

MALDIVES DEVELOPMENT UPDATE

TOWARDS RESILIENT AND AFFORDABLE HOUSING



October 2022

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Preface

The Maldives Development Update (MDU) has two main goals. First, it takes the pulse of the Maldivian economy by providing key developments over the past 12 months. Placing these in a global context, and based on these recent developments, it analyzes the outlook over the medium term. Second, the MDU provides a more in-depth investigation of selected economic and policy issues. It has a wide audience including policymakers, policy analysts from think tanks or non-governmental organizations, and business and financial sector professionals interested in Maldives' economic development.

The MDU was prepared by Richard Walker, Karishma Sheriff, Erdem Atas (*Macroeconomics, Trade and Investment, South Asia Region*) and Dao Harrison (*Urban Development, Southeast Asia Region*). The team is grateful to Upamanyu Datta (*Poverty*), Tatsiana Kliatskova (*Finance, Competitiveness and Innovation*), Namooos Zaheer (*Finance, Competitiveness and Innovation*), Biying Zhu (*Consultant, Macroeconomics, Trade and Investment*) and Francis Goyes (*Consultant, Urban Development*) for their input to the publication. The team thanks Mathew Verghis (*Director, Equitable Growth, Finance and Institutions - EFI, South Asia Region*), Faris Hadad-Zervos (*Country Director for Maldives, Nepal and Sri Lanka*), Chiyo Kanda (*Country Manager, Maldives and Sri Lanka*), Shabih Ali Mohib (*Practice Manager, Macroeconomics, Trade and Investment*), and Taehyun Lee (*Lead Country Economist, EFI*) for their guidance and comments. Sashikala Jeyaraj provided valuable administrative support and helped format and layout the report, while Shadiya Adam, Dilinika Peiris and Ali Naafiz led the dissemination efforts.

The report was prepared based on published data available on or before September 20, 2022. Data sources included the World Bank, International Monetary Fund, Ministry of Finance, Maldives Monetary Authority, Maldives Bureau of Statistics, Ministry of Tourism, and press reports.

Previous report editions:

- [April 2022: Maldives Development Update: Navigating Choppy Seas](https://openknowledge.worldbank.org/handle/10986/37662)
- [April 2021: Maldives Development Update: A Digital Dawn](https://openknowledge.worldbank.org/handle/10986/35832)

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Abbreviations

BML	Bank of Maldives
CAD	Current Account Deficit
CAR	Capital Adequacy Ratio
CPI	Consumer Price Index
COVID-19	Coronavirus Disease 2019
DHS	Demographic and Health Survey
EMDEs	Emerging Markets and Developing Economies
FDC	Fahi Dhiriulhun Corporation
FDI	Foreign Direct Investment
FRA	Fiscal Responsibility Act
GDP	Gross Domestic Product
GoM	Government of Maldives
GGST	General Goods and Services Tax
HDC	Housing Development Corporation Ltd.
HDFC	Housing Development Finance Corporation
HIES	Household Income and Expenditure Survey
ICBC	Industrial and Commercial Bank of China
IDR	Issuer Default Rating
LIBOR	London Inter Bank Offered Rate
MDU	Maldives Development Update
MIB	Maldives Islamic Bank
MMA	Maldives Monetary Authority
MNPHI	Ministry of National Planning, Housing and Infrastructure
MoF	Ministry of Finance
MPI	Multidimensional Poverty Index
MUDRP	Maldives Urban Development Resilient Program
MVR	Maldivian Rufiyaa
MPI	Multi-Dimensional Poverty Index
MRR	Minimum Reserve Requirement
NBS	National Bureau of Statistics
NDA	Net Domestic Assets
NPL	Non-performing loan
NFA	Net Foreign Assets
ODF	Overnight Deposit Facility
OLF	Overnight Lombard Facility
OMO	Open Market Operations
PPG	Public and Publicly Guaranteed
PPP	Public Private Partnership
PSPH	Public Sector Pay Harmonization
PSIP	Public Sector Investment Program
RBI	Reserve Bank of India
SDF	Sovereign Development Fund
SDG	Sustainable Development Goals
SOE	State-Owned Enterprise
STO	State Trading Organization
TGST	Tourism Goods and Services Tax
US\$	United States Dollar
y-o-y	year on year

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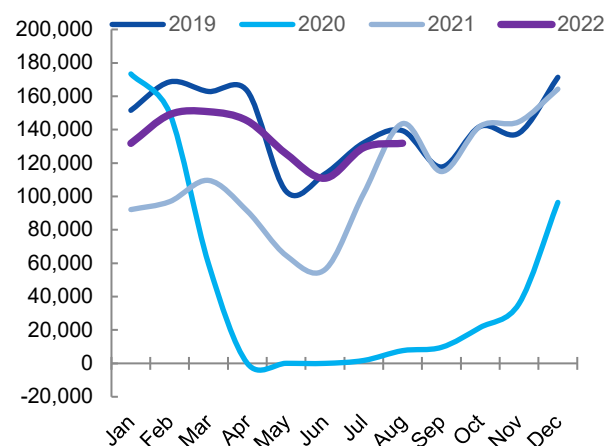
Executive Summary

A. Economic Update, Outlook and Risks

Driven by a rebound in tourism, Maldives' economy continued to recover strongly in 2022, and poverty is expected to return to pre-pandemic levels by end-2022. The number of tourist arrivals grew by 42.9 percent (y-o-y) in the first eight months of 2022 and are on course to reach the annual pre-pandemic high of 1.7 million (Figure ES.1). A decline in arrivals from Eastern Europe and Russia was offset by other markets, particularly Western Europe, India, and Middle East countries. Formal sector employment and wages also picked up with the strong economic rebound, but a weaker recovery of informal sector jobs is concerning, given the impact this might have on further increasing inequality in the country.

Figure ES.1: Real GDP continues to recover on the back of high tourist arrivals...

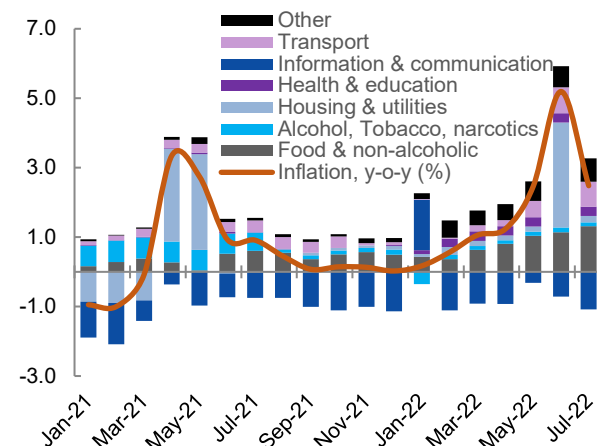
Total number of tourist arrivals



Source: Ministry of Tourism, staff calculations.

Figure ES.2: ...but inflation increased as food, utilities, and transport prices surged

Contributions to CPI growth, percentage points



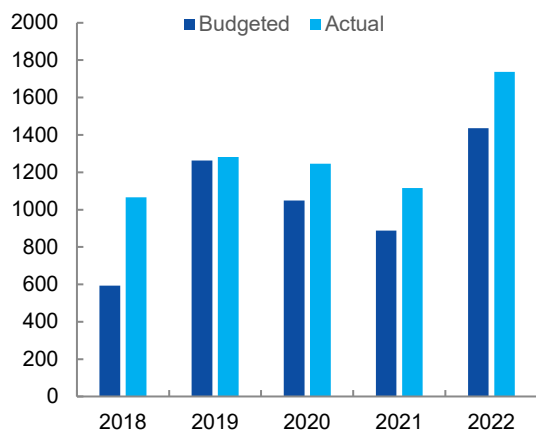
Source: Maldives Bureau of Statistics, WB staff calculations.

Maldives was hit by the surge in global commodity prices, putting pressure on domestic inflation, government's fiscal position and the balance of payments. Maldives' inflation climbed to 5.2 percent (y-o-y) in June 2022 before declining to 2.5 percent (y-o-y) in July 2022, compared to 0.5 percent in 2021 (Figure ES.2). Due to blanket subsidies provided on fuel and food items, government is facing significant pressure to continue financing the subsidy program in its current form (Figure ES.3). The merchandise trade deficit has widened considerably this year – with fuel imports climbing to over 14 percent of GDP in H12022 compared to on average 8 percent of GDP in the 2020-21 period. This is exerting considerable pressure on official reserves that have fallen by 9.6 percent since end-2021; declining to US\$728 million in July, and only sufficient to cover 2.7 months of imports compared to 3.8 months at end-2021 (Figure ES.7).

Despite the increase in, particularly, tourism related revenues, overall fiscal performance is being constrained by the sharp rise in subsidies and interest payments. Due to the increase in global commodity prices, government's spending on food and fuel subsidies, of US\$112 million in H12022, already substantially exceeds the US\$92 million that was budgeted for the whole of 2022. Interest payments have also jumped up and are already at US\$115 million or 3.8 percent of GDP for H12022, compared to the annual average of US\$85 million or about 2 percent of GDP in the 2014-19 period. This is being driven by the large increase in domestic interest payments and the additional burden of external commercial debt, which is likely to be even more demanding in the medium-term.

Figure ES.3: Actual subsidy spending already exceeds the amount budgeted for 2022...

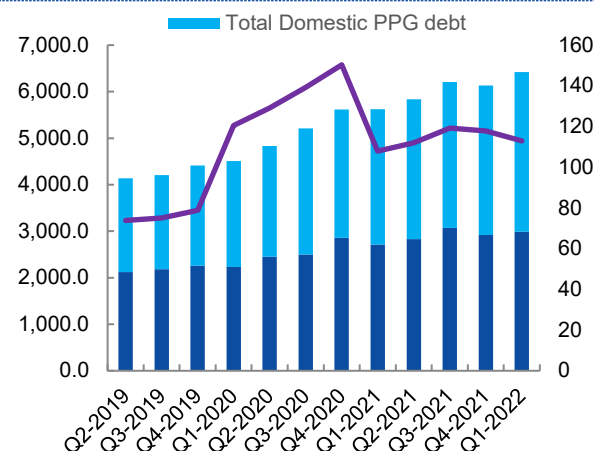
MVR million



Source: Ministry of Finance, World Bank staff calculations.

Figure ES.4: ...and public debt stock remains high

PPG in US\$ million and percent of GDP (rhs)

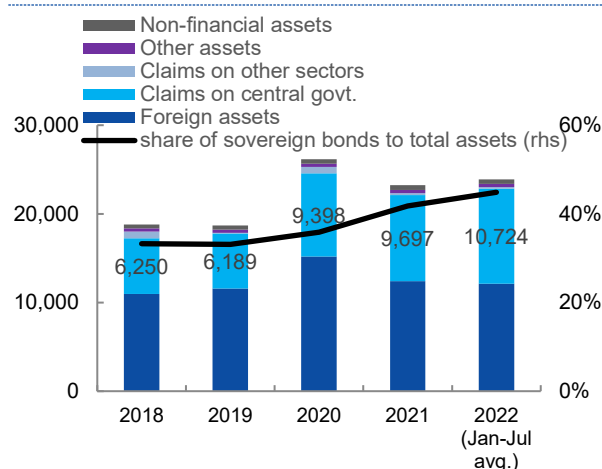


Source: Ministry of Finance, World Bank staff calculations.

Exposure to sovereign bond holdings remains high, as the Maldives Monetary Authority (MMA) increasingly finances the budget deficit. The temporary suspension of the Fiscal Responsibility Act (FRA), which has been extended until end-2023, has led to a significant increase in MMA’s claims on central government. The suspension allowed the Ministry of Finance (MoF) to overdraw MVR 4.4 billion (US\$286 million) from the MMA/public banks, which would normally be limited to MVR 170 million. As a result, MMA’s asset exposure (including Treasury bills and bonds, and advances) increased to 52.5 percent of its total financial assets at end-August 2022, from 42 percent at end-2021 (Figure ES.5). This has been mirrored by an increase in net claims on central government by commercial banks, with their sovereign exposure climbing from about 70 percent in 2019 to 83 percent in July 2022, further tightening the sovereign-banking system nexus. At the same time, growth in credit to the private sector has been decelerating (Figure ES.6).

Figure ES.5: MMA’s claims on central government continue to increase...

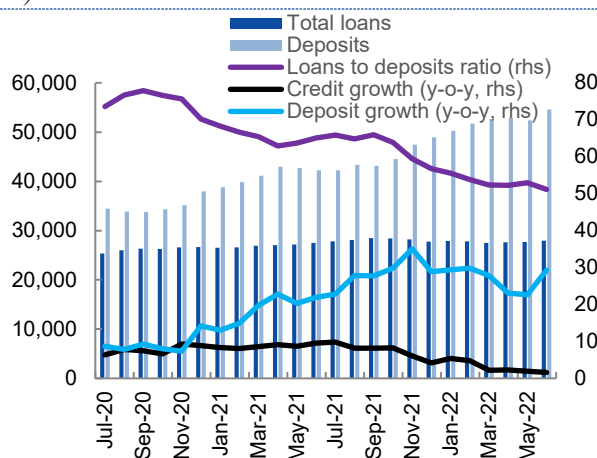
MVR million



Source: MMA, World Bank staff calculations.

Figure ES.6: ...while credit growth declined

Private sector credit and deposit growth, MVR million and percent (rhs)



Source: MMA, World Bank staff calculations.

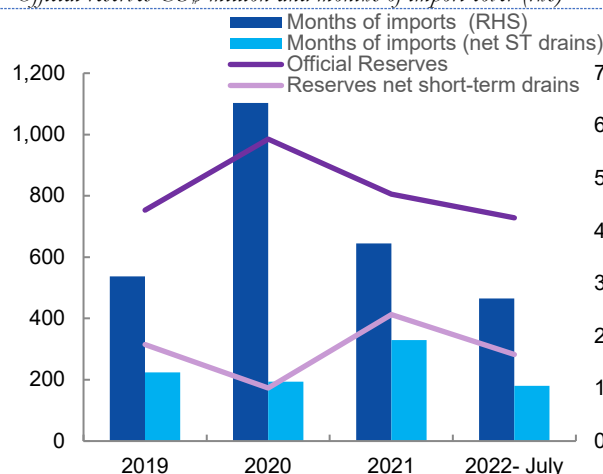
Public debt is at unprecedented levels, exceeding the size of Maldives’ entire economy. Total public and publicly guaranteed (PPG) debt stood at US\$6.1 billion or an estimated 118 percent of GDP at end-2021 (Figure ES.4). Domestic debt accounted for the bulk of total debt (62 percent of GDP), while external and

externally guaranteed debt accounted for the remainder (56 percent of GDP). These figures do not include the significant advances from MMA/public banks. Moreover, fiscal risks – mostly stemming from guaranteed and on-lent loans, as well as trade payables, subsidies, and capital injections to SOEs – were estimated at about US\$2.5 billion or 45 percent of GDP in 2019. While such risks have not materialized, Maldives lacks the fiscal space to address any potential fallout to public finances, should they occur.

External debt and fiscal vulnerabilities are a significant concern for Maldives in the medium term. The country is projected to pay, on average, US\$330 million annually as external debt servicing over the 2022-24 period (Figure ES.8). Debt servicing is then expected to reach US\$1 billion in 2026, which includes bullet payments for the US\$500 million Sukuk and US\$100 million private placement – significantly testing the country’s ability to repay or rollover this debt. The latter is also very much dependent on an improved global financing environment by 2026. While the government is taking steps to transfer certain revenues to the Sovereign Development Fund (SDF), which is designed to pay off some of the debt maturing, the limited resources in the fund may put Maldives in a difficult position and thereby further elevate the risk of not being able to service the debt.

Figure ES.7: Reserves depleting with jump in import bill...

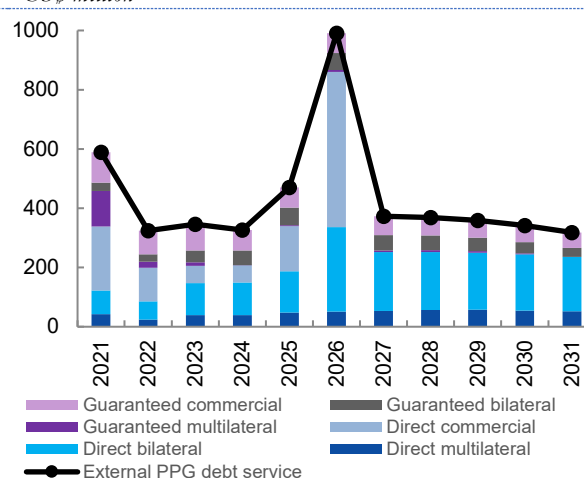
Official reserves US\$ million and months of import cover (rhs)



Source: MMA, World Bank staff calculations.

Figure ES.8: ...while there are significant external debt servicing needs in the medium-term

US\$ million



Source: Ministry of Finance and World Bank staff calculations.

Restoring fiscal and debt sustainability is critical for sustainable long-term growth. Government’s recently announced GST rate increases are a positive start, but not sufficient for the adjustment that is required. A notable reduction in (and more effective) spending is also required, especially for capital expenditures that are largely financed by external borrowing. These expenditure reforms, coupled with more effective revenue mobilization, are crucial to restore debt and fiscal sustainability. Reforms to Aasandha, reducing and rationalizing subsidies to SOEs, and better investment management – including in the housing sector – by considering PPP models, are amongst the key reform areas to bring down the high levels of public expenditure, replenish fiscal buffers against future shocks, and lower the cost of growth-enhancing investments. On the other hand, revenue mobilization can be further improved by diversifying the tax base and mobilizing more domestic sources of revenue, reducing informality, and enhancing the tax morale and equity of the tax system.

Although downside risks persist, the medium-term outlook is positive due to an increase in tourist arrivals, capital spending and private consumption. Real GDP growth is projected to be 12.4 percent in 2022 and 8.1 percent on average in the 2023-24 period. Inflation is expected to moderate as global commodity prices normalize. However, the existence of significant global uncertainties, as well as any additional global shock, poses substantial risk to this outlook, especially if there is a slowdown in key source countries for tourists. As a result, reducing the dependency on tourism and diversifying the economy remains a major

objective over the next few years. Maldives could benefit from a more diversified tourism sector that also provides benefits to those living in the outer Atolls and inhabited islands. Boosting the fisheries sector by expanding fish processing facilities and reaching new export markets could help reduce the country’s high dependency on tourism. Additional avenues for diversification, trade and growth also need to be explored.

