Program Information Document (PID)

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BASIC INFORMATION

A. Basic Project Data

Country Tuvalu	Project ID P161867	Project Name Tuvalu Fourth Development Policy Operation	Parent Project ID (if any)
Region East Asia and Pacific	Estimated Board Date May 23, 2018	Practice Area (Lead)(s) Macroeconomics, Trade & Investment	Financing Instrument Development Policy Financing
Borrower(s) Tuvalu	Implementing Agency Ministry of Finance and Economic Development		

Proposed Development Objective(s)

The objective is to support the reform agenda of the Government of Tuvalu in:
* improving social service delivery, and
* building macroeconomic stability

Financing (in US$, Millions)

SUMMARY

Total Financing	US$ 5 million

DETAILS

Source: IBRD/IDA/Others (Specify) Co-financing	IDA

Decision

The Decision from the Concept Meeting was to proceed with the preparation of the operation.

B. Introduction and Context

Country Context

Tuvalu's economy is highly vulnerable to challenges stemming from its very small size, geographic isolation and structural economic conditions, and relies heavily on grants and buffer assets to absorb shocks. Tuvalu is comprised of three reef islands and six atolls. With a total land area of only 26km2 and a population estimated at 11,000, it is one of the smallest and most remote states in the world. The private sector remains small (consisting mainly of small firms in the wholesale and retail sectors), and has struggled to grow partly due to the inherent lack of economies of scale resulting from remoteness and the dispersion of a small population across nine islands. The public sector is the main river of economic activity, accounting for around 36 percent of GDP in 2015[1], as well as the majority of formal sector employment.

These extreme physical challenges in turn limit growth prospects. The Tuvalu Trust Fund (TTF) and its auxiliary fund the Consolidated Investment Fund (CIF) are the main stabilizing tool for volatile fiscal outcomes, and building adequate buffers in these funds to meet long term financing needs is critical to the sustainability of Tuvalu. Geography, external shocks and access to services pose challenges to poverty reduction and inclusive growth. The Government of Tuvalu (GoT) has laid out an agenda to address these challenges and improve macroeconomic sustainability as set out in its National Strategy for Sustained Development 2016-2020 (TKIII). Drawing from this, a policy reform matrix was developed by the GoT, in consultation with the World Bank and other development partners, to pursue measures that would reduce vulnerabilities, ease fiscal constraints, and enhance the effectiveness of key government programs, including in health and education. The proposed operation builds on the policy dialogue between the GoT and the World Bank over the past five years, and supports reform areas where the World Bank can add value in coordination with other development partners. This operation is proposed as the second in a programmatic series of two Development Policy Operations in support of Tuvalu's ongoing reform efforts and its broader development strategy. Financing provided through the operations will support the maintenance of buffers to meet long term financing needs, including those arising from future climate related shocks. Maintenance of adequate buffer assets will in turn ensure Tuvalu's ability to absorb future shocks without disruption to the level of service delivery.

Relationship to CPF

The proposed operation is aligned with the priorities identified in the Regional Partnership Framework (RPF) for 9 Pacific Island Countries[2]. The RPF is focused around four themes, namely: i) fully exploiting the available economic opportunities; ii) enhancing access to employment opportunities; iii) protecting incomes and livelihoods; and iv) as a cross-cutting theme, strengthening the enablers of growth opportunities (macroeconomic management, infrastructure, and addressing knowledge gaps). The proposed operation will contribute directly to these priorities by supporting reforms to improve social service delivery and improved health and education outcomes, further improve the management of the TTF, and provide more efficient and evidence-based public expenditure management, which will in turn improve the investment climate and encourage private sector growth.

[1] based on latest available data
[2] The RPF was developed for Kiribati, the Republic of Nauru, the Republic of the Marshall Islands, Federated States of Micronesia, Republic of Palau, Independent State of Samoa, Kingdom of Tonga, Tuvalu and Vanuatu – drawing on the PIC-8 SCD.

C. Proposed Development Objective(s)

The proposed operation continues to support the reform agenda of the Government of Tuvalu (GoT) in the critical areas of (i) improving social service delivery; and (ii) building macroeconomic sustainability. These two areas are central to the GoT's National Strategy for Sustainable Development (NSSD) or Te Kakeega III (TKIII), and to the Systematic Country Diagnostic for eight small Pacific Island Countries (PIC-8 SCD).

Key Results

The first pillar of the proposed operation supports reforms to improve social service delivery. More specifically, reforms under this pillar will improve longer-term education outcomes through improved school-readiness and childhood literacy during the early years of education. Increasing selected excise taxes, including on tobacco products, will help reduce risk factors to non-communicable diseases. Together these reforms will allow the GoT to achieve higher quality health and education outcomes.

The second pillar of the proposed operation supports reforms to improve macroeconomic sustainability. Reforms to strengthened reserve asset management and improve the effectiveness of wage bill controls will help reduce Tuvalu's unique vulnerabilities by building fiscal resilience to better respond to exogenous shocks. These reforms are not only aligned with the TKIII objectives of supporting security and prosperity of all Tuvaluans, but are also aligned with the broader World Bank goal of boosting shared prosperity.

D. Concept Description

The reforms under the first pillar, improving social service delivery, are focused on (a) improving longer-term education outcomes through supporting improved school-readiness and childhood literacy during the early years of education; and (b) supporting improved health sector outcomes while ensuring its ongoing fiscal sustainability. The reforms under the second pillar of the operation aim at improving macroeconomic stability through (a) strengthening the investment management of the country's reserve assets; and (b) supporting ongoing reforms to improve the linkage between public service hiring decisions with budget implications to promote more fiscally sustainable public service delivery. The government recognizes the critical importance of improving service provision, if it is to achieve the objective of its development strategy to achieve a greater level of security and prosperity for all Tuvaluans, including through achievement of higher standards of quality health and education. It also recognizes that reforms under the second pillar will help reduce Tuvalu's vulnerabilities by building resilience to better respond to exogenous shocks. Financing provided through the proposed second operation of this programmatic series will support these endeavors, by directly supporting the maintenance of fiscal buffers and meet Tuvalu's long-term financing needs. More importantly, the operation will sustain the reform momentum built throughout the previous operations in this and the previous programmatic series of DPOs.

