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GOVERNMENT OF KIRIBATI  
**MINISTRY OF FINANCE & ECONOMIC DEVELOPMENT**  
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Mr. Jim Young Kim  
President  
The World Bank  
Washington, D.C., 20433

Dear President Kim,

**Re: Letter of Development Policy**

Kiribati faces important fiscal and economic challenges arising from frequent external shocks. In the last three years, Kiribati has enjoyed record fishing license fee revenue which helped boost growth, improve fiscal position, and strengthen the current account. At the same time, large donor-financed infrastructure projects have helped buoy domestic demand and mobilizing tax revenue. Low global food and commodity prices, too, have reduced import bills and kept down inflationary pressures. On the other hand, there were also challenges. Cyclone Pam and strong waves it generated pummeled many of our islands and damaged our fragile infrastructure. An outbreak of chikungunya affected a large segment of the population and required emergency government responses. Weakness in global trade and shipping activity has continued to weaken remittances from our seamen working on foreign vessels. And heightened volatilities in financial market, driven both by diverging monetary policies among advanced economies and sharp slowdowns in major emerging markets, has negatively affected the returns on the assets held in the Revenue Equalizing Reserve Fund (RERF).

To effectively deal with the frequent external shocks, the government is committed to building fiscal resilience and diversifying economic opportunities. After coming to power in March this year, the government launched the 2016–19 Kiribati Development Plan (KDP) identifying key development priorities in the medium term. In May, the government introduced the 2016 budget, increasing pro-poor spending on education and health, and the financial assistance to outer islands population, while maintaining the balanced budget. In June, the government has made the decision to replenish the RERF by \$70 million—the largest single transfer in more than a decade—to save wealth for future generations, and set aside \$56 million as cash reserves to build an adequate buffer against the unexpected shocks to which Kiribati is highly vulnerable. The government is committed to maintaining fiscal discipline, continuing to improve the quality of expenditure, and managing its resource revenue carefully to support the country's long run development priorities.

As elaborated in the KDP, prudent management of resources and promoting private sector growth remain the government's key policy priorities. The government recognizes the

importance of improving the management of the country's fisheries revenue, which is the most important domestic source of revenue. To improve the transparency of its management, the government has already undertaken important reforms, including the development of the national fisheries policy for 2013–2025 and the annual publication of a joint fisheries revenue report by the Ministry of Fisheries and Ministry of Finance. More recently, the government has begun reviewing the existing fisheries joint ventures to monitor their contribution to domestic employment and investment as well as sustainable management of fisheries resources. The government also recognizes the importance of prudent management of debt for safeguarding Kiribati's fiscal sustainability. To this end, the government has pursued a policy of no commercial borrowing, and strengthened the oversight of contingent liabilities arising from implicit and explicit guarantees to the SOEs. Finally, the government recognizes the importance of the RERF in anchoring Kiribati's economic and fiscal sustainability. With the support of the World Bank, the government has implemented a series of far reaching reforms to improve the management of the RERF, and most recently, appointed two new external asset managers to reduce management costs while improving the management standards to prevailing market benchmarks. At the same time, the government has completed the strategic reallocation of the RERF assets to better reflect the risk-return preference of the government and to ensure that the RERF's long term investment objectives will be met. The government has also requested the World Bank and the IMF to provide technical input on how to strike an appropriate balance between the welfare of the current and future generations in the management of the RERF, and options for making the transfers to and withdrawals from the RERF more predictable and transparent to safeguard its long term sustainability. The government looks forward to continuing its successful working with both institutions to strengthen the governance and the management of the RERF as well as the management of the cash reserves.

Private sector led growth remains a challenge as well as an opportunity for Kiribati. Because of its smallness, remoteness, and dispersed population across many islands, the country faces important constraints to private sector development. This government remains committed to expanding the opportunities for private sector led growth in the country, building on the successes of recent reforms. To reduce the communications and transport problems, the government is addressing the huge backlog in basic infrastructure with donor support, including roads, ports, and airports. To improve the business environment, the government is investing in improving telecommunications by encouraging domestic competition and expanding services to outer islands. The government is also pursuing a multi-year reforms to improve delivery of basic public services including electricity, water, and sanitation, which will be critical for encouraging local small businesses to take root, expand, and create jobs for the country's growing population.

The government welcomes the World Bank's assistance and continued engagement in Kiribati to maintain the reform momentum. The previous budget support operations have helped the government build the strong partnership with the World Bank as well as with the broader donor community, and to develop a shared vision and the consensus on priority reforms. The government looks forward to the World Bank's continued active engagement in Kiribati and its support for the country's ongoing reforms.

Yours sincerely

A handwritten signature in black ink, consisting of a large, stylized initial 'T' followed by a long horizontal stroke that ends in a small hook.

Hon Dr Teuea Toatu

Minister for Finance and Economic Development