B. Facilitating Affordable and Sustainable Housing Provision

As a small island state, Maldives faces unique affordable housing constraints. The scarcity of land, limited access to construction finance, and reliance on costly material imports are amongst the key drivers contributing to a severe gap in affordable housing supply. Internal migration to Greater Malé, drawn by its educational and employment opportunities, has led to overcrowding and densification in the capital, and with this, an unrelenting demand for affordable housing.

Housing ownership is unaffordable for most Maldivians, especially in the Greater Malé region, forcing the majority of the population to resort to renting. In part due to the country’s small island state unique constraints, home ownership is affordable only for the richest (top 20th percentile) of Maldivian households who can obtain access to a bank loan (Figure ES.9). Most households living in the Greater Malé region rely on rental units for their accommodation. According to the 2016/19 HIES, 74 percent of households living in Malé rented their homes in 2019, a sharp increase from 64 percent in 2016. Rental prices are also out of reach for many households and availability of units is scarce, leading multiple households to live together in overcrowded conditions.

Figure ES.9: Purchasing a home is out of the question for many Maldivians
In MVR

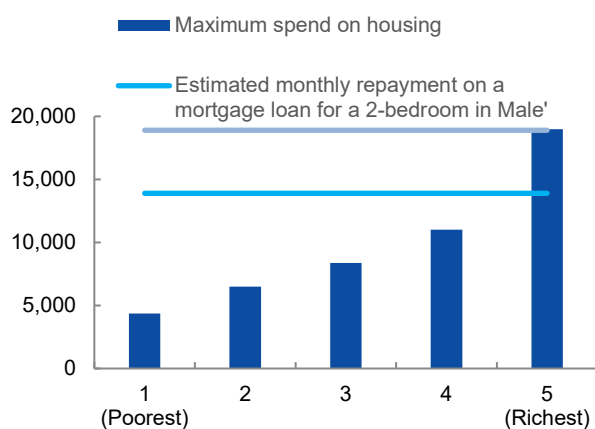
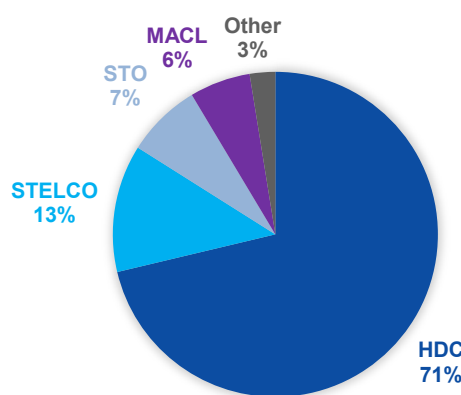


Figure ES.10: HDC accounts for over half of guaranteed debt to SOEs
Share of total external guaranteed debt, percent



Source: Staff calculations based on Statistics Maldives, 2021b and WB MUDRP.
Note: Flat price is assumed to be MVR 1.8 million. Monthly rent is assumed to be MVR 18,900.

Source: MOF 2020.
Note: Excludes the US\$400 million MMA swap with RBI and a US\$121 million guarantee to Ahmed Siyam Holding, a private entity.

Affordable housing for all Maldivians has long been a key government priority. The 2019-2023 Strategic Action Plan outlines ambitious policy actions to increase the accessibility and affordability of housing, including (i) the development of 20,000 new social housing units, and (ii) increased funding for the interest-rate subsidized housing loan scheme (*Gedborweriya*) to support construction and upgrade of homes in the atolls. To address land scarcity pressures, the Government of Maldives (GoM) has pursued land reclamation strategies around the capital city, notably in the neighboring island of Hulhumalé and in other key atolls.

However, such undertakings have been costly and have a detrimental impact on the fragile marine habitats surrounding the islands.

The affordable housing market is led by the Government, with minor engagement from the private sector. The GoM, along with its subsidiaries, has become the largest investor, developer, and operator of affordable housing in Maldives. To meet its affordable housing targets, the GoM has ramped up public investment over the last decade, at a high fiscal cost and long-term risk. Some of the key factors precluding private participation in the affordable housing sector are the costly and constricted access to domestic construction finance and a limited regulatory framework to mitigate lender risk.

There is an overlap in the roles of the key implementing agencies. To support implementation of the Rent-to-Own program, the Government has relied on two State-Owned Enterprises (SOE): the *Housing Development Corporation* (HDC) – the master developer of Hulhumale, Thilafushi and Gulhi Falhu – and the *Fabi Dhiruulhun Corporation* (FDC) – a new housing agency established in 2019 with the mission of taking on the bulk of social housing financing, development and implementation from HDC and MNPHI – Housing Department. Nonetheless, this transition has yet to take place and there is a risk of duplication and administrative overlap between HDC and FDC. The current implementation framework limits the efficiency and results of the government social housing programs.

The Rent-to-Own Program is the primary affordable housing scheme in Maldives. Under the Hulhumalé Phase 1 project, the Government built 5 projects totaling 2,592 housing units¹ (1, 2, 3 and 4-bedroom units) in 4-story, low-rise buildings. Hulhumalé Phase 2 (Hiyaa) was even more ambitious in scale: 6,720 housing units were built in 16 blocks of 25-story high-rises (2-bedroom units of 550 square feet). An additional 6,000 social housing units are under construction by FDC and when completed will yield a combined volume of approximately 15,000 rent-to-own units in Hulhumale. To address the housing needs in the atolls, the Government has planned to build 1,575 units in 14 atolls starting in 2022.² To purchase their Rent-to-Own flats, beneficiaries pay a fixed rental rate that varies depending on the size of the unit, over a long-term rental contract of up to 25-year period. Ownership title will be transferred to the beneficiaries at the end of the rental contract.

The government's exposure from external loans and guarantees associated with public housing has grown to nearly US\$1 billion or approximately 19 percent of GDP as of 2020. In 2017, the government began to use the balance sheet of HDC to finance social rent-to-own housing developments, primarily in Hulhumalé. All in all, the government total external debt outstanding and disbursed related to housing (including guarantees for HDC loans) amounted to an estimated US\$739 million at end-2021, equivalent to a third of the total external public and publicly guaranteed debt. HDC accounts for more than half of external guaranteed debt (Figure ES.2), with the majority of its housing debt load being due to the Hiyaa project. The estimated combined cost for the Hiyaa project is MVR 10.5 billion or US\$679 million. This works out to about MVR 1.6 million (US\$101,000) per unit, or MVR 1.3 million (US\$82,000) per unit excluding the land cost.

The cost of debt repayment is high. From 2021-2028, Ministry of Finance (MoF) estimates indicate that debt service payments on existing housing-related debt amount to US\$40 million annually on average, or about a third of total external debt service due over the period. The high cost of debt servicing reflects the expensive terms of all six guarantees HDC contracted in 2017-2018, which had short grace and maturity periods (2 and 3-13 years, respectively) and variable interest rates (3-3.3percent plus 6-month LIBOR).

The Rent-to-Own program's effectiveness has been dampened by poor and regressive targeting. Subsidy programs are not being allocated based on household incomes, allowing households that are not in need of assistance to benefit from government programs. For instance, the Hiyaa project prioritizes specific

¹ Five sub-projects are: 280 flats (2004); 120 flats (2007); 488 flats (2009); 1000 flats (Sept 2013); and 704 flats (2017)

² <https://psmnews.mv/en/98881>

demographic and job categories: Thirteen categories of applicants were prioritized to receive Rent-to-Own housing under the Hiyaa project. Among these groups were civil servants, teachers, single parents, doctors, and nurses; married people between the ages of 18 and 35; and Malé residents which had previously experienced issues with public housing projects. This practice of prioritizing employment types, with several in the highest income segment, counters the social housing targeting principle to serve those most in need of government support. As a result, the rental rate for *Hiyaa* is the same across all categories regardless of the households' income and capacity-to-pay.

Rental default rates are high, as HDC has limited ability to enforce collection. Although the law and several court decisions state that the HDC has the right to evict households who are delinquent, eviction is not enforced. Furthermore, as HDC is not a bank nor a financial services company, it has no ability to report rental delinquencies to the Credit Information Bureau. Rental default, defined as non-payment of 90 days and above, are on average at 37percent across all social housing projects in both Hulhumale Phase 1 and 2, as of July 31, 2022. HDC's short-term solution has been to reschedule the payments by extending rental tenure, though not with significant impact. Given the high default rate, *revenues from public housing projects are insufficient to cover debt service repayments.*

The Hiyaa project has exacerbated HDC's financial vulnerabilities which require ongoing cash flow support from the Government. The long delay in the Hiyaa project lease-up and the rental moratorium related to the COVID-19 pandemic have added to HDC's cash flow constraints. However, the key financial strain is mostly driven by two factors: first, the structural mismatch between the lengthy rental payment period and the high cost of servicing debt in the short and medium term, and secondly, the lower-than-expected monthly revenues from rental due to the high rental default rate.

The “one-size-fits-all” design of the Rent-to-Own program does not answer to beneficiaries' varying needs. The current rental contract locks beneficiaries in a long-term commitment of up to 25-years as a renter. This is detrimental to households in two ways: One, it prevents households from accommodating evolving housing needs or lifestyles that would call for different home sizes, types, or locations. Second, households who have the financial capacity to transition toward ownership by prepaying to gain early homeownership are not able to do so. These constraints not only limit household preferences, but also prevent the GoM from receiving a higher cash flow for debt repayment.

Spending more will not necessarily help the GoM solve Maldives' housing challenges. Rather than take on more costly external debt to finance large-scale Rent-to-Own programs and trapping such funds pay-back under the Rent-to-Own contract for up to a 25-year period, the government could undertake three main sets of reforms to address institutional and organizational gaps that significantly impact the provision of social housing in the country:

1. **Targeting and housing policy and regulatory reforms:** Improved targeting in all social housing programs is critical to increase the efficiency and effectiveness of public spending in the housing sector. The draft National Housing Policy (dated July 2020) provides a better definition of low-income housing and a clearer explanation of the targeted segments that can be used for future public housing eligibility criteria. Building on this definition, and implementing mechanisms for regular income and tenure verification, will ensure that households with the greatest need are the main program beneficiaries.

A fair, transparent, and predictable legal and regulatory framework for housing on both supply and demand sides is a critical determinant of investment decisions for both public and private sector stakeholders. On the supply-side, a set of new regulations, including a new Land Law, Building Code, and Tenancy Act have been either adopted or are being drafted, but have not yet been implemented as at the time of writing. On the demand-side, Title Registration legislation, Foreclosure Act, and Bankruptcy and Solvency Act would reduce lending risks for banks and

would help to catalyze a more healthy and resilient growth for the mortgage market.

2. ***Reforming the Rent-to-Own program design and implementation.*** Incentives between households and the government need to be better aligned to improve the program's fiscal sustainability and to address evolving housing needs, preferences and capacity-to-pay of the households. For example, middle-income earners can be given the option to purchase their homes with a mortgage loan and subsidy, while low-income earners can progress through different rental payment levels in line with their capacity-to-pay.

Furthermore, rather than solely promoting home ownership, the government could provide a rental subsidy or voucher to these households and create permanent rental housing. The government could also leverage domestic or international housing non-profits with the capacity to manage permanent affordable rental housing to play a more prominent role. This would enable the government to disassociate itself from the role of collection agent, reduce moral hazard, and thus improve delinquency and default rates in public housing schemes.

3. ***Support enabling environment reforms to improve the implementation of housing policies and programs.*** The FDC mandate can be strengthened to include the 'post off-take' ownership role and property manager for all social housing projects in Hulhumale. This would differentiate the SOEs roles and improve the quality of public housing assets. An integrated housing data system can also allow public and private stakeholders to quickly assess market needs and find the most efficient ways to fulfill them. Such a system would include data on consumer housing needs and demand (by location, income, and employment), construction updates, home price trends, and rental data. Access to reliable and timely housing-related data can help Maldives to develop targeted regulations and policies, monitor the effectiveness of public housing programs, and accelerate private sector investments.

A1. Economic Update



1. Context

A strong recovery in tourist arrivals has boosted economic growth...

Following the reopening of borders after the COVID-19 pandemic, tourist arrivals grew strongly from the second quarter of 2021 due to Maldives' successful vaccination campaign and the country's "One Island, One Resort" concept. Total arrivals for 2021 was 1.3 million, only 22 percent lower than the pre-pandemic level. A rebound in arrivals from key European markets, high numbers from India, and growing interest from Middle Eastern countries have offset the absence of tourists from China and slowdown in Russian visitors. As a result, the Maldivian economy grew by 37 percent in 2021, after the sharp contraction of 33.5 percent in 2020.

...while inflation rose with the surge in global commodity prices...

Rising global commodity prices have put pressure on domestic inflation, government's fiscal position and the balance of payments. Maldives' inflation climbed to 5.2 percent (y-o-y) in June 2022 before declining to 2.5 percent (y-o-y) in July 2022, compared to 0.5 percent in 2021, driven largely by rising global commodity prices (Box 1). Due to blanket subsidies provided on fuel and food items, government is facing significant pressure to continue financing the subsidy program in its current form. Additionally, sharp growth in capital and construction material imports – to support completion of mega Public Sector Investment Program (PSIP) projects in 2023 – adds further pressure to current account balances.

...and external debt distress remains a real concern.

Continued public expenditure, particularly on ambitious PSIP projects, has maintained high levels of public debt. Total public and publicly guaranteed (PPG) debt was 120 percent of GDP at the end of 2021, as government contracted new debt worth US\$1 billion in 2021 to finance general expenditure, support budget deficits, rollover maturing debt, and fund PSIP projects. PPG debt dropped to 113 percent of GDP by the end of the first quarter of 2022, with the share of external debt remaining high at 53 percent of GDP.

Box 1: Global Economic Developments

Global economies have experienced a sharp slowdown in the last three years on the back of major economic shocks. The COVID-19 pandemic, adverse spillover effects from the Russia-Ukraine war, and tighter monetary policy to combat inflation have caused a decline in economic activity. As a result, global GDP growth is expected to decrease to 2.9 percent in 2022 from 5.7 percent in 2021 (Figure A.1).

U.S. growth is projected to slow to 2.5 percent in 2022, owing to tighter financing conditions and the economic effects of the war in Ukraine. Growth in emerging markets and developing economies (EMDEs) has also been weighed down, with average growth in this group of countries forecasted to be 3.4 percent in 2022, significantly lower than the 4.8 percent during the 2011-19 period. This is mainly due to rising commodity prices, limited government support, and a decline in economic activity. As a result, catching up with advanced-economy income levels is expected to be markedly slower in EMDEs over the next few years, than in the pre-pandemic period, with progress reversing in EMDEs excluding China.

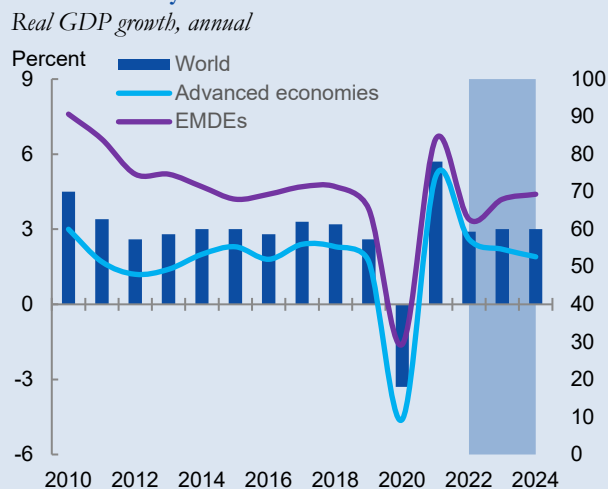
The global commodity price index increased fourfold in 2022, reaching the highest level since 2003. Commodities that are largely exported by Russia and Ukraine, such as energy and wheat, experienced the most pronounced price increases, as the war disrupted production and trade. As a result, inflation has accelerated in both advanced economies and EMDEs, reflecting the surge in commodity prices.

The global median headline Consumer Price Index (CPI) inflation was 7.8 percent in April 2022, the highest since 2008, with average advanced economies inflation at 6.9 percent and EMDE inflation at over 9.4 percent (Figure A.2). Rising inflation has led to a tightening of monetary policies across the world. Bond yields in advanced economies have increased, and there has been a consistent increase of equity volatility. Meanwhile, capital outflows from EMDEs have accelerated. In March 2022, equity and debt inflows to EMDEs turned sharply negative, with Q1 bond issuance being the weakest among any first quarter since 2016.

Goods trade experienced major disruptions in the first half of 2022 due to a combination of the COVID-19 pandemic, supply chain issues, and the Russia-Ukraine war. As economies rebounded from lockdowns, supply chains struggled to keep up with the demands, causing a supply bottleneck. Russia’s invasion of Ukraine further exacerbated these pre-existing issues.

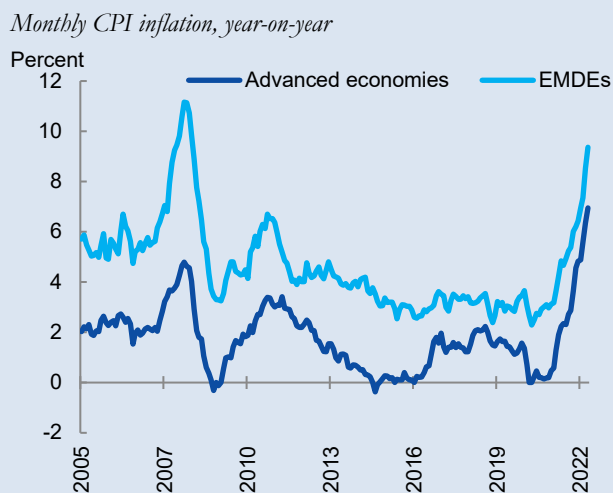
Overall, global risks have tilted to the downside in 2022. This has had a significant impact on Maldives – a small economy that is dependent on trade and external financing.

Figure A.1: Global growth has experienced major shocks recently and the outlook is uncertain



Source: Global Economic Prospects, June 2022.

Figure A.2: Inflation has accelerated globally



Source: Global Economic Prospects, June 2022.

Source: World Bank Global Economic Prospects, June 2022.

