ADB

Report and Recommendation of the President to the Board of Directors

Project Number: 50210-001
November 2016

Proposed Programmatic Approach and Policy-Based Grant for Subprogram 1 Independent State of Samoa: Fiscal Resilience Improvement Program

Asian Development Bank

CURRENCY EQUIVALENTS
(as of 28 October 2016)

Currency unit	–	tala (ST)
ST1.00	=	$0.3980
$1.00	=	ST2.5126

ABBREVIATIONS

ADB	–	Asian Development Bank
GDP	–	gross domestic product
JPAM	–	joint policy action matrix
MOF	–	Ministry of Finance
MTDS	–	medium-term debt management strategy
MTFF	–	medium-term fiscal framework
PFM	–	public financial management
PFMRP	–	Public Financial Management Reform Plan
PPP	–	public–private partnership
PSDI	–	Private Sector Development Initiative
SOE	–	state-owned enterprise
TA	–	technical assistance

NOTES

(i) The fiscal year (FY) of the Government of Samoa ends on 30 June. “FY” before a calendar year denotes the year in which the fiscal year ends, e.g., FY2016 ends on 30 June 2016.
(ii) In this report, "$" refers to US dollars, unless otherwise stated.

Vice-President	S. P. Groff (Operations 2)
Director General	X. Yao, Pacific Department (PARD)
Regional Director	R. Jauncey, Pacific Subregional (SPSO), PARD
Team leader	S. R. Singh, Senior Public Management Officer, SPSO, PARD
Team members	C. Currie, Senior Country Economist, SPSO, PARD
	K. Emzita, Principal Counsel, Office of the General Counsel
	T. Faletau, Safeguards Officer, SPSO, PARD
	M. Hazelman, Associate Project Analyst, SPSO, PARD
	M. Melei, Senior Country Coordination Officer, SPSO, PARD
	L. Tora, Country Economist, PARD
Peer reviewer	W. Turner, Senior Public Financial Management Specialist, Sustainable Development and Climate Change Department

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PROGRAM AT A GLANCE

1. Basic Data			**Project Number:** 50210-001
Project Name	Fiscal Resilience Improvement Program, Subprogram 1	**Department /Division**	PARD/SPSO
Country	Samoa	**Executing Agency**	Ministry of Finance
Borrower	Ministry of Finance		

2. Sector	Subsector(s)	ADB Financing ($ million)
✓ **Public sector management**	Public administration	1.00
	Public expenditure and fiscal management	2.00
	Reforms of state owned enterprises	2.00
	Total	**5.00**

3. Strategic Agenda	Subcomponents	Climate Change Information	
Inclusive economic growth (IEG)	Pillar 1: Economic opportunities, including jobs, created and expanded	Climate Change impact on the Project	Low

4. Drivers of Change	Components	Gender Equity and Mainstreaming	
Governance and capacity development (GCD)	Public financial governance	No gender elements (NGE)	✓
Partnerships (PAR)	Bilateral institutions (not client government) Official cofinancing		
Private sector development (PSD)	Conducive policy and institutional environment		

5. Poverty and SDG Targeting		Location Impact	
Geographic Targeting	No	Nation-wide	High
Household Targeting	No		
SDG Targeting	Yes		
SDG Goals	SDG9		

6. Risk Categorization: Low

7. Safeguard Categorization **Environment:** C **Involuntary Resettlement:** C **Indigenous Peoples:** C

8. Financing

Modality and Sources	Amount ($ million)
ADB	**5.00**
Sovereign Program grant: Asian Development Fund	5.00
Cofinancing	**0.00**
None	0.00
Counterpart	**0.00**
None	0.00
Total	**5.00**

9. Effective Development Cooperation

Use of country procurement systems	Yes
Use of country public financial management systems	Yes

I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on (i) a proposed programmatic approach for the Fiscal Resilience Improvement Program, and (ii) a proposed policy-based grant to the Independent State of Samoa for subprogram 1 of the Fiscal Resilience Improvement Program.[1]

2. The policy-based program is designed to improve Samoa's macroeconomic stability and to strengthen the country's fiscal resilience. It supports the government's medium-term fiscal framework (MTFF) through the implementation of the joint policy action matrix (JPAM) on public financial management (PFM) policies and processes, developed by the Government of Samoa and its development partners.[2]

II. THE PROGRAM

A. Rationale

3. **Development context.** As a small (population 180,000) island state with a very open economy, Samoa is highly vulnerable to exogenous shocks and faces particular challenges in achieving sustainable development. The global economic crisis in 2008, a tsunami in 2009, and Tropical Cyclone Evan in 2012 have had adverse, long-lasting impacts on growth, which averaged just 1.2% during FY2008–FY2015, well below the 4.3% average during FY1999–FY2007. Growth increased to 6.4% in FY2016 with strong performance in the fishing, tourism, transport, and construction sectors. New fishing operators have contributed to a more than doubling of output over FY2015 and FY2016. Growth in visitor arrivals has contributed to growth in the tourism and transport sectors. Upgrading of the airport and investments in hotels are contributing to increased construction activity. Growth remains highly volatile, however, and is expected to decline to 2.0% in FY2017 as a result of the imminent closure of Samoa's automotive wire harness plant (a significant manufacturing sector employer, with 740 staff).[3]

4. **Narrow and vulnerable economic base.** Samoa's vulnerability stems in large part from its limited resources. The economy is characterized by a large nonmonetary sector and a relatively high dependence on remittances and development assistance. Two-thirds of all Samoans depend on the agriculture sector for their livelihoods—mainly small-scale subsistence farming and fishing at the local level. The manufacturing sector (with the exception of the wire harness plant) largely processes agricultural produce, which makes up the bulk of Samoa's exports. Tourism accounts for approximately 25% of gross domestic product (GDP), with Samoa receiving approximately 135,000 visitors per year. Samoa's reliance on these two sectors increases its vulnerability to damage and loss from natural disasters, which have immediate impacts on the economy, and on the welfare of the majority of the population. Post-disaster needs assessments following the recent disasters estimated that the tsunami cost the economy $124 million in lost output, equivalent to 22% of GDP in 2009; Tropical Cyclone Evan cost $204 million in lost output, equivalent to 28% of GDP in 2012.

