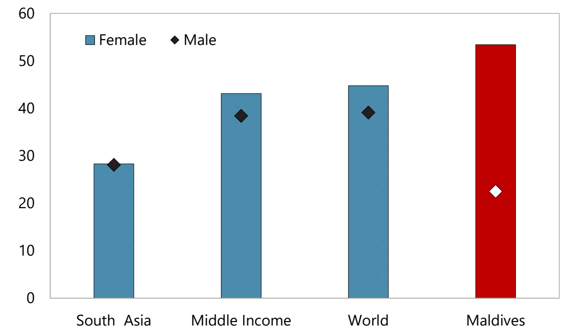
(In thousands)



High education attainment has supported…

School Enrollment at Tertiary Education

(In percent, 2022)

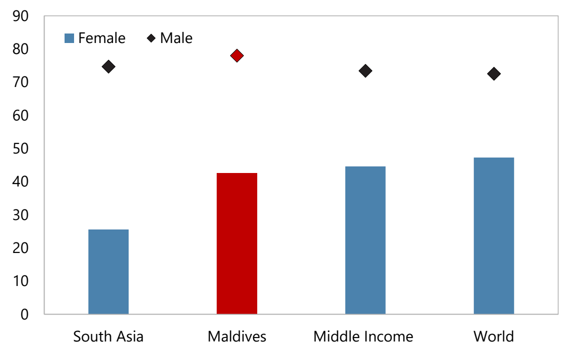


Note: 2019 Data for Maldives.

… labor participation and employment.

Labor Force Participation Rate

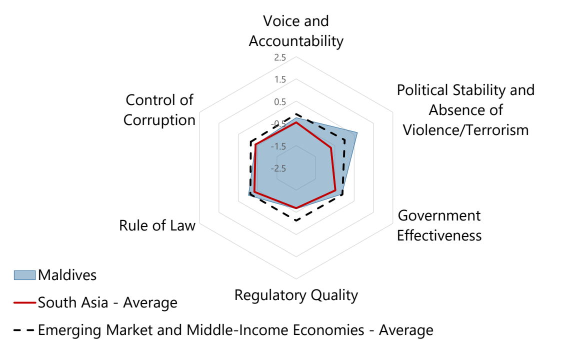
(In percent of population ages 15+, 2022 data)



There is room to improve governance.

Governance Indicators, 2022

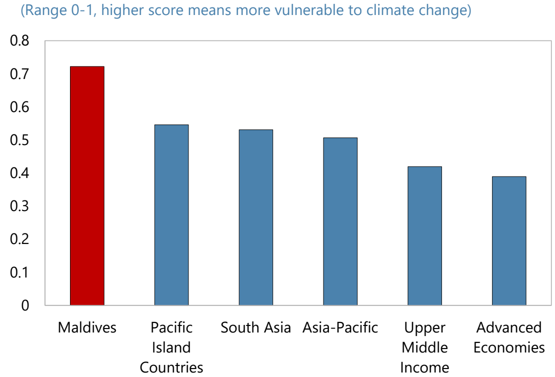
(Ranges from approximately -2.5 (weak) to 2.5 (strong) governance performance)



The Maldives has the highest exposure to climate change among all Asia-Pacific countries.

Exposure to Climate Change Index

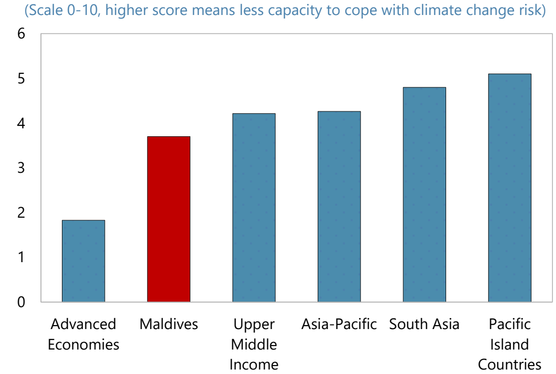
(Range 0-1, higher score means more vulnerable to climate change)



More can be done to scale up capacity to cope with the climate change risks.

Lack of Climate Change Coping Capacity

(Scale 0-10, higher score means less capacity to cope with climate change risk)



Sources: UN Population (2022); World Governance Indicators (2022); International Labour Organization; World Bank Gender Data Portal; UNESCO Institute for Statistics; INFORM Global Risk Index (2024); Notre Dame Global Adaptation Initiative (2021); and IMF staff calculations.

Table 1. Maldives: Selected Economic and Financial Indicators, 2021–2029

Population (2022): 523,787
GDP per capita (in U.S. dollars; 2022): 11,818
Poverty rate (in percent, $6.85 per day per person, 2019): 3.9
Quota (in million SDRs, as of December 2023): 21.2

	2021	2022	2023	2024	2025	2026	2027	2028	2029
			Est.			Proj.			
Output and prices					(Annual percentage change)				
Real GDP	37.7	13.9	4.4	5.2	6.5	5.0	4.8	4.5	4.5
Inflation (end-of-period) 1/	0.2	3.3	1.9	4.8	2.3	2.0	2.0	2.0	2.0
Inflation (period average) 1/	0.2	2.6	2.6	3.8	3.0	2.0	2.0	2.0	2.0
GDP deflator	4.7	1.6	2.6	2.4	3.0	2.0	2.0	2.0	2.0
Central government finances					(In percent of GDP)				
Revenue and grants	25.7	30.5	32.3	30.0	29.3	29.2	29.2	29.1	29.1
Expenditure and net lending	39.5	41.5	45.7	42.2	38.6	36.1	34.6	33.9	33.3
Overall balance	-13.8	-11.0	-13.4	-12.2	-9.4	-6.9	-5.4	-4.8	-4.2
Overall balance excl. grants	-15.0	-12.1	-14.1	-13.3	-10.1	-7.6	-6.1	-5.4	-4.8
Financing	13.8	11.0	13.4	12.2	9.4	6.9	5.4	4.8	4.2
of which :									
Financing gap 2/	…	…	…	2.9	…	…	…	…	…
Primary balance	-11.2	-7.4	-9.6	-7.6	-4.9	-2.9	-1.5	-1.0	-0.5
Public and publicly guaranteed debt	119.9	110.4	118.7	121.1	118.8	117.0	114.3	111.6	108.5
Monetary accounts					(Annual percentage change)				
Broad money	26.2	6.0	7.9	7.7	9.7	7.1	6.9	6.6	6.6
Domestic credit	8.8	12.4	13.1	12.4	12.6	10.9	10.5	9.9	9.6
Balance of payments					(In percent of GDP, unless otherwise indicated)				
Current account	-8.4	-16.1	-22.8	-19.4	-13.9	-12.9	-10.0	-9.7	-9.9
Of which:									
Exports	5.3	6.4	6.6	6.1	5.8	5.6	5.4	5.2	5.1
Imports	-44.3	-53.2	-49.5	-48.2	-46.4	-44.9	-44.2	-44.0	-43.9
Tourism receipts (in nonfactor services, net)	65.1	72.1	60.8	60.8	60.8	60.8	60.8	60.8	60.8
Income (net)	-9.9	-11.4	-12.4	-10.3	-10.1	-9.7	-9.7	-9.6	-9.6
Current transfers	-7.8	-7.8	-8.3	-7.8	-8.3	-8.5	-6.4	-5.7	-6.0
Capital and financial account (including e&o)	5.1	16.5	19.2	18.3	14.7	12.6	13.3	12.1	11.0
Of which:									
General government, net	3.8	3.0	3.9	2.5	2.6	4.0	2.0	1.8	0.7
Banks and other sectors, net	-2.7	2.5	3.8	0.2	0.3	0.3	0.3	0.3	0.3
Overall balance	-3.3	0.4	-3.6	-1.1	0.7	-0.2	3.2	2.4	1.1
Gross international reserves (in millions of US$; e.o.p.)	806	832	589	512	565	539	824	1,051	1,161
In months of GNFS imports	2.0	2.1	1.4	1.1	1.2	1.1	1.6	1.9	2.0
Exchange Rate (rufyiaa/US$, e.o.p.)	15.4	15.4	15.4	15.4	15.4	15.4	15.4	15.4	15.4
Memorandum items:									
GDP (in millions of rufiyaa)	83,098	96,132	103,011	110,937	121,696	130,384	139,375	148,558	158,346
GDP (in millions of U.S. dollars)	5,392	6,238	6,685	7,199	7,897	8,461	9,044	9,640	10,276
Tourism bednights (000')	10,073	12,260	13,103	14,123	15,689	16,693	17,650	18,482	19,392
Tourist arrivals (000')	1,322	1,675	1,879	2,018	2,210	2,385	2,521	2,640	2,770
Tourism bednights (% change)	152.8	21.7	6.9	7.8	11.1	6.4	5.7	4.7	4.9
Tourist arrivals (% change)	137.8	26.7	12.1	7.4	9.5	7.9	5.7	4.7	4.9
Dollarization ratio (FC deposits in percent of broad money)	…	…	…	…	…	…	…	…	…

Sources: Maldivian authorities; World Bank; and IMF staff projections.
1/ CPI-Male definition.
2/ Including possible new sources of domestic financing or negotiated official bilateral financing as higher external financing costs are limiting options to tap international capital markets.

Table 2. Maldives: Balance of Payments, 2021–2029

(In millions of USD, unless otherwise indicated)

	2021	2022	2023	2024	2025	2026	2027	2028	2029
			Est.			Proj.			
Current account	-453	-1,004	-1,525	-1,394	-1,101	-1,090	-908	-932	-1,018
Balance of goods and nonfactor services (GNFS)	502	196	-143	-89	355	452	543	549	580
Trade balance	-2,105	-2,916	-2,872	-3,030	-3,207	-3,327	-3,503	-3,738	-3,993
Exports (f.o.b.)	285	400	440	441	458	473	490	504	522
Domestic exports	151	159	163	158	154	148	143	133	125
Re-exports	134	241	265	283	303	324	347	371	397
Imports (f.o.b.)	-2,391	-3,316	-3,312	-3,471	-3,664	-3,800	-3,994	-4,242	-4,515
Tourism-related	-456	-594	-537	-578	-634	-679	-726	-774	-825
Other	-1,934	-2,722	-2,775	-2,893	-3,030	-3,121	-3,268	-3,469	-3,690
Of which: Construction	-219	-354	-365	-406	-431	-454	-489	-520	-553
Nonfactor services, net	2,608	3,113	2,728	2,941	3,561	3,780	4,046	4,287	4,573
Of which: Travel receipts	3,508	4,498	4,062	4,374	4,799	5,141	5,496	5,858	6,244
Income, net	-535	-711	-827	-739	-801	-819	-875	-928	-985
Current transfers, net	-421	-489	-555	-565	-654	-723	-576	-553	-613
Receipts	112	80	114	83	57	55	57	54	55
Payments	-532	-603	-668	-648	-711	-778	-633	-607	-668
Capital and financial account	601	847	1,183	1,316	1,157	1,070	1,199	1,164	1,134
Financial account	601	847	1,183	1,316	1,157	1,070	1,199	1,164	1,134
Of which: 1/									
Foreign direct investment, net	643	732	769	972	1,027	1,058	995	964	1,028
Portfolio investment, net	284	-83	0	50	0	-350	0	0	0
Other investment, net	-326	198	414	295	131	362	204	200	107
Monetary authorities 2/	-220	100	-100	100	-100	0	0	0	0
General government	207	184	259	177	209	338	177	170	73
Of which: Disbursements of loans	421	412	526	460	438	534	370	357	327
Amortization	-214	-228	-266	-283	-229	-196	-193	-187	-254
Banks	-337	89	98	-25	-26	-26	-27	-27	-28
Other sectors 3/	189	68	157	43	47	51	54	58	62
Errors and omissions	-327	183	99	0	0	0	0	0	0
Overall balance	-179	26	-243	-77	57	-20	290	232	116
Gross international reserves (increase: -)	179	-26	243	77	-54	26	-285	-227	-110
SDR allocation	29	0	0	0	0	0	0	0	0
Use of Fund credit, net	0	0	0	0	-3	-6	-6	-6	-6
Purchases	0	0	0	0	0	0	0	0	0
Repurchases	0	0	0	0	-3	-6	-6	-6	-6
Memorandum items:									
Gross international reserves (stock; e.o.p.)	806	832	589	512	565	539	824	1,051	1,161
In months of GNFS imports	2.0	2.1	1.4	1.1	1.2	1.1	1.6	1.9	2.0
Current account (in percent of GDP)	-8.4	-16.1	-22.8	-19.4	-13.9	-12.9	-10.0	-9.7	-9.9
GNFS balance (in percent of GDP)	9.3	3.1	-2.1	4.5	4.5	5.3	6.0	5.7	5.6
Exports (volume, percent change)	-9.0	21.9	2.6	1.7	11.2	5.6	5.7	6.5	6.5
Imports (volume, percent change)	11.0	19.6	7.1	4.7	6.5	4.4	5.0	6.2	6.4
Tourism: bednights (percent change)	152.8	21.7	6.9	7.8	11.1	6.4	5.7	4.7	4.9
Tourism: travel receipts (percent change)	151.0	28.2	-9.7	7.7	9.7	7.1	6.9	6.6	6.6
Foreing Direct Investment (in percent of GDP)	11.9	11.7	11.5	13.5	13.0	12.5	11.0	10.0	10.0
External debt (in percent of GDP) 4/	64.1	55.8	56.7	56.1	54.4	51.2	50.4	49.7	47.9
of which: External public and publicly guaranteed	56.5	49.2	49.8	49.0	47.3	44.0	43.0	42.1	40.1
Short-term	1.5	1.3	1.4	1.4	1.4	1.4	1.5	1.5	1.6
Debt service (in percent of domestic GNFS exports)	9.9	7.4	11.8	11.3	9.0	18.0	7.4	7.1	7.9
Exchange rate (rufiyaa per U.S. dollar; average)	15.41	15.41	15.41	15.41	15.41	15.41	15.41	15.41	15.41
GDP (in millions of U.S. dollars)	5,392	6,238	6,685	7,199	7,897	8,461	9,044.4	9,640	10,276

Sources: Maldivian authorities; and IMF staff projections.
1/ There are no capital transfers.
2/ MMA liabilities include swaps with Reserve Bank of India (RBI)
3/ These flows include external borrowing of the private sector.
4/ Public and private external debt includes IMF, but excludes domestic foreign-currency denominated debt.

Table 3. Maldives: Summary of Government Operations and Stock Positions, 2021–2029
(In millions of Rufiyaa)

	2021	2022	2023		2024		2025	2026	2027	2028	2029
			Budget	Est.	Budget	Proj.			Proj.		
Total revenue and grants	21,368	29,317	32,373	33,313	33,552	33,253	35,644	38,096	40,676	43,255	46,065
Revenue (excluding privatization receipts)	20,322	28,274	29,892	32,572	32,278	31,959	34,751	37,223	39,774	42,396	45,190
Tax revenue	14,682	19,456	23,540	24,066	25,618	25,358	27,873	29,854	31,896	33,998	36,238
Import duties	2,843	3,497	3,790	3,470	4,023	4,023	4,413	4,728	5,054	5,387	5,742
Airport service charge	473	831	969	988	1,029	1,029	1,128	1,209	1,292	1,377	1,468
Business profit tax (BPT)	1,106	2,147	2,807	2,803	3,030	3,030	3,323	3,561	3,806	4,057	4,324
Personal income tax	217	316	362	359	395	365	400	428	458	488	520
Goods and services tax (GST)	7,733	9,751	13,299	13,239	13,803	13,708	15,037	16,111	17,222	18,357	19,566
Of which: General GST	2,486	3,154	4,203	4,497	4,734	4,640	5,089	5,453	5,829	6,213	6,622
Tourism GST	5,248	6,597	9,096	8,742	9,068	9,068	9,948	10,658	11,393	12,144	12,944
Tourism tax ($6 green tax)	802	973	997	999	1,083	1,083	1,245	1,325	1,401	1,493	1,591
Other	1,507	1,942	1,911	2,208	2,257	2,121	2,326	2,492	2,663	2,839	3,026
Nontax revenue	5,640	8,819	6,352	8,506	6,660	6,601	6,877	7,369	7,878	8,398	8,952
Grants	1,032	1,025	2,462	436	1,270	1,276	873	850	876	832	845
Expenditure and net lending	32,806	39,905	40,718	47,100	47,317	46,763	47,030	47,125	48,267	50,383	52,782
Current expenditure	23,983	28,032	28,637	31,869	34,804	34,649	35,846	37,574	40,058	42,524	45,196
Primary current expenditure	21,879	24,580	25,200	27,960	29,560	29,548	30,426	32,321	34,550	36,826	39,252
Of which: Salaries and allowances	8,681	9,341	5,942	10,140	11,923	11,923	13,079	14,013	14,980	15,966	17,018
Administrative Services	2,276	2,231	2,590	2,555	2,871	2,752	3,019	3,234	3,457	3,685	3,928
Social welfare contributions	2,910	3,101	…	3,807	…	4,520	4,973	5,328	5,695	6,070	6,470
Repairs and maintenance	310	295	488	372	420	351	385	412	441	470	501
Subsidies and transfers	4,227	5,651	…	7,654	…	5,991	5,017	5,123	5,477	5,837	6,222
Interest	2,104	3,453	3,437	3,908	5,244	5,101	5,420	5,254	5,508	5,698	5,944
Other	3,474	3,960	…	3,432	…	4,011	3,953	4,210	4,500	4,797	5,113
Capital expenditure	8,615	11,124	12,081	14,040	12,513	11,514	10,674	9,045	8,209	7,858	7,586
Overall balance	-11,438	-10,588	-8,345	-13,786	-13,764	-13,510	-11,386	-9,029	-7,591	-7,127	-6,717
Overall balance, excluding grants	-12,484	-11,630	-10,826	-14,528	-15,039	-14,805	-12,279	-9,902	-8,493	-7,987	-7,592
Financing	11,438	10,588	…	13,786	…	13,510	11,386	9,029	7,591	7,127	6,717
External	5,182	1,715	…	4,413	…	2,711	4,376	6,371	3,782	3,685	2,136
Domestic	6,256	8,873	…	9,373	…	10,800	7,010	2,658	3,810	3,443	4,581
of which: SDF contribution 1/	-485	0	…	185	…	0	0	-5,703	0	0	0
Memorandum items:											
Current balance	-3,662	242	3,736	703	-1,251	-2,690	-1,096	-352	-283	-128	-6
Primary balance	-9,333	-7,135	-4,909	-9,878	-8,520	-8,409	-5,966	-3,775	-2,083	-1,429	-773
Current primary balance	-1,557	3,695	7,173	4,612	3,993	2,411	4,325	4,902	5,225	5,570	5,937

Sources: Maldivian authorities; and IMF staff projections.
1/ Transfers to the Sovereign Development Fund are recorded as negative domestic financing, and withdrawals as positive financing.

Table 4. Maldives: Summary of Government Operations and Stock Positions, 2021–2029

(In percent of GDP, unless otherwise indicated)

	2021	2022	2023		2024		2025	2026	2027	2028	2029
			Budget	Est.	Budget	Proj.			Proj.		
Total revenue and grants	25.7	30.5	31.4	32.3	30.2	30.0	29.3	29.2	29.2	29.1	29.1
Revenue (excluding privatization receipts)	24.5	29.4	29.0	31.6	29.1	28.8	28.6	28.5	28.5	28.5	28.5
Tax revenue	17.7	20.2	22.9	23.4	23.1	22.9	22.9	22.9	22.9	22.9	22.9
Import duties	3.4	3.6	3.7	3.4	3.6	3.6	3.6	3.6	3.6	3.6	3.6
Airport service charge	0.6	0.9	0.9	1.0	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Business profit tax (BPT)	1.3	2.2	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
Personal income tax	0.3	0.3	0.4	0.3	0.4	0.3	0.3	0.3	0.3	0.3	0.3
Goods and services tax (GST)	9.3	10.1	12.9	12.9	12.4	12.4	12.4	12.4	12.4	12.4	12.4
Of which: General GST	3.0	3.3	4.1	4.4	4.3	4.2	4.2	4.2	4.2	4.2	4.2
Tourism GST	6.3	6.9	8.8	8.5	8.2	8.2	8.2	8.2	8.2	8.2	8.2
Tourism tax ($6 green tax)	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Other	1.8	2.0	1.9	2.1	2.0	1.9	1.9	1.9	1.9	1.9	1.9
Nontax revenue	6.8	9.2	6.2	8.3	6.0	6.0	5.7	5.7	5.7	5.7	5.7
Grants	1.2	1.1	2.4	0.4	1.1	1.2	0.7	0.7	0.6	0.6	0.5
Expenditure and net lending	39.5	41.5	39.5	45.7	42.7	42.2	38.6	36.1	34.6	33.9	33.3
Current expenditure	28.9	29.2	27.8	30.9	31.4	31.2	29.5	28.8	28.7	28.6	28.5
Of which: Salaries and allowances	10.4	9.7	5.8	9.8	10.7	10.7	10.7	10.7	10.7	10.7	10.7
Administrative Services	2.7	2.3	2.5	2.5	2.6	2.5	2.5	2.5	2.5	2.5	2.5
Social welfare contributions	3.5	3.2	…	3.7	…	4.1	4.1	4.1	4.1	4.1	4.1
Repairs and maintenance	0.4	0.3	0.5	0.4	0.4	0.3	0.3	0.3	0.3	0.3	0.3
Subsidies and transfers	5.1	5.9	…	7.4	…	5.4	4.1	3.9	3.9	3.9	3.9
Interest	2.5	3.6	3.3	3.8	4.7	4.6	4.5	4.0	4.0	3.8	3.8
Other	4.2	4.1	…	3.3	…	3.6	3.2	3.2	3.2	3.2	3.2
Capital expenditure	10.4	11.6	11.7	13.6	11.3	10.4	8.8	6.9	5.9	5.3	4.8
Overall balance	-13.8	-11.0	-8.1	-13.4	-12.4	-12.2	-9.4	-6.9	-5.4	-4.8	-4.2
Overall balance, excluding grants	-15.0	-12.1	-10.5	-14.1	-13.6	-13.3	-10.1	-7.6	-6.1	-5.4	-4.8
Financing	13.8	11.0	…	13.4	…	12.2	9.4	6.9	5.4	4.8	4.2
External	6.2	1.8	…	4.3	…	2.4	3.6	4.9	2.7	2.5	1.3
Domestic	7.5	9.2	…	9.1	…	9.7	5.8	2.0	2.7	2.3	2.9
of which: SDF contribution 1/	-0.6	0.0	…	0.2	…	0.0	0.0	-4.4	0.0	0.0	0.0
Memorandum items:											
Current balance	-4.4	0.3	3.6	0.7	-1.1	-2.4	-0.9	-0.3	-0.2	-0.1	0.0
Primary balance	-11.2	-7.4	-4.8	-9.6	-7.7	-7.6	-4.9	-2.9	-1.5	-1.0	-0.5
Current primary balance	-1.9	3.8	7.0	4.5	3.6	2.2	3.6	3.8	3.7	3.7	3.7
Public and publicly guaranteed debt	119.9	110.4	…	118.7	…	121.1	118.8	117.0	114.3	111.6	108.5
Domestic	63.4	61.1	…	68.8	…	72.1	71.5	73.0	71.3	69.5	68.4
External (excl. currency swaps by MMA)	56.5	49.2	…	49.8	…	49.0	47.3	44.0	43.0	42.1	40.1
GDP (in millions of rufiyaa)	83,098	96,132	103,011	103,011	110,937	110,937	121,696	130,384	139,375	148,558	158,346

Sources: Maldivian authorities; and IMF staff projections.

1/ Transfers to the Sovereign Development Fund are recorded as negative domestic financing, and withdrawals as positive financing.

