

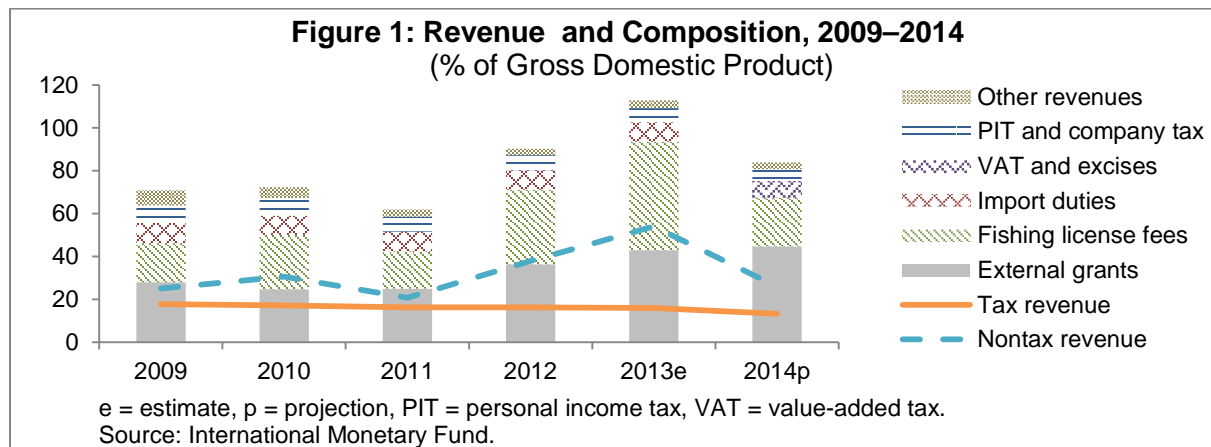
## SECTOR ASSESSMENT (SUMMARY): PUBLIC SECTOR MANAGEMENT<sup>1</sup>

### Sector Road Map

#### 1. Sector Performance, Problems, and Opportunities

1. **Background.** Kiribati's remote geographic location, the wide dispersion of its territory and population over 32 atolls and one island, a narrow economic base, and a small market naturally limit economic growth and contribute to macroeconomic volatility. Growth depends on high public spending, which crowds out opportunities for the weak private sector to develop. Without independent monetary and exchange rate policies, given the use of the Australian dollar, and limited leverage through banking regulation and interest rate policy, the government relies on fiscal policy to manage the impact of shocks and stimulate inclusive growth.

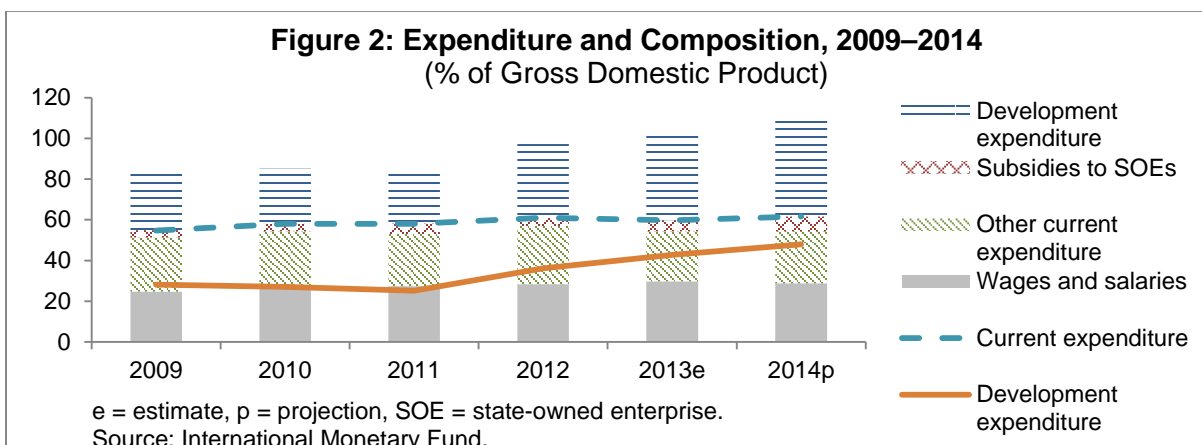
2. **Revenue performance.** Current revenues rose as a share of gross domestic product (GDP) from an average of 42.5% in 2009–2011 to an average of about 62.0% in 2012–2013. This was driven by a strong rise in fishing license revenue that has masked an overall decline in tax receipts. Tax receipts fell from 17.7% of GDP in 2009 to 15.9% in 2013 due to a narrow tax base, weak tax compliance, and the poor performance of state-owned enterprises (SOEs) leading to foregone tax payments (Figure 1). The government passed new tax legislation in 2013 to improve compliance and introduced a value-added tax in 2014 to replace phased-out import duties and broaden the revenue base. To strengthen resource management and maximize license revenues, the government approved a national fisheries policy in the same year.



