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DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

DOMINICAN REPUBLIC

EMERGENCY PROGRAM FOR MACROECONOMIC AND FISCAL SUSTAINABILITY

(DR-L1145)

LOAN PROPOSAL

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ABBREVIATIONS

BCRD	Banco Central de República Dominicana [Central Bank of the Dominican Republic]
COVID-19	Coronavirus disease 2019
FASE	Fondo de Asistencia Solidaria al Empleado [Employee Solidarity Assistance Fund]
IMF	International Monetary Fund
RFI	Rapid Financing Instrument
SARS-CoV-2	Severe acute respiratory syndrome coronavirus 2
SDL	Special Development Lending
SDR	Special drawing rights
TC	Technical cooperation
WHO	World Health Organization

PROJECT SUMMARY

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<table>
<tr><th colspan="5">Financial Terms and Conditions</th></tr>
<tr><td colspan="3">Borrower:</td><td colspan="2">Special Development Lending[a]</td></tr>
<tr><td colspan="3">Dominican Republic</td><td>Amortization period:</td><td>7 years</td></tr>
<tr><td colspan="3">Executing agency:</td><td>Disbursement period:</td><td>1 year</td></tr>
<tr><td colspan="3">Ministry of Finance</td><td>Grace period:</td><td>3 years</td></tr>
<tr><td>Source</td><td>Amount (US$)</td><td>%</td><td>Interest rate:</td><td>3-month LIBOR in U.S. dollars, plus/minus the IDB lending spread, plus the variable interest spread for Ordinary Capital resources, plus the fixed premium on the lending spread of 115 basis points[a]</td></tr>
<tr><td rowspan="2">IDB (Ordinary Capital):</td><td rowspan="2">250,000,000</td><td rowspan="2">100</td><td>Front-end fee:</td><td>1% of the loan principal, payable within 30 days after entry into effect of the contract[a]</td></tr>
<tr><td>Credit fee:</td><td>0.75%[a]</td></tr>
<tr><td rowspan="2">Total:</td><td rowspan="2">250,000,000</td><td rowspan="2">100</td><td>Weighted average life:</td><td>5 years</td></tr>
<tr><td>Currency of approval:</td><td>U.S. dollars</td></tr>
<tr><th colspan="5">Project at a Glance</th></tr>
<tr><td colspan="5">Project objective/description: The general objective of the program is to contribute to strengthening the fiscal and economic policies underpinning the response of the Government of the Dominican Republic to the COVID-19 pandemic, with a view to ensuring fiscal sustainability and macroeconomic stability. The specific objectives are: (i) to restore fiscal discipline to achieve public debt sustainability; and (ii) to maintain a stable balance of payments.
The program's objectives and components are aligned with the Rapid Financing Instrument (RFI) of the International Monetary Fund (IMF), approved on 29 April 2020. The budgetary support provided under the Special Development Lending (SDL) category will contribute to finance efforts to contain the health crisis, mitigate its impact on vulnerable households, and promote countercyclical policies to reduce its effect on the economy in the short term. The program is structured as a single operation to be disbursed in a single tranche.</td></tr>
<tr><td colspan="5">Commitments and disbursement of the loan proceeds: The sole disbursement of the loan proceeds will be made in accordance with the terms established in the Loan Contract to be signed between the borrower and the Bank, including the provision requiring that proceeds under the RFI financing arrangement approved by the IMF are being or have been disbursed. The Commitments Matrix (Annex II) identifies the commitments made by the Government of the Dominican Republic and contained in its Letter of Intent to the IMF, dated 13 April 2020, which forms an integral part of the IMF report, Request for Purchase Under the Rapid Financing Instrument, approved by the IMF Executive Board. These commitments are also identified in the Policy Letter sent by the Government of the Dominican Republic to the Bank on 10 June 2020 and will be reflected in the abovementioned Loan Contract (see paragraph 4.2).</td></tr>
<tr><td colspan="5">Exceptions to Bank policies: None.</td></tr>
<tr><th colspan="5">Strategic Alignment</th></tr>
<tr><td colspan="2">Challenges:[b]</td><td>SI ☐</td><td>PI ☐</td><td>EI ☐</td></tr>
<tr><td colspan="2">Crosscutting themes:[c]</td><td>GD ☐</td><td>CC ☐</td><td>IC ☒</td></tr>
</table>

[a] Under the Special Development Lending category (document AB-3134) and its Operational Guidelines (document GN-2031-17), this operation will be documented under the Flexible Financing Facility (FFF) with limited debt management options. The borrower has the option of requesting currency, interest rate, and commodity conversions. The Bank will take operational and risk management considerations into account when reviewing such requests. The applicable amortization schedule for this loan will consist of equal, six-monthly installments that begin to accrue at the end of the grace period.

[b] SI (Social Inclusion and Equality); PI (Productivity and Innovation); and EI (Economic Integration).

[c] GD (Gender Equality and Diversity); CC (Climate Change and Environmental Sustainability); and IC (Institutional Capacity and Rule of Law).

