

RISK ASSESSMENT AND RISK MANAGEMENT PLAN

Risk Description	Risk Assessment	Mitigation Measures or Risk Management Plan
<p>Government ownership. Political and bureaucratic ownership of the reform process and commitment to fiscal discipline weakens.</p>	Medium	The reform process has relied on strong government commitment since 2012, as indicated by recent reform achievements such as the building up of the CIF from \$3.2 million in 2012 to \$20.4 million at the end of 2014, and a \$2.2 million contribution to the Tuvalu Trust Fund in 2015. The ongoing government-led policy dialogue with joint development partners on reform priorities will continue.
<p>Broad support for reforms. Parliamentary and community support for reform implementation is insufficient.</p>	Medium	The Ministry of Finance and Economic Development conducts regular and systematic policy dialogue between the government and key stakeholders to sustain ownership of and support for reforms. The government hosts a development partner meeting annually. Regular joint missions undertaken by ADB and development partners on the PRM, and consultations held with government, private sector and civil society representatives help ensure consistent policy messaging and public understanding of the reform program.
<p>External shocks. External shocks (e.g., natural disasters, high oil and food prices) damage the economy and the government's fiscal position.</p>	High	ADB will support the government's efforts to achieve fiscal sustainability by supporting the maintenance of the fiscal buffer to improve fiscal resilience to economic shocks (the desired balance to be kept in the CIF account is equivalent to 16% of the Tuvalu Trust Fund's real maintained value, or around 45% of GDP). Maintaining this buffer will also improve fiscal resilience to natural disasters. ADB will work with development partners to support Tuvalu's cyclone Pam recovery plan, with ADB providing \$2 million in the form of budget support under this plan. ADB will also make available an additional \$3 million from the Disaster Response Facility for the outer islands ports project planned in 2016.
<p>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.</p>	Medium	Tuvalu's remoteness from markets and trading partners, 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 private sector accounts for just one-quarter of domestic production, and that share has not risen significantly. There are opportunities, however, to improve private sector development. The Tuvalu National Strategy for Sustainable Development, 2005–2015 aims to increase the private sector share of GDP to 50% by 2015. ¹ This objective is consistent with the PRM, which is supported by this program. Specific reforms supported by this program include the sale of the government-owned hotel to a private operator, and the contracting out of capital works projects currently undertaken by the Public Works Department to private sector operators. Development partner assistance provided to technical and vocational education and training could also help develop the skills of Tuvaluans (in carpentry, joinery, plumbing, etc.) to open up their own businesses or seek employment overseas.

¹ Government of Tuvalu. 2004. *National Strategy for Sustainable Development, 2005–2015*. Funafuti.

<p>Spending restraint. Relaxing or reversal of public spending restraint undercuts fiscal consolidation efforts.</p>	High	<p>The government's medium-term fiscal framework for 2015–2017 explicitly targets a sustainable budget framework. The introduction of fiscal ratios in 2012 (e.g., domestic revenue–GDP, recurrent expenditure–GDP, wages and salaries–domestic revenue), the production of quarterly fiscal reports, strengthened commitment control, and regular reconciliation of key revenues have helped strengthen the government's ability to accurately track fiscal performance and facilitate timely corrective action.</p>
<p>Quality of expenditure. Weak planning–budgeting links and excessive non-priority spending undermine medium-term growth prospects.</p>	Medium	<p>As part of the reform agenda, the government has reoriented expenditure to better support priority sectors (primary health and education) and encourage growth. Efforts in 2012–2014 to increase the efficiency of tertiary health care and education expenditure have helped enhance fiscal sustainability (without which fiscal constraints could force spending cuts, reducing public service provision). The government's development policy letter highlights long-term government commitment to increasing priority sector allocations for social spending and infrastructure. Ongoing multi-partner 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.</p>
<p>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.</p>	Medium	<p>The program provides funding based on the government's financing requirements, the cost of the government's reform program, and the cost of cyclone recovery efforts. Projections of budget financing requirements (inclusive of post-cyclone reconstruction) indicate a fiscal deficit of 50% of GDP in 2015, equivalent to around \$22 million. Budget support from ADB and PRM partners will (i) help reduce the amount the government will withdraw from the CIF to fund cyclone reconstruction efforts, and (ii) free up future resources that can be allocated to priority infrastructure and social spending. The government's Infrastructure Investment Plan and the Tropical Cyclone Recovery Plan guide all capital projects prioritized for Tuvalu.²</p>
<p>Revenue. Tax and nontax revenues are insufficient to achieve a basic level of fiscal sustainability.</p>	Medium	<p>Tuvalu is a member of the Parties to the Nauru Agreement, which has initiated a more strategic management of tuna resources with higher economic returns for member countries through the Vessel Day Scheme. Fishing license fees reached a record high of \$13 million in 2013, where it is expected to stabilize, because of improved negotiating power under the Vessel Day Scheme. The government aims to improve value-added tax compliance to 75% of eligible taxpayers, including all public enterprises, and has recommended a further rate increase from 7% since 2013 to 10% in 2016. The Inland Revenue Department has also taken steps to effectively capture the potential tax base and clear any roadblocks to compliance. A long-term tax adviser funded by the government of Australia is helping to improve the capacity of local tax officers and the overall tax administration system.</p>
<p>Public enterprise reform. Progress and commitment to performance improvements are halted or reversed.</p>	Medium	<p>Significant progress has been made in establishing the policy and legislative environment for improving the performance of Tuvalu's eight public enterprises, including the adoption of a Public Enterprises Act in 2009. The Public Enterprise Reform and Monitoring Unit, established in 2010, monitors, reports, and manages the performance of public enterprises and ensures compliance with the act</p>