2. The economy continued to rebound in 2022, as inflationary pressures emerged

Economic growth has been strong on robust tourist arrivals...

Real GDP grew by 19.3 percent (y-o-y) in 2022Q1, primarily driven by strong activity in the tourism sector. This sector is estimated to have grown by 35.1 percent (y-o-y) in this quarter, compared to a contraction of 11.8 percent (y-o-y) in 2021Q1, and constituted half of the economic growth over this period (Figure A.3).

...as the tourism sector continues to perform well...

The number of tourist arrivals grew by 42.9 percent (y-o-y) in the first eight months of 2022 and is on course to reach the annual pre-pandemic high of 1.7 million (Figure A.4). Furthermore, hotel and resort occupancy rates for the first seven months of 2022 were 60.5 percent compared to 51 percent during the same period in 2021, while the average stay for the period was 8.1 nights, a significant improvement from the pre-pandemic level of 6.3 nights.

...leading to a recovery in other sectors...

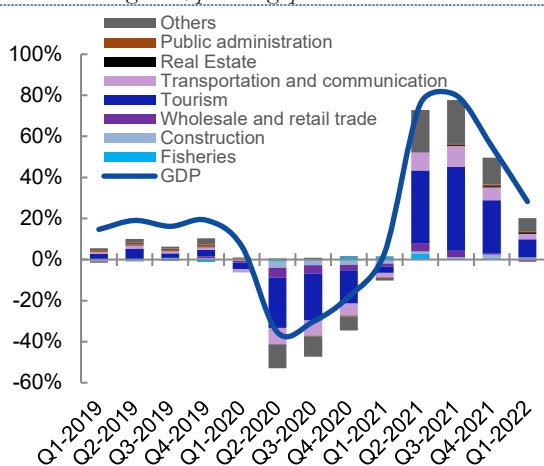
With increasing visitors, growth in the transportation and communication sector picked up. The sector grew by 23.6 percent in 2022Q1 as growth in travel agency services, air travel, and warehousing and transportation support services drove overall growth in the sector.

...with construction receiving a further boost from the continuation of PSIP projects.

The construction sector, which also suffered during the COVID-19 pandemic, grew by 22.3 percent (y-o-y) in 2022Q1, compared to a 32.1 percent contraction in 2021Q1. This recovery was mainly driven by PSIP projects in transportation infrastructure and housing that started again from the second quarter of 2021.

Figure A.3: Real GDP continues to recover...

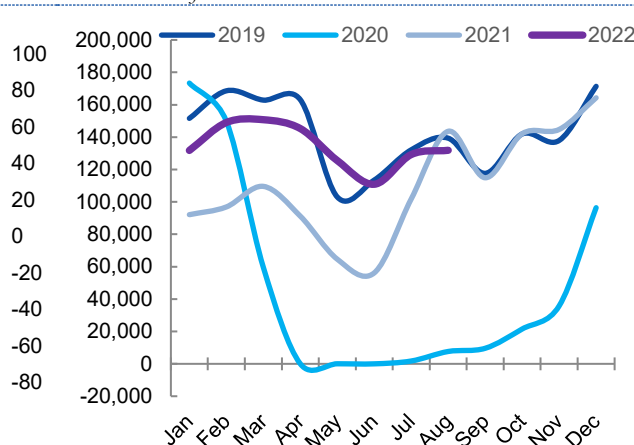
Contribution to growth, percentage points



Source: National Bureau of Statistics Maldives (NBS), staff calculations.

Figure A.4: ...as tourist arrivals remain high.

Total number of tourist arrivals



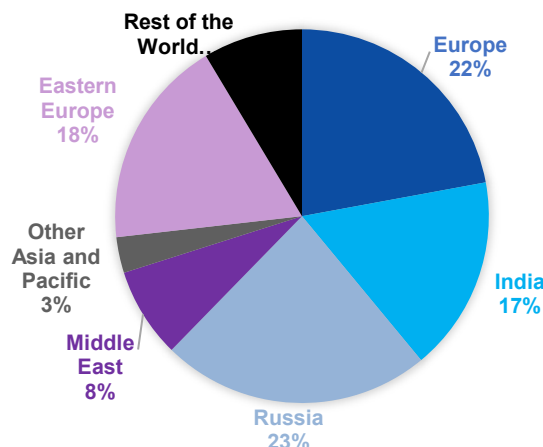
Source: Ministry of Tourism, staff calculations.

A decline in arrivals from Eastern Europe and Russia was offset by other markets.

In the first seven months of 2022, tourist arrivals from Eastern Europe and Russia declined by 9 and 12 percentage points, respectively, compared to the same period in 2021. However, tourists from Europe and other Asia and Pacific countries increased by 20 and 6 percentage points over the same period, more than offsetting the decline in arrivals from Eastern Europe and Russia (Figure A.5 and Figure A.6).

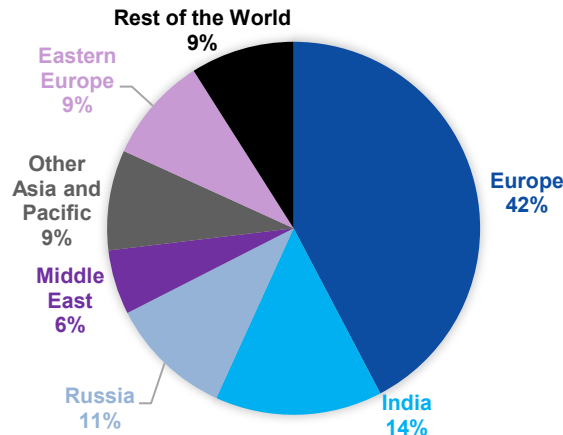
Figure A.5: Decline in arrivals from Eastern Europe and Russia... and Figure A.6: ...was more than offset by tourists from Europe and Asia

Share of tourist arrivals in Jan-Jul 2021



Source: Ministry of Tourism, WB staff calculations.

Share of tourist arrivals in Jan-Jul 2022

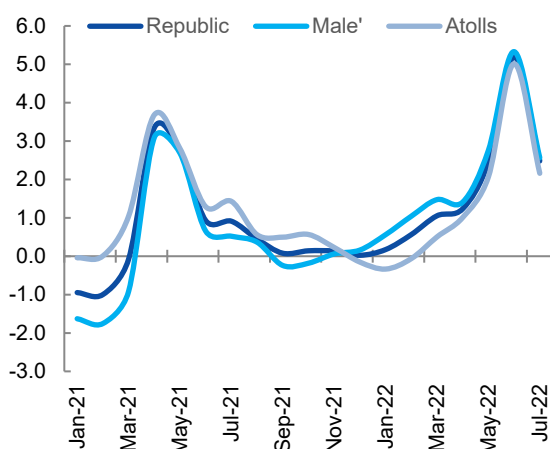


Source: Ministry of Tourism, WB staff calculations. Note: Data as of Aug 30, 2022.

Maldives was hit by the surge in global commodity prices.

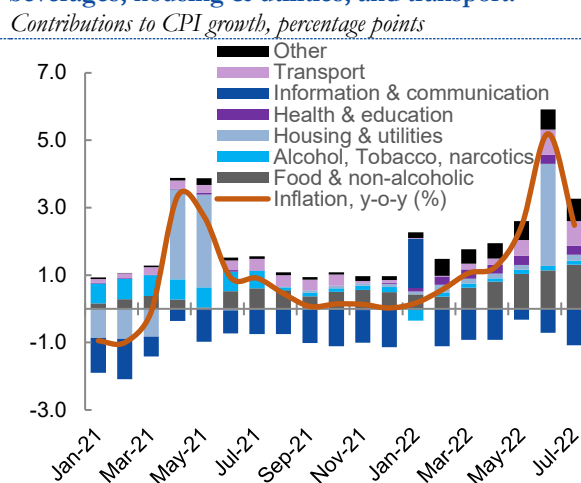
Inflation started to rise in 2022Q2 following the impact of the Ukraine-Russia war on global commodity prices. This culminated with prices increasing in Maldives by 2.5 percent (y-o-y) in July, compared to an average of 0.5 percent in 2021. This increase was slightly more pronounced in Malé (2.6 percent) than in the Atolls (2.2 percent) (Figure A.7). The rise in prices was driven largely by three major components: the CPI for food & non-alcoholic beverages, transport, and housing & utilities – which account for more than half of the total CPI basket of goods and services – increased by 3.7, 4.1 and 2.4 percent (y-o-y) on average, respectively, in the first seven months of 2022 (Figure A.8).

Figure A.7: Prices surged across the country in 2022... Year-on-year change in consumer price index (CPI), percent



Source: Maldives Bureau of Statistics, WB staff calculations.

Figure A.8: ...especially in food & non-alcoholic beverages, housing & utilities, and transport.



Source: Maldives Bureau of Statistics, WB staff calculations.

3. Poverty levels improved with the economic recovery, but inequalities persist

Poverty has fallen sharply with the economic recovery.

Against the international poverty line for upper middle-income countries (US\$6.85 per person per day), the poverty rate of Maldives, which was estimated to be 3.9 percent in 2019, shot up to an estimated 19.8 percent in 2020 due to the pandemic. Robust economic growth should contribute to an estimated reduction in poverty levels to 3.8 percent by the end of 2022 (Figure A.9).

Even though poverty is low at the national level, Maldives remains an unequal country.

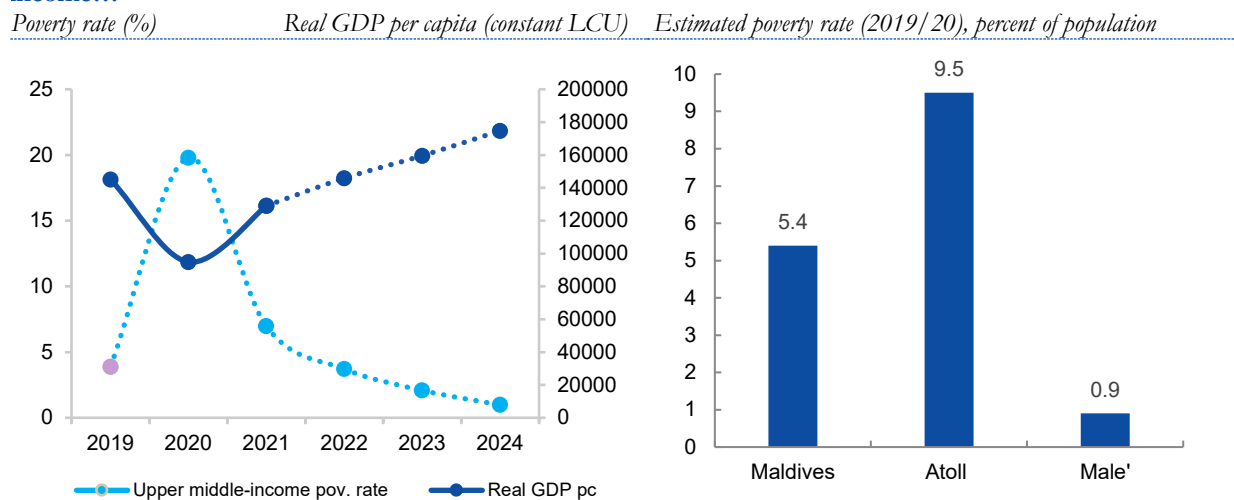
The poverty rate at the national poverty line (MVR 71.4 per person per day) – which is used for the country’s policy making – was estimated at 5.4 percent in 2019/20. While less than 1 percent of Male’ was poor under this line in 2019, about 10 percent of the population in the Atolls lived below the national poverty line (Figure A.10).

Inequality between Malé and the Atolls is even more pronounced when considering other dimensions.

Maldives published its first Multi-Dimensional Poverty Index (MPI) in 2020,³ based on the Demographic and Health Survey (DHS) 2017. Unlike the poverty lines, the MPI considers non-monetary metrics to classify individuals as poor or non-poor. While the Atolls had a higher incidence of multi-dimensional poverty than Malé, the differences in the underlying dimensions of deprivation are instructive. Malé’s multi-dimensional poverty is driven largely by over-congestion and lack of access to healthcare. Higher multi-dimensional poverty in the Atolls is driven by low years of schooling, lack of access to safe drinking water, lack of access to sewer systems, and lack of access to healthcare. The Maldives Poverty Assessment (2022) shows that, while these disparities have improved, access to infrastructure and opportunities in the Atolls remain limited (Box 2).

Figure A.9: Poverty levels fall on improved per-capita income...

Figure A.10: ...but inequality is still a major concern



Note: Upper middle-income poverty line – US\$6.85/person/day

Source: World Bank staff estimates based on MBS HIES (2019). Note: National Poverty Line – MVR71.4 per person per day or MVR2,173 per person per month

Box 2: Poverty Profile in Maldives

Framing Maldives' development challenge simply as "Atolls versus Malé" could lead one to overlook the differences in socio-economic outcomes within the Atolls. Atolls that are more remote from Malé do not necessarily have higher monetary poverty rates. Rather, there are clusters of better-off and worse-off Atolls in each zone. For example, Raa and Baa are the Atolls with the highest (18.9 percent) and lowest (1.7 percent) poverty rates, respectively, and are located in the Lower North Zone. Haa Alif (12.5 percent) and Haa Dhaalu (12.9 percent) have lower poverty rates than Raa and are in the Upper North Zone, further away from Malé, and clustered with Shaviyani (5.6 percent poverty rate).

Large households, congested living, and a high ratio of children to adults increases the probability of Maldivians being poor. For example, a household with 10 members or more is three times more likely to be poor than a household with nine members or fewer. Lower educational attainment among members, especially the household head, is associated with poverty. Households whose head suffers from a chronic illness or disability are also more likely to find themselves in poverty.

Wage employment is associated with a lower incidence of poverty, as is employment in the tertiary sector, which encompasses services and trading activities. Involvement in primary activities such as fisheries and agriculture or secondary activities such as manufacturing and construction is associated with a higher incidence of poverty, as is any type of self-employment. Poverty does not vary with employment in the public or formal private sector. Persons in informal employment are twice as likely to be impoverished as those in formal employment. Nationally, households that have migrated to their present location are three times less likely to be poor than households native to their location.

Source: Maldives Poverty Assessment, 2022.

Formal sector employment and wages have picked up with the strong economic rebound...

Employees registered under the pension system – a proxy for formal employment – increased by 6 percent in 2021 to 119,000 employees and surpassed the pre-pandemic level of employment (Figure A.11). Growth in jobs was mostly driven by the accommodation sector, reflecting the recovery of tourism, followed by public administration and wholesale and retail sectors. Average basic wages in the formal sector grew by 7 percent (y-o-y) in 2021 to MVR 7,566 (US\$490), while wages in the accommodation sector were up by 3 percent over the same period.⁴

... but informal employment experienced structural changes as a result of the pandemic.

According to the Informal Sector Survey⁵, one-third of employees experienced a negative impact on wages during the COVID-19 pandemic. The majority of those who quit or lost their jobs due to the pandemic were lower income earners, with 60 percent of those earning up to MVR 4,999 (US\$324) per month and 25 percent of those earning between MVR 5,000-9,999 (US\$325-649) a month. The highest informal sector employment losses were in the construction, education, and manufacturing sectors, while there has been an increase in employment in the wholesale and retail trade and public administration sectors⁶ as workers look for more stability (Figure A.12). The overall weaker recovery of informal sector jobs, compared to formal jobs, is also concerning given the impact this might have on further increasing inequality (Box 2).

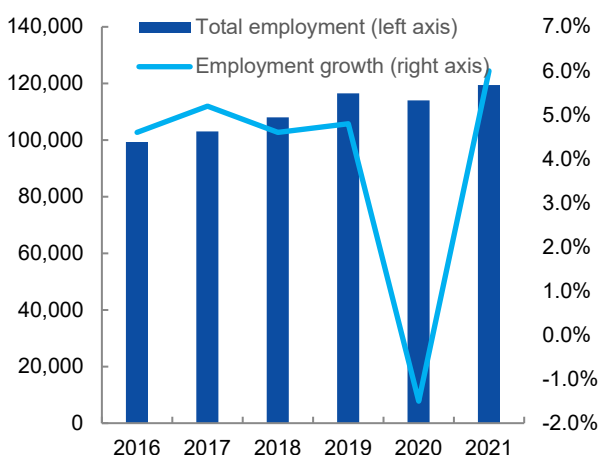
⁴ Minimum wage implementation for the tourism sector came into effect in 2022, which is projected to double the wages of 60 percent of resort employees (<https://avas.mv/en/109675>)

⁵ UNDP (2021) considers informal sector workers as those (i) people who are engaged in businesses which are not registered, (ii) people who run their own businesses with less than 5 employees (regardless of registration status), and (iii) employees working in living quarters/agricultural plots or no fixed location without social security are all considered informal sector workers. The informal sector excludes domestic workers employed by private households.

⁶ While public administration jobs in general are considered formal sector employment, not all employees are considered as formal employees due to them not contributing towards the pension system and/or not receiving annual leave benefits.

Figure A.11: Employment recovered in 2021...

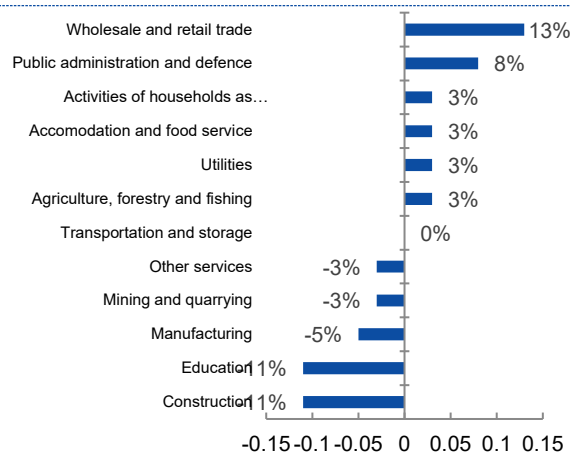
Employment and employment growth



Source: Ministry of Economic Development, Labour Market Report 2021.

Figure A.12: ...while there were sectoral shifts by informal workers

Percentage change in informal employment from Dec-2019 to Sep-2021



Source: Maldives Bureau of Statistics, Informal Sector Survey 2021.

4. MMA's exposure to the sovereign climbs, while lending to the private sector falls

Policy rates have been maintained at the same level in 2022 despite inflationary pressures.