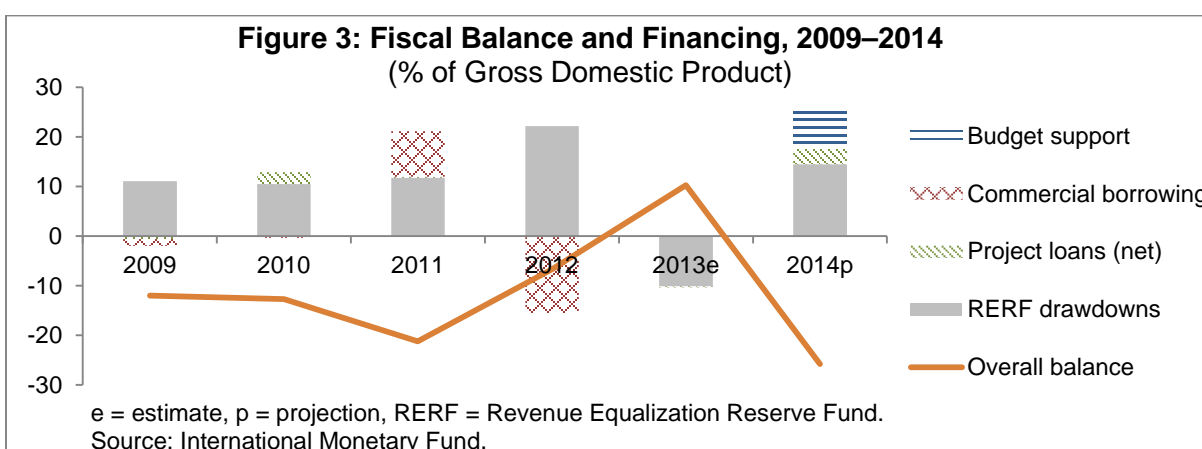
3. **Expenditure performance.** Due to its volatile revenue base, the government exercised recurrent expenditure restraint. Real recurrent spending was 13% lower in 2012 than in 2007. The public sector wage bill has remained constant in real terms since 2007, and the government reduced temporary workers to curb salary expenditures in 2013. Subsidies to SOEs remained high at 5.6% of GDP in 2013, up from 4.7% of GDP in 2007 (Figure 2). Capital spending,

<sup>1</sup> This summary is based on ADB. Kiribati: 2014 Country Performance Assessment. Unpublished; International Monetary Fund (IMF). 2014. *Kiribati Article IV Consultation 2014: IMF Country Report No. 14/138*. Washington, DC; Government of Kiribati. Kiribati Public Expenditure Analysis. Unpublished. For a detailed assessment of the public financial management (PFM) system, refer to Government of Kiribati. 2010. *Kiribati Public Financial Management—Performance Report*. Tarawa; ADB. 2010. *Country Partnership Strategy: Kiribati, 2010–2014*. Manila. Governance Assessment: Supplementary Appendix A; Government of Kiribati. 2011. PFM Plan, 2011–2014. Unpublished; ADB. Strengthening PFM: Interim Report for TA7995-KIR. Unpublished. A summary of relevant updates is provided in paras. 28–29 of the report and recommendation of the President.

financed entirely by external grants and loans, was more than 40% of GDP in 2013, driving total spending to more than 100% of GDP. Education and health constitute the two largest expenditure items with 18% and 13% of current spending in 2012, respectively.