² Government of Tuvalu. 2012 *Tuvalu Infrastructure Investment Plan*, Funafuti; Government of Tuvalu. 2014 *Tuvalu Tropical Cyclone Pam Recovery and Vulnerability Reduction Plan*. Funafuti.

Crowding out of private sector. Support for public enterprises entrenches their positions and crowds out private sector investment and competition.	Medium	Public enterprises provide 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 public enterprise reform and private sector development that focuses on (i) opening up potentially competitive sectors, and (ii) commercializing public enterprises in areas that are not commercially viable due to natural economic limitations. The Public Enterprise and Reform Plan supported by this program will help the government decide which public enterprises should be retained, sold, or absorbed within a ministry.
Institutional capacity. The government cannot implement policy reform actions because it lacks the capacity.	High	The government and its development partners jointly developed the policy reform actions, which are tailored to available government capacities. Reform areas are highly prioritized and linked to available TA support, which covers capacity development for government staff and capacity supplementation in highly specialized functions. ³ The government is committed to assigning required staff to core functions. Ongoing government–development partner policy dialogue will ensure continuation of reform implementation.
Public financial management. Weak government PFM systems and limited capacity undermine revenue mobilization and expenditure discipline.	Medium	Tuvalu's relatively strong annual budget formulation process and the accompanying medium-term fiscal framework provide a sound platform for the achievement of aggregate fiscal discipline and strategic allocation of resources. Ongoing development partner support is available from bilateral and multilateral partners to support strengthening of PFM systems and capacities.
Procurement. Weak procurement capacities and controls undermine budget execution.	Medium	From 2012 to 2014, ADB supported the adoption of the 2012 national procurement policy, the Public Procurement Act 2013, and the Public Procurement Regulations 2014, which collectively aimed at regulating and improving public procurement. The Central Procurement Unit, established within the Ministry of Finance and Economic Development, is now responsible for carrying out all government procurement and ensuring compliance with the Public Procurement Act 2013. Regular training and upgrading of skills of procurement officers is supported under the ongoing ADB TA.
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 need to strengthen internal controls and external oversight was identified by a public expenditure and financial accountability assessment undertaken in 2011. Support to the Office of the Auditor General through a long-term advisor is funded by the government of Australia. Regional ADB TA is also available. ⁴ The appointment of a government ombudsman in 2014 will help eliminate or greatly reduce corrupt practices in government.
Overall	Medium	

ADB = Asian Development Bank, CIF = Consolidated Investment Fund, GDP = gross domestic product, PFM = public financial management, PRM = policy reform matrix, TA = technical assistance.

³ ADB. 2012. *Technical Assistance to Tuvalu for Institutional Strengthening of the Ministry of Finance and Economic Development*. Manila.

⁴ ADB. 2013. *Implementing the Pacific Regional Audit Initiative (Phase 2)*. Manila.