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Shifting financial landscapes: options for Maldives to leverage innovative financing approaches to achieve the 2030 Agenda


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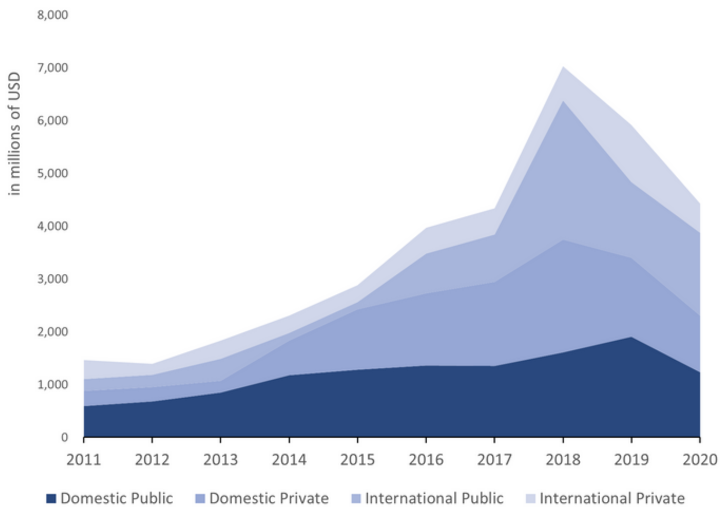
Understanding the dynamics of a fast-changing financing landscape for the Maldives is certainly becoming a key capability for policy makers. Concurrent trends across public, private, domestic, and international financing are deeply connected to both local and international contexts and a constant analysis of such variables will help anticipate fiscal space challenges as well as take full advantage of opportunities that the Maldives is facing in addressing its quest to sustainable development. Being able to build integrated financing strategies for national development in an upper-middle income setting such as the Maldives is a trait to be mastered.

Figure 1: Overall development financing landscape of Maldives 2011-2020



Source: calculations by UNDP using publicly available financing data[1] on the Maldives

Prior to the COVID-19 pandemic in 2020, the total development financing inflows into the Maldives grew at an average rate of 21% per annum from 2011-2018, rising from $1.5 billion in 2011 to $7 billion in 2018. The share of domestic sources of financing (budget and private financing) has been decreasing consistently, while the share of foreign financing increased during the same period, as the development financing requirements exceeded domestic capacities to generate revenues. Most notably, the share of Maldives budgetary finance in the overall financing mix has reduced from 40% in 2011 to 32% in 2019, while the remaining financing flows came from domestic private sources and international sources.

The COVID-19 pandemic in 2020 caused a staggering 25% decline in overall financing inflows into the Maldives, reflecting a loss of nearly $2.6 billion compared to the peak level of financing in 2018. Total foreign direct investments into the country declined by 50% from $1 billion in 2019 to $0.51 billion in 2020, while the loss of tax revenue at the height of the pandemic also meant that budgetary financing declined by 36% from $1.9 billion in 2019 to $1.2 billion in 2020.

[1] Domestic public: Budget figures published by the Ministry of Finance, Domestic Private: Estimated as a residual item, deducting Gross Fixed Capital Formation (GFCF) and Foreign Direct Investment (FDI) data, International Public: International Borrowings and ODA grants, International Private: FDI data.

Taken together, this has left a large financing deficit which continues to be unfilled. At the height of the pandemic, the Government of Maldives increased its external borrowings, largely financed through the issuance of conventional bonds and loans leading to a 10% increase in international public financing inflows ($142 million dollars), but largely failed to fill the funding gap. The Maldives income status as an Upper-Middle Income (UMI) also meant that the country had challenges to mobilise donors as recent budgetary records suggest that the country attracted only $78 million in donor grants in 2021 (3.2% of budget), and is uncertain to expand its donor grants at scale given its status as a UMI as well as overarching priorities derived from a new combo of international crisis. The government also continues to face challenges in undertaking an expansionary fiscal policy to boost its public sector investment programs as the budget remains mostly dominated by recurrent expenditures such as government emoluments and a range of social sector expenditure which are forecasted to take up 44% of the national budget in 2022.