I. PROJECT DESCRIPTION AND RESULTS MONITORING

A. Background, problem addressed, and rationale

1.1 **Macroeconomic environment.** The Dominican Republic has the largest economy in the region of Central America and the Caribbean, with a GDP of around US$88 billion (2019). After the 2003 economic crisis, the country embarked on a path of sustained growth. The Dominican economy averaged 5.5% annual growth in 2006-2019, surpassing the Latin America and Caribbean average of 2.4% and posting the highest growth rate in Latin America in 2018 and 2019. The current account deficit has averaged 3.5% of GDP in the past decade, driven by a trade deficit in goods (12% of GDP on average) and a sizable outflow of payments, albeit moderated by the inflow of remittances (7.1% of GDP on average) and revenues from tourism (8.3% of GDP on average).

1.2 The consolidated deficit shrank from 8.0% to 4.1% of GDP between 2012 and 2016, due mainly to a decrease in public spending (particularly capital expenditure) equivalent to 2.3 percentage points of GDP. Progress has stalled since then, however, and the consolidated deficit has stayed around 4% of GDP.

Table 1. Selected economic indicators, 2015-2019

	2015	2016	2017	2018	2019
Real GDP growth (% variation)	6.5	7.0	4.7	7.0	5.1
Unemployment (% of economically active population)	7.3	7.1	5.5	5.7	6.2
Inflation (%, end of period)	2.3	1.7	4.2	1.2	3.7
Total revenue (% GDP)	16.6	13.9	14.0	14.2	14.4
Tax revenue (% GDP)	12.8	12.9	13.0	13.0	13.3
Total central government expenditure (% GDP)	16.7	17.0	17.1	16.3	16.6
Primary expenditure (% GDP)	14.3	14.4	14.8	13.9	14.0
Consolidated public-sector fiscal balance (% GDP)	-1.7	-4.1	-4.1	-3.5	-3.3
Remittances received (% GDP*)	7.0	6.9	7.4	7.6	7.2
Public sector debt (% GDP)	44.7	46.6	48.9	50.4	53.6

Sources: IMF, World Economic Outlook (April 2020) and Country Report 20/154.

* Balance of payments data is from the Balance of Payments and International Investment Position Manual, sixth edition, updated from 2010 onward.

1.3 **The COVID-19 pandemic and the health crisis.** Severe acute respiratory syndrome coronavirus 2 (SARS-CoV-2), which causes coronavirus disease 2019 (COVID-19), was first detected in China in late 2019 and quickly spread to the rest of the world. On 11 March 2020, the World Health Organization (WHO) declared it a pandemic, and as of 1 June 2020 there were more than 6 million confirmed cases and over 371,000 deaths related to COVID-19 worldwide.[1] Although the spread of SARS-CoV-2 in the Americas began later than in Asia and Europe, the number of cases has also been increasing rapidly. By 1 June

[1] World Health Organization (2020). Situation Report.

2020, North, Central, and South America had 2,817,232 confirmed infections and more than 160,500 deaths,[2] although these figures will soon be out of date.

1.4 COVID-19 is a highly contagious disease.[3] On average, recorded cases in a country rise daily by 33%.[4] This high rate of contagion leads to spikes that can overwhelm the capacity of health systems, since sick patients require specialized medical care. To keep this from happening, social distancing and isolation have become essential measures in the public health response, since they slow the transmission of COVID-19[5] and delay demand for medical services.[6] Implementing this type of measure is particularly important in Latin America and the Caribbean, considering that a recent WHO analysis shows that most countries of the region are unprepared to manage pandemics.[7]

1.5 As of 1 June 2020, the Dominican Republic had a total of 17,752 confirmed cases, including 6,162 active cases, 11,075 recovered patients, and 515 deaths.[8] Of the active cases, 1,989 (32%) are hospitalized, and 4,173 (68%) are quarantined at home. Residents of the National District (4,542) and the provinces of Santo Domingo (4,700), Santiago (1,487), San Cristóbal (1,050), and La Vega (918) account for a combined 70% of the confirmed cases.

1.6 **Pandemic response actions.** Although social distancing and stay-at-home restrictions may slow the transmission of COVID-19, they have not fully stopped the spread of the disease worldwide. For that reason, countries have had to implement additional health measures. First, to replicate relatively successful experiences like South Korea's, early health sector interventions are needed for mass testing of the population to detect the presence of the virus and trace possible cases of contagion so they can be isolated. Interventions of this kind have proven effective in ending health crises more swiftly.[9] [10] Additionally, the supply of health services must be increased, to treat infected people with serious symptoms. Both types of interventions require physical and financial resources delivered in an urgent and timely manner. Many countries, including several in Latin America and the Caribbean, have been rapidly scaling up public health

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2 World Health Organization (2020). Situation Report.

3 COVID-19 can be spread from person to person through respiratory secretions and direct contact.

4 This means that the number of new infections more than doubles approximately every three days, if public health measures are not taken to contain the spread. Financial Times (2020).

5 Eichenbaum M. S., Rebelo S., and Trabandt, M. (2020). The Macroeconomics of Epidemics (No. w26882). National Bureau of Economic Research.

6 Hellewell J., Abbott S., Gimma A., Bosse N. I., Jarvis C. I., Russell T. W., et al. Feasibility of Controlling COVID-19 Outbreaks by Isolation of Cases and Contacts. Lancet 2020; 8(4):488-496.

7 Operational capacity was assessed according to the percentage of fulfillment of the 13 core capacity requirements to manage public health events established in the International Health Regulations (2005), an agreement among 196 countries to build capacity to respond to such events.