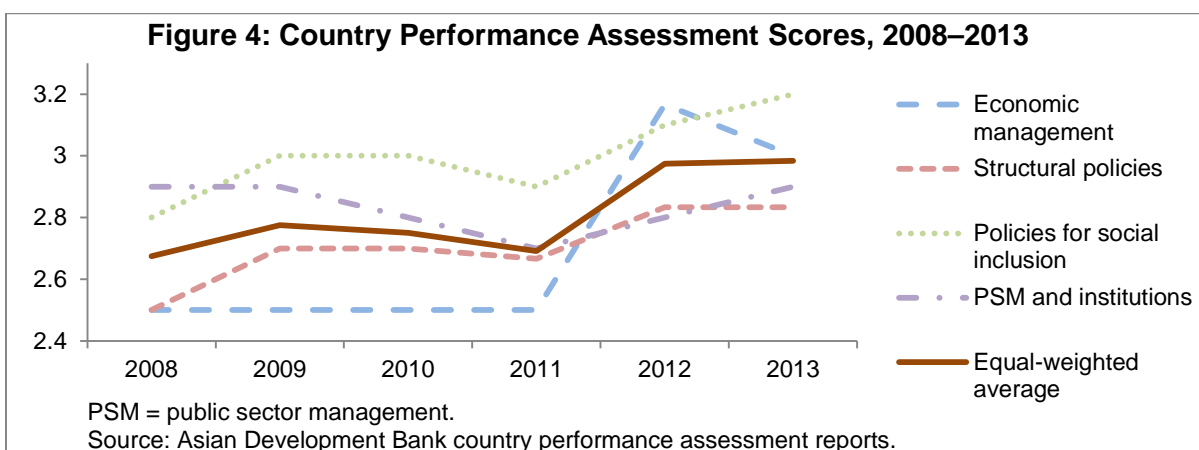
4. **Management of assets and liabilities.** The government is estimated to have posted an overall fiscal surplus of 10.3% of GDP in 2013 due to a combination of better fishing conditions and higher fishing license fees (Figure 3). The government drew heavily from the country's main fiscal buffer—the Revenue Equalization Reserve Fund (RERF)—to support fiscal deficits during 2009–2012. At 11%–22% of GDP, these drawdowns were unsustainable. Combined with losses on RERF investments resulting from the 2008–2009 global economic crises, the withdrawals reduced the RERF balance in constant per capita terms by almost half. This severely limits the government's ability to manage economic volatility in the long-run. In an effort to better manage the RERF, the government set up an RERF investment committee in 2013. A debt policy approved in 2013 has prevented new nonconcessional government borrowing since then and introduced a high level of scrutiny and oversight for other government borrowing and guarantees.



5. **Structural reforms and private sector development.** Large parts of the economy are dominated by SOEs, which crowd out entrepreneurial activity in potentially competitive sectors. The inefficiencies of the SOEs create a drain each year on the government's fiscal resources. This includes forfeited corporate tax payments due to non-profitability of SOEs and the need for subsidies. Since 2012, the government has undertaken significant reform efforts in the SOE sector with the support of Asian Development Bank (ADB) technical assistance (TA). This led to

the passing of an SOE act in 2013, the initiation of restructuring and privatization processes for some SOEs, and the development of an improved oversight framework that has brought about better corporate governance.<sup>2</sup> The government has made parallel efforts to support the development of the private sector. It approved a private sector development strategy in 2013 to provide a basis for sustainable growth and fiscal stabilization. Development partners have been helping move this process ahead by supporting the development of transport infrastructure; the financial, telecommunications, and energy sectors; and skills training.

6. **Country performance assessment scores.** The equal-weighted average score of the four institutional components of ADB's country performance assessment for Kiribati increased gradually during 2008–2013 from 2.7 to 3.0 on the scale of 0–6 (Figure 4).<sup>3</sup> Scores have risen more rapidly since 2011, coinciding with the mounting government efforts to carry out reforms. They are expected to have improved further in 2014 due to continued progress on reforms.