Table 5. Maldives: Monetary Accounts, 2021–2029

	2021	2022	2023	2024	2025	2026	2027	2028	2029
			Est.			Proj.			
				(In millions of rufiyaa, e.o.p.)					
Net foreign assets	14,163	11,801	10,214	9,850	11,065	10,864	15,373	18,950	20,719
Maldives Monetary Authority, net	11,265	9,960	7,764	7,283	8,439	8,186	12,640	16,163	17,876
Assets	12,410	12,823	9,074	7,882	8,713	8,311	12,698	16,189	17,888
Liabilities	-1,145	-2,863	-1,310	-600	-274	-126	-57	-26	-12
Commercial banks, net	2,898	1,841	2,451	2,567	2,626	2,679	2,732	2,787	2,843
Net domestic assets	38,058	43,573	49,517	54,477	59,501	64,739	65,444	67,191	71,098
Domestic credit	59,477	66,852	75,595	84,958	95,658	106,069	117,222	128,880	141,315
Public sector	30,736	36,669	42,902	49,799	57,152	64,860	73,109	81,910	91,300
Central government (net)	27,783	33,247	38,294	44,730	51,811	59,412	67,552	76,242	85,518
Public enterprises	2,953	3,422	4,609	5,069	5,341	5,448	5,557	5,668	5,781
Private sector	28,161	29,441	32,049	34,515	37,863	40,566	43,363	46,220	49,265
Other items (net)	-21,419	-23,278	-26,079	-30,481	-36,158	-41,330	-51,778	-61,689	-70,217
Broad money	52,222	55,375	59,731	64,327	70,565	75,603	80,817	86,141	91,817
Narrow money	22,343	22,401	23,429	25,232	27,679	29,655	31,700	33,789	36,015
Currency	3,269	3,188	3,346	3,346	3,346	3,346	3,346	3,346	3,346
Demand deposits	19,074	19,213	20,083	21,886	24,333	26,309	28,354	30,442	32,669
Quasi-money	29,879	32,974	36,302	39,095	42,886	45,948	49,116	52,353	55,802
				(Annual percentage change)					
Broad money	26.2	6.0	7.9	7.7	9.7	7.1	6.9	6.6	6.6
Narrow money	17.6	0.3	4.6	7.7	9.7	7.1	6.9	6.6	6.6
Domestic credit, net	8.8	12.4	13.1	12.4	12.6	10.9	10.5	9.9	9.6
Central government	11.9	19.7	15.2	16.8	15.8	14.7	13.7	12.9	12.2
Public enterprises	43.1	15.9	34.7	10.0	5.4	2.0	2.0	2.0	2.0
Private sector	3.7	4.5	8.9	7.7	9.7	7.1	6.9	6.6	6.6
				(In percent of GDP)					
Broad money	62.8	57.6	58.0	58.0	58.0	58.0	58.0	58.0	58.0
Narrow money	26.9	23.3	22.7	22.7	22.7	22.7	22.7	22.7	22.7
Domestic credit, net	71.6	69.5	73.4	76.6	78.6	81.4	84.1	86.8	89.2
Central government	33.4	34.6	37.2	40.3	42.6	45.6	48.5	51.3	54.0
Public enterprises	3.6	3.6	4.5	4.6	4.4	4.2	4.0	3.8	3.7
Private sector	33.9	30.6	31.1	31.1	31.1	31.1	31.1	31.1	31.1
				(In millions of U.S. dollars)					
Gross international reserves (stock; e.o.p.) 1/	806	832	589	512	565	539	824	1,051	1,161
Commercial banks NFA	188	119	159	167	170	174	177	181	184
Commercial banks Balance Sheet FX Gap 2/	157	162	166	174	178	181	185	189	192
Memorandum items:									
Velocity	1.6	1.7	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Money multiplier	4.2	4.4	4.8	4.8	4.8	4.8	4.8	4.8	4.8
Reserve money (in millions of rufiyaa, e.o.p.)	12,429	12,706	12,438	13,394	14,693	15,742	16,828	17,937	19,119

Sources: Maldivian authorities; and IMF staff projections.

1/ Gross international reserves is equivalent to gross foreign assets of MMA.

2/ Commercial Bank Balance Sheet FX Gap is the difference between total FX denominated assets and total FX denominated liabilities on commercial banks' balance sheets.

Table 6. Maldives: Financial Soundness Indicators—Local Banking Sector, 2018–2023Q3

(In percent, unless otherwise indicated)

	2018	2019	2020	2021	2022	2023Q3 1/
Core FSIs						
Regulatory capital to risk weighted assets	44.7	46.4	46.3	46.8	50.9	51.1
Regulatory Tier 1 capital to risk-weighted assets	36.0	39.0	41.0	36.4	40.8	43.5
Non-performing loans net of provisions to capital	2.9	2.3	0.1	0.5	0.2	0.4
Non-performing loans to total gross loans	8.9	9.4	8.2	6.7	5.9	5.2
Return on assets	5.7	4.6	2.5	5.7	5.0	5.2
Return on equity	15.9	13.3	7.5	19.7	17.2	16.0
Interest margin to gross income	64.2	65.0	71.6	58.1	62.1	65.0
Non-interest expenses to gross income	30.5	31.8	31.8	28.9	31.6	31.1
Liquid assets to total assets	42.0	42.6	42.6	46.4	45.2	41.8
Liquid assets to short-term liabilities	66.5	68.2	69.7	72.0	71.8	68.7
Net open position in FX to capital	9.1	6.4	-9.2	6.1	6.0	-8.5
Additional FSIs						
Capital to assets (leverage ratio)	19.4	20.8	19.0	15.8	17.8	...
Large exposures to capital	86.6	60.7	70.2	68.2	49.5	...
Gross assets position in derivatives to capital	0.0	0.0	2.3	2.1	0.9	...
Gross liabilities position in derivatives to capital	0.0	0.0	0.0	0.0	0.0	...
Trading income to total income	4.5	4.1	3.6	3.1	3.7	...
Personnel expenses to total income	36.5	34.9	37.2	34.4	31.1	...
Customer deposits to total non-interbank loans	129.4	131.1	137.2	165.0	166.8	...
FX loans to total loans	50.2	48.1	47.6	47.1	45.0	...
FX liabilities to total liabilities	54.2	56.3	55.0	54.4	54.6	...

Sources: IMF Financial Soundness Indicators; and Maldives Monetary Authority.
1/ Data for 2023Q3 are from Maldives Monetary Authority.

Table 7. Maldives: FSAP Recommendations

Recommendations	Timing[1/]	Agency[2/]
Systemic Risk Mitigation		
Adopt regulation for money changing businesses and foreign exchange regulation.	ST	MMA
Differentiate reserve requirements by currency to mitigate risks from high financial dollarization.	I	MMA
Resume liquidity management operations and take measures towards an active secondary market.	ST	MMA
Develop indicators for monitoring of systemic risks.	ST	MMA
Bank Stress Testing and Climate Risk Analysis		
Improve integrity and granularity of supervisory data, including data compiled by the Credit Information Bureau (CIB)	ST	MMA
Develop methodologies for solvency, liquidity, and market risk stress tests and engage banks in a dialogue about stress test procedures and results, including banks' own stress tests.	ST	MMA
Improve granularity and coverage of climate data, geographical exposures of the country and financial system, and climate-related damages and foster intra-agency collaboration to support access to existing data.	ST	MoED, MBS, MMA
Initiate climate risk analysis in collaboration with other agencies to assess the effect of actual and future climate conditions on the financial sector and the economy.	MT	MMA
Macroprudential Policy		
Augment reporting of data on recurrent household payment obligations from leasing contracts to the CIB.	I	MMA
Establish a macroprudential framework, including a committee for macroprudential coordination, and publish a financial stability report.	ST	MMA
Introduce key borrower-based and capital-related macroprudential policy instruments.	ST	MMA
Banking Regulation and Supervision		
Amend capital regulation to apply a 100 percent risk weight on bank holdings of Maldives government securities in foreign currency (perhaps phased in) and introduce liquidity requirements.	I	MMA
Issue regulatory standards to clarify the enforcement regime and to ensure that non-compliant actions by banks are immediately met with enforcement action.	I	MMA
Review MMA's off-site monitoring procedures and staffing count, including redefining the methodology and including mandatory meetings with bank senior management.	ST	MMA

Table 7. Maldives: FSAP Recommendations (Concluded)		
Strengthen the independence of MMA's Board of Directors by changing the overall composition and voting rights of members.	ST	MMA, MoF
Climate Regulation and Supervision		
Develop and publish an institutional strategy on climate risk and opportunities	ST	MMA
Issue supervisory expectations on the integration of climate risks into business strategies, governance and risk management as well as regulatory reporting.	MT	MMA
Financial Integrity		
Share the Maldives' national risk assessment (NRA) findings with financial sector.	ST	MMA, MoF
Adopt a risk-based approach to supervision of the financial sector.	MT	MMA
Address identified technical compliance deficiencies related to financial sector laws and regulations.	ST	MoJ, MMA
Crisis Management and Resolution		
Make amendments to the Banking Act and deposit insurance regulation to address shortcomings in early intervention, bank resolution and deposit insurance framework and to the MMA Act to include provisions for ELA; and strengthen policies and procedures in these areas.	I	MoF, MMA
Establish an ELA framework.	I	MMA
Require systemically important banks to prepare recovery plans; and prepare resolution plans and undertake resolvability assessments for them.	ST	MMA
Financial Sector Development		
Develop the NFIS with a specific MSME access to finance pillar.	ST	MMA, MoF MoED
Enhance credit infrastructure, including: (i) passage of the Secured Transaction Act and Insolvency Law, (ii) reviewing the Civil Procedure Code for fast-track or simplified procedures for smaller claims, and (iii) expanding the collection of credit information.	ST	MMA, DJA
Introduce a national green taxonomy and develop a framework for tracking green finance provided by public and private sources.	MT	MoF, MMA

1/ I: Immediately; ST: short term = 1-2 years; MT: medium term = 3–5 years.

2/ MMA: Maldives Monetary Authority; MoED: Ministry of Economic Development and Trade; MoF: Ministry of Finance; MoJ: Ministry of Justice; MBS: Maldives Bureau of Statistics; DJA: Department of Judicial Administration; ELA: Emergency Liquidity Assistance; NFIS: National Financial Inclusion Strategies; MSME: Micro, Small, and Medium Enterprise.

Annex I. Implementation of IMF Policy Recommendations

Article IV Policy Recommendations	Related Policy Actions
Swiftly implement the authorities' ambitious and homegrown fiscal consolidation plan to reduce public debt	In January 2023, the authorities increased the Goods and Services Tax (GST) rates (from 6 to 8 percent) and the Tourism Goods and Services Tax (TGST) (from 12 to 16 percent), which have helped mobilize additional tax revenue of 3.1 percent of GDP in 2023. The medium-term fiscal strategy for 2024-2026 established four medium-term fiscal anchors, including (i) reducing public debt to less than 95 percent of GDP by 2026, (ii) reducing primary budget deficit to less than 5 percent of GDP by 2024, (iii) maintaining public and publicly guaranteed debt relative to GDP on a downward trend, and (iv) reducing recurrent expenditure to levels that do not exceed government revenue by 2024.
Rationalize capital spending and subsidies, combined with targeted assistance to the most vulnerable	The 2024 budget presents a reform plan to phase out fuel, electricity, and other existing subsidies and replace them with targeted cash transfers toward low-income households, which will be implemented starting in the second half of 2024. Moreover, election-related pressures have fueled a large increase in capital spending and frontloaded harmonization of public servant wage bills.
Reform state-owned enterprises (SOEs) to reduce their dependence on the central government budget and improve governance	A new State Shareholder Management Department was created within the Ministry of Finance with the aim of actively monitoring SOE fiscal risks, rationalizing their capital spending, and scrutinizing support for SOEs. Efforts have been made in improving transparency, as the authorities have enhanced quarterly reporting and SOE financial database.
Improve public financial and debt management	A draft Debt Management Law has been reviewed within the Ministry of Finance, and the Fiscal Responsibility Act has been prepared for the submission to Parliament.
Gradually reduce Maldives Monetary Authority (MMA) advances until fully phased out	MMA advances were discontinued at the end of 2023 and all outstanding advances at that time were securitized. Other pandemic-related policy support measures were fully unwound. Going forward, MoF is committed not to resort to rely on MMA advances in the future.
Safeguard financial stability considering the large exposure of the banking sector to the sovereign and the expiration of pandemic-related lending support schemes.	Banking sector prudential measures (including higher risk weight on FX-denominated sovereign bonds and borrower-based macroprudential instruments), regulatory and supervisory framework, crisis management arrangements (including intervention and resolution framework), and systemic risk monitoring data and analysis were discussed in the context of a joint IMF-World Bank FSAP. Currently, MMA is discussing the plan to implement FSAP recommendations with stakeholders.
Reform FX markets	A roadmap for FX reforms including to strengthen regulations of money changers, encourage the use of Rufiyaa in domestic transactions, and limit transaction types on FX accounts was developed; nevertheless, the discussion between MMA and stakeholders from both public and private sectors on the roadmap is lagging.

Article IV Policy Recommendations	Related Policy Actions
Build climate resilience	The lack of concessional financing and grants for climate financing has constrained climate resilient investment. The IMF technical assistance on Climate-Public Investment Management Assessment (C-PIMA) and Green Public Financial Management (Green-PFM) is scheduled for January 2024, which would help develop the authorities' capacity to meet public financial and investment management requirements to facilitate access to climate funding, including through the Green Climate Fund (GCF).

Annex II. External Sector Assessment [1/]

Overall Assessment: *Maldives' external position in 2023 was assessed to be substantially weaker than the level implied by medium-term fundamentals and desirable policies. Despite robust tourism revenues, the current account (CA) deficit has widened further, due to surging capital goods imports, high import costs of food and fuel, and strong import demands associated with tourism activity. Real effective exchange rate marginally appreciated in 2023 and stayed well above its long-term historical average. Gross international reserves declined further, and dollar shortages have persisted.*

Potential Policy Responses: *Safeguarding FX reserves is a near-term priority. Front-loaded fiscal consolidation, accompanied by tighter monetary and macroprudential policies, is urgently needed to help strengthen external buffers and rebuild resilience to external shocks. FX market reforms will improve the functioning of FX markets and enhance the credibility of the peg.*

Foreign Assets and Liabilities: Position and Trajectory

Background. External public and publicly guaranteed (PPG) debt stood at US$3,072 million (or around 49 percent of GDP) in 2022 (latest available data), up from US$3,046 million in 2021 in nominal terms. External PPG debt is predominantly owed to bilateral (41 percent) and commercial (42 percent) creditors. For the commercial portion, PPG external debt includes global sukuk bond (US$500 million) and Abu Dhabi Eurobonds (US$100 million) with both maturing in 2026. The scheduled repayment of US$600 million will require refinancing needs in 2026, exerting additional pressures on the already-low international reserves. The authorities established the Sovereign Development Fund (SDF) in 2017 to set aside funds for future debt repayment obligations of the Maldives. As of December 2023, SDF has accumulated funds in Rufiyaa with transfers from MOF, equivalent to about US$511 million.

Assessment. Maldives remains at a high risk of external and overall debt distress. Without significant fiscal adjustments, public debt is on an unsustainable path under the authorities' current policies. Large external financing needs and maturing debt in 2026 continue to make the debt profile vulnerable to rollover risks. The authorities have requested IMF technical assistance to develop SDF law and strengthen the SDF management.

2023 (% GDP)	NIIP: -	Gross Assets: -	Debt Assets: -	Gross Liab.: -	Debt Liab.: 50

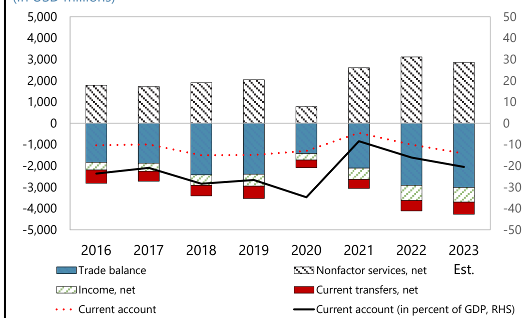
[1] Prepared by Yasuhisa Ojima (APD).

Current Account

Background. Despite robust tourism revenues, the current account deficit is estimated to further deteriorate from 16.1 percent of GDP to 22.8 percent of GDP in 2023, due to surging capital goods imports, high import costs of food and fuel, and strong import demands associated with tourism activity. CA dynamics have been driven mainly by trade balance and nonfactor services. Despite continued tourism recovery, CA deficit is expected to be persistently high, amid higher recurrent and capital spending and rising debt services.

Maldives: Current Account Balance

(In USD millions)



Source: Maldives Monetary Authorities; and IMF Staff calculations.

Assessment. The preliminary result of external balance assessment (EBA)-Lite Current Account (CA) model suggests that the Maldives' external position in 2023 was substantially weaker than the level implied by fundamentals and desirable policies. The cyclically adjusted CA is estimated at -22.5 percent of GDP in 2023. Given that tourism activity fully rebounded to the pre-pandemic level, the temporary adjustors to account for tourism impacts from COVID-19 were excluded. The multilaterally consistent cyclically adjusted CA norm is estimated at -8.1 percent of GDP. This implies a CA gap of -14.4 percent of GDP in 2023, with a policy gap of -0.9 percent of GDP, mainly due to a negative policy gap stemming from fiscal policy (i.e., higher deficit vis-à-vis rest of the world).

Maldives: Model Estimates for 2023 1/

(in percent of GDP)

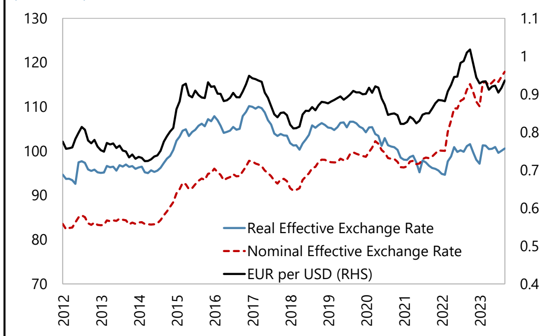
	CA model	REER model
CA-Actual	**-22.8**	
Cyclical contributions (from model) (-)	-0.3	
Natural disasters and conflicts (-)	0.0	
Adjusted CA	**-22.5**	
CA Norm (from model) 2/	**-8.1**	
Adjustments to the norm (-)	0.0	
Adjusted CA Norm	**-8.1**	
CA Gap	**-14.4**	**7.1**
o/w Relative policy gap	-0.9	
Elasticity	-0.5	
REER Gap (in percent)	**28.9**	**-14.2**

Source: IMF Staff Estimates.

1/ Based on the EBA-lite 3.0 methodology

2/ Cyclically adjusted, including multilateral consistency adjustments.

Real Exchange Rate



Sources: Maldivian Authorities; and IMF Staff calculations.

Background. The nominal effective exchange rate (NEER) has appreciated in recent years, in line with the movement of the U.S. dollar to which the rufiyaa has been pegged. The real effective exchange rate (REER) appreciated by around 1 percent in 2023.

Assessment. The CA model implies the overvaluation of real exchange rate of about 28.9 percent, based on the CA-REER elasticity of 0.5. The REER model indicates that the real exchange rate in the Maldives is undervalued by 14.2 percent; however, the REER-model estimate is not suitable for the Maldives, given its large uncertainties.

Capital and Financial Accounts: Flows and Policy Measures

Background. The Maldives has a relatively open capital account. Net FDI inflows in 2022 grew by 13.9 percent year-on-year to US$732 million, or about 11.7 percent of GDP, but remained below the pre-pandemic level of US$961 million in 2019. The government did not issue any international securities in 2022 and 2023.

Assessment. The authorities should finalize the FX reform strategy including to: i) enhance the use of Rufiyaa by implementing both legal and institutional measures; ii) promote alternative financing instrument denominated in Rufiyaa; and iii) calibrate policies that create a macro-fundamental-driven interest rate wedge.

FX Intervention and Reserves Level

Background. Gross international reserves (GIRs) declined from US$832 million at end-2022 to US$589 million at December 2023, or around 1.4 months of prospective imports. FX shortages persisted.

Assessment. The reserve adequacy tool for credit-constrained economies is applied to the Maldives and incorporates the fixed exchange rate regime. Using the marginal cost of capital as the cost of holding reserves, estimated at 6.2 percent, the Maldives reserve adequacy level is estimated to be 2.4 months. Nevertheless, gross reserve coverage of around 3 months of prospective imports is recommended, given the Maldives' low usable FX reserves, high dollarization, and reliance on volatile tourism revenues.

Annex III. Risk Assessment Matrix [1/]

Source of Risk	Likelihood	Expected Impact on the Maldives	Policy Responses
		Global	
Commodity price volatility. A succession of supply disruptions (e.g., due to conflicts, uncertainty, and export restrictions) and demand fluctuations causes recurrent commodity price volatility.	**High** **ST**	**High.** A sharp rise in commodity prices could further widen current account deficits, adding pressures on FX reserves.	• Provide targeted and temporary social assistance to the most vulnerable. • Swiftly implement subsidy reforms to allow pass-through of higher global prices. • Rebuild fiscal and external buffers.
Abrupt global slowdown. Global and idiosyncratic risk factors cause a synchronized sharp growth downturn (e.g., U.S., Europe, and China) and adverse spillovers through trade and financial channels.	**Medium** **ST**	**High.** Lower growth of the Maldives' major tourism source countries could drag on tourism activities and FDI inflows, adding external pressures and dampening economic growth.	• Provide targeted and temporary policy support to the most vulnerable and affected businesses. • Tighten monetary policy to support the exchange rate peg and protect FX reserves drain. • Build economic resilience against negative shocks through structural reforms to boost productivity and competitiveness, and foster diversification.
Systemic financial instability. Higher interest rates and risk premia trigger market dislocation, with cross-border spillovers and an adverse macro-financial feedback loop affecting weak banks and non-bank financial institutions.	**Medium** **ST**	**Medium-High.** Increased global financial volatility could lead to higher financing costs and reduced options of external market-based financing for the government and the SOEs and possible depreciation pressures.	• Swiftly implement reform-based fiscal consolidation to reduce financing requirements and rebuild buffers. • Tighten monetary policy to support the exchange rate peg and protect the foreign reserves.
Deepening geoeconomic fragmentation. Broader conflicts, inward-oriented policies, and weakened international cooperation result in a less efficient configuration of trade and FDI, and supply disruptions.	**High** **ST, MT**	**Medium.** Supply disruptions and weaker confidence could adversely affect economic activity, FDI inflows, and overall external accounts.	• Build economic resilience against negative shocks through structural reforms to boost productivity and competitiveness, and foster diversification.

1/ The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. Structural risks are those that are likely to remain salient over a longer horizon.

Source of Risk	Likelihood	Expected Impact on the Maldives	Policy Responses
Domestic			
Delayed fiscal consolidation and failure to reduce debt. Overruns in fiscal spending, including from public investment, subsidies, and contingent liabilities from SOEs, further exacerbate fiscal deficit, public debt, and FX reserve positions.	**High** **ST**	**High.** Continued rise in public spending will lead to fiscal deficit overruns, and increase financing requirements and public debt, adding risks to economic stability.	• Swiftly implement reform-based fiscal consolidation to reduce financing requirements and rebuild buffers.
Sovereign-bank nexus. Despite strong buffers, risk arising from the banking sector's large exposure to the sovereign, which increased markedly since the pandemic, could pose risk to financial stability.	**Medium** **ST**	**Medium.** Banks' capital could erode rapidly in the event of sovereign stress considering that risk weight on banks' sovereign debt exposure is zero while sovereign debt represents more than 25 percent of banks' total assets.	• Swiftly implement fiscal consolidation to reduce bank borrowing and adjust risk weights on banking sector's sovereign debt exposure. • Develop contingency planning and strengthen crisis management institutional framework.
Extreme climate events. Major natural disasters (e.g., floods or tsunami) disrupt economic activity and affect sentiment, resulting in higher fiscal expenditure. More frequent natural disasters also cause severe damage to infrastructure.	**Medium** **ST-MT**	**Medium-High.** Disruption in tourism-related and overall economic activity, poor fishing and agriculture production, damage to properties, and higher food inflation, with larger impact on low-income households.	• Prioritize public investment in disaster-resistant infrastructure and sustainable growth. • Implement climate-related fiscal reforms to help mobilize climate finance through concessional funding and grants.

Annex IV. Reforms of State-Owned Enterprises [1/]

State-owned enterprises (SOEs) pose significant challenges for the public finances in the Maldives, as they often require large and ad-hoc budget support to address their solvency and liquidity issues. Their elevated external debt guaranteed by the government constitutes contingent liability to the central government. The current legislation and oversight framework for SOEs are inadequate and fragmented, and the performance management of SOEs is not aligned with their objectives and long-term goals. Reforms to SOE framework and operations are critical to support the sustainability of public finances. Priorities include rationalizing the SOE portfolio, harmonizing SOE institutional and oversight framework, and adopting a structured performance management framework.

A. SOE Fiscal Risks in the Maldives

1. **Continued support to SOEs have weighed on central government budget.** There have been substantial budget transfers to SOEs by way of both capital injections and subsidy payments, and the Ministry of Finance supports a small number of SOEs with sovereign guarantees of their external borrowings. During 2022, equity injections and subsidies were budgeted to be MVR 2.4 billion and cover 22 of the 30 SOEs. In actuality, the total funding provided to SOEs in 2022 by way of subsidies and equity was substantially higher at MVR 5.2 billion. As the purchase prices for many subsidized goods have increased significantly over the last two years, the funded value of the subsidies has been significantly in excess of the budgeted amounts earmarked to fund the subsidies. These ad-hoc funding support also crowded out other priority spending. While SOEs themselves have poorly developed risk management frameworks, this has resulted in many corporate risks being unnecessarily borne by the central government.

2. **The Government of Maldives also provides sovereign guarantees for some SOEs**. Sovereign guarantee of SOE debt currently accounted for US$1.5 billion, or 1.4 percent of GDP. SOEs such as Housing Development Corporation (HDC) and Fahi Dhiriulhun Corporation (FDC), which deliver large-scale government-funded housing projects and take up around 70 percent of total guaranteed SOE debt, face challenges in servicing their debt, due to high rental arrears. Such SOE guaranteed debt is also attached with cross-default clauses[2], which amplifies the magnitude of potential sovereign support.

3. **Financial risks arising from liquidity strains has further deteriorated.** Based on IMF's SOE Health Check Tool, 6 out of 9 SOEs have seen upgrades in the overall risk rating in recent years (Annex Table 1). The improvement mainly reflects better SOE profitability (e.g., cost recovery) and solvency conditions (e.g., debt to assets and debt to earnings before interest, tax, depreciation, and amortization (EBITDA)). However, non-financial SOEs in the Maldives remain vulnerable to significant

[1] Prepared by Yizhi Xu (APD) based on IMF's SARTTAC technical assistance provided to the Maldives and its report of "Review of Fiscal Risk Management in State Owned Enterprises" (August 2023).