8 Special Bulletin No. 75 of the Ministry of Public Health, 1 June 2020.

9 A recent study on the impacts of the 1918 flu pandemic found that cities that acted earlier and more aggressively grew faster once the pandemic was over. S. Correia, S. Luck, and E. Verner. Pandemics Depress the Economy, Public Health Interventions Do Not: Evidence from the 1918 Flu.

10 Prem K., Liu Y., Russell T. W. et al. The Effect of Control Strategies to Reduce Social Mixing on Outcomes of the COVID-19 Epidemic in Wuhan, China: A Modelling Study. Lancet Public Health 2020 (published online on 25 March).

spending. Paraguay, for example, announced a package of health measures that entails expenditure equivalent to 2.7% of its GDP. Chile, El Salvador, and Peru also announced similar packages with approximate costs of 0.65%, 0.27%, and 0.25% of their respective GDP.[11]

1.7 Consistent with this international experience, the Dominican Republic adopted prompt and urgent measures to address the pandemic, including the following:

a. **Declaration of a national state of emergency (Congressional Resolution 62-20 and Executive Decree 134-20).** On 19 March, the Dominican Congress authorized the President to declare a state of emergency for an initial period of 25 days,[12] allowing for: (i) restrictions on freedom of movement, association, and assembly to prevent gatherings that might lead to further spread of COVID-19; (ii) measures to ensure that public health facilities have the means to prevent and treat all types of disease; and (iii) measures to support various sectors of the Dominican economy during the emergency, as a way of saving jobs and protecting workers' income.

b. **Restrictions on movement.** To help prevent the spread of COVID-19, the government took measures to restrict people's movement. Decree 135-20, as amended,[13] ordered a curfew and barred people from moving about during certain hours, except for those engaged in key sectors such as health care, food, security, and electricity. This measure took effect throughout the country for an initial period of 15 days.[14]

c. **Economic response and relief plan.** The national government is taking steps to mitigate the negative impact of the pandemic, including: (i) the "Quédate en Casa" [Stay Home] program, which provides cash transfers to households identified as poor or in which at least one resident is deemed vulnerable to the pandemic; (ii) the Employee Solidarity Assistance Fund (FASE), which provides temporary cash transfers to laid-off workers; (iii) distribution of raw and cooked foods through the Social Affairs Commission, comprised of entities that run government social programs and representatives of churches; (iv) arrangements to help taxpayers stay in compliance, such as extending deadlines for filing tax returns and paying certain taxes, authorizing interest-free payment plans, bringing taxpayers with past-due tax bills back into compliance without charging fines; and (v) adoption of monetary and financial measures by the Central Bank of the Dominican Republic (BCRD) and the Monetary Board to provide liquidity to intermediary financial institutions to maintain favorable monetary conditions and boost lending to the country's productive sector, particularly to micro, small, and medium-sized enterprises and Dominican households.

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11 IDB Fiscal Management Division (FMM) (2020). FMM Technical Note: Fiscal Measures to Reduce the Impact of COVID-19.

12 The executive branch issued this authorization through Decree 134-20. The state of emergency has been extended four times (via Congressional Resolutions 63-20, 64-20, 65-20, and 66-20 and Executive Decrees 148-20, 153-20, and 160-20 and 187-20) and is currently in force until 1 June 2020.

13 Decrees 138-20 and 142-20.

14 This measure has been extended four times (via Decrees 151-20, 154-20, 161-20, and 188-20) and is currently in force until 13 June 2020.

1.8 From a regional perspective, the Dominican Republic is among the hardest-hit countries in Central America and the Caribbean, with 17,752 confirmed cases as of 1 June 2020, despite moving promptly to impose social distancing measures and close borders.

1.9 **Financing of the emergency response.** The Dominican government is making great efforts to contain the impact of the pandemic. To finance pandemic response measures, the government plans to incur further public debt (see Table 2) in 2020. Given the difficulties in accessing international markets, the country is expected to seek additional resources from bilateral and multilateral development banks, to help it close the financing gap of US$2.5 billion to US$2.7 billion. Without assistance in the form of loans from multilateral agencies, the Dominican Republic may lack sufficient access to finance on affordable terms to meet its net international obligations, such as payments for imports or external debt redemptions, while maintaining prudent reserve buffers. The government has identified the sources of bilateral and multilateral financing identified in Table 2 in the stated amounts. Such financing would be channeled through unrestricted loans. The country has also secured US$650 million under a Rapid Financing Instrument (RFI) from the International Monetary Fund (IMF) (see paragraph 1.13), which is to be used to strengthen the international reserves of the BCRD and guarantee macroeconomic stability.

Table 2. Identified financing*

Source	Amount (US$ millions)	Status
World Bank (Cat DDO**)	150	Disbursed
Development Bank of Latin America (CAF)	300	In preparation
Agence Française de Développement (AFD)	220	In preparation
Central American Bank for Economic Integration (CABEI)	50 to 250	In preparation
Japan International Cooperation Agency (JICA)	100 to 200	In preparation
World Bank (PBP)	100	In preparation
IDB (SDL)	250	In preparation***
IDB (PBP)	250	In preparation
Total	**1,420 to 1,720**	

* The US$650 million under the IMF's RFI is not included because that financing will be allocated to increase the BCRD's international reserves and ensure macroeconomic stability.

