Inter-American Development Bank

Board of Executive Directors

For consideration

On or after: 29 June 2995

PR-2939
7 June 2005
Original: English

To:	The Board of Executive Directors
From:	The Secretary
Subject:	Regional. Loan proposal for Grenada reconstruction, recovery and development program

Basic Information:	Borrower	…………...........………………Caribbean Development Bank.
	Amount	......………………..…............……..….. up to US$10 million
	Source	………………………………….. Fund for Special Operations

Inquiries to: Mr. Hunt Howell (extension 2494)

Remarks: The proposed loan to the Caribbean Development Bank is in support of a disaster recovery operation for Grenada, a regional non-member country.

References: GN-1838-1(7/94), DR-398-5(5/03)

Other distribution: IDB Representatives

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

REGIONAL

GRENADA RECONSTRUCTION, RECOVERY, AND DEVELOPMENT PROGRAM

(RG-L1006)

LOAN PROPOSAL

This document was prepared by the project team consisting of: Hunt Howell (RE3/FI3) Project Team Leader; Felipe Morris (consultant), Jose M. Cabral (RE3/FI3); Marie Laurence Telson (COF/CBA); Kevin McTigue (LEGIII); Patricia Torres (RE3/SC3); Annette B. Killmer (RE3/EN3); and Rosario Gaggero (RE3/FI3) who was in charge of document production.

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Basic Socioeconomic Data	http://www.iadb.org/RES/index.cfm?fuseaction=externallinks.countrydata
Status of Loans in Execution & Loans Approved from IDB to CDB	http://portal.iadb.org/opsfilters/xmlToHtml.aspx?Output=HTML&AppName=EXECUTIONLOANS&Language=EN&Sort=&Link=Filter&Country=rg
Tentative Lending Program	http://opsgs1/ABSPRJ/tentativelending.ASP?S=RG&L=EN
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Annex II (CDB Intervention in Grenada)	http://idbdocs.iadb.org/wsdocs/getDocument.aspx?DOCNUM=536261
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ABBREVIATIONS

APEC	Audit and Post Evaluation Committee
ARD	Agency for Reconstruction and Development
BOD	Board of Directors
CABEI	Central American Bank for Economic Integration
CAF	Corporación Andina de Fomento
CARICOM	Caribbean Community
CDB	Caribbean Development Bank
CDERA	Caribbean Disaster Emergency Response Agency
CIDA	Canadian International Development Agency
DMFC	Disaster Mitigation Facility for the Caribbean
ECCB	Eastern Caribbean Central Bank
ECCU	Eastern Caribbean Currency Union
ECG	Evaluation Cooperation Group
EGR	Environmental Review Guidelines
EIA	Environmental Impact Assessment
EMP	Environmental Management Plans
EOC	Emergency Operations Centre
EOV	Evaluation Oversight Division
ERG	Environmental Review Guidelines
ESS	Environmental and Social Strategy
FSO	Fund for Special Operations
GDP	Gross Domestic Product
GOGR	Government of Grenada
IAU	Internal Audit Unit
IDB	Inter-American Development Bank
IFRS	International Financial Reporting Standard
IMF	International Monetary Fund
NDMSOG	Natural Disaster Management Strategy and Operational Guidelines
NEMS	National Environmental Management Strategy
NERO	National Emergency Relief Organization
NGOs	Non Governmental Organizations
NIS	National Insurance Scheme
OCR	Ordinary Capital Resources
OECS	Organization of Eastern Caribbean States
OSF	Other Special Funds
PCR	Project Completion Report
PPES	Project Performance Evaluation System
PPI	Project Implementation Performance Index
PPMS	Project Portfolio Management System
PSDOG	Private Sector Development and Operational Guidelines
PSDPOG	Private Sector Development Policies and Operational Guidelines
SDF	Special Development Fund
SFR	Special Funds Resources
UNDAC	United Nations Disaster Assessment and Coordination
UNDP	United Nations Development Program
USAID	United States Agency for International Development

PROJECT SUMMARY
REGIONAL
GRENADA RECONSTRUCTION, RECOVERY, AND DEVELOPMENT PROGRAM
(RG-L1006)

Financial Terms and Conditions				
Borrower: Caribbean Development Bank Guarantor: Executing Agency: Caribbean Development Bank			Amortization Period: Grace Period: Disbursement Period:	40 years 10 years 5 years
Source	**Amount**	**%**	Interest Rate:	1% First ten years 2% 11-40 years
IDB (FSO)	10 MM		Supervision and Inspection Fee:	Exemption
Local	1,1 MM			
Other/Cofinancing [1]			Credit Fee:	Exemption
Total	11.1 MM	100	Currency:	US$

Project at a Glance

Project objective: To provide IDB resources to CDB for socially and economically viable projects in Grenada to support its economic recovery and rehabilitation in the aftermath of Hurricane Ivan. Operations financed by the program will be selected and appraised with the policies and procedures of CDB that are consistent with IDB policies. The Operating Regulations agreed with CDB detail the eligibility criteria and requirements for access to the funds of this program and for measuring performance indicators.

Special contractual clauses: The adoption by CDB of the Operating Regulations of the Program. ¶3.29, ¶3.30

Exceptions to Bank policies: In order to provide FSO resources to Grenada at a cost that is not substantially more than the cost for Bank members and to coordinate the IDB and CDB's procurement policies, the following waivers to Bank policy are requested ¶3.31:

1. The Bank's inspection and supervision fee, as well as commitment fees.
2. Limiting of advance of funds to 10% of the loan amount (To allow for an advance of funds up to one-third of the loan amount.)
3. Country eligibility for procurement. (To include members of CDB that are not members of the IDB.)

Project consistent with Regional Strategy: Yes [X] No [ ]

Project qualifies for: SEQ[No] PTI [No] Sector [ ] Geographic[ ] Headcount [ ]

Verified by CESI on: April 22, 2005

Procurement: CDB has procurement policies and procedures similar to those of the Bank and is participating in the World Bank-led effort to harmonize procurement policies of multilateral development banks. The procurement procedures for the proposed operation will follow the model of the Global Credit Facility (Lo. 1108/SF-RG), currently in execution. ¶3.32, ¶3.33

[1] The CDB may provide parallel financing for some components of the operation ¶2.19

I. FRAME OF REFERENCE

A. Socioeconomic framework

1.1 Grenada is one of eight island states comprising the Eastern Caribbean Currency Union (ECCU), with its 104,000 citizens enjoying a pre-hurricane per capita income of about US$4,200. The country accounts for nearly 15% of the region's GDP. The common currency of the ECCU, the EC dollar, has been pegged to the U.S. dollar at the rate of EC$2.70 per US$1 since 1976.

1.2 Prior to Hurricane Ivan, the Government of Grenada (GOGR) was making progress to restore fiscal sustainability and spur growth. The primary fiscal balance registered a surplus in 2003—for the first time in nearly a decade—and was projected to remain in surplus in 2004. Real GDP was projected to grow by over 4 percent in 2004. This growth was expected to come from the performance of the agricultural sector, tourism, banking and insurance. The economic performance of Grenada before the hurricane was the best among OECS countries (Table 1).

Table 1
Economic and Social Indicators

	GDP Growth		**Inflation** (2004)	**Current Account (BOP)** (2003,% of GDP)	**Poverty Rate** (% of population)	**Human Development Indicator Rank** (2002)
	Avg. 1993-2003	Est. 2004				
Dominica	0.7%	2.6%	2.0%	-10.8%	39%	95
Grenada	**4.1%**	**-3.0%**	**2.5%**	**-29.3%**	**32.1%**	**93**
St. Lucia	1.2%	5.4%	3.5%	-16.6%	25.1%	71
St. Vincent & Grenadines	3.7%	5.0%	1.7%	-20.1%	37.5%	87

Source: International Financial Statistics, IMF; World Bank, UN Development Report 2003. Average HDI Rank for Latin American and Caribbean nations is 70 out of a total ranking of 177 countries.

1.3 These commendable efforts were set back by Hurricane Ivan. On September 7^{th}, 2004, the eye-wall of Hurricane Ivan passed over Grenada, bringing sustained winds of 120 miles per hour and gusts upwards of 135 miles per hour. The hurricane affected the entire island with a particularly severe impact in the southern portion of the island below a line drawn roughly from Grenville to St. George's. Visible damage included the partial or total loss of building structures, broken and uprooted trees, broken utility poles and damaged vehicles.