5. **Private sector development is constrained**. The small size of the economy precludes some economic activity, while lack of scale means private sector firms are relatively small, limiting the absorptive capacity for both aid and investment. The lack of access to finance, gaps

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[1] The design and monitoring framework is in Appendix 1.

[2] Development partners include the Asian Development Bank (ADB), the governments of Australia and New Zealand, the European Union, and the World Bank. The list of linked documents is in Appendix 2, the development policy letter is in Appendix 3, and the policy matrix for subprograms 1 and 2 is in Appendix 4.

[3] *Radio New Zealand.* 2016. Yazaki Samoa to shut down in 2017, hundreds to lose jobs. 12 October. www.radionz.co.nz/international/pacific-news/315443/yazaki-samoa-to-shut-down-in-2017,-hundreds-to-lose-jobs

in the commercial legal framework, inefficient state-owned enterprises (SOEs), barriers to agricultural development, and poorly defined property rights are some of the identified barriers to private sector development. An opaque and difficult foreign investment regime has resulted in net foreign direct investment averaging the equivalent of just 2.8% of GDP per year during FY2006–FY2016. As a result of the constrained private sector, the public sector is left with a significantly large share of the burden of delivering necessary services, which has to be funded through a relatively higher proportion of taxes and other sources of revenue. Economic diversification will lead to a more resilient economy in which the private sector is able to deliver a wider range of services, with a reduced role for the public sector. Private sector growth is widely acknowledged to be an essential component of poverty alleviation through the provision of an increased number and range of economic opportunities, thereby reducing the burden on public delivery of poverty-alleviation measures.

6. **Financial inflows require diversification.** Remittances and development assistance contribute about a quarter of annual GDP. Remittances largely support private consumption and are an integral part of the traditional social welfare system that supports Samoa's largely rural-based population. Following the global economic crisis, remittances declined from an average of 22.0% of GDP in FY2004–FY2009 to an average of 20.0% of GDP in FY2010–FY2016; the decline in remittances occurred despite the two subsequent natural disasters. The series of exogenous shocks caused growth to slow to an average of 1.2% in FY2008–FY2015. Domestic revenues declined sharply in FY2010–FY2012 to an average of 23.2% of GDP, and then rose beginning in FY2013, with domestic revenue collection reaching 26.8% of GDP in FY2016. The government responded with a substantial fiscal stimulus financed by grants and domestic and external debt accumulation (largely concessional), as well as monetary stimulus in the form of lower interest rates. The government is committed to economic diversification to develop a more resilient economic structure. Diversification is focused beyond the agriculture and tourism sectors, and includes recent investments in the transport and communication sectors. Development partners have worked closely with the government to provide support, with grants averaging 9.2% of GDP during FY2009–FY2015. Growth has been slow to accelerate, however, and fiscal deficits and debt levels remain high. Selected economic indicators are in Table 1.

Table 1: Selected Economic Indicators

Indicator	FY2013	FY2014	FY2015	FY2016	FY2017 Forecast	FY2018 Forecast
Real GDP growth (% change)	(1.9)	1.2	1.6	6.4	2.0	2.0
Inflation (annual average % change)	(0.2)	(1.2)	1.9	0.1	2.0	3.0
Revenue (% of GDP)	33.7	38.1	34.5	33.4	38.4	36.3
Of which: Grants	9.7	12.6	9.1	6.7	11.3	9.2
Tax revenues	22.1	23.1	22.7	24.2	22.8	22.8
Nontax revenues	1.9	2.4	2.6	2.6	4.2	4.2
Expenditure	37.5	43.3	38.3	33.8	41.9	39.3
Of which: Development	11.5	15.0	11.3	9.3	13.1	11.0
Recurrent	26.0	28.4	27.0	24.5	28.8	28.3
Goods and services	6.3	7.6	7.8	5.9	12.5	12.0
Subsidies	1.5	1.0	0.9	0.7	0.9	0.9
Overall fiscal balance	(3.8)	(5.3)	(3.9)	(0.4)	(3.5)	(3.0)
Public debt	53.6	54.4	57.8	52.6	54.1	54.5
Gross reserves (in months of GNFS)	4.0	4.3	4.1	3.6	4.0	4.6
Current account balance (% of GDP)	(2.5)	(7.0)	(3.9)	(3.9)	(5.3)	(4.8)

( ) = negative, FY = fiscal year; GDP = gross domestic product, GNFS = goods and nonfactor service imports.
Sources: Samoa Bureau of Statistics and Asian Development Bank estimates.

7. **Budgetary pressures**. Although fiscal expansion undertaken in recognition of the weak economic environment provided some impetus for growth, it resulted in high fiscal deficits and escalating public debt. The government sought to stimulate the economy through public investments in infrastructure, but this did not result in higher growth. Expenditures on the hosting of regional and international events also did not result in higher visitor spending or the intended economic stimulus. Two–thirds of the budget funded recurrent expenditures with one third allocated to development expenditures. Interest was a major driver of the 10% annual growth in recurrent expenditures during FY2008–FY2016; this compared with 3% growth in wage expenditures. Tax revenues have fluctuated since FY2008, falling to a low of 19.6% of GDP in FY2011 and FY2012, and gradually increasing to 24.2% of GDP in FY2016. Nontax revenues fell from 3.3% of GDP in FY2008 to 1.9% in FY2013; following inflation adjustments to government fees and charges, nontax revenues increased to 2.6% of GDP in FY2016.

8. **Deficits exceeded targets.** Since FY2009, budget deficits have exceeded the government's long-term target of 3.5% of GDP, and public debt rose from around 30% of GDP in FY2008 to about 53% in FY2016.[4] The increase in debt was a result of both the recovery and reconstruction needs (power sector expansion, agriculture sector support, post-tsunami reconstruction, and general budget support loans), and the construction of a national broadband network and public buildings funded by the China EXIM Bank (such as the convention center, a national medical center, office complexes, and a recent upgrade of the airport terminal building). The increase in debt requires the government to continuously strengthen its debt management. With the recovery phase following the 2012 cyclone coming to an end, grant assistance declined to an estimated 6.7% of GDP in FY2016 (from an average of 10.5% of GDP during FY2013–FY2015), which required the government to reduce total expenditures. The fiscal deficit in FY2016 was reduced to 0.4% of GDP, which was largely achieved through lower development and recurrent expenditures.