** Catastrophe deferred drawdown option.

*** This operation is being processed separately from other, complementary programs now in preparation.

1.10 **Macroeconomic repercussions.** The pandemic will have a strong impact on the Dominican economy. In March, despite lockdowns since the second half of the month, economic activity fell 9.4% on a year-to-year basis.[15] The IMF's preliminary projections indicate that real GDP will fall -1% in 2020 (after growing 5.1% in 2019), while the current account deficit may widen to 5.2% of GDP in

[15] "La actividad económica registra un comportamiento neutral en el primer trimestre de 2020 ante COVID-19."

2020 (compared to 1.4% in 2019), which will exert heavy pressure on the exchange rate and on reserves at the BCRD.

1.11 The balance of payments will be hard hit by the decline in tourism and free zone activity, as well as reduced capital inflows, although the historic drop in oil prices slightly offsets some of these stressors. The impact of the COVID-19 shock on the balance of payments can be analyzed by comparing current projections of the balance of payments for this year to a benchmark projection in the absence of COVID-19. By this metric, the shock's impact on the balance of payments for 2020 could amount to 5.2% of GDP despite the relief provided by lower oil prices. The balance of payments shortfall is driven by a projected deterioration in the current account (US$3 billion) and in portfolio investment (US$1.3 billion). This shortfall will be partially bridged using international reserves.

1.12 **Fiscal impact.** The government will face additional fiscal pressures due to the nature of the crisis. As the economy decelerates and conditions deteriorate, it will be difficult for taxpayers to meet their obligations. Tax revenues and other public revenues will suffer. The IMF conservatively estimates that revenue may fall approximately 0.9% of GDP. The authorities will need to allocate more resources to health and social benefits, including by redirecting budget appropriations from other areas. The IMF also projects that expenditures may rise by 1.2% of GDP. Thus, the consolidated deficit of the public sector has been estimated at 6% of GDP in 2020 (some 2.3% of GDP higher than before the COVID-19 shock).

B. Program for Macroeconomic and Fiscal Sustainability

1.13 On 29 April 2020, the IMF approved the use of the Rapid Financing Instrument (RFI) for the Dominican Republic in an amount equivalent to US$650 million, or 100% of its quota in special drawing rights (SDR). The RFI provides, rapid, low-access financial assistance to member countries facing an urgent balance of payments need, without the need to have a full-fledged program in place. A member country requesting RFI assistance is required to cooperate with the IMF to make efforts to solve its balance of payment difficulties and describe the general economic policies it proposes to follow. The RFI can provide support for a broad range of urgent needs, including those arising from commodity price shocks, natural disasters, conflict and postconflict situations, and emergencies resulting from fragility. Unlike other IMF instruments, the RFI does not require structural measures to be adopted in order to trigger the disbursement of funds. As part of the eligibility criteria, a member country requesting RFI assistance is required to make a set of commitments to confront the crisis and restore fiscal and financial sustainability, and these commitments are stated in a letter of intent that forms an integral part of the document (report) submitted to the IMF Executive Board for approval. According to the IMF's technical report issued at the time of approval, the rationale is based on an analysis of urgent balance of payments needs resulting from different types of emergencies, as well as a public debt sustainability analysis. If the debt is deemed to be unsustainable, the borrower should also undertake a commitment to adopt subsequent measures to

return the country to a path of fiscal sustainability.[16] The following IMF estimates support the approval of the RFI in the Dominican Republic:[17]

a. **Economic contraction.** GDP is projected to fall 1% in 2020, followed by a 4% recovery in 2021.

b. **Impact on balance of payments.** The current account deterioration due to contraction of external demand (declining exports and tourism) and reduced capital flows will result in a balance of payments shortfall equivalent to at least 5.4% of GDP in 2020.

c. **Fiscal impact.** The projected fiscal cost of the crisis response will result in a deterioration of the fiscal balance equivalent to about 2.3% of GDP in 2020, largely due to increased current public expenditure and tax receipts that will fall short of projections made at the start of the year, bringing the consolidated deficit to 6% of GDP.

1.14 **Measures to ensure fiscal sustainability and macroeconomic stability**. The government's commitment to implement measures in the medium term to restore fiscal discipline, ensure public debt sustainability, and maintain a stable balance of payments is contained in the Letter of Intent dated 13 April 2020. For fiscal sustainability, the main commitments stated in the Letter of Intent are to gradually tighten fiscal policies once the pandemic recedes to ensure that public debt-to-GDP ratios remain on a clear downward path; to strengthen public financial management; and to adhere to best practices in procuring and awarding contracts related to the pandemic. For macroeconomic stability, the main commitments are to avoid any measures or policies that would exacerbate balance of payments difficulties; to not impose new or intensify existing restrictions on the making of payments and transfers for current international transactions, trade restrictions for balance of payments purposes, or multiple currency practices; and to not enter into bilateral payment arrangements which are inconsistent with Article VIII of the IMF Articles of Agreement (see paragraphs 2.14 and 2.15).

1.15 **Findings of the IMF Staff Report for the RFI request.** In assessing the RFI request from the Dominican Republic, the IMF found as follows: (i) the COVID-19 pandemic is severely affecting the Dominican Republic, with a sharp decline in tourism revenue; (ii) the authorities have taken appropriate steps to temporarily widen the fiscal deficit to accommodate higher health care spending, along with other mitigation measures; (iii) the authorities agree on the need to carefully monitor the financial system and pursue macroprudential policies, to ensure the proper functioning of the financial system; (iv) the authorities are urged to allow greater exchange rate flexibility as a shock absorber and preserve the reserve cover; and (v) the authorities' request for assistance under the RFI in the amount of SDR477.4 million, equivalent to about US$650 million (100% of quota), is recommended for approval.

