

RISK ASSESSMENT AND RISK MANAGEMENT PLAN

Risk Description	Risk Assessment	Mitigation Measures or Risk Management Plan
Government ownership. Political and bureaucratic ownership of the reform process and commitment to fiscal discipline weakens.	Medium	The reform process has built on strong government commitment since 2012, as indicated by recent reform achievements. A continued government commitment to fiscal consolidation and structural reforms until elections in 2015 is outlined in the development policy letter and the P3F, which provides a mitigation strategy against weakened reform implementation. ADB will continue policy dialogue with the government and development partners through the EWG and with executing and implementing agencies at the administrative level.
Broad support for reforms. Parliamentary and community support for reform implementation is insufficient.	Medium	A strong consensus has emerged among government and development partners since the start of the reform efforts in 2012 on the severity of Kiribati's ongoing economic difficulties, the necessity of adopting serious reform measures to deal with imbalances, and the imperative that the cabinet and parliament take the lead in this reform process. Community buy-in for public sector reforms has noticeably increased since 2012 due to visible success of the SOE reform program. ^a Regular and systematic policy dialogue between the government, development partners, and key stakeholders—including dialogue through the EWG—will ensure broad support.
External shocks. External shocks (e.g., natural disasters, high oil and food prices) damage the economy and the fiscal position.	High	The program supports government efforts toward fiscal consolidation and stabilization of the RERF as buffers against external shocks and the country's increasing vulnerability to climate change. ADB and other development partners also support private sector development to expand the economic base and generate employment to increase resilience. However, large external shocks can disrupt reform initiatives and outcomes. ADB will continue to monitor national, regional, and global economic developments and environmental risks and respond in a timely manner to possible government requests for assistance if unforeseen events occur.
Growth. Weak private sector response to improved economic conditions and resulting slow growth undermine fiscal consolidation and lead to a need for ongoing budget support.	Medium	Because the constraints of remoteness, the wide dispersion of territory and population, the small market size, and lack of management expertise restrict the country's private sector growth potential, the government promotes priority sectors (fisheries, labor migration, niche tourism) while addressing business confidence through continued economic and fiscal reform. Specific efforts to improve the business climate include (i) telecommunications sector liberalization, (ii) financial and energy and transport sector development, and (iii) skills development. ADB-supported structural reform also contributes to market development by opening up selected SOE dominated markets to competition. ^b Private sector uptake in these areas has been prompt and sizeable, indicative of the private sector's willingness to do business. ^a
Spending restraint. Relaxing or reversing of public	Medium	The government's medium-term fiscal framework for 2014–2016 shows continued restraint in recurrent expenditure allocations, based on conservative fishing license revenue projections. Past expenditure performance demonstrates strong government

spending restraint undercuts fiscal consolidation efforts.		commitment to fiscal consolidation. The upgraded PFM system, completed in April 2014, introduced a commitment control system that helps the MFED control budget execution across the government.
Quality of expenditure. Weak planning—budgeting links and excessive non-priority spending undermine medium-term growth prospects.	Medium	Policy actions aim at improving expenditure quality by increasing the efficiency of the copra subsidy and reducing the fiscal drain from inefficient SOEs. Past policy actions have included the reduction of spending on temporary workers in non-priority ministries, and the P3F and the development policy letter highlight long-term government commitment to increasing priority sector allocations for social spending and infrastructure. Ongoing multipartner policy dialogue and TA, as well as PFM reform, will safeguard the government's leadership in and implementation of efforts to improve the quality of spending.
Use of budget support. Funding of recurrent annual costs through budget support and failure to prioritize capital works based on economic returns exacerbate future budget deficits.	Medium	The program provides funding for a share of the fiscal deficit in 2014. Part of this deficit derives from the clearance of high-interest SOE debt taken on by the government as part of the SOE reform process supported by ADB and the IMF. ^{ab} This frees up future resources that can be allocated to priority infrastructure and social spending. The program also requires that the government implement debt policy that prescribes the avoidance of nonconcessional debt and sets out due process and conditions for all new borrowing and issuance of guarantees. Public capital spending is limited. Projects funded by development partners in the 2014 budget are aligned with the KDP for 2012–2015 and show positive economic returns. Nonetheless, the country's natural limitations imposed by its small market size and geography will continue to pose a risk to financial and economic sustainability.
Revenue. Tax and non-tax revenues are insufficient to achieve a basic level of fiscal sustainability.	High	Revenue potential from marine resources, particularly tuna fishing, is significant, if collectively managed by Pacific economies. The government has initiated reforms in fishing license revenue management, complemented by progress on tax reform through the introduction of a VAT. The program includes policy actions in both areas to ensure continued implementation of reform efforts. TA from PFTAC, the Government of Australia, and the World Bank is available to continue revenue reforms.
SOE reform. Progress and commitment to performance improvements are halted or reversed.	Medium	SOE reform has shown remarkable progress since 2012 through the implementation of an SOE act and closure of selected underperforming SOEs. ^a TA from ADB, complemented by continued policy dialogue, has been and is available to implement policy actions and continue SOE reform efforts beyond program completion. ^b
Crowding out of private sector. Support for SOEs entrenches their positions and crowds out private sector investment and competition.	Low	SOEs are providing key goods and services, and improving their efficiency can contribute greatly to the economy and the government's fiscal position. The associated risk of crowding out the private sector is managed by pursuing a coordinated approach to SOE reform and private sector development that focuses on opening up potentially competitive sectors and on SOE commercialization in areas that are not commercially viable due to natural economic limitations.
Institutional capacity. The government	High	The government and its development partners developed the policy reform actions jointly. They are tailored to available government capacities. Reform areas are highly prioritized and

