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Executive Summary

Raising Pasifika

Strengthening Government Finances to Enhance Human Capital in the Pacific

A Public Expenditure Review for Nine Pacific Island Countries

Kiribati, Nauru, Republic of the Marshall Islands, Federated States of Micronesia, Palau, Samoa, Tonga, Tuvalu, and Vanuatu

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Executive Summary

The objective of this Public Expenditure Review (PER) is to improve the efficiency of public spending in the health, education, and social sectors, and to increase domestic revenues across nine Pacific Island Countries (the PIC-9: Kiribati, Nauru, Republic of the Marshall Islands (RMI), Federated States of Micronesia (FSM), Palau, Samoa, Tonga, Tuvalu, and Vanuatu). World Bank PERs generally evaluate the effectiveness, efficiency, and equity of public spending as well as fiscal sustainability. The PIC-9 PER, however, focuses on how to: (i) improve the allocative, and to some extent, technical efficiency of public spending within the sectors of analysis;[1] and (ii) increase domestic revenues. Combined, the measures identified could deliver a fiscal impact of 3–43 percent of GDP for each of the PIC-9, while also supporting improved human capital outcomes and enhanced fiscal sustainability. Executive Summary (ES) Tables 1–9 summarize the measures identified and their estimated fiscal impact, where feasible, for each of the PIC-9.

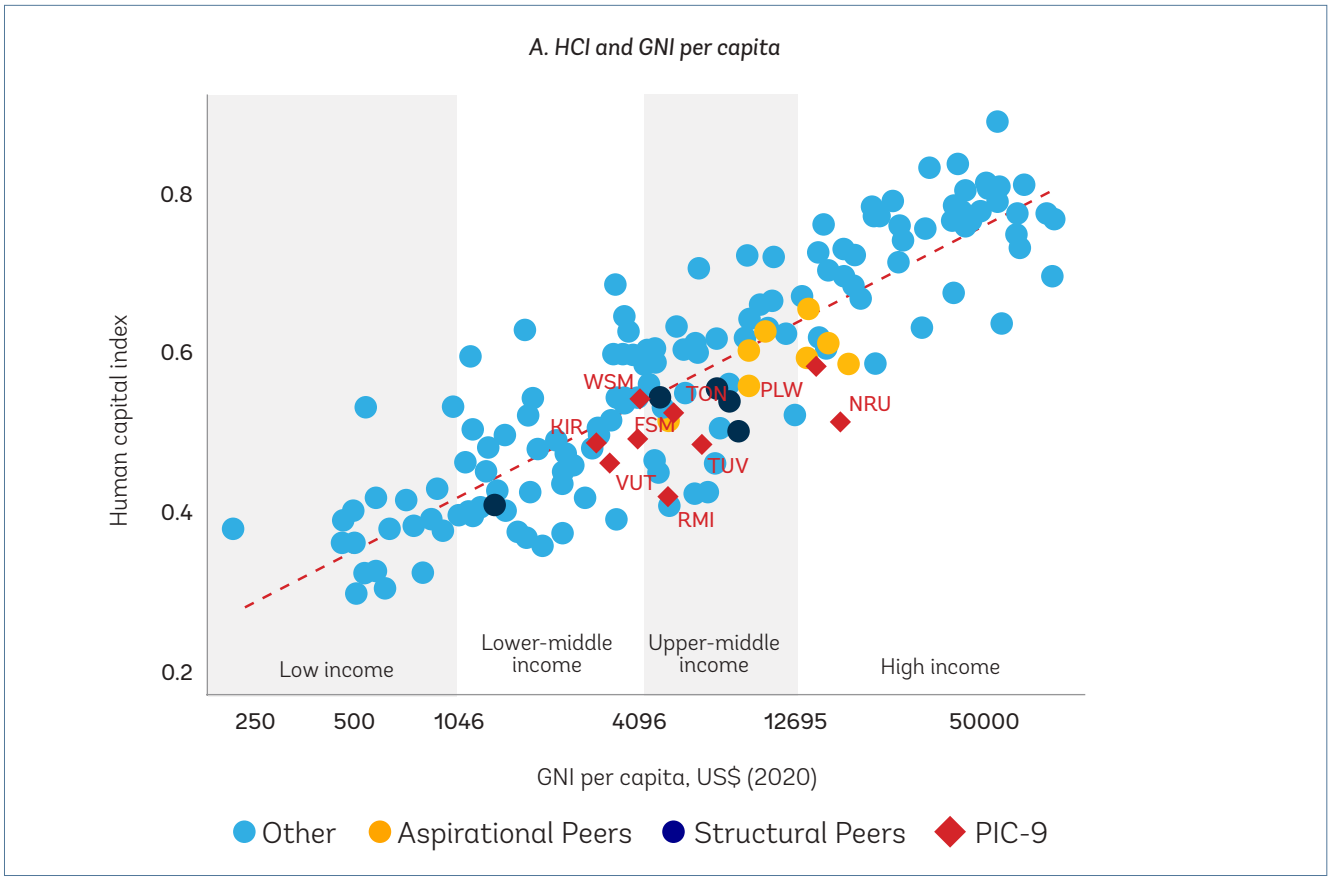
The COVID-19 shock, combined with overlapping shocks from natural disasters and global inflation, risks reversing a decade of progress in building human capital across the Pacific. Remoteness helped the PIC-9 avoid a COVID-19 health crisis, but the prevention strategies employed by governments have had severe economic consequences. Strict international border restrictions, in some cases compounded by natural disasters, have led to substantial negative effects on economic output, employment, and government finances. Households have shouldered a heavy burden from the shock, with surveys showing that many withdrew children from school, avoided non-urgent health care, and reduced food consumption—all of which could have long-term consequences for human capital. Vulnerable households are most likely to be forced to make such decisions, exacerbating existing income inequalities. The pandemic has also widened existing gender inequalities, including in the labor market and access to health services, and has been associated with a rise in physical and sexual violence. Combined, these effects risk reversing hard-won gains in human capital across the PIC-9, which could have permanent scarring effects on productivity and prosperity.

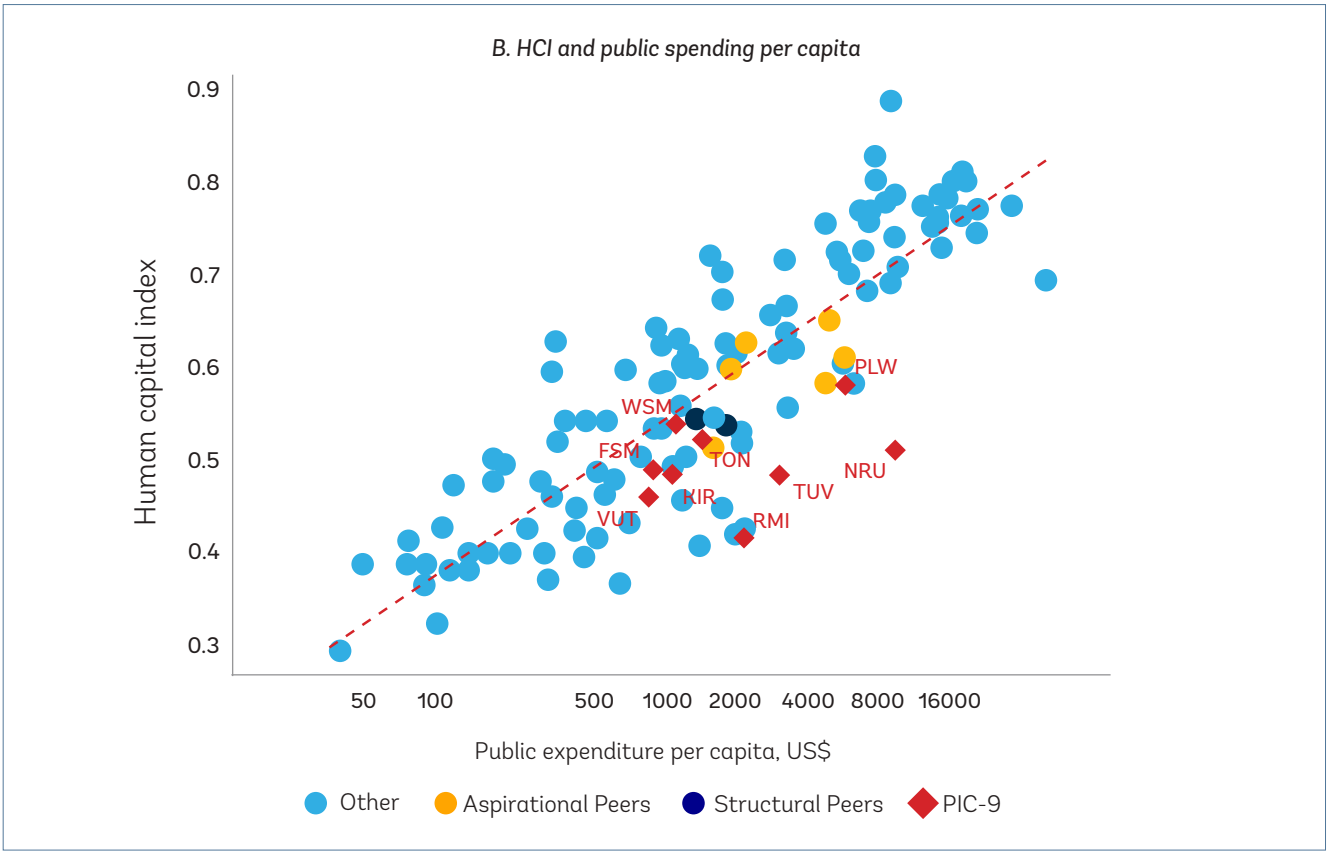
Public finance has a critical role to play in building human capital as a central element in a green, resilient, and inclusive recovery. Human capital is a crucial driver of economic growth and development, poverty reduction, and improved wellbeing. Limited human capital is a key constraint to inclusive growth in the PIC-9 (World Bank, 2023). Yet, human development in the PIC-9 (proxied by the Human Capital Index, HCI) was low prior to the pandemic, relative to their level of income and public spending (Figure ES1). As the PIC-9 emerge from the pandemic and overlapping shocks, governments will need to turn their attention to building back fiscal buffers, supporting growth, and addressing key development goals. The pandemic and associated border closures have highlighted that to improve livelihoods and support a diversification in the drivers of economic growth, the PIC-9 must invest in their greatest resource: their people.

