SOUTH PACIFIC ISLANDS

Table 1  2021
Population, million
Samoa  0.20
Tonga  0.10
Vanuatu  0.31
GDP, US$, billion
Samoa  0.84
Tonga  0.46
Vanuatu  0.95
GDP per capita, current US$
Samoa  4216
Tonga  4669
Vanuatu  3045

Sources: WDI, Country authorities, and World Bank staff estimates.

The economies of Samoa, Tonga, and Vanuatu have been hit by multiple shocks, including natural disasters, the COVID-19 pandemic, and the war in Ukraine. Notably, Tonga was devastated by a volcanic eruption and tsunami. The pandemic continues to dampen economic activity as strict travel restrictions hit tourism-related activity with negative spillovers to the rest of the economy. Governments need to continue supporting the vulnerable and embark on structural reforms to support inclusive economic recovery.

Key conditions and challenges

Natural disasters and external shocks pose a constant threat to livelihoods, economic growth, and fiscal sustainability in the South Pacific. Enhancing resilience is crucial to supporting long-run growth and achieving sustainable improvements in living standards and poverty reduction. The economies continue to be battered by consecutive shocks, delaying economic recovery. This creates significant potential for scarring effects in the longer term, particularly in the tourism sector. Lost firms and jobs create adverse structural changes to the economy that are not reversed when aggregate demand recovers. The economic shocks and slow recovery greatly increase the risk of poverty, particularly as households deplete savings and assets to cope with lost incomes.

The main immediate challenge is to limit harm to the most vulnerable from rampant inflation. For Tonga, the priority is also on recovery from the recent tsunami. While the COVID vaccination rate is encouraging in Samoa and Tonga, Vanuatu needs to step up the vaccine rollout. The near-term challenge will be to strike an appropriate balance between catalyzing a sustainable and inclusive economic recovery and maintaining macroeconomic balance in the face of several competing pressures. With limited fiscal space, governments need to prioritize strategic measures that lay the foundation for economic recovery, while also supporting livelihoods for the bottom 40 percent of households. Effective implementation of structural reforms will be critical to ensure a sustainable economic recovery.

Recent developments

Border closures in response to the pandemic created economic downturns. Substantial donor funding cushioned the negative impact on fiscal and external balances. Inflation remained low prior to the war in Ukraine but has spiked in recent months. The Samoan economy recorded a historical-high recession in FY21. Border closure resulted in a sharp contraction of tourism and related industries, and hindered construction activity. Despite policy support and robust remittances, real GDP contracted by 7.1 percent. Inflation tanked to a historical low of -3.0 percent amid the economic slowdown but has been soaring in recent months. Poverty, measured against national standards of living, is likely to have risen from the latest pre-pandemic rate of 22.7 percent (2018), with urban areas affected more due to the higher concentration of jobs in the services sector. Substantial development partner grants, spending under-execution, and favorable tax revenue outturn, reflecting improved tax compliance helped attain a fiscal surplus of 2.2 percent of GDP. The current account recorded a substantial deficit (14.3 percent of GDP) as tourism receipts came to a standstill. The Tongan economy is estimated to have contracted by 2.7 percent in FY21, due to the impacts of COVID-19 and TC Harold—a
category 5 cyclone that struck the country in April 2020. These shocks resulted in a slowdown in the tourism, retail, and agriculture sectors. However, a severe contraction was avoided due to the fiscal stimulus implementation, ramp-up of reconstruction activities from TC Gita (2018) and TC Harold, and buoyant remittance inflows. Inflation remained low at 1.4 percent due to the economic slowdown and depressed import prices but has been increasing recently. A marginal fiscal deficit of 0.4 percent of GDP was recorded, supported by high grants and better-than-expected domestic revenue collections. Robust remittances and lower service imports helped attain a current account surplus of 5.3 percent of GDP.