[2] The cross-default clause added to HDC and FDC bonds stipulates that a default event with one bond would trigger defaults on all other bonds issued by the same borrower.

and persistent liquidity risks. Particularly, all non-financial SOEs in the Maldives are facing "very high risk" of failing to collect bills from customers on time—as indicated by very high creditor turnover days—whereas 6 SOEs were considered as facing "very high risk" in 2020.

Table 1. Maldives: SOE Fiscal Risk Assessment 1/

	SOE Risk Ratings (2022 data)						Overall Risk Rating		
	Profitability		Liquidity		Solvency		2022	2020	2015
	Return on Equity	Cost Recovery	Quick Ratio	Creditor Turnover Days	Debt to Equity	Interest Coverage			
SOE1	Moderate Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk	Very High Risk	High Risk	Very High Risk	Very High Risk
SOE2	Moderate Risk	Very Low Risk	Very Low Risk	Very High Risk	Very Low Risk	Very Low Risk	Moderate Risk	Moderate Risk	High Risk
SOE3	Low Risk	Very Low Risk	Very High Risk	Very High Risk	Moderate Risk	Very Low Risk	Moderate Risk	High Risk	Low Risk
SOE4	Low Risk	Moderate Risk	Very High Risk	Very High Risk	Very Low Risk	Very Low Risk	Moderate Risk	High Risk	Low Risk
SOE5	Moderate Risk	Very Low Risk	Low Risk	Very High Risk	Very Low Risk	Moderate Risk	Moderate Risk	High Risk	High Risk
SOE6	Moderate Risk	Very Low Risk	Low Risk	Very High Risk	Very Low Risk	Very High Risk	Moderate Risk	Moderate Risk	Moderate Risk
SOE7	Moderate Risk	Very Low Risk	Low Risk	Very High Risk	Very High Risk	High Risk	Moderate Risk	Moderate Risk	Very High Risk
SOE8	Moderate Risk	Very Low Risk	Low Risk	Very High Risk	Very Low Risk	Very Low Risk	Moderate Risk	High Risk	Moderate Risk
SOE9	Moderate Risk	Very Low Risk	Very Low Risk	Very High Risk	Very Low Risk	Very Low Risk	Low Risk	Moderate Risk	Low Risk

Source: IMF Staff Estimates.

1/ Profitability ratios measure the capacity of the SOE to generate sufficient profit for its shareholders. Liquidity ratios measure the capacity of the SOE to meet its short-term obligations. Solvency ratios measure the capacity of the SOEs to meet its long-term obligations.

B. Institutional Arrangements

4. **The underlying causes of the fiscal risks embedded in Maldives' SOEs are many.** They include the lack of clear and commercial objectives for SOEs, the absence of a proper framework for identifying, funding and costing non-commercial services, and the poor risk management practices of SOEs. Most SOEs do not have a formal risk management policy and leave the government to bear the consequences of external shocks, such as interest rate and oil price fluctuations.

5. **Institutional arrangements for SOEs oversight are fragmented.** These include:

- *The Privatization and Corporatization Board (PCB)* is the main entity responsible for overseeing state-owned enterprises (SOEs) in the Maldives, under its own legislation. PCB monitors and evaluates SOEs through quarterly and annual financial reports, which are often delayed and incomplete. PCB also develops and applies various codes and policies to improve the governance of SOEs, such as a corporate governance code, procurement regulations, and a strategic action plan.

- *The State Shareholding Management Division (SSMD),* newly established at the Ministry of Finance, which focuses on supporting the budget process for SOEs (in particular, in relation to subsidy payments and capital injections) and then managing the immediate cash needs of SOEs. This occurs on a fortnightly basis and has allowed very little time for SSMD to focus on more strategic management of fiscal risk.

The delineation of responsibilities between Privatization and Corporatization Board (PCB) and State Shareholder Management Division (SSMD) is not well defined. While PCB is responsible for monitoring and evaluation of SOEs, SSMD has been tasked with fiscal risk management. By separating performance management (which is the responsibility of PCB) from fiscal risk oversight (the responsibility of SSMD), the structured performance management framework is compromised and the capacity to effectively manage fiscal risks is diluted. It is therefore crucial for the authorities to take a more coordinated approach to structure the performance management framework.

6. **The current administrative framework could be enhanced.** With the help of IMF TA, the authorities are drafting a new SOE law to establish clear roles and responsibilities for the government and SOEs, and set out a consistent and effective approach to risk management, capital allocation, and governance. The law would also enable a review of the ownership model for SOEs, which could have a significant impact on reducing fiscal risks.

C. Conclusions and Policy Recommendations

7. **Reforms of SOEs and their institutional arrangements are critical to lessen their reliance on central government and safeguard public finances**. SOE fiscal risks remain acute, particularly because most SOEs require large and unpredictable budget support, and many SOEs are facing heightened liquidity risk. Meanwhile, the government guarantees some of the SOE debt, which is highly exposed to the heavy debt service obligations of these SOEs. Reform priorities should include:

- ***Rationalizing SOE portfolios***. A more precise definition of SOEs and the SOE ownership rationale should be adopted to pave the way for a rationalization of the current large portfolio of SOEs. For instance, some SOEs are too small or unprofitable to justify the costs of their operations and management, while others are non-commercial in nature and do not fit the performance criteria of SOEs. The government should consider different options for these SOEs, such as dissolution, reclassification, or sale. The adoption of a new SOE Law could provide a clear and consistent framework for defining and regulating the SOE portfolio.
- ***Harmonizing SOE institutional and oversight framework***. A new SOE law should include an ownership policy that defines the objectives and scope of SOEs, an institutional framework that clarifies the roles and responsibilities of the oversight bodies, and a performance management and oversight framework that sets and enforces SOE specific goals. Although creating an SOE holding company could help consolidate institutional framework, this would require a rationalization of the SOE portfolio as mentioned above.
- ***Adopting a structured performance management framework***. The PCB oversees the performance of SOEs through five-year agreements that link management and board remuneration to financial metrics. However, this approach has some drawbacks, such as neglecting the specific objectives and long-term goals of each SOE. A better framework would involve setting clear and enduring objectives for each SOE, and agreeing on a set of financial and non-financial performance targets that are tailored to each entity and industry. The performance agreement would also include a financial budget, a capital expenditure program, and a documentation of all non-commercial activities and their funding arrangements. The oversight body would monitor the compliance with the agreement and evaluate the performance of the board and management based on the criteria, objectives and targets. This would allow for more effective and accountable management of SOEs and their fiscal risks.

Annex V. Macro-Financial Linkages and Financial Sector Vulnerabilities [1/]

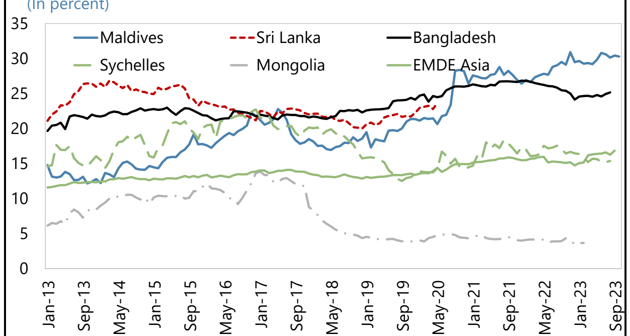
Macro-financial linkages generated from sovereign-bank nexus, high dollarization, and shortages of foreign exchange (FX) pose a combination of vulnerabilities to the Maldives. The recent Financial Sector Assessment Program (FSAP) for the Maldives concluded that the financial system is resilient to moderate shocks but vulnerable to severe shocks related to economic downturn and currency devaluation. Reforms to strengthen the systemic liquidity management framework, the banking sector regulatory and supervisory framework, macroprudential policy instruments, and the stress testing and climate risk analysis are essential to contain systemic risks to financial stability.

A. Macro-Financial Linkages in the Maldives

1. Macro-financial stability in the Maldives is threatened by pockets of vulnerabilities. They stem from high public debt, sovereign-bank nexus, sectoral loan concentration, FX shortages, limited market mechanisms, under-reported shadow banking activities, and susceptibility to external shocks and climate change. While risks arising from public and non-financial corporate borrowers could migrate to banks' balance sheets through direct exposure, lack of market liquidity management mechanism to redistribute excess liquidity further deteriorates FX shortages that originate from a surge in import-related public investment and rising global commodity prices. In a broader financial system, shadow banking activities remain substantially underreported and climate risks are rising, while poor data disclosure could hinder proper measures to tackle these vulnerabilities.

2. The sovereign-bank nexus remains the main macro-financial vulnerability, as regulatory policies continue to contribute to banks' sovereign debt holdings. Banking sector exposure to sovereign debt continues to rise above 30 percent of total banking sector assets, and sovereign exposure as share of total bank capital is higher than 400 percent in some banks. Compared with peer countries in the region, the banking system in the Maldives stands out with the highest sovereign exposure. In the current regulatory framework, the Maldives' government securities bear zero risk weight and provisioning is not required. The Maldives' government securities across all maturities are treated by banking supervisors as High-Quality Liquid Assets (HQLA) although liquidity coverage ratio (LCR) regulation has not been introduced in the Maldives, and sovereign debt holdings and government-guaranteed loans are exempt from single exposures limits. All these

Banking Sector Sovereign Debt Holding to Total Asset Ratio
(In percent)



Sources: Haver Analytics; and IMF staff calculations.

[1] Prepared by Yizhi Xu (APD).

regulatory policies have induced banks' substantial sovereign debt holding. Meanwhile, heightened public and SOE debt could erode fiscal space and jeopardize SOEs' viability, which could risk spillovers to banks that are significantly exposed to sovereign risks.

3. **Banks face risks from large exposures to a few sectors and corporates, loan dollarization, and FX liquidity mismatches**. Banks' loan portfolios are highly concentrated in tourism and construction, and many banks are highly exposed to a few large corporates. Some are close to the single exposure limit of 15 percent of regulatory capital. Under sufficient stress, banks may breach the single exposure limit even if remaining above the minimum capital adequacy ratio (CAR) requirement. Dollarization of loans to private nonfinancial corporates is particularly high at 75 percent, and a large bank has a negative net open FX position (NOP) outside the regulatory limit. Significant maturity mismatch between longer-term loans and ample daily callable deposits that also exhibit seasonality poses FX liquidity risk.

4. **Market mechanisms for redistributing liquidity across banks are limited in Maldives.** Excess liquidity in the system arose as the Maldives Monetary Authority (MMA) provided significant amount of financing to the central government. In absence of active open market operations or standing facilities, the main monetary instrument to manage systemic liquidity is the minimum reserve requirement (MRR). Lack of differentiation between MRR on local currency and FX deposits could increase dollarization in the economy.

5. **Another vulnerability centers around "shadow banking" by non-banks.** Finance companies providing lease and hire purchase options not always perform rigorous creditworthiness checks. Total recurrent household payment obligations remain unclear since most companies are not registered with the credit information bureau (CIB). As such schemes flourish unobserved by regulators, households could become overstretched and delinquencies rise.

6. **Finally, the Maldives' longstanding macroeconomic vulnerabilities are also exposed to various external risks to financial stability.** External shocks commodity price volatility, higher bank funding costs, balance sheet deterioration, and security incidents could spill over to banking sector through loan portfolio deterioration. The Maldives is exceptionally vulnerable to climate change, especially sea level rise and coastal flooding, which could affect the economy and the financial system.

B. Banking Sector Vulnerabilities

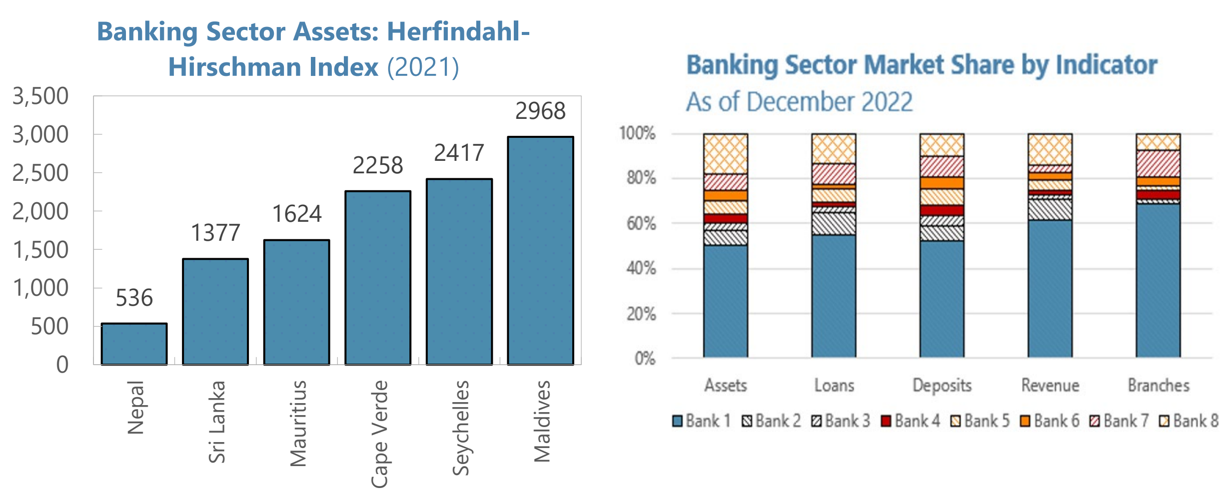
7. **Banks dominate the financial sector (Annex Table 1).** As of end-2022, total asset size of Maldives' banking sector reached MVR 88,552 million, accounting for more than three-fourths of financial system assets (two private domestic banks, five foreign-controlled banks and one domestic state-owned bank, with two of the foreign banks also state-owned). Three-fourths of banking system assets are controlled by either the Maldives or foreign governments. The sector is very concentrated (Herfindahl-Hirschman Index near 3,000, well above peers, Annex Figure 1), with the largest bank holding 51 percent of system assets.

Table 1. Maldives: Structure of the Financial System
(Data as of end-2022)

Financial Institution	Number of Institutions	Assets (millions of MVR)	Share of total assets	Share of GDP
Banks	8	88,552	78%	92%
Other Financial Corporations (OFC)	8	25,646	22%	27%
of which:				
Finance Companies, regulated	3	7,152	6%	7%
Insurance Companies	5	2,784	2%	3%
Pension Fund (MRPS)	1	15710	14%	16%
Total	16	114,198	100%	119%

Sources: MMA Monthly Statistics, Maldives Pension Administration Office (MPAO); IMF Staff calculations.
Note: Financial service providers outside the regulatory perimeter are not included.

Figure 1. Maldives: Banking Sector



Sources: Data for Maldives are from the Maldives Financial Review, data for the rest of the countries from their respective central bank or Fitch Connect.
Note: Data for Seychelles and Nepal as of 2020, and for Mauritius as of 2022 Q2.

8. **The joint IMF-World Bank's Financial Sector Assessment Program (FSAP) stress tests cover a range of analysis to gauge the banking sector resilience to economic shocks.** These span from stress tests to bank solvency and credit concentration, liquidity, sovereign risks, market risk, and climate change shocks. The stress tests were performed from both top-down at the aggregate banking sector level and bottom-up at bank-by-bank balance sheet analysis. The solvency stress test is predicated on three scenarios. The baseline and moderate stress scenarios reflect the IMF's projections[2]. The third is a bespoke crisis scenario assuming a deep, if short-lived, recession

[2] Baseline and downside scenarios in the 2022 IMF Article IV staff report of the Maldives.

from external distress that combined with mounting domestic imbalances causes a devaluation (by 20 percent) and a domestic debt exchange of T-bills for bonds (25 percent face value reduction). The credit risk modeling found only inflation and import growth (proxy for economic activity)[3] to be robust drivers. In addition, the sovereign stress in the severe scenario is based on a hypothetical situation of domestic debt exchange. It assumes a large exogenous shock that leads to a period of severe sovereign stress. Debt sustainability concerns limit external commercial and official sector support, resulting in a restructuring of domestic debt where T-bills and any other outstanding domestic government bonds (excluding those held by the MMA) are converted into a new bond on financial terms comparable to that given to the MMA in the most recent securitization of MMA claims (20-year maturity at an interest rate of 2.5 percent, equating to a 24.9 percent net present value loss applied as a haircut to the face value).

9. The stress test results corroborate that banks are less vulnerable to economic shocks than to an unraveling of the sovereign-bank nexus (Annex Table 2). The system's CAR remains largely unchanged in the moderate scenario. However, the impact of the assumed domestic debt exchange in the severe scenario[4] causes the CAR to drop by 14.8 percentage points, with 3 banks (12 percent of assets) becoming undercapitalized. In addition, several banks combining for 30 percent of assets would breach the applicable single exposure limit due to falling capital. This finding, together with strongly falling CAR in the credit concentration test assuming default of the largest five borrowers, suggests the need for more frequent syndication of large commercial loans. Lastly, if imposing a 100 percent risk weight on domestic FX securities (as the BCP assessment recommends[5]), the CAR would drop by 9 percentage points when added to the severe scenario, with one bank exhausting most of its excess capital.

10. Nevertheless, the bottom-up tests by banks see a more moderate impact. In the severe scenario, despite significant decline in CAR among some reporting banks, all of them would maintain sufficient capital. The NPL ratio projections are largely consistent with the FSAP team's estimates, especially in the severe scenario. Banks also project high profitability under the baseline and a worsening performance under stress. In fact, the more benign results based on bottom-up tests could be due to cross-bank discrepancies (some banks did not submit the required metrics or used different starting-point capital than official data).

11. Liquidity stress tests[6] indicate significant risk at individual institutions and a high susceptibility to withdrawals of large deposits. While all but one bank would meet the liquidity coverage ratio (LCR) requirements in both local and foreign currency, one bank each combining for

[3] Exports could not be used because they do not include tourism, and real GDP growth is available only annually.

[4] The test simulates a domestic debt exchange of T-bills into longer-dated and lower-yielding bonds. Consistent with Fund guidance (IMF WP/19/266) and standard practice in FSAPs with sovereign nexus analyses (e.g., Bahamas (2019), South Africa (2022), WAEMU (2022)), all T-bills were stressed, irrespective of regulatory treatment.

[5] BCP assessment conducted during the recent FSAP mission recommended amending capital adequacy rules to increase risk-weight on domestic sovereign exposure in FX from 0 to 100 percent, which is in line with the Basel III framework that requires such risk-weight for the Maldives' B- rating (Fitch).

[6] The Net Stable Funding Ratio was not computed due to lack of information on stable vs. non-stable funding.

25 percent of system assets would fail a cashflow-based maturity mismatch test[7] in local and foreign currency. Even more concerning is that about half of the banking system (measured by size) could not withstand the withdrawal of the five largest deposits, indicating inordinate deposit concentration.

12. Market risk from an interest rate shock is found to be manageable for most banks, while some are relatively exposed to FX risks in their balance sheets. The interest rate risk test simulates a symmetric increase of 200 basis points on the interest rates of assets and liabilities with residual maturities up to one year. The capitalization ratio drops by only 1.3 percentage point under this scenario, due to the short-term nature of loans and securities, of which two-thirds mature within one year (compared to 8 percent for liabilities). [8] The FX risk in balance sheets causes moderate changes in net open positions (NOPs) under a 20 percent devaluation assumption, but two banks exceed the relatively high upper NOP limit and a large bank's NOP becomes more negative and nears the single currency limit.

13. Climate stress test indicates that risks to financial stability from natural disasters may materialize over the long run. The climate risk analysis estimated a shock to physical capital under different climate scenarios[9], leveraging authorities' and global data, and imposes it onto the financial system. The physical risk analysis suggests no material mid-century coastal flood impact on the banking system, but great uncertainty about more extreme conditions at the end of the century remains. The direct damages to the capital stock for mid-century may reach up to 3.4 percent, and 20 percent for the end-century. Despite the slow arrival of climate-related impact on financial stability, these results need to be interpreted with caution, given the high uncertainty surrounding the climate data, limited data to model the geographical exposures, as well as the possible indirect damages and spillover effects in Maldives' tourism-dependent economy.

C. Conclusions and Policy Recommendations

14. Banking sector stress tests suggest that Maldives' financial system remains vulnerable to severe shocks related to sovereign, liquidity, market, and climate risks. The solvency stress test shows that the sovereign-bank nexus has exposed banks to sovereign risks. The liquidity stress test reveals significant risk at individual banks and a high dependence on large deposits. The market risk test indicates manageable interest rate risk but some exposure to FX risk for some banks. The climate risk test suggests no major impact from coastal floods until the end of the century, but with great uncertainty and possible indirect effects.

15. Systemic liquidity management framework and FX regulations should be established to mitigate risks posed by excess liquidity. MMA should swiftly differentiate reserve requirements by

[7] Based on assumptions for run-off rates on funding sources and roll-off rates on assets to estimate the funding gap based on historical volatility.

[8] The average maturity of T-bills is 290 days. Banks deliberately space their bond purchases such that equal parts come due each month. The short maturity would, however, lengthen a lot in case of a domestic debt exchange.

[9] For the hazard component, the assessment considered global climate data on sea level rise and storm surge height on actual conditions and future climate scenarios, SSP2-4.5, SSP3-7.0, and SSP5-8.5.

currency (higher rate on FX deposits) and within FX reserves by maturity (lower MRR on longer-term deposits) to mitigate dollarization risks. In the near-term, MMA should resume liquidity management operations, and introduce secondary local bonds market, including active primary dealers and an electronic platform for government debt securities auctions and trading. In addition, regulations on money changing businesses in the foreign exchange markets should be adopted. Reforms in the FX markets could mitigate FX shortage and prevent further pressures on the exchange rates due to excessive structural liquidity in the banking system.

16. The banking sector regulatory and supervisory framework needs further improvement to contain excessive risk-taking. The authorities should amend capital regulation to apply a 100 percent risk weight on bank holdings of Maldives government securities in foreign currency in a gradual pace and introduce liquidity requirements. Besides, MMA, as both financial regulator and supervisor, should issue regulatory standards to clarify the enforcement regime, reevaluate off-site monitoring procedures, and strengthen the independence of MMA's Board of Directors.

17. Macroprudential policy framework and instruments should be deployed to tackle pockets of vulnerabilities. MMA should augment reporting of data on recurrent household payment obligations from leasing contracts to the CIB. MMA should also consult with stakeholders and establish a macroprudential framework, including a committee for macroprudential coordination, and publish a financial stability report. As credit flow is rebounding, it is also important to introduce key borrower-based and capital-related macroprudential policy instruments.

18. Finally, banking sector stress testing analysis and climate risk analysis should be further enhanced to closely monitor systemic risks. The supervisors should improve integrity and granularity of supervisory data, including data compiled by the Credit Information Bureau (CIB) that could help better track and safeguard household leverage. MMA is recommended to develop methodologies for solvency, liquidity, and market risk stress tests and engage banks in a dialogue about stress test procedures and results, including banks' own stress tests. Furthermore, there is an urgent need to improve granularity and coverage of climate and geographical exposures data for establishing climate risk analysis.

Table 2. Maldives: Banking Sector Stress Test Results

	Dec. 22	Dec. 23	Dec. 24	Dec. 25
Credit Risk:	(in percent of total loans)			
NPL projection foreign currency model				
NPL ratio stress baseline scenario	9	10.5	11.8	12
Highest NPL ratio of any bank	34.4	41.6	46.1	46.8
NPL ratio stress moderate scenario	9	11	12.6	13
Highest NPL ratio of any bank	34.4	43.2	48.5	49.5
NPL ratio stress severe scenario	9	12.3	14.8	14.7
Highest NPL ratio of any bank	34.4	47	54.4	54
NPL projection local currency model				
NPL ratio stress baseline scenario	3.4	4.5	5.1	5.4
Highest NPL ratio of any bank	27.5	36.1	40.4	42.1
NPL ratio stress moderate scenario	3.4	4.7	5.5	5.7
Highest NPL ratio of any bank	27.5	37.4	42.4	43.6
NPL ratio stress severe scenario	3.4	5.4	6.3	6.2
Highest NPL ratio of any bank	27.5	41	46.2	46.2
	(in percent of risk-weighted assets)			
Capital adequacy ratio (CAR) baseline scenario	50.9	52.3	53.9	55
CAR moderate scenario	50.9	53.1	50.6	50.2
CAR severe scenario	50.9	39.3	44	45.1
Number of banks failing	...	1	...	...
Pct. of banking system <12 percent CAR	...	3.3	...	...
Capital shortfall in percent of GDP	...	0.1	...	...
CAR baseline scenario adjusted for 100 percent RW on domestic securities in foreign currency	...	41.1	...	...
Sovereign Risk:	(in percent of risk-weighted assets)			
Drop in CAR due to impact of domestic debt exchange	...	14.8	...	...
Credit Concentration Risk:				
CAR baseline scenario in 2023	50.9	52.3	53.9	55
CAR two-notch downgrade of 5 largest borrowers	50.9	46.7	48	49
CAR downgrade to loss of 5 largest borrowers	50.9	20.6	21.1	21.6
Number of banks failing	...	5	...	...
Percent of banking system <12 percent CAR	...	27.1	...	...
Capital shortfall in percent of GDP	...	0.7	...	...
Interest Rate Repricing Risk:	(in percent of risk-weighted assets)			
Increase of interest rates by 2.0 percent	...	51.1	...	...
Liquidity Risk:	(in percent of risk-weighted assets)			
Number of banks failing cashflow-based test in either currency	...	2	...	...
Banks failing the cashflow test in either currency in percent of system assets	...	25.3	...	...
Banks failing the cashflow test in either currency in percent of GDP	...	23.3	...	...
Basel III Liquidity Coverage Ratio, MVR	...	253.8	...	...
Basel III Liquidity Coverage Ratio, USD	...	235.1	...	...
Deposit Concentration Risk:	(in percent of risk-weighted assets)			
Number of banks failing test in either currency	...	7	...	...
Assets of banks failing the test in percent of banking system assets	...	49.9	...	...
Assets of banks failing the test in percent of GDP	...	46	...	...
Foreign Currency Risk:	(in percent of risk-weighted assets)			
Number of banks breaching NOP limits after 20 percent devaluation 1/	...	2	...	...
Assets of banks the test in percent of banking system assets	...	23.3	...	...
Assets of banks failing the test in percent of GDP	...	20.1	...	...