1.4 The productive base of the economy was destroyed by Hurricane Ivan. The critical tourism and agricultural sectors were virtually obliterated. Damage to the

island of Grenada is extensive and is estimated at 200% of GDP. Overall, in excess of 80% of building structures on the island have sustained some form of damage, including 90% of the housing stock and nearly every school in the country. Other sectors severely affected include: the power sector, with an estimated 80% of the distribution grid to be replaced; the tourism industry with close to 70% of its infrastructure made unusable; and the agriculture sector, which was significantly affected. Public infrastructure, in particular school and health clinic buildings, suffered major losses. Other government buildings, including the government complex, have suffered significant water damage. Small individual houses suffered greater damage proportionally than larger ones because the former tended to be lighter, single storey structures; also the smaller houses may not have been well designed nor constructed by skilled trades people in accordance with the Grenada Building Guidelines then in force[2]. Houses were vulnerable to the hurricane because of the poor location chosen, such as on exposed hillcrests and in open-ended valleys where they were more subject to the full force of the hurricane winds.[3] There is no information on the extent to which they were covered by insurance; however it is likely that lower income households were underinsured, if at all.

1.5 The economy contracted by 3 percent in 2004, and is only expected to expand by about 1 percent this year given the depressed level of activity in the two main sectors, tourism and agriculture. The loss of foreign exchange earnings from tourism and agricultural products is also anticipated to be high, about 6 percent of GDP. The National Insurance Scheme (NIS) estimates that about 8 percent of the labor force was displaced by the effects of the hurricane, though some may subsequently have been absorbed in employment in other sectors such as construction. Inflation remains subdued within the framework of the regional currency board arrangement—the annual inflation rate in December 2004 was 2.5 percent. Foreign assistance in reconstruction will help restore growth in 2006. Thereafter, growth is projected to return to a medium-term trajectory of about 4 ½ percent per year.

1.6 The IMF projects a financing gap of EC$56.9 million in 2005 (4.6% of GDP) even after very strong donor support—grants are expected to be EC$170.2 million (13.6% percent of GDP). Financing gaps in the years beyond 2005 are expected to be even larger, as reconstruction expenditures remain high and grant commitments beyond 2005 fall off sharply. Hence, even though revenues are expected to recover—helped by growth and a strong fiscal effort—and current expenditures are assumed to be controlled, the IMF estimates a financing gap of about 13.4 percent of GDP in 2006 and between 12 and 13percent per year through 2010.[4]

[2] As noted in Chapter IV Grenada's Parliament enacted a new building code in 2004
[3] Anthony Gibbs "Final Report on the Damage to Houses Less Than 2000 sq ft" October 2004
[4] IMF Article IV consultation mission to Grenada, May 12, 2005

1.7 The government has responded swiftly to these challenges. Nonessential budgetary expenditures have been streamlined and US$15 million (nearly 3 percent of GDP) of capital expenditures have been reoriented from existing projects to more pressing reconstruction and rehabilitation needs. The Customs' collection system, including physical infrastructure, which was heavily damaged, is being restored. Efforts are also being made to ensure that insurance claims are processed efficiently. Nonetheless, in December 2004 the country defaulted on certain commercial obligations and issued a statement asking its creditors for their cooperation to restructure its commercial debt. With this purpose in mind it hired a financial advisory firm (Bear & Stearns) to assist in this effort. CDB has provided concessional financing to assist GOGR in meeting its financial obligations to CDB to sustain an economic recovery program.

B. Bank policy and strategy for lending to Caribbean non-Bank member countries

1.8 The Bank's Charter gives the Bank the authority to finance the development of borrowing member countries of the Caribbean Development Bank, which are not members of the IDB by channeling loans and technical cooperation through CDB. During the Eighth Replenishment, it was agreed that FSO lending for these countries would be limited to those which are IDA-blend eligible due to their status as "small vulnerable island nations". These countries include Dominica, Grenada, St. Lucia, and St. Vincent and the Grenadines.

1.9 This mechanism has proven to be efficient for both the Bank and the beneficiary countries, as it provides significant levels of Bank resources for needed development efforts, with low administrative costs.

1.10 Bank policy (OP-601) for lending to sub-regional development financing institutions is based on meeting three principal eligibility criteria:

(1) **Compatibility,** which requires that the strategies and policies of the IDB and the sub-regional institution are consistent with each other.

(2) **Complementarity,** which requires that the sub-regional institution have the capacity to act more efficiently that the IDB in specific activities, and as such Bank support leads to more efficient support to the borrowing country.

(3) **Additionality,** which involves that the Bank's support of the regional institution, has a multiplier effect with regard to financial resource flows to the sub-regions.

1.11 In lending to sub-regional banks, IDB practice is to evaluate the policies and operating procedures of these institutions and if found consistent with those of IDB, program execution is delegated to the sub-regional borrowing bank. This is the case for this operation with CDB.

C. Eligibility of CDB as a borrower of bank resources

1.12 This operation meets all three eligibility criteria for lending to sub-regional banks. A review of CDB policies and operational practices found that they are compatible with those of the IDB and are based on essentially the same consistent principles detailed in their respective Charters. The results of this review are presented in more detail in Chapter 3 as part of the analysis of the Executing Agency. Moreover, there are few rules that conflict with each other, and those that do have been dealt with in this program's credit regulation or via a waiver, in the case of procurement policies.

1.13 This operation clearly meets the **complementarity** criteria, as the Bank cannot lend directly to non-member countries, such as Grenada, although the Bank Charter calls for the Bank to specially assist non-member Caribbean countries. CDB provides the instrument and mechanism for the Bank to fulfill this Charter mandate.

1.14 With regard to **additionality**, this operation has a multiplier effect for Grenada in several ways. First, the business reactivation operations funded by the loan would facilitate the recovery of important export-oriented sectors in the economy such as agriculture and tourism, restoring fiscal revenues and foreign exchange proceeds existing prior to the hurricane. These changes should not only result increased exports but would also help Grenada to obtain greater access to private sources of finance in the medium-term. Second, the program will also help Grenada make use of houses pledged by various country donors that otherwise could not be built due to lack of appropriate sites with services that would be funded by this loan.

D. Donor coordination and activities in support of reconstruction after the hurricane.

1.15 There has been a significant donor response and more coordination in Grenada after Hurricane Ivan than there has been with other natural disasters in the Caribbean. The donors conference held at the time of the World Bank & IMF Annual Meetings in October 2004, and the follow-up donors' conference held in Grenada in November were key events to help the country to receive pledges of support in excess of US$100 million. USAID is the largest donor with about US$42 million pledged for various interventions in housing, business reactivation and school rehabilitation. The World Bank has provided US$20 million, focused primarily on the education sector, rebuilding about 26 schools, and is also working with other donors in the health sector to help rebuild two hospitals and some clinics.

1.16 In the immediate aftermath of Hurricane Ivan, the National Emergency Relief Organization (NERO) put into effect the Emergency Operations Centre (EOC) through which all relief and response efforts were coordinated and channelled. These donor conferences were attended by all local and international partners involved in the ongoing relief efforts and took the form of reporting and

information sharing by all parties. The coordination of the relief effort among international donors and partners on the ground was carried out initially by the United Nations Disaster Assessment and Coordination Team (UNDAC), which arrived in the country shortly after the hurricane struck. The coordination role was taken over by UNDP with the departure of the UNDAC team and the establishment of a UNDP Liaison Office in Grenada.

1.17 After careful analysis, the Government concluded that the task of reconstruction and development would be so large and complex that it could not be effectively managed within the confines of the traditional ministerial structure and Public Service rules of operations. On November 18, 2004 the Government established the Agency for Reconstruction and Development (ARD) to coordinate the reconstruction work of Government ministries and agencies, external organizations and NGOs, and to work with and through them for the programs it manages directly. The Agency will also coordinate with the funding institutions to ensure proper accountability for the financial support provided. The ARD commenced operations with staff appointments in January 2005 and held the first meeting of its permanent Board in February 2005. Bilateral development agencies such as UNDP and CIDA have provided direct funding and technical assistance to help set up the Agency, which is now fully operative.

