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July 15, 2021

**Statement by Mr. Azal and Mr. Zaborovskiy on Tuvalu
(Preliminary)
Executive Board Meeting
July 19, 2021**

We thank staff for the informative set of papers, and Messrs. Huh and Iona for their insightful Buff statement. As a fragile island microstate with a population of around 11,000, Tuvalu faces significant development challenges, including its vulnerability to climate change and rising sea levels, and volatile fishing revenues. The global COVID-19 pandemic added to these challenges by halting travel, with a sizable negative impact on the implementation of infrastructure projects and travel-related economic activities. Nevertheless, the authorities acted decisively, allowing Tuvalu to remain COVID-19-free and avoid a recession in 2020 by providing the needed financial support to affected households and businesses. International donors also helped Tuvalu cushion spillovers from the global pandemic. We positively note that the authorities broadly concurred with staff's assessment and found policy recommendations tailored. **Against this backdrop, we agree with the thrust of staff's appraisal and policy advice.**

Strengthening the fiscal framework and advancing public financial management remain important priorities to ensure budget and debt sustainability. While the Tuvaluan authorities managed to achieve a budget surplus in 2020 as fishing-related revenues soared, medium-term fiscal challenges are elevated. Revenue volatility and pressures on the expenditure side – including public sector wages, overseas scholarships, project-related capital investments, and the uncertainty around the course of the global pandemic – create significant risks to budget sustainability. We also agree with staff that significant resources will be necessary for climate adaptation and to build buffers against future shocks, including natural disasters and the materialization of contingent liabilities. In this regard, we concur with the advised gradual growth-friendly fiscal consolidation, guided by a well-established fiscal anchor, and underpinned by increasing spending efficiency and mobilizing domestic revenues. *Regarding the proposed fiscal anchor, we wonder whether a broader definition, capturing some fishing-related revenues and capital expenditures, would be more*

appropriate given the economy's structure, rather than the narrow approach favored by staff. Staff's further comments are welcome. Overall, we support the well-justified fiscal policy recommendations outlined in the Report, and are encouraged to learn from the Buff statement that the authorities plan to proceed with their implementation.

Addressing the underlying causes limiting financial sector development and credit to the private sector would be critical to support Tuvalu's sustainable growth and boost financial inclusion. In Tuvalu, as in other microstates, many structural constraints hinder financial sector development. Over the recent years, financial depth in Tuvalu significantly declined and lending to the private sector remains noticeably lower than in peer countries. In this regard, implementing a mutually consistent reform package to increase financial depth, foster financial inclusion, and boost financial efficiency is of the utmost importance. We caution against considering FinTech solutions as a main means to resolve the current problems in the financial sector and agree with staff's emphasis on a careful cost-benefit analysis and technical support from development partners before launching any state-supported projects in this field. We are also concerned about the sudden loss of the National Bank of Tuvalu's correspondent banking relationship with an Australian bank earlier this year. As noted in the Buff statement, this creates a risk of Tuvalu being cut off entirely from the international payments system. *As Mr. Nakunyada and Ms. Basutli in their statement, we would like staff to further elaborate on the effectiveness of the authorities' remedial measures.* We echo staff's comprehensive recommendations on safeguarding the integrity and stability of Tuvalu's financial system.

We welcome the authorities' efforts to continue implementing structural reforms envisaged in the Policy Reform Matrix (PRM), underpinned by development partners' financial assistance. A clear accountability framework is needed to ensure that structural reforms, including ones outlined in the PRM, are implemented timely. We note with concern that staff assessed the lack of strong commitment to PRM and poor engagement with development partners as a high probability risk in the Risk Assessment Matrix. *Could staff comment on the main reasons?* We encourage the Tuvaluan authorities to press ahead with the reform agenda to achieve higher and more inclusive growth. Mapping the National Strategy for Sustainable Development into the UN Sustainable Development Goals (SDGs) framework would also facilitate the mobilization of international financial support to achieve the SDGs in areas such as Climate, Affordable and Clean Energy, the Fight Against Hunger, Quality Education, and Gender Equality.

Finally, as Messrs. Bevilaqua and Fuentes, and Ms. Mahabir in their statement, we stress the importance of boosting capacity in the field of the collection, processing, and dissemination of national statistics in Tuvalu. We welcome the Fund's continued support in this area.