## 2. Government's Sector Strategy

7. **Public sector reform strategies.** The Kiribati Development Plan (KDP) for 2012–2015 provides the framework for achieving fiscal sustainability and growth in Kiribati and guides policy and strategy formulation.<sup>4</sup> Public sector management activities are covered in the economic growth and poverty reduction priority area. The macroeconomic strategies in the KDP that are relevant to the implementation of ADB's proposed Strengthening Fiscal Stability Program call for (i) implementing a new tax regime to expand and diversify the revenue base; (ii) accelerating private sector development; (iii) improving public financial management (PFM); (iv) improving the performance of SOEs; and (v) improving livelihoods through effective implementation of subsidies in the local copra and sea weed processing industries. The KDP also makes human resource development and better governance priority goals.

8. **Implementation of sector strategies.** Implementation of sector strategies is guided by the Kiribati Economic Reform Plan (KERP), a PFM plan for 2011–2014, and an SOE reform road

<sup>2</sup> ADB. 2008. *Technical Assistance to Kiribati for Economic Management and Public Sector Reform*. Manila; ADB. 2013. *Technical Assistance to Kiribati for Enhancing Economic Competitiveness through State-Owned Enterprise Reform*. Manila.

<sup>3</sup> The four institutional components cover economic management, structural policies, policies for social inclusion, and public sector management and institutions. The equal-weighted average provided here does not include country portfolio performance and does not follow ADB's composite country performance rating calculation formula.

<sup>4</sup> Government of Kiribati. 2012. *Kiribati Development Plan, 2012–2015*. Tarawa.

map.<sup>5</sup> The capacity of government agencies to implement reform measures is severely constrained by weak management and a lack of technical expertise. These agencies have only a small skills pool, limited financial resources, and infant performance management systems. Strategies therefore require implementation support through development partner TA and need to be carefully prioritized and sequenced. Past experience shows that the implementation of reforms may stall if internal capacity and external assistance are lacking, even with a strong commitment to reform from the government.

### 3. ADB Sector Experience and Assistance Program

9. **ADB support.** In support of the KDP for 2012–2015, ADB’s country partnership strategy for 2010–2014 addressed Kiribati’s macroeconomic imbalances by aiming support at strengthening economic and fiscal management and alleviating the binding constraints on private-sector-led economic growth through structural reforms.<sup>6</sup> Recently completed and ongoing ADB TA has supported the design and implementation of SOE reforms through restructuring in inefficient SOEs and strengthening corporate governance (footnote 2). Other TA supported the implementation of PFM reforms based on the PFM plan for 2011–2014 (footnote 5 and para. 8). This was achieved through the automation of the budget execution and reporting functions within the Attaché financial management information system. ADB will provide the policy-based grant for the Strengthening Fiscal Stability Program in a collaborative cofinancing effort with the Government of New Zealand and the World Bank in support of the Government of Kiribati to carry out critical reforms and as an incentive for maintaining reform momentum. This will reinforce TA work to improve public sector performance.

10. **Coordination of sector assistance.** In addition to its alignment with national plans and priorities, ADB support is coordinated with that of all major development partners (the governments of Australia and New Zealand, the Pacific Financial Technical Assistance Centre, and the World Bank). This is done through an economic working group made up of government and development partner representatives, as well as through such other fora as the annual IMF Article IV consultations and a biennial development partner forum. Coordination efforts build on experience from previous ADB and development partner assistance operations. Past lessons include the need to (i) build strong political reform consensus, (ii) limit reform to a few substantive areas, (iii) institutionalize a joint government–partner coordination mechanism, and (iv) adopt a medium-term perspective that recognizes the severity of Kiribati’s challenges. Developed by the economic working group, the KERP prioritizes fiscal and structural reforms, sets up the framework for budget support, and facilitates coordination of development partner TA.