The Maldives Monetary Authority (MMA) has kept the minimum reserve requirement (MRR) unchanged at 10 percent of average local currency deposits, after the last increase from 7.5 percent in June 2021, while the MRR for foreign currency deposits has been maintained at 5 percent since July 2020. In addition, the interest rate corridor was also maintained at the same band, with the overnight deposit facility (ODF)⁷ and overnight Lombard facility (OLF)⁸ kept unchanged at 1.5 percent and 10 percent, respectively.

Exposure to sovereign bond holdings remains high, as MMA increasingly finances the budget deficit.

The temporary suspension of the Fiscal Responsibility Act (FRA),⁹ which is extended until the end of 2023, has led to a significant increase in MMA's claims on central government. The suspension allowed the Ministry of Finance (MoF) to overdraw MVR 4.4 billion (US\$ 286 million) from the MMA/Public banks, which would normally be limited to MVR 170 million. As a result, MMA's asset exposure (including Treasury bills and bonds, and advances) increased to 52.5 percent of its total financial assets at end-August 2022, from 43 percent at end-2021. The MMA's claim on central government has risen from MVR 6.2 billion in 2019 to MVR 10.9 billion in July 2022 (Figure A.13).

⁷ MMA commenced the ODF for commercial banks on 23 March 2010, whereby banks can place their excess funds at MMA overnight. This facility carries the lowest rate in the system, below the deposit rate offered to commercial banks' customers. The ODF rate is 1.5 percent per annum, effective 1 September 2014.

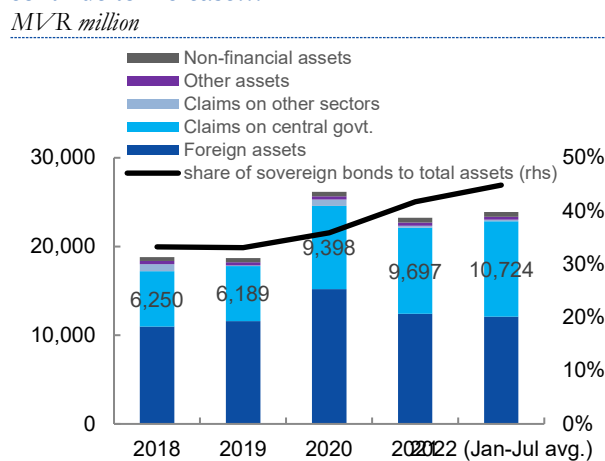
⁸ The MMA introduced OLF to commercial banks on 9 May 2010, allowing for banks to borrow from the MMA on an overnight basis mainly to avoid disruptions in the payments system and to meet the MRR level. This facility carries the highest rate in the system, above the overnight lending rates among commercial banks. The OLF rate is 10 percent per annum, effective 1 September 2014.

⁹ The Fiscal Responsibility Act (FRA) aims to achieve fiscal stability and sustainability, improve fiscal transparency, and increase the accountability of government. The Act sets out a number of quantitative fiscal targets and procedural rules to be followed in order to enforce responsibility in fiscal management. The suspension of certain clauses of the FRA was approved by parliament in April 2020 on the request of the Minister of Finance, citing weak government cashflows due to the COVID-19 pandemic.

Maldives continues to maintain a *de facto* stabilized exchange rate arrangement.

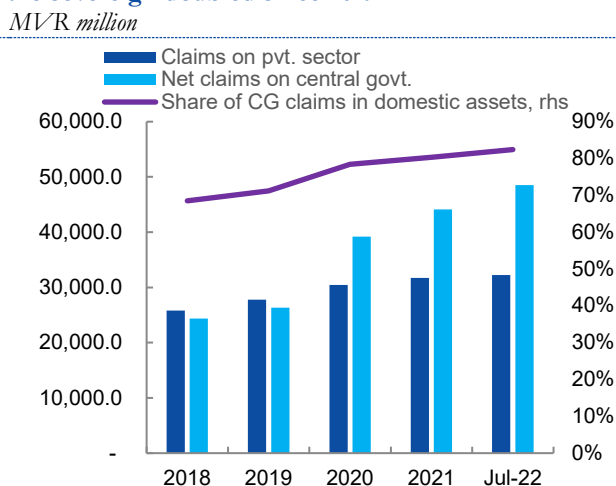
Under the current monetary policy framework, the exchange rate peg to the US dollar is used as the nominal anchor to help maintain price stability through the exchange rate. The MMA aims to maintain the exchange rate peg within a set horizontal band, where the exchange rate is allowed to fluctuate within the bounds of MVR 10.28 to MVR 15.42. Furthermore, the MMA continues to manage excess liquidity in the banking system through Open Market Operations and the Foreign Exchange Swap Facility to maintain the domestic money supply and support exchange rate stability consistent with economic activity.

Figure A.13: MMA’s claims on central government continue to increase...



Source: MMA, World Bank staff calculations.

Figure A.14: ...while commercial banks’ exposure to the sovereign doubled since 2019



Source: MMA, World Bank staff calculations.

Excess liquidity has been increasingly invested in foreign assets and government securities.

Broad money grew by 26.6 percent (y-o-y) in June 2022, being driven largely by growth in net foreign assets and lending to central government (Figure A.15). Net foreign assets of the banking system increased substantially, stemming from the rise in foreign currency deposits held abroad by commercial banks. The increase in net claims on central government by commercial banks reflects primarily the annual expansion in government securities. The commercial banks’ sovereign exposure climbed from about 70 percent in 2019 to 83 percent in July 2022, further tightening the sovereign-banking system nexus (Figure A.14).

Banking sector remains well capitalized...

The banking sector, which accounts for more than 90 percent of the financial sector assets, continues reporting high levels of capital, well above the minimum regulatory requirement of 12 percent. The aggregated banks’ capital adequacy ratio (CAR) grew marginally from 47.3 percent in December 2021 to 48.3 percent in June 2022. The high CAR levels are indicative of the banking sector’s increasing exposure to the sovereign, which also shows signs of crowding out private sector credit (discussed further below). The asset quality has also been reported as improving, with non-performing loans (NPLs) dropping from 6.7 percent to 6 percent over the same period, which is attributed to a write-off of a few NPLs. The loan-loss provisions were more than the NPL portfolio at 106.5 percent. Banking sector liquidity remains adequate, with liquid assets covering 74.6 percent of short-term liabilities.

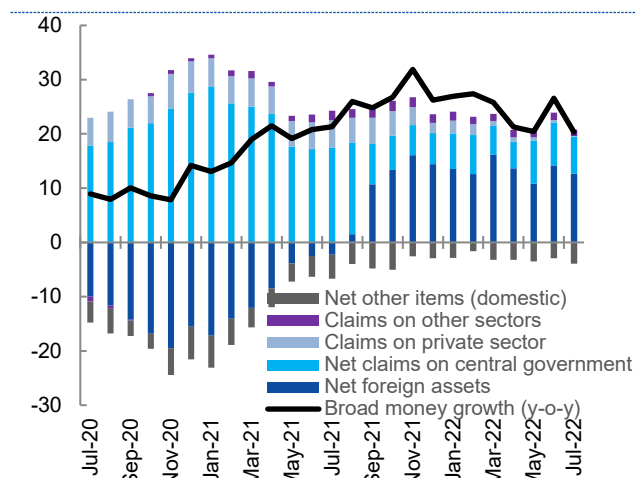
...but deposit growth has not translated into increased lending.

Banks’ performances as financial intermediaries have deteriorated, with the sharp deposit growth not translating into an increase in private sector lending (Figure A.16). While interest rates on deposits remained broadly unchanged, both local and foreign currency deposits increased in nominal terms, with overall deposit growth reaching

29.3 percent (y-o-y) in June 2022. This growth was mostly driven by a substantial increase in transferable deposits denominated in foreign currency by private non-financial corporations and private individuals, due to the recovery in the tourism sector and related inflow of foreign currency. At the same time, however, growth in credit to the private sector has been decelerating, plunging to 1.9 percent (y-o-y) in June 2022, as commercial banks have invested more in sovereign bonds. Credit to the tourism and construction sectors experienced a decline of 6.8 and 0.5 percent (y-o-y), respectively, mostly due to a decline in lending for new resort development and renovation of resorts. As a result, credit to GDP dropped from above 50 percent in 2020 to around 34 percent of GDP in mid-2022, and the credit to deposit ratio dropped from above 70 to 51 percent over the same period.

Figure A.15: Broad money continued to grow...

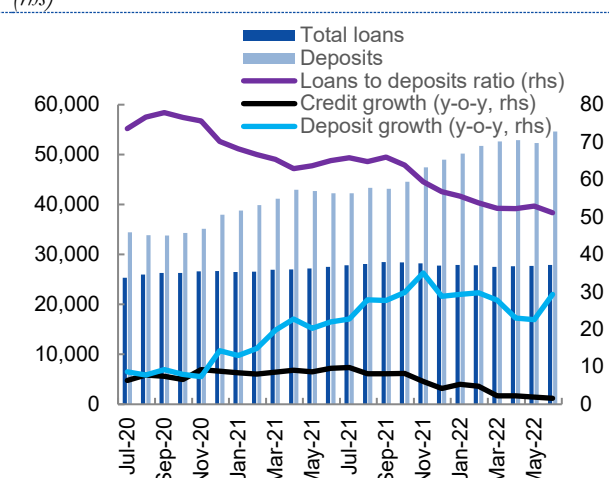
Contribution to broad money growth, in percent



source: MMA, World Bank staff calculations.

Figure A.16: ...while credit growth declined

Private sector credit and deposit growth, MVR million and percent (rhs)



source: MMA, World Bank staff calculations.

5. Higher commodity prices are putting pressure on external balances and reserves

The current account deficit narrowed significantly in 2021 on improved tourism inflows.

The current account deficit (CAD), which widened to 35.5 percent of GDP (US\$1,327million) in 2020, narrowed to 9 percent (US\$458 million) in 2021, following a significant jump in tourism sector receipts to almost 67 percent of GDP – these account for about 90 percent of service exports (Annex 1). At the same time, merchandise imports remained relatively constant as a share of GDP, with close to 50 percent being fuel and capital and construction goods imports. Remittance outflows in 2021 grew only 25 percent (y-o-y) to US\$496 million, still well below the pre-pandemic (2019) level of US\$596 million.

FDI and a Sukuk issuance largely financed the CAD in 2021.

While net FDI remained relatively stable at US\$443 million compared to 2020, it is still less than half of the pre-pandemic (2019) level of US\$960 million. The government also issued a Sukuk worth US\$500 million in 2021, of which a portion of the proceeds were used to pay off 77 percent or US\$192 million of a US\$250 million Euro bond maturing in 2022. The rest of the Sukuk proceeds were used to cover budgetary deficits (Annex 1 and Figure A.19).

The trade deficit has widened

The merchandise trade deficit has widened considerably this year (Annex 1), by 47 percent (y-o-y) in H12022 to US\$1.5 billion, due to the larger fuel import bill (up to over 14 percent of GDP), as well as higher construction and capital goods imports.

considerably in 2022...

Accelerated PSIP projects and, in particular, higher fuel prices have driven this growth. Petroleum imports grew sharply by 160 percent (y-o-y) during 2022Q2 and contributed to half of overall import growth during the quarter (Figure A.17). Imports of transport equipment and construction related imports soared by 89 percent (y-o-y) over the same period. Despite the ongoing recovery in tourism, the widening of the trade deficit is adding pressure to the balance of payments (Figure A.18).

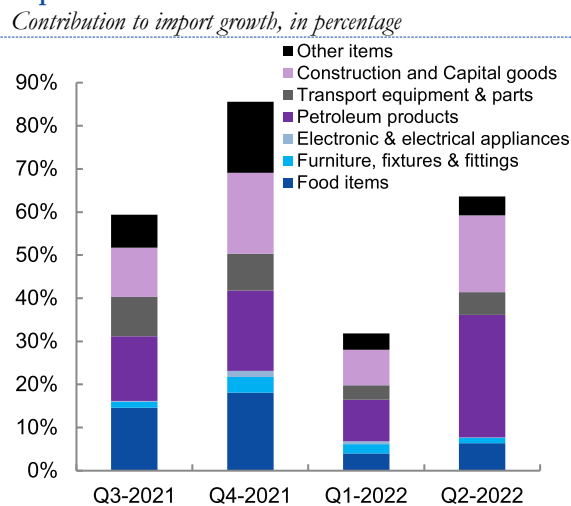
...while an increase in re-exports of jet-fuel supported exports.

Merchandise export growth was primarily driven by jet-fuel re-exports (Annex 1). Higher global oil prices and increased air travel to Maldives have led to a growth in jet-fuel re-export earnings by 89 percent (y-o-y) in the first seven months of 2022 to US\$130 million. Fish exports, which traditionally lead in merchandise exports, went up by 15.6 percent (y-o-y) over the same period to US\$89 million, driven by growth in tuna and canned or processed fish exports.

Official reserves deteriorated in 2022 due to the sudden increase in the import bill as global commodity prices spiked.

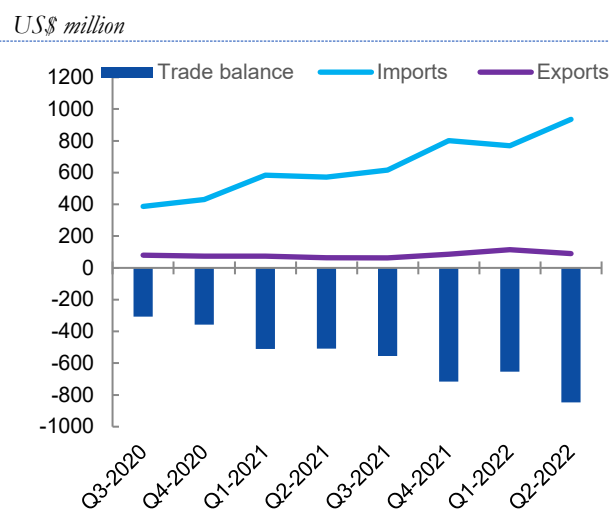
A widening trade deficit (Figure A.18), due to higher global commodity prices, is exerting further pressure on official reserves (Figure A.20). As the import bill has increased this year – to US\$1,705 million in H12022 from US\$1,155 million in the same period of 2021 – official reserves have fallen by 9.6 percent since end-2021, declining to US\$728 million in July, the lowest level since 2018. These reserves are sufficient to cover 2.7 months of imports, a drop from 3.8 months at end-2021. At the same time, short-term liabilities (i.e., coming due within the next 12 months) increased to US\$446 million by end-July, up from US\$393 million at the end of 2021. As a result, usable reserves (total reserves minus net short-term liabilities) fell to US\$282 million in July from US\$413 million at end-2021, which is estimated to be sufficient to cover only 1.1 months of goods imports based on the last 12 months’ average.

Figure A.17: Rising fuel and capital goods imports...



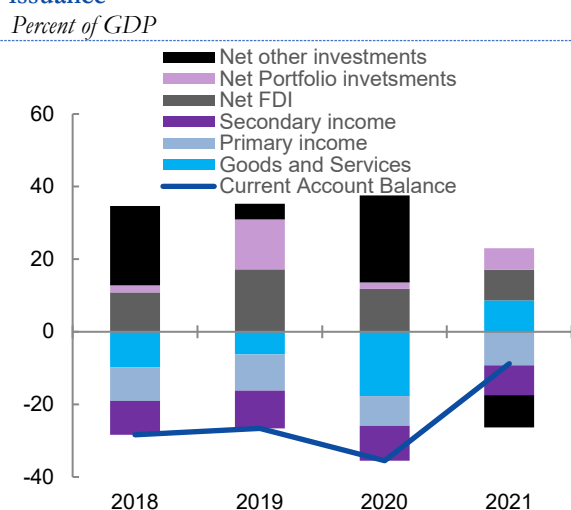
Source: MMA, World Bank staff calculations.

Figure A.18: ...have widened the trade deficit



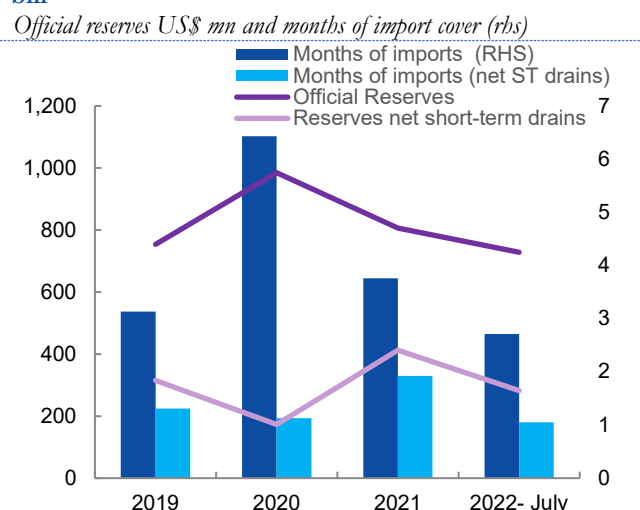
Source: MMA, World Bank staff calculations.

Figure A.19: CAD financed by FDI and Sukuk issuance



Source: MMA, World Bank staff calculations.

Figure A.20: Reserves depleting with jump in import bill



Source: MMA, World Bank staff calculations.

6. Fiscal deficit and public debt remain high, even as revenues start to strengthen

Fiscal deficit remained high in H12022 despite the improvement in revenue.

The overall fiscal deficit in H12022 was about 14 percent of GDP, similar to the outcome in 2021 (Annex 2). Despite an almost 3 percent of GDP improvement in revenues to over 28 percent of GDP compared to 25.3 percent in 2021, expenditure also increased by about 1.5 percent in H12022 to over 42 percent of GDP. The latter is significantly higher than total spending of about 31 percent of GDP in 2019, but lower than the peak of almost 50 percent of GDP in 2020.

Increase in budget revenues were driven by the strong recovery in tourism...

As was the case in 2021, the stronger than expected recovery in tourism and related taxes has continued to drive revenue growth in 2022. Much of this growth has come from the Tourism Goods and Services Tax (TGST) and resort rents. At about 11.5 percent of GDP, they constitute over 40 percent of revenues. Government also introduced changes to the Airport Development Fee and a new Airport Departure Tax in 2022. Business tax and the General Goods and Services Tax (GGST), at about 7.2 percent of GDP, also pushed up revenue growth in H12022, as domestic consumption and business activity continued to recover (Figure A.21).