9. **Planned fiscal consolidation.** The government is committed to consolidating its fiscal position, but the speed of consolidation needs to be managed carefully to minimize possible impacts on poverty and hardship from low economic growth. Consequently, the government has requested development partner support to help mitigate the macroeconomic challenges and build greater fiscal resilience. The government has been successful in reducing subsidies to public corporations from 1.5% of GDP in FY2013 to 0.7% of GDP in FY2016. It is intended that private sector partnerships will further reduce the need for subsidies and facilitate private sector growth. Goods and services to be procured in FY2017 are budgeted at 12.5% of GDP. Improvements to procurement processes will help introduce efficiencies, improve value for money in public expenditures, and enhance public service delivery. Significant revenue reforms have taken place, notably through the passage of legislation in 2012. Samoa's Customs Modernization Project is also nearing completion. These changes have resulted in improved taxpayer compliance through increased awareness and enforcement. Government fees and charges are being adjusted for inflation, resulting in significantly improved nontax revenue collection. Revenue reforms are not included in the program to allow time for past reforms to be implemented. Development partner support also assists Samoa maintain an adequate level of foreign exchange reserves.

[4] Samoa is currently classified by the International Monetary Fund and the World Bank as a country at moderate risk of debt distress. This is an improvement on the FY2014 rating, which rated Samoa as being at high risk of debt distress. International Monetary Fund. 2015. Debt Sustainability Analysis. *Staff Report for the 2015 Article IV Consultation.* Washington DC. The improvement is largely a result of technical changes, which include the use of a longer-term reference interest rate, revised GDP estimates as a result of rebasing, and inclusion of remittances in the analysis.

10. **Political commitment to reforms**. The government has shown strong commitment to reforms that lead to efficient and effective delivery of public services. Phase 1 of the Public Financial Management Reform Plan (PFMRP) was launched in 2008, under which aid policy and debt management strategies were developed, outcome-based budgeting was adopted, sector plans were prepared, and the Ministry of Revenue was strengthened. Phase 2 of the PFMRP commenced in 2011, and strengthened internal audit functions, implemented a debt management reform plan, and developed a medium-term expenditure framework. Following the 2012 cyclone, the government and development partners worked together to develop an MTFF incorporating integrated policies to achieve economic stability. The MTFF specified a clear path to bringing the government's fiscal position to more sustainable levels over 3–5 years, while maintaining aggregate demand and improving productivity. The MTFF essentially lays the basis for sustained economic growth through (i) support for structural reforms to improve medium-term growth prospects, and (ii) support for mitigation strategies to strengthen climate resilience. Samoa is currently implementing phase 3 of its PFMRP. [5]

11. **Programmatic approach**. The program's proposed programmatic approach consists of two subprograms, and is part of the sequenced MTFF reform process supported by development partners (including the World Bank, the governments of Australia and New Zealand, and the European Union) to help the government reduce debt and achieve fiscal consolidation, while focusing on reforms needed to build resilience and improve stability. The program is consistent with the International Monetary Fund assessment that finds fiscal consolidation is consistent with macroeconomic fundamentals, and that continued reforms will help improve the business environment. It is designed to augment ongoing PFM reforms and will be delivered within the JPAM. The program policy matrix is a subset of the JPAM. The JPAM involves regular policy dialogue between the government, the Asian Development Bank (ADB), and other development partners. The two subprograms allow flexibility for the program to respond to ongoing and new risks to the economy and shifts in government priorities. The program is consistent with the Strategy for the Development of Samoa, 2012–2016. [6] The request for a policy-based operation in 2016 was received during JPAM discussions in 2016, and followed up during the country programming mission for the country operations business plan, 2017–2019.[7]

12. **Lessons from previous programs**. The program builds on the lessons of the Economic Recovery Support Program,[8] the Public Sector Financial Management Program (PSFMP),[9] and ADB support for reform around the region. Lessons from these operations have highlighted the following good practices, which have been incorporated in the program design: the need to ensure (i) political ownership and understanding of the program, (ii) that program-supported processes are mainstreamed in PFM practices, and (iii) that stakeholders understand that reforms in a country vulnerable to disasters can take time to become self-sustaining. In Samoa's context, political ownership and understanding have been particularly necessary for reform progress. The ongoing dialogue under the JPAM processes ensures continuing, coordinated

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[5] Phase 1 of the PFMRP (2008–2011) built on capacity-building initiatives prior to 2008; it was followed by phase 2 (2012–2014) and phase 3 (2015–2017).
www.mof.gov.ws/AboutUs/PublicFinanceManagementReforms/tabid/6008/Default.aspx

[6] Government of Samoa. 2012. *Strategy for the Development of Samoa, 2012–2016*. Apia.

[7] ADB. 2016. *Country Operations Business Plan: Samoa, 2017–2019*. Manila.

[8] ADB. 2010. *Report and Recommendation of the President to the Board of Directors: Proposed Program Cluster and Loan to the Independent State of Samoa for Subprogram 1 of the Economic Recovery Support Program*. Manila; and ADB. 2011. *Report and Recommendation of the President to the Board of Directors: Proposed Loan to the Independent State of Samoa for Subprogram 2 of the Economic Recovery Support Program*. Manila.

[9] ADB. 2013. *Report and Recommendation of the President to the Board of Directors: Proposed Policy-Based Grant Independent State of Samoa: Public Sector Financial Management Program*. Manila.

support for this initiative while ensuring flexibility where it is warranted. The policy actions attributed to the program are a subset of the JPAM.

B. Impact and Outcome

13. The impact will be maintained macroeconomic stability over the medium-term, which is a key objective of the Strategy for the Development of Samoa, 2012–2016. The outcome will be improved fiscal resilience.