1.18 The ARD's main functions are to: (i) assist the Government to create an improved policy and institutional framework that will facilitate cost-effective reconstruction and development; (ii) mobilize additional resources to meet the continuing challenges of post-Ivan reconstruction and development; (iii) identify and prepare reconstruction and development projects, facilitate the management of the approval processes, implementing agency resources and management capacity; (iv) coordinate the reconstruction and development activities of stakeholders to ensure efficiency through the elimination of duplication and waste, and the selection of optimized implementation solutions; (v) collect and analyze data in order to monitor implementation, evaluate progress and report to Government, funding institutions and other stakeholders on the outcomes of funded activities; and (vi) maintain an up-to-date centralized information resource and ensure that stakeholders are kept informed about reconstruction and development program progress and issues.

1.19 It is expected that the ARD will play an important role in enhancing prioritization and planning within the ministries, facilitating coordination between donors, ensuring that the appropriate implementing agency is utilized, and monitoring the impact of the interventions. ARD staff has prepared a Strategic Plan, already approved by the Government of Grenada, which sets out the Agency's vision and strategies for collaboration, coordination and implementation, with particular emphasis on 2005. It highlights the priorities that have been set, provides an estimate of the resources the Agency will require, and describes the monitoring and reporting arrangements.

E. CDB activities in support of Grenada after the hurricane

1.20 Following the passage of Hurricane Ivan in Grenada, CDB approved immediate assistance in September 2004, amounting to US$620,000 under its Natural Disaster Management Strategy and Operational Guidelines (NDMSOG). This consisted of a grant of US$100,000 through the Caribbean Disaster Emergency Response Agency (CDERA) for emergency relief, a loan of US$500,000 to the Government of Grenada for cleaning and clearing of debris, restoration of public services including utilities. An associated grant of US$ 20,000 covered consultant fees for inspection of works and certification of disbursements.

1.21 In line with the NDMSOG, which provides that CDB, in consultation with the affected country, may reallocate available balances under loans already approved, the Board of Directors of CDB, at its October 2004 meeting, approved the reprogramming of approximately US$25 million in undisbursed credits from a number of operations, in accordance with new priorities to be agreed between CDB and the GOGR. This included US$2.7 million in grants under CDB's Basic Needs Trust program. The requirement for GOGR counterpart contribution for projects financed utilizing these redirected resources was also waived. In addition, a concessional loan of US$8.1 million from its Special Development Fund was provided to assist GOGR in meeting its fiscal obligations. CDB also applied to, and obtained from, IDB a grant of US$200,000 for relief assistance for the immediate repairs to housing and medical supplies to health clinics. The latter grant was executed through CDERA and was fully disbursed by CDB in March 2005. Thus, while there is no formal cofinancing from CDB for this program, it has already provided assistance to Grenada for disaster relief and recovery and is expected to continue doing so with its own resources.

F. Experience of the Bank in lending to the Caribbean Development Bank

1.22 The IDB has ample experience in working with CDB. The IDB has approved seven loans and 13 technical cooperation projects. As CDB's institutional capacity has strengthened and in keeping with the objectives of the Bank's policy for sub-regional institutions, which encourages the bank not to direct credit to specific operations, but rather to focus on the capabilities of the institution itself, the last operation approved in 2002 was a global credit program (Loan 1108/OC-RG). In this program, as in a previous one in 1996, resources were not allocated to predefined projects, but rather project eligibility criteria and guidelines were established in a credit agreement. CDB then was able to develop programs consistent with the country's development priorities and in line with CDB's strategy for the beneficiary countries.

1.23 The 1996 program consisted of two loans (975/SF-RG and 926/OC-RG) for a total of US$37 million. Ninety seven percent of the loan amounts had been disbursed as of end-2004 (the date of the most recent PPMR). Progress implementation has been classified as satisfactory. Two approved sub-loans are

still under implementation and as of September 2004 an extension of the period of disbursement to June 2006 was agreed between CDB and IDB.

1.24 The 2002 credit program consists of a loan of US$20 million and a technical cooperation grant in three phases (Phase 1, ATN/SF-8237-RG has already been signed and Phase 2, ATN/SF- 9019-RG is to be signed by June 2005). The loan has been fully committed, and disbursements stand at about 33% of the loan program and 100% of the first phase of the grant. CDB's Board has approved four sub-loans under the program and the contracts signed with the sub borrowers.[5] The projects financed total US$33.0 million of which US$12.3 million is to be supported with IDB resources. There are two remaining projects in the pipeline totalling US$9.75 million of which US$7.7 million is to be financed from IDB resources. The TC program (Phases 1 and 2) will fund six activities and three additional activities are contemplated under Phase 3 in 2005. CDB estimates that the loan and TC programs will be fully disbursed by 2009. The most recent PPMR on the program classifies it as satisfactory.

1.25 The effectiveness of the program cannot be evaluated yet, as none of the loan-funded projects has been completed. Nevertheless, the flexibility provided by the operation allowed CDB to support programs in different sectors that met the priorities of the various countries receiving funding. In this regard it should be noted that the bulk of the program's resources have so far gone to projects that improve social sector services. The importance of these sectors reflected CDB's strategy to expand the range of its operations, and to place greater emphasis on social services and poverty reduction.

G. Program strategy and justification

1.26 The Government of Grenada requested support from the IDB, through CDB[6], for longer-term support for recovery and reconstruction of the country's economic, social and environmental assets, including housing infrastructure and private sector credit. The program is justified by the extensive damage in Grenada's economy caused by Hurricane Ivan, one of the strongest storms ever in the Caribbean, which passed directly over the country. During donor coordination meetings it was agreed that since other donors were financing the immediate relief requirements and the temporary rehabilitation needs of Grenada, IDB could play a more significant role in the reconstruction stage. Thus this operation has been scheduled for approval after initial relief efforts have been undertaken.

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[5] The Economic Reconstruction Program – Rehabilitation of Primary Schools in Grenada (US$4.4 million), the Economic Reconstruction Program – Rehabilitation of Primary Schools and Health Clinics in St Lucia (US$6 million), the Disaster Mitigation project in St. Lucia (US$5 million) and the Basic Education II project in St. Vincent and the Grenadines (US$17.6 million).

[6] Letter of January 12, 2005 addressed from Mr. Compton Bourne, President of CDB to Mr. Bruce Juba, IDB Representative in Barbados.

II. The program

A. Objectives and description

2.1 The objective of this program is to provide an effective mechanism to support the economic recovery and reconstruction of Grenada in the aftermath of Hurricane Ivan that hit the island in September 2004. The funds of the Program will be available to CDB to finance investment projects in the private sector in the area of business revitalization and in the public sector in the areas of housing infrastructure for properties with clear land titles, and environmental and public infrastructure reconstruction. The activities to be financed with loan funds will be specific development projects that are technically, socially, economically, financially, and environmentally viable and sound. Within Operating Regulations agreed by the Bank and CDB, the latter will determine the composition and design of the specific projects to be financed.

2.2 The Bank's Charter authorizes it to promote the economic and social development of Caribbean countries that are not members of the Bank through the provision of loans and technical cooperation support to CDB. On the other hand, CDB´s strategy in the Caribbean region is to contribute to the harmonious economic growth and development of its borrowing member countries and to the systematic reduction of poverty by providing regular or concessional resources to finance projects and other development interventions. This Program clearly fits within the parameters of the strategies of both banks in the Caribbean Region by providing support to the reconstruction efforts of a country greatly affected by a natural disaster. Furthermore, as a loan supporting post-disaster recovery and reconstruction, this operation also falls within the Bank's and CDB's disaster risk management policy/strategy frameworks (including the application of best practices in reconstruction operations to avoid rebuilding vulnerabilities – see Chapter IV).

2.3 As established in the Operating Regulations agreed with CDB, funding to financial intermediaries will be possible with program resources. Resources would be on-lent to private sector enterprises affected by Hurricane Ivan in all economic sectors. CDB would ensure that these funds are provided, at market rates and conditions (see below), to borrowers affected by the Hurricane for the purpose of restoring their businesses (hotels, manufacturing plants, stores, or other economic activity). Funds will not be used for providing housing mortgage credit. Economic reactivation activities will be funded with resources from this program only if the corresponding sector policies, legal and institutional framework, and enforcement mechanisms are adequate as determined by CDB's guidelines.