To finance the post-covid development agenda, the country would need to adopt a different financing approach which places sustainability at its heart. Several countries in the Asia Pacific such as Indonesia, Fiji and Seychelles are aligning financing policies to the United Nation's Sustainable Development Goals (SDGs) and pursuing innovative financing strategies to supplement scarce budgetary resources and to diversify funding base to reach new investors. The Maldives stands to significantly benefit from aligning its financing ecosystem with global sustainability frameworks to attract a new breed of international investors eager to explore sustainable investment opportunities in emerging markets.

In particular, three financing approaches can lead to meaningful systemic change and additional resource mobilisation to achieve the 2030 Agenda in the Maldives.

1. Introducing blended financing options

The idea behind blended financing is to attract private capital by the strategic use of grant financing to de-risk investment projects.

Publicly available data suggests that government ministries and entities operate a system of trust funds which show significant ability to generate grant capital. One the of the most well-known of these trust funds is the Maldives Green Fund, which is capitalised by the "Green Tax" levied on tourism. Data[1] suggests that between 2015-2021, the fund collected an average revenue of $38 million per annum, collecting a total of $266 million during the period. Another important vehicle is the regional trust, Baa Atoll Conservation Fund which was established to provide financing for conservation activities in the UNESCO World Biosphere Reserve in Baa Atoll region. Financial reports published by the fund indicates that the fund has collected on average $120,000 per annum between 2014-2018, reaching a total collection of $601,000 for the same period.

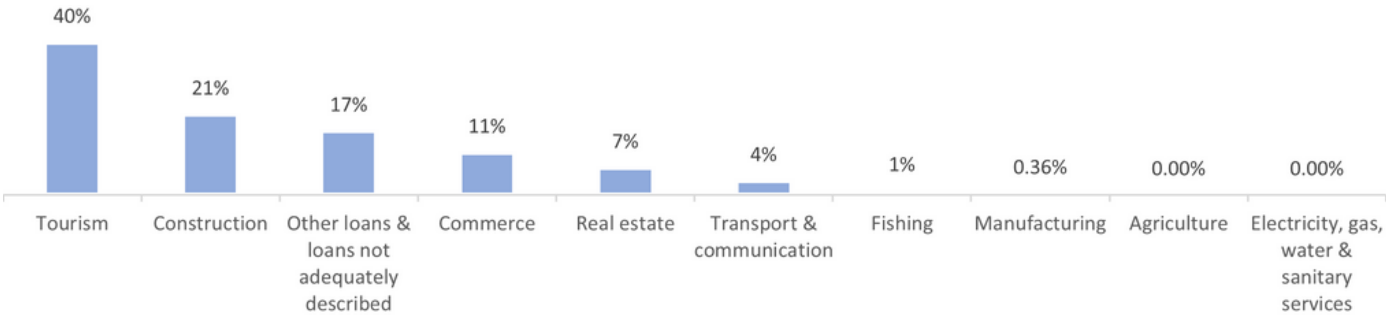
These trusts continue to operate largely as revolving trusts and represent the opportunity adopt a blended financing approach through strategic partnerships with private investors, where grants can strategically reduce risk to private investors in exchange for bridging finance to scale-up projects. In 2020, the UN launched its first strategic blended financing vehicle, called the Global Fund for Coral Reefs (GFCR), which is essentially using donor-based grants to de-risk pro-coral investments in several countries and help business entities achieve the maturity and revenue capacities to afford commercial capital.

To move away from the grant modality to blended financing solutions, a wider systemic review of the existing trust funds in Maldives could help the country scale-up its investments for environmental conservation through better use of grants to attract private capital.

[1] Ministry of Finance Green Fund Reports

2. Greening the capital and financial markets

Figure 2: Share of Maldives Banking credit by Industry 2021



Source: Maldives Monetary Authority, Monthly Statistics 2022

The Maldives has a vibrant banking sector and a developing capital market with sector assets representing 73% and 22% of national GDP, by the end of 2019. However, analysis of banking sector portfolios show that few investments are being made in critical sectors such as climate-resilient smart investments. Banking data published by the Maldives Monetary Authority (MMA) indicates that nearly 67% of bank lending is provided to traditional infrastructure development such as building resorts and commercial real estate development with only 1.36% directed towards green and blue economic activities (such as fisheries and agriculture) and WASH (water, sanitation, and hygiene) sectors.