Source: Authorities' data and IMF Staff Estimates.

1/ According to MMA's Prudential Regulation on Foreign Currency Exposure Limits, the foreign currency open position exposure for all currencies shall not exceed 40 percent of a bank's capital base, and the single currency open position exposure shall not exceed 25 percent of a bank's capital base for a long position, and 15 percent for a short position.

Annex VI. Strengthening Integration of Climate Considerations into Public Financial and Investment Management[1/]

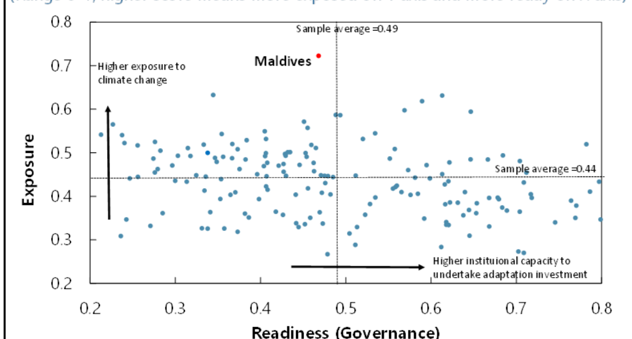
The Maldives is highly exposed to the climate change vulnerabilities and natural disasters. The integration of climate sensitivity into public financial management (PFM) and public investment management (PIM) processes can be a key contributor to government's strategies to combat the climate change. Key actions include: (i) introducing climate budget tagging (CBT) and a climate budget statement (CBS) into the budget process alongside more in-depth periodic long-term assessment of the fiscal costs and risks of climate change; (ii) providing new guidance to the public sector on how to incorporate climate sensitivity into investment plans; and (iii) adding climate dimensions to new policies on appraisal and selection projects and to those dealing with asset management and maintenance.

A. Context

1. The Maldives is highly exposed to climate change. The average elevation of the Maldives' land area is under 1.5 meters above sea level, and more than 40 percent of the population live within 100 meters of the shoreline. Climate change poses a potentially existential threat to the low-lying islands of the Maldives through sea level rise and flood. The country is also vulnerable to ocean warming and resulting coral bleaching events, potentially affecting tourism activity over the longer term. The fiscal and climate vulnerabilities together pose significant risks to the economy, livelihoods, and food security, where the atolls outside of Malé are particularly vulnerable.

Maldives: Climate Change - Exposure and Readiness

(Range 0-1, higher score means more exposed on Y axis and more ready on X axis)



Note: Sample include 188 countries. Readiness (X axis) is based on goveranance sub-componet which captures instituional factors that enhance application of investment for adaptation .

Source: Notre Dame Global Adaption Initiative 2023.

2. The Maldivian authorities are taking steps to enhance climate policies to meet its renewed climate mitigation objectives and adaptation needs. Various national mitigation and adaptation strategic plans and policies are enacted. Importantly, the Nationally Determined Contribution (NDC) of Maldives updated in 2020 lays out plans to reduce CO_2 emissions by 26 percent by 2030 and strive to achieve net zero emissions by 2030 if there is adequate international support and assistance. In addition, the Climate Emergency Act of 2021 that sets out the conditional plans to achieve net-zero emission and large adaptation needs mainly in renewable energy and resilient infrastructure. The Maldives' Integrated Financing Framework (INFF) in 2023 also provides broad principles and options for pursuing climate financing. The climate adaptation

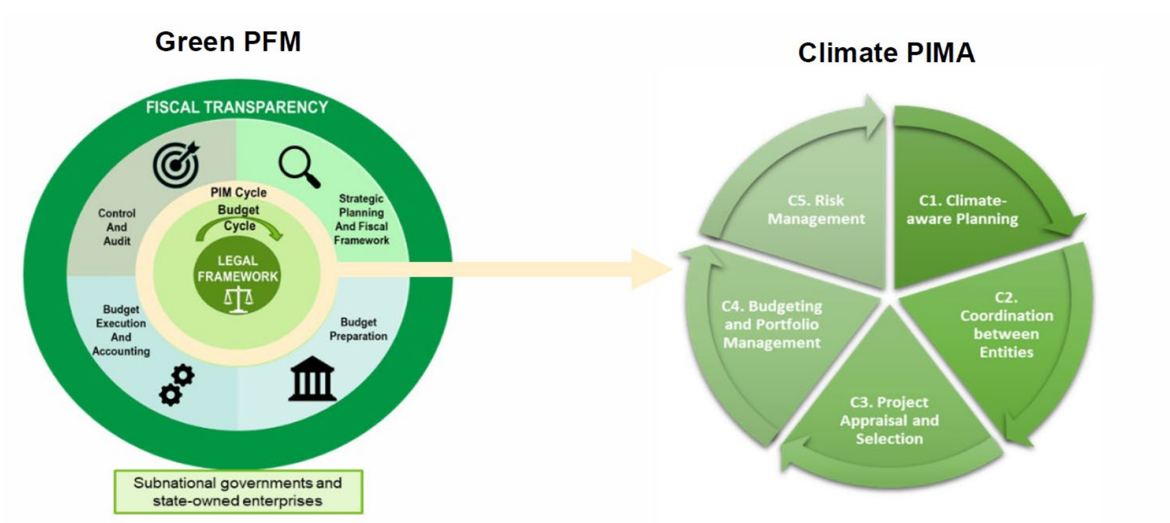
[1] Prepared by Yasuhisa Ojima (APD), based on IMF's FAD technical assistance provided to the Maldives and its draft report of "Mainstreaming Climate Change into Public Financial and Investment Management Green PFM and Climate PIMA" (January 2024).

and mitigation costs are estimated at US$8.8 billion (159 percent of 2022 GDP) and US$1 billion (18 percent of 2022 GDP) respectively. The cost of adaptation is based on some sectoral assessments mainly covering the cost of coastal protection in all inhabited islands. The Government of the Maldives is developing the National Development Strategy that lays out the country's 20-year development vision, which will include a new National Adaptation Plan (NAP) and associated implementation strategies.

B. Integration of Climate Considerations into PFM and PIM

3. The integration of climate sensitivity into public financial and investment management processes can be a key contributor to government's strategies to combat climate change. Green Public Financial Management (Green PFM) helps with the design and implementation of fiscal and expenditure policies that are responsive to climate. It allows for the integration of climate change considerations into fiscal strategy, budget preparation, budget implementation, and control and audit processes. The Green PFM assessment is complemented by the climate-sensitive Public Investment Management (Climate PIMA) framework – with a focus on ensuring that climate change considerations are mainstreamed into the public investment decision-making processes, including project appraisal, selection, and management.

Figure 1. Maldives: Linking Green PFM and C-PIMA



Source: IMF Staff.

4. Delivering on Green PFM and climate-related PIM reforms could be part of the ongoing broader PFM and PIM reforms. A new PFM reform strategy is being prepared to continue improving the fundamental elements of the budgeting process accompanied by legal reforms. Ongoing PFM initiatives supported by development partners could serve as enablers for developing green PFM tools. With the limited fiscal space, spending efficiently and making carefully prioritized spending decisions to respond to the climate challenge is more critical than ever. Where access to climate financing is demanding on PFM related requirements, the authorities are encouraged to continue their PFM reforms to improve current PFM practices and make them environment and climate sensitive. IMF's Public Investment Management Assessment (PIMA) highlighted underlying weaknesses in public investment and financial management, including critical areas such as investment planning, project appraisal and selection, project funding, and the development of a realistic project pipeline. Without progress on these fundamentals the integration of more advanced climate change considerations into PFM procedures is unlikely to be successful. The C-PIMA assessment needs to be built on these ongoing efforts for improving the underlying PFM system.

5. Key actions to incorporate climate considerations into PFM and PIM could be summarized as the following:

- ***Introducing climate budget tagging (CBT) and a Climate Budget Statement (CBS) into the budget process alongside more in-depth periodic assessment of the fiscal costs and risks of climate change.*** The authorities could design CBT methodology and introduce this methodology in the preparation of the 2026 budget, including for the assessment of new policy initiatives, and use CBT to monitor climate-related expenditures in execution. Work is ongoing in this respect with UNDP (United Nations Development Program) support, building up on experience with Sustainable Development Goals (SDG) budgeting. Meanwhile, the authorities could prepare and publish a first CBS as part of the budget proposal, including elements from CBT applied in budget preparation. In the longer term, the authorities should undertake an in-depth periodic assessment of the long-term fiscal costs and risks of climate change by committing to regular periodic analysis of the long-term fiscal costs, risks, and impacts of climate change, and potentially other policy areas that will affect long-term fiscal sustainability.

- ***Providing new guidance to the public sector on how to incorporate climate sensitivity into investment plans***, with a stronger role for the Ministry of Finance (MoF) and Ministry of Climate Change, Environment and Energy (MoCCEE) in enforcing this. The authorities should issue joint MOF/MoCCEE regulation providing guidance on developing costed climate-sensitive sector and local public investment plans and SOE business plans; and require MoF and MoCCEE to review and verify that these plans contribute to NDC targets and are financially realistic.

- ***Adding climate dimensions to new policies on project appraisal and selection processes and to improved systems dealing with asset management and maintenance.*** The authorities should develop PIM regulations clarifying the project appraisal and selection processes and include climate-related analysis and criteria in these processes. Meanwhile, climate dimensions need to be incorporated into improved systems for dealing with asset management and maintenance by preparing guidelines for fixed assets registration that include climate related information and a methodology for calculating the costs of maintenance of fixed assets that includes climate considerations.

Annex VII. Capacity Development Strategy [1/]

The Maldives is one of the intensive IMF capacity development (CD) recipients amongst countries in Asia and the Pacific region. CD priorities are closely aligned with IMF surveillance policy recommendations that include revenue mobilization, expenditure rationalization, public financial and debt management, financial sector reforms, and monetary and exchange rate policies.

1. **CD continues to support the authorities' reform efforts to address economic vulnerabilities in the Maldives.** Reflecting IMF Surveillance policy priorities to swiftly implement a comprehensive set of reforms to reduce fiscal, debt, and external vulnerabilities, and strengthen economic resilience, CD support for the Maldives has been intense, particularly to strengthening its institutions and policy frameworks in the area of tax policy and administration, expenditure policy, and public financial management (Annex Text Figure 1, left chart). CD provided to the Maldives has been effective, where more than half of CD activities achieved their milestones (Annex Text Figure 1, right chart). CD is currently delivered by both regional advisors from IMF South Asia Regional Training and Technical Assistance Center (SARTTAC) and headquarter-based missions.

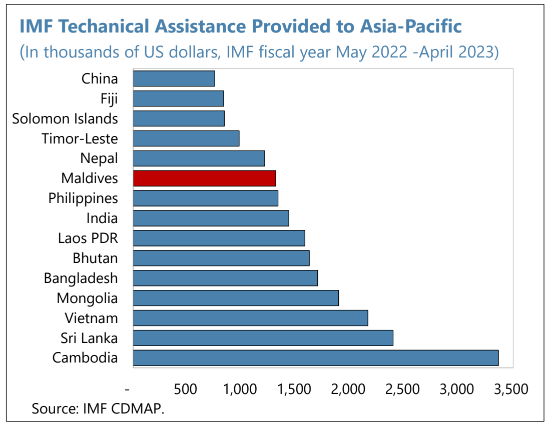
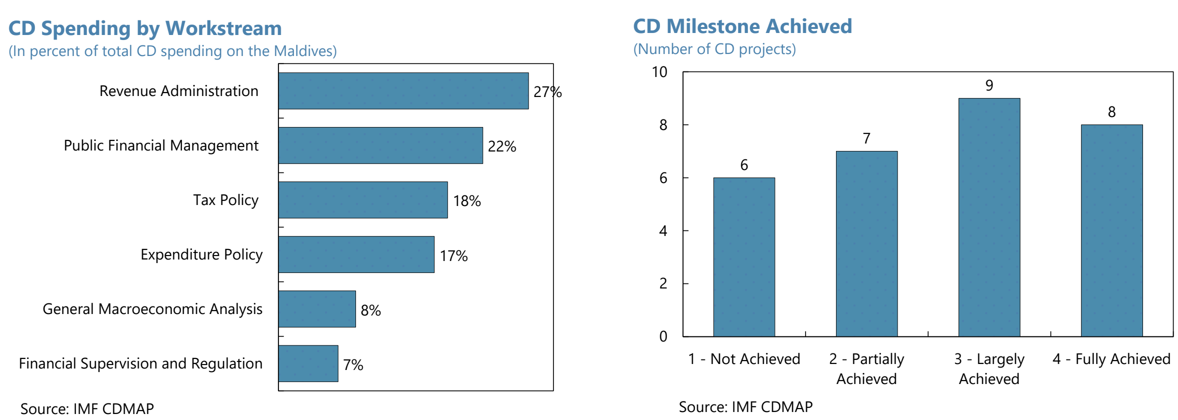


Figure 1. Maldives: CD Workstream and Achievements in FY23



[1] Prepared by Yasuhisa Ojima (APD).

Fiscal Policy

2. Background. CD in fiscal policy area highlights the Maldives' urgent need to implement a sustained fiscal consolidation comprising revenue mobilization effort and expenditure rationalization to reduce public debt vulnerabilities. Fiscal reforms to improve public spending efficiency, enhance fiscal transparency, and manage fiscal risks are also crucial.

3. Ongoing and planned activities on tax policy and administration. Ongoing activities include a review of the amendments to income tax act on tax policy and strengthening custom administrations with the Maldives Customs Service (MCS) (e.g., Integrated IT system). Going forward, on income tax policy, planned activities include a review of productivity and scope for improvement (e.g., simplification measures such as a presumptive tax for SMEs), tax thresholds, and anti-avoidance provisions for large multinational businesses). On excise, CD priorities would include the introduction of a new Excise Act that is currently deliberated as part of the ongoing Medium-Term Revenue Strategy (MTRS). On tax expenditures, a follow-up on reporting and evaluation would be considered. On tax administration, CD support to the Maldives Inland Revenue Authority (MIRA) and MCS is expected to continue to support the MTRS in priority areas, such as international tax, development of an IT Strategy, high-wealth individual compliance, taxation in the financial sector, and post clearance audit. Coordination with other development partners will continue.

4. Ongoing and planned activities on expenditure policy and public financial management. Strengthening public financial management and public investment management remains priorities. Ongoing activities include a review of pension system reform to assess its fiscal sustainability, a review of fiscal risk management in SOEs, and integration of climate change into the public financial and investment management (Green PFM and Climate PIMA). The authorities are implementing the recommendations of the past CD support including on the Fiscal Responsibility Act (FRA), the Public Debt Management Law, and drafting of the Sovereign Development Fund (SDF) law in 2023, energy subsidy reforms in 2022, and on fiscal transparency evaluation (FTE) in 2021. CD on developing macro-fiscal forecasting and medium-term macroeconomic framework tools, currently being provided by ICD, will also help build the authorities' capacity to strengthen fiscal policy making. Planning activities include "drafting a Sovereign Development Fund Law" and "drafting a new SOE Law."

Monetary and Exchange Rate Framework

5. Background. For monetary and exchange rate policies, CD will continue to focus on operationalizing an interest rate-based framework (i.e., interest rate corridor). The Maldives Monetary Authority (MMA) strategy to build reserves is also aiming at normalizing FX operations, redirecting FX receipts from the parallel market, and reviewing FX allocation to SOEs. This would help enhance macroeconomic stability and bolster external buffer against external shocks.

6. Ongoing and planned activities. IMF TA has covered MMA strategic plan, central bank governance, function two-way FX market, and active liquidity management. Looking ahead, IMF TA will continue to assist the implementation of the MMA's Strategic Plan through a multi-year TA program, aiming to: (i) strengthen the monetary policy and operational framework, including defining an interest rate corridor and directing interbank interest rates inside it, through re-activating open market operations (OMOs), (ii) develop functioning FX markets, and (iii) review the current exchange rate regime to support resilience and implement a strategy for partial and gradual de-dollarization and FX reserve accumulation.

Financial Sector

7. Background. Since January 2018, SARTTAC has provided CD support to strengthening the financial sector supervisory capacity of the MMA in three areas, including banking and insurance supervision and non-bank financial institutions (NBFIs) regulation. A joint IMF-World Bank Financial Sector Assessment Program (FSAP) with the Maldives concluded May 2023 identified the key financial sector vulnerabilities arising from bank-sovereign nexus, high dollarization, and FX scarcity. FSAP recommendations centered on strengthening bank regulations and supervisions to address such macro-financial systemic vulnerabilities.

8. Ongoing and planned activities. IMF CD focused on developing and implementing risk-based banking supervision (e.g., the preparation of the implementation of risk management guidelines, reviews of on-site inspection and off-site supervision manuals, and drafting of a regulation on liquidity risk management), as well as improving and disseminating financial soundness indicator (FSI). Going forward, while CD will continue to assist the authorities in the area of risk-based supervision, CD activities will be aligned with FSAP recommendations and priorities.

Table 1. Maldives: Integrating Fund Surveillance and Capacity Development (CD)

CD Priorities	Surveillance Policy Recommendations	CD Activities and Plans
Tax policy and administration	A sustained fiscal consolidation that relies both on expenditure rationalization and domestic revenue mobilization is key.	• In 2022, FAD provided a technical assistance (TA) on medium-term revenue strategy that provides options to raise up to 9.4 percent of GDP in revenue by 2028. An FAD TA mission also reviewed the goods and services tax (GST) and additional support was provided by FAD and SARTTAC to improve tax administration, including the management of international tax risks, estimate of GST gap, and completion of a Tax Administration Diagnostic Assessment Tool. • In 2023, FAD TA mission reviewed the draft amendments to Income Tax Act and continued to support the MTRS formulation and strengthening custom administrations.
Expenditure policy	Rationalizing subsidies, combined with targeted assistance to the most vulnerable, and a reform of SOEs would support the fiscal consolidation effort.	• In 2022, FAD provided TA on reviewing the fuel and electricity subsidies regimes. • In 2023, FAD have supported review of fiscal risk management in SOEs and review of pension oversight and fiscal risks management.
Public financial management	Accelerating reforms in public financial and investment management would help enhance the credibility of fiscal policy.	• In 2023, FAD provided TA on developing a law for the Sovereign Development Fund (SDF), and an evaluation of fiscal transparency following the Fiscal Transparency Code of the IMF. SARTTAC reviewed Fiscal Risk Management in State Owned Enterprises. FAD assisted the authorities revising the Fiscal Responsibility Act (FAD 2020). • A TA on Climate Public Investment Management (C-PIMA) and Green Public Financial Management (Green PFM) is scheduled for early 2024.
Debt management	Improving debt management capacity will help better assess and address debt-related risks.	• In 2023, TAs on SDF and SOEs contributed to strengthening debt management capacity in 2023, while Fund TA assisted to develop a Debt Management Law (FAD/MCM/LEG- two missions in 2021)
Monetary and Exchange Rate Policies	Implementing the FX reform strategy.	• SARTTAC provided several TA missions to the MMA to provide guidance on wide range of areas including on the MMA Strategic Plan, central bank governance, functioning two-way FX markets, de-dollarization, currency baskets and active domestic liquidity management. • In 2023, SARTTAC TA focused on introducing the interest rate corridor for an active liquidity management to support the peg.
Macro Forecasting	Enhancing macroeconomic forecasting and policy analysis capacity.	• ICD is providing a 3-year TA project to build MMA's capacity for consistent baseline forecasts and scenario analyses to further support policy discussions.
Statistics	Improving macroeconomic statistics for better forecasting and policy analysis.	• In 2023, SARTTAC provided TA to help the authorities collect data and map it to the GFSM2014 frameworks for key city councils and extrabudgetary units. STA provided TA to assist the Maldives Monetary Authority (MMA) in compiling Financial Soundness Indicators (FSIs) based on international standards as set out in the IMF's 2019 FSIs Compilation Guide (2019 FSIs Guide).

Source: IMF Staff.
Note: CD providers by IMF departments include Fiscal Affairs Department (FAD), Institute of Capacity Development (ICD), Legal (LEG) Department, Monetary and Capital Markets (MCM) Department, Statistics (STA) Department, and South Asia Regional Training and Technical Assistance Center (SARTTAC).

INTERNATIONAL MONETARY FUND

MALDIVES

February 28, 2024

STAFF REPORT FOR THE 2024 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By	Asia and Pacific Department (In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of January 2024)

Membership Status: Joined: January 13, 1978; Article XIV

General Resources Account:	**SDR Million**	**Percent Quota**
Quota	21.20	100.00
Fund holdings of currency (exchange rate)	16.40	77.34
Reserve Tranche Position	4.80	22.66

SDR Department:	**SDR Million**	**Percent Allocation**
Net cumulative allocation	28.01	100.00
Holdings	0.95	3.38

Outstanding Purchases and Loans:	**SDR Million**	**Percent Quota**
RCF Loans	21.2	100

Latest Financial Commitments:

Arrangements:

Type	**Arrangement Date**	**Expiration Date**	**Amount Approved (SDR million)**	**Amount Drawn (SDR Million)**
Stand-By	12/04/2009	12/3/2012	49.20	8.20
ESF	12/04/2009	12/3/2011	8.20	2.05

Outright Loans:

Type	**Commitment Date**	**Expiration Date**	**Amount Approved (SDR million)**	**Amount Drawn (SDR Million)**
RCF	04/22/2020	04/24/2020	21.20	21.20

Projected Payments to Fund[1]

(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2024	**2025**	**2026**	**2027**	**2028**
Principal		2.12	4.24	4.24	4.24
Charges/Interest	0.11	1.10	1.10	1.10	1.10
Total	**0.11**	**3.22**	**5.34**	**5.34**	**5.34**

[1]When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Exchange Arrangements

Since April 2011, the rufiyaa has floated in a band of 20 percent on either side of MVR 12.85 per dollar. In practice, however, the rufiyaa has been virtually fixed at the band's weaker end of MVR 15.42 per dollar. The de jure exchange rate arrangement is a pegged exchange rate within horizontal bands and the de facto exchange rate arrangement is classified as a stabilized exchange rate arrangement. Maldives continues to avail itself of the transitional provisions of Article XIV but no longer maintains any measures under this provision, and has not yet accepted the obligations of Article VIII, Sections 2, 3, and 4.

The Maldives maintains an exchange restriction arising from the Maldives Monetary Authority's rationing of its supply of foreign exchange (FX) to commercial banks and state-owned enterprises to certain priority items, which also result in a channeling of FX for current international transactions to the illegal parallel market[1]. The authorities should continue undertaking reasonable efforts to eliminate the spread with the parallel market.

Last Article IV Consultation

The 2022 Article IV consultation was concluded by the Executive Board on November 23, 2022.