...but overall fiscal performance was constrained by the sharp rise in subsidies and interest payments.

Although total expenditure is largely in line with what was budgeted for 2022, subsidy and interest spending shot up in H12022 (Figure A.22). This has been driven by the rise in global commodity prices and tighter global financing environment. In fact, due to the sharp increase in global commodity prices, government's spending on food and fuel subsidies, of MVR1.74 billion (US\$112 million) in H12022, already substantially exceeds the MVR1.44 billion (US\$92 million) that was budgeted for the whole of 2022 (Figure A.23). Between 2014-2019, government spent MVR1.3 billion (US\$85 million) annually on average on interest payments or about 2 percent of GDP. This increased to 2.8 and 2.6 percent of GDP in 2020 and 2021, respectively. In H12022 interest payments have jumped up further and are already at MVR1.78 billion (US\$115 million) or 3.8 percent of GDP. This is being driven by the large increase in domestic interest payments and the additional burden of external commercial debt, which is likely to be more demanding in the medium term (Figure A.25).

Subsidy reforms are essential to reduce pressures on fiscal balances and better target more vulnerable households.

Fuel subsidies provided by the government take the form of revenue loss compensation to the State Trading Organization (STO), which provides fuel to state-owned electricity suppliers at a controlled price. As global oil prices surged in 2022, fuel subsidy expenditure reached MVR550 million (equivalent to US\$35.6 million, or more than 4 percent of total revenues) in the first four months alone, exceeding fuel subsidy spending for the whole of 2021. This has caused a significant burden on the government's fiscal position. If price pressures and crisis conditions persist, these measures will require significant cumulative resources and pose serious risks for energy sector performance and fiscal sustainability. Global evidence suggests, however, that subsidies generally benefit the rich more than the poor.¹⁰ As a result, properly targeted transfers are more effective (and often at a lower cost to the budget) instruments for reaching the most vulnerable households, rather than broad-based price subsidies.¹¹ Furthermore, lessons from international experience strongly suggest that any subsidy measure to keep fuels or electricity affordable should be time-bound, transparent, and fully budgeted. It should also not disincentivize energy efficiency and conservation, especially in a country like Maldives with the renewable energy potential that exists.¹²

Capital spending continues to average about a third of total spending in recent years.

As a share of GDP, PSIP spending in 2020-H12022 was on average over 7 percent, compared to under 5 percent in 2019 (Annex 2). Although PSIP spending in H12022 was below the PSIP budget for 2022, this is expected to pick up again in the second half of 2022 and into 2023, as government looks to complete certain major infrastructure projects by end-2023, including the Velana International Airport terminal and runway expansion project, Greater Malé Connectivity Project, and large-scale public housing developments in Hulhumalé. Some of the financing for the latter still needs to be secured. However, given that Maldives has already contracted a billion dollars in external loans and guarantees to finance large-scale public housing projects, Part B. of this report proposes a different approach to providing affordable housing to Maldivians, whilst lessening the fiscal burden and risks.

Public debt remains at unprecedented levels ...

Public debt exceeds the size of Maldives' entire economy. Total public and publicly guaranteed (PPG) debt stood at US\$6.1 billion or an estimated 118 percent of GDP as at end-2021 (Figure A.24). Domestic debt accounted for the bulk of total debt (62 percent of GDP), while external and externally guaranteed debt accounted for the remainder (56 percent of GDP). Even excluding guarantees, central government direct debt stood at US\$5.2 billion or 100 percent of 2021 GDP. These figures do not include the significant advances from the central bank, which has occurred since the suspension of the FRA (see section 4) in April 2020. Moreover, fiscal risks – mostly stemming from guaranteed and on-lent loans, as well as trade payables, subsidies and capital injections to SOEs – were estimated at about US\$2.5 billion, or 45 percent of GDP in 2019. While such risks have not materialized, Maldives lacks the fiscal space to address any potential fallout to public finances, should they occur.

...and refinancing risks remain heightened in the medium term.

Through the US\$500 million Sukuk issuance in 2021, the government managed to pay off 77 percent of a US\$250 million Eurobond maturing in 2022, thereby mitigating some medium-term debt servicing risks. However, the Sukuk issuance came at a higher cost with a coupon rate of 9.875 percent and a yield of 10.5 percent. Additionally, a privately placed bond of US\$100 million, initially due in 2023, has been extended to 2026. However, since both the Sukuk and privately placed bond

¹⁰ <https://www.imf.org/en/Blogs/Articles/2013/06/24/for-richer-not-poorer-energy-subsidies-in-india>

¹¹ <https://blogs.worldbank.org/energy/amid-energy-price-shocks-five-lessons-remember-energy-subsidies>

¹² World Bank 2020.

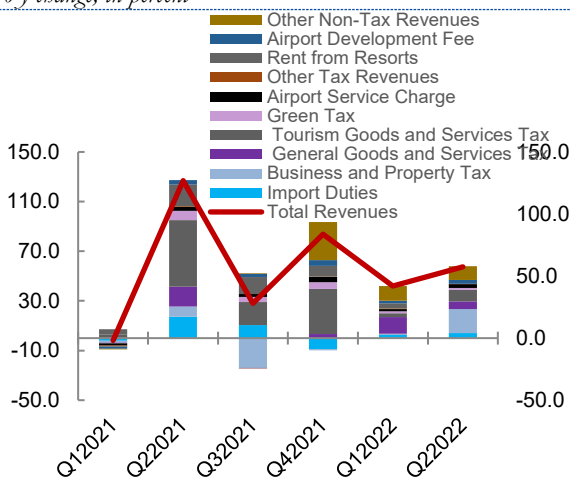
will be due in 2026, this year exhibits a spike in debt service payments, with total payments on existing debt expected to jump to almost US\$1 billion in 2026 (Figure A.29) – equivalent to an estimated 20 percent of 2021 GDP or 76 percent of 2021 revenues. Although the Sovereign Development Fund (SDF) could partially finance some of these repayments, these revenues are unlikely to be sufficient to repay the full external debt service costs.¹³

To address the elevated fiscal and debt vulnerabilities, government recently announced fiscal consolidation measures.

These measures aim to reduce the fiscal deficit by 6 percent of GDP in 2023. On the revenue side, MoF announced, in early July 2022, a proposal to increase the general GST rate from 6 to 8 percent and the tourism GST rate from 12 to 16 percent, which is expected to increase government revenue annually by 3 percent of GDP. On the expenditure side, government is undertaking austerity measures to reduce administrative and operational costs, planning to reduce SOEs reliance on state subsidies, and delaying the full roll out of the *Public Sector Pay Harmonization* (PSPH) policy; all of which are expected to reduce public expenditure by another 3 percent of GDP in 2023. Other recent expenditure reforms include: (i) bulk procurement of drugs and medical consumables through either international wholesalers or by pooling requirements with bilateral partners; (ii) elimination of exclusivity in importing medicines; and (iii) controlling the number of new hires into government.

Figure A.21: Growth in public revenues driven by tourism sector recovery

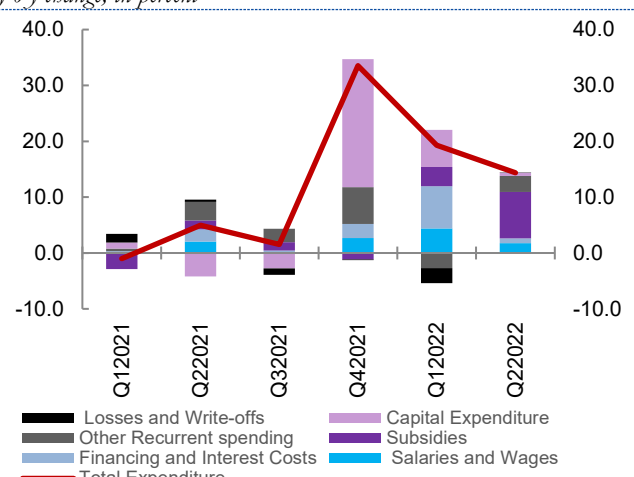
y-o-y change, in percent



Source: Ministry of Finance, World Bank staff calculations.

Figure A.22: Public expenditure remains elevated due to capital spending, interest costs and subsidies

y-o-y change, in percent

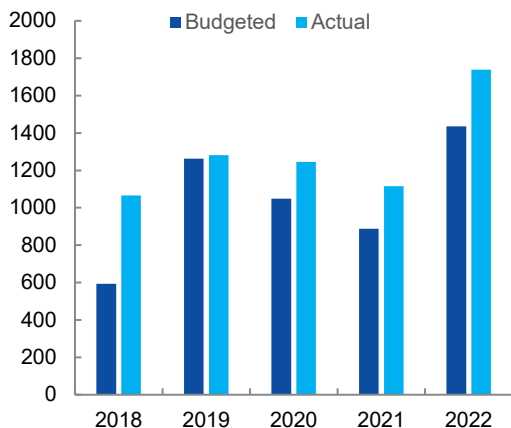


Source: Ministry of Finance, World Bank staff calculations/estimate.

¹³ Proceeds from the Airport Development Fee and dividends from the state-owned airport operator, MACL, are transferred into the SDF and earmarked for debt repayment. As of early June 2022, the SDF Fund amounted to US\$ 264.8 million, of which US\$72.1 million consists of long-term investments. The remainder of the SDF is included in Maldives’ foreign reserves. See World Bank 2022c.

Figure A.23: Actual subsidy spending already exceeds the amount budgeted for 2022...

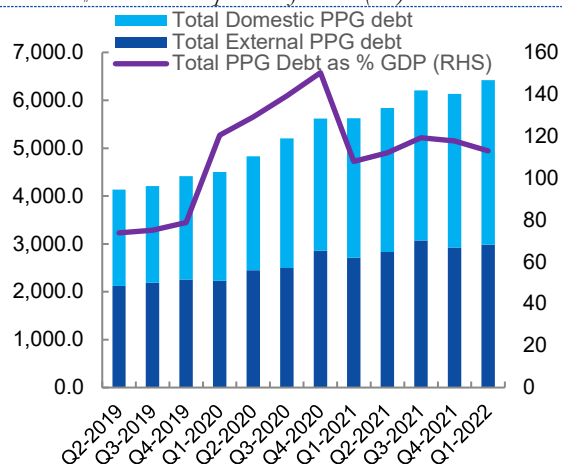
MVR millions



Source: Ministry of Finance, World Bank staff calculations.
Note: 2022 spending as at end-June 2022.

Figure A.24: ...and public debt stock remains high

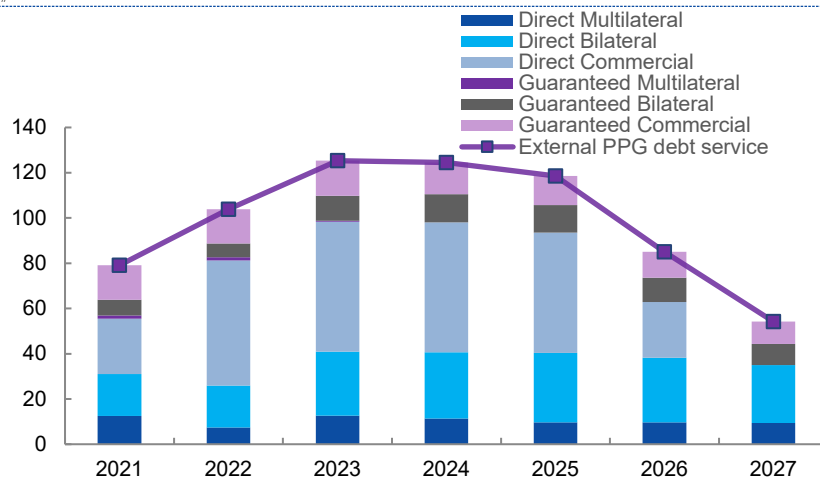
PPG in US\$ millions and percent of GDP (rhs)



Source: Ministry of Finance, World Bank staff calculations.

Figure A.25: Foreign Interest payments are expected to rise in the coming years

US\$ millions



Source: MoF, World Bank Staff calculations

A2. Outlook and Risks



7. Medium-term outlook is positive, but fiscal vulnerabilities are concerning

The outlook for tourism and, thus, the economy is positive over the medium-term.

The economy is expected to experience robust growth due to an increase in tourist arrivals, capital spending and private consumption. Real GDP growth is projected to be 12.4 percent in 2022 and 8.1 percent on average in the 2023-24 period. Compared to forecasts in early 2022, growth is expected to be 4.8 percentage points higher in 2022, driven by higher-than-expected tourist arrivals, and 2 percentage points lower in 2023 due to the base effect and delays in the Velana Airport capacity expansion project (Figure A.26). This outlook compares favorably with the pre-pandemic period during which growth averaged 6.3 percent from 2015-19. The likely return of Chinese tourists in early 2023, and increasing number of arrivals from India, Western Europe, and the Middle East, may provide an additional boost. Private consumption will likely be positively affected by both the spillover effects of growth in the tourism sector and the progressive roll out of the PSPH policy, which should lead to a rise in household incomes and purchasing power. Increasing PSIP spending on infrastructure, housing, and renewable energy projects are also expected to contribute to economic growth, especially over the longer-term. (Table A.1).

Table A.1: Growth is expected to remain high, but fiscal vulnerabilities are concerning

	2020	2021	2022e	2023f	2024f
Real GDP Growth, at constant market prices	-33.5	37.0	12.4	8.2	8.1
Inflation (Consumer Price Index)	-1.4	0.5	3.5	1.3	1.1
Current Account Balance (% of GDP)	-35.5	-9.0	-29.1	-19.1	-17.6
Fiscal Balance (% of GDP)	-23.5	-14.6	-16.1	-9.6	-8.7
Debt (% of GDP)	150.3	120.2	122.8	119.0	118.3

Source: World Bank estimates as of September 2022.

Inflation is expected to moderate as global commodity prices normalize.

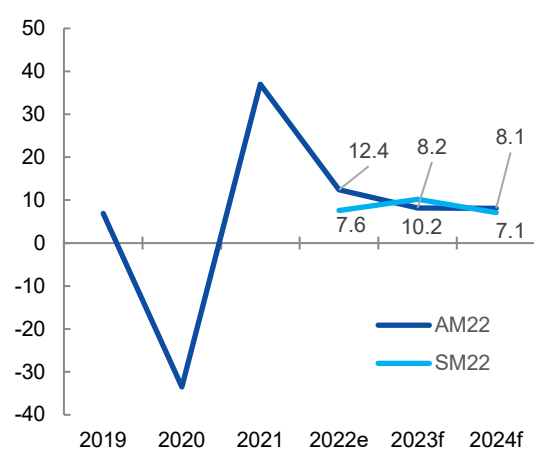
Inflation is projected to rise to 3.5 percent in 2022, reflecting the only partial pass-through from higher global fuel and food prices due to increasing price subsidies and price controls for certain staple foods. Over the medium term, inflation is expected to slacken to 1.3 and 1.1 percent in 2023 and 2024, respectively. This is premised on oil prices declining from a high of US\$98 per barrel in 2022 to US\$80 per barrel in 2024.¹⁴ However, spending pressures for the 2023 elections may maintain higher than historical inflationary pressures.

Government spending is expected to remain elevated...

Subsidies to SOEs, capital spending and implementation of the PSPH policy are expected to keep government spending high. As global commodity prices remain elevated, the government’s blanket subsidy program on staple foods and fuel is expected to keep recurrent spending elevated in 2022 and 2023, while the PSPH policy, which is expected to be rolled out from late 2023, is projected to push spending up further. Although austerity measures may cushion some of the spending growth in 2022-23, upcoming election-related spending may increase government administrative and operational expenses. The continuous provision of blanket subsidies may exert undue pressure on government finances, and a better targeted subsidy program is recommended to reduce the overall fiscal burden. Capital spending is expected to remain elevated over the medium-term as government aims to complete the Velana airport terminal project in 2024, whilst housing, harbors, roads, and land reclamation projects continue in the medium term.

Figure A.26: Real GDP growth is expected to remain strong in the medium term

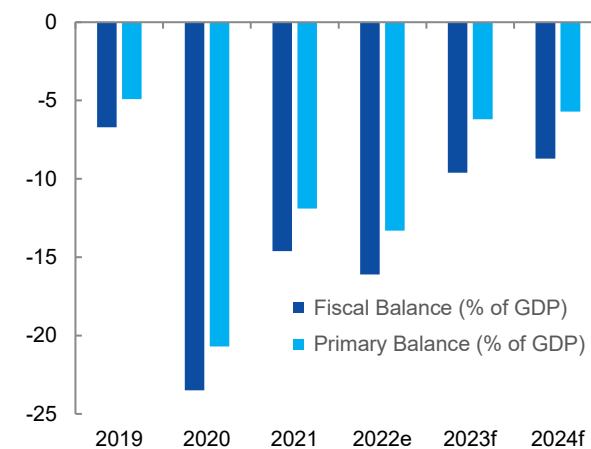
Year-on-year growth, percent



Source: Ministry of Finance and World Bank projections. Notes: 2022e denotes World Bank estimates.

Figure A.27: Revenue mobilization measures are projected to help narrow the fiscal deficit

Percent of GDP



Source: Ministry of Finance and World Bank projections. Notes: 2022e denotes World Bank estimates.

...but new revenue mobilization measures may improve the fiscal outlook to some extent.

Government’s proposed increase of the TGST rate from 12 to 16 percent and GGST rate from 6 to 8 percent, likely to be implemented in 2023, are expected to lead to additional revenues of 3 percent of GDP per year and help improve the fiscal balances over the medium term. As a result, the fiscal deficit is expected to decline from 16.1 percent of GDP in 2022 to 9.6 and 8.7 percent in 2023 and 2024, respectively (Figure A.27). These measures are a meaningful step towards a fiscal adjustment, but more is needed, especially on the expenditure side, including reducing the fiscal burden of SOEs and better managing the provision of several subsidized goods and services.

¹⁴ World Bank 2022d. October 2022

Despite the recovery in tourism, the current account deficit is expected to remain elevated.