2.4 The Government has determined that the following areas have priority: (i) human shelter; (ii) agriculture and reforestation, including watershed management; (iii) business sector reactivation; (iv) school rehabilitation; (v) social recovery,

including counselling; (vi) skills training; and (vii) sporting facility rehabilitation, including the national stadium.

2.5 Consistent with the original request and current thinking at CDB about the evolving circumstances in Grenada, and as noted above, the program will broadly support a series of sub-projects in Grenada in the following three component areas: (i) housing infrastructure (sites and services), (ii) business revitalization,[7] and (iii) environmental and public infrastructure reconstruction. CDB has identified potential sub-projects totalling almost US$40 million to which the government has assigned high priority; thus demand substantially exceeds the available program resources. An allocation between these and related sub-projects will be made according to the relative priority of each and its compliance with program requirements, including environmental safeguards as described in Chapter IV. Once determined eligible, the selection of projects will be done by CDB on a first-come-first-served basis. Following is a description of each component along with its associated parameters. A rough initial estimate of potential demand for program resources is also provided.

2.6 **Sites and services component.** With respect to sub-projects in the sites and services preparation component, specific eligibility criteria will be included to ensure that: (i) when the beneficiary takes possession, he or she will also have clear title to the property or a valid long-term leasehold contract on the land; (ii) the site is in a safe area[8]; (iii) the site complies with all relevant urban regulations (e.g. land use, zoning requirements, etc.); (iv) the site has access to primary transportation, water, and power networks; (v) the housing complies with appropriate building codes (see environmental safeguards discussion in Chapter IV); and (vi) an effective beneficiary selection mechanism is in place that targets vulnerable and low-income households. While demand is estimated to be considerably greater, an initial set of sub-projects totalling approximately US$3 million have been tentatively identified for this component.

2.7 **Business revitalization component.** A line of credit for business reactivation will be funded through this program, in which CDB will act as the second-tier financial institution and will only lend to eligible first-tier intermediaries willing to on-lend resources to businesses in Grenada. When it is activated it will be a multisectoral credit line open to all sectors of the economy for reconstruction and recovery activities. Only medium and long-term investments will be financed with this credit line[9]. Funds cannot be used for working capital financing. The size of individual operations with, and total CDB exposure to, each intermediary will be limited by CDB policy. (see para. 3.40) In addition single loans to final beneficiaries cannot exceed US$1 million. The wholesale lending rate of DB to first-tier financial institutions will be market-based, as determined by rates paid

[7] Including rehabilitation and restoration of tourist infrastructure especially at heritage sites frequented by cruise ships and a line of credit for refurbishment or rehabilitation of all type of business activities in the country, including the commercial and tourist sectors.
[8] i.e. construction will be limited to areas not prone to natural hazards (see ¶4.11iii)
[9] The CDB definition of medium term (4 – 7 years) and long term (8+ years) will be used.

on time deposits and term CDs. A more detailed specification will be contained in the overall credit regulations to be agreed between IDB and CDB prior to activation of the credit line. The retail lending rate to final sub-borrowers will be freely set by the first-tier institutions. The interest rate spread earned by CDB for this component, net of administration and risk costs, and all reflows from this loan net of debt service to IDB shall be utilized in accordance with any stipulations or policies of the Borrower regarding the use of its Other Special Funds

2.8 First-tier institutions will on-lend the resources according to terms agreed with CDB prior to implementation of the credit component. These terms will be consistent with the aforementioned credit regulations[10].

2.9 Financial institutions normally require all-risk cover insurance for real assets and inventory. Some even require key man insurance and they do take life insurance assignments. Credit risk insurance is not normal in Grenada; the risk is borne by the financial institutions directly.

2.10 CDB will be responsible for reviewing the condition of the first-tier financial institutions to determine their eligibility to participate in the program. Such review will be done in accordance with the Credit Regulations previously agreed with the Bank.

2.11 Grenada is a member of the Eastern Caribbean Currency Union (ECCU). The Eastern Caribbean Central Bank (ECCB) Act and the Uniform Banking Act provides a common set of financial legislation for financial institutions of all member countries. The uniform Banking Act recognizes the ECCB as the region's Central Bank with responsibility for the supervision of the financial system. The ultimate authority in the application of the Act is vested in the Minister of Finance of the respective member country. Licensed financial institutions are required to submit monthly, quarterly and annual returns to the ECCB that allows it to assess the performance of the financial system and to inform policy decisions. Grenada is in the process of passing the Uniform Banking Act.

2.12 Grenada's financial system consists of one state-owned development bank, 22 credit unions, 25 insurance companies or agencies, one national development foundation, one finance company, one building association and five commercial banks. The five commercial banks are the following: Bank of Nova Scotia, a branch of a non-regional bank; First Caribbean International Bank, a branch of a regional bank; RBTT Bank Grenada Ltd and National Commercial Bank of Grenada Ltd. which are locally incorporated subsidiaries of regional banks; and Grenada Cooperative Bank Ltd., a locally incorporated bank.

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[10] The Operating Regulations for the entire program as agreed during negotiations are annexed to the loan contract. They include the general eligibility and selection criteria for the three components of the program, including the credit line. The credit regulations, governing the credit line component will be consistent with these Operating Regulations.

2.13 Grenada has a very deep banking system, with total assets amounting to EC$1.2 billion (equivalent to 1.8 times its GDP). Prudential indicators are generally better than the ECCU average, with the ratio of non-performing assets to total loans being the lowest in the region (6.2% as of September 2004). Loan provisions amount to 67% of non performing loans (compared to 34.5% in ECCU countries). 59% of the loan portfolio of Grenada's banks is in personal loans, of which 84% is in housing loans. The remaining portfolio is relatively well diversified with allocations to commerce, manufacturing, tourism, entertainment, tourism, professional services and public utilities. Agriculture and fishing only account for about 1.5% of the total portfolio. Two-thirds of the loan portfolio has long-term maturities (over 5 years), largely explained by the housing loans, although other sectors of the economy also have access to long-term loans. A recent IMF report[11] concluded that the domestic banking system is highly liquid and stated that important progress has been made in recent years to strengthen the financial system. The ratio of liquid assets to total assets reached 34.4%, compared with 28.2% in all ECCU countries.

2.14 Reflecting the high liquidity of the banking system deposit rates are relatively low in Grenada (saving deposit rates range between 3% and 4% and time deposit rates fluctuate between 1% and 8%, depending on the maturity). The prime lending rate ranges between 8.5% and 9.5% and general lending rates go up to 15%. Rates for US$ denominated loans range between 7.5% and 9.5%.

2.15 CDB has extensive experience in lending to financial institutions, both public and privately owned. As of end-2003, CDB had 23 credits outstanding provided to financial institutions, of which nine were to private entities. CDB is aware that portfolio management of financial sector subprojects require constant supervision including the monitoring of the financial and operating performance of the institutions. Supervision reporting on the performance of each financial institution covers all aspects of the institution's operations and is usually done annually. Since this supervision is dependent on timely and efficient reporting by the financial institutions to CDB, the Credit Regulations will include the reporting requirements of the borrowing financial institutions, including the description of the monitoring indicators and financial ratios to be provided.

2.16 Initial estimates of demand for this component of the program are on the order of US$ 10 million.

2.17 **Environmental and public infrastructure reconstruction component.** This component will be financed with sub-loans directly to the GOGR and will be subject to the procurement and environmental provisions discussed in Chapters III and IV respectively. Sub-projects include control of land slips and related natural disaster management activities, primary bridge and road improvement, bridge replacement, and secondary road improvement. The funding will rectify damage

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[11] "Grenada Use of Fund Resources – Request for Emergency Assistance", Country Report No. 04/405, IMF, December 2004.

suffered during the hurricane and/or will rehabilitate infrastructure critical to the post hurricane economic recovery. Sub-projects initially identified for this component total roughly US$ 27 million. CDB will take into consideration government priorities in selecting eligible sub-projects.

B. Cost and financing

2.18 In response to CDB request of January 12, Bank management indicated a willingness to consider a loan of up to US$10 million for the program. Consistent with the Eighth Replenishment mandate, the Bank would provide these resources to CDB from the Fund for Special Operations (FSO) for on-lending in support of the reconstruction and economic reactivation efforts of the Government of Grenada.