1. 'Allocative efficiency' refers to reallocations of public spending between spending areas with a view to improving the quality of spending. 'Technical efficiency' refers to maintaining the same level/quality of outputs with reduced inputs or increasing the level/quality of outputs with the same level of inputs.

An education crisis, the non-communicable diseases (NCDs) epidemic, and high vulnerability to climate change and natural disasters impose substantial costs on the PIC-9 that require urgent action. The HCI shows that the average child born in the PIC-9 today will be only half as productive when they grow up as would have been the case if they had optimal health and education. Across the region (except Palau), too many 10-year-olds are not acquiring minimum proficiency in literacy and numeracy. This education crisis is compounded by poor health outcomes that predate COVID-19. Largely due to NCDs, Pacific Islanders lose over 37 years of life from premature morbidity and mortality for every 100 citizens, 16 percent more than in peer countries. Without intervention to address the NCDs epidemic, the economic burden is projected to increase by 5–9 percent of GDP by 2040 (World Bank, 2017). Implementation of the Pacific Agreement on Closer Economic Relations (PACER Plus)—a regional free trade agreement—could result in losses of 2–14 percent of revenues, curbing the region's capacity to finance key development spending. Finally, the Pacific is one of the world's most disaster-prone regions, and among the most exposed to sea-level rise. Left unaddressed, these challenges risk making the economies weaker, societies more unequal, and families poorer and more vulnerable.

Figure ES1: Human capital in the PIC-9 is lower than would be expected for the region's level of development and public spending





Note: Values are FY15-FY20 averages.
Source: World Bank World Development Indicators (WDI) and country national budgets.

The recommendations from this PER provide a set of opportunities to address these challenges and achieve the region's development goals. As the region emerges from the overlapping shocks and looks towards the future, these challenges underscore the importance of not reverting to 'business as usual'. Achieving the region's development goals and enhancing resilience to climate change will require not just improvements in physical infrastructure, but also a transformation in the quality of human capital. Financing, though crucial, will not be enough. Achieving shared prosperity will require more efficient health, education, and social protection systems, combined with prudent fiscal management.

The PIC-9 PER differs from a traditional World Bank PER due to its objective and scope. In summary, these differences include: (i) the coverage of nine countries; (ii) a strong emphasis on the objectives of spending efficiency and fiscal sustainability (but a more limited discussion of equity issues); and (iii) the very challenging data environment in the Pacific. For example, many of the PIC-9 do not regularly publish fiscal data consistent with the Government Finance Statistics (GFS) standardized framework. To address this constraint, this PER supported the preparation of a BOOST dataset for six of the PIC-9 countries—Kiribati, RMI, Palau, Samoa, Tonga, and Tuvalu (all nine countries were approached). This was possible owing to the respective governments providing detailed revenue and expenditure data. The BOOST program is a World Bank-sponsored

open budget portal that provides highly disaggregated budget data in a standardized format, facilitating analysis over time and across countries.[2] The six BOOSTs will be published to improve the Pacific data environment and facilitate future analysis by interested parties. In addition, FSM, Palau, Samoa, and Tuvalu completed a more detailed revenue questionnaire that provided additional data. Working with PIC-9 governments, the World Bank will seek to expand and periodically update these datasets.

Due to the challenging data environment, this PER follows a two-tiered analytical approach. The first tier takes stock of the evolving trends of domestic revenues and social sector spending in recent years across the PIC-9. The second tier undertakes deeper analysis to identify specific measures to increase domestic revenue and improve spending efficiency based on the BOOST and additional revenue datasets, household income and expenditure surveys, and complementary global and country-level data. Consequently, the depth and breadth of analysis across the nine countries is heterogenous.

The PER is designed to inform PIC-9 government priorities, promote closer coordination within governments, and encourage greater participation by citizens in policy issues. The PER is designed to inform government budget decisions and future World Bank operational priorities by providing evidence on how to improve the quality of social sector spending while rebuilding fiscal buffers. The analysis and measures identified can also encourage further dialogue between ministries of finance and ministries of health, education, and social protection about sector priorities, allocations, spending efficiency, and how results are measured. Finally, by providing an independent assessment of fiscal policy, the report can catalyze deeper engagement by citizens regarding national priorities and government policy.

In this report, the PIC-9's public spending dynamics and performance are compared with other relevant countries using an international benchmarking exercise. This study applies the World Bank's Country Economic Memorandum 2.0 framework to select two sets of countries for comparison with the PIC-9. The first is a set of structural peer countries with broadly similar economic structure to the PIC-9, and similar performance on a target indicator. The second is a set of aspirational peer countries that also have similar characteristics but have outperformed the PIC-9 on the target indicator. Benchmarking was done based on the following characteristics: (i) population; (ii) GDP per capita (current $US); and (iii) government effectiveness (from the Worldwide Governance Indicators). This provides a list of comparator countries from the Caribbean Island countries (CICs) and other small island developing states (SIDS). Structural and aspirational peers were defined based on 2020 HCI scores relative to Samoa (the top ranked PIC-9). This provides the following groupings, which are used throughout the report:

a. **Aspirational peer countries:** Fiji, Antigua & Barbuda, Grenada, St. Kitts & Nevis, St. Lucia, Trinidad & Tobago, Mauritius, Seychelles.
b. **Structural peer countries:** The remaining CICs (the Bahamas, Barbados, Belize, Dominica, Guyana, Jamaica, St. Vincent & the Grenadines, Suriname) plus selected SIDS (Comoros, Guinea-Bissau, Sao Tome and Principe, Timor-Leste, Cabo Verde, Solomon Islands).

2. For further information and access to the datasets, see https://www.worldbank.org/en/programs/boost-portal

The macro-fiscal context and the case for fiscal consolidation

The PIC-9 share several structural characteristics, but also have important differences that lead to heterogeneous opportunities and challenges to achieve fiscal sustainability and spending efficiency. The PIC-9 are among the world's smallest and most isolated nations. Their unique economic geography, including extreme remoteness, small size, geographic dispersion, and vulnerability to shocks, makes achieving inclusive economic growth and fiscal sustainability particularly challenging. These characteristics lead to higher public expenditure to deliver a given level of coverage and quality of public goods and services, due to high fixed costs and a lack of economies of scale. Their small populations and domestic labor markets also mean that the PIC-9 face serious capacity constraints, further impeding the functioning of the public sector. The Pacific is also one of the most aid dependent regions in the world, with all the PIC-9 among the top 13 countries in terms of net aid flows per capita. Yet, even within the group, aid dependency varies from 15 percent of total revenue in Samoa and Nauru, to 40–50 percent in FSM, RMI, and Tonga. In recent years, sovereign rents have emerged as a key source of fiscal revenue in six of the PIC-9, mainly from selling fishing access rights in their Exclusive Economic Zones (EEZs), but also from other novel sources. These windfall rents have presented new opportunities and challenges for fiscal management. Variations in their dependence on tourism as a key source of economic activity, jobs, and tax revenues has also meant that the COVID-19 shock has had heterogenous impacts across the region. Finally, the level of development (proxied by Gross National Income (GNI) per capita) also varies widely, from US$2,960 in Kiribati to US$15,590 in Nauru. Despite these differences, medium-term fiscal sustainability remains a key enabler to green, resilient, and inclusive development across the region.

Following a period of relatively robust economic performance, COVID-19-related border closures and natural disasters led to deep and protracted recessions across most of the PIC-9 in FY20-21. Prior to the pandemic, the PIC-9 economic performance had been relatively strong, with higher growth and improved fiscal positions compared to historical trends. However, the pandemic represented a large negative shock to the region's economies. Over two years of strict travel restrictions slashed tourism exports, disrupted temporary worker programs and goods exports, and increased the cost of imports. Domestic lockdowns led to business closures and curtailed construction activity. In Tonga and Vanuatu, these impacts were compounded by natural disasters, which caused significant damage to housing, infrastructure, and crops. In 2022, domestic outbreaks of COVID-19 in several countries and higher global commodity prices due to the Russian invasion of Ukraine further buffeted the PIC-9 economies. Consequently, output across most of the region is not expected to recover to pre-pandemic levels until 2023 at the earliest.