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[16] For further details on the IMF instrument, see the following link: RFI.

[17] All estimates in this section are based on the macroeconomic framework under the RFI.

II. ELIGIBILITY CRITERIA

2.1 **Eligibility criteria for SDL loan.** The Special Development Lending (SDL) category, established in the Proposal to Create a Special Development Lending Category (document AB-3134), approved by the Board of Governors on 30 June 2017 pursuant to Resolution AG-9/16, and its Special Development Lending Category Operational Guidelines (document GN-2031-17), is a budgetary support lending instrument for dealing with macroeconomic crises[18] and preserving social gains and economic growth in countries of the region facing a macroeconomic crisis. The Government of the Dominican Republic meets the eligibility criteria for this loan (document AB-3134), inasmuch as the Dominican Republic: (i) is experiencing a macroeconomic crisis (see paragraphs 1.10 to 1.15); and (ii) has a lending arrangement approved by the IMF, which has already been disbursed. The RFI arrangement was approved by the IMF on 29 April 2020 in the amount of US$650 million, equivalent to 100% of the country's quota in special drawing rights (SDR). The SDL operation amount (US$250 million) falls within the limit set by IDB policies: 2% of the country's GDP or a maximum of US$500 million.[19]

2.2 The IMF's Rapid Financing Instrument (RFI) is one of the eligible IMF instruments that can be accompanied by an SDL from the Bank[20] but does not include a policy matrix with actions to be completed prior to disbursement. In addition to the IMF analysis certifying the need for urgent balance of payments support, the RFI requires a Letter of Intent from the country describing the steps it commits to take in order to restore macroeconomic and fiscal stability. To ensure consistency with the IMF instrument, this program incorporates a Commitments Matrix that reflects the country commitments contained in the RFI Letter of Intent.

2.3 This program also contributes to the objective of the SDL instrument to protect social gains and economic growth. The proceeds of this operation, despite being for budgetary support and thus unrestricted, will directly finance measures to protect family incomes in the most vulnerable populations. The proceeds will also help finance economic relief measures for businesses, mitigating the impact on the business economy and job losses.

2.4 **The Bank's operational work and technical support in the country.** The Bank has supported the strengthening of public finances in the Dominican Republic for many years. Currently, investment loan 4114/OC-DR is aimed at consolidating the managerial capacity of the tax administration to reduce tax noncompliance and increase receipts, as well as strengthening government budget planning and management; technical cooperation (TC) operation ATN/OC-16547-DR is helping to build capacity at the Ministry of Finance to

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18 Defined as a situation in which the country lacks or potentially lacks sufficient financing on affordable terms to meet its net international obligations, such as payments for imports or external debt redemptions, while maintaining prudential reserve buffers (document GN-2031-17).

19 Whichever amount is less. This limit applies to new country funds (see paragraph 4.6 of document AB-3134).

20 See document GN-2031-17, paragraph 3.1.

monitor and evaluate tax policy and lay the groundwork for the medium-term fiscal framework; and the TC operations ATN/KR-17905-DR, ATN/KR-16875-RG, ATN/KR-16172-RG, and ATN/KR-16851-RG are helping to develop capacities in tax administration, design and implementation of public investment, regulation and management of public-private partnerships, and oversight of State-owned enterprises. In recent years, the Bank has supported tax policy reform and public spending control measures through loan 3110/OC-DR and provided technical assistance for staff management systems (operation ATN/FI-14511-DR) and procurement systems (operations ATN/ME-13937-DR, ATN/OC-16326-RG, and ATN/OC-17036-RG). Important lessons have been learned from this operational and knowledge-related work. The most significant such lesson in designing this operation is that technical assistance and ongoing dialogue with the authorities and with other development cooperation partners supporting the country's efforts to strengthen public finance management go a long way toward forging a shared medium-term vision and consensus on the necessary reforms to reach this goal.

2.5 **The Bank's experience in the region and lessons learned.** The Bank has experience assisting the countries of the region in overcoming macroeconomic crises and fiscal imbalances similar to those faced by the Dominican Republic. For example, the SDL approved for the Government of Barbados (loan 4656/OC-BA) supported: (i) the restoration of macroeconomic stability; (ii) fiscal adjustments to promote sustainable fiscal balance in the short and medium term; and (iii) protection of social spending to preserve social gains. The SDL approved for Ecuador (loan 4771/OC-EC) supported: (i) macroeconomic stability; (ii) the restoration of fiscal sustainability; (iii) strengthening of the central bank's institutional structure; and (iv) safeguarding of social spending to support the most vulnerable population. Both operations were approved in conjunction with IMF macrofiscal support. In 2014, moreover, the Bank approved the Development Sustainability Contingent Credit Line in Ecuador (loan 3415/OC-EC), which offered liquidity to withstand the external shock caused by the oil price drop.

2.6 The many lessons learned from this experience include the following: (i) the Bank's SDL instrument is an effective vehicle for channeling budgetary support resources swiftly in crisis situations; (ii) its main value-added, other than financial, is that it leverages and strengthens the IMF program and adds a layer of technical support to help the government meet its agreed commitments; and (iii) TC assistance and ongoing dialogue with the authorities to support fulfillment of the commitments with the IMF play an important role. These lessons confirm the appropriateness of the SDL instrument in view of the situation and challenges to which the Dominican Republic is responding, as well as the importance of supplementing it with the operational work under way or in preparation (see paragraphs 2.8 and 2.9).