Technical Assistance

IMF Fiscal Affairs Department (FAD): FAD's main areas of engagement in recent years have been on tax policy and tax administration, subsidy reforms, public investment and financial management, and debt management. Public Investment Management Assessment (PIMA) was conducted by FAD in December 2016, with the purpose to identify, and propose improvements in, PFM practices that are associated with efficient public investment. October 2017 Tax Administration technical assistance (TA) mission reviewed progress with the strategic priorities in the Maldives Inland Revenue Authority (MIRA) 2015–19 Strategic Plan. The January 2018 Budget Formulation TA mission focused on budget preparation and public investment management. A follow-up mission on Strengthening Public Investment Management took place in June 2018. In July 2018, a TA mission focused on developing a risk management framework for Maldives Inland Revenue Authority (MIRA). A Tax Policy TA took place in February 2019, to assess the overall design of taxation in the Maldives and identify reform options to support revenue, efficiency, and equity. Also, in February 2019, concurrent tax administration missions took place to advise MIRA on the development of the 2020-24 Strategic Plan and risk framework, as well as improve the skills of staff. In February 2020, a mission took place to strengthen the management of fiscal risks of SOEs and a tax policy reform assessing the recent

[1] The Maldives previously maintained a multiple currency practice resulting from the lack of a mechanism to prevent the spread between the official exchange rate used by the MMA for government transactions and the prevailing market exchange rate from deviating by more than 2 percent. In line with the revised Multiple Currency Practice (MCP) policy that became effective on February 1, 2024, all MCPs maintained by members under the previous MCP policy are considered eliminated as of February 1, 2024. The following MCPs are considered eliminated as of July 1 2022: MCPs arising from (i) FX auction if the auction meets the criteria set out in Paragraph 15, (ii) official exchange rate if its calculation conforms to the conditions specified in Paragraph 16 and (iii) illegal parallel markets as specified in Paragraph 17 of the "Review of the Fund's Policy on Multiple Currency Practices—Proposals for Reforms" (2022).

progress and proposing further improvements. Also, in November 2020, two missions took place on reviewing the current Fiscal Responsibility Act and a Fiscal Transparency Evaluation following the Fiscal Transparency Code of the IMF. In 2021, FAD with MCM conducted a joint desk review of the debt management law and a Tax Administration Assessment Tool (TADA) mission was conducted. In 2022, three missions took place, on Medium-term Revenue Strategy (MTRS), GST Gap Analysis, and Fuel and Electricity Subsidy Reforms. In 2023, FAD assisted the authorities in i) developing a legal, policy and operational framework for the Sovereign Development Fund (SDF) in February, ii) reviewing draft MTRS, especially on revenue administration in May, iii) reviewing SOE risk management jointly with South Asia Regional Training and Technical Assistance Center (SARTTAC) in July, iv) reviewing draft amendments to Income Tax Act (ITA) in November; iv) improving the custom administration (e.g., valuation control) by Maldives Custom Services (MCS) in September and November; and v) developing a baseline understanding of the pension system's sustainability and opportunities to increase long-term sustainability for the Maldives Pension Administration Office (MPAO) in November. In 2024, FAD assisted the authorities in mainstreaming climate change considerations into public financial and investment management (Green PFM and Climate PIMA).

IMF Legal Department (LEG): In October 2003, LEG provided TA on the revision of the Maldives Monetary Authority (MMA) Act. A series of missions (March and September 2005, and April 2006) were provided to revamp the banking law. In August 2009, a mission provided help with the MMA Act (jointly with MCM). A follow-up mission in February 2011 focused on payments law. LEG conducted an AML/CFT assessment in October 2010 and conducted a desk-based review of the draft AML/CFT law in May 2012. In 2014 and 2015, LEG provided advice on the Special Economic Zones Law, offshore banking legislation and deposit insurance.

IMF Monetary and Capital Markets Department (MCM): In 2006, two missions provided TA on monetary operations, financial market development, and banking issues. In 2007, TA on debt management, monetary policy and financial supervision was delivered. In 2008, three missions consulted on monetary operations and liquidity management, monetary policy, and financial supervision issues. In November 2008 and March/May/August 2009, TA was provided on research capacity building, banking supervision, and monetary policy and reviewing of the MMA Act with recommendations. Furthermore, two missions also provided advice on monetary operations, liquidity management, and the development of a crisis management framework. In December 2010, MCM conducted a TA mission on crisis preparedness and management, bank restructuring, and monetary operations. In May and September 2011, TA on the development of debt markets and on-site banking supervision was provided and in February 2012, on assessing the FX operations framework. In the first half of 2014, MCM continued its TA delivery on banking supervision along with a joint MCM-APD mission on developing FX market. The Department also provided advice on deposit insurance schemes during 2014. Banking supervision (March) and FX reserve management (September) continued to be areas of priority to the authorities in 2015 with MCM TA responding with follow-up missions. In March 2016, further TA on FX and monetary policy operations was also provided. A follow-up mission on banking supervision with a focus on operational risk took place in May 2016. During 2017, two HQ missions covering accounting and auditing framework for MMA, and two SARTTAC missions establishing the work plan for monetary operations and banking supervision took place. Four TA missions took place during 2017-18 as part of the multi-year TA program to enhance the supervisory capacity of the Insurance Division of the MMA. In December 2018, a multitopic TA took place to formulate a TA roadmap to support MMA's reforms, including central bank governance, monetary and FX operations and financial sector supervision and regulation, with a follow up mission in 2019 and desk-review of various of policy notes in 2021 on Use of MVR in all monetary transactions; Repatriation and surrender of export earnings; Licensing money changers. SARTTAC fielded a mission in 2020 to assist MMA in strengthening its supervisory capacity in financial supervision and regulation of the banking and insurance. In January 2019, a TA mission assisted the authorities in the application of International Financial Reporting Standard 9 – Financial Instruments and reviewing progress in the strengthening of their Internal Audit and Enterprise Risk Management practices. In February 2019, an external expert visited Maldives to advise the MMA governor on strengthening the MMA governance and internal organization. During December 2021 to January 2022, a TA mission on operationalizing an interest rate corridor provided a set of recommendations on the introduction and implementation of an interest rate corridor as a way to support an active liquidity management policy and a policy tool to support the development of the money market and the use of domestic currency. TA missions on strengthening MMA's banking supervision capacity were concluded in June 2022 and November 2023 to assess MMA's implementation of corporate governance regulations and risk management guidelines and provided further recommendations to ensure full implementation in practice.

***IMF Statistics Department (STA)*:** An April 2018 external sector statistics SARTTAC mission assessed data reliability and assisted in improving specific balance of payments (BOP) components, advised on further developments in source data and statistical techniques to address existing data gaps. An August 2018 SARTTAC mission has provided government finance statistics (GFS) and public sector debt statistics (PSDS) training - the onset of a broader SARTTAC training and technical assistance effort to enable the Maldives to improve and strengthen its fiscal reporting. In January 2019, a SARTTAC mission on GFS and PSDS focused on strengthening compilation and dissemination of the statistics in line with internationally accepted statistical standards. A subsequent SARTTAC PSDS training mission, held in August 2019, provided training to compilers on the concepts, methods, and practices related to PSDS compilation and dissemination. In February 2019, SARTTAC missions assisted with the updating of the consumer price index and developing experimental annual GDP estimates by expenditure at current prices for 2017. In January 2020 and January 2021, SARTTAC GFS and PSDS missions focused on enhancing compilation and dissemination practices, including aligning GFS and PSDS reports to the *GFSM 2014* framework, moving forward to producing quarterly GFS reports, and broadening the institutional coverage of the fiscal statistics. During 2020 and the first half of 2021, several SARTTAC missions focused on national accounts statistics including improving the expenditure approach for annual GDP and quarterly national accounts. In June 2022, SARTTAC provided a technical assistance mission to assist the Maldives Bureau of Statistics (MBS) with developing the producer price index (PPI) and updating the consumer price index (CPI). In December 2022, SARTTAC also assisted MBS develop the supply use tables (SUTs) to rebase GDP with new base year of 2019. In January and November 2023, SARTTAC sent an in-person mission to help the authorities start collecting data and mapping it to the GFSM2014 frameworks for key city councils and EBUs. In March 2023, an in-person TA mission was conducted to assist the MMA in compiling financial soundness indicators (FSIs) based on international standards as set out in the IMF's 2019 FSIs Compilation Guide (2019 FSIs Guide).

IMF Institute of Capacity Development (ICD): Two in-person TA missions took place in May and August 2023, as part of an ongoing TA project to assist the MMA to customize and implement an Excel-based microframework in line with the "Comprehensive Adaptive Expectations Model" (CAEM). The framework will assist the MMA to produce a consistent and comprehensive baseline forecast and risk analysis that will enhance surveillance and policy discussions with the authorities.

Safeguards Assessment

In line with the Fund's safeguards assessments policy, an assessment of the MMA was concluded in March 2010. In addressing Fund's recommendations, the MMA appointed an external auditor and strengthened controls over foreign payments through the automation of the authorization process. A Chief Internal Auditor was also appointed and capacity in the internal audit function has continued to improve. In addition, to strengthen the legal framework, amendments to the MMA Act were approved in 2020. The authorities have committed to undergo an update safeguards assessment in connection with the rapid credit facility (RCF) arrangement, which is currently in progress.

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

Information on the activities of other IFIs in Maldives can be found at:

World Bank: https://www.worldbank.org/en/country/maldives

Asian Development Bank: https://www.adb.org/countries/maldives/main

STATISTICAL ISSUES

(As of January 2024)

I. Assessment of Data Adequacy for Surveillance
General: Macroeconomic statistics have improved in recent years, with technical assistance from STA and the Asian Development Bank (ADB). While data are broadly adequate for surveillance there are nonetheless data gaps remaining affecting the balance of payments, government finance, and national accounts statistics.
Real sector: Maldives compiles quarterly and annual national accounts (base year 2019) using supply and use tables (SUTs 2019). IMF's STA and SARTTAC assisted in modernizing and improving the EXCEL-based GDP compilation system which further improved the consistency between GDP-Production and Quarterly GDP estimates. GDP by expenditure and quarterly GDP series were also improved and disseminated on Maldives official website. SARTTAC organized a mission in December 2022 to support the authorities' work program to develop SUTs for 2019 and to subsequently rebase GDP to 2019. The Maldives Bureau of Statistics (MBS) released the new GDP series by production on its website in August 2023. In December 2022, the MBS released an updated Consumer Price Index (CPI) based on weights from the 2019 Household Income and Expenditure Survey. Plans to expand CPI coverage to include owner occupied housing have been put on hold until the next update as further improvements are needed to the rent index. The MBS compiles and disseminates Producer Price Indexes (PPI) for electricity, water supply, resorts (accommodation and food services), construction, information and communication, and education. Monthly PPI data are disseminated on a quarterly basis. PPI coverage will be expanded to include fishing and transportation in early 2024.
Fiscal sector: With support from SARTTAC, the authorities are currently disseminating GFS data based on the *Government Finance Statistics Manual 2014* for the budgetary central government (BCG). The authorities have also started compiling on an experimental basis quarterly GFS for BCG. Furthermore, the authorities have ongoing reforms to update the chart of accounts and update the accounting basis to follow international standards allowing for the production of balance sheet data. Data on local government is limited; however, with decentralization being implemented, plans are underway to provide a portal with detailed data on the finances of local government. On SOEs, a quarterly report is produced with data on individual SOEs; however, GFS data for a consolidated public corporations subsector is not currently being produced.
Financial sector: The MMA uses the standardized report forms (SRFs) to report monthly data for the central bank, other depository corporations and other financial corporations to the Fund on a regular basis. An integrated monetary database that meets the needs of the MMA, STA, and APD is operational. There are inconsistencies between monetary and fiscal data regarding the financing of the fiscal deficit due to issues of timing and coverage. Maldives also reports data on some key series of the Financial Access Survey, including mobile money and gender-

disaggregated series, and the two indicators (commercial bank branches per 100,000 adults and ATMs per 100,000 adults) adopted by the United Nations to monitor Target 8.10 of the Sustainable Development Goals. Following a TA mission from STA in 2023, MMA now reports 14 core Financial Soundness Indicators (FSIs) and ten additional FSIs for deposit takers, and two FSIs on real estate markets on a monthly basis; as well as two additional FSIs on other financial corporations (OFCs), three additional FSIs on insurance corporations and one FSI on households on a quarterly basis for publication on the IMF's FSI website.	
External sector: The MMA compiles balance of payments data on an annual basis only. The MMA is finalizing new international transaction reporting system (ITRS) that will assist them in the compilation of quarterly BOP and international investment position (IIP) statistics. They also have taken some actions to improve the coordination among data producers and the data collection processes. MMA does not compile Coordinated Direct Investment Survey (CDIS), Coordinated Portfolio Investment Survey (CPIS) data, and there are difficulties in pulling together all the existing information that would allow for a consistent compilation of the financial transactions for the preparation of these data. Quarterly data on external debt and debt service are available for the government and the MMA, and to some extent for the banking sector and state enterprises, but no data are reported to the World Bank Quarterly External Debt Statistics (QEDS) database. The main source for external debt statistics (EDS) is the Commonwealth Secretariat Debt Recording Management System (DRMS). This system has inbuilt EDS templates for reporting these data to the World Bank and for assisting the MMA in improving external sector statistics (ESS). Official reserves assets are reported every two weeks with a (variable) one-week lag. Predetermined foreign currency outflows (mainly debt service payments) are known and reported to APD at the time of annual Article IV consultation missions, while other movements of foreign currency assets are not identified.	
II. Data Standards and Quality	
Maldives has participated in the IMF's General Data Dissemination System (GDDS) since October 14, 2011, with its metadata posted on the Data Standards Bulletin Board. On June 18, 2019, with IMF support, Maldives implemented the recommendations of the Enhanced General Data Dissemination System (e-GDDS) by publishing essential macroeconomic statistics through a National Summary Data page (NSDP).	No data on the report on the observance of standards and codes (ROSC) available.

Maldives: Table of Common Indicators Required for Surveillance

(As of January 31, 2024)

	Date of Latest Observation	Date Received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of Publication[6]
Exchange Rates	December 2023	January 2024	M	M	M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	December 2023	January 2024	M	M	M
Reserve/Base Money	December 2023	January 2024	M	M	M
Broad Money	November 2023	December 2023	M	M	M
Central Bank Balance Sheet	December 2023	January 2024	M	M	M
Consolidated Balance Sheet of the Banking System	November 2023	December 2023	M	M	M
Interest Rates[2]	December 2023	January 2024	M	M	M
Consumer Price Index	December 2023	January 2024	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	N.A.	N.A.	N.A.	N.A.	N.A.
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	2022	September 2023	A	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2022	September 2023	A	A	A
External Current Account Balance	2022	September 2023	A	A	A
Exports and Imports of Goods and Services	2022	September 2023	A	A	A
GDP/GNP	2022A, 2023Q3	August 2023, January 2024	A, Q	A, Q	A, Q
Gross External Debt	2022A	September 2023	A	A	A
International Investment Position		Not available			

[1]Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2]Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes, and bonds. Interest rates on bank deposits are not provided.
[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.
[5]Including currency and maturity composition.
[6]Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).

INTERNATIONAL MONETARY FUND

MALDIVES

March 5, 2024

STAFF REPORT FOR THE 2024 ARTICLE IV CONSULTATION—DEBT SUSTAINABILITY ANALYSIS

Approved By
Anne-Marie Gulde-Wolf and Boileau Yeyinou Loko(IMF) and Manuela Francisco and Mathew A. Verghis (IDA)

Prepared by the staffs of the International Monetary Fund and the International Development Association.[1]

Maldives: Joint Bank Fund Debt Sustainability Analysis	
Risk of external debt distress	High
Overall risk of debt distress	High
Granularity in the risk rating	Unsustainable
Application of judgement	No

The Maldives remains at a high risk of external and overall debt distress same as the previous Debt Sustainability Analysis (DSA).[2,3] *External gross financing needs have increased relative to the previous DSA due to (i) high commodity prices, (ii) a more expansionary fiscal stance amid increases in capital project related spending, subsidies, and recurrent expenditures, and (iii) repayments and rollovers of non-concessional debt, mainly global sukuk. External refinancing pressures are expected to peak in 2026. Increasingly higher amortizations and large interest payments would trigger protracted breaches in several debt indicators, leading to the assessment of debt not sustainable under the authorities' current policies. The debt dynamics will remain vulnerable to adverse shocks in growth, interest rates, and fiscal position in the near term. The key external debt indicators, the present value (PV) of external debt-to-GDP, will converge to the 30 percent threshold by the medium-term. Restoring debt sustainability requires sustained fiscal consolidation, continued strong growth, and prudent debt management.*

[1] This DSA has been prepared jointly by the IMF and World Bank, following the 2018 Guidance Note on the Bank-Fund Debt Sustainability Framework for Low Income Countries.

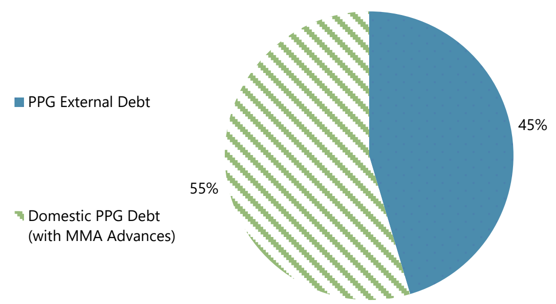
[2] IMF Country Report No.23/366, November 2023.

[3] The Maldives Composite Indicator of 2.40 indicates a weak debt-carrying capacity, based on the October 2023 IMF's World Economic Outlook (WEO) and the 2022 World Bank's Country Policy and Institutional Assessment (CPIA).

BACKGROUND AND DEVELOPMENTS ON DEBT

1. **Supported by strong tourism rebound, total public and publicly guaranteed (PPG) debt-to-GDP ratio declined in 2022.** Total PPG debt fell to about 110 percent of GDP in 2022, from 120 percent in 2021. Nevertheless, public debt-to-GDP ratio remains elevated and is estimated to rise further in 2023, compared to its pre-pandemic level of 78.8 percent in 2019, reflecting large fiscal deficits in response to spending pressures and heightened global commodity prices. Nominal PPG debt stock increased to US$6,885 million in 2022 from US$6,469 million in 2021, driven by a large annual increase in central government budgetary debt, to about US$5,939 million (an increase of about 7.4 percent), even as guaranteed debt remained broadly unchanged at about US$946 million. Overall, both external and domestic debt increased during 2022 with domestic debt slightly above half of the mix (55 percent of total).

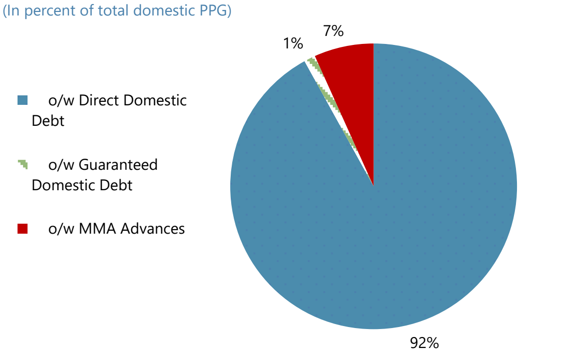
Maldives: PPG Debt, 2022
(In percent of total)



Source: Maldives Ministry of Finance.

2. **Domestic PPG debt increased.** Domestic PPG debt rose to US$3,813 million (or around 61 percent of GDP) in 2022, up from US$3,452 million in 2021. To bridge the financing of the government, the parliament of the Maldives approved the temporary suspension of elements of Fiscal Responsibility Act (FRA) to allow for expansion of the cap on government advances with the Maldives Monetary Authority (MMA) to MVR 4.4 billion (US$286 million) until end-2023.[4] Domestic PPG debt in 2022 also included US$256 million (MVR 3,946 million) in advances or around 7 percent of total domestic PPG debt, from the MMA to the central government. In 2022, the authorities securitized the outstanding MMA advances, in the amount of MVR 2.5 billion (US$160 million) by converting the advances into a 40-year bond at a 2.4 percent annual interest. Commercial banks had the largest claim on central government, around US$1,695 million (44 percent of domestic PPG debt). The State Bank of India (SBI) Male Branch purchased a US$100 million bond in 2022, in addition to a US$250 million bond purchased in 2020 as budget support to buffer the impact of COVID-19 pandemic. The bond issued in 2020 is expected to be paid back in 10 years and that in 2022 in

Maldives: Domestic PPG Debt, 2022
(In percent of total domestic PPG)



Sources: Maldives Ministry of Finance; and Maldives Monetary Authority.

[4] The advances were initiated in March 2020. The Ministry of Finance was granted a one-year extension to the increase in the cap on government advances to help bridge financing needs in 2021. A further extension of the increase in cap in the amount of MVR 4.4 billion was granted until April 2022 and extended until December 2023 at 1.5 percent per annum. In September 2021, the authorities securitized in the amount of MVR 2.5 billion of the outstanding advances converting into 40-year bond at 2.4 percent per annum.

7 years as a bullet payment with bi-annual interest payment in dollars at the interest rates of 3.75 percent and 7.75 percent respectively.[5]

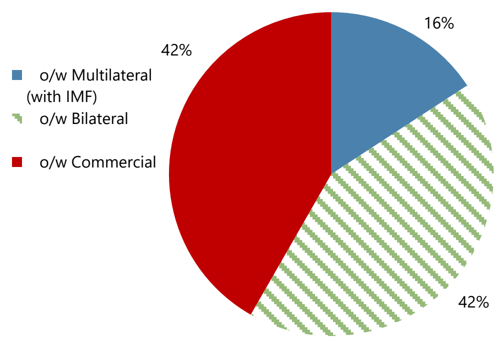
3. External PPG debt was broadly unchanged, amid high costs and limited access to external financing. External PPG debt stood at US$3,072 million (or around 49 percent of GDP) in 2022, up from US$3,046 million in 2021 in nominal terms. External PPG debt is predominantly owed to bilateral and commercial creditors. Direct budgetary debt constituted 71 percent of external PPG debt, and the remaining 29 percent contracted by State-Owned Enterprises (SOEs) with sovereign guarantees. Guaranteed external loans for housing development projects carried out by SOEs, including the Housing Development Corporation (HDC) and the Fahi Dhiriulhun Corporation (FDC), accounted for about 60 percent of total guaranteed external loans. Guaranteed external SOE debt is owed mainly to commercial creditors (around 8 percent of total) with the rest (4 percent) to bilateral creditors and a small amount (1 percent) to a multilateral creditor. China is the largest creditor with about 19 (42) percent of total (external) PPG debt. The Maldives used a swap arrangement with Reserve Bank of India (RBI) in the amount of US$100 million in 2022, which was paid back in full in 2023. This swap with RBI was excluded from external PPG.[6]

Maldives: Composition of External Debt, 2022

	US$ million	Percent of total PPG debt	Percent of PPG external debt
Direct External debt	2,175	31.6	70.8
Multilateral	447	6.5	14.6
Bilateral	1,028	14.9	33.5
o/w China	588	8.5	19.1
Commercial	700	10.2	22.8
Guaranteed External debt	897	13.0	29.2
Multilateral	38	0.5	1.2
Bilateral	277	4.0	9.0
o/w China	169	2.5	5.5
Commercial	582	8.5	18.9
o/w China	534	7.9	17.8
Total	3,072	44.6	100.0

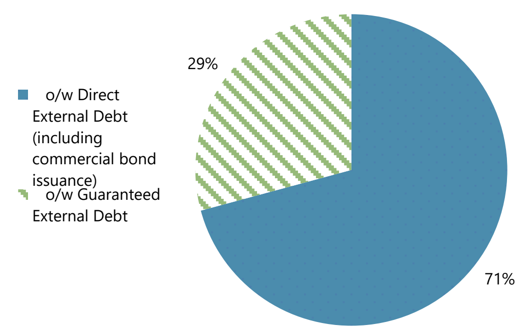
Sources: Maldives Ministry of Finance.

Maldives: External PPG Debt by Creditor Type, 2022
(In percent of total)



Source: Maldives Ministry of Finance.

Maldives: External PPG Debt, 2022
(In percent of total)



Source: Maldives Ministry of Finance

[5] The SBI bond is included in commercial bank claims on the central government.

[6] The Maldives used the swap arrangements with the Reserve Bank of India (RBI) in the amount of US$400 million in 2020. This was paid back in full in two tranches, an early payment of US$150 in January 2021 and remaining US$250 at end end-December 2021. The Maldives and RBI subsequently entered a swap arrangement in the amount of US$100 mil in (Dec) 2022, which was paid back in full in 2023. The swap arrangement with the RBI was for the purpose of reserve management and there is no indication of it is being used for fiscal purposes. Thus, the swap with RBI was excluded from external public debt.

4. The DSA includes PPG external and domestic debt. Public debt includes the debt of central government as well as guarantees to SOEs (Text Table 1). The stock of externally guaranteed SOE debt stood at around US$789 million (around 13 percent of GDP) with large exposures to the HDC and mainly from Chinese creditors (see ¶13). External debt is defined by residency criteria. The calibration of the contingent liability shock is based on the default values for SOE debt (2 percent of GDP) and financial market component (5 percent of GDP) since they are sufficient to represent fiscal risks.

Text Table 1. Maldives: Debt Coverage

Public debt coverage

	Subsectors of the public sector	Check box
1	Central government	X
2	State and local government	
3	Other elements in the general government	
4	o/w: Social security fund	
5	o/w: Extra budgetary funds (EBFs)	
6	Guarantees (to other entities in the public and private sector, including to SOEs)	X
7	Central bank (borrowed on behalf of the government)	X
8	Non-guaranteed SOE debt	

Public debt coverage and the magnitude of the contingent liability tailored stress test

1	The country's coverage of public debt	The central government, central bank, government-guaranteed debt	
		Default	Used for the analysis
2	Other elements of the general government not captured in 1.	0 percent of GDP	0.0
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	2.0
4	PPP	35 percent of PPP stock	3.3
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5 percent of GDP	5.0
	Total (2+3+4+5) (in percent of GDP)		10.3

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

MACROECONOMIC AND FINANCING ASSUMPTIONS

5. The macroeconomic assumptions underlying this DSA are as the following (Text Table 2):

- **Growth.** Economic activity continued to rebound in 2022, despite headwinds from Russia's invasion of Ukraine. Real GDP grew by 13.9 percent in 2022, benefiting from broad-based inflows of tourist arrivals. The resilience in the tourism sector and associated spillovers to other sectors are expected to support real GDP growth to 4.4 percent in 2023 and 5.2 percent in 2024. Medium-term growth outlook is expected to remain positive, with growth converging to around 4.5 percent. The expansions of the Velana International Airport terminal and hotel accommodation capacities are expected to boost potential growth, due to larger capacity to support tourism activity. Nevertheless, medium-term growth is expected to be weighed down by China's structural deceleration, which may materialize as smaller share of Chinese tourist arrivals in the medium term. Complementary structural reforms, including plans for financial market deepening and to enhance skills in the tourism and hospitality sector, are expected to improve labor productivity.