C. Outputs

14. The program is structured around four reform areas, including (i) reduction of fiscal drain through SOE reforms, (ii) improvement of procurement systems, (iii) improvement of debt management, and (iv) promotion of resilience to climate change and variability. Subprogram 1 has 10 policy actions while 7 policy actions are proposed for Subprogram 2. ADB will support Samoa through regional technical assistance (TA) projects for SOE reform and public sector management during the program. The ADB Private Sector Development Initiative (PSDI) TA will support a range of private sector reforms under way in Samoa that include assistance for developing a public–private partnership (PPP) pipeline.[10] PSDI will continue support for improving the business regulatory environment. Support for climate change adaptation and mitigation activities will be guided by the ADB climate change implementation plan.[11] All the outputs are fully aligned with the JPAM, and all policy actions under subprogram 1 have been complied with prior to the ADB Board of Directors' consideration of subprogram 1.

15. **Output 1: Fiscal drain reduced through state-owned enterprise reform.** SOE reforms have been introduced to improve performance and reduce their dependence on public finances. Subsidies to public corporations in FY2016 are estimated at 0.7% of GDP. Following the privatization of SamoaTel and the establishment of a joint venture with Virgin Airlines, Samoa has steadily reduced the number of civil servants and elected officials to comply with Schedule 3 of the regulations in the Public Bodies Act 2001. The reform program has made significant progress in improving the governance structures of the SOEs. In April 2014, a minister for public enterprises was appointed with sole responsibility for all SOEs, and a Ministry of Public Enterprises (MPE) was established in July 2015.

16. The government has approved a PPP framework for collaboration between SOEs and the private sector, and for delivery of selected services. The MPE now has an established PPP Division with technical support from ADB. ADB will continue its support for SOE reforms and facilitate business-enabling reforms through the regional PSDI TA. PPPs offer Samoa the potential to boost opportunities for private sector involvement and investment, while at the same time driving improvements in asset maintenance, operational efficiency, and service quality among SOEs. The government recognizes that, by facilitating appropriately structured concessions and inviting private sector participation, PPPs can help strengthen SOE performance and reduce the burden on public finances over the long term. PPPs are also a means for the government to attract more private sector investment and skills into SOE operations.

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[10] ADB. 2006. *Technical Assistance for the Private Sector Development Initiative*. Manila (TA 6353-REG); ADB. 2009. *Technical Assistance for the Pacific Private Sector Development Initiative Phase II*. Manila (TA 7430-REG); and ADB. 2013. *Technical Assistance for the Pacific Private Sector Development Initiative, Phase III*. Manila (TA 8378-REG).

[11] ADB. 2009. *Mainstreaming Climate Change in ADB Operations: Climate Change Implementation Plan for the Pacific (2009–2015)*. Manila.

17. To maintain the reform momentum, policy actions completed under subprogram 1 include (i) cabinet approval of at least one PPP, (ii) completion of the Agriculture Store Corporation's privatization, and (iii) cabinet approval of a privatization and divestment policy. The cabinet has endorsed the establishment and structure of the Samoa Submarine Cable Company, a PPP in the communication sector. ADB provided substantial cofinancing for Samoa's broadband cable project and helped set up the Samoa Submarine Cable Company, involving three private sector operators (Digicel, Bluesky, and Computer Services Limited) and three SOEs (Unit Trust of Samoa, the Samoa National Provident Fund, and Samoa Life Assurance Corporation) in a joint venture. The government approved the sale of the Agricultural Store Corporation in December 2015; and the sale and purchase agreement was signed in April 2016, and subsequently executed. In 2015 the government approved the Privatization and/or Divestment Policy following a policy review with ADB support. The review found the government policy on SOEs to be broadly appropriate, but noted that there should be no differentiation between strategic and nonstrategic assets when considering divestment, nor should commercially operating trading bodies be owned by the government.

18. Subprogram 2 will support the establishment of a solid waste management PPP, which aims to (i) improve service provision, through improvements to infrastructure and compliance with international best practice relating to transportation, treatment, and disposal; (ii) ensure solid waste management services are provided to all waste generators in Samoa, including commercial and industrial premises; (iii) facilitate new private sector investment into the sector; and (iv) introduce the "polluter pays" principle to achieve full cost recovery and ensure no reliance on public sector funding in the long term. Subprogram 2 also intends to support completion of external audits of SOEs in FY2016.

19. **Output 2: Improved procurement systems.** Strengthening of procurement systems is important in improving value-for-money in public expenditure and enhancing public service delivery. Samoa has made substantial progress in reforming public procurement systems during 2008–2015, and has built the capacity of the Ministry of Finance (MOF) procurement division. The division has spearheaded reform of the legal and regulatory framework for procurement; the government-approved procurement framework is the basis for instructions, guidelines, and standard tender templates for minor works, minor goods and related services, and minor general services. Subprogram 1 has supported the issuance of standard tender templates for major works.

20. Framework agreements enhance value-for-money in procurement by pooling of similar small contracts over time within and across multiple government agencies. Framework agreements will enable faster procurement (e.g., of medical or building supplies) in emergency situations. Pooled procurement increases efficiency through economies of scale, and by decreasing the number of different tenders and subsequent workload, leading to considerably lower expenses for suppliers and consumers. Further efficiency gains can be expected by prequalification of suppliers and products, introducing framework agreements with call-off orders, and by tendering required items separately, instead collating them into small lots as is now done. This will promote greater competitiveness among suppliers, resulting in lower prices.

21. Under subprogram 1, the government has included provisions in its Treasury Instructions (Part K) that provide a legal basis for the use of the framework agreement method. To assist the line ministries and SOEs with implementation, the financial secretary subsequently issued the Guidelines on Framework Arrangement. Subject to that document and the amended Treasury Instructions, the government's Tenders Board has revised its Guidelines for Government Procurement and Contracting: Goods, Works and General Services. This allows

the implementation of the framework arrangement method. To ensure the implementation of these reforms, subprogram 2 will support the pilot procurement of pharmaceutical items using framework arrangements. It is also intended that subprogram 2 will support the establishment of a complaints mechanism to further enhance the procurement system.

22. **Output 3: Improved debt management.** Strengthening debt policy and debt management remains a key priority, given rapid increases in debt stock during FY2009 and FY2015. The government has produced two medium-term debt management strategies (MTDSs) (in 2010 and 2013) and included debt statistics in its official statistical releases for government finances. In 2014, the government established formal procedures for contracting loans and issuing government guarantees, which were designed to ensure that all loan and guarantee proposals go through the same channels, are subject to the same level of scrutiny, and are assessed against the same criteria. This was intended to reduce the chances of loans or guarantees being agreed without adequate scrutiny and without complying with the MTDS. However, there were subsequent increases in non–concessional borrowing.