Governments responded with substantial stimulus, resulting in fiscal deficits. The economic downturn led to large shortfalls in domestic revenues, combined with additional spending to support health-sector preparedness, vaccine rollout, and to mitigate the economic impacts on households and businesses. Averaging 15 percent of GDP, the COVID-19 fiscal response packages implemented by the PIC-9 were among the highest in the world. In Tonga and Vanuatu, authorities also had to create fiscal space for disaster response and recovery. This resulted in

an expansion in PIC-9 fiscal deficits (before accounting for grants) to an average of 19 percent of GDP in FY20-FY21, compared to 13 percent in FY13-FY19. After accounting for grants, five of the PIC-9 registered fiscal deficits in FY21, while the other four registered lower surpluses than in previous years. The stimulus packages were financed by unprecedented levels of development partner grants (and/or highly concessional loans in the case of Vanuatu and Palau), spending reprioritization, the drawing down of contingent financing, emergency funds and cash reserves, new domestic debt, and participation in the Debt Service Suspension Initiative (DSSI).[3]

Going forward, fiscal consolidation is required to protect medium-term fiscal sustainability. Six of the PIC-9 are already at a high risk of debt distress (Vanuatu is rated at medium risk and Palau and Nauru's debt is rated as sustainable), and several countries have run down fiscal buffers to finance recent expansionary fiscal policy. Over the coming years, aid is likely to return to pre-crisis levels and sovereign rents are projected to remain flat as a share of GDP. The PIC-9 lack access to international capital markets and domestic debt markets are shallow. Consequently, fiscal consolidation is necessary to balance the budget, and to avoid a sharp cut in public service delivery in the future. In addition, long-term projections indicate that the PIC-9 are likely to face significant fiscal challenges over the coming 20 years and have limited capacity to finance additional spending, including for human capital. While several countries have sizeable sovereign wealth funds, almost all have strict withdrawal rules, meaning governments cannot easily use them for immediate budget financing. Even where this is possible (FSM and Tuvalu), repeated drawdowns to finance fiscal deficits are not advisable, as this will undermine the funds' intergenerational equity objectives. Thus, a medium-term fiscal adjustment is needed to meet the region's large development spending needs, while managing the risk of debt distress and rebuilding fiscal buffers to prepare for future shocks. The fiscal adjustment could include a gradual increase in domestic revenues and containing current expenditure at prudent levels. Continued access to grants in line with pre-pandemic trends is also essential to fund capital investment projects for sustainable development and climate resilience.

Improvements in human capital outcomes will need to come from increased spending efficiency. The education and health sectors already account for a high proportion of spending across the PIC-9. This means that it is unlikely that governments will be able or willing to increase social spending via reallocation from other sectors. Given the PIC-9's limited capacity to finance additional spending, improving human capital outcomes will thus require efforts to improve the efficiency of sector spending within the existing allocations. In contrast, fledgling social protection systems across the region will require additional spending to increase coverage and improve delivery systems. This could be financed from increased domestic revenues or efficiency savings in other sectors, including via the measures identified in this report. The exceptions are RMI and Kiribati, where copra subsidies represent sizeable expenditure items. Reallocating some of this spending to poverty-targeted social assistance programs should be the focus in these countries.

3. Established by the G20 and operational from May 2020 to December 2021, the DSSI facilitated the suspension of debt-service payments to official bilateral creditors from 48 developing countries that requested the suspension (including Samoa and Tonga).

This PER aims to identify measures that deliver additional domestic revenues and public spending efficiency savings to support both improved human capital outcomes and the required fiscal adjustment. In a fiscally constrained environment, improved allocative efficiency of spending is a natural first step towards the goal of improving human capital outcomes, as it aims to improve the quality of public services while keeping the level of sector spending largely unchanged. As such, efficiency measures would be expected to encounter relatively less political and public opposition compared to direct spending cuts that may impact public service delivery negatively. The timing of measures to increase revenues should be calibrated with the economic recovery, to ensure they do not undermine the recovery. The subsequent sections, and Tables ES1–9 at the end of this Executive Summary, identify key revenue-raising and efficiency-enhancing measures and estimate their potential fiscal impact, where feasible.

Increasing domestic revenue mobilization

Closing part of the large tax gaps—estimated to be 8–17 percent of GDP—needs to be at the heart of the PIC-9's medium-term revenue strategy and can be started once the recovery is underway. The PIC-9 lack access to international debt markets, so the fiscal envelope is constrained by the taxes they can collect, sovereign rents, and concessional financing from development partners. The last two have the potential to be very volatile, so tax collection needs to be the foundation of the PIC-9 revenue strategy as the region emerges from the COVID-19 crisis. Low domestic revenues (excluding sovereign rents) in several PIC-9 economies reflect sizeable structural 'tax gaps'. These are a measure of the difference between estimated tax collection potential, based on the performance of other countries at a similar income level, and actual tax revenue. Tax gaps for the PIC-9 are estimated to be between 8 and 17 percent of GDP. These large tax gaps arise from a combination of low compliance and tax bases that are narrow due to high thresholds and costly exemptions. In a few cases, the absence of a general consumption tax (Nauru), a corporate income tax (CIT) (Palau), or any income taxes (Vanuatu) represents the most significant case of narrow tax bases. Tax potential in several of the PIC-9 can also be raised through increases in select tax rates. Revenue reforms can be introduced once the recovery is underway. These should be prioritized and sequenced as part of a medium-term revenue strategy that is integrated in a medium-term fiscal strategy.

Improving the quality of indirect taxation will support revenue efficiency and fairness. Value-added tax (VAT) policy reforms that can help close the VAT gap include expanding the base by lowering VAT thresholds (Kiribati, Palau, Samoa) and rationalizing VAT exemptions (Tonga, Kiribati). These reforms would help VAT efficiency and improve horizontal equity by removing some of the distortions that come from uneven treatment of different sectors and businesses. On the administration side, ensuring timely VAT refunds may result in revenue losses in the short term, but improve trust and voluntary compliance, helping raise revenue over the medium term. Voluntary compliance can also be improved through other measures that ease the burden of paying taxes, including rolling out VAT e-filing and e-payment. Higher compliance is also likely to follow from strengthened enforcement, including through using third-party data to enhance audits as part of a broader compliance improvement strategy. Higher VAT can also come from raising the statutory rate in countries whose rate is currently below comparator countries (Tuvalu, Palau, Kiribati). For FSM and RMI, moving from a gross-revenue regime to a VAT regime is a critical

reform, which can improve horizontal and vertical equity, and increase revenue. Indirect taxation in the PIC-9 can also be improved through reform of excises. Implementation of the PACER Plus trade agreement will lead to losses in trade taxes. These losses can be offset by higher excises on tobacco, alcohol, and sugar-sweetened beverages, which would also support economic, health, and fiscal objectives over the medium term.

Higher indirect taxation on vulnerable groups should be offset by more progressive direct taxation and government spending. Overall, higher indirect taxation may result in an increased tax burden on, or higher prices for, vulnerable groups in society. This challenge is best addressed in two ways that together make fiscal policy supportive of poverty and equity considerations: (i) strengthening direct taxes, so that the tax system in sum is progressive, with the higher-income deciles paying more; and (ii) ensuring that spending supports the poor and vulnerable, including through targeted cash transfers, and public goods and services consumed by the poor and vulnerable.

Increased use of direct taxation will increase progressivity and raise more tax revenue. Direct taxation instruments are central to improving the progressivity of tax systems. However, direct taxes are currently underutilized by the PIC-9. Vanuatu has no income taxes at all, while Palau has no corporate income tax. Most of the PIC-9 rely on personal income taxation (PIT). Yet, even here, the tax net in countries like Tuvalu appears very narrow due to high thresholds and noncompliance, and the rate for the top marginal bracket in FSM, RMI, and Palau is low compared to peer countries. In contrast to the performance of PIT, CIT productivity is low compared to peer countries, particularly in Samoa and FSM. Reforms that could help improve CIT productivity include rationalizing CIT exemptions; strengthening measures that counter base erosion and profit shifting and other forms of tax avoidance; and improving compliance management to tackle tax evasion. Property taxes, which can be some of the most efficient and progressive types of taxes, are also very low in the PIC-9. Higher taxes on immovable property can be a useful instrument to raise local revenue to finance local services, strengthening the accountability linkages between revenue, spending, and local governance.

In addition, greater regional cooperation in the management of fishing license fees has the potential to generate substantial increases in domestic revenues for several PIC-9 countries. Fishing revenues related to the Parties to the Nauru Agreement (PNA) Vessel Day Scheme (VDS) for purse-seine tuna vessels represent 8–75 percent of domestic revenues in Kiribati, Tuvalu, RMI, FSM, Nauru, and Palau. Maximizing the long-term benefits from these resources is crucial to fiscal sustainability. Reforms that provide greater flexibility and transferability of VDS days could lead to an annual increase in fisheries sector revenues of 8–25 percent of GDP in FSM, RMI, and Kiribati. Higher revenues are also possible in Palau, Nauru, and Tuvalu. However, translating high and volatile fishing revenues into better development outcomes will also require better quality spending. This can be achieving by strengthen medium-term fiscal frameworks, including improved capacity for revenue forecasting, fiscal rules to manage windfall revenues, and stronger medium-term expenditure frameworks.

Improving education outcomes and spending efficiency

Public education spending is relatively high across the PIC-9 when compared to peer countries, but is especially high in Kiribati, Tuvalu, RMI, and FSM (the 'high-spending countries'). Spending per student (unit costs) and public education spending as a share of GDP and total public spending is similar to peer countries in Samoa, Tonga, Palau, Nauru, and Vanuatu. However, public spending is much higher than peers in the high-spending countries.