2.19 Bank policy does not specify a counterpart requirement for lending to sub-regional financial institutions such as CDB, nonetheless CDB has been providing disaster relief and reconstruction assistance to Grenada and is likely to continue doing so with its own resources in parallel to this operation (see ¶1.20 - ¶1.21). At the sub-borrower level, Grenada's public finances and export revenues have been affected by the damage caused by Hurricane Ivan, resulting in financing constraints, which would argue for a reduced counterpart requirement if any. However given the reconstruction, as distinct from emergency, nature of the program, the Operating Regulations stipulate the same 10% counterpart contribution as CDB normally requires for loans to Grenada when funded with resources from its Special Development Fund (Unified). Thus the Government of Grenada will commit to providing US$1.1 million in counterpart funds and the total cost of the project would amount to US$11.1 million. This counterpart requirement could be met with contributions from other donors, GOGR own funds, and/or sub-borrowers.

Table 2
Total Cost and Sources of Financing
(US$ millions)

	IDB Contribution	Counterpart	Total
FSO Loan	10	1.1	11.1
Inspection and Supervision Fees	Not Applicable	Not Applicable	Not Applicable
TOTAL	10	1.1	11.1

III. PROGRAM EXECUTION

A. The borrower and executor

3.1 The Caribbean Development Bank will be the borrower and the executing agent of this program. CDB was founded in 1970 with the objective of contributing the economic growth and development of member countries in the Caribbean and to promoting economic cooperation and integration among them. The original members of CDB were the 16 Commonwealth Caribbean governments and two non-regional members, Canada and the UK. The membership of CDB is currently twenty-five; twenty regional and five non-regional members (Italy, Germany and the People's Republic of China joined the original two). Only Caribbean countries are borrowers (seventeen). The non-borrowing regional members are Colombia, Mexico, and Venezuela.

3.2 CDB can provide loans to both public and private sector entities in its borrowing member countries that contribute to the countries' social and economic development. CDB historically provided financing primarily for infrastructure projects. However, since the mid-1990s, CDB has expanded its lending to the social sectors, and more recently to support economic policy and institutional reforms. Lending to private entities remains limited, due to the higher risks of these projects and the requirement that the project have important and demonstrable development impact.

3.3 CDB is the most important source of multilateral credit to the OECS countries, comprising about 22% of their external credit and about 13.6% of Grenada's external credit. CDB provides both Ordinary Capital resources that are provided at rates linked to private financial market financing, as well as soft-term resources financed from contributions and low cost loans. OC and soft-term (Special Fund) resources can be blended to finance a specific project.

1. Financial Performance and Management

3.4 CDB has diverse funding sources that it uses to finance its activities, including Ordinary Capital Resources (OCR), Special Funds Resources (SFR) and Other Special Funds (OSF). CDB prepares separate financial statements for each of these Funds and does not have a consolidated financial report. OCR constitutes its largest Fund, and the basis for any financial analysis of CDB.

3.5 CDB's Charter requires that Special Fund resources be managed, accounted and disposed of separately from Ordinary Capital Resources (OCR). Some portion of the net income of Ordinary Capital Resources, however, may be appropriated to the Special Fund Resources (SFR). The SFR are in turn financed and managed from two separate funds. The largest is the Special Development Fund (SDF), financed primarily by contributions from members, that provides low-cost loans and grant technical cooperation. In addition, soft resources lent or contributed by individual donors or institutions to CDB for their management under specific

terms are consolidated and accounted for separately in Other Special Funds (OSF). The repayment of loans lent to OSF is supported by the net income of the consolidated OSF. The proceeds of IDB FSO loans are managed and accounted for in Other Special Funds. Nonetheless, the loan by IDB to CDB will constitute a general responsibility of CDB.

3.6 For the purpose of its lending operations, CDB classifies its borrowing member countries in various groups, depending on their respective economic situation. This classification is used to determine the cost of funds to borrowers and the tenor of the loans. Special Development Fund resources have an interest rate between 2% and 5% and maturities of between 10 and 30 years, depending on the level of development of the borrowing country. Grenada is classified in CDB Group 3, (the second lowest group in terms of level of development). It can borrow from the Special Development Fund at a rate of 2.5%, with a maximum maturity of 30 years, and a maximum grace period of 10 years. The minimum counterpart requirement is 10% of the project costs. The interest rate on loans financed from SDF includes a service charge of 1% per annum.

3.7 OC resources are raised from private market borrowing, lending from multilateral institutions, and returns on investment financed from capital subscriptions and past earnings. OC assets totaled about US$934 million at year-end 2004, of which 68% were loans to borrowing countries. Due to prudent financial management, CDB is currently rated AAA by Moody's and Standard & Poor's, and is able to borrow in the market at rates similar to that of the IDB. An indication of the increasing financial strength and capacity of CDB is that market borrowings are expanding and make up an increasing proportion of its OC funds liabilities, reaching over 95% by 2004.[12]

3.8 Loans from the OCR are repayable over varying periods depending on the grouping of the borrowing country, and the maximum period (inclusive of a five-year grace period) is 22 years for Groups 3 and 4 countries. The current interest on loans from the OCR to the public sector is 5.75% per annum. In the case of direct lending to the private sector, the current interest rate on loans approved is 7.75% per annum. A commitment fee of 1% per annum is levied on all undisbursed balances of loans funded from OCR.

3.9 Previously, the soft term funds financed the majority of CDB lending. However, over the past five years with the relatively rapid growth of CDB market borrowings, and the difficulty in obtaining new soft-term loans and contributions, soft-term lending now makes up about 40% of CDB lending, compared with 46%, in 2000. CDB operating expenses have declined over the past five years, however are in general are about twice as high as those of the IDB in terms of a percentage

[12] CDB manages its funds prudently given the limitations of its lending market and the need to minimize risks to its creditors. Reserves as a percent of outstanding loans are three to four times higher than most other multilateral development banks, and its interest coverage ratio about 80% greater, as its net income is about twice borrowing costs, and the returns on its paid-in-capital are about 2 percentage points higher.

of assets. These higher costs are due primarily to the much smaller average size of CDB operations relative to those of the IDB.

Table 3
Size, Growth and Distribution of CDB Funds
(US$ Millions, except as noted).

	Ordinary Capital		**Special Develop.**		**Oth. Special Fund**		**TOTAL**	
	2000	**2004**	**2000**	**2004**	**2000**	**2004**	**2000**	**2004**
Assets (Annual Growth)	546	934 (11.3%)	554	644 (3.1%)	156	194 (5.7%)	1256	1772 (7.1%)
Loans	379	637	282	360	41	64	702	1061
Liabilities	203	487	17	36	77	79	297	602
Capital/Equity	343	447	537	608	79	115	959	1170
Administrative Costs (% of Assets) *IDB*	5.8 (1.1%) 0.5%	7.2 (0.8%)	6.2 (1.7%) 0.6%	10.8 (1.7%)	2.3 (1.5%)	1.2 (0.6%)	17.7 (1.4%)	19.2 (1.1%)

Source: CDB Annual Reports, IDB Annual Report

3.10 Shareholder support to CDB is reflected by the capital backing secured from its members. As of year-end 2004, the subscribed capital of CDB was US$705 million, of which US$156 million had been paid and the remaining was callable. In addition, unlike most other sub-regional multilateral development finance institutions[13], CDB has a substantial portion of callable capital (US$137 million) from non-borrowing member countries rated AAA by Standard & Poor's.

3.11 Total Assets reached US$934 million at year-end 2004, of which loans amounted to US$637 million. Loans grew by 24% in 2004, reflecting strong demand from borrowing member countries. 96% of total loans were public sector loans guaranteed by borrowing member countries. There were no non-accruing loans at the end of 2004.