23. In November 2014, a bilateral loan agreement for CNY340 million (approximately $55 million, or about 6.6% of 2014 GDP) was signed to fund the upgrade of the airport terminal at Faleolo International Airport. The terms of the loan implied a grant element of about 25%, below the 35% threshold used for assessing concessionality. Moreover, implementation of the procedures for contracting loans occurred only after the loan was signed, and an economic analysis to assess whether the project would show a net economic benefit (as required to establish compliance with the MTDS) was prepared with a delay. To maintain focus and compliance with approved policies, a policy action for an updated MTDS following an assessment of the previous MTDS has been completed under subprogram 1. A project economic analysis training has been delivered by ADB in September 2016 to assist the government with its capacity building. An external debt management performance audit is intended as a policy action under subprogram 2.

24. **Output 4: Resilience to climate change and variability promoted.** Climate change and variability have the potential to have immediate and long-lasting implications on fiscal resources. Possible economic implications on output and productivity in climate-sensitive sectors such as agriculture and tourism require fiscal responses, particularly following climate-related disasters. Disasters also affect sensitive coastal areas and stress health and education systems and economic infrastructure. Disruptions to financial systems and trade also impact fiscal resources. Mainstreaming climate resilience in public investments has the potential to facilitate decisions that may reduce long-term fiscal risks and contingent public liabilities. ADB has, in the Public Sector Financial Management Program (footnote 9), supported the development of the Apia Town Spatial Plan that incorporates climate change mitigation measures. The spatial plan has since been approved by the government and new developments have been approved according to the plan.

25. The need to monitor and coordinate a large number of policies and projects associated with building resilience to climate change is now important. Subprogram 1 has supported (i) the establishment of a national monitoring and reporting framework for climate change; and (ii) the inclusion of climate risk and resilience indicators in the Strategy for the Development of Samoa, 2016–2020, which is due for finalization in the latter part of 2016. Subprogram 2 will support an integrated policy framework that allocates responsibilities for resilience across government agencies; informs decisions to increase resilience across key sectors that include agriculture, forestry, water, and coastal and urban areas; and will be gender-responsive. It will also support the development of a strategic investment plan that identifies key national infrastructure and

prioritizes risk-reduction interventions, thereby providing a basis for more coordinated climate resilience financing. The policy matrix for subprogram 1 is in Appendix 4.

D. Development Financing Needs

26. The government has requested a grant of $5.0 million from the Asian Development Fund resources for subprogram 1. The grant size (equivalent to 0.6% of FY2017 GDP estimate) is based on the estimates of budget financing requirements and the availability of resources for Samoa. Samoa is in need of external assistance to meet resource requirements for budget financing, given that economic recovery has been relatively weak following the negative economic impact of Tropical Cyclone Evan, and that fiscal consolidation needs to be paced so as to not adversely affect growth. The program will be an integral part of a joint undertaking with other development partners to provide policy–based support, monitored through the JPAM. The total value of grants from Samoa's development partners independent policy–based operations are equivalent to 1.8% of GDP in FY2017 and FY2018. Without these grants, the expected fiscal deficit in FY2017 would be equivalent to 5.3% of GDP, and likely a similar level in FY2018, thus contributing to an increase in public debt; if the government were to maintain its fiscal deficit target, expenditure levels would need to be reduced and public services could be compromised. The FY2017 projected deficit will be financed by concessional loans for the Agriculture Sector Support Program (World Bank), the Power Sector Expansion Project (ADB), the Petroleum Bulk Storage Facility (Organization of the Petroleum Exporting Countries), and the Faleolo International Airport Terminal (China EXIM Bank).

27. The proposed ADB and parallel collaborative partner financing (not administered by ADB) are indicated in Table 2. The grant will be released as a single tranche of $5.0 million upon grant effectiveness and in accordance with the ADB *Loan Disbursement Handbook* (2015, as amended time to time). The government will ensure that the local currency funds generated by the grant will be used to (i) meet its financing requirements, and (ii) provide the necessary impetus for sustained action on critical agreed reforms.

Table 2: Financing Plan

	Amount ($ million)		**Share of Total**
Source	**Subprogram 1**	**Subprogram 2**	(%)
Asian Development Bank			
Asian Development Fund (grant)	5.0	0.0	11.6
Asian Development Fund (loan)	0.0	5.0	11.6
World Bank	5.0	5.0	23.3
Australia	2.3	2.3	10.7
New Zealand	2.5	2.1	10.7
European Union	6.1	7.7	32.1
Total	**20.9**	**22.1**	**100.0**

Source: Asian Development Bank estimates.

E. Implementation Arrangements

28. The MOF will be the executing agency, and will oversee and coordinate the timely implementation of agreed policy actions. The MOF will also be responsible for program administration, disbursements, and maintenance of all program records. The MOF and the MPE will be the implementing agencies for the program. The MPE will implement SOE reform outputs, while the MOF will implement the remaining outputs under the program. The government, ADB, and other development partners will participate in at least one annual review of the program by June 2017. The design and monitoring framework (Appendix 1) indicates the program framework, including the indicative policy actions for subprogram 1. The policy matrix (Appendix

4) indicates the policy actions that have been completed for subprogram 1. The JPAM process facilitates broad consultations on reform priorities. Individual reform initiatives form part of the government's existing reform priorities and are being discussed with the private sector and civil society groups during program preparation and implementation. The program implementation period is January 2016 to March 2018. The implementation period for subprogram 1 is from January 2016 to March 2017, and for subprogram 2 from April 2017 to March 2018.

III. DUE DILIGENCE

29. The program's major benefit will be its contribution to Samoa's improved fiscal management and stability, which will in turn help maintain macroeconomic stability in the country and sustain growth. Strengthened public sector management and better-performing SOEs will also allow for improved service delivery, which is essential to make growth inclusive and to foster employment and poverty reduction.