- **Inflation**. Despite the tourism and domestic goods and services tax (TGST and GST respectively) rate increases, headline inflation is expected to remain subdued in 2023, helped by the government's price subsidies. Nevertheless, inflation is projected to rise to 3.8 percent in 2024, as the authorities' subsidy reforms are expected to be implemented in July 2024. In the medium term, inflation is expected to stabilize at around 2 percent in line with an inflation target in the United States, given a currency peg to U.S. dollar.

- **Risks to the outlook** are tilted to the downside. Delayed fiscal consolidation and failure to reduce debt, including from potential social and political resistance, will add pressures on exchange rate and foreign exchange (FX) reserves, thus amplifying near-term liquidity and solvency risks. Any potential failure to reduce capital spending would result in larger-than-expected external financing gap and current account deficits, leading to further drains in FX reserves. Slow implementation of macro critical structural reforms to boost productivity, revenue and exports, or a large depreciation with rising debt servicing costs without matching increases in domestic revenues, diverting resources from growth friendly investment spending are other plausible risks. External downside risks are related to an economic slowdown in key source countries for tourists, volatile commodity prices, and tightening global financial conditions. Nevertheless, upside risks include the early completion of airport terminal expansion that would prepone a boost to growth. In addition, swift and decisive implementation of fiscal consolidation needed to bring debt back to a sustainable path will help restore macroeconomic stability, supporting sustained and stable economic growth over the medium term.

Text Table 2. Maldives: Macroeconomic Assumptions

	2022	2023	2024	2025	2026	2027	2028	Avg.2029-40
		Est.			Proj.			
Real GDP growth (in percent change)								
Current	13.9	4.4	5.2	6.5	5.0	4.8	4.5	4.5
Previous	10.5	6.6	5.7	6.5	5.9	5.5	5.1	4.9
Inflation (in percent change)								
Current	2.6	2.6	3.8	3.0	2.0	2.0	2.0	2.0
Previous	3.9	4.9	2.4	2.0	2.0	2.0	2.0	2.0
Primary fiscal deficit (in percent of GDP)								
Current	7.4	9.6	7.6	4.9	2.9	1.5	1.0	0.2
Previous	11.0	6.2	6.1	2.3	1.3	1.0	0.3	0.5
Non-interest current account deficit (in percent of GDP)								
Current	15.1	20.1	17.1	11.8	11.2	8.4	8.1	7.1
Previous	15.4	13.3	12.0	12.1	8.5	8.2	6.5	6.7
Capital Expenditures (in percent of GDP)								
Current	11.6	13.6	10.4	8.8	6.9	5.9	5.3	4.2
Previous	13.2	8.9	9.2	6.5	5.6	5.3	4.5	4.4
Public Debt (in percent of GDP)								
Current	110.4	118.7	121.2	118.8	117.1	114.4	111.7	94.6
Previous	122.6	117.5	117.7	112.9	107.7	103.2	98.7	79.5

Source: IMF Staff Projections

- **Fiscal policy**. Amid increased fiscal spending, the primary fiscal deficit is projected to be higher than that of last DSA. The primary fiscal deficit is estimated to peak in 2023 and the authorities anticipate the deficit to remain high in 2024, due to sustained high infrastructure spending, subsidies and wage bills. While the primary fiscal deficit is expected to improve over the medium term, public debt is projected to remain elevated, with public debt-to-GDP ratio rising to 121.2 percent in 2024 and declining marginally over the medium term. The government's ambitious public infrastructure investment agenda, executed mainly by SOEs, has been a key driver of debt vulnerabilities. Fiscal risks could also arise from materialization of contingent liabilities and capital contributions to SOEs, mainly to repay their debt contracted with sovereign guarantees, and inadequate targeting of social assistance, including in social housing programs. Meanwhile, the authorities made efforts to mobilize domestic revenues by increasing GST and TGST rates from 6 to 8 percent and from 12 to 16 percent, respectively in 2023. The medium-term fiscal strategy for 2024-2026 established four medium-term fiscal anchors, including (i) reducing public debt to less than 95 percent of GDP by 2026, (ii) reducing primary budget deficit to less than 5 percent of GDP by 2024, (iii) maintaining public and publicly guaranteed debt relative to GDP on a downward trend, and (iv) reducing recurrent expenditure to levels that do not exceed government revenue by 2024.

- **Current account dynamics.** The non-interest current account deficit (CAD) is expected to be persistently large, amid high import demands for food, fuel, and construction materials related to infrastructure development projects. Profit and workers' remittance outflows associated with FDI on tourism sectors would continue to put pressures on the current account balance. The CAD is expected to be gradually decreasing especially from 2025, due to the expected completion of larger infrastructure projects (e.g., the expansion of Velana International Airport terminals). Foreign exchange reserves are expected to remain low, while dropping to about 1.1 months of prospective imports in 2026 at the peak of external debt servicing.

- **Financing assumptions** (Text Table 3). The authorities in 2021 raised US$500 million Sukuk maturing in 2026 and rolled over US$100 million Eurobond maturing in 2026[7]. The authorities plan to access to concessional financing to mitigate roll-over of risk, with limiting expensive external financing in the near term. Around US$27 million of IDA disbursements in small economy terms is in the baseline between 2023 and 2029. The baseline assumes that around US$20 million, on average, of IDA financing per year until 2043 will generate marginal interest savings, subject to implementation of all annual Performance and Policy Actions (PPAs) under

[7] The Maldives issued two sovereign Eurobonds with a total face value of US$350 million: i) the first US$250 million maiden Eurobond (also known as Sunny side bond) issued to the international market, which was partly repurchased in March 2021, with the remainder repaid on maturity in June 2022; and ii) another US$100 million issued to Abu Dhabi in 2018, which was expected to fall due in 2023 and extended to 2026. In April 2021, the government issued a global Sukuk bond, due to mature in 2026, in the amount of US$200 million priced at 97.616 with a yield of 10.5 percent, that helped repurchase 77 percent of the US$250 million maiden Eurobond that was expected to mature in 2023. Subsequently, the Maldives issued another US$100 million Sukuk in April 2021 under the same conditions, and another US$200 million in September 2021 to cover budgetary expenses, trading at about 20 percent yield. In May 2022, the government also secured a US$100 million loan through private placement maturing in 2025 at a 7 percent annual interest rate.

the IDA's Sustainable Development Finance Policy (SDFP)[8]. The SDR allocation equivalent to US$29 million were added to reserves in 2021 and later used for budget support in 2022[9]. Going forward, the authorities do not plan for significant issuances from international financial markets prior to 2025. A budget financing gap (unidentified financing) of around 2.9 percent of GDP could open in 2024, and the DSA assumes that domestic financing is a mechanical gap filler. Nonetheless, risks to domestic financing remain high, given the discontinued exceptional use of MMA advances and the banking sector's sizeable sovereign exposures. The Sukuk issuance program was established for three-years with total value of US$1 billion. Moving ahead, the authorities plan to issue additional tranches/series when required and when market conditions become favorable[10]. The framework assumes: (i) a bond issuance of around US$250 million in 2026 maturing in 2031; (ii) repayment of around US$220 million with funds from projected airport development fees for 2024-2026 deposited in FX-nominated assets through Sovereign Development Fund (SDF) in 2026; and (iii) the remainder is set aside as unidentified financing. Nevertheless, the utilization of SDF involves risks such as the adequacy of SDF's FX accumulation and the availability of convertible foreign currencies to exchange Rufiyaa funds from SDF for external debt repayments; therefore, it is important to urgently strengthen the governance of SDF and ensure SDF's FX accumulation in liquid and redeemable FX assets. Meanwhile, a large share of domestic financing in the Maldives was short term (maturity of less than one year). Interest rates on short-term debt have ranged between 3.5 and 4.6 percent since December 2016. Over the medium term, the DSA assumes around 60 percent of domestic financing is short term with an interest rate of 4 percent and that the share of long-term debt gradually increases over time.

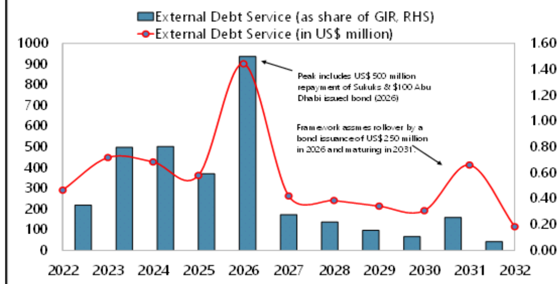
[8] The Maldives is classified as a small state IDA-only country, and currently assessed to be at a high risk of debt distress under the Bank-Fund Low-Income Country Debt Sustainability Framework (LIC DSF). In FY23, the Maldives breached its zero non-concessional borrowing (NCB) ceiling Performance and Policy Action (PPA) for the third consecutive year under the IDA's Sustainable Development Finance Policy (SDFP). Due to the repeated breaches of the NCB ceiling, IDA management has approved a hardening of terms for the Maldives to 100 percent credit in FY24. Previously, the breaches in FY21 and FY22 had resulted in a hardening of terms from 100 percent grant to 50/50 grant/credit for FY23. As a small island economy, the country remains eligible to receive IDA credit on IDA small economy terms in FY24. To improve debt management and fiscal sustainability, Maldives will be required to implement four PPAs in FY24: (i) approval of the Medium-Term Revenue Strategy, (ii) revision in the Fiscal Responsibility Act, (iii) approval of the Public Debt Management Bill and (iv) zero limit for non-concessional borrowing.

[9] The new SDR allocation was transferred in 2022 to the Ministry of Finance together with the associated liability and therefore recorded as external debt.

[10] The first tranche of US$200 million was issued on April 8, 2021, with a tap on the same series on April 30, of US$ 100 million, and another US$200 million later in September 2021, leaving another US$500 million to access, of which a total of US$250 million is assumed to be used in the baseline for rollover. This issuance of 5 years is priced at 97.616 with a coupon of 9.875 percent with a yield of 10.5 percent at issuance. The US$ sukuk currently trades at a yield of around 18-19 percent, suggesting global bond market access would not be affordable.

Text Table 3. Key Financing Assumptions in the Medium Term

Maldives: External Debt Services
(In mil US dollars (RHS) and share of Gross International Reserves (GIR) (LHS))



Source: IMF Staff Estimates.

- A bond issuance of around US$250 million in 2026, maturing in 2031 with interest rate at around 10 percent.
- Use of around US$220 million from Sovereign Development Fund (SDF), through the FX accumulation of projected airport development fees during 2024-2026, for debt repayments in 2026.
- Around 12 percent of external financing is assumed from unidentified financing in 2026.
- Domestic financing projected at about ¾ of total financing in 2026, then gradually increasing over the medium term.
- Around 60 percent of domestic financing is short term, with an interest rate of 4 percent.
- The share of long-term debt gradually increases over time.

Source: IMF Staff.

6. **Drivers of debt dynamics is expected to remain broadly unchanged from the previous DSA** (Figure 3). Debt dynamics in the Maldives will be driven mainly by real GDP growth, primary fiscal deficits, and nominal interest rates. In the past, the current account deficits and the primary fiscal deficits have been the main contributors to the accumulation of external[11] and domestic debt, respectively. Over the next five years, real GDP growth will be the dominating driver, countering the expansion of nominal external interest costs. Domestic debt dynamics over the next five years are balanced by growth and primary fiscal deficits, leading to a moderate decline in projected debt-to-GDP ratios. Gross financing needs continue to breach their indicative benchmark, reflecting higher borrowing needs arising from both exogeneous shocks and domestic spending push (Figure 5).

7. **Realism tools suggest that macroeconomic projections are broadly consistent with historical patterns.** The gradual improvement in the primary balance-to-GDP ratio is driven by a return to more moderate levels of capital spending and a recovery in GDP but at a more gradual and realistic pace of adjustment than in the previous DSA. Given large volatility in growth rates, driven by changes in tourism, the multiplier approach would not be suitable for calculating alternative growth paths. The baseline fiscal adjustment is at the 73rd percentile of LIC programs. The contribution of government capital expenditure to growth is expected to remain close to that in the previous DSA. While the government plans to continue with several large infrastructure projects[12], the disbursement is expected to be slow to avoid sudden stops and disruptions.

[11] Residuals to changes in total external debt would be largely attributed to movements in private sector, primarily tourism resorts, on their debt-creating inflows and outflows.

[12] The Government of Maldives signed lines of credit for more than US$1.2 billion with EXIM Bank India. The largest, for US$800 million and US$400 million, were signed in March 2019 and October 2020 respectively to finance several infrastructure projects (e.g., the development of the Gulhifalhu Port and relocation of Male Commercial Harbour, the Greater Male' Connectivity Project, construction of social housing units, and water and sanitation projects).

COUNTRY CLASSIFICATION AND DETERMINATION OF SCENARIO STRESS TEST

8. **The debt carrying capacity of the Maldives remains weak** (Text Table 4). The composite indicator (CI) score is 2.40 (less than the 2.69 threshold) using the Oct 2023 WEO and the 2023 World Bank Country Policy and Institutional Assessment (CPIA). The CI is based on a weighted average of several factors such as the country's real GDP growth, remittances, international reserves, world growth, and the CPIA score. The calculation of the CI is based on 10-year averages of the variables, across five years of historical data and five years of projections, and the corresponding CPIA.

9. **Tailored stress tests for natural disasters, contingent liabilities, and market financing are relevant for the Maldives.** Given that the Maldives is susceptible to rising sea levels, flood, and natural disasters, the natural disaster stress test and relevant default parameters are applied, as in the last DSA. Rising global interest rates are expected to have material impacts on budgetary external debt, where almost all outstanding external guaranteed SOE debt (around US$720 million) are loans with adjustable interest rates linked to the Secured Overnight Financing Rate (SOFR)[13]. Risks from the non-guaranteed SOE debt are covered by the contingent liability shock. The tailored stress tests were kept to their default calibrations as these are appropriate for the Maldives. The tailored stress tests are not the most extreme shocks for any of the debt indicators. The most extreme shocks are the shock to exports for the PPG external debt indicators, and the shock to growth for the public debt indicators and external debt service to revenue indicator.

Text Table 4. Maldives: Country Classification

Debt Carrying Capacity	Weak

Final	Classification based on current vintage	Classification based on the previous vintage	Classification based on the two previous vintage
Weak	Weak 2.40	Weak 2.38	Weak 2.35

Applicable thresholds

APPLICABLE	
EXTERNAL debt burden thresholds	
PV of debt in % of	
Exports	140
GDP	30
Debt service in % of	
Exports	10
Revenue	14

APPLICABLE	
TOTAL public debt benchmark	
PV of total public debt in percent of GDP	35

[13] "About 83 percent of the existing debt is based on fixed interest rate instruments," page 13, Debt Bulletin, Issue 10, December 2022, Debt Management Department, Ministry of Finance.

EXTERNAL AND PUBLIC DEBT SUSTAINABILITY

10. Three external debt indicators breach their respective thresholds under the baseline scenario (Figure 1). Maldives remains at a high risk of external debt distress, even though strong growth in recent years helped improve external debt indicators since the last DSA. The PV of the PPG external debt-to-GDP ratio will remain above the threshold of 30 percent until 2030, after which it will converge and then fall below the threshold from 2031 onward. Meanwhile, the PV of the debt-to-exports ratio is expected to stay below its threshold in the baseline scenario as with the last DSA. Both liquidity indicators, the debt service-to-exports ratio and the debt service-to-revenue ratio, breach their thresholds under the baseline scenario due to elevated debt service obligations on existing external PPG debt as with the last DSA. Stress tests suggest that the Maldives' external debt is most vulnerable to shocks to exports. Compared to shocks to real growth, the fiscal balance, exchange rate depreciation, and external flows, the impact of an exports shock is the most severe—the PV of the external debt-to-GDP ratio increases sharply, from around 45 percent of GDP in 2023 to around 146 percent of GDP in 2025. The ratio gradually falls over the medium term but continues to breach the threshold. The shocks to exports also lead to protracted breach of thresholds for PV of debt-to-exports ratio and debt service-to-exports ratio (Figure 1).

11. Overall public debt indicators suggest a high overall risk of debt distress (Figure 2). Under the baseline, the total PPG debt-to-GDP ratio declined to around 110 percent in 2022 on the back of higher tourism led-GDP. On the back of continued expansionary fiscal policy stance, the ratio is projected to increase to around 121 percent of GDP in 2024, before gradually decline to around 112 percent of GDP by 2028. The Maldives breaches this threshold for the entire projection periods and remains at a high risk of overall debt distress. The stress tests indicate that PPG debt is vulnerable to shocks to growth. Under the growth shock scenario, all of the three ratios (PV of Debt-to-GDP ratio, PV of Debt-to-Revenue ratio and Debt Service-to-Revenue Ratio) will continue to rise over the course of medium term with the PV of debt-to-GDP ratio protracted breach of the indicative threshold of 35 percent.

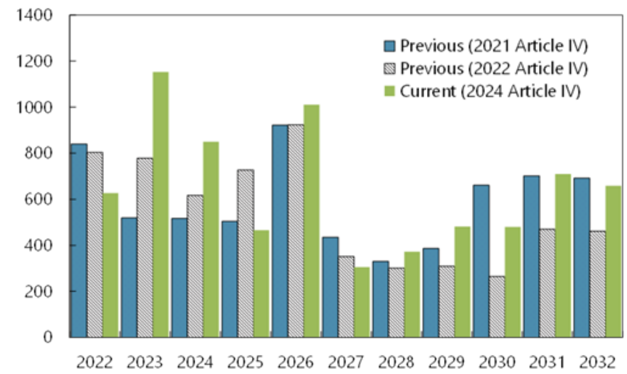
12. Restoring debt sustainability requires sustained fiscal consolidation, continued strong growth, and seeking additional concessional financing that would substitute for other expensive financing. Fiscal consolidation should include rationalizing capital spending, especially in large public investment projects carried out by the central government or SOEs, and improving the targeting of social assistance, including in social housing programs. It should also comprise streamlining current expenditures—both rationalizing subsidies and holding back wage increases—and further domestic revenue mobilization. In addition to the increase of GST rates in 2023, a sustained fiscal consolidation of around 2-3 percent of GDP annually during 2024-29, would help to lower the public debt to GDP ratio around 90 percent of GDP by 2030 and increase the probability of bringing the debt back on a sustainable path (Text Figure 1). To alleviate FX shortages and debt servicing requirements, seeking additional concessional financing could be considered, in addition to the MMA's potential FX swap arrangements. The authorities' FX reform initiatives (e.g., strengthen regulations of money changers, encourage the use of Rufiyaa in domestic transactions) should also be accelerated.

VULNERABILITY ASSESSMENT

13. The Maldives remains at a high risk of external and overall debt distress. Since the previous DSA, some debt indicators, such as debt-to-GDP ratio, have slightly improved in 2022, reflecting robust economic recovery. Nevertheless, external and fiscal positions from 2023 onward are expected to weaken relative to the previous DSA, due to higher fiscal spending pressures arising from expanded medium-term public investment programs. Gross external financing needs are projected to increase further from that of previous DSA, due to more expansionary fiscal policy stance reflecting increased capital project related spending, subsidies, and recurrent expenditures, as well as repayments and rollovers of non-concessional debt, mainly global sukuk. External refinancing pressures are expected to peak in 2026 with higher amortizations and large interest payments, triggering protracted breaches in several debt indicators, similar to the previous DSA. The debt dynamics will remain vulnerable to adverse shocks in growth, interest rates, and fiscal position in the near term. The PV of external debt-to-GDP, will converge to the 30 percent threshold and then fall below the threshold in the medium-term. As with previous DSA, debt is assessed as unsustainable under the authorities' current policies, given sustained threshold breaches of several debt indicators and significant rollover risk from external refinancing requirements in the coming years.

Gross External Financing Needs

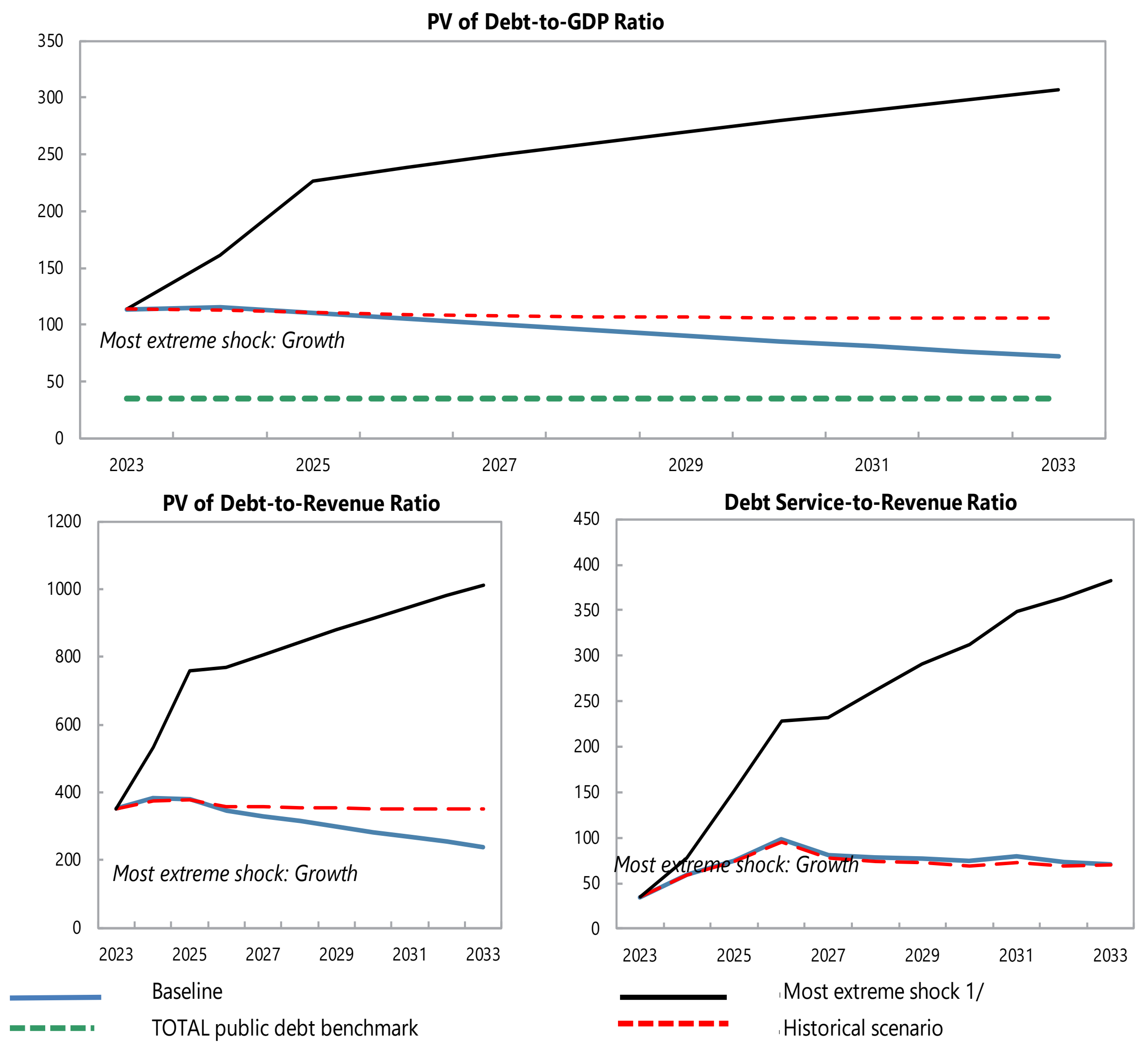
(In millions of USD)



Sources: IMF staff calculations

Text Figure 1. Maldives: Indicators of Public and Publicly Guaranteed Debt under Fiscal Consolidation Scenario, 2023–2033 1/

(In percent, unless otherwise mentioned)



Sources: Country authorities; and staff estimates and projections.