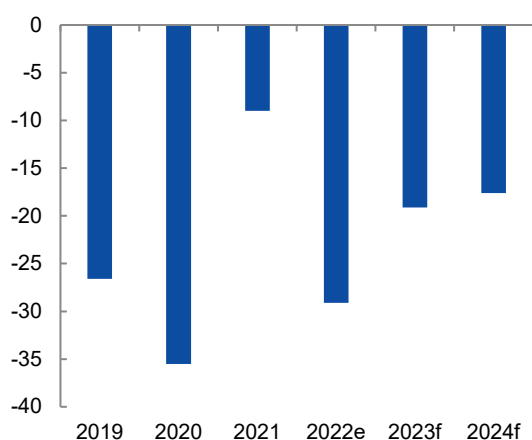
Imports of capital goods and growth in consumption spending are expected to keep the current account deficit high over the medium term. Heightened global commodity prices along with increased imports of construction materials and household consumption goods are likely to widen the current account deficit to 29.1 percent of GDP in 2022, before declining to 19.1 and 17.6 percent in 2023 and 2024, respectively as commodity prices normalize over the medium term (Figure A.28). Together with the large import bill, external debt repayment projections signal further pressures for official reserves which, as discussed, have depleted sharply in 2022 (Figure A.20).

A strong fiscal adjustment is required, given external debt distress remains a real concern.

As discussed, public debt significantly exceeds the size of Maldives’ entire economy. Although fiscal and current account deficits are expected to gradually narrow over the medium term, total PPG debt to GDP is forecast to remain elevated at around 120 percent (Table A.1). Such high levels of public debt, and associated refinancing risks, make the Maldivian economy very vulnerable to domestic and external shocks. Thus, despite improving growth and fiscal prospects, prudent debt management remains a top priority for improving fiscal sustainability, lowering the cost of growth-enhancing investments – especially with large debt service obligations coming due (Figure A.29) – and ensuring a more resilient economy going forward.

Figure A.28: Current account deficit expected to remain elevated due to higher imports

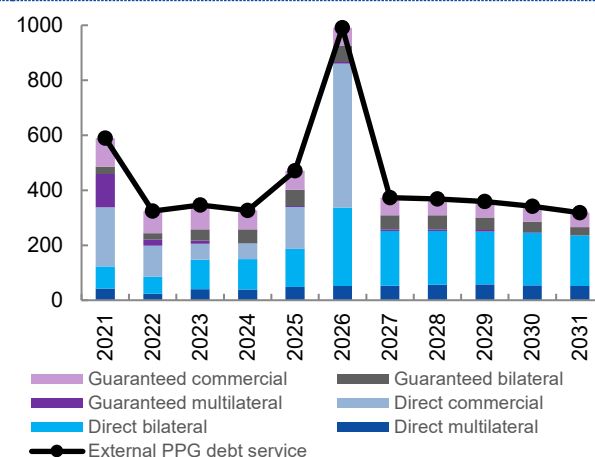
Percent of GDP



Source: Maldives Monetary Authority and World Bank estimates.

Figure A.29: External debt servicing projections show significant repayment needs in the medium-term

US\$ million



Source: Ministry of Finance and World Bank staff calculations.

8. Downside risks persist, so restoring fiscal and debt sustainability remain priorities

Significant downside risks cloud the medium-term growth prospects.

The global economic outlook is clouded by high levels of uncertainty, stemming from supply-side shocks caused by the pandemic and war in Ukraine, as well as monetary tightening measures to address rising global inflation. As discussed in Box 1, major economies are projected to experience a sharp slowdown in 2023. The existence of these global uncertainties, as well as any additional global shock, poses significant risks to Maldives’ economic outlook, especially if there is a slowdown in key source countries for tourists, as was the case during the height of the pandemic.

External financing risks are large and highly sensitive to global conditions.

External debt and fiscal vulnerabilities remain a significant concern for Maldives in the medium term. The country is projected to pay, on average, US\$330 million annually as external debt servicing over the 2022-24 period (Figure A.29). Debt servicing is then expected to reach US\$1 billion in 2026, which includes bullet payments for the US\$500 million Sukuk and US\$100 million private placement – significantly testing the country’s ability to repay or roll over this debt. The latter is also very much dependent on an improved global financing environment by 2026. While the government is taking steps to transfer some of its revenues to the SDF, which is designed to pay off some of the debt maturing, the limited resources in the fund may put Maldives in a difficult position and, thereby, further elevate the risk of not being able to service its debt. In addition, the continuation of high global commodity prices could lead to a sustained deterioration in the country’s fiscal and current account balances, and further deplete the official reserves while these high external debt repayments loom in the medium term.

Restoring fiscal and debt sustainability is critical for sustainable long-term growth.

A significant fiscal adjustment is needed. Government’s recently announced GST rate increases are a positive start, but not sufficient for the adjustment that is required. A notable reduction in (and more effective) spending is also required, especially for capital expenditures that are largely financed by external borrowing. These expenditure reforms, coupled with more effective revenue mobilization, are crucial for Maldives’ debt and fiscal sustainability. Reforms to Aasandha, reducing and rationalizing subsidies to SOEs, and better investment management – including in the housing sector (see Part B) – by considering PPP models, are amongst the key reform areas to bring down the high levels of public expenditure, replenish fiscal buffers against future shocks, and lower the cost of growth-enhancing investments. The housing sector in particular is a key source of fiscal risks, accounting for about a third of total external PPG debt outstanding and disbursed. As discussed in Part B, there are, however, options to address these risks. On the other hand, revenue mobilization can be improved by diversifying the tax base and mobilizing more domestic sources of revenue, reducing informality, and enhancing the tax morale and equity of the tax system.

Reducing the dependency on tourism and diversifying the economy remains a major challenge.

Maldives’ heavy dependence on tourism makes the country vulnerable to external shocks, emphasising the need for structural diversification of the economy. Having built a reputation for luxury tourism, Maldives could benefit from a more diversified tourism sector that also provides benefits to those living in the outer Atolls and inhabited islands. Boosting the fisheries sector by expanding fish processing facilities and reaching new export markets could help reduce the country’s high dependency on tourism. Additional avenues for diversification, trade and growth also need to be explored.

B. Facilitating Affordable and Sustainable Housing Provision



1. The challenge of affordable housing provision in a small island state

Maldives faces unique housing constraints...

As a small island state, Maldives faces unique housing constraints including high construction costs due to the scarcity of land, lack of technical expertise, and heavy reliance on imports. Over a third of the population of Maldives is concentrated in the capital, Malé, drawn by its educational and employment opportunities. The wide dispersion of the rest of the population and lack of economies of scale make it difficult to provide even service coverage, leading to wide disparities in access to public services between Greater Malé and the atolls. Internal migration to Greater Malé has led to overcrowding and overdevelopment in the capital, while unplanned growth has resulted in traffic congestion and air pollution in the city. To address the development pressures, the Government of Maldives (GoM) has pursued land reclamation, notably on the neighboring island of Hulhumalé and now beyond. However, such undertakings have been costly and at the expense of natural ocean habitats. Furthermore, as the Maldives lacks natural resources and a domestic production base, all construction materials are imported, weighing on the trade balance and external financing needs, and developers must often rely on foreign technical assistance and labor.

...and private sector participation in new affordable housing construction is low.

New affordable housing provision is overwhelmingly led by the government. Private construction is limited to high-end residential and commercial buildings, hotels and resorts, and owner-driven residential developments for investment and the rental market. The high cost of construction materials and lack of access to domestic construction finance hinders engagement in the affordable housing sector. Furthermore, the limited number of local banks have a low appetite for financing the social housing sector, precluding private participation in the affordable construction sector.

Home ownership remains a challenge...

Government of Maldives (GoM) initiatives to improve access to land have not yielded an increase in home ownership. GoM has allocated land for free to households to increase the supply of housing in the atolls. However, without proper targeting and technical assistance, the strategy has not resulted in an increase of housing units. In addition to the economic benefits of migrating to Malé, most households owning land plots in atolls have been unable to build housing due to lack of financial resources and knowledge. The absence of technical support and guidelines for self-built housing has resulted in parcels that are left undeveloped, unfinished, or poorly built.

... and the majority of households in Greater Male resort to rental.

Partly due to these constraints, home ownership is unaffordable for most Maldivians, especially in the Greater Malé region. According to World Bank estimates, a household would need to have a monthly income of around MVR 46,000 (US\$3,000) to be able to afford the most inexpensive available 2-bedroom flat in the market, which is estimated to be priced at MVR 1.8 million (US\$117,000). Currently, only the richest (top 20th percentile) of Maldivian households, who have average monthly incomes of MVR 57,000 (US\$3,700), would be able to take out a bank loan to make this purchase. As a result, most households living in the Greater Malé region cannot afford to purchase a home, but instead rent their accommodation. According to the 2019/20 HIES, 74 percent of households living in Malé rented their homes in 2019, an increase from 64 percent in 2016.¹⁵

Rental prices are also out of reach for many households, leading multiple families to co-inhabit the same unit.

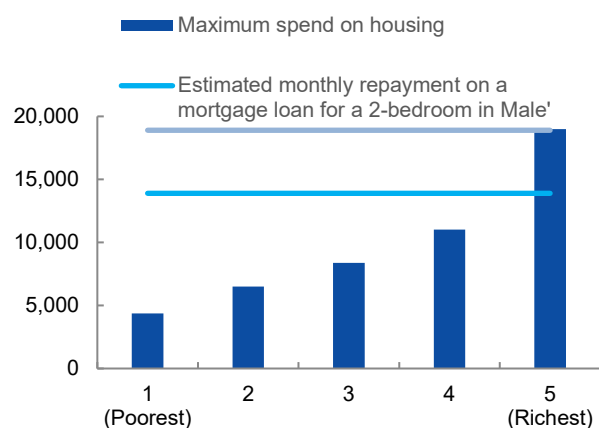
Due to the high housing rental prices which are out of reach for many families, overcrowding of homes is an issue in the Greater Malé region, affecting about 12 percent of households (and disproportionately affecting lower-income households). Assuming the cheapest available 2-bedroom rental flat in Malé costs MVR 18,900 (or US\$1,227) monthly, households in the bottom 60 percent of the distribution would have to pool their incomes to be able to afford the rent. Assuming that households do not spend more than a third of their income on rent, this means that 2-4 families have to share the same apartment, hence leading to overcrowding (Figure B.1). In a World Bank MUDRP¹⁶ survey conducted in 2021, about 56 percent of respondents in Malé and 51 percent of respondents in atolls responded as being unsatisfied with their current housing conditions (regardless of ownership or rental), noting the lack of space as the key driver of their dissatisfaction (Figure B.2). However, despite their high dissatisfaction with current housing conditions, survey respondents were hesitant to move elsewhere due to the lack of alternatives.

¹⁵ Statistics Maldives 2016, 2019.

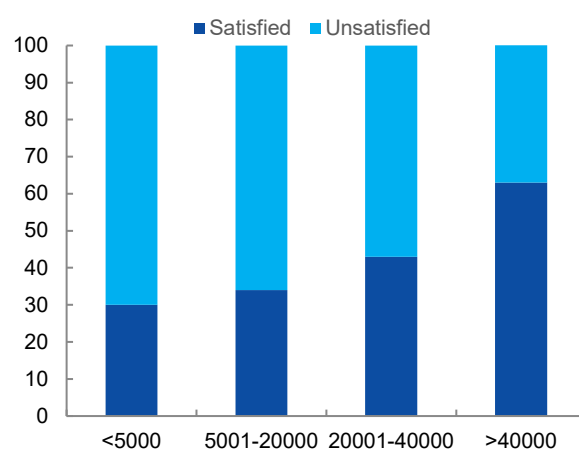
¹⁶ World Bank MURDP 2021. Maldives Urban Development Resilient Program (MUDRP) is a World Bank lending program. The housing study was led by the Ministry of National Planning, Housing and Infrastructure (MNPFI) and supported by the World Bank.

Figure B.1: Purchasing a home is out of the question for many Maldivians **Figure B.2: Independent of tenure, most Maldivians are dissatisfied with their current housing situation**

In MVR



Share of survey respondents, percent



Source: Staff calculations based on Statistics Maldives, 2021 and WB MUDRP study 2021.

Source: WB MUDRP study 2021.

Note: Flat price is assumed to be MVR 1.8 million. Monthly rent is assumed to be MVR 18,900.

The undeveloped housing finance market has curtailed access to affordable housing.

As in most small island states, Maldives' financial sector is under-developed, with limited access to long-term financing and housing finance programs. The mortgage market is small, with outstanding loans at 7 percent of GDP – half the expected size for a country with Maldives' level of income. Only three banks, notably the Bank of Maldives (BML), the Maldives Islamic Bank (MIB) and the Housing Development Finance Corporation (HDFC) actively lend in the housing sector. Housing finance is largely inaccessible to them for two reasons:

- **Mortgage loans require a 20 percent down payment; building such equity is very difficult for most low-income households.** Banks require a 20 percent down payment, on par with international prudential measures for residential mortgage loans. Lower-income households cannot easily save for a down-payment, and at present there are no demand-side government subsidies to address the affordability gap between commercial mortgage loan products and the high savings requirement.
- **Undeveloped regulations are a key constraint to banks' risk appetite and mortgage market growth.** Strata title registration on newly completed housing projects can take up to four years to be issued. This forces banks to carry the risk of un-collateralized loans while waiting for title registration. When banks decide to foreclose on a borrower, they are exposed to a long court foreclosure process that can take up to 8 years to resolve, increasing the cost of loss provisioning and quickly recouping non-performing loans (NPLs).

2. Large public spending and fiscal risks associated with the housing sector

The government's housing related debt exposure is at 19 percent of GDP...

The government's exposure from external loans and guarantees associated with public housing is estimated at nearly US\$1 billion or approximately 19 percent of GDP as of 2020. In the past decade, the government has significantly ramped up public investments to address the lack of affordable housing. From 2010 to 2021, the government and the Housing Development Corporation (HDC), a 100 percent State-Owned Enterprise (SOE), contracted 11 external loans amounting to US\$1.1 billion to finance the construction of housing units, primarily in Hulhumalé. The government further guaranteed US\$134 million in external loans to HDC to design and construct roads and electricity systems in Hulhumalé. Most of these obligations were signed in 2017 and 2018 in the form of guarantees to HDC, leading the external guaranteed debt ratio to jump by 12 percentage points of GDP in a single year. Combined, total external debt outstanding and disbursed related to housing (including guarantees) amounted to an estimated US\$739 million at end-2021, equivalent to a third of the total external public and publicly guaranteed debt. The bulk of this debt (86 percent) is due to Chinese lenders – particularly the Industrial and Commercial Bank of China or ICBC.

...and the cost of housing-related debt repayments is high.

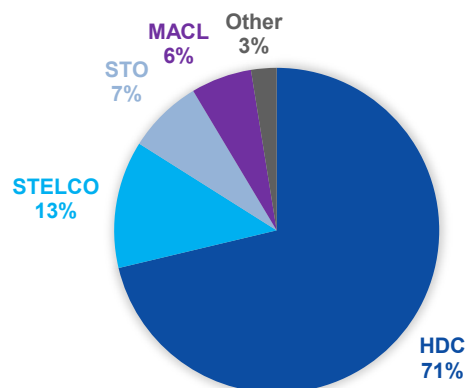
From 2021 to 2028, Ministry of Finance (MoF) estimates indicate that debt service payments on existing housing-related debt will amount to US\$40 million annually on average, or about a third of total external debt service due over the period. The high cost of debt servicing reflects the expensive terms of all six guarantees HDC contracted in 2017-2018, which had short grace and maturity periods (2 and 3-13 years, respectively) and variable interest rates (3-3.3 percent plus 6-month LIBOR).

Revenues from public housing projects are insufficient to cover debt service repayments...

HDC accounts for over half of external guaranteed debt (Figure B.3), but its projected revenues from rental payments on public housing projects are insufficient to cover the high cost of debt servicing, which is mostly due in the short- and medium-term (Figure B.4). In line with the social housing mandate, the government has also 'capped' monthly rental rates for Rent-to-Own program beneficiaries, tolerated high delinquency rates on loan repayments and provided lengthy repayment periods (up to 25 years). ***The cost of debt service is thus a major fiscal risk that will likely have to be borne by the public sector balance sheet.*** HDC's other revenue sources such as sales of land are uncertain, as they depend on external timelines and buyers' demand. HDC itself is highly leveraged and holds more foreign currency liabilities than assets.

Figure B.3: HDC accounts for over half of guaranteed debt to SOEs

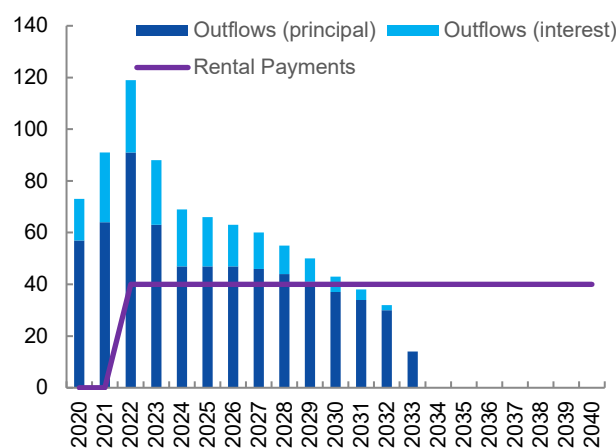
Share of total external guaranteed debt, percent



Source: MoF Public Debt Bulletin, December 2020.
 Note: Excludes the US\$400 million MMA swap with RBI and a US\$121 million guarantee to Ahmed Siyam Holding, a private entity.

Figure B.4: There is a mismatch between HDC's debt service repayments and rental payments

US\$ millions



Source: World Bank analysis based on estimates from MoF received on 24 February 2021.
 Note: Rental payments assume 100% of all units are leased starting in 2022 at the monthly rate of MVR7,500.

... and fiscal risks from housing may become even more significant going forward.

In 2019, a new housing agency, the Fahi Dhiriulhun Corporation (FDC) was established to take on the bulk of social housing development and implementation from HDC. However, FDC lacks the revenue and cross-subsidization sources that HDC has traditionally relied on such as land leasing and sales of properties. Capital expenditure and fiscal risks related to housing are thus likely to increase as FDC contract external loans to develop its pipeline of two new projects of 4,000 housing units, with a total funding requirement of approximately US\$226.5 million.¹⁷ Unlike HDC, FDC will be fully reliant on capital contributions from MoF to address any cash flow imbalance, given its lack of revenue sources beyond the social housing projects.