High unit costs are driven by non-wage factors, due to the lack of economies of scale, large school grants, and high spending on scholarships and food provisions. The teacher wage bill represents an unusually small share of public education spending in the PIC-9. Yet, teacher salaries are adequate and class sizes are not too large. Rather, the reduced share of teacher wages reflects larger-than-usual non-wage expenditures. There are three reasons for this: (i) limited economies of scale, as despite their limited number of students, the PIC-9 still need fully-fledged institutions with all the usual functions of an education system (administration, assessment, training, statistics, etc.); (ii) large direct transfers to schools through grants; and (iii) generous provision of food, scholarships, or transfers to various independent administrative bodies[4] in the high-spending countries.

Access has been improving, although primary education is not yet universal while access to secondary education remains limited, especially for youth and boys. However, this is likely to improve as entrance exams for secondary schools are being lifted and repetitions are declining. The limited number of secondary schools is a bottleneck, as travel distance to reach them from settlements can be prohibitive.

Learning outcomes were already very poor and worsened during the pandemic.[5] While official measures of learning poverty are not yet available for the PIC-9, World Bank estimates indicate that pre-pandemic learning poverty may be above the rates observed in PIC-9 peer countries, despite similar or higher spending. The latest data on student performance collected in late 2021 suggest that literacy rates declined during COVID-19.

Worse outcomes than peers despite their high level of spending suggests that the PIC-9 could improve the efficiency of public education spending. Cross country analysis suggests that, after accounting for population size and dispersion, education unit costs in the high-spending countries could be expected to be 13 to 23 percent lower. Savings are most likely to be feasible in overseas scholarships, school operational costs, and private subsidies and school grants.

Although the PIC-9 (and six other Pacific nations) have been participating in a regional assessment every three years since 2012, the data has not been made public, contrary to common practices. This hinders public debate about the quality of education provided and may contribute to an education crisis going unnoticed.

4. Education systems typically have several independent administrative bodies for overseeing the universities, for school inspectorates, and sometimes for facility management or a central assessment center.
5. According to the preliminary Pacific Islands Literacy & Numeracy Assessment (PILNA) 2021 report.

Analysis suggests that several factors may be behind the poor outcomes. First, official curricula are not providing long enough periods of teaching in vernacular language, while learning materials and assessment tools in local languages are lacking. Second, teachers' content knowledge and teaching practices may not be effective. Third, both the coverage and quality of Early Childhood Education is insufficient to prepare learners.

Education recommendations

Recommendations to accelerate learning and reduce spending inefficiencies are as follows:

Short-term actions

First, make improved learning outcomes for all children a national priority. To do this, the PIC-9 should: (i) reaffirm a national commitment to achieving Sustainable Development Goal (SDG) 4.1 and initiate public discussion on achieving critical education outcomes; (ii) develop and then launch a costed plan for accelerating learning, using evidence-informed strategies and interventions (for example, recent pilot programs in FSM and Tonga have shown positive results)—the RAPID framework[6] supported by the World Bank can help in identifying such strategies and interventions; and (iii) engage all partners involved in education, including parents, in a national movement to achieve SDG4 benchmarks on foundational learning.

Second, as part of the costed, evidence-informed plan for accelerating learning, consider including strategies and interventions consistent with evidence. For example, instruction should be aligned with learning needs through approaches such as targeted instruction, structured pedagogy, tutoring, and self-guided learning. In addition, information should be gathered about teachers' subject knowledge and teaching practice to target support to teachers, including through classroom observation. This can help to strengthen teacher training through coaching, mentoring, and peer learning. The PIC-9 should also reinforce learning in vernacular language, especially in primary school, by adapting curriculum, materials, and related assessment.

Third, more and better data are needed to guide decisions, including the following: (i) making public the information collected from the Pacific Islands Numeracy and Literacy Assessment (PILNA) and using these data to better understand the underlying drivers of poor performance; (ii) gathering data on teachers' content knowledge and current teaching practices to help design what training (and what amount) is needed and track whether such training is having an impact; (iii) reporting on a yearly basis the number of tertiary students and beneficiaries of overseas scholarships to ensure that economic returns and equity can be assessed, and reviewing the effectiveness of overseas scholarship with the development partners that contribute to their funding; (iv) ensuring regular data collection (especially enrolment numbers) to inform the distribution of school grants, deployment of teachers, and development of plans to increase enrolment; (v) filling large knowledge gaps in public accounting of education spending and how decentralized funding is used, both at the local and the school level when applicable; and (vi) building capacities in ministries of finance and education to engage in more evidence-based and strategic discussions around spending relative to the results the education sector is achieving.

6. For more details on the RAPID framework, see the World Bank's Guide for Learning Recovery and Acceleration.

Fourth, explore ways of reducing 'overhead' costs, including through enhanced regional cooperation, focusing on which functions could be delivered better through cooperation. For example, on curriculum design, monitoring teacher standards, and more pooling of budget resources to expand a regional university system.

Medium-term actions

Improve children's readiness for school by widening access to Early Childhood Education from the age of three, through local centers close to the population settlements (particularly in RMI, Samoa, Tonga, and Vanuatu). While such expansion would require substantial additional resources, statistical analysis suggests that this is likely the easiest way to improve overall poor outcomes.

Use a range of different policy instruments to expand access to secondary schools for children residing in the most remote areas, experimenting with different modalities to expand access while rigorously monitoring the costs of such modalities and their impact. This could involve supporting outer island students to access secondary schooling in urban centers by providing subsidies for transport and the cost of living away from home. Alternatively, countries could consider adding additional grades to existing primary schools in the most remote areas to allow students to continue to study (beyond their primary grades) in nearby schools. Allowing such an expansion would likely be cheaper than the boarding option, as it would facilitate enrolment at the secondary level while utilizing the existing teaching force and infrastructure to lower unit costs. However, such decisions should also consider the relative quality of learning in the urban secondary schools compared to outer island schools.

Strengthening the quality of health care and efficiency of public spending

Public spending on health is high across the PIC-9 compared to peer countries, both as a share of GDP and as a share of total government spending. Only Vanuatu and Tonga have spending similar to peer countries in both metrics. All other PIC-9 countries have considerably higher spending than peers across one or both measures. To some degree, this reflects a strong commitment to health by PIC-9 governments. However, it also reflects substantial support to the public health sector from external partners, and the cost of providing publicly funded services to a geographically dispersed population with limited economies of scale.

The delivery and financing of health in the PIC-9 is predominantly public, financed by governments through domestic revenue and foreign aid. Across the region, the public sector accounts for 80–95 percent of current health spending (including social health insurance schemes in FSM, RMI, and Palau), while private sector and household 'out of pocket' (OOP) payments are low. This composition is unique compared to peers due to the PIC-9 benefiting from substantial foreign aid to the health sector, along with low household spending (which the PIC-9 are encouraged to maintain to support access and equity objectives). However, the financing landscape is evolving due to some development partners transitioning out of the region, and the unwinding of considerable pandemic support. In this context, improved spending efficiency is crucial to improve health service delivery. To achieve this, health sector governance needs to be strengthened, and development partners are urged to improve transparency of funding to assist governments to better track, coordinate, and effectively use resources for health.

Ministries of Health (MOH) spend more than half of their annual budget on human resources (HR), followed by pharmaceuticals and medical supplies, and/or overseas medical referrals (OMR). The distribution of facilities and human resources for equitable access to health services is a major challenge, with spending focused on hospitals and urban centers. MOHs are urged to review and adopt service delivery models that: (i) focus on primary health care and ambulatory care sensitive conditions (ACSCs);[7] (ii) make the best use of resources along the whole continuum of care (from prevention and primary health care all the way to OMR); and (iii) can adapt and respond to crises, including by taking advantage of evolving digital tools and telehealth opportunities.

Despite substantial public health spending, PIC-9 progress towards Universal Health Coverage (UHC) is slower than in peer countries. Non-communicable diseases (NCDs) make up an increasing share of the overall disease burden and premature deaths. This has considerable implications for human capital, the resilience of populations to disease outbreaks and broader disasters, and the economic potential of individuals, households, and economies. Challenges remain with communicable diseases, particularly tuberculosis (TB), along with intermittent outbreaks of food- and water-borne infections. While there have been some improvements in reproductive, maternal, neonatal, child, and adolescent health, levels of stunting and teenage pregnancies remain a concern in certain countries. Violence against women and girls in the Pacific is amongst the highest globally. Data is limited on the impact of COVID-19 on health outcomes, but there is evidence of a deterioration of some routine vaccinations, forgone care for NCDs, reduced active case finding for TB, and increased domestic violence.

Given the need for fiscal consolidation with already high public health spending, improvements in health outcomes will need to come from increased efficiency and equity of spending. Taxation policies on both unhealthy and healthy products could also be further leveraged.

Health recommendations

Recommendations to improve the quality of health spending are as follows:

First, and as a pre-requisite to successfully implement and monitor the impact of any other changes:

Strengthen corporate and clinical governance as this will deliver more efficient and quality health results. The PIC-9 are encouraged to reinvigorate governance mechanisms that will improve health sector performance, informed by timely and fit-for-purpose data and analytics. Policies to progress UHC will need to be developed where they are not available (RMI), and more actively rolled-out and monitored where they are (Tonga, Kiribati, Vanuatu).

7. ACSCs are conditions for which hospitalizations are thought to be avoidable through public health interventions and early disease management, usually delivered in an ambulatory setting (outpatient) such as primary care.