A. Economic and Financial

30. The reforms supported under the program envisage macroeconomic stability and improved fiscal resilience, which will reduce the negative impacts of external shocks, including on growth and service delivery. SOE reforms are expected to positively impact private sector development and job creation, while reducing the drain on fiscal resources from ineffective and inefficient public enterprises. Improved public procurement systems and debt management will contribute to building fiscal resilience through reductions in the government's operating costs. Mainstreaming climate change in public investments will contribute to reduced post-disaster costs in the long term. Costs for policy reforms supported under the JPAM are not estimated, and their impacts are not quantified because of data and capacity constraints.

B. Governance

31. Promoting good governance is a priority for the government, which is implementing phase 3 of its PFM reform plan (footnote 5), following considerable progress under the earlier phases. The government prepared phase 3 based on the weaknesses highlighted in the most recent Public Expenditure and Financial Accountability assessment, carried out in 2013.[12] The plan also accounted for outstanding reforms from phase 2, and actions identified during consultations within the government and with development partners through the JPAM process. A high level of ownership for the reforms is evident, and a strong monitoring and evaluation system now in place. The ADB Anticorruption Policy (1998, as amended to date) was explained to and discussed with the government.

C. Poverty and Social

32. A stable macroeconomic position and existence of fiscal buffers will reduce the impact of external shocks and allow the government to appropriately respond to immediate needs following disasters, while maintaining basic social services. An efficient PFM has a positive impact on service delivery. Private sector development creates employment, which is critical for addressing poverty. Subprogram 1 is classified as having *no gender elements*, with better PFM and employment-creation function under the program bringing no specific benefits to women.

[12] PEFA. Samoa 2014. https://pefa.org/sites/default/files/assements/comments/WS-Dec14-PFMPR-Public.pdf

D. Safeguards

33. In accordance with the ADB Safeguard Policy Statement (2009), subprogram 1 is classified as *category C* for environment, involuntary resettlement, and indigenous peoples. The activities under the program will support policy and institutional reforms, and none of the activities will result in or lead to involuntary resettlement, or affect indigenous peoples or the environment.

E. Risks and Mitigation Measures

34. Major risks and mitigating measures are summarized in Table 3 and described in detail in the risk assessment and risk management plan.[13] PFM systems are assessed as sound and able to reasonably support the implementation of the government's fiscal policies and delivery of services. Integrated benefits and impacts of the program are expected to outweigh the costs.

Table 3: Summary of Key Risks and Mitigating Measures

Risks	Mitigating Measures
Commitment to sound macroeconomic management and fiscal management weakens	Continuous policy dialogue with the government and partners to develop joint expectations and commitments
High staff turnover diminishes reform implementation capacity	Technical assistance can be provided on a needs basis to supplement capacity
Delays in technical assistance delivery to implement reforms	Regular coordination discussions among development partners to identify and bridge gaps
External shocks undermine implementation of reforms and achievement of program goals	Continuous strengthening of the fiscal position to rebuild buffers; additional assistance in case of shocks

Source: Asian Development Bank.

IV. ASSURANCES

35. The government and the MOF have assured ADB that implementation of the program shall conform to all applicable ADB policies including those concerning anticorruption measures, safeguards, gender, procurement, consulting services, and disbursement as described in detail in the grant documents. The government has agreed with ADB on certain covenants for the program, which are set forth in the grant agreement.

V. RECOMMENDATION

36. I am satisfied that the proposed programmatic approach and policy-based grant would comply with the Articles of Agreement of the Asian Development Bank (ADB) and, acting in the absence of the President, under the provisions of Article 35.1 of the Articles of Agreement of ADB, I recommend that the Board approve

(i) the programmatic approach for the Fiscal Resilience Improvement Program, and
(ii) the grant of $5,000,000 to the Independent State of Samoa for subprogram 1 of the Fiscal Resilience Improvement Program, from ADB's Special Funds resources, and such other terms and conditions as are substantially in accordance with those set forth in the draft grant agreement presented to the Board.

Stephen Groff
Vice-President

10 November 2016

[13] Risk Assessment and Risk Management Plan (accessible from the list of linked documents in Appendix 2).

DESIGN AND MONITORING FRAMEWORK

Impact the Program is Aligned With			
Macroeconomic stability is maintained over the medium term (Strategy for the Development of Samoa, 2012–2016)[a]			
Results Chain	**Performance Indicators with Targets and Baselines**	**Data Sources and Reporting Mechanisms**	**Risks**
Outcome Fiscal resilience improved	**The Program** Current expenditure remains below 29.0% of GDP in FY2017 and FY2018 budgets (Baseline: FY2016 budgeted current expenditure of 29.1% of GDP). **Subprogram 1** Government targets fiscal deficit at or below 3.5% of GDP for FY2017 (Baseline: FY2016 deficit of 0.4% of GDP). **Subprogram 2** Government maintains its fiscal deficit target at or below 3.5% of GDP for FY2018.	Budget estimates IMF reports Budget estimates IMF reports Budget estimates IMF reports	Commitment to sound macroeconomic management and fiscal management weakens.
Outputs 1. Fiscal drain reduced through SOE reform	**The Program** Advances in SOE reform and performance, including through partnerships with the private sector, measured by the number of PPPs and privatization of SOEs **Subprogram 1** Cabinet approval of at least one PPP in line with the PPP framework Completed sale of Agriculture Store Corporation (August 2016) Cabinet approval of privatization policy **Subprogram 2** Establishment of a solid waste management PPP All public trading bodies to submit their audited annual accounts as required by Section 23 of the Public Bodies Act 2001 (as amended) for the fiscal year ending June 2017	Cabinet decision and MPE reports MPE reports MPE reports Cabinet decision and approved privatization policy MPE reports MPE reports	High staff turnover diminishes reform implementation capacity Delays in technical assistance delivery to implement reforms External shocks undermine implementation of reforms and achievement of program goals
2. Procurement systems improved	**The Program** An increase in the extent to which commonly procured items (such as pharmaceuticals and stationery) are	MOF reports	

Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting Mechanisms	Risks
	procured through framework arrangements that reduce the need for repetitive tender processes for the procurement of common items **Subprogram 1** Issue guidelines for the use of framework arrangement in public procurement, including speedy procurement in emergency situations. Revised treasury instructions that allow the use of framework arrangements (August 2016) New standard templates for procurement of major works issued **Subprogram 2** Establishment of an independent complaints mechanism Pilot framework arrangements for the purchase of pharmaceutical items	 MOF reports; revised instructions MOF reports; issued templates MOF reports; issued templates MOF reports MOF reports	
3. Debt management improved	**The Program** Compliance with medium-term debt management strategy, particularly on the concessionality of and economic returns from external loans, is maintained. **Subprogram 1** Approval by the cabinet of the new medium-term debt strategy Assessment of the previous medium-term debt strategy **Subprogram 2** External performance audit on debt management	 MOF reports MOF reports MOF reports MOF reports	
4. Resilience to climate change and variability promoted	**The Program** Informed public investment decisions to increase resilience across sectors **Subprogram 1** Approval of a national monitoring and reporting framework for climate change Include climate risk and resilience indicators in the updated Strategy for	 MOF reports MOF reports New Strategy for the Development of	

Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting Mechanisms	Risks
	the Development of Samoa. **Subprogram 2** Develop an integrated policy framework that allocates responsibilities for resilience across government agencies and informs decisions to increase resilience across key sectors including agriculture, forestry, water, coastal, and urban areas. Prepare a strategic investment plan that identifies key national infrastructure and prioritizes risk-reduction interventions, thereby providing a basis for more coordinated climate resilience financing.	Samoa, 2016–2020 MOF reports MOF reports	

Key Activities with Milestones

Not applicable.

Inputs

Asian Development Fund (grant):	Subprogram 1	$5.0 million
Asian Development Fund (loan):	Subprogram 2	$5.0 million

Assumptions for Partner Financing

World Bank (loan):	Subprogram 1	$5.0 million
	Subprogram 2	$5.0 million
Government of Australia (grant):	Subprogram 1	$2.3 million
	Subprogram 2	$2.3 million
Government of New Zealand (grant):	Subprogram 1	$2.5 million
	Subprogram 2	$2.1 million
European Union (grant):	Subprogram 1	$6.1 million
	Subprogram 2	$7.7 million

FY = fiscal year, GDP = gross domestic product, IMF = International Monetary Fund, MOF = Ministry of Finance, MPE = Ministry of Public Enterprises, PPP = public–private partnership, SOE = state-owned enterprise.

[a] Government of Samoa. 2012. *Strategy for the Development of Samoa, 2012–2016*. Apia.

Source: Asian Development Bank

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LIST OF LINKED DOCUMENTS

http://www.adb.org/Documents/RRPs/?id=50210-001-2

1. Grant Agreement
2. Sector Assessment (Summary): Public Sector Management (Public Expenditure and Fiscal Management)
3. Contribution to the ADB Results Framework
4. Development Coordination
5. Country Economic Indicators
6. International Monetary Fund Assessment Letter
7. Summary Poverty Reduction and Social Strategy
8. Risk Assessment and Risk Management Plan
9. List of Ineligible Items

DEVELOPMENT POLICY LETTER

Please address all correspondence to:
The Minister of Finance
Private Bag
Apia, Samoa

Telephone: (685) 34332
(685) 34183
Facsimile: (685) 21312

Government of Samoa

OFFICE OF THE MINISTER OF FINANCE

(Ministry of Finance; Central Bank of Samoa; Samoa National Provident Fund; Development Bank of Samoa; Samoa International Finance Authority; Samoa Life Assurance Corporation; Unit Trust of Samoa; Cabinet Development Committee; Tenders Board)

September 30, 2016

Mr. Takehiko Nakao
President
Asian Development Bank
6 ADB Avenue
Mandaluyong
Philippines

Dear Mr. Nakao

FISCAL RESILIENCE IMPROVEMENT PROGRAM

Samoa was the lead reformer and one of the most rapidly growing economies in the Pacific over the decade up to FY2008. The global economic crisis in 2008 and the impact of natural disasters have had adverse long-term impacts on growth, which averaged just 1.2% between FY2008 and FY2015—well below the 4.3% average between FY1999 and FY2007. Agriculture and tourism, contributing 35% of total output, have been the hardest hit sectors. Reflecting its resilience, Samoa has remained committed to reforms and targets development of the private sector. We joined the World Trade Organization in 2015 and have liberalized telecommunications and financial sectors. Macroeconomic and political stability, continued reforms and public investments in infrastructure has helped our economy grow.

2. The government launched the first phase of Public Financial Management Reform Plan (PFMRP) in 2008 following earlier capacity building initiatives. Under this phase aid Policy and Debt Management Strategy was developed, outcomes based budgeting was adopted, sector plans were prepared and the Ministry of Revenue was strengthened. Phase 2 of the PFMRP commenced in 2011 under which internal audit functions were strengthened, debt management reform plan was implemented and a medium term expenditure framework developed. Phase 3 of the PFMRP was launched in 2014 with the intention to build on reforms under the previous 2 phases.

3. Based on the PFMRP, the government, together with ADB, Governments of Australia and New Zealand and the World Bank agreed to a joint policy action matrix (JPAM) in March 2013. The JPAM has undergone revisions since then but the strategic focus on public financial management reform remains. The policy actions are designed to trigger budget support from various development partners.

4. Budget deficits since FY2009 have been above government's long-term target of 3.5% of GDP largely as a result of having to meet the country's reconstruction needs following natural disasters and the need to maintain growth in an adverse economic environment. The average annual fiscal deficit from FY2009 to FY2016 is equivalent to 4.7% of GDP. The fiscal balance has not been helped by the sharp decline in budgeted development partner grants in FY2016, which could lead to a worsening of the country's debt position. After bringing external debt down from over 100% of GDP in the late 1980s to about 30% in FY2009, debt levels have increased to 57.8% of GDP in FY2015. This is now estimated to have reduced to 52.6% of GDP in FY2016 mainly due to repayments to and grant financing from the ADB and the World Bank. The government is committed to consolidating its fiscal position, but the speed of consolidation needs to be managed carefully in order to minimize the possible impact on economic growth.

5. Despite average growth of 1.2% between FY2008 and FY2015 the Government is satisfied that the efforts to date have resulted in improving growth potential. While growth in FY2015 was 1.6%, the Government anticipates growth of 3.5% in FY2016 and 3.0%in FY2017. Inflation is relatively stable and foreign exchange reserves are reasonable although higher levels are preferred to ensure that buffers are adequate for the Government to respond appropriately to exogenous shocks. Debt levels, although declining in FY2016, still does not represent an adequate fiscal buffer.