E. Poverty and Social Impacts and Environment Aspects

Poverty and Social Impacts

The policy actions supported under the proposed operation are expected to have a significant positive impact on poor people and vulnerable groups. Under the second pillar of the operation, embedding a wage bill model into the annual budget planning and preparation cycle will benefit all Tuvaluans—but especially the poor and vulnerable. In general, their wellbeing is disproportionately dependent on government services, and so they stand to benefit most from improved efficiency in public spending and service delivery. The prior action to strengthen investment management of the TTF are also expected to benefit the poor and vulnerable for the same reason, and furthermore, as the government plans on aligning the management of the TSF under the TTF governance structure. Moreover, the poor are likely to be acutely dependent on public relief and recovery efforts in the event of a natural disaster, and thus most inclined to benefit from improved resilience, facilitated through TSF disbursements. They are likely to be particularly adversely impacted by natural disasters, in part because they tend to live in housing that is more vulnerable to damage in wild weather. The 2010 HIES indicates that households living below the basic-needs poverty line are twice as likely to live in dwellings made of relatively less sturdy materials (walls of traditional thatched materials, or improvised corrugated iron) than households above the poverty line (8 versus 4 percent). Also, they tend to have fewer private resources to draw upon in the event of a shock, and are more likely to be excluded from traditional social networks which might offer some support during trying times. World Bank (2014) analysis of the 2010 HIES indicates that over a two-week period[3], gift receipts were reported by less than 20 percent of households in the poorest decile in Tuvalu, but close to half of all households in the wealthiest decile.

The amendments to excise taxes on tobacco, alcohol and sugary drinks are expected to have a net positive impact on the poor over the long run. In the short term, the higher taxes on sin goods will have an adverse impact on household budgets for the poor, particularly where members continue to consume the affected products unabated. However, the magnitude of the impact is likely to be relatively small. World Bank staff estimates from the 2010 HIES suggest that on average, households living below the basic needs poverty line currently spend next to nothing on alcohol, probably a negligible amount on the sugary drinks (namely, cordial) which will be subject to higher taxation, and only 1.5 percent of their consumption budgets on tobacco. An analysis of aggregate imports data, coupled with existing excise rates, suggests that around half of current consumer spending on tobacco is on cigarettes—whose excise rate will be unchanged—and the other half on 'Other manufactured tobacco'—whose excise rate will increase from 10 to 185 percent. This implies that without any change in consumption behavior, the increase in the taxes on sin goods is likely to displace just a little over 1 percent of spending that poor households were previously directing towards other basic needs. Ultimately the tax increases aims to reduce consumption levels of the sin goods—to reduce the incidence of NCD and reallocate public health expenditure toward primary and preventative care. Since the poor are more resource-constrained, their consumption of the sin goods is potentially more price-sensitive than wealthier households. In any case, the poor in Tuvalu, like the broader population, often have high levels of risk factors for NCD, so they stand to benefit substantially from changing consumption behavior over the long run.

The policy actions supported under the proposed operation are also expected to have a positive gender impact. Under the second pillar of the operation, improving macroeconomic sustainability will support sustained service delivery and economic opportunities, including to women. Under the first pillar of the operation, reforms to improve early childhood literacy and school readiness will likely disproportionately benefit women given attendance rates are higher for girls. Similarly, reforms to reduce consumption of sin goods could also disproportionately benefit women, including through reduced domestic violence against women which has been a concern in Tuvalu. The 2007 DHS reported that 4 in 10 women have been subjected to some type of physical violence, with their current husbands or partners being the main perpetrators (84.6 percent) and the frequency of husband's alcohol consumption is in turn associated with level of spousal violence. In the long term, reducing the cost of treatment for NCDs will create room to reorient expenditure towards primary, preventative and maternal care, which women disproportionately depend on.

Environment Impacts

[3] World Bank (2014), Hardship and Vulnerability in the Pacific Island Countries

The policy reforms supported by this operation are unlikely to have any negative effects on Tuvalu's environment. Reforms to improve social service delivery have the potential opportunities to attain environmental benefits by having environmental linkages manifested through improvements to health and education service delivery. Reforms to support macroeconomic sustainability through the strengthening of the investment management of the country's reserve assets and improving the effectiveness of payroll expenditures are not likely to have any significant environmental impacts. Therefore, the prior actions supported under this operation are not expected to create negative impacts on Tuvalu's environment, forests and other natural resources.

In general, Tuvalu's environmental protection regime is adequate and has been strengthened over time by substantial project engagements and technical assistance from development partners. The Environmental Protection Act (2008) provides the overarching legislative framework for environmental protection and management, including the requirement to perform environmental impact assessments for larger projects. Capacity in the Department of Environment, however, remains thin – such that the GoT will continue to be heavily reliant on outside expertise provided by regional organizations, notably the Secretariat of the Pacific Regional Environment Program (SPREP). Substantial project engagements and technical assistance from development partners, including from the World Bank, in recent years have supported the strengthening of the environmental protection framework and capacity for risk management. As such, it is generally considered that adequate protection would be provided by the existing legal and administrative frameworks for environmental assessment and land management in Tuvalu.

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APPROVAL

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