Secondly, the PIC-9 are encouraged to improve technical efficiencies by implementing better systems and processes starting with large expenditure areas:

Better management and coordination of patient medical referrals (both local and overseas), alongside more effective use of visiting specialist medical teams, will make health dollars go further. PIC-9 countries with substantial and/or rapidly increasing OMR expenditure (Kiribati, Nauru, RMI, FSM, and Tuvalu) should complete a detailed analysis of the costs and options to improve the use of these funds. Practical, fit-for-purpose administration processes are needed, including comprehensive, regularly updated, and standardized patient databases for routine monitoring and analysis. In addition, the PIC-9 are encouraged to become strategic purchasers of OMR services—including exploring shared regional agreements—rather than being 'passive' buyers. Concurrently, MOHs must continue strengthening core diagnostic, rehabilitative and palliative services that can be delivered safely in-country, so that OMR is predominantly used to meet treatment deficits.

Strengthening supply chain management systems for pharmaceutical and medical supplies can generate savings by reducing costs, stock-outs, and wastage. The PIC-9 are encouraged to complete a detailed analysis of existing procurement practices. Such reviews have the potential to reduce line-item costs by up to 30 percent. In addition, investments are needed in systems that enable timely monitoring of supplies across facilities. Pooled procurement and multi-year procurement contracts should also be explored.

Better adaptive design of infrastructure and management of utility consumption may generate considerable savings. The PIC-9 are encouraged to complete an audit of utility expenditure and monitor actions to reduce costs, with findings used to inform new/renovation designs and maintenance plans for more climate resilient and efficient facilities.

Updating service delivery models—including reviewing the total number of health facilities—combined with better management and coordination of HR can lead to more efficient and equitable health care. The PIC-9 are encouraged to review the number and expected functions of health facilities, with a view to consolidating finite resources into fewer better-resourced facilities, combined with effective, regular outreach and use of digital tools, rather than having many poorly resourced facilities. This review will inform adjustments to improve the skill mix and distribution of HR. This should be complemented by better use of standard operating procedures for quality of care, and implementation of 'best buys' for priority services.

Thirdly, the PIC-9 are encouraged to improve allocative efficiency by increasing the share of resources provided for large return-on-investment areas:

Better integration of health services is needed across the continuum of care in the PIC-9. The PIC-9 are encouraged to improve horizontal integration across health programs. This includes directing more resources to both primary and secondary prevention and ACSCs to avoid disease progression and costly avoidable hospitalization, with a focus on prevention, detection, and routine management of NCDs. In Kiribati, Nauru, Tuvalu, FSM, RMI, and Vanuatu, additional efforts are required on child health and nutrition, and sexual and reproductive health. Better vertical integration of health services is also needed across the continuum of care, with more

emphasis on health promotion and early disease intervention activities, through to more complex clinical curative, rehabilitative, and palliative care. Better integration across sectors is also crucial to tackle the social and economic determinants of health, with focused multi-sectoral approaches to improving health for all.

Finally, effective management of health resources requires staff that are empowered to take timely action, informed by quality information and processing systems. The PIC-9 are encouraged to address health sector management challenges by expanding information systems and analytical capacities to develop and use data for decision making, including digital tools.

Investing in an expansion of social protection

Social protection is a key enabler of inclusive growth, human capital accumulation, and poverty alleviation. Social protection measures enhance resilience by insuring against negative impacts on wellbeing due to shocks; foster equity by combating chronic poverty and ensuring a minimum income or consumption floor; and create opportunity through promoting investments in human capital (education and health) and linking people to gainful employment.

Social protection in the PIC-9 is inadequate, especially in the case of social assistance. Social assistance is underfunded, with formal schemes mostly restricted to small programs targeting the elderly and people with disabilities. Employment programs are largely non-existent, apart from labor mobility units established as part of overseas employment programs. Social insurance is more developed, though coverage is limited given the size of the informal sector in the PIC-9 and adequacy is a concern.

Prior to the pandemic, most of the PIC-9 were spending less than 0.5 percent of GDP on social assistance, far below global (1.5 percent), regional (1.1 percent), and comparator country (2.2 percent) averages. Low levels of spending are reflected in low coverage, with PIC-9 social assistance programs reaching only 10 percent of the population on average, compared to 43 percent in East Asia and the Pacific. The exceptions are Kiribati and RMI, which spend around 9 and 3 percent of GDP, respectively (14 and 5 percent of the annual budget, respectively) seeking to support poor and vulnerable households through copra subsidies. The value of formal social assistance programs in the Pacific was highlighted during the pandemic, with simulations showing that pandemic-related social protection expansions reduced poverty by up to 5 percent of the population, compared to what it would have been in the absence of such programs.

Social protection recommendations

Achieving a resilient and inclusive recovery will require additional spending on social protection and reforms to current programs. Recommendations to improve the adequacy and efficiency of social protection spending are as follows:

First, PIC-9 countries should allocate more resources to social assistance, with a view to bringing spending towards the global average of 1.5 percent of GDP. There is a strong case for increasing spending on formal social assistance, given the vulnerability of the PIC-9 to shocks, the low levels of current spending, and international evidence of the positive impact that cash

transfer programs and related measures can have on the poor and vulnerable. Therefore, even in the context of overall fiscal consolidation, additional spending on social protection is justified. Increased spending, coupled with improved targeting, will expand both the coverage and adequacy of safety nets in PIC-9 countries.

Second, improving the targeting of social assistance will reduce poverty, especially when coupled with spending increases. Simulations suggest that poverty-targeted cash transfers can significantly impact poverty levels, with spending of 1.5 percent of GDP halving poverty in Samoa, Tonga, and RMI. Such transfers can be linked to productive inclusion and employment services.

In the case of Kiribati and RMI, the focus should be on improving the allocative efficiency of spending on copra subsidies. Such support is an inefficient way of targeting the poor, with benefits accruing unequally to those that have the ability and resources to harvest copra. The impacts on poverty of redirecting a portion of the copra subsidy towards cash transfer programs are very significant in both countries. In RMI, reverting to the 2016 copra price (US$0.30/pound) and using the associated US$3m (1.2 percent GDP) in savings on a poverty targeted cash transfer program would more than halve poverty (from 7.2 to 3.4 percent of households). In Kiribati, reverting to the 2021 copra subsidy ($A 2/kilo) and channeling the $A 20 million (7.3 percent of GDP) of fiscal savings via a similar program would reduce the share of households in poverty by 72 percent (from 21.9 to 6.1 percent of households). Alternatively, a poverty targeted social assistance program costing only $A 4.4 million (1.6 percent of GDP) could achieve the same reduction in poverty as the doubling of the copra price implemented this year, while also generating a fiscal saving of $A 15.6 million (5.7 percent of GDP).

Third, investments in social assistance programs and delivery systems are needed to facilitate improved support to the poor and vulnerable. Improved collection and use of information on the socioeconomic situation of poor and vulnerable households is crucial, with the establishment of consolidated social registries of households and their information (including payment details) important in the long term to helping the PIC-9 respond to future shocks through adaptive social assistance support.

Fourth, there is also a case for PIC-9 countries to invest in employment and productive inclusion services, which are currently either absent or very limited in reach and scope, and to link these to an expansion of social assistance. Such programs (which combine cash grants and skills training) can help to both overcome political opposition to cash transfers, while also making social assistance programs more sustainable by providing exit strategies and support for beneficiaries to move into self-employment and wage employment. The case for increased spending is especially compelling for services related to labor mobility and migration, given its significant returns. For Kiribati, Tuvalu, Tonga, Vanuatu, Samoa, and Nauru, labor mobility-related employment services can both ensure that the most is made of preferential access to the Australian and New Zealand labor markets, while also supporting reintegration of returning workers. For FSM, RMI, and Palau—where citizens have open access to the United States—the focus should be on training and education that will improve outcomes for migrants. A priority is to ensure that skills and vocational education and training meet the needs of employers. Labor market intermediation services, informed by up-to-date assessments of labor market demand for skills, can assist. Reforms to lower the costs of sending and receiving remittances can also help to maximize the societal benefits of labor mobility and migration.

Finally, country-specific reforms to social insurance across the PIC-9 can help to improve sustainability, coverage, and adequacy. In general, FSM, RMI, and Palau with defined benefits schemes should prioritize the sustainability of their schemes, given past challenges in this area coupled with large-scale migration. In the case of defined contribution schemes that exist in other PIC-9 countries, the priorities are (in)adequacy of pension savings and in some cases low levels of coverage, which are particularly evident in the informal sector. Age of retirement, contributions, investment performance, rules relating to withdraw, and the formalization of employment are important determinants. Reform of social insurance is complex and specific to country context, so any changes should be preceded by detailed actuarial studies. However, analysis indicates that the following areas should be studied in the six PIC-9 with defined contribution schemes—Kiribati, Nauru, Tonga, Samoa, Vanuatu, and Tuvalu (although Nauru only recently established their Superannuation Fund, so parametric changes should be avoided in the immediate future): (i) an increase in the retirement age; (ii) withdrawal provisions and limits (for early retirement, unemployment, disability, economic shock)—including the introduction of these in countries where they do not currently exist; (iii) the form of payouts and implications for adequacy; and (iv) the age of eligibility for non-contributory social assistance (social pensions).

The role of development partners

Given the PIC-9's structural aid dependence, the volume, terms, and modality of developing partner financing have a critical role to play in supporting fiscal sustainability and a human capital transformation in the PIC-9. Grants finance one-third of government spending across the PIC-9, on average. As a result, development partner decisions and the design of their financial support have a significant impact on PIC-9 public finances and service delivery. In some cases, these introduce or exacerbate rigidities and inefficiencies in PIC-9 budget processes, contributing to sub-optimal results. In addition, achieving the region's development goals and enhancing resilience to climate change will require considerable financing over the medium term.