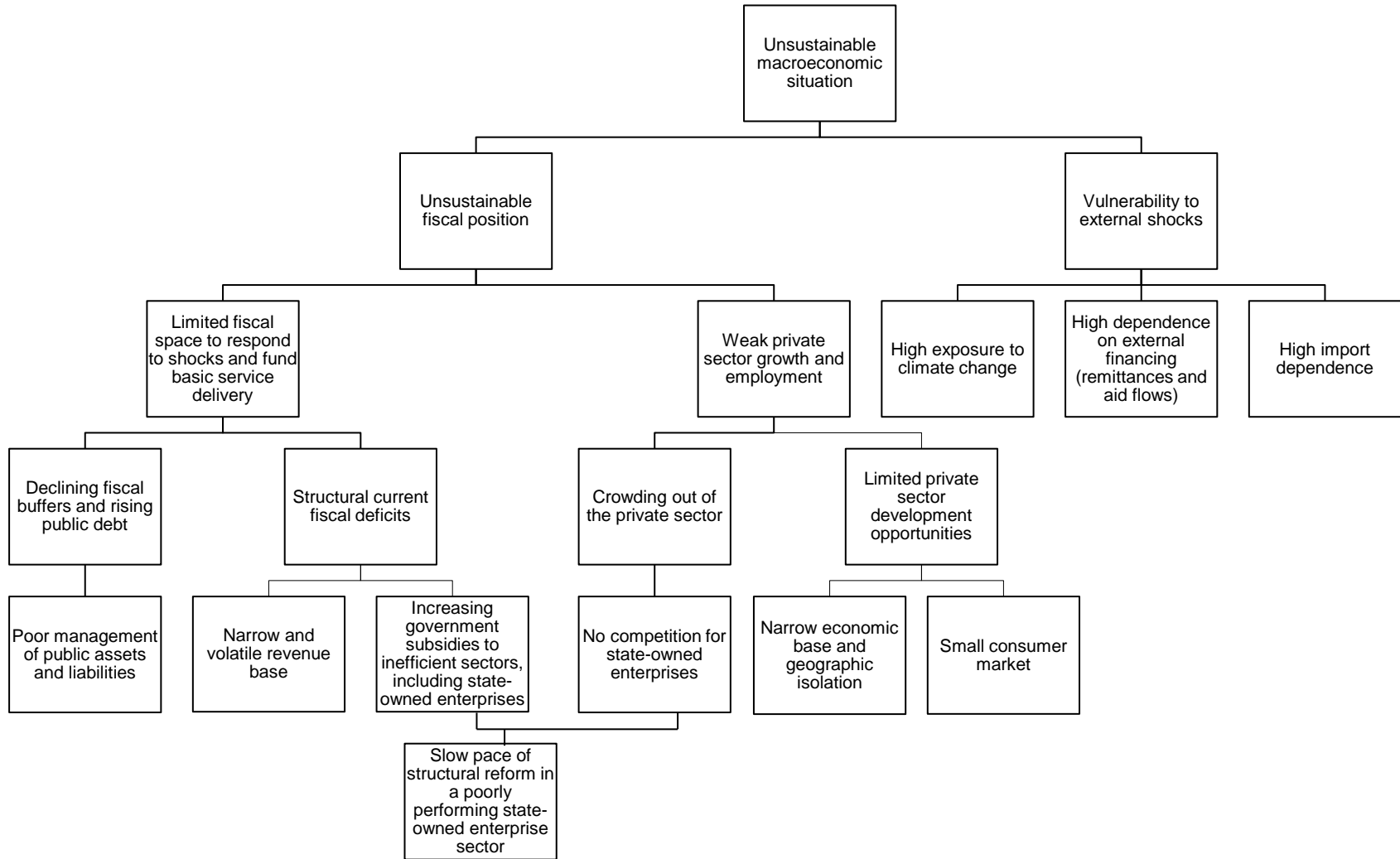
11. **Future ADB support.** ADB support for public sector management is expected to continue through policy-based lending and TA to implement reforms in the four areas identified in the KERP—quality of expenditure, revenue performance, management of assets and liabilities, and creating an enabling business environment. During 2014–2017, reform priorities are expected to shift gradually toward inclusive growth, including a focus on public social spending and the empowerment of women. Capacity development and performance management in the civil service will be targeted as cross-cutting issues throughout ADB assistance. Regional TA will support improvements in economic management, structural reforms, and PFM.<sup>7</sup>

<sup>5</sup> Government of Kiribati. Kiribati Economic Reform Plan, 2013–2014. Unpublished (accessible from the list of documents in Appendix 2); Government of Kiribati. PFM Plan, 2011–2014. Unpublished; Government of Kiribati. SOE Stocktake and Recommended Reforms. Unpublished.