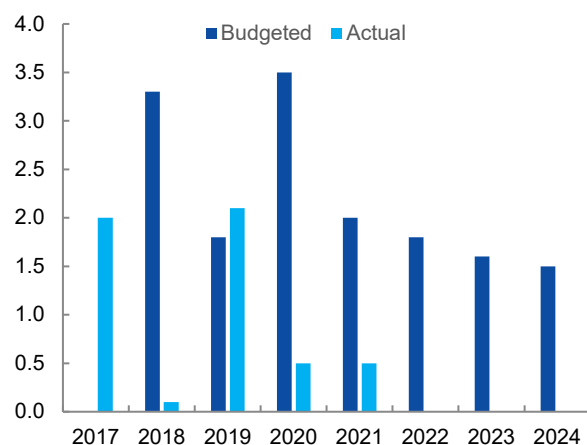
Housing SOEs receive significant support.

Housing development expenditure financed by domestic resources is not high, but housing SOEs receive significant support. On average, only US\$3 million or 2.3 percent of total expenditures is budgeted for housing development each year, which is on par with the share of budget spent for housing in several other emerging market economies. Actual expenditures have come in at about half of that amount (Figure B.5). These resources have generally funded the construction of social housing projects in the atolls. However, the government also makes significant capital contributions to HDC and FDC. Between 2018-2020, the government provided US\$135.2 million in capital contributions to HDC and US\$0.8 million to FDC, or approximately 60 percent of total capital contributions over the period (Figure B.6). HDC relies on such contributions to balance out its operational losses. Finally, the government foregoes tax revenues by providing Goods and Services tax exemptions on sales of properties classified as social housing, and by providing land for free for self-built homes and developer-led housing projects.

¹⁷ Loan of US\$226.5 mm to EXIM bank of India to build two projects (4000 units) in Hulhumale in 2021. A third 2000-unit social housing project is on the way.

Figure B.5: Domestically financed housing development spending is not high...

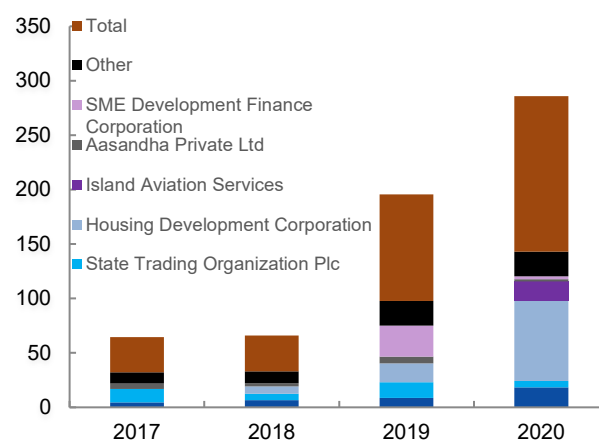
Housing development as a share of total budget, actual and budgeted expenditures (% of total)



Source: MoF, WB staff calculations.
Note: 2022-2024 refer to proposed budget estimates.

Figure B.6: ...but the government transfers an increasing and significant number of resources to housing SOEs

Capital contributions to SOEs, US\$ millions



Source: MoF, WB staff calculations.

The lengthy foreclosure process could pose financial risks for the banking sector in the longer term.

Even though commercial banks have a low level of exposure to the housing sector, the lengthy foreclosure process could pose financial risks in the longer term. Interest rates and household incomes are two key determinants for assessing commercial banks’ exposure to real estate. While the average interest rate has been relatively stable at 11.5 percent over 2018-2021, household income has been adversely impacted by the large contraction in GDP growth in 2020 due to the COVID-19 pandemic. Nonetheless, the moratorium on housing and other loan repayments cushioned the impact on loan repayments. The NPL ratio declined from 9.4 in 2019 to 7.5 percent at end-Q3 2021. Moreover, real estate represents only 7.1 percent of commercial banks’ total loan portfolio, and the mortgage debt-to-GDP ratio is low at 7 percent. While banks’ requirement of a 20 percent down payment theoretically protects them in the case of default, the lengthy foreclosure process and the lack of foreclosure laws put banks at high risk of loss in the event of a default. Reform of the foreclosure process is needed to ensure that default rates on housing loan repayments do not become a systemic financial risk.

3. Is public spending on housing and the Rent-to-Own Program efficient?

Affordable housing for all Maldivians has long been a key government priority.

Since the formulation of Maldives’ first National Housing Strategy in 2009, national strategic plans have included large-scale housing interventions to achieve this goal. The 2019-2023 Strategic Action Plan outlines ambitious policy actions to increase the accessibility and affordability of housing, including (i) the provision of 20,000 new social housing units, (ii) the allocation of MVR 1 billion (US\$65 million) for the social housing loan scheme (*Gedborweriya*), and (iii) the plan to enact a tenancy and condominium law. To meet the government’s housing provision goal, public spending on housing is concentrated on supply-side strategies, namely: (i) the Rent-to-Own program in Hulhumalé (Phase 1 and Phase 2 – the latter is also called “Hiyaa”); (ii) the Rent-to-Own program in the atolls; and (iii) *Gedborweriya*, which provides a subsidized 6 percent fixed-rate loans to eligible households in the atolls for housing construction and upgrades.

The Rent-to-Own Program has cost the government a significant amount of public resources.

The Rent-to-Own Program is the primary public housing scheme in Maldives and has cost the government a significant amount of public resources. Under the Hulhumalé Phase 1 project, the government built five sub-projects totaling 2,592 housing units (1, 2, 3 and 4-bedroom units) in 4-story, low-rise buildings.¹⁸ Hulhumalé Phase 2 (Hiyaa) was even more ambitious in scale: 6,720 housing units were built in 16 blocks of 25-story high-rises, but the units were uniform (2-bedroom units of 550 square feet). To purchase their flats, Phase 1 beneficiaries pay MVR 2,000 to 7,000 or US\$130 to US\$455 monthly over 20-25 years to HDC, whereas Phase 2 beneficiaries pay MVR 7,500 or US\$487 monthly over a 25-year period. The estimated combined cost for the Hiyaa project is MVR 10.5 billion or US\$679 million, as laid out in (Table B.1). This works out to about MVR 1.6 million (US\$101,000) per unit, or MVR 1.3 million (US\$82,000) per unit excluding the land cost. To finance this, HDC contracted several expensive loans from external creditors such as Credit Suisse and ICBC.

Table B.1: The per unit cost of the Hiyaa public housing is extremely high

Components	Cost (MVR billion)	Cost (US\$ million)
Land	2.1	133.1
Infrastructure	1.1	71.4
Construction	7.1	459
Refinancing of debt	0.2	14.9
Total cost	10.5	678.5
Cost per unit	MVR 1,554,895	US\$100,967
Cost per unit excluding land	MVR 1,249,875	US\$81,160

Source: WB MUDRP 2021.

The government provides a subsidy of approximately US\$31,800 for each Hiyaa unit...

Overall, it is estimated that the government provides a subsidy of approximately US\$31,800 for each Hiyaa unit. Given the low monthly Rent-to-Own payments of MVR 7,500 (US\$487), the per unit economic cost of the Hiyaa is MVR 489,000 (US\$31,800), accounting for 39 percent of the total combined cost of construction, infrastructure, and refinancing. If land were to be included in the total cost, the subsidy would be 69 percent of the unit cost. This subsidy calculation excludes cash flow reduction due to the high default rates, repair and maintenance costs exceeding the MVR 1,000 (US\$65) monthly maintenance payment by tenants (if paid), and refinancing costs due to HDC's tight cash position.

.. and completion failures incurred further costs for the government and the people.

The weaknesses in the Hiyaa project design and implementation have led to the project not completing to a satisfactory standard and further costs being incurred for the government and the people. The Hiyaa project has several design weaknesses: (i) the 25-story high-rises are an unusual building typology in Maldives, where households typically live in low-rises or single-family homes; (ii) each of the 16 housing towers has four small elevators within narrow lobby areas to serve more than 400 units, leading to congestion during peak hours and requiring HDC to incur additional costs to extend the lift lobby areas in several towers; and (iii) units have been left unfinished, with beneficiaries expected to complete the remaining work at their own cost. BML provided home improvement loans up to MVR 150,000 (US\$9,740) to enable households to finish and furnish their new flats, but it is unlikely that all beneficiaries will be able to afford the additional expense.

¹⁸ 5 sub-projects are: 280 flats (2004); 120 flats (2007); 488 flats (2009); 1000 flats (Sept 2013); and 704 flats (2017)

Changes in allocation criteria have led to uncertainties.

The public perception is that the Government is obligated to provide housing to deserving citizens based on allocation criteria that shift with new government administration. In selecting households for the Rent-to-Own scheme, the Ministry of National Planning, Housing and Infrastructure (MNPHI) does not assess a household's repayment capacity and therefore cannot ensure that selected households will regularly pay the social housing rent. HDC is only responsible for collecting against the rental contract and has no prerogative over households' selection.

Rental default rates are high as HDC has limited ability to enforce collection.

Although the law and several court decisions state that the HDC has the right to evict households who are delinquent, eviction is not enforced. Furthermore, given that HDC is neither a bank nor a financial services company, it has no ability to report rental delinquencies to the Credit Information Bureau.¹⁹ Rental default, defined as non-payment of 90 days and above, of all social housing projects in both Hulhumale phase 1 and 2, are high, averaging at 37 percent across all projects (Table B.2) as of July 31, 2022. HDC's short-term solution has been to reschedule the payments by extending rental tenure, though not with significant impact.

Table B.2: The default rate of the Rent-to-Own projects in Hulhumale

Hulhumale	Project	Start Date	Total Occupied Units	Number of default customers	Default percentage by count
Phase 1	280 Flats	June '04	204	84	41%
	120 Flats	Jan '07	82	27	33%
	488 Flats	Jul '09	518	210	41%
	1,000 Flats	Sept '13	963	278	29%
	7041	2017	702	217	31%
Phase 2	Hiyaa 2	April '22	6338	2,345	37%

Source: HDC and HDFC reports as of July 2022.

(1) 704 project is managed by MNPHI (Construction Department). Rentals are being collected by HDFC on behalf of the GoM. All other projects are managed by HDC.

All in all, Hiyaa has exacerbated HDC's financial vulnerabilities...

HDC has faced cash flow shortfalls that endanger the long-term financial sustainability of the Hulhumalé Phase 2 project. In 2019, HDC took four loans totaling US\$40 million to refinance the Hiyaa project's interest and principal repayment obligations. The pandemic has added to HDC's financial hardship, and its cash ratio has been severely constrained due to the shortfall in revenues. The company is also at risk due to the long delays in project lease up, as HDC absorbs all risks once units are built (developers are paid upon project completion and pre-lease up). Finally, there is a mismatch between the lengthy repayment period and low monthly repayments, as well as the high cost of servicing debt in the short and medium term (Figure B.4).

...and there are significant delays in the completion and allocation process.

Outside of Hulhumale, the construction of Rent-to-Own programs in the atolls face significant delays in the completion and allocation process resulting in some households receiving sub-standard units. Housing developments built through the Rent-to-Own Program, especially those in the outer atolls, have faced lengthy delays through construction and lease up. The reasons, as highlighted by respondents to the

¹⁹ At this writing, there is an effort to change the policy to allow HDC to report rental delinquencies to the Credit Information Bureau.

World Bank MUDRP study, include changes in administration and project management issues leading to delays in construction completion.²⁰ These delays are considerable: lease-up took two years in Addu, six years in Thinadhoo, and 6-7 years in Kulhudhuffushi. The lengthy allocation process has degraded the quality of housing units, which were left vacant for years. As a result, beneficiaries were forced to pay for repair and renovation work when they moved in.

4. Is the Rent-to-Own Program effective?

The Rent-to-Own scheme's effectiveness has been marred by poor targeting of beneficiaries.

Despite the government's considerable financial investment in the Rent-to-Own scheme, its effectiveness has been marred by poor targeting of beneficiaries. To select recipients, the government scores applicants based on the number of their dependent children, current living conditions (e.g., the number of bathrooms/rooms versus the number of people residing in the household), and whether applicants already own other housing and land. These eligibility criteria do not filter out higher-income earners, resulting in a huge housing application backlog (as almost everyone is eligible to apply). Moreover, confirming households' declarations of their living conditions is a costly and lengthy process that requires resources. Since the number of applications has significantly outpaced the number of available social housing units, the verification process leads to delays in the selection process.

The Hiyaa project prioritizes specific demographic and job categories, rather than income.

Similarly, the Hulhumalé Phase 2 (Hiyaa) project prioritizes specific demographic and job categories, rather than income. Thirteen categories of applicants were prioritized to receive Rent-to-Own housing under the Hiyaa project. Among these groups were civil servants, married people between the ages of 18 and 35, and Malé residents who had previously experienced issues with public housing projects. Other priority categories were teachers, single parents, doctors, and nurses. This practice of prioritizing employment types, with several in the highest income segment, counters the social housing targeting principle to serve those most in need of government support. As a result, the rental rate for Hiyaa is the same across all employment categories, regardless of households' income and capacity-to-pay.

Rent-to-Own assets are more valued by many beneficiaries as investment assets.

Rent-to-Own assets are not being used as intended by the government housing policy but are more valued by many beneficiaries as investment assets. By law, beneficiaries of public Rent-to-Own units in Hulhumalé cannot sublease or resell their units until they have fully paid for their flat. However, according to several stakeholders interviewed for the World Bank MUDRP study, sub-leasing social housing units at commercial rental rates (that can go as high as ten times the Rent-to-Own rate) is a common practice in Hulhumalé.²¹ While HDC is aware of this practice, it has not been able to take any actions to prevent nor enforce the law requiring social units being used only by beneficiaries.

Rent-to-Own design limits households' capacity to transition to ownership until the end of the contract.

On the other hand, Rent-to-Own design limits households' capacity to transition to ownership until the end of the contract and from monetizing the property as a financial asset. The rental contract locks beneficiaries in a long-term commitment of up to 25 years as a renter in two detrimental ways. One, it prevents households from accommodating evolving housing needs or lifestyles that would call for different home sizes, types, or locations. Second, households who have capacity to transition toward ownership by prepaying to gain early home ownership are not able to do so. The Rent-to-Own program's "one-size fits all" structure treats all households

²⁰ World Bank MURDP 2021.

²¹ World Bank MURDP 2021.

similarly, regardless of their capacity to pay and housing preferences.

Most public housing beneficiaries are dissatisfied with the outcomes.

According to the World Bank MURDP study, 72 percent of all respondents who participate in the Rent-to-Own scheme are dissatisfied with their homes. Reasons include: (i) the poor construction quality of many public housing units (e.g. loose floor tiles, plumbing issues with sinks and toilets, water leaks), coupled with the lack of maintenance, leading to substandard living conditions for program beneficiaries; (ii) lack of minimum safety guidelines or design standards resulting in beneficiaries feeling unsafe in their homes (e.g., a lack of supporting facilities, security services, or safety features such as proper lighting and surveillance of public spaces; and beneficiaries experiencing theft, vandalism, and misuse of public spaces); and (iii) lack of consultation on living preferences (e.g., housing projects not addressing preferences, weather considerations regarding the design of units, climate risk considerations, etc.).²²

5. Spending more will not necessarily help the government solve housing problems

Despite high government spending having been used for housing, the challenges persist.

The Government of Maldives has directed a significant number of resources to tackling the challenge of affordable housing, but so far fallen short of the SDG goals of safe, adequate and affordable housing. Among the key constraints that hinder the efficient and effective delivery of government housing expenditures are:

- (i) ***'One-size fits all' housing strategy.*** Households have diverse needs in terms of housing types (ownership, rental, Rent-to-Own, housing upgrade/expansion, etc.), locations (Greater Malé vs. other atolls), income, and employment type (low-mid-high income; salaried/non-salaried). Until recently, 90 percent of public funding in the housing sector has been directed to the Rent-to-Own Program in Hulhumalé at the expense of other housing needs. It is also unclear whether the government's plan to build 1,575 units in 14 atolls starting in 2022 adequately meets housing needs in the atolls, or if new units will be left vacant given the internal migration to Greater Malé. The current administration's decentralization agenda requires a more nuanced housing strategy that considers the diverse needs of households.
- (ii) ***Overlapping and weak institutional arrangements and capacity:*** Starting from 2019, FDC was supposed to replace HDC and MNPHI in social housing financing, provisioning, and implementation. Nevertheless, HDC continues to manage the completed social housing projects in Hulhumale Phase 1 and 2, and the Rent-to-Own housing developments in the atolls is continuing responsible by MNPHI - Housing Department. Over the next few years, once FDC completed construction of its social housing projects in Hulhumale Phase 2, the risk of duplication and administrative overlap between HDC and FDC will become more apparent, and the poor coordination and implementation capacity of the key housing stakeholders will likely continue to impact the performance and results of the government social housing programs.
- (iii) ***Lack of an integrated housing project data system:*** The basic data on public housing projects such as construction start/completion date, target units/completed units, budget versus actuals, construction costs, monitoring and evaluation data are not centralized nor easily accessible across the

²² World Bank MURDP 2021.
October 2022

different key housing stakeholders (i.e., MNPHI, MoF, HDC, FDC, HDFC, island councils, etc.). The absence of data consolidation on a project-by-project basis precludes the government's ability to assess: (i) the inherent cost of the project; (ii) the level of subsidy/support per project, per unit, or by income segmentation; and (iii) the performance of the project and how to improve it. A transparent monitoring process of public housing programs could lead to more timely adjustments to improve program implementation.

6. Recommendations: How can the government achieve its housing policy goals without jeopardizing fiscal and debt sustainability?

Expensive external debt has not helped meet SDG goals of providing adequate, and affordable housing.

This discussion has illustrated that Maldives' public housing expenditure – mostly financed through expensive external debt – has not helped the government meet the Sustainable Development Goals (SDGs) of providing adequate, safe, and affordable housing. Rather than take on more costly external debt to finance large-scale Rent-to-Own programs and trapping such funds pay-back under the Rent-to-Own contract for up to a 30-year period, the government could undertake three sets of reforms to address institutional and organizational gaps that significantly impact the provision of social housing in Maldives. These are divided into three categories: (i) **targeting** and housing policy and regulatory reforms; (ii) **reforming the Rent-to-Own program** to attract more private participation in the housing sector on both supply and demand-sides; and (iii) **enabling environment reforms** to improve the implementation of housing policies and programs.

