

**PROGRAM INFORMATION DOCUMENT (PID)
APPRAISAL STAGE**

June 23, 2016
Report No.:

Operation Name	Samoa Second Fiscal and Economic Reform Operation
Region	East Asia and Pacific
Country	Samoa
Sector	Central government administration (50%) Public administration – industry and trade (33%) Payments, settlements and remittance systems (17%)
Operation ID	P155118
Lending Instrument	Development Policy Lending
Borrower(s)	Independent State of Samoa
Implementing Agency	Ministry of Finance and Economic Development
Date PID Prepared	June 23, 2016
Estimated Date of Appraisal	July 15, 2016
Estimated Date of Board Approval	August 30, 2016
Corporate Review Decision	Following the corporate review, the decision was taken to proceed with the preparation of the operation.

I. Country and Sector Background

As a very small remote economy that is highly vulnerable to external shocks, Samoa illustrates many of the constraints facing even well-performing small island states. Samoa's 189,000 residents live on two main islands located approximately 3,000km from New Zealand and 4,000km from Australia. As is the case in other Pacific Island Countries, the small size of the domestic economy and its extreme remoteness from major markets push up the costs of economic activity, as economies of scale cannot be realized in domestic production and transport costs significantly increase the cost of trade. Moreover, Samoa's narrowly-based economy and vulnerability to exogenous shocks and natural disasters have led to a high degree of volatility in economic performance, particularly in recent years.

Given these geographic constraints, remittances, tourism, and aid flows are critical to improving livelihoods and supporting the domestic economy. Remittances from Samoans living and working abroad, which have averaged around a quarter of GDP over the last four years, are vital to the livelihoods of the resident population. Tourism is also an important contributor to the economy of Samoa, with its distinctive geographical and cultural features allowing premium prices to be charged that are sufficient to cover relatively high costs.

In recent years, economic growth in Samoa has been low and volatile, as the country slowly recovers from a series of major external shocks, including the global financial crisis, a tsunami in 2009, and Cyclone Evan in December 2012. The government responded to this succession of shocks by increasing public expenditures, which supported growth but also led to

significant increases in public debt. In this context, consolidating the fiscal situation and returning the economy to a more robust growth path are a formidable challenge.

II. Operation Objectives

The proposed operation is structured around three development objectives: (i) to improve fiscal management in the areas of debt, procurement and revenue; (ii) to strengthen the payments system, tourism sector policy and private sector development opportunities as foundations for more robust economic growth over the medium term, and (iii) to strengthen the monitoring, reporting, and coordination of climate resilience activities in Samoa, as an important step toward increasing its resilience to the effects of climate change. The third objective is new to this operation and has been introduced in line with a priority of government: to improve its monitoring and coordination of the large number of policies and projects associated with building climate resilience. Contributing to the first objective, the operation will support reforms to ensure compliance with and review the implementation of the government's debt management strategy and procedures, improve value for money in expenditure by strengthening public procurement processes, and increase the efficiency of revenue collection. Contributing to the second objective, the proposed operation will support reforms to modernise the payments system, review and assess initiatives to boost tourism sector activity, and encourage private sector activity and more efficient service provision through SOE divestments. On the third objective, the operation will support reforms to strengthen the screening and monitoring of climate resilience activities, which will ultimately facilitate better-coordinated and less-fragmented climate resilience policies and projects, reducing the risk to vulnerable communities. In general, the actions in this Development Policy Operation (DPO) seek to support the government's focus on implementing reforms, following the substantial reform achievements supported by the first operation.

The development objectives and associated reform actions of the proposed operation are closely aligned with the priorities and strategic areas in the economic development pillar of the *Strategy for the Development of Samoa*. The first objective is also closely aligned with the government's own Public Financial Management reform plan, which is currently in the third 'roll-out' phase. In general, the operation is structured around key aspects of the government's program for which solid reform momentum exists: in these circumstances, DPOs in Samoa tend to achieve good results with manageable risks. The Ministry of Finance has a strong sense of ownership of each reform area, and considerable experience coordinating the actions of the other agencies whose engagement is needed to achieve these reforms.

III. Rationale for Bank Involvement

Following on from the substantial reforms supported by the first operation in the series, a second operation is the most appropriate mechanism to support implementation and next steps, especially the continued need for budget support in Samoa. Fiscal and monetary policies are broadly consistent with the prevailing economic conditions, and Samoa is implementing a plan to consolidate its fiscal position and return its debt to more sustainable levels over the medium-to-long term. Nevertheless, like many small island states, Samoa is

reliant on international development assistance, with grant aid flows averaging around 10 per cent of GDP over the past four years.