In Vanuatu, following a deep recession in 2020, economic growth is estimated to have recovered to 0.5 percent in 2021, with around 40 percent of the population living below the lower-middle-income poverty line (US$3.65 per day in 2017 PPP terms). The recovery was underpinned by an uptick in industrial production, rising agricultural output, and the fiscal stimulus implementation. Inflation averaged 3 percent in 2021, within the Reserve Bank of Vanuatu’s target rate of 0-4 percent. Stronger than expected revenue collections and development partner grants helped record a fiscal surplus of 2.3 percent of GDP. The current account recorded a deficit of 1.9 percent of GDP, predominantly driven by subdued tourism receipts and high demand for imported machinery and transport equipment.

### Outlook

The materialization of downside risks, primarily associated with the war in Ukraine and the deepening global economic slowdown is expected to suppress the pace of economic recovery. Vanuatu re-opened its borders in July 2022, followed by Samoa and Tonga a month later. While tourism has prospects to show some resilience post-border reopening, external headwinds may have implications on the sector’s recovery. Inflation is projected to spike in FY22 driven by higher commodity prices and supply chain constraints resulting from the war in Ukraine and gradually fall from FY23. Downside risks to inflation include a protracted war in Ukraine that further elevates commodity prices and other external shocks. Poverty rates across the three countries will gradually decline as economic activity picks up and jobs become available but will remain higher than pre-pandemic levels until full economic recovery is achieved.

In Samoa, the economy is projected to contract further by 5 percent in FY22, driven by the continued border closure and the domestic COVID outbreak in March 2022. Nonetheless, a gradual recovery is projected from FY23 onwards with growth averaging 3.3 percent in FY23-24. The rebound is expected to be driven by a gradual resumption of tourist activity, spillovers to other sectors, and ramping up of capital projects. Inflation is estimated at 8.8 percent in FY22 as supply-related shocks to commodity prices continue. A modest average fiscal deficit of 1 percent of GDP is projected from FY22-24, supported by a gradual withdrawal of fiscal stimulus and the economic recovery. With the slow recovery tourism, the current account deficit is expected to remain elevated in FY22 before narrowing over the medium term.

In Tonga, the economy is expected to contract by 1.6 percent in FY22, reflecting the impact of the recent tsunami on agricultural production, the commercial sector, and tourism, aggravating the COVID-related impact. Meanwhile, food insecurity has become more severe—particularly among poorer households—as indicated by the first round of the World Bank high-frequency phone surveys, collected from April to May 2022. Growth is expected to rebound to 3.3 percent in FY23 and FY24 driven by reconstruction activity, recovery in agriculture, and a gradual pick up in tourism receipts. Inflation is expected to rise to 7.2 percent in FY22 due to higher fuel and food prices amid supply chain constraints, COVID-19 restrictions, and the tsunami, before subsiding from FY23. The fiscal and current account deficits are projected to remain elevated in FY23-24 as reconstruction activities and recovery efforts continue, before narrowing over the medium term.

### TABLE 2 South Pacific Islands / Macro poverty outlook indicators

<table>
<thead>
<tr>
<th></th>
<th>2019</th>
<th>2020</th>
<th>2021e</th>
<th>2022f</th>
<th>2023f</th>
<th>2024f</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Real GDP growth, at constant market prices</strong></td>
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<td></td>
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</tr>
<tr>
<td>Samoa</td>
<td>4.5</td>
<td>-3.1</td>
<td>-7.1</td>
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<tr>
<td>Tonga</td>
<td>0.7</td>
<td>0.5</td>
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<td>-1.6</td>
<td>3.3</td>
<td>3.2</td>
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<tr>
<td>Vanuatu</td>
<td>3.2</td>
<td>-5.4</td>
<td>0.5</td>
<td>2.2</td>
<td>3.4</td>
<td>3.5</td>
</tr>
<tr>
<td><strong>Lower middle-income poverty rate ($3.65 in 2017 PPP)</strong></td>
<td>34.5</td>
<td>39.4</td>
<td>40.2</td>
<td>40.5</td>
<td>39.9</td>
<td>39.3</td>
</tr>
</tbody>
</table>

Sources: World Bank and IMF.
Note: e = estimate; f = forecast. Financial years for Samoa and Tonga are July-June, for Vanuatu it is January-December.
\( a / \) Calculations based on EAPPOV harmonization, using 2019-NSDP.
\( b / \) Projection using neutral distribution (2019) with pass-through = 1 (High) based on GDP per capita in constant LCU.