Pillar 1 – Targeting and housing policy and regulatory reforms

Improved targeting is critical.

Clear targeting in social housing programs is critical to improve the efficiency and effectiveness of public spending in the housing sector, thereby ensuring that public funds are spent on supporting households with the greatest need. While the draft National Housing Policy (dated July 2020) provides a better definition of low-income housing and a clearer understanding of the targeted segments for future public housing (Table B.3), implementing the policy would require better mechanisms for verifying income. To avoid sub-leasing of public housing and to create an exit strategy for households who are no longer eligible for a housing subsidy, the government could place targeting and income verification requirements at the time of original purchase or rental move-in and at regular intervals. Annual home visits and income recertification would help to confirm that beneficiaries continue to reside in the unit and are eligible for assistance.

Table B.3: Housing programs need to be better targeted based on income

Housing Typology	Monthly Rent/Loan Repayment	Property Value (MVR)	Income Segment (Monthly income in MVR)
Council Housing	Free or Subsidy	755,580	Below 15,000
Affordable Housing	8,600 to 13,000	1 million to 1.5 million	15,000 – 25,000
Mid-range	13,000 to 23,8000	1.5 million to 2.5 million	25,000 – 45,000

Source: MNPHI 2020.

A fair, transparent, and predictable legal and regulatory framework for housing is necessary...

A fair, transparent, and predictable legal and regulatory framework for housing is a critical determinant of investment decisions for both public and private sector stakeholders. Hence, improving the legal and regulatory framework is crucial on both supply and demand sides. On the supply-side, a set of new regulations, including a new Land Law, Building Code, and Tenancy Act have been either adopted or are being drafted, but have not yet been implemented at the time of this report. On the demand-side, Title Registration legislation, Foreclosure Act, and Bankruptcy and Solvency Act would reduce lending risks for banks and would help to catalyze a more healthy and resilient growth for the mortgage market.

...and a successful land policy.

Land rationalization is key to an effective and sustainable public housing policy. The current allocation of free land to households has been neither strategic nor economic. Land allocated in the atolls remains vacant and low cost, while land allocated in Hulhumalé to Malé households would carry far more value for those beneficiaries. New land reclamation initiatives to expand available allocations are very costly and environmentally detrimental. Furthermore, comprehensive urban planning and data management systems for land are scarce, leaving policymakers with little ability to make data-informed decisions. Finally, the lack of a secondary land market in Maldives have affected land-related decision-making processes and the development of a commercial real estate market. It is essential that MNPHI reevaluates the existing free land policy, support the capacity of local councils to design and implement strategic land policy and land use plans, and establish an improved land data management system.

Pillar 2 – Reforming the Rent-to-Own Programs

Reform the Rent-to-Own program while strengthening private sector engagement.

The Rent-to-Own model faces significant challenges, including the lack of financial sustainability, targeting issues, and weak design and implementation. The following are specific ways to optimize this program:

- (i) ***Redesign the Rent-to-Own product:*** Currently, the shorter-term capital funding for the development of Rent-to-Own housing units is constrained by the longer-term 25-year Rent-to-Own Program repayment plan. Incentives between households and the government ought to be better aligned to improve the program’s fiscal sustainability and the evolving housing needs, preferences and capacity to pay of beneficiaries. This can be done by redesigning the eligibility criteria based on beneficiary income to enable a more progressive level of subsidy support. For example, middle-income earners can be given the option to purchase their homes with a mortgage loan and subsidy, while low-income earners can progress through different rental payment levels in line with their capacity to pay.
- (ii) ***Strengthen the targeting system:*** The GoM needs to reassess the targeting and eligibility criteria, and reform its assessment and compliance systems to improve household targeting under the Rent-to-Own Program. In addition to being screened for income eligibility, beneficiaries should also be screened by capacity to pay prior to being allocated a unit. Annual recertification of tenure and income would limit illegal subleasing and ensure those with the highest need are given assistance. This redesign would also improve the program’s cash flow, thereby mitigating fiscal risks to the GoM. Tools available for the GoM are means-testing, partnering with banks for income verification and assessment, and using available data such as credit bureau information – all of which would reduce the rate of mistargeting and

eventually the risk of delinquency. Implementing an integrated data management system for all Rent-to-Own properties would also provide a clear picture of beneficiaries' behavior and challenges.

- (iii) ***Improve capacity to manage properties:*** Rental property management requires specific knowledge and processes which are currently missing from the Rent-to-Own housing program. The government could consider establishing a joint venture between the newly established social housing implementing agency, FDC and an international non-profit housing management entity so that FDC can learn and implement property management skills and processes. Developing a robust maintenance plan and budget would also be a critical part of this effort. The value of the GoM and beneficiaries' investment in the Rent-to-Own program will in large part be determined by how well buildings are maintained for decades to come.
- (iv) ***Create permanent affordable rental stock while partnering with non-profit housing agencies for rental management.*** As previously noted, many Maldivian families cannot afford to rent homes without pooling incomes in the Greater Malé region. Rather than solely promoting home ownership, the government could provide a rental subsidy or voucher to eligible households to facilitate rental payments, and create permanent rental housing stock to mitigate housing shortages. The government could also leverage domestic or international housing non-profits with the capacity to manage permanent affordable rental housing to play a more prominent role. This would enable the government to disassociate itself from the role of collection agent, thereby reducing moral hazard, and thus limiting high delinquency rates in public housing schemes.

Strengthen private sector engagement.

The private sector can play a more prominent role in the development of affordable housing, both on the supply and demand sides. Currently, Maldives' commercial banks have limited risk appetite to provide construction financing to developers/contractors and mortgages for low-income and non-salaried workers due to their internal limiting guidelines and capital requirements. The government can explore the use of incentives and technical assistance to support banks in reaching the low- and informal income segment. These could include: (i) co-investing in mortgage (credit loss) guarantee schemes; (ii) developing alternative credit scoring for informal and low-income workers in partnership with financial technology companies to improve underwriting capacity; and (iii) exploring innovative loan products such as incremental housing loans that better meet the needs of the consumers. Moreover, addressing the lengthy foreclosure process is key to ensure that the banking system can manage losses in the event of a default.

Use of public-private partnerships (PPP) to develop mixed-income housing:

Although not without its risks, PPPs can help Maldives engage a broader range of private sector developers in the housing sector, potentially increasing efficiency, and economies of scale. New housing PPPs would create the opportunity for a proof-of-concept laboratory to develop demand-side products (loans, savings programs, down payment assistance, others) that are compatible with supply-side initiatives. The PPP model would also allow various offtake solutions within one development to increase financial viability and to promote mixed communities. However, PPPs are not without their fiscal risks (see Box 3) and are not a guaranteed mechanism to reduce the costs of building affordable housing in Maldives. Establishing a legal and regulatory framework to monitor PPPs and ensure adequate risk sharing is critical to maximizing their benefits while minimizing their costs.

Pillar 3: Improve the enabling environment for program implementation

Reform institutional arrangements to develop distinct mandates for HDC and FDC.

To address the institutional efficiencies described earlier, the government could establish clear mandates for key institutions in charge of housing. Rather than splitting these by housing typologies and income segments (social housing for FDC and market-priced housing for HDC), the distinction between the two state-owned agencies could be based on their roles:

- *FDC could take on the ‘post-offtake’ ownership role and become the property manager for all affordable housing projects (Greater Male and atolls)*, which would significantly improve its rental cash flows and quality of public housing assets. It could cement joint ventures with international property managers to build capacity and implementation know-how, as described in the prior section.
- *As for land use and allocation, HDC has undertaken this role for Hulhumalé and could potentially do it for the entire country*, with decentralized agencies or branches in different atoll regions or islands. HDC could support other housing agencies and/or local councils in engaging more proactively in land markets in the atolls, helping them create long-term development plans and adjust land allocation according to local development needs (e.g., releasing public land in stages, or bidding it out through an auction process to private investors).

Develop an integrated housing data system for policy making and project monitoring.

A healthy housing market benefits from an integrated housing data system that allows public and private stakeholders to quickly assess market needs and find the most efficient ways to fulfill them. Such a system would include data on consumer housing needs and demand (by location, income, and employment), construction updates, home price trends, and rental data. Access to reliable and timely housing-related data can help Maldives to develop targeted regulations and policies, monitor the effectiveness of public housing programs, and accelerate private sector investments.

Strengthen disaster and climate-resilient building practices.

Despite its high vulnerability to disaster risks and climate change,²³ Maldives currently lacks a comprehensive framework for resilient building practices (e.g., construction permits, code compliance monitoring and green construction guidelines and certification). Existing construction standards fail to account for disaster and climate risks, green and energy efficient construction materials and techniques are not prioritized, and there is limited quality assurance and control, particularly for low-rise houses. While the MNPHI issued the Construction Act in 2017, further work is needed to ensure proper compliance with regulations, standards, and procedures. For public housing specifically, the government can further collaborate with the private sector to ensure the inclusion of code-compliant and climate-smart aspects into the design structure, engineering, construction, materials, monitoring, and certification of housing units. In the medium- to long-term, the process of integrating resilience into land use planning, regulations, land tenure, building codes, and building approval processes would further promote resilience in housing and buildings. Alternative construction technologies that support climate-smart embedded construction

²³ Located in the central Indian Ocean, around 70% of the country’s land area is less than one meter above sea level, 97% are reporting shoreline erosion and over 90% of the islands have been reported to flood annually. Approximately 50% of all housing structures are within 100 meters of the shoreline, few of which are capable of withstanding tidal floods, let alone tsunamis (Nachmany, et al., 2015). With a fragile ecological profile, low elevation, sea levels that are expected to rise, and extreme weather events that are likely to increase in frequency and intensity, the Maldives is considered one of the world’s most vulnerable countries. High frequency events such as monsoonal flooding, coastal erosion, salt-water intrusion, sea level rise, as well as less frequent events such as earthquakes, thunderstorms, flash floods and prolonged dry periods pose a real threat to lives and the economy of Maldives.

materials can also be explored for the market. However, these materials may not necessarily bring down the total costs.

Promote infill development and risk informed planning.

Malé, Hulhumale, and other urbanizing atolls such as Fuvahmulah, Addu City and Kulhudufushi have either started or are in the process of developing and/or ratifying their first master plans. However, none of these have incorporated a review of disaster or climate risks. The spatial strategy to reclaim land for housing and commercial purposes, partly driven by the land allocation policy and the country's geographic land constraints is both expensive and detrimental to the natural ecosystem. In some urbanizing areas, reclamation is being pursued while there are vacant allocated lots available in urban centers. To address this, densification strategies through infill development of vacant plots in existing urban centers, thereby limiting the need for costly and harmful reclamation efforts can be explored. Where reclamation efforts are necessary, long-term climate change risks should be considered in the planning.

Develop a long-term savings program, especially for low-income households.

While there are macroeconomic barriers limiting Maldivian households' ability to build wealth, the GoM can support local banks' financial literacy and savings programs for homeownership and incremental building. A financial literacy program can increase Maldivian households' financial knowledge and skills, while a savings programs designed specifically for homeownership can encourage households to save for a down-payment to obtain access to affordable housing. Additional programs can focus on saving for home improvements or additions, as well as for climate change adaptation.

Box 3: Public-private partnerships can deliver affordable housing, but they are not a silver bullet

PPPs can help governments provide affordable housing without overly burdening public finances. In the housing sector, a PPP is defined as “a partnership between the public and private sectors, established through a contractual relationship which seeks to access private sector finance, design, construction, commercialization, maintenance or operational management for the delivery of affordable housing, and, in some cases, ancillary services”. The public sector contribution can occur in the form of cash or equivalents such as land, development rights, revenues generated from land, infrastructure and building assets, taxation relief and/or a share in the equity generated over a fixed period. The private party's remuneration is typically linked to performance.

Where effectively used in the affordable housing sector, PPPs can help the government transition from “government as builder” to “government as enabler and regulator”. PPPs can transfer risk to the most competent party, control project costs throughout the project life cycle, and harness the private sector's experience and efficiency in delivering infrastructure projects. However, PPPs in emerging economies often fail because the institutions and supporting legal and financial systems are insufficiently mature to facilitate implementation or to reduce the costs and risks for the private sector to deem them viable/profitable. Moreover, some PPPs have ended up continuing to rely heavily upon government land, subsidies or guarantees, making it questionable whether the private sector has taken its fair share of risks and whether the deal has maximized value for money.

Housing PPPs are therefore not silver bullets. Governments must first identify the key constraints in the enabling environment (policy, legal/regulatory and administrative) along the housing value chain. By removing/reducing these constraints, the market as a whole will benefit from more private sector entry/competition. Establishing the necessary institutional mechanisms to manage and monitor the implementation of PPPs, for example through the recently established PPP unit in the Ministry of Finance, is therefore a prerequisite to embarking on such projects. In the short term, the government can ensure that the procurement process for public housing projects allows for better transparency and screening of contract awardees and involves the community in project design.

Source: World Bank et. al. 2014.

Tailor land and housing interventions according to location.

The multiplicity of situations that exist across the atolls requires diverse strategies for land use, management, and housing development. In the Greater Malé region, large-scale housing PPPs can be considered, provided that the requisite institutions and framework to implement and monitor PPPs are set up by the central government. In parallel, the central government could also partner with atoll councils to support housing projects by developers and small owner-occupants who wish to redevelop their plot of land. In urbanizing islands, the government can consider developing small housing PPPs, partnerships with SOEs, and provision of block grants and technical assistance to support community projects. In smaller islands, the government could accelerate the implementation of *Gedboruweriya* and provide technical assistance for self-built and housing retrofits. The GoM will need to weigh costs and benefits of each potential strategy, as there is no one-size-fits-all program for affordable housing provision.

Annex 1: Balance of Payments (percent of GDP)

	2019	2020	2021	H12022
Current account balance	-26.6	-35.5	-9.0	...
Balance on Good and Services	-6.2	-17.7	8.8	...
Merchandise Trade Balance	-42.6	-38.8	-41.2	-50.0
Merchandise Exports	6.4	6.9	5.6	6.8
<i>o/w fish exports</i>	2.7	4.2	2.7	2.8
<i>o/w jet fuel re-exports</i>	2.4	1.3	1.9	3.1
Merchandise Imports	49.1	45.7	46.8	56.9
<i>o/w fuel</i>	8.3	7.1	8.7	14.1
<i>o/w capital and construction goods</i>	13.6	12.6	10.9	12.7
Services Trade Balance	36.4	21.1	50.0	...
Service Exports	60.3	40.9	71.8	...
<i>o/w travel services (tourism)</i>	56.4	37.4	66.7	...
Service Imports	23.8	19.8	21.7	...
Primary Income, net	-10.0	-8.2	-9.5	...
Secondary Income, net	-10.4	-9.6	-8.3	...
<i>o/w worker remittance outflows</i>	10.6	10.6	9.7	...
Capital account balance	0.0	0.0	0.0	...
Net borrowing (balance from current and capital a/c)	-26.6	-35.5	-9.0	...
Financial account balance	35.2	37.6	5.6	...
<i>Direct investment, net</i>	17.1	11.8	8.7	...
<i>Portfolio investment, net</i>	13.8	1.8	6.0	...
<i>o/w general government debt issuance</i>	14.4	-0.6	5.9	...
<i>Other investment, net</i>	4.3	23.9	-9.1	...
<i>o/w government borrowings</i>	8.7	23.2	-1.6	...
Net errors and omissions	-7.9	4.2	-0.1	...
Overall balance	0.8	6.2	-3.5	...
Official reserves and related items (- increase)	-0.8	-6.2	3.5	...

Note: H12022 figures are estimates using the projection of GDP in 2022. Only certain indicators are currently available, as shown.

Annex 2: Key fiscal indicators (percent of GDP)

	2019	2020	2021	H12022	B2022
Total Revenue and Grants	26.9	26.5	26.6	28.6	28.1
Total Revenue	25.6	24.8	25.3	28.2	24.8
Tax Revenue	19.1	19	18.2	20.7	17.5
<i>o/w Import Duties</i>	4.0	3.9	3.5	2.8	3.7
<i>o/w Business and Property Tax</i>	4.1	6.3	3.4	3.8	3.1
<i>o/w Tourism Goods and Services Tax</i>	5.7	3.9	6.5	8.5	5.5
<i>o/w General Goods and Services Tax</i>	3.3	3.6	3.1	3.4	3.3
<i>o/w Airport Service Charges</i>	0.8	0.5	0.6	0.9	0.9
<i>o/w Green tax</i>	1.0	0.6	1.0	1.2	0.9
Non-tax Revenues	6.5	5.8	7.1	7.5	7.3
<i>o/w Airport Development Fees</i>	0.9	0.5	0.5	0.9	0.9
<i>o/w Property Income</i>	2.2	1.4	2.8	2.9	2.7
Grants	1.3	1.7	1.3	0.4	3.3
Total expenditure	31.9	49.7	40.9	42.4	42.1
Recurrent expenditure	23.1	33.4	28.1	33.1	28.2
<i>o/w Personal Emoluments</i>	9.6	14.3	10.8	10.1	11.2
<i>o/w Pensions, Retirement Benefits & Gratuities</i>	1.8	2.7	2.1	1.9	1.9
<i>o/w Goods and Services</i>	5.5	7.3	6.9	8.5	6.3
<i>o/w Grants, Contributions and Subsidies</i>	4.4	6.3	5.4	8.8	5.5
<i>o/w Interest Payments</i>	1.8	2.8	2.6	3.8	3.3
Capital Expenditure	8.8	16.3	12.3	9.3	13.9
<i>o/w Public Sector Investment Program</i>	4.9	8.3	6.7	6.3	7.2
<i>o/w Development project Investment & Loan Outlays</i>	3.9	6.3	4.2	2.9	1.1
Primary fiscal balance	-3.2	-20.4	-11.7	-10.0	-10.7
Overall fiscal balance	-5.0	-23.2	-14.3	-13.8	-14.0

Note: H12022 figures are estimates using the projection of GDP in 2022 and B2022 figures are the approved budget for 2022.

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