3.12 Since its inception, CDB has strived to achieve an appropriate balance between its development and banking roles and has succeeded in maintaining a strong financial position as evidenced by the AAA rating it has received from Moody´s and Standard & Poor's. CDB´s high rating results from careful financial management backed by a comprehensive set of conservative financial policies and operational procedures, coupled with the strong capital backing from its developed member countries, and preferred creditor status with borrowing member countries. The combination of adequate lending practices, controlled administrative expenses and careful financial management has allowed CDB to

[13] Such as CAF, CABEI, FLAR, etc.

obtain reasonable rates of return on earning assets. CDB's annual return on average assets has varied between 2% and 3% over the past five years, while annual return on average unadjusted shareholders equity ranged between 3.6% and 5.4%.

3.13 CDB's object is not to maximize profits, but to earn an adequate net income to ensure its financial strength and to maintain its development activities. CDB's net income dropped from US$27.1 million in 2002 to US$19.5 million in 2004 as a result of a combination of factors, including changes in the interest rate environment in the international financial markets which affected its financial margin and the introduction of accounting rule International Financial Reporting Standard (IFRS) 39 in 2003 that obliges CDB to treat certain hedging operations as derivatives held for trading with fair value gains and losses reported in income.[14] Nonetheless, in recent years net income has been sufficient to continuing building up the capital base of CDB through allocations to reserves and to support its development activities. An alternative measurement of performance is operating income, which shows a more stable performance in recent years (operating income was US$18.9 million in 2004 compared with US$20 million in 2003 and US$16 million in 2002).

2. Operational Policies and Procedures

3.14 **Country programming.** CDB has an integrated system for managing all phases of the project cycle. At the programming stage, Country Strategies are prepared for each of its borrowing member countries every two to three years. These Country Strategies are designed to ensure consistency between CDB's activities in its member countries with CDB's overall Strategic Objectives and Corporate Priorities, and with the countries' own development objectives and priorities. Once agreement is reached with national authorities on the country strategy, a country strategy paper, which includes an action plan with performance indicators, is submitted for review and approval by CDB's Board of Directors. The Country Strategies provide the framework within which all projects submitted for approval by the Board are to be developed.

3.15 Once a project has been included in CDB pipeline, a project team is formed to assist in its preparation and to appraise the project. Projects are appraised on the basis of their technical, commercial, and financial, social, economic, institutional and environmental viability. In addition, projects are appraised with regard to their contribution to the removal of economic bottlenecks, poverty reduction, external debt capacity of the country, the introduction of technologies to increase productivity and the expansion of employment opportunities. Preparation of a

[14] Prior to IFRS 39, derivatives were reported as off-balance sheet items at their fair value. Under IFRS 39, derivative instruments must be recorded on the balance sheet and stated at fair value, i.e. marked-to-market. CDB uses derivative instruments-mostly interest rate and currency swaps-as part of its asset and liability strategy in order to reduce risk and lower costs. However as a matter of operating policy, CDB does not trade the derivatives, holding them instead to maturity, thereby avoiding any trading losses over the life of these instruments.

logical framework matrix, similar to that used by IDB, is standard procedure at CDB for all projects and technical assistance activities with a total cost over $100,000.

3.16 .**Project monitoring.** Over the past three years CDB has implemented a *Project Performance Evaluation System (PPES)* that has greatly improved the bank's ability to monitor and evaluate the development effectiveness of its projects. The system uses best practices and the harmonized evaluation criteria adopted by the Evaluation Cooperation Group of the major MDBs.[15] The criteria are divided into categories reflecting all major aspects of project design and administration as follows:

a. <u>Project rationale</u>, including (i) strategic relevance and (ii) poverty relevance

b. <u>Outcomes</u>, including (i) efficacy, (ii) cost efficiency, (iii) institutional development, and (iv) sustainability;

c. <u>Summary of project performance</u> as a measure of overall project performance

d. <u>Institutional performance</u>, including (i) borrower and executing agency performance, and (ii) CDB performance

3.17 These criteria are used for decision making and monitoring at every stage of the project cycle, from appraisal through supervision to completion and evaluation with an emphasis on poverty reduction.

3.18 A computerized *Project Portfolio Management System (PPMS*), which incorporates the PPES, has been in operation since 2000. CDB staff has been trained in its use, and portfolio performance reviews have been completed for the 2000-2003 annual cycles, with the cycle for 2004 underway. This computerized system enables the Bank to organize in one place all information for each project throughout its entire life-cycle. The module for projects under implementation is fully operational and the recording of data for projects in the pipeline has recently been started. In each cycle the performance scores are entered into the PPMS, and those scores are used to calculate an average *Project Implementation Performance Index (PPI)* for the year. PPIs are computed for thematic groups of projects (sectors) and by country. Upon request the Bank will have access to these PPIs.

3.19 The Project Supervisor for each project prepares an annual Project Supervision Report in which the PPES performance scores are updated. Management reviews these reports and the performance scores, and the Evaluation and Oversight Division (see below) verifies a sample of them during the preparation of the Annual Portfolio Performance Review. The annual review also describes

[15] MDB Evaluation Cooperation Group (ECG), Harmonization of Evaluation Criteria among MDBs, December 1999.

the portfolio performance by country and by sector, which is an important contribution to CDB's ongoing country and sector strategies.

3.20 **Evaluation and oversight.** The Evaluation and Oversight Division (EOV) was created in 2003. It retained the ex-post evaluation function and added the responsibility for performance monitoring of all areas of Bank operations. The creation of this Division reflects the Bank's recognition of the importance of performance evaluation and oversight in the conduct of its operations. Regarding ex-post evaluations the EOV is responsible for the independent evaluation of projects, programs, and technical assistance financed by the Bank. In 2004, EOV prepared evaluation reports for the Board that assessed the development effectiveness of CDB's interventions utilizing the harmonized evaluation criteria. In 2005 a new policy and guidelines for ex-post evaluation incorporating the harmonized evaluation criteria will be prepared.

3.21 CDB has very stringent audit requirements and procedures. These audit procedures are deemed to be adequate. CDB has an Audit and Post Evaluation Committee (APEC) made up of four members of the Board of Directors (BOD) who are appointed by the BOD for a term of two years. The Committee is advisory in nature and its main function is to assist the BOD in discharging its oversight responsibility for the financial reporting process, the system of internal control, the internal and external audit functions and the project evaluation process.

3.22 The Internal Audit Unit (IAU) reports to the President and is accountable to the Audit and Post Evaluation Committee (APEC). The main objective of the internal audit function is to provide independent assurance regarding the adequacy, efficiency and effectiveness of control systems and processes and the Bank's compliance with regulations as stipulated by the Bank's Charter and relevant decision-making groups. This is achieved by conducting audits and making recommendations for improvements, as required.

3.23 The external auditors of the Bank are selected through a tendering process and appointed by the Board of Governors for a term of five years. The successful accounting firm must be in operation for a minimum of ten years, have an international infrastructure, operate under common policies and standards worldwide and have formal continuing education programs. No firm may serve for more than two consecutive terms but is eligible to express an interest after sitting out for one term. The process of selecting external auditors is under the oversight of APEC.

3.24 The role of the external auditors is to audit the financial statements of the Bank in accordance with International Standards on Auditing and to issue an audit opinion on financial statements accordingly.[16] The external auditors are also

[16] In the case of the OCR, audits are prepared in accordance with International Financial Reporting Standards.

required to support the Bank’s various note and/or bond offerings in the capital markets worldwide.

3.25 **Poverty Reduction, and Governance.** CDB's *Poverty Reduction Strategy* provides a broad framework for addressing the causes and characteristics of poverty in the Caribbean, and is consistent with the objectives of the Millennium Development Goals. Three broad priorities or 'strategic levers' are at the heart of the Bank's poverty reduction strategy: the enhancement of capabilities, the reduction of vulnerability, and good governance. It is important to note that the priorities are overlapping, and in some cases focus on different aspects of the same factors and programs.

3.26 The strategy also includes an integrated set of measures including the undertaking and updating of country poverty assessments as an essential knowledge base for policy and program and project design, support for the development of national poverty reduction strategy papers, preparation of country strategy papers for CDB's own operations, and the strengthening and use of social analysis as an essential underpinning for application of the poverty prism. Each of these elements of the strategy is part of a results-based action plan for the SDF 6 period, 2005-2008.

3.27 CDB has long recognized that sustainable human development requires governance structures and processes that are open, inclusive and facilitative. The institutional setting within which development activities are planned, implemented and managed is a critical element in the Region's quest for sustainable development and meaningful improvements in living standards. A comprehensive governance policy framework was endorsed by Contributors in the SDF 5 Agreement and subsequently elaborated in the Bank's Strategy on Governance and Institutional Development approved by the Board of Directors in December 2003.