The second operation in this DPO series supports the government in its efforts to strengthen public finances, support growth, and foster climate resilience. The government recognizes that reforms to debt management, procurement and revenue collection will help it to achieve its fiscal consolidation objectives and rebuild the fiscal buffers it needs to respond to future external shocks. It also recognizes the importance of returning the economy to a more robust growth path and of boosting resilience to the effects of climate change and natural disasters, if it is to achieve the objective of the *Strategy for the Development of Samoa* of an ‘improved quality of life for all’. The second operation in this DPO series supports the achievement of these objectives, through a reform program for which the government has very strong ownership.

The operation follows the established good practice in the Pacific of using a joint donor matrix for budget support. The World Bank Group team has worked closely with the Asian Development Bank, the Australian Department of Foreign Affairs and Trade, and New Zealand Ministry of Foreign Affairs and Trade to prepare this operation. The team has also benefitted from close consultations with the IMF on the macroeconomic framework.

IV. Tentative Financing

Source:	(\$m)
Borrower/Recipient	0
International Development Association (IDA)	<u>5</u>
Total	5

V. Institutional and Implementation Arrangements

The Ministry of Finance will be responsible for coordinating the monitoring and evaluation of the results indicators for the proposed operation. The Ministry of Finance will directly monitor the results indicators for the actions on debt, procurement, and climate resilience, and will collaborate with the relevant agencies on the other indicators. The Ministry of Finance has demonstrated a good capacity to monitor and evaluate the results of budget support operations to date. Where possible, it will utilise existing systems for monitoring and evaluation purposes.

VI. Risks and Risk Mitigation

The main risks to the proposed operation stem from Samoa’s macroeconomic context, its thin institutional capacity, and its vulnerability to external shocks. Samoa faces a heightened overall risk of public debt distress, which will only be reduced through fiscal consolidation and sound debt management. Otherwise Samoa’s fiscal situation could become increasingly difficult to manage, which could lead to a shift in focus away from implementation of the longer-term reforms supported by this operation. Thin institutional capacity in Samoa could also hinder the implementation or sustainability of the supported reforms. Finally, if it experiences another major natural disaster, Samoa’s macroeconomic stability could be threatened, and large parts of

the bureaucracy will be required to focus their attention on disaster recovery and reconstruction efforts. While not all of these risks can be completely mitigated, the government's recent efforts and ongoing plans to consolidate its finances and maintain debt sustainability will mean it is in a stronger position to respond to a future economic shock or natural disaster. Better coordination and monitoring of climate-related projects and activities should also help to build climate resilience over the longer term.

VII. Poverty and Social Impacts and Environment Aspects

Poverty and Social Impacts

The supported reforms are important to prospects for boosting shared prosperity in Samoa. Returning Samoa to a situation where its fiscal position is both sustainable and has scope to respond to external shocks is particularly important for the poorest two quintiles of the population, which are disproportionately dependent on publicly-funded education, health and community development services and are the most vulnerable to any contraction in their provision in the event that the government lacks the means to respond to external shocks. They also tend to be the most vulnerable to the direct impacts of severe weather events, increasing their reliance on the government's capacity to respond through relief and reconstruction activities. The debt, procurement and revenue reforms being supported by this operation strengthen public financial management, assisting government efforts to consolidate its public finances and rebuild its fiscal buffers. While the poorest two quintiles are also more dependent on remittances than other quintiles, the current high costs of remittances should also decline over time as the payments system reforms supported by the operation are implemented.

Environment Aspects

The policy actions supported under the operation are not expected to create negative impacts on Samoa's environment, natural resources or forests. Policy actions related to debt policy and management, public procurement processes, revenue administration, and the national payments system are not expected to have any significant environmental impacts. Similarly, the actions relating to the revision of Samoa's tourism sector policy and state-owned enterprise policy are not expected to create negative environmental impacts. The policy action relating to the review of Samoa's tourism sector policy will mainly affect tourism promotion and associated market access arrangements, rather than physical works. To the extent that environmental impacts do arise from increased tourism, such impacts would be captured and managed by Samoa's environmental protection regime, which includes the Planning and Urban Management Act as the overarching legislative framework that governs all environmental and social safeguards. In general, Samoa's environmental protection regime is one of the strongest among Pacific Island countries, and has been strengthened over time by substantial project engagements and technical assistance from both the ADB and the World Bank. Reforms to improve the coordination and monitoring of climate-related projects and activities should also improve environmental outcomes over the longer term.

VIII. Contact point

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