Development partner recommendations

Recommendations for development partners are as follows:

i. **First, development partners should seek to maintain the volume of financial support** at least at pre-COVID-19 levels.

ii. **Second, all financing should be highly concessional,** and on grant terms for the six PIC-9 countries rated at a high risk of debt distress under the IMF/World Bank Debt Sustainability Analysis (DSA).

iii. **Third, to the extent possible, financing should be 'on plan', 'on budget', and 'on system'.** That is, development partner-financed activities should be reflected in the government's annual work plans, financing should be recorded in the government's budget, and funds should flow through the government's own budgetary and financial systems.

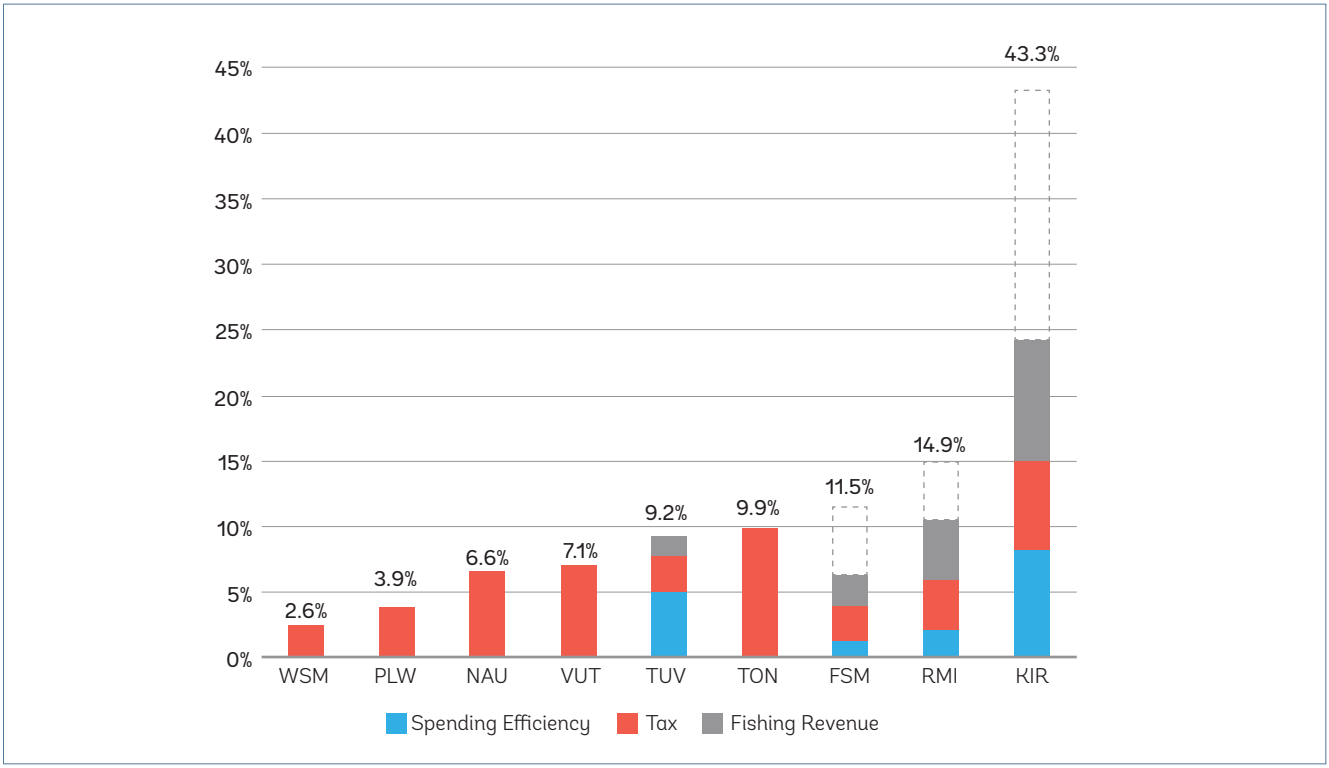
iv. **Fourth, development partner financing modalities should be long term and flexible,** to avoid introducing rigidities, inefficiencies, and volatility that limit the responsiveness of PIC-9 public spending to emerging priorities.

v. **Finally, improving the efficiency of PIC-9 health, education, and social protection systems will require concerted efforts by development partners** to: (i) build PIC-9 governments' capacity for project management and implementation; (ii) provide long-term complementary capacity to support local capacity, not just short-term technical assistance; (iii) enhance donor coordination (including through joint projects); and (iv) consider increasing the role of budget support to complement project financing.

Conclusion: Building human capital during fiscal consolidation

The reforms identified in this report could deliver a fiscal impact of 3–43 percent of GDP for each of the PIC-9 (Figure ES2). Tables ES1–9 summarize the measures identified and their estimated fiscal impact, where feasible, for each of the PIC-9. Combined, the estimated revenue gains and spending efficiency savings represent total potential annual fiscal impacts ranging from 2.6 percent of GDP in Samoa to 43.3 percent of GDP in Kiribati. These figures do not include reforms for which the potential fiscal impact could not be quantified at this time (for example, improving the efficiency of OMR schemes). The overall potential fiscal impacts could, therefore, be even higher. Additionally, by focusing on social sector spending, this PER analyzes spending that accounts for 28–45 percent of total government spending across the PIC-9 (except Nauru, where it is only 16 percent). Additional efficiency gains may also be feasible in the spending not analyzed in this PER. Tables ES 1–9 also highlight specific areas where this additional fiscal space could be prioritized to improve human capital outcomes and livelihoods, supporting a diversification in the drivers of economic growth. The reforms can also underpin a medium-term fiscal adjustment which can simultaneously meet the region's large development spending needs, while managing the risk of debt distress and rebuilding fiscal buffers to prepare for future shocks. A recommended timeframe for each reform is also provided. These recommendations reflect the complexity of several reforms and the need to prioritize reform efforts given the PIC-9 governments' limited capacity and varying economic contexts. These are summarized as short term (in the next 2 years), medium term (2–4 years), and longer term (4+ years). By implementing the measures outlined in this report, the PIC-9 can emerge stronger from the pandemic and recent overlapping shocks from natural disasters and inflation.

Figure ES2: Reform recommendations could deliver a fiscal impact of 3–43 percent of GDP for each of the PIC-9



Note: Spending efficiency measures refer to the education, health, and social protection sectors. For fishing revenues, the solid bars represent the estimated minimum impact of the reforms, while the dotted bar represents the estimated maximum impact.

Table ES1:
Summary of Policy Actions and Potential Fiscal Impact

KIRIBATI

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Close part of the VAT gap, through (i) lowering VAT threshold; (ii) rationalizing VAT exemptions; (iii) easing the VAT admin burden (e-filing, e-payment, and timely VAT refunds)	*Commence admin reforms in short term, continuing policy reforms over medium term*	Up to US$10.7m	5.2%
	Tax	2. Improve CIT productivity, through a focus on compliance management, including: (i) rolling out e-filing and e-payment; (ii) enforcing on-time filing; (iii) dedicated focus on compliance management of largest businesses	*Develop medium-term strategy, but begin implementing in short term*	Up to US$1.9m	0.9%
	Tax	3. Increase the VAT statutory rate in line with peers	*Medium term (2–4 years)*	For every 1 pp increase in VAT rate	
				Up to US$1.2m	0.6%
	Fishing Revenue	4. Regional reform to increase flexibility and transferability of a PNA VDS day (pooling, duration, transferability)	*Longer term*	US$19.1–58.3m	9.3–28.3%
Spending Efficiency Measures	Education	5. Based on Kiribati's size and dispersion, simulations suggest that spending per student (unit costs) could be at least 13 percent lower. Savings are most likely to be feasible in overseas scholarships, private subsidies and school grants, and school operational costs	*Complete detailed studies in the short term, reform in the medium to longer term*	US$5.8m	2.8%
	Health	6. Undertake a detailed analysis of spending and options to reduce unit costs of the overseas medical referral scheme (including potential multi-country agreements)	*Short term*	Lower spending on overseas medical referrals	
	Health	7. Strengthened supply chain management, planning and procurement for key pharmaceuticals and medical supplies could reduce costs by up to 30 percent	*Medium term*	US$0.7m	0.4%

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Spending Efficiency Measures	Social Protection	8. Doubling the copra price to $A 4/kilo is simulated to reduce national poverty by 3.8 percentage points (from 21.9 percent to 18.1 percent). Reverting to the 2021 copra subsidy ($A 2/kilo) and directing $A 20 million (7.3 percent of GDP) in fiscal savings to a poverty-targeted social assistance program would reduce poverty by almost three-quarters (from 21.9 percent to 6.1 percent of households).[8] Alternatively, the authorities could achieve the same level of poverty reduction as the $A 4/kilo copra price by channeling $A 4.4 million (1.6 percent of GDP) into a poverty-targeted social assistance program—creating fiscal savings of $A 15.6 million (5.7 percent of GDP)	*Complete detailed studies in the short term, reform in the medium term*	Reduce national poverty by almost three-quarters (from 21.9 percent to 6.1 percent) with no fiscal saving **OR** Reduce national poverty by 3.8 percentage points (from 21.9 percent to 18.1 percent) AND save US$11.7 (5.7 percent of GDP)	
	All	**Overall Revenue/Efficiency Impacts**		**US$39.4–90.4m**	**19.1–43.9% GDP**
Quality of Spending Measures	Education	9. Assess the economic returns, equity, and efficiency of tertiary scholarship and allowance spending	*Short term*	Improve efficiency and equity of scholarship spending	
	Education	10. Consider extending teaching in vernacular language at least until the end of primary school to help accelerate learning	*Medium term*	Improve education quality	
	Health	11. Accelerate roll out and monitoring of role delineation policies to progress Universal Health Coverage	*Short term*	Strengthen quality and coverage of care	
	Social Protection	12. Following detailed actuarial studies, consider: (i) increasing the retirement age from 50 to 65 with a transition and eliminating early withdrawal at age 45; and (ii) reviewing withdrawal provisions and limits (for unemployment, disability, economic shock)	*Medium to longer term*	Strengthen adequacy and sustainability of pension scheme	
Other Measures	Public Financial Management	13. Consider establishing an accumulation rule for the Revenue Equalization Reserve Fund to reduce procyclicality of public spending	*Medium term*	Enhance fiscal sustainability	

8. Assumes targeting to the bottom 20 percent of the income distribution, with 20 percent inclusion and exclusion errors.