2.7 **Coordination with other donors.** Since the SDL instrument requires that an IMF program is approved and is being or has been disbursed, ongoing coordination with the IMF was necessary to prepare this operation. The Bank is also actively coordinating with other donors supporting the country during the COVID-19 emergency, including the Agence Française de Développement (AFD), the Japan International Cooperation Agency (JICA), the Central American

Bank for Economic Integration (CABEI), and the World Bank (see paragraph 1.9).[21]

2.8 **Complementarity with other Bank operations.** In addition to this SDL, the Dominican government requested a policy-based loan from the Bank to make public policy and fiscal management more efficient and effective in responding to the health and economic crisis caused by COVID-19 by designing and implementing effective, fiscally responsible policy measures.

2.9 Loan operation 4114/OC-DR and TC operations ATN/OC-16547-DR, ATN/KR-17905-DR, ATN/KR-16875-RG, ATN/KR-16172-RG, and ATN/KR-16851-RG (see paragraph 2.4), now in execution, will contribute in multiple ways to the country's fulfillment of the commitments in its RFI Letter of Intent. The Bank is also preparing a set of regional TC operations to assist countries in the post-pandemic economic and fiscal recovery. These TCs, each with a subregional focus, will help member countries leverage each other's solutions and will offer specific technical assistance to strengthen fiscal and institutional management.[22] Moreover, like the loan operation and TCs now in execution, they will support the implementation of the commitments underpinning this operation and the fulfillment of medium-term measures included in the policy matrix of the programmatic policy-based loan requested by the country (see paragraph 2.8).

2.10 **Strategic alignment.** The program is consistent with the Update to the Institutional Strategy (document AB-3190-2) and aligned with the crosscutting area of institutional capacity and rule of law through reduction of the fiscal deficit to achieve public debt sustainability. The program will also contribute to the Corporate Results Framework 2020-2023 (document GN-2727-12) through the indicator, "countries with strengthened tax and expenditure policy and management." It is aligned with the public sector management and financing and macrofiscal management areas of the Sector Strategy: Institutions for Growth and Social Welfare (document GN-2587-2), and is consistent with the Fiscal Policy and Management Sector Framework Document (document GN-2831-9), which emphasizes the importance of institution-strengthening to improve the quality of public expenditure, as well as fiscal equity and social inclusion. This program is aligned with the IDB Country Strategy with the Dominican Republic 2017-2020 (document GN-2908) in the priority area of improving the management of public finances, institution-strengthening, and transparency, and in the strategic objectives of increasing the efficiency of the tax system and increasing the efficiency and transparency of public spending.

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[21] During the program, efforts will be coordinated with multilateral institutions and donors through ad hoc coordination roundtables and senior management meetings. The Bank will share its progress in program implementation with the IMF and the other donors.

[22] These regional TCs will provide technical assistance to: (i) identify and structure, in a nimble way, the most effective measures for helping to restore the fiscal position and rebuild economic activity in the post-pandemic period in view of the specific circumstances of each beneficiary country; (ii) strengthen countries' capacity to operationalize such measures; and (iii) strengthen the capacity of government entities designated by the countries to execute such measures and support them over time.

A. Objectives, components, and cost

2.11 **Program objective.** The general objective of the program is to contribute to strengthening the fiscal and economic policies underpinning the Dominican government's response to the COVID-19 pandemic, with a view to ensuring fiscal sustainability and macroeconomic stability. The specific objectives are: (i) to restore fiscal discipline to achieve public debt sustainability; and (ii) to maintain a stable balance of payments.

2.12 The program's objectives and components are aligned with the IMF's Rapid Financing Instrument (RFI), approved on 29 April 2020. The budgetary support provided through this loan under the Special Development Lending (SDL) category will contribute to finance efforts to contain the health crisis, mitigate its impact on vulnerable households, and promote countercyclical policies to reduce its effect on the economy in the short term. The program is structured as a single operation to be disbursed in a single tranche.

2.13 In line with the IMF's RFI, the paragraphs below describe the specific commitments assumed by the Government of the Dominican Republic under the components of the proposed program, as reflected in the Policy Letter for this operation and the Letter of Intent to the IMF.

2.14 **Component 1: Restore fiscal discipline to achieve public debt sustainability.** The commitments are: (i) to gradually tighten fiscal policies once the pandemic recedes, to ensure that public debt-to-GDP ratios remain sustainable and on a clear downward path in the medium term; (ii) to strengthen public financial management to ensure effective oversight over the entire public sector, including State-owned enterprises; and (iii) to adhere to best practices in procuring and awarding contracts related to the pandemic as well as publishing an externally audited report on virus-related expenditures once the crisis is over.