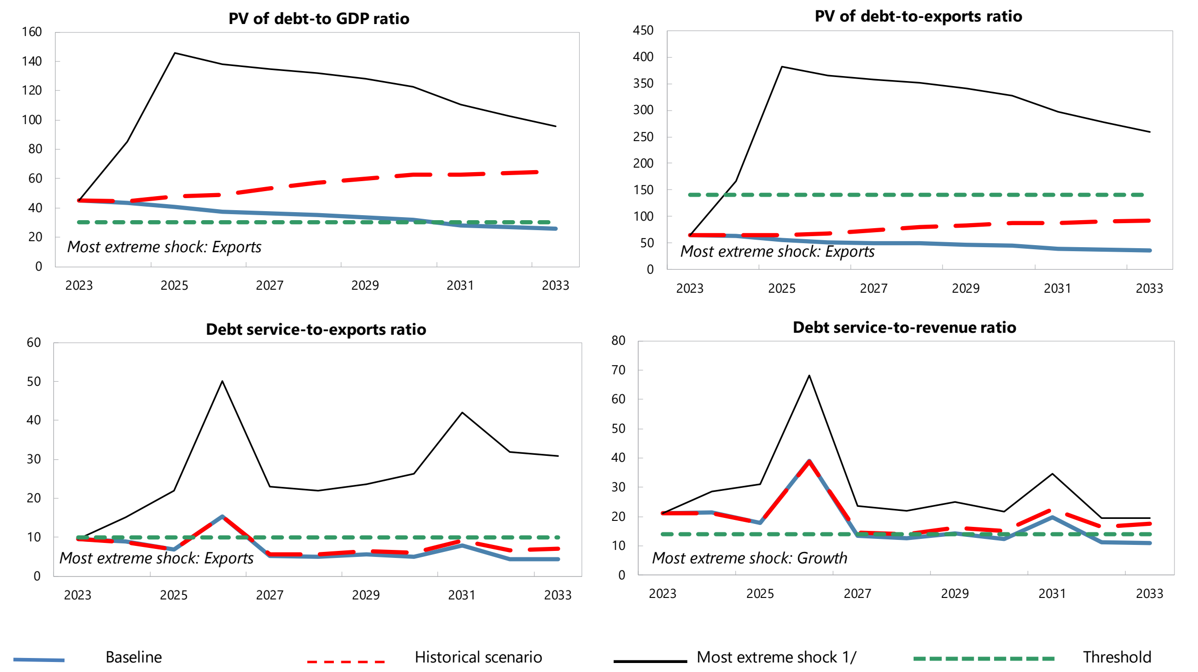
AUTHORITIES' VIEWS

14. **The authorities agreed that, without significant policy changes, the risk of external debt distress and overall risk of debt distress remains high.** The authorities are committed to a fiscal consolidation path that will bring debt-to-GDP ratio to a downward trend. In this regard, the authorities are taking a welcome step to develop an ambitious and homegrown fiscal reform agenda, including subsidy reforms that phase out existing subsidies and replace them with targeted direct income transfers, *Aasandha*—healthcare reform, reprioritization and rationalization of public sector investment program (PSIP), and SOE reforms, and committed to urgently implement this. The authorities highlighted the Sovereign Development Fund (SDF), established in 2017 to set aside funds for future debt repayment

obligations, has accumulated at around US$500 million at end-2023, of which US$115 million in foreign currencies. With the expected increase in the tourist arrivals and the expansion of the Male International Airport, the SDF size will continue to grow in the coming years in foreign currencies. The authorities underscored that the SDF will be further strengthened, as the new SDF law to be enacted this year will further clarify its legal status and improve governance. The authorities have been working to draft the Public Debt Management Law to strengthen debt management process with, for instance, ensuring transparency (e.g., debt reporting). The authorities also underscored that the medium-term debt strategy would be further articulated under the upcoming debt management law. The authorities will explore a new FX swap agreement under the South Asian Association for Regional Cooperation (SAARC) framework, should the need arise. The authorities are also working to establish FX swap arrangements with bilateral partners.

Figure 1. Maldives: Indicators of Public and Publicly Guaranteed External Debt, 2023-2033 1/2/

(In percent, unless otherwise indicated)



Customization of Default Settings	Size	Interactions
Tailored Stress		
Combined CL	No	
Natural disaster	No	No
Commodity price	n.a.	n.a.
Market financing	No	No

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

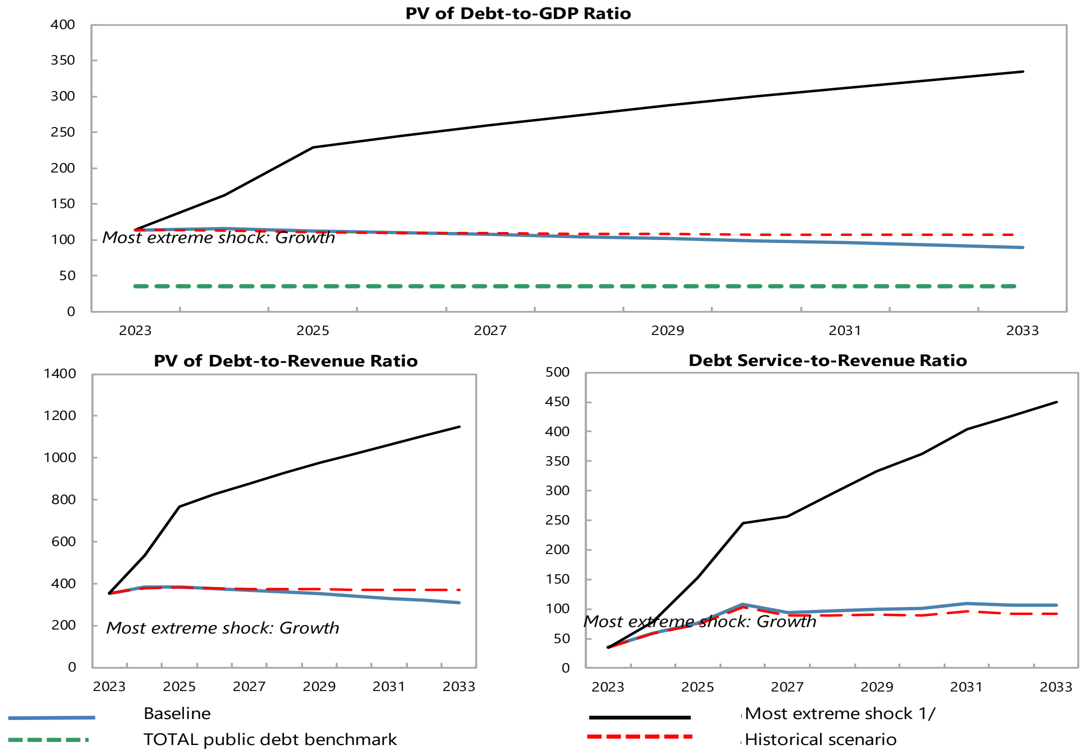
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	3.7%	3.7%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	19	19
Avg. grace period	5	5

* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in or before 2033. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.
2/ The magnitude of shocks used for the commodity price shock stress test are based on the commodity prices outlook prepared by the IMF research department.

Figure 2. Maldives: Indicators of Public Debt, 2023-2033 1/

(In percent, unless otherwise indicated)



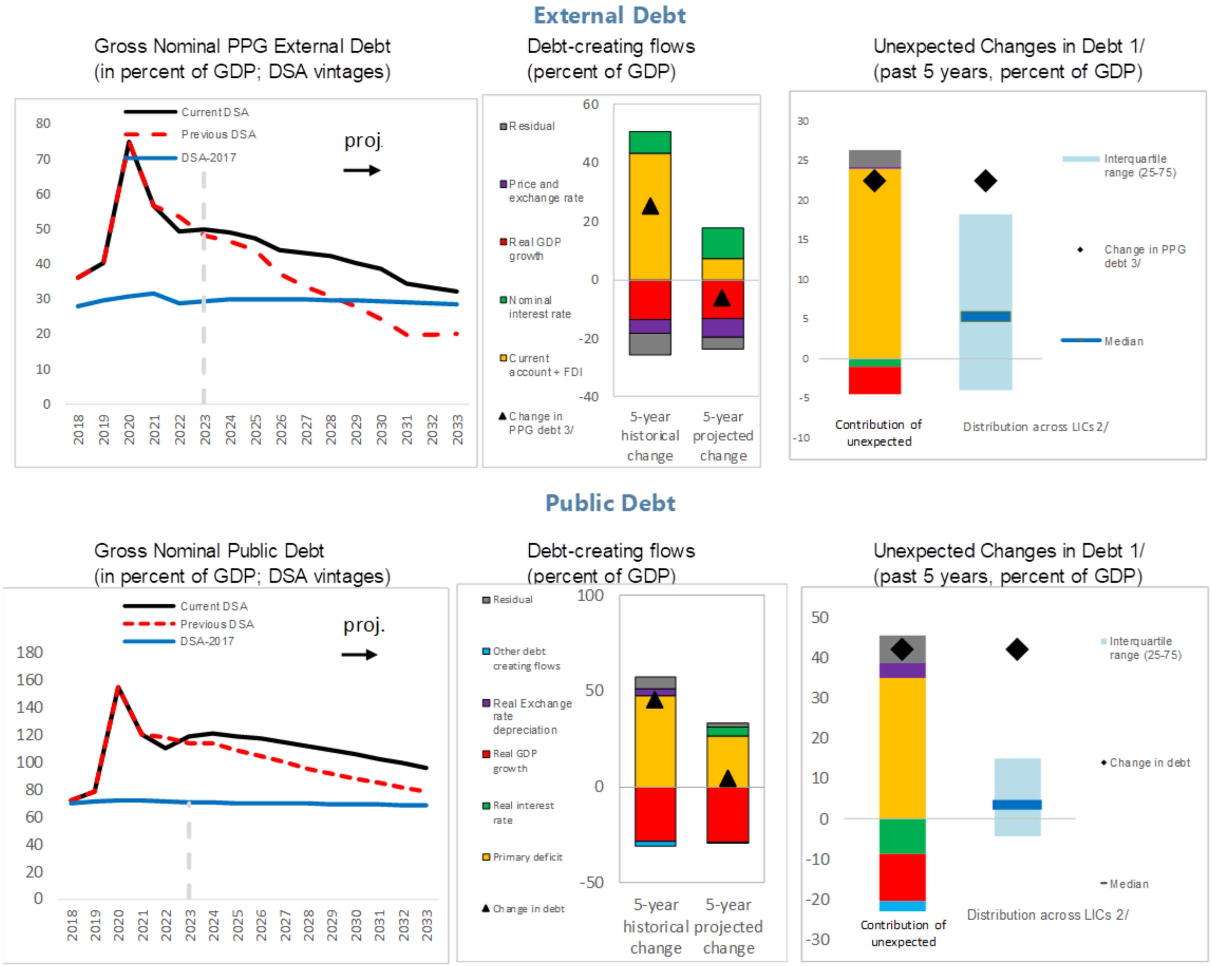
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	17%	12%
Domestic medium and long-term	33%	31%
Domestic short-term	50%	57%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	3.7%	3.7%
Avg. maturity (incl. grace period)	19	19
Avg. grace period	5	5
Domestic MLT debt		
Avg. real interest rate on new borrowing	3.0%	2.5%
Avg. maturity (incl. grace period)	2	3
Avg. grace period	1	1
Domestic short-term debt		
Avg. real interest rate	2.4%	1.5%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2033. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 3. Maldives: Drivers of Debt Dynamics—Baseline Scenario



1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

Figure 4. Maldives: Realism Tools—Baseline Scenario

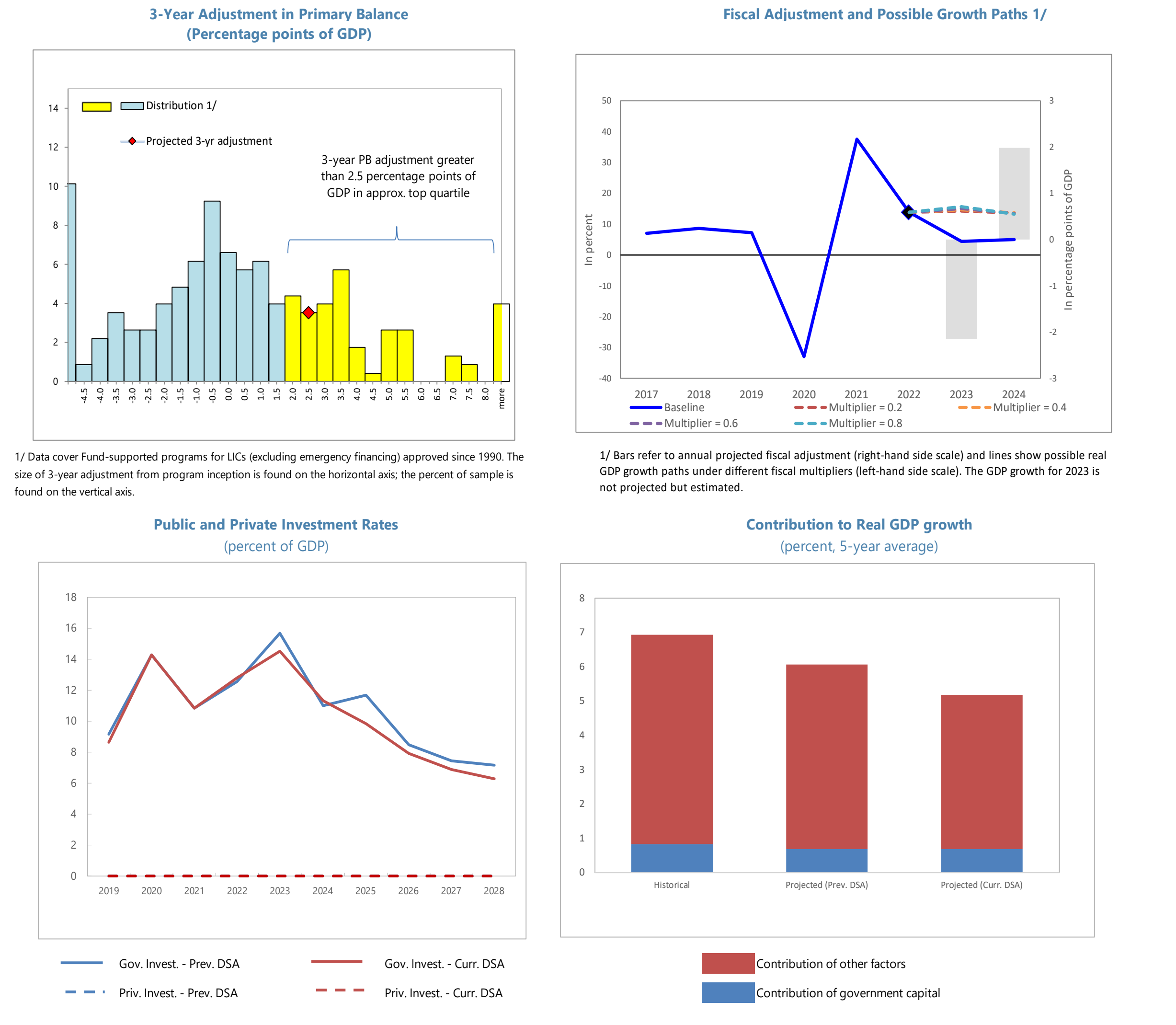
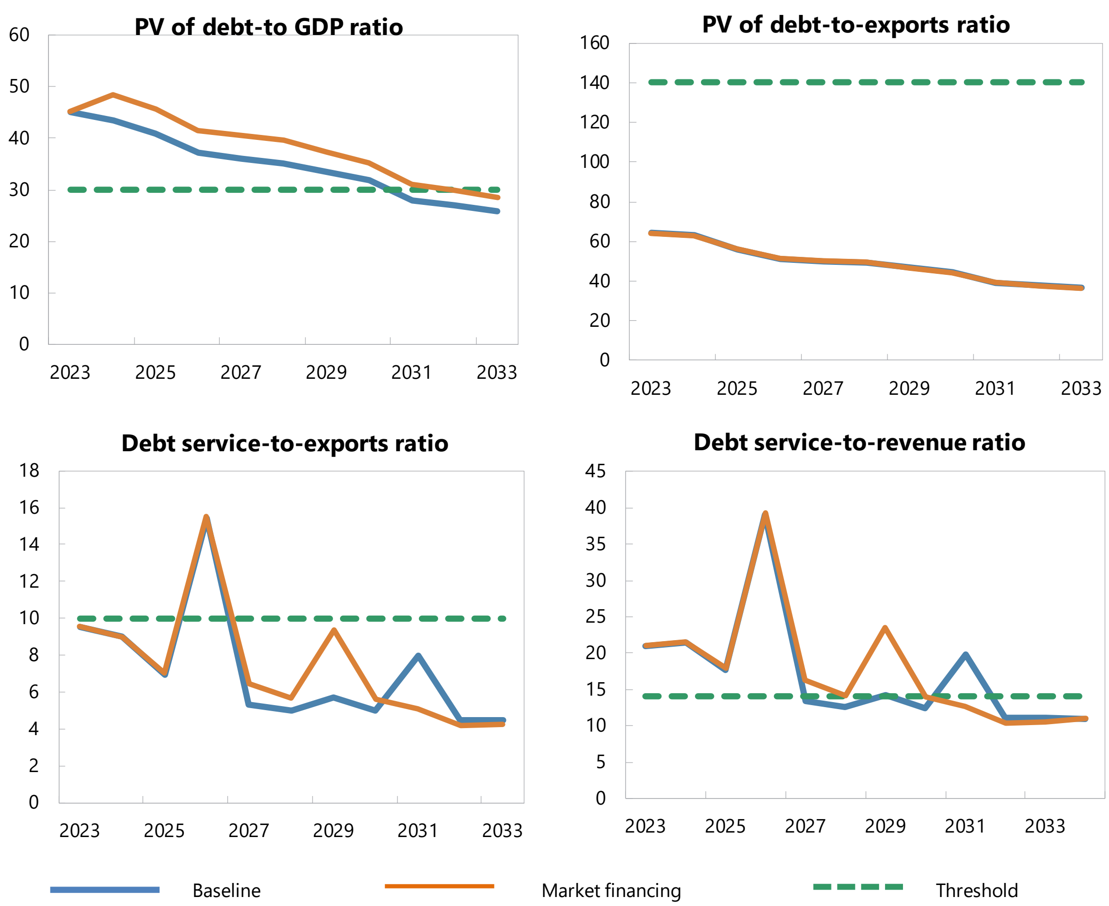


Figure 5. Maldives: Market-Financing Risk Indicators—Baseline Scenario

	GFN	1/	EMBI	2/
Benchmarks	14		570	
Values	27		n.a.	
Breach of benchmark	Yes		n.a.	
Potential heightened liquidity needs	Moderate			

1/ Maximum gross financing needs (GFN) over 3-year baseline projection horizon.
2/ EMBI spreads correspond to the latest available data.



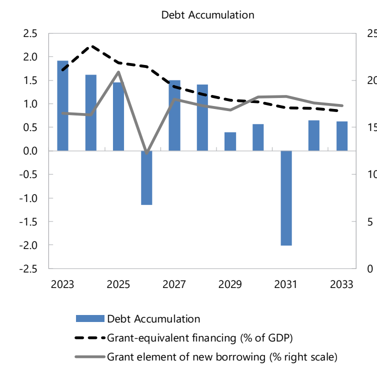
Sources: Country authorities; and staff estimates and projections.

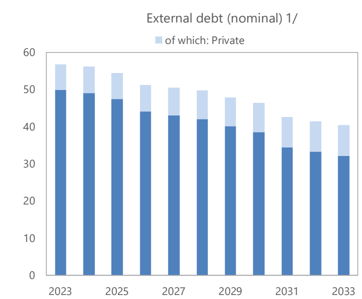
Table 1. Maldives: External Debt Sustainability Framework, Baseline Scenario, 2020–2043 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Est	Projection							Average 8/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2033	2043	Historical	Projections
External debt (nominal) 1/	84.4	64.1	55.8	56.7	56.1	54.4	51.2	50.4	49.7	40.4	37.3	**42.3**	**48.8**
of which: public and publicly guaranteed (PPG)	74.8	56.5	49.2	49.8	49.0	47.3	44.0	43.0	42.1	32.1	26.8	**35.8**	**41.2**
Change in external debt	42.2	-20.3	-8.3	0.9	-0.6	-1.7	-3.2	-0.8	-0.8	-1.0	1.2		
Identified net debt-creating flows	43.9	-29.4	-4.3	9.0	3.1	-2.4	-2.2	-3.3	-2.5	-1.1	-0.9	**3.2**	**-0.6**
Non-interest current account deficit	31.8	6.5	15.1	20.1	17.1	11.8	11.2	8.4	8.1	7.5	7.4	**16.5**	**10.4**
Deficit in balance of goods and services	17.0	-9.3	-3.1	2.1	1.2	-4.5	-5.3	-6.0	-5.7	-8.2	-8.8	**-1.5**	**-4.9**
Exports	48.5	73.9	81.7	70.4	69.0	72.9	72.3	72.2	71.7	70.6	69.0		
Imports	65.5	64.6	78.5	72.5	70.2	68.4	66.9	66.2	66.0	62.4	60.2		
Net current transfers (negative = inflow)	9.6	7.8	7.8	8.3	7.8	8.3	8.5	6.4	5.7	7.7	7.9	**9.5**	**7.1**
of which: official	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other current account flows (negative = net inflow)	5.3	8.0	10.4	9.6	8.0	8.0	8.0	8.0	8.0	8.1	8.3	**8.4**	**8.2**
Net FDI (negative = inflow)	-11.8	-11.9	-11.7	-11.5	-13.5	-13.0	-12.5	-11.0	-10.0	-8.0	-7.5	**-11.1**	**-10.5**
Endogenous debt dynamics 2/	23.9	-24.0	-7.7	0.4	-0.5	-1.2	-0.9	-0.7	-0.5	-0.7	-0.8		
Contribution from nominal interest rate	2.9	1.9	1.0	2.7	2.3	2.1	1.7	1.6	1.6	1.1	0.8		
Contribution from real GDP growth	20.8	-22.0	-7.7	-2.3	-2.7	-3.3	-2.5	-2.3	-2.1	-1.8	-1.5		
Contribution from price and exchange rate changes	0.2	-3.8	-1.0	-1.4	-1.3	-1.6	-1.1	-1.0	-1.0	-0.8	-0.3		
Residual 3/	-1.7	9.1	-4.0	-6.7	-2.4	2.3	0.1	3.5	2.7	0.9	2.4	**-0.6**	**0.3**
of which: exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators													
PV of PPG external debt-to-GDP ratio	...	...	46.5	45.2	43.4	40.9	37.1	36.1	35.2	25.8	21.3		
PV of PPG external debt-to-exports ratio	...	...	56.9	64.2	63.0	56.1	51.4	50.1	49.1	36.6	30.8		
PPG debt service-to-exports ratio	17.4	7.9	5.7	9.5	9.0	7.0	15.4	5.3	5.0	4.5	3.3		
PPG debt service-to-revenue ratio	34.1	24.0	15.9	21.0	21.5	17.8	39.0	13.5	12.6	11.1	7.7		
Gross external financing need (Million of U.S. dollars)	1111.7	138.7	626.5	1152.2	849.8	465.4	1010.7	306.0	372.3	680.2	1207.3		
Key macroeconomic assumptions													
Real GDP growth (in percent)	-32.9	37.7	13.9	4.4	5.2	6.5	5.0	4.8	4.5	4.5	4.5	**6.7**	**4.8**
GDP deflator in US dollar terms (change in percent)	-0.5	4.7	1.6	2.6	2.4	3.0	2.0	2.0	2.0	2.0	1.0	**2.6**	**2.2**
Effective interest rate (percent) 4/	4.6	3.2	1.8	5.2	4.3	4.2	3.3	3.4	3.4	2.7	2.3	**2.4**	**3.5**
Growth of exports of G&S (US dollar terms, in percent)	-51.5	119.6	27.9	-7.7	5.5	15.9	6.2	6.7	5.9	6.2	6.4	**14.0**	**5.8**
Growth of imports of G&S (US dollar terms, in percent)	-40.1	42.2	40.7	-1.0	4.2	6.9	4.8	5.7	6.3	4.1	5.0	**11.2**	**4.9**
Grant element of new public sector borrowing (in percent)	...	...	...	16.5	16.3	20.9	12.3	18.0	17.3	17.3	15.5	**...**	**17.2**
Government revenues (excluding grants, in percent of GDP)	24.8	24.5	29.4	31.9	28.8	28.6	28.5	28.5	28.5	28.5	29.4	**26.1**	**28.9**
Aid flows (in Million of US dollars) 5/	62.2	67.0	66.5	129.5	176.4	172.7	171.3	137.4	127.6	125.2	153.4		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	1.7	2.2	1.9	1.8	1.4	1.2	0.8	0.6	**...**	**1.4**
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	20.8	28.6	30.0	18.0	28.9	28.2	25.4	18.6	**...**	**26.8**
Nominal GDP (Million of US dollars)	3,739	5,392	6,238	6,685	7,199	7,897	8,461	9,044	9,640	13,263	24,344		
Nominal dollar GDP growth	-33.2	44.2	15.7	7.2	7.7	9.7	7.1	6.9	6.6	6.6	5.5	**9.6**	**7.1**
Memorandum items:													
PV of external debt 7/	...	...	53.0	52.0	50.5	48.0	44.4	43.6	42.8	34.2	31.7		
In percent of exports	...	...	64.9	73.9	73.2	65.8	61.4	60.4	59.7	48.4	46.0		
Total external debt service-to-exports ratio	19.9	10.8	8.2	12.3	11.9	9.7	18.3	8.3	8.1	7.9	7.4		
PV of PPG external debt (in Million of US dollars)			2899.1	3018.8	3127.1	3231.7	3140.9	3267.6	3394.8	3423.5	5179.2		
(PVt-PVt-1)/GDPt-1 (in percent)				1.9	1.6	1.5	-1.2	1.5	1.4	0.6	1.3		
Non-interest current account deficit that stabilizes debt ratio	-10.4	26.8	23.4	19.2	17.7	13.5	14.4	9.2	8.9	8.6	6.2		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**Yes**





Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g) + Εα (1+r)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, ρ = growth rate of GDP deflator in U.S. dollar terms, Ε=nominal appreciation of the local currency, and α= share of local currency-denominated external debt in total external debt.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Current-year interest payments divided by previous period debt stock.

5/ Defined as grants, concessional loans, and debt relief.

6/ 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).