Greening the financial and capital markets in the country would require Maldives to introduce sustainability loan frameworks at scale and industry-wide and establish a range of de-risking mechanisms such as credit guarantee schemes to attract investments into the under-served markets mentioned above. In the past, the Maldives operated two special schemes[3] to target housing shortages and to ease access to credit for SMEs, however both schemes were discontinued by 2021, leaving a window of opportunity to conceive credit guarantee schemes with better targeting and coverage to increase lending to underserved markets. Countries such as Fiji have already introduced dedicated financing products for sustainable energy generation[4] and more advanced peers such as the Netherlands are introducing green loan mortgage products[5] to encourage green infrastructure development.

Financial services reforms such as greening the financial and capital markets can help Maldives divert private credit to help the country achieve its nationally determined contributions (NDCs) targets.

3. Issuance of thematic securities to finance climate agenda

The Maldives has ambitious NDC plans which will require significant international financing to achieve these targets. The latest updated NDC targets (2020) pledges to reach a 26% reduction of emission by 2030 while also striving to achieve net-zero emissions if adequate financial resources are available. Further, the Government has also made pledges to increase the share of electricity production generated by renewable energy to at least 15% of the energy mix which includes both the public and private sectors. The NDC also outlines enhanced adaptation efforts which are "considered economy wide and targets all the sectors"[6].

[3] MMA's Affordable Housing Scheme (2017) and SME Credit Guarantee Scheme (2016)
[4] Sustainable Energy Financing Facility introduced by the Fijian Development Bank
[5] Energy Efficient Mortgages Action Plan, Netherlands
[6] Key NDC adaptation areas are identified as: agriculture and food security, infrastructure resilience, health, water security, coastal protection, safeguarding coral reefs, tourism, fisheries, early warning, disaster risk reduction.

Based on broad estimates of investment needs published by various international financial intuitions[7] on the Maldives, the country will require investments of more than $3.1 billion ($316 million per annum) between 2018-2030 for WASH and Environmental protection sectors to attain its NDC targets and to reach an ambitious target of achieving 70% renewable energy mix by 2030. The Maldives is unlikely to meet these targets without international capital as available local financing is not considered sufficient enough to achieve these targets. Historical figures available for the Maldives' government budget for the period 2013-2020, indicate a seven-year historical spending mark of roughly $130 million per annum for the areas stated above – suggesting an investment gap of approximately $186 million per annum for these sectors. The actual investment needs are estimated to be higher since the coverage of studies costing Maldives climate ambitions are mostly sectoral, leaving some sectors without proper costing.

An increasing number of countries are opting to issue thematic bonds (such as SDG-aligned, green, and blue bonds) to borrow from international markets. Recent examples of such issuances include Uzbekistan's SDG bond, issued under an SDG framework which raised $635 million in its first tranche at 3.9% interest rate, while Indonesia became the first country to issue a Green Sukuk raising $3 billion at an interest rate between 3.75 – 4.4% in 2018.

Prior to the issuances, UNDP worked closely with the Ministries of Finance and other line ministries in both the countries to provide technical support to develop the impact management strategies which are often required under thematic issuances to comply with investor impact reporting requirements.

The issuance of sustainability linked bonds for countries like the Maldives remain a viable option to finance the climate agenda given the tremendous nature capital that the country can leverage to attract investors and potentially reduce the cost of borrowing in the long term.

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[7] IFC: Climate Investment Opportunities in South Asia 2017, Maldives Climate-Smart Investment Potential P-90, and World Bank Maldives Development Update: In stormy Seas, June 2020

"With the quarterly Economic Bulletin, UNDP in Maldives intends to revamp its support to SDG Integration to ensure faster progress on sustainable development and offer narrative options in areas such as integrated policy and programming solutions; SDG metrics; and data and analysis using tools for modelling and forecasting.

We aim at promoting the sharing of knowledge as well as innovation, and solicit a more robust pace towards SDG Financing so to expand public and private contributions to reach the 2030 Agenda."

– Enrico Gaveglia, UNDP Resident Representative in the Maldives.

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