3.28 Given its limitations in human and financial resources, CDB is unable to respond to every need identified within this framework and therefore it has established medium-term priorities. In setting priorities, CDB is guided by its comparative advantages and core competencies as well as its particular area of influence. These emphasize improving the capability of BMCs to design and implement appropriate policies, programs and projects to create the conditions for sustained pro-poor growth and development and expanding partnerships in order to optimize the benefits of resource flows to BMCs. Accordingly, the intervention strategy takes account of the activities of other donors in order to promote synergy and avoid duplication. The emphasis is on collaborative relationships with development partners – bilateral and multilateral agencies and inter-governmental organizations – in the design and implementation of good governance interventions. This operational approach reflects the international harmonization and alignment agenda among aid agencies.

B. Program execution and administration

3.29 The operation will be executed and administered by CDB and in turn CDB will implement its sub-projects through sub-executing agencies, including the respective Ministries and financial institutions (in the case of the credit line component). Operations financed by the program will be selected and appraised following the policies and procedures of CDB, which are consistent with the policies and objectives of the IDB. Details on the environmental safeguards are provided in Chapter IV. The Operating Regulations agreed with CDB specify the eligibility criteria and requirements for access to the funds of this program. In particular, these regulations limit the use of the funds to sub-projects in Grenada that support its economic recovery and rehabilitation and are socially and economically viable. In addition, the regulations also specify the types of operations and uses of funds that are prohibited by Bank policies. CDB will provide semi-annual progress reports, a mid-term evaluation and a final evaluation for each sub-project, in addition to a copy of its annual report on project implementation that provides general information on the sub-projects as requested. These reports will assist in IDB's ex-post monitoring of sub-project compliance with program objectives. ARD will also be expected to present harmonized or standardized performance reports to donors on projects funded with external resources that will be used by CDB to complement its own inspection visits and analysis.

3.30 Moreover, to ensure effective evaluation of the operations supported, the Operating Regulations of the program include specific reporting requirements to facilitate an evaluation of the effectiveness of the sub-projects and thereby the development effectiveness of the program itself (see ¶3.38).

3.31 **Exceptions to Bank policy.** In order to provide FSO resources to Grenada at a cost that is not substantially more than the cost for Bank members and to coordinate the IDB's and CDB's procurement policies, the following waivers to Bank policy are requested[17]:

i. The Bank's inspection and supervision fee, as well as commitment fees (so as not to impose both Bank and CDB fees on the sub-borrowers).

ii. Limiting of advance of funds to 10% of the loan amount (to allow for an advance of funds up to one-third of the loan amount that will permit CDB to meet the financial demands for sub-project execution -- see ¶3.35).

iii. Country eligibility for procurement (to include members of CDB that are not members of the IDB.)

[17] These waivers were requested and approved for Loan 1108/SF-RG to the CDB for the Regional Program "Global Credit for Small Caribbean States" (RG-0056).

C. Procurement of goods and services

3.32 CDB procurement policies and procedures are similar to those of the Bank, and CDB is participating in the World Bank-led effort to harmonize procurement policies of multilateral development banks. The Program will follow similar procurement procedures as the previous Global Credit Facility (LO-1108/SF-RG) that include a provision for IDB member countries to participate in international bidding on projects financed with IDB resources and other CDB financing[18]. All procurement above US$750,000 for works and US$1 million for goods and works together must be carried out by international competitive bidding, including announcements in Development Business, the local press and foreign embassies of eligible countries. Where the estimated costs of goods and works are below the aforementioned limits, procurement will follow CDB's guidelines, subject to the provisions of the following paragraph.

3.33 In order to both facilitate the administration of the program and to provide sub-executing agencies with uniform procedures in order to facilitate access to the program's resources, it is recommended that CDB's procurement procedures be used with the following provisions:

(i) Eligibility for procurement using the resources of the loan should be open only to IDB member countries and CDB member countries;

(ii) With the non-objection of the IDB, CDB may permit the use of loan resources to finance the execution by force account, including community self-help programs, up to US$2 million**;**

(iii) The IDB reserves the right to carry out, at any stage of the procurement process, ex-ante or ex-post review of the procedures being followed;

(iv) Sub-executing agencies may reject all bids, after consultation with CDB, if the lowest evaluated bid exceeds the estimate by an amount deemed by CDB to provide a reasonable justification. In such cases, with the approval of CDB, the executing agency may call for new bids from at least all who were invited to bid in the first instance.

D. Execution and disbursement schedule

3.34 Program resources would be committed over three years and disbursed to the final borrower in five years. This is considerably faster than the previous two programs, and reflects the special needs of the country and the nature of the operation: to support reconstruction and recovery after a natural disaster. Of course the ultimate pace of disbursement will depend on the effectiveness of the

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[18] CDB *Guidelines for Procurement,* paragraph 1.01(d)

sub-executing agencies in Grenada to prepare and present potential projects. CDB has requested use of up to US$500,000 in program resources for retroactive financing of expenditures incurred since the Hurricane on September 7, 2004 for the housing component, following CDB norms, which are fully consistent with those of the IDB.

3.35 To defray in part the administrative costs of the program, it is recommended that a waiver to the Bank's advance of fund policy be provided, such that the resources would be disbursed to CDB in three equal tranches. The funds pending disbursement to final sub-borrowers may be used for investment purposes according to CDB's applicable policies.

E. Monitoring and evaluation

3.36 A Logical Framework has been developed that will be the basis for monitoring progress under the program (see Annex I). This framework has been prepared taking into consideration CDB's suggestions and includes a set of indicators for the evaluation system. The Bank has also agreed with CDB on the mechanisms for a mid-term evaluation of the program that would allow the implementation of corrective actions if deemed necessary. This evaluation will consist of joint IDB/CDB reviews of the various sub-projects and an assessment of the effectiveness of the program as a whole.

3.37 The IDB country office in Barbados will supervise the execution of the Program. As noted earlier, CDB's PPES is a relatively advanced monitoring and evaluation system. CDB will make data from this system available to the Country Office, as well as semi-annual supervisory reports of the sub-projects financed with loan resources. These reports include an assessment of the sub-project's performance and the specification of remedial measures, when necessary. In addition, CDB will provide a copy of its annual report on the implementation of projects, which provides data on all CDB projects in execution. This report will allow the IDB to compare the performance of projects financed with the loan resources with other CDB loans by sector and by country. This information will be sufficient to indicate whether the project is meeting the execution goals in the logical framework. The Bank's Project Completion Report (PCR) will be based on CDB's own project completion exercise.

3.38 As indicated in Para 3.15, all projects financed by CDB have a logical framework that includes measurable result indicators to show whether the supported projects meet their development objectives. These indicators and development objectives will be reviewed periodically by CDB and IDB staff as part of the evaluation process. The PPES scores for each sub-project supported by the Program and an appropriately weighted average will be provided. CDB Appraisal Documents should include baseline data and define execution and project termination benchmarks for these performance indicators that are agreed with the borrower as part of the sub-loan agreements. These indicators, along with the information included in CDB's performance evaluation system, will allow for an evaluation of

the effectiveness of the operations supported by this loan and thereby the effectiveness of the Program itself.

F. Private Sector Development Policies and Operational Guidelines

3.39 CDB's private sector lending is regulated by its *Private Sector Development Policies and Operational Guidelines (PSDPOG)* of May 2003. CDB's strategic objective for private sector development in its borrowing member countries is to support initiatives aimed at improvement in the global competitiveness of the Region's productive sectors on a sustainable basis. CDB's private sector operations are also guided by the general principles of additionality, catalytic role for CDB and the establishment of partnerships and alliances with other financial institutions operating in the region (including multilaterals). Financing programs with private financial intermediaries are done in accordance with these general principles. CDB also establishes specific Financial Policies to guide the size of each intervention and exposure to individual financial institutions.

3.40 Implementation of CDB's p*rivate sector development policy* is effected through CDB's PSDPOG which includes a series of limits and ratios presented for guidance only and are subject to the requirements contained in CDB's *Financial Policies*, as are presently determined, and may be adjusted from time to time. Single financial intermediary operations are limited to US$5 million and cumulative loans outstanding to any financial institution cannot exceed US$10 million.