6. It is with these tight economic conditions in view that the government is working with development partners to seek support to help rebuild buffers. At the same time the government is taking strong measures to ensure prudent fiscal management to reduce deficits and debt levels. Development partner support will enable the government to improve fiscal resilience in the medium term. Continued efforts to privatize public bodies and PPPs will create fiscal space and enhance opportunities for the private sector.

7. The program is expected to support macroeconomic stability. The program outcome is intended to be improved fiscal resilience. The program outputs are in line with government priorities and include (i) improved fiscal position through State Owned Enterprise (SOE) reforms; (ii) improved procurement systems; (iii) improved debt management; and to (iv) promote resilience to climate change and variability. The design and monitoring framework for the Program is attached as Annex 2. The policy-based operation through two sequential subprograms in 2016 and 2017 will support government objectives consistent with the program outcomes. Subprogram 1 outcomes are intended to be completed before 30 September 2016. These outcomes will be augmented through related reforms to be achieved before 30 September 2017 under Subprogram 2.

8. Government intends an improved fiscal position through SOE reforms. State Owned Enterprises (SOEs) continue to play an important role in the economy and in providing key services. SOE reforms will reduce Samoa's dependence on public finances. Privatization programs will continue in line with updated policies on ownership, performance and divestment. We have just finalized the privatization of Agriculture Stores Corporation and established a Public–private partnership (PPPs) Unit under the new MPE which will explore possibilities for improving SOE performances through PPPs.

9. Procurement reforms support our plans to ensure an efficient and strong public financial management system. We will continue to strengthen our procurement processes and systems through our legal and regulatory framework for public procurement approved in

2013. Efficient procurement systems ensure effective use of public resources. To continue with procurement reforms, Government will use with framework arrangements for public procurement of commonly procured items and for urgent procurement in times of emergencies.

10. Government will continue to improve its debt management processes. We have recently reviewed and updated our Medium Term Debt Management Strategy 2016-2020. Consistent with the JPAM our FY2017 budget intends to harness the productivity gains from the reform programs and has met the fiscal deficit target of 3.5% of Gross Domestic Product (GDP). The budget is consistent with our Fiscal Strategy Statement and the Medium Term Debt Management Strategy. Government has brought down the public debt level to 53% of GDP. This reaffirms our commitment to gradually reduce the debt to GDP ratio over the next decade.

11. Government intends to mainstream climate resilience in its plans and investments. Despite the good progress made, Samoa continues to suffer from climate change and variability. Agriculture and tourism are the mainstays of the Samoan economy. Agriculture comprises around 10% of the economy and employs roughly two-thirds of the largely rural-based population. Agricultural produce makes up the bulk of the country's exports, leaving the Samoan economy particularly vulnerable to natural disasters. Tourism accounts for approximately 25% of GDP. The tourism industry was hard hit by the tsunami and cyclone, following which many hotels and resorts were forced to close for essential repairs. The Government intends to mainstream climate resilience in public decisions and public investments. This will result in minimal disruptions to public infrastructure as a result of disasters.

12. The policy actions adopted under the Program grant reflect the national priorities as laid out in the Strategy for Development of Samoa (SDS) 2012-2016. The implementation of these policy actions will give direction to future public sector financial management reforms. Support provided by ADB, and other development partners to the JPAM will help the country build fiscal resilience and maintain macroeconomic stability. I am confident that our strong leadership, supported by financial and technical assistance from ADB and other development partners, will assist us to achieve these reform goals.

Sincerely yours,

Hon. Sili Epa Tuioti
MINISTER OF FINANCE

POLICY MATRIX

Subprogram 1

Output	Policy Actions	Verification Documents
Output 1: Fiscal drain reduced through state owned enterprise reform	1.1 Cabinet approval of at least one public private partnership (PPP).	1.1.1 Cabinet Decision
	1.2 Completion of sale of Agriculture Store by Ministry of Public Enterprises.	1.2.1 Cabinet Decision 1.2.2 Sale and Purchase Agreement
	1.3 Cabinet approval of privatization policy.	1.3.1 Cabinet Decision
Output 2: Improved procurement systems	2.1 Approved guidelines for the use of framework arrangements in public procurement, including speedy procurement in emergency situations issued by Ministry of Finance.	2.1.1 Guidelines for Goods, Works and General Services
	2.2 Approved Revised treasury instructions allowing the use of framework arrangements issued.	2.2.1 Certificate of Endorsement 2.2.2 Treasury Instructions Amendment
	2.3 Approved new standard template for procurement of major works issued.	2.3.1 Certificate of endorsement 2.3.2 Standard template for procurement of major works
Output 3: Improved Public Debt Management	3.1 Approval by the cabinet of the new medium term debt management strategy (MTDS).	3.1.1 Cabinet Decision 3.1.2 Medium–Term Debt Management Strategy 2016–2020
	3.2 Assessment of previous MTDS.	3.2.1 Assessment reported in MTDS 2016–2020
Output 4: Promoting resilience to climate change	4.1 Establish a national monitoring and reporting framework for climate resilience.	4.1.1 Cabinet Decision
	4.2 Include climate risk and resilience indicators in SDS, 2016–2020.	4.2.1 Key outcome in SDS 2016–2020

Subprogram 2

Output	Proposed policy actions
Output 1: Reduced fiscal drain through state owned enterprise reforms	1.1 Establishment of a solid waste management public private partnership.
	1.2 All SOEs to be up-to-date with their external audits.
Output 2: Improved procurement systems	2.1 Establishment of an independent complaints mechanism.
	2.2 Pilot framework arrangements for purchase of pharmaceutical items.
Output 3: Improved Public Debt Management	3.1 External performance audit on debt management.
Output 4: Promoting resilience to climate change	4.1 Develop an integrated policy framework that allocates responsibilities for resilience across government agencies and informs decisions to increase resilience across key sectors including agriculture, forestry, water, and coastal and urban areas, and be gender–responsive.
	4.2 Prepare a strategic investment plan that identifies key national infrastructure and prioritizes risk reduction interventions, thereby providing a basis for more coordinated climate resilience financing.

Source: Asian Development Bank.