2.15 **Component 2: Maintain a stable balance of payments.** The commitments are: (i) to ensure macroeconomic stability and avoid any measures or policies that would exacerbate balance of payments difficulties; (ii) to not impose new or intensify existing restrictions on the making of payments and transfers for current international transactions, trade restrictions for balance of payments purposes, or multiple currency practices; and (iii) to not enter into bilateral payment arrangements that are inconsistent with Article VIII of the IMF Articles of Agreement.[23]

B. Key results indicators and program beneficiaries

2.16 The expected impact is to contribute to macroeconomic stability and fiscal sustainability, as reflected in an increase in the GDP growth rate from the projected -1.0% growth for this year to 5.0% in 2025, and in a reduction of the public debt of the nonfinancial public sector (NFPS) from the projected 50.3% of GDP for this year to 45.2% of GDP in 2025. The main expected outcomes are: (i) the NFPS primary fiscal balance will improve by 2.3 percentage points of GDP between 2020 and 2024; (ii) 100% of the entities making COVID-19-related purchases via emergency procurement procedures will submit detailed reports

[23] Article VIII: General Obligations of Members.

on such purchases to the Office of the Comptroller General; (iii) that subsidies to State-owned enterprises will not exceed 0.6% of GDP in 2024; and (iv) that the current account deficit of the balance of payments will decline by 2.3 percentage points of GDP between 2020 and 2024.

2.17 The program will benefit:

a. the Government of the Dominican Republic, by: (i) securing fast-disbursing resources to finance actions for the pandemic response and economic recovery; and (ii) creating a medium-term fiscal policy strategic framework for restoring fiscal sustainability.

b. the general public, by financing income-protection programs for families and businesses and, in the medium term, actions to maintain macroeconomic stability.

III. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instruments

3.1 This Special Development Lending (SDL) loan will be financed with the Bank's Ordinary Capital resources. However, it is not part of the Bank's regular lending program approved in the Long-term Financial Plan, so use of the Bank's enhanced lending capacity is proposed for financing this SDL. The operation has been prepared in coordination with the Rapid Financing Instrument (RFI) approved by the International Monetary Fund (IMF). The single-tranche structure and complementary financing arrangements with the IMF provide a flexible and effective mechanism for supporting the government's emergency measures to mitigate the health and economic impacts of the pandemic. The SDL resources will be disbursed to the government in a single tranche into the bank account designated for such purpose by the Ministry of Finance.

3.2 The amount of this program is US$250 million, in addition to the US$650 million to be disbursed under the RFI in 2020, bringing the total to US$900 million. The following factors were taken into account to determine the loan amount: (i) the size of the package of macroeconomic adjustment measures needed to address the macroeconomic crisis; (ii) the US$650 million available from the IMF; and (iii) the fiscal and balance of payment shortfalls, the country's debt sustainability, and risk factors (see paragraph 3.3 of the SDL guidelines (document GN-2031-17)). The program will help cover the additional financing needed by the country as a result of the pandemic, currently estimated at between US$2.5 billion and US$2.7 billion for the remainder of 2020, by providing US$250 million.

B. Environmental and social safeguard risks

3.3 Under Directive B.13 of the IDB's Environment and Safeguards Compliance Policy (Operational Policy OP-703), no ex ante impact classification is required for this program. The operation supports the development of policies, regulations, management instruments, and other institutional strengthening actions, so no significant direct impacts on the environment or natural resources are foreseen.

C. Fiduciary risks

3.4 No fiduciary risks have been identified for this program. The loan proceeds will be disbursed directly to the account designated by the Ministry of Finance and used to cover financing needs. The executing agency has the necessary financial management instruments and control systems for such purpose.

D. Other key risks and issues

3.5 **Macroeconomic and fiscal sustainability (high).** This operation is being prepared before the COVID-19 pandemic begins to abate, and there is no certainty as to how long the state of emergency will last. If the pandemic lingers and the economic recovery takes longer than expected, the impact of the crisis on public finances could be much stronger than anticipated. If this scenario materializes, the Bank will offer technical assistance through its regional pandemic response TC operations (see paragraph 2.9), to identify additional measures for restoring fiscal sustainability while protecting the most vulnerable populations.

3.6 **Public management and governance (high).** Any shift in political priorities as a result of the August 2020 presidential and legislative elections and/or post-pandemic social demands could jeopardize the implementation of policies to restore fiscal balance and macroeconomic stability. This risk will be partially mitigated with technical assistance from the Bank through its regional pandemic response TC operations (see paragraph 2.9) in priority areas for the fiscal adjustment and improvement of public expenditure. More generally, the ongoing dialogue between the Bank and the government, both in the transition period and after the new authorities take office, is expected to help the country meet its macroeconomic commitments for 2021 and beyond.

IV. Implementation and Management Plan

A. Summary of implementation arrangements

4.1 **Borrower and executing agency.** The borrower will be the Dominican Republic. The executing agency will the Ministry of Finance, which will be responsible for: (i) providing evidence that the commitments for disbursement of the loan, as agreed between the government and the Bank, have been met; (ii) promoting measures to achieve the program objectives; and (iii) compiling, maintaining, and providing to the Bank the necessary information, indicators, and parameters for monitoring and evaluation of the program outcomes.

4.2 **Commitments and disbursement of the loan proceeds. The sole disbursement of the loan proceeds will be made in accordance with the terms established in the Loan Contract to be signed between the borrower and the Bank, including the provision requiring that proceeds under the RFI financing arrangement approved by the IMF are being or have been disbursed. The Commitments Matrix (Annex II) identifies the commitments made by the Government of the Dominican Republic and contained in its Letter of Intent to the IMF, dated 13 April 2020, which forms an integral part of the IMF report, Request for Purchase Under the Rapid Financing Instrument, approved by the IMF Executive Board. These commitments are**

also identified in the Policy Letter sent by the Government of the Dominican Republic to the Bank on 10 June 2020 and will be reflected in the abovementioned Loan Contract.