NAURU

Table ES2:
Summary of Policy Actions and Potential Fiscal Impact

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Introduce a broad consumption tax	*Medium term (2–4 years)*	Up to US$8.8m	6.6%
	Fishing Revenue	2. Regional reform to increase flexibility and transferability of a PNA VDS day (pooling, duration, transferability)	*Longer term (4+ years)*	Potential positive impact	
Spending Efficiency Measures	Education	3. Teacher remuneration appears high and class sizes are declining fast, so rationalization may be needed in the medium to longer term	*Medium to longer term*	Improve spending efficiency	
	Health	4. Undertake a detailed analysis of spending and options to reduce unit costs of the overseas medical referral scheme (including potential multi-country agreements)	*Short term (<2 years)*	Lower spending on overseas medical referrals	
Quality of Spending Measures	Social Protection	5. Invest in social assistance programs and delivery systems to support the poor and vulnerable; with a view to moving towards spending of 1.5 percent of GDP in the longer term. These should be linked to employment and productive inclusion services where possible	*Commence in the short term, continuing over medium and longer term*	Develop social assistance programs and related services	
	Social Protection	6. Avoid parametric changes in the short term. In the future, following detailed actuarial studies, consider increasing the retirement age from 55 to 65 and introducing early withdrawal provisions for hardship/shocks	*Longer term*	Strengthen adequacy and sustainability of pension scheme	

RMI

Table ES3: Summary of Policy Actions and Potential Fiscal Impact

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Strengthen tobacco taxation by raising rates and simplifying tariff structure	*Short term (<2 years)*	Raise revenue and reduce health impacts	
Revenue Measures	Tax	2. Move from Gross Revenue Tax to a VAT with a broad base (low threshold and limited exemptions)	*Medium term (2–4 years)*	Up to US$9.3m	3.6%
Revenue Measures	Tax	3. Strengthen property tax collection to the level of peers	*Medium term (2–4 years)*	Up to US$0.5m	0.2%
Revenue Measures	Fishing Revenue	4. Regional reform to increase flexibility and transferability of a PNA VDS day (pooling, duration, transferability)	*Longer term (4+ years)*	US$11.6–23.1m	4.5–8.9%
Spending Efficiency Measures	Education	5. Based on RMI's size and population dispersion, simulations suggest that unit costs could be 14 percent lower. Savings are most likely to be feasible in capital spending and school operational costs	*Complete detailed studies in the short term, reform in the medium to longer term*	US$5.7m	2.2%
Spending Efficiency Measures	Health	6. Undertake a detailed analysis of spending and options to reduce unit costs of the overseas medical referral scheme (including potential multi-country agreements)	*Short term*	Lower spending on overseas medical referrals	
Spending Efficiency Measures	**All**	**Overall Revenue/Efficiency Impacts**		**US$27.2–38.7m**	**10.5–14.9% GDP**

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Quality of Spending Measures	Education	7. Assess the economic returns, equity, and efficiency of tertiary scholarship spending. Consider alternative selection criteria to improve equity and align to domestic skill needs	*Short term*	Improve efficiency and equity of scholarship spending	
	Education	8. Increase spending in Early Childhood Education to expand access (currently 18 percent of children aged 3–5 years)	*Medium term*	Improve acccess to Early Childhood Education	
	Health	9. Develop national policies to progress Universal Health Coverage (such as Role Delineation Policies or Packages of Essential Health Services)	*Short term*	Strengthen strategic management of health resources	
	Social Protection	10. Reverting to the 2016 copra subsidy (US$0.30/pound) and directing the US$3 million (1.2 percent of GDP) in fiscal savings to a poverty-targeted social assistance program would more than halve national poverty[9]	*Complete detailed studies in the short term, reform in the medium term*	Reduce national poverty by more than half (from 7.2 percent to 3.4 percent)	
Other Measures	Public Financial Management	11. Seek reform to the RMI Compact Trust Fund distribution rule to mitigate against market volatility resulting in unstable annual distributions	*Short term*	Enhance fiscal sustainability	

9. Assumes targeting to the bottom 10 percent of the income distribution, with 20 percent inclusion and exclusion errors.

FSM

Table ES4: Summary of Policy Actions and Potential Fiscal Impact

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Strengthen tobacco taxation by raising rates and simplifying tariff structure	*Short term (<2 years)*	Raise revenue and reduce health impacts	
	Tax	2. Collect more from PIT, through adding a new top PIT rate, rationalizing exemptions, and/or improvements in compliance management	*Develop medium-term strategy, begin implementing in short term*	Up to US$1.2m	0.3%
	Tax	3. Improve productivity of CIT, through (i) lowering CIT threshold; (ii) improving compliance management; (iii) rolling out CIT e-filing and e-payment	*Commence admin reforms in short term, continuing policy reforms over medium term*	Up to US$2.0m	0.5%
	Tax	4. Move from Gross Revenue Tax to a VAT with a broad base (low threshold and limited exemptions)	*Medium term (2–4 years)*	Up to US$7.7m	1.9%
	Fishing Revenue	5. Regional reform to increase flexibility and transferability of a PNA VDS day (pooling, duration, transferability)	*Longer term (4+ years)*	US$9.2–30.7m	2.3–7.5%
Spending Efficiency Measures	Education	6. Based on FSM's size and population dispersion, simulations suggest that unit costs could be 14 percent lower. However, realizing these savings may be challenging, given the decentralized system where many administrative costs are duplicated at the federal and state level	*Complete detailed studies in the short term, reform in the medium to longer term*	US$5.3m	1.3%
	Health	7. Undertake a detailed analysis of spending and options to reduce unit costs of the overseas medical referral scheme (including potential multi-country agreements)	*Short term*	Lower spending on overseas medical referrals	
	All	**Overall Revenue/Efficiency Impacts**		**US$25.5–47.0m**	**6.3–11.5% GDP**

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Quality of Spending Measures	Social Protection	8. Invest in social assistance programs and delivery systems to support the poor and vulnerable; with a view to moving towards spending of 1.5 percent of GDP in the long term. These programs should be linked to employment and productive inclusion services where possible	*Commence in the short term, continuing over medium and longer term*	Develop social assistance programs and related services	
Other Measures	Public Financial Management	9. Seek reform to the FSM Compact Trust Fund distribution rule to mitigate against market volatility resulting in unstable annual distributions	*Short term*	Enhance fiscal sustainability	

PALAU

Table ES5:
Summary of Policy Actions and Potential Fiscal Impact

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Increase the VAT statutory rate in line with peers	*Medium term (2–4 years*	For every 1 percentage point increase in VAT rate	
				Up to US$1.1m	0.5% GDP
	Tax	2. Introduce a CIT regime	*Medium term (2–4 years)*	Up to US$6.8m	3.2% GDP
	Fishing Revenue	3. Regional reform to increase flexibility and transferability of a PNA VDS day (pooling, duration, transferability)	*Longer term (4+ years)*	Potential positive impact	
Spending Efficiency Measures	Health	4. Strengthened supply chain management, planning and procurement for key pharmaceuticals and medical supplies could reduce costs by up to 30 percent	*Short term (<2 years)*	US$0.4m	0.2% GDP
	All	**Overall Revenue/Efficiency Impacts**		**US$8.3m**	**3.9% GDP**
Quality of Spending Measures	Education	5. Assess the economic returns, equity, and efficiency of tertiary scholarship spending	*Short term*	Improve efficiency and equity of scholarship spending	
	Social Protection	6. Invest in social assistance programs and delivery systems to support the poor and vulnerable; with a view to moving towards spending of 1.5 percent of GDP in the long term. These programs should be linked to employment and productive inclusion services where possible	*Commence in the short term, continuing over medium and longer term*	Develop social assistance programs and related services	
	Social Protection	7. Following detailed actuarial studies, consider parametric reforms to both national pension systems	*Medium term*	Strengthen sustainability of pension funds	

Table ES6:
Summary of Policy Actions and Potential Fiscal Impact

SAMOA

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Improve productivity of CIT through rationalization of CIT incentives, strengthening anti-tax avoidance measures, and improvements in compliance management	*Develop medium-term strategy, begin implementing in short term (<2 years)*	US$16.9m	2.0%
Revenue Measures	Tax	2. Strengthen property tax collection to the level of peers	*Medium term (2–4 years)*	US$3.4m	0.4%
Spending Efficiency Measures	Health	3. Strengthened supply chain management, planning and procurement for key pharmaceuticals and medical supplies could reduce costs by up to 30 percent	*Short term*	US$1.5m	0.2%
	All	**Overall Revenue/Efficiency Impacts**		**US$21.8m**	**2.6% GDP**