cannot implement policy reform actions because it lacks the capacity.		linked to available TA support, ^b which covers capacity development for government staff and capacity supplementation in highly specialized functions. The government shows strong commitment to assigning required staff to core functions (e.g. debt policy implementation in line with policy actions). Ongoing government–development partner policy dialogue—and, as part of that, the P3F—will ensure continuation of reform implementation.
Public financial management. Weak government PFM systems and limited capacity undermine revenue mobilization and expenditure discipline.	Medium	Past policy reform actions of the KERP included a PFM system upgrade in April 2014, which introduced a commitment control systems allowing the MFED to control budget execution across the government. ADB TA and policy dialogue has been and is supporting the strengthening of PFM functions. ^{bc} Implementation of the Kiribati PFM plan for 2011–2014 has led to (i) a medium-term budget framework to underpin strategic allocation of resources, (ii) improved capacities for accounting and financial reporting, and (iii) increased external audit capabilities. Ongoing development partner support, including engagement of a PFM advisor funded by the European Union and ADB TA, is available to support strengthening of PFM systems and capacities.
Procurement. Weak procurement capacities and controls undermine budget execution.	Medium	Government procurement is undertaken according to the Procurement Act 2002, which applies to all central government bodies and SOEs and specifies the methods of procurement and tendering procedures. The Government of Australia has been addressing gaps in procurement systems and capacities by providing support that has included a review in 2012–2013 of the Procurement Act. Government commitment to fully implement review findings by mid-2015 is provided in the development policy letter and the P3F.
Anticorruption. Weak internal controls and oversight capacities lead to significant leakage of funds.	Medium	Weak overall government capacities also affect the standard of controls and oversight in place. The PFM plan prioritizes support efforts by the government and development partners to strengthen internal controls and external oversight. Multipartner support for the PFM reform process is available. This includes support through regional ADB TA. ^c The program's policy actions address several loopholes that have led to significant leakages in the past. These actions include increasing transparency in the management of fisheries agreements and related license fee payments, increasing scrutiny of the management of public assets and liabilities, reforming the copra subsidy, and strengthening SOE governance to counter potential nepotism and misuse of funds (supported by past and ongoing ADB TA ^b).
Overall	Medium	

ADB = Asian Development Bank, EWG = economic working group, IMF = International Monetary Fund, KDP = Kiribati Development Plan, KERP = Kiribati Economic Reform Plan, MFED = Ministry of Finance and Economic Development, P3F = post-program partnership framework, PFM = public financial management, PFTAC = Pacific Financial Technical Assistance Centre, RERF = Revenue Equalization Reserve Fund, SOE = state-owned enterprise, TA = technical assistance, VAT = value-added tax.

^a IMF. 2014. *Kiribati Article IV Consultation 2014: IMF Country Report No. 14/138*. Washington, DC.

^b ADB. 2008. *Economic Management and Public Sector Reform*. Manila; ADB. 2011. *Strengthened Public Financial Management*. Manila; and ADB. 2013. *Enhancing Economic Competitiveness through State-owned Enterprise Reform*. Manila.

^c ADB. 2008. *Strengthening PFM in Pacific Developing Member Countries*. Manila; ADB. 2011. *Technical Assistance for the Pacific Financial Technical Assistance Centre 2011-2014*. Manila; and ADB. 2013. *Implementing the Pacific Regional Audit Initiative (Phase 2)*. Manila.

Source: Asian Development Bank.