B. Summary of arrangements for monitoring results

4.3 **Monitoring.** The borrower and the Bank will meet regularly to monitor the commitments described in the Commitments Matrix. The Bank will also maintain regular contact with the IMF mission to the Dominican Republic and take note of any IMF decision related to the RFI and any potential new arrangement with the country. The executing agency will compile and process all data necessary for program monitoring and evaluation. Consulting engagements to verify Results Matrix indicators and Commitments Matrix activities will be financed with IDB administrative funds.

4.4 **Evaluation.** After the close of fiscal year 2024, when the medium-term commitments reflected in the Results Matrix have concluded, the Bank will prepare an evaluation of the agreed indicators and respective targets for this operation, as input for an assessment of the SDL instrument's overall effectiveness.

4.5 **Policy Letter**. The Policy Letter of the Government of the Dominican Republic, reaffirming its commitment to the macroeconomic measures agreed upon with the Bank, is aligned with the program's Commitments Matrix and Results Matrix.

RESULTS MATRIX

Objective: The general objective of the program is to contribute to strengthening the fiscal and economic policies underpinning the response of the Government of the Dominican Republic to the COVID-19 pandemic, with a view to ensuring fiscal sustainability and macroeconomic stability. The specific objectives are: (i) to restore fiscal discipline to achieve public debt sustainability; and (ii) to maintain a stable balance of payments.

EXPECTED IMPACT

Indicators	Unit	Baseline 2020[1]	2022	2024	Target 2025	Means of verification
General objective: Ensure macroeconomic stability and fiscal sustainability						
GDP growth	%	-1.0	5.0	5.0	5.0	IMF report
Public debt of the nonfinancial public sector as % of GDP	%	50.3	47.3	45.9	45.2	IMF reports

EXPECTED OUTCOMES

Indicators	Unit	Baseline 2020[1]	2021	2022	2023	Target 2024	Means of verification
Specific objective 1: Restore fiscal discipline to achieve public debt sustainability							
Primary fiscal balance of the nonfinancial public sector as % of GDP	%	-1.7	0	0.1	0.2	0.6	IMF report
Subsidies to State-owned enterprises as % of GDP	%	0.6[2]	0.6	0.6	0.6	0.6	IMF report
Entities making COVID-19-related purchases via emergency procurement procedures that submit detailed reports to the Office of the Comptroller General	%	0.0 (2019)	0	0	0	100.0 (2020)[3]	Office of the Comptroller General

[1] The baseline is the end-2020 projection listed in the IMF's Staff Report for the Dominican Republic's RFI request. For evaluation purposes, this figure will be updated once final, official data are available.

[2] The 2020 projection for this indicator is well below the values posted for this indicator between 2015 and 2019 (0.6% to 1.0% of GDP).

[3] This target has been set for 2020 but not for 2024, since the commitment deals with procurement processes specifically related to the COVID-19 pandemic.

Indicators	Unit	Baseline 2020[1]	2021	2022	2023	Target 2024	Means of verification
Specific objective 2: Maintain a stable balance of payments							
Current account balance of the balance of payments as % of GDP	%	-5.2	-3.7	-3.4	-3.1	-2.9	IMF report

COMMITMENTS MATRIX

Objective: The general objective of the program is to contribute to strengthening the fiscal and economic policies underpinning the response of the Government of the Dominican Republic to the COVID-19 pandemic, with a view to ensuring fiscal sustainability and macroeconomic stability. The specific objectives are: (i) to restore fiscal discipline to achieve public debt sustainability; and (ii) to maintain a stable balance of payments.

Action area objectives	Commitments[1]
Restore fiscal discipline to achieve public debt sustainability	I. Gradually tighten fiscal policies once the pandemic recedes, to ensure that public debt-to-GDP ratios remain sustainable and on a clear downward path in the medium term.
	II. Strengthen public financial management to ensure effective oversight over the entire public sector, including State-owned enterprises.
	III. Adhere to best practices in procuring and awarding contracts related to the pandemic as well as publishing an externally audited report on virus-related expenditures once the crisis is over.
Maintain a stable balance of payments	I. Ensure macroeconomic stability and avoid any measures or policies that would exacerbate balance of payments difficulties.
	II. Not impose new or intensify existing restrictions on the making of payments and transfers for current international transactions, trade restrictions for balance of payments purposes, or multiple currency practices.
	III. Not enter into bilateral payment arrangements that are inconsistent with Article VIII of the IMF Articles of Agreement.

[1] This matrix identifies the commitments made by the Government of the Dominican Republic and contained in its Letter of Intent to the IMF, dated 13 April 2020, which forms an integral part of the IMF report, Request for Purchase Under the Rapid Financing Instrument, approved by the IMF Executive Board on 29 April 2020.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-___/20

Dominican Republic. Loan ____/OC-DR to the Dominican Republic
Emergency Program for Macroeconomic and Fiscal
Sustainability

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Dominican Republic, as Borrower, for the purpose of granting it a financing to cooperate in the execution of the Emergency Program for Macroeconomic and Fiscal Sustainability. Such financing will be for the amount of up to US$250,000,000 from the resources of the Bank's Ordinary Capital, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on __ ____________ 2020)

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