7/ Assumes that PV of private sector debt is equivalent to its face value.

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

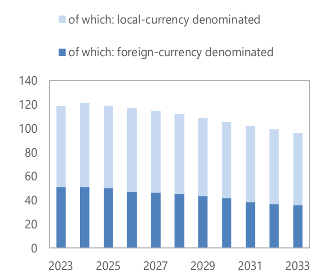
Table 2. Maldives: Public Sector Debt Sustainability Framework, Baseline Scenario, 2020–2043

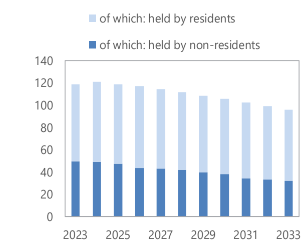
(In percent of GDP, unless otherwise indicated)

	Actual			Est	Projection							Average 6/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2033	2043	Historical	Est
Public sector debt 1/	**154.2**	**119.9**	**110.4**	**118.7**	**121.2**	**118.8**	**117.1**	**114.4**	**111.7**	**96.0**	**78.2**	**82.9**	**110.3**
of which: external debt	**74.8**	**56.5**	**49.2**	**49.8**	**49.0**	**47.3**	**44.0**	**43.0**	**42.1**	**32.1**	**26.8**	**35.8**	**41.2**
Change in public sector debt	75.5	-34.3	-9.6	8.3	2.5	-2.3	-1.8	-2.7	-2.7	-3.0	-0.7		
Identified debt-creating flows	**...**	**-31.4**	**-6.7**	**5.5**	**2.7**	**-1.7**	**-1.6**	**-2.5**	**-2.6**	**-3.0**	**-0.5**	**-4.3**	**-1.4**
Primary deficit	**20.7**	**11.2**	**7.4**	**9.6**	**7.6**	**4.9**	**2.9**	**1.5**	**1.0**	**0.1**	**0.3**	**6.4**	**2.6**
Revenue and grants	26.4	25.7	30.5	32.3	30.0	29.3	29.2	29.2	29.1	28.9	29.5	**27.0**	**29.4**
of which: grants	1.7	1.2	1.1	0.4	1.2	0.7	0.7	0.6	0.6	0.3	0.1		
Primary (noninterest) expenditure	47.1	36.9	37.9	41.9	37.6	34.2	32.1	30.7	30.1	29.0	29.9	**33.4**	**32.0**
Automatic debt dynamics	**...**	**-42.7**	**-14.2**	**-4.1**	**-4.9**	**-6.6**	**-4.5**	**-4.0**	**-3.6**	**-3.1**	**-0.8**		
Contribution from interest rate/growth differential	...	-42.4	-16.7	-4.1	-4.9	-6.6	-4.5	-4.0	-3.6	-3.1	-0.8		
of which: contribution from average real interest rate	...	-0.2	-2.1	0.6	0.9	0.8	1.1	1.3	1.3	1.2	2.6		
of which: contribution from real GDP growth	38.6	-42.2	-14.6	-4.7	-5.8	-7.4	-5.7	-5.4	-4.9	-4.3	-3.4		
Contribution from real exchange rate depreciation	...	-0.3	2.6	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	**-3.4**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**-0.2**	**0.0**
Privatization receipts (negative)	-3.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (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		
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 debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	**...**	**-2.9**	**-2.8**	**2.8**	**-0.2**	**-0.6**	**-0.2**	**-0.1**	**-0.1**	**0.0**	**-0.2**	**1.7**	**0.1**
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	**...**	**...**	**107.6**	**114.0**	**115.5**	**112.4**	**110.2**	**107.5**	**104.8**	**89.8**	**72.7**		
PV of public debt-to-revenue and grants ratio	**...**	**...**	**353.0**	**352.5**	**385.7**	**384.1**	**377.4**	**368.6**	**360.3**	**310.9**	**246.1**		
Debt service-to-revenue and grants ratio 3/	**48.7**	**146.1**	**26.0**	**34.8**	**59.8**	**75.7**	**107.5**	**93.9**	**96.3**	**106.4**	**46.4**		
Gross financing need 4/	30.2	48.8	15.4	20.9	25.5	27.1	34.3	28.9	29.0	30.8	14.0		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	-32.9	37.7	13.9	4.4	5.2	6.5	5.0	4.8	4.5	4.5	4.5	**6.7**	**4.8**
Average nominal interest rate on external debt (in percent)	4.8	3.7	2.1	5.9	4.9	4.8	3.8	4.0	3.9	3.4	3.1	**2.9**	**4.1**
Average real interest rate on domestic debt (in percent)	2.0	0.2	0.4	-1.0	-0.7	-0.9	0.4	0.6	0.7	1.2	3.7	**0.5**	**0.4**
Real exchange rate depreciation (in percent, + indicates depreciation)	...	-0.6	5.5	...	...	...	...	...	...	...	...	**-0.3**	**...**
Inflation rate (GDP deflator, in percent)	-0.5	4.7	1.6	2.6	2.4	3.0	2.0	2.0	2.0	2.0	1.0	**2.6**	**2.2**
Growth of real primary spending (deflated by GDP deflator, in percent)	-0.7	8.0	16.9	15.5	-5.8	-3.0	-1.4	0.1	2.5	4.5	5.6	**9.4**	**2.4**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	-54.8	45.6	17.0	1.3	5.1	7.2	4.7	4.2	3.7	3.1	1.0	**2.6**	**3.9**
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**Yes**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The central government, central bank, government-guaranteed debt . Definition of external debt is Residency-based.

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.

4/ 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 and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Table 3. Maldives: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2023–2033

(In percent)

	Projections 1/										
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
PV of debt-to GDP ratio											
Baseline	**45**	**43**	**41**	**37**	**36**	**35**	**33**	**32**	28	27	26
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**45**	**44**	**48**	**49**	**53**	**57**	**60**	**62**	**63**	**64**	**65**
B. Bound Tests											
B1. Real GDP growth	**45**	**58**	**72**	**65**	**63**	**62**	**58**	**56**	**49**	**47**	**45**
B2. Primary balance	**45**	**44**	**43**	**40**	**39**	**39**	**37**	**36**	**32**	**31**	**30**
B3. Exports	**45**	**85**	**146**	**138**	**135**	**132**	**128**	**122**	**111**	**103**	**96**
B4. Other flows 3/	**45**	**51**	**55**	**51**	**49**	**48**	**46**	**44**	**39**	**37**	**35**
B5. Depreciation	**45**	**55**	**50**	**45**	**44**	**43**	**41**	**39**	**34**	**33**	**31**
B6. Combination of B1-B5	**45**	**74**	**85**	**79**	**78**	**76**	**73**	**69**	**62**	**58**	**55**
C. Tailored Tests											
C1. Combined contingent liabilities	**45**	**45**	**43**	**39**	**39**	**38**	**36**	**35**	**32**	**31**	30
C2. Natural disaster	**45**	**45**	**43**	**40**	**39**	**39**	**37**	**36**	**33**	**32**	**31**
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	**45**	**48**	**46**	**42**	**41**	**40**	**37**	**35**	**31**	30	29
Threshold	30	30	30	30	30	30	30	30	30	30	30
PV of debt-to-exports ratio											
Baseline	64	63	56	51	50	49	47	45	39	38	37
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	64	64	65	67	74	80	84	87	88	90	92
B. Bound Tests											
B1. Real GDP growth	64	63	56	51	50	49	47	45	39	38	37
B2. Primary balance	64	64	59	55	54	54	52	50	45	44	43
B3. Exports	64	**166**	**382**	**365**	**357**	**352**	**341**	**327**	**297**	**278**	**259**
B4. Other flows 3/	64	74	75	70	69	67	65	62	55	52	50
B5. Depreciation	64	63	55	50	48	48	45	43	38	37	35
B6. Combination of B1-B5	64	111	85	123	120	118	114	108	97	92	87
C. Tailored Tests											
C1. Combined contingent liabilities	64	65	58	54	53	53	51	49	44	43	42
C2. Natural disaster	64	67	60	56	56	55	53	52	47	46	45
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	64	63	56	52	50	50	47	44	39	38	36
Threshold	140	140	140	140	140	140	140	140	140	140	140
Debt service-to-exports ratio											
Baseline	10	9	7	**15**	5	5	6	5	8	4	4
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	10	9	7	**15**	6	6	6	6	9	7	7
B. Bound Tests											
B1. Real GDP growth	10	9	7	**15**	5	5	6	5	8	4	4
B2. Primary balance	10	9	7	**16**	6	5	6	5	8	5	5
B3. Exports	10	**15**	**22**	**50**	**23**	**22**	**24**	**26**	**42**	**32**	**31**
B4. Other flows 3/	10	9	7	**16**	6	6	6	6	10	6	6
B5. Depreciation	10	9	7	**15**	5	5	6	5	8	4	4
B6. Combination of B1-B5	10	**11**	**12**	**26**	**10**	9	**10**	**11**	**16**	**11**	**11**
C. Tailored Tests											
C1. Combined contingent liabilities	10	9	7	**16**	5	5	6	5	8	5	5
C2. Natural disaster	10	9	7	**16**	6	5	6	5	8	5	5
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	10	9	7	**16**	6	6	9	6	5	4	4
Threshold	10	10	10	10	10	10	10	10	10	10	10
Debt service-to-revenue ratio											
Baseline	**21**	**22**	**18**	**39**	13	13	**14**	12	**20**	11	11
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**21**	**21**	**18**	**39**	**14**	**14**	**16**	**15**	**23**	**16**	**18**
B. Bound Tests											
B1. Real GDP growth	**21**	**28**	**31**	**68**	**24**	**22**	**25**	**22**	**35**	**19**	**19**
B2. Primary balance	**21**	**22**	**18**	**39**	14	13	**15**	13	**21**	12	12
B3. Exports	**21**	**27**	**29**	**66**	**31**	**29**	**31**	**35**	**55**	**41**	**40**
B4. Other flows 3/	**21**	**22**	**19**	**41**	**15**	**14**	**16**	**16**	**24**	**15**	**15**
B5. Depreciation	**21**	**27**	**22**	**49**	**17**	**16**	**18**	**15**	**25**	14	14
B6. Combination of B1-B5	**21**	**26**	**28**	**58**	**23**	**21**	**23**	**25**	**36**	**24**	**23**
C. Tailored Tests											
C1. Combined contingent liabilities	**21**	**22**	**18**	**39**	14	13	**15**	13	**20**	12	12
C2. Natural disaster	**21**	**22**	**18**	**39**	14	13	**15**	13	**20**	12	12
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	**21**	**22**	**18**	**39**	**16**	**14**	**23**	**14**	13	10	11
Threshold	14	14	14	14	14	14	14	14	14	14	14

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the threshold.
2/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Includes official and private transfers and FDI.

Table 4. Maldives: Sensitivity Analysis for Key Indicators for Public Debt, 2023–2033

(In percent)

	Projections 1/										
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
						PV of Debt-to-GDP Ratio					
Baseline	**114**	**116**	**112**	**110**	**108**	**105**	**102**	**99**	**96**	**93**	**90**
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**114**	**113**	**111**	**110**	**109**	**108**	**108**	**108**	**107**	**107**	**107**
B. Bound Tests											
B1. Real GDP growth	**114**	**162**	**229**	**245**	**260**	**274**	**287**	**300**	**312**	**323**	**335**
B2. Primary balance	**114**	**121**	**125**	**122**	**119**	**116**	**113**	**109**	**106**	**103**	**100**
B3. Exports	**114**	**140**	**176**	**172**	**168**	**165**	**160**	**155**	**147**	**140**	**133**
B4. Other flows 3/	**114**	**123**	**126**	**124**	**121**	**118**	**115**	**111**	**107**	**103**	**99**
B5. Depreciation	**114**	**122**	**115**	**110**	**105**	**101**	**96**	**91**	**86**	**82**	**77**
B6. Combination of B1-B5	**114**	**123**	**133**	**135**	**136**	**137**	**138**	**138**	**138**	**138**	**138**
C. Tailored Tests											
C1. Combined contingent liabilities	**114**	**126**	**122**	**119**	**116**	**113**	**110**	**107**	**104**	**100**	**97**
C2. Natural disaster	**114**	**127**	**124**	**122**	**119**	**117**	**114**	**111**	**108**	**105**	**102**
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	**114**	**116**	**112**	**110**	**108**	**105**	**102**	**99**	**96**	**93**	**90**
TOTAL public debt benchmark	35	35	35	35	35	35	35	35	35	35	35
						PV of Debt-to-Revenue Ratio					
Baseline	352	386	384	377	369	360	351	340	331	320	311
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	352	376	380	376	374	373	372	371	371	371	372
B. Bound Tests											
B1. Real GDP growth	352	535	768	825	876	927	974	1,018	1,064	1,107	1,150
B2. Primary balance	352	405	426	418	408	399	388	377	366	355	345
B3. Exports	352	468	602	591	577	565	552	534	508	484	460
B4. Other flows 3/	352	411	432	424	414	405	395	382	369	356	343
B5. Depreciation	352	407	395	379	362	347	331	314	298	283	267
B6. Combination of B1-B5	352	409	451	459	464	470	473	475	476	477	479
C. Tailored Tests											
C1. Combined contingent liabilities	352	420	417	409	399	390	379	368	358	347	337
C2. Natural disaster	352	425	424	417	409	401	391	381	372	362	353
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	352	386	384	378	370	361	351	340	330	320	310
						Debt Service-to-Revenue Ratio					
Baseline	35	60	76	107	94	96	100	101	110	107	106
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	35	59	75	104	89	89	91	90	96	92	91
B. Bound Tests											
B1. Real GDP growth	35	78	153	245	257	295	333	362	405	426	450
B2. Primary balance	35	60	88	130	115	116	118	118	125	122	121
B3. Exports	35	60	79	116	102	104	108	113	129	125	124
B4. Other flows 3/	35	60	77	109	96	98	102	104	114	111	110
B5. Depreciation	35	59	76	113	95	94	98	97	108	102	101
B6. Combination of B1-B5	35	62	89	125	119	129	142	150	166	168	173
C. Tailored Tests											
C1. Combined contingent liabilities	35	60	96	124	111	111	114	113	121	118	117
C2. Natural disaster	35	61	97	126	114	115	118	118	127	124	123
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	35	60	76	108	97	98	109	102	102	106	106

Sources: Country authorities; and staff estimates and projections.

1/ A bold value indicates a breach of the benchmark.

2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.

3/ Includes official and private transfers and FDI.

Statement by Mahmoud Mohieldin, Executive Director for Maldives
Ali Alhosani, Alternate Executive Director for Maldives
and Ali Abdul Raheem, Advisor to Executive Director
March 20, 2024

Introduction

On behalf of the Maldivian authorities, we would like to thank Ms. Sodsriwiboon and her team for a constructive and effective Article IV mission and candid policy discussions. The authorities look forward to continuing their close engagement with the Fund, and highly appreciate the IMF's valuable technical assistance.

Recent Economic Developments and Outlook

Maldives economy has recovered strongly from the COVID-19 pandemic and has shown resilience to subsequent shocks. In 2023, Maldives surpassed the pre-pandemic record for tourist arrivals, with 1.88 million visitors. The strong performance of the tourism sector has carried onto 2024, with 409,777 visitors in the first two months of the year, which is a 16.9 percent growth compared to the same period for 2023. The authorities are confident regarding the prospects for the tourism sector in 2024, with a target to reach 2 million tourist arrivals in the year. Authorities cautioned against a statics view of shifts in specific source markets; as the Maldives tourism sector has shown itself to be dynamic and highly adaptive to shifts in the source markets since the pandemic. The strong economic recovery has led to a faster normalization of growth, than previously estimated. Real GDP growth is estimated to have moderated to 4.4 percent in 2023, however with the anticipated growth in tourist arrivals for 2024, we expect growth to accelerate to 5.2 percent.

The authorities are prioritizing the completion of the Velana International Airport upgrade project which has the potential to significantly shift the production capacity of the economy. The main bottleneck facing the expansion of the tourism sector has indeed been the capacity constraints in the Velena International Airport, the main gateway into the Maldives. Fast tracking the much-delayed airport upgrading project is a major priority of the new administration. The government aims to open the new airport terminal in phases, with the goal of operationalizing the first phase in time for the 2024 tourism peak season, in the fourth quarter of the year. The full operationalization of the new terminal will alleviate the bottlenecks, allow more flights and passengers, and will help to raise the occupancy of the tourism properties. Authorities forecast that tourist arrivals will increase to 3-5 million per year with the completion of the project. With bed occupancy at 58 percent in 2023, and more beds in the pipeline, they note that the tourism sector has the capacity to absorb the additional arrivals. As per current projections, growth will accelerate to 6.5 percent in 2025 with the terminal opening and authorities are confident that this will support robust growth in the medium term.

Inflation has come down in recent months supported by falling food and energy prices and price subsidies. As an import dependent economy, global commodity price shocks in 2022 caused inflation to accelerate to 2.3 percent on average. Headline inflation rose further to 2.9 percent on average in 2023, partly due to the increase in the rates for the Goods and Services Tax. Inflation peaked in the first quarter of 2023 and has since been on a declining trend. The latest inflation figure for January 2024 shows further deceleration in inflation rate to 0.9 percent (y-o-y). The authorities acknowledge that the passthrough of global commodity prices to consumers have been contained by generous subsidies, particularly for energy, which has come at a large fiscal cost. With the proposed subsidy reforms the authorities expect inflation to accelerate to 3.8 percent in 2024.

The authorities concur with staff that strong real GDP growth and declining inflation provides substantial policy space to bring the necessary fiscal and monetary tightening.

Fiscal Policy and Reforms

The new administration is committed to implement an ambitious homegrown fiscal consolidation program. In his inaugural address to the Parliament on 5th February 2024, President Dr. Mohamed Muizzu laid out an ambitious home-grown program of fiscal consolidation, focusing on the long overdue expenditure reforms. The authorities have committed to reform the generous indirect subsidies on electricity, fuel and staple foods and to introduce targeted subsidies starting from July 2024. The authorities also plan to control the cost of the *Aasandha* health scheme, to reform the scheme design and control the cost of medical procurement through bulk procurement arrangements, which are already being piloted with the assistance of the UNDP. Recognizing the fiscal risks of State-Owned Enterprises (SOEs), the cabinet has endorsed an SOE reform plan and the regulator is currently developing SOE specific reforms. Finally, the government is reviewing the pipeline of public investment projects to prioritize and rationalize capital expenditures. The authorities highlight their commitment to raise the ambition of fiscal consolidation plans, compared to the 2024 Budget- which was formulated during a political transition. They highlight the criticality of properly calibrating reforms and managing policy communications to secure public buy in for the reforms and reduce the risk of reversals.

In addition to the fiscal adjustment, the authorities plan to implement measures to strengthen the Public Financial Management system in the Maldives. Among the top priorities of the new government is the strengthening of the Sovereign Development Fund (SDF), which was established in 2017 to earmark resources to manage the external debt repayment risks. As part of the first 14 weeks plans of the new government, an SDF Act has been drafted and submitted to the Parliament, which will strengthen the management and governance of the SDF and enhance transparency on the allocations, management and use of the SDF. Authorities also highlight their decision to resume deposits to the SDF in foreign currency. The legislative agenda for the new administration also includes a new Fiscal Responsibility Act, a Public Debt Management Act, a new SOE Act and amendments to the Public Finance Act and Regulation.

On Debt Sustainability Analysis (DSA), the authorities take note of staff's assessment and are confident that their ambitious fiscal consolidation plan can meaningfully shift the debt trajectory towards a sustainable path. Nevertheless, the authorities reiterate their long-standing concerns regarding the Low-Income Country Debt Sustainability Framework (LIC-DSF), including the failure to consider country specificities. The authorities welcome the upcoming LIC-DSF review, and hope that the review will give due consideration to the major shifts in the debt burden for LICs collectively, since the pandemic.

Monetary Policy and Financial Stability

The Maldives Monetary Authority (MMA) agrees on the need for gradually tightening monetary policy, in congruence with the proposed fiscal tightening, to absorb the excess structural liquidity. The authorities highlight the discontinuation of the suspension in the Fiscal Responsibility Act (FRA) clauses which has allowed government deficits to be financed by central bank advances since March 2020. Upon taking office in November 2023, the new government submitted a request to the Parliament to halt the suspension in the FRA clauses, which was made effective on 31st December 2023. The MMA is considering a well sequenced and gradual increases in the Minimum Reserve Requirement (MRR) to absorb some of the excess liquidity and signal monetary policy tightening.

Fiscal and monetary tightening is needed to reduce foreign exchange demand, to rebuild FX buffers. Since 2022, with the global commodity price shocks, combined with the higher demand for imports from a recovering tourism sector, and expansionary fiscal policy has widened the current account deficit and weighed on foreign exchange reserves. Authorities acknowledge the need for well-coordinated fiscal and monetary tightening to reduce foreign exchange demand and rebuild buffers. Additionally, MMA has developed a package of measures to reform the FX market, which will support the de-dollarization of the economy. They also note that the *Favara* Instant Payment System, which was rolled out in 2023, will complement the FX reforms in expanding the usage of the Maldivian rufiyaa. The authorities are also exploring options for FX swap arrangement with bilateral partners.

The MMA continues to ensure that the financial sector is sound and resilient and welcomes the findings and recommendations of the 2023 FSAP. Overall, the banking sector remains sound, with high capital buffers, strong profitability, and historically low levels of non-performing loans. The authorities appreciate the in-depth analysis of the financial sector developments and the supervisory and regulatory frameworks, under the joint IMF-World Bank FSAP conducted in 2023. The authorities broadly concur with the FSAP findings and recommendations. The authorities acknowledge the vulnerabilities related to the sovereign-bank nexus, which they plan to address partly by gradually phasing in higher risk weights on bank holding of foreign currency sovereign securities. Ultimately unwinding the sovereign-bank nexus will also rest on containing the financing need of the government through fiscal consolidation, diversifying the sovereign debt portfolio and developing the domestic secondary market for public debt. To strengthen AML/CFT frameworks, the authorities have completed a national risk assessment and are working on mitigating the risks identified and addressing the gaps in the legal framework.

Climate change and other structural reforms

Maldives' vulnerability to climate change and natural disasters highlights the need for well-planned climate adaptation investments. Maldives is one of the most vulnerable nations to climate change and natural disasters. The low-lying islands of Maldives are vulnerable to sea level rise and changing weather patterns. Ocean warming and coral bleaching events could potentially affect the tourism sector, on which the economy largely depends on. In their Nationally Determined Contributions, the Maldives has pledged to reduce carbon emissions by 26 percent by 2030 and strive towards net-zero emissions by 2030, with adequate international support. At COP 28, President Dr. Mohamed Muizzu has committed to ramp up the energy production through renewable sources from 4 percent currently to 33 percent in 5 years. The authorities note the high cost of climate adaptation and mitigation, and limited access to climate financing. The cost of climate adaptation and mitigation are substantial for the Maldives and are estimated at USD 8.8 billion (159 percent of 2022 GDP) and USD 1 billion (18 percent of 2022 GDP), respectively. However, the authorities note that access to climate financing is constrained by strict procedural requirements as well as constrained access levels. The authorities appreciate the recently completed Green Public Financial Management (Green-PFM) and climate sensitive Public Investment Management Assessment (Climate-PIMA) exercises by the Fund. They believe that the assessments will help the authorities in establishing the institutional mechanisms to identify, prioritize and fund climate adaptation. The Ministry of Finance notes the work currently ongoing on climate budget tagging and fine tuning their environmental, social and governance (ESG) framework. Additionally, the MMA is working to develop a green taxonomy for the banking sector with the support of the Alliance for Financial Inclusion.

The authorities are developing a National Development Strategy, as a strategic vision for economic growth and poverty reduction for the next 20 years. Maldives has made impressive gains in development and poverty reduction over the past decades, which has been made possible by the growth of the tourism sector led by the private sector, along with public sector investments in health and education. Going forward, the authorities note a lack of a strategic direction for the development of the country, which recognizes the challenges facing the country over the longer horizon, including climate change and the changing demographic dynamics. The new administration plans to formulate the National Development Strategy, for the next 20 years and enshrine this strategy in law.

The authorities continue to seek avenues for economic diversification and expansion in trade and investment. Tourism will continue to be the main economic activity into the foreseeable future, and the authorities give a high priority to the development of the sector, by facilitating private sector investments and developing critical public infrastructure, such as airports. The authorities see further potential to diversify the tourism products and the source markets. For the fisheries sector, the focus is on enhancing the domestic processing capacity to increase the value added of fish exports. While Maldives practices sustainable pole-and-line fisheries, the authorities note that the country does not receive a premium value for their products. Furthermore, major export markets do not provide preferential access for their sustainably produced fisheries products. The government has recently set up a fisheries promotion agency to develop the Maldives sustainable fisheries brand and market their products.

Maldives is a testament to the value of the Fund capacity development assistance in strengthening institutions and policies. Maldives is among the most intensive Fund capacity development recipients in the Asia Pacific region. The authorities highly value the capacity development and technical assistance provided by the Fund.

Conclusion

The authorities welcome the timing of the Article IV, coinciding with the beginning of the new administration. The new government is strongly committed to take decisive action to address fiscal and debt sustainability and appreciates the opportunity to discuss their home-grown program of fiscal consolidation and macroeconomic stabilization with the Fund.