<sup>6</sup> ADB. 2010. *Country Partnership Strategy: Kiribati, 2010–2014*. Manila.

<sup>7</sup> ADB. 2013. *Technical Assistance for Pacific Economic Management (Phase 2)*. Manila; ADB. 2013. *Technical Assistance for Pacific Private Sector Development Initiative (Phase 3)*. Manila.

# Problem Tree for Public Sector Management



## Sector Results Framework (Public Sector Management, 2014–2017)

Country Sector Outcomes <sup>a</sup>		Country Sector Outputs		ADB Sector Operations	
Outcomes with ADB Contribution	Indicators with Targets and Baselines	Outputs with ADB Contribution	Indicators with Incremental Targets	Planned and Ongoing ADB Interventions	Main Outputs Expected from ADB Interventions
Increased sustainable economic growth and improved standard of living for all of Kiribati's people by 2015	<p>Real GDP growth increases to 3% by 2015 (Baseline: 2.5% in 2011)</p> <p>Proportion of population living on less than \$1 per day (PPP) declines to 14.9% by 2015 (Baseline: 21.8% in 2011)</p> <p>Life expectancy increases for females to 69.0 years and for males to 65.0 years by 2015 (Baseline: 63.1 years for females and 58.9 years for males in 2011)</p> <p>Poverty gap ratio decreases to 6.0% by 2015 (Baseline: 7.2% in 2011)</p>	<p>Economic benefits from marine and fisheries resources maximized</p> <p>Revenue base broadened and existing revenue sources safeguarded</p> <p>Performance of SOEs improved</p>	<p>Transparent coordination mechanism for fisheries license management established by 2014 (Baseline: No coordination mechanism existing in 2013)</p> <p>VAT revenue increased to 9.9% of GDP by 2015 (Baseline: 0.0% of GDP in 2013)</p> <p>Key provisions of the SOE Act (statements of intent, subsidies to SOEs reflected in budget as CSOs, compliance with legislative provisions for board appointments) implemented by 2014 (Baseline: No SOEs complied with SOE act in 2013)</p>	<p><b>Planned target subsectors</b></p> <p>Economic management and management of public affairs (50%)</p> <p>Public expenditure and fiscal management (50%)</p> <p><b>Pipeline projects with estimated amounts</b></p> <p>SFSP in 2014 (\$3.0 million)</p> <p>Strengthened PFM II TA in 2015 (\$0.8 million)</p> <p>SFSP, Phase II in 2016 (\$2.5 million)</p> <p>Implementing SOE Reforms TA in 2017 (\$0.8 million)</p> <p><b>Ongoing projects with approved amounts</b></p> <p>Enhancing Economic Competitiveness through SOE Reform TA (\$0.8 million)</p> <p>Strengthened PFM TA (\$1.8 million)</p>	<p><b>Planned target subsectors</b></p> <p>Improved macroeconomic management</p> <p>Improved public expenditure and fiscal management</p> <p><b>Pipeline projects</b></p> <p>Strengthened PFM and improved targeting of public social spending</p> <p>Improved efficiency and effectiveness of SOEs</p> <p><b>Ongoing projects</b></p> <p>Selected SOEs restructured</p> <p>Transparency and accountability of government strengthened</p> <p>Strategic allocation of resources strengthened through use of the medium-term budget framework</p>

CSO = community service obligation, GDP = gross domestic product, ODA = official development assistance, PFM = public financial management, PPP = purchasing power parity, SFSP = Strengthening Fiscal Stability Program, SOE = state-owner enterprise, TA = technical assistance.

<sup>a</sup> Country sector outcomes, including indicators, targets, and baselines, are derived from key policy area 2 (economic growth and poverty reduction) of Government of Kiribati. *Kiribati Development Plan, 2012–2015*. Tarawa.

Sources: Asian Development Bank; Government of Kiribati. *Kiribati Development Plan, 2012–2015*. Tarawa.