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Quality of Spending Measures	Education	4. Additional classrooms and at least 33 percent more teachers are needed to meet the 30 pupil/teacher ratio maximum in public primary schools. Fiscal implications should be carefully assessed	*Complete detailed studies in the short term, reform in the medium term*	Support improved learning outcomes	
	Education	5. Increase spending in Early Childhood Education to expand access (currently 30 percent of children aged 3–5 years)	*Medium term*	Improve access to Early Childhood Education	
	Education	6. Consider extending teaching in vernacular language at least until the end of primary school to help accelerate learning	*Medium term*	Improve education quality	
	Education	7. Large subsidies to private schools and school grants make teacher remunerations not transparent. They should be phased out while training spending should be increased	*Medium term*	Higher spending efficiency and teacher quality	
	Social Protection	8. Invest in social assistance programs and delivery systems to support the poor and vulnerable; with a view to moving towards spending of 1.5 percent of GDP in the long term. This should involve gradual reform of existing programs, aimed at improving impacts on poverty, and linkages to employment and productive inclusion services where possible	*Commence in the short term, continuing over medium and longer term*	Develop social assistance programs and related services	
	Social Protection	9. Following detailed actuarial studies, consider increasing the retirement age from 55 to 65, and increasing the early retirement age from 50 to 55	*Medium to longer term*	Strengthen adequacy and sustainability of pension scheme	

TONGA

Table ES7:
Summary of Policy Actions and Potential Fiscal Impact

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Reduce tax exemptions and zero ratings on consumption tax, excise tax, and customs duties, particularly for SOE fuel imports	*Commence in the short term (<2 years), continuing over medium term (2–4 years)*	Up to US$31.0m	6.2%
	Tax	2. Improve VAT compliance management through administrative reforms	*Develop medium-term strategy, but begin implementing in short term*	US$16.0m	3.2%
	Tax	3. Strengthen property tax collection to the level of peers	*Longer term*	US$2.0m	0.4%
Spending Efficiency Measures	Health	4. Strengthened supply chain management, planning and procurement for key pharmaceuticals and medical supplies could reduce costs by up to 30 percent	*Short to medium term*	US$0.7m	0.1%
	All	**Overall Revenue/Efficiency Impacts**		**US$49.7m**	**9.9% GDP**

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Quality of Spending Measures	Education	5. Large subsidies to private schools and school grants reduces the transparency of teacher remunerations and are inefficient. They should be reviewed and connected more strongly with enrollment	*Complete detailed studies in the short term, reform in the medium term*	Higher spending efficiency and better allocation of resources	
	Education	6. Assess the economic returns, equity, and efficiency of tertiary scholarship and allowance spending	*Short term*	Improve efficiency and equity of scholarship spending	
	Education	7. Increase spending in Early Childhood Education to expand access (currently only at 34 percent of children aged 3–5 years)	*Medium term*	Improve access to Early Childhood Education	
	Education	8. Consider extending teaching in vernacular language at least until the end of primary school to help accelerate learning	*Medium term*	Improve education quality	
	Health	9. Accelerate roll out and monitoring of packages of essential health services to progress Universal Health Coverage	*Short term*	Strengthen quality and coverage of care	
	Social Protection	10. Invest in social assistance programs and delivery systems (including the development of a social registry) to support the poor and vulnerable; with a view to moving towards spending of 1.5 percent of GDP in the long term. This should involve gradual reform of existing programs, aimed at improving impacts on poverty, and linkages to employment and productive inclusion services where possible	*Commence in the short term, continuing over medium and longer term*	Develop social assistance programs and related services	
	Social Protection	11. Following detailed actuarial studies, consider: (i) increasing the retirement age from 60 to 65, contingent on review of the early withdrawal provisions; and (ii) introducing a cap on withdrawals due to unemployment	*Longer term*	Strengthen adequacy and sustainability of pension scheme	

Table ES8:
Summary of Policy Actions and Potential Fiscal Impact

TUVALU

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Strengthen tobacco taxation by raising rates and simplifying tariff structure	*Short term (<2 years)*	Raise revenue and reduce health impacts	
	Tax	2. Improve CIT efficiency, including by (i) updating the CIT register; (ii) rolling out CIT e-filing and e-payment; (iii) enforcing on-time filing	*Develop medium-term strategy, but begin implementing in short term*	Up to US$1.5m	2.4%
	Tax	3. Increase the VAT statutory rate in line with peers	*Medium term (2–4 years)*	For every 1 percentage point increase in VAT rate	
				Up to US$0.2m	0.3%
	Fishing Revenue	4. Regional reform to increase flexibility and transferability of a PNA VDS day (pooling, duration, transferability)	*Longer term (4+ years)*	Up to US$0.9m	1.4%
Spending Efficiency Measures	Education	5. Based on Tuvalu's smallness and dispersion, simulations suggest that unit costs could be 23 percent lower. Savings are most likely to be feasible in overseas scholarships and school operational costs	*Complete detailed studies in the short term, reform in the medium to longer term*	US$3.0m	4.8%
	Health	6. Strengthened supply chain management, planning and procurement for key pharmaceuticals and medical supplies could reduce costs by up to 30 percent	*Short to medium term*	US$0.2m	0.3%
	Health	7. Undertake a detailed analysis of spending and options to reduce unit costs of the overseas medical referral scheme (including potential multi-country agreements)	*Short term*	Lower spending on overseas medical referrals	
	All	**Overall Revenue/Efficiency Impacts**		**US$5.8m**	**9.2% GDP**

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Quality of Spending Measures	Education	8. Assess the economic returns, equity, and efficiency of tertiary scholarship spending. Consider alternative models, such as flying in educators	*Complete detailed studies in the short term, reform in the medium term*	Improve efficiency and equity of scholarship spending	
	Education	9. Consider extending teaching in vernacular language at least until the end of primary school to help accelerate learning	*Medium term*	Improve education quality	
	Social Protection	10. Invest in social assistance programs and delivery systems to support the poor and vulnerable; with a view to moving towards spending of 1.5 percent of GDP in the long-term. This should involve gradual reform of existing programs, aimed at improving impacts on poverty, and linkages to employment and productive inclusion services where possible	*Commence in the short term, continuing over medium and longer term*	Develop social assistance programs and related services	
	Social Protection	11. Following detailed actuarial studies, consider increasing the eligibility age to receive a lump-sum benefit, balancing this against the incentive for compliance with the relatively high contribution rate	*Medium to longer term*	Strengthen adequacy and sustainability of pension scheme	
Other Measures	Public Financial Management	12. Consider establishing an accumulation rule for the Tuvalu Trust Fund to reduce procyclicality of public spending	*Medium term*	Enhance fiscal sustainability	

VANUATU

Table ES9:
Summary of Policy Actions and Potential Fiscal Impact

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Revenue Measures	Tax	1. Improve VAT efficiency to the level of Samoa, focusing on improvements in compliance management	*Develop medium-term strategy, but begin implementing in short term (<2 years)*	US$11.3m	1.2%
	Tax	2. Introduce a PIT regime	*Medium term (2–4 years)*	US$24.5m	2.6%
	Tax	3. Introduce a CIT regime	*Longer term (4+ years)*	US$30.1m	3.2%
Spending Efficiency Measures	Health	4. Strengthened supply chain management, planning and procurement for key pharmaceuticals and medical supplies could reduce costs by up to 30 percent	*Short to medium term*	US$0.6m	0.1%
	All	**Overall Revenue/Efficiency Impacts**		**US$66.5m**	**7.1% GDP**

	Sector	Policy Action	Recommended Timing	Potential Impact	
				US$	%GDP
Quality of Spending Measures	Education	5. Increase spending in Early Childhood Education to expand access (currently 43 percent of children aged 3–5 years)	*Medium term*	Improve access to Early Childhood Education	
	Education	6. Consider extending teaching in vernacular language at least until the end of primary school to help accelerate learning	*Medium term*	Improve education quality	
	Health	7. Accelerate roll out and monitoring of role delineation policies to progress Universal Health Coverage	*Short term*	Strengthen quality and coverage of care	
	Social Protection	8. Invest in social assistance programs and delivery systems to support the poor and vulnerable; with a view to moving towards spending of 1.5 percent of GDP in the long-term. These programs should be linked to employment and productive inclusion services where possible	*Commence in the short term, continuing over medium and longer term*	Develop social assistance programs and related services	
	Social Protection	9. Following detailed actuarial studies, consider: (i) increasing the eligibility age from the retirement savings account from 55 to 65; and (ii) reviewing the withdrawal conditions for retirement, Medisave, and Investment accounts	*Longer term*	Strengthen adequacy and sustainability of pension scheme	
Other Measures	Education	10. Although school grants are large, they are transparent and have been reviewed as effective. But a recent household survey indicates that parents, even the poorest ones, are still paying considerable amounts in school fees to cover costs that should be paid for by the school grants. These fees should be formally eliminated and enforced	*Short term*	Improve education access and equity	
	Public Financial Management	11. Consider establishing a Sovereign Wealth Fund financed by revenues from the Economic Citizenship Program	*Short term*	Enhance fiscal sustainability