3.41 In its intermediary lending, the PSDPOG indicate that CDB is guided by its requirements of sound management, acceptable asset quality, prudent financial and operational policies and adequate capital structure. Financial institutions will also be required to adhere to prudential principles, generally accepted accounting principles and regulations accepted by the appropriate supervisory authority, where applicable. Resources from this Program will not be used to restructure debts.

IV. VIABILITY AND RISKS

A. Institutional viability

4.1 CDB continues to improve its operational effectiveness. As noted earlier, it has devoted considerable energy and resources to improve all stages of the program cycle. A more rigorous, comprehensive and open programming process has been implemented. With the implementation of the Project Performance Evaluation System, CDB is better able during the appraisal phase to predict project performance as well compare more objectively different programs. This system also helps to provide more effective supervision of programs during implementation. Finally, CDB has placed greater emphasis on evaluation, requiring baseline data for performance indicators, which allows for more accurate measurement of program results and effectiveness.

4.2 In addition to these operational modifications, CDB has taken measures to improve the effectiveness and efficiency of its human resources. These include a restructuring of its program areas. CDB has separated the staffing for program analysis and supervision, and previous sector divisions have been eliminated. Groups of projects have been placed under the management of a portfolio manager either for preparation or supervision. These changes have allowed a more efficient use of CDB human resources as well as making staff responsibilities more transparent

B. Socioeconomic viability

4.3 CDB usually requires as part of its appraisal the estimation of economic rates of return of its programs, as well as the definition of indicators to measure the improvement in access and quality of social services for social sector programs. In addition, all subprojects are evaluated during appraisal for their effectiveness and relevancy to reduce poverty as well as for their institutional development impact.

4.4 When economic rates of return cannot be estimated, CDB requires the estimation of the costs of at least three alternative technically feasible methods to achieve the project objective in order to assure that the subproject meets its development goals at the least cost. With this appraisal and evaluation process, CDB works to assure that subprojects they finance are socially and economically viable.

C. Financial viability

4.5 The proposed Program is small relative to the size of CDB, measured by capital, assets or liabilities. Therefore it is very unlikely that this operation could affect the financial viability of the borrower. Nonetheless it is expected that the financial returns from the loan should exceed operational costs.

D. Environmental impact

4.6 **Potential Impacts**. Given the nature of the Program, directed at financing through CDB the rehabilitation of public infrastructure and residential and business structures severely damaged by Hurricane Ivan, as well as environmental restoration, the anticipated environmental and social impacts will mainly be significantly positive. However, if adequate socio-environmental management and mitigation measures are not properly implemented, some project components could have potential moderate and minor negative impacts, and the housing project component could generate significant negative impacts.

4.7 Sub-projects related to business revitalization (reconstruction and repair of business establishments such as hotels, stores, offices, etc.), environmental restoration (cleaning up and stabilization of areas in which mass movements have occurred) and infrastructure rehabilitation (repair, restoration and maintenance of roads and bridges) are likely to generate only minor to moderate, limited, short-term, spatially-restricted and easily preventable and mitigable impacts during the execution of civil works.

4.8 On the other hand, the housing component, which involves the provision of lots with services to install prefabricated houses donated by third parties, is the only Program component with the potential to produce moderate to significant negative impacts, since eventual housing sites have not been identified. The potential negative impacts of this component include: the generation of dust, noise and gases due to use of construction equipment; traffic congestion; risk of on-the-job accidents and sickness for workers; soil erosion and landscape degradation resulting from earth movement; among others. As mentioned, other Program components could produce some of these impacts, but in lesser magnitudes.

4.9 **Environmental and Social Strategy (ESS).** The ESS designed by the Project Team to ensure the environmental and social sustainability of the Program consists of actions and measures in the following areas: (i) impact prevention and mitigation; and (ii) supervision and follow up. The details of the Strategy are elaborated in the Environmental and Social Annex.

4.10 **Impact Prevention and Mitigation.** The Program will use the environmental and social review and management procedures of the executing agency, the Caribbean Development Bank (CDB). CDB has developed adequate *Environmental Review Guidelines* and *Guidelines for the Social Analysis of Development Projects* in order to classify proposed projects based on their environmental and social impacts, and determine the corresponding breadth and depth of the socio-environmental analyses and impact management measures required. Both of these instruments are consistent with IDB's *Environmental and Safeguards Compliance Policy* currently under review. CDB will update its *Environmental Review Guidelines (ERG)* to formally and systematically integrate natural hazards impact assessment into its guidelines. CDB also routinely addresses natural hazard risk considerations as part of the environmental review process, but the revised ERG

will formally include a systematic procedure for natural hazard impact assessment in the environmental review process.

4.11 Based on the preliminary impact analysis a series of socio-environmental measures and studies will need to be implemented as described in detail in the Environmental and Social Annex and summarized as follows:

i. Regarding Business Revitalization, the reconstruction and repair of structures will be required to meet the design, material and construction standards contained in the National Building Code and Guidelines based on the Organization of Eastern Caribbean States (OECS) Building Codes and Guidelines, and formally enacted by Grenada in 2004. These Codes and Guidelines which include norms and criteria for natural hazard protection have been reviewed and considered appropriate by IDB, and thus will contribute to the avoidance of rebuilding vulnerability. In addition, building contractors or other executing entities[19] must obtain the construction permits required in Grenada before starting construction works and follow good practices in construction. CDB has agreed to include environmental and social criteria in the Credit Regulations of any credit line financed by this Program. These criteria will have to be followed by participating first-tier financial institutions and will require that their financing of projects complies with the Exclusion List (see sub-paragraph iii below).

ii. For Environmental Restoration, construction contractors or other executing entities will be required to meet technical environmental specifications agreed upon by CDB and the Bank, which will be incorporated into construction contracts. In addition, contractors must obtain the applicable permits, concessions or authorizations for the use of natural resources. In the case of Infrastructure Rehabilitation, Environmental Management Plans (EMP) will be required, in addition to the preceding requirements. The EMP will be part of bidding documents and construction contracts.

iii. The application of CDB's *Environmental Review Guidelines* and *Guidelines for the Social Analysis of Development Projects* to potential housing sites and services will determine the specific socio-environmental analyses required. The Bank and CDB staff has agreed on an Exclusion List for both site selection and building repair and reconstruction that will eliminate from consideration potential sites that are environmentally or socially sensitive or present high environmental risks, and thus it is anticipated that no Environmental Impact Assessments (EIA) will be required. The Exclusion List prohibits construction on sites located in the following: (i) environmentally sensitive areas (wetlands, primary forest, etc.); (ii) protected natural

[19] such as government agencies that carry out construction directly by force account.

ecosystems (national parks, wildlife refuges, etc.); (iii) locations prone to natural hazards (floods, geotechnically unstable, etc.); and (iv) sites requiring extensive earth movement (cut and fill) or significant intervention of vegetation or water bodies. The resulting EMPs, as well as technical environmental specifications to be defined for the Program, will be incorporated into bidding documents and construction contracts. Contractors or other executing entities must obtain required construction permits, as well as authorizations or permits for the use of natural resources. The prefabricated housing structures to be provided by other donors and installed in the selected sites must meet the standards set forth in the National Building Codes and Guidelines, in particular those related to natural hazard protection. Together with the exclusion list these codes and guidelines define the site selection, and will avoid rebuilding vulnerability. The Program will require that lot development and conditioning will only take place in sites where land property rights are clear and undisputed. CDB is in the process of evaluating the potential housing sites. Building code enforcement is an issue in Grenada and the Government has received assistance from the Organization of American States (OAS) to support the Planning Office in developing the capabilities to enforce the Building Code through updating the Physical Planning Act. OAS will provide materials, expertise and related training to build these capabilities.

4.12 **Supervision and Follow Up.** CDB will require that only competent, qualified and experienced engineering firms are engaged in the supervision of Program components with the potential to cause moderate to significant adverse impacts (i.e., infrastructure rehabilitation and housing sites). CDB policy is to publish in Development Business any requests for bidding proposals over US$100,000. For these components, CDB Environmental Specialists will determine the need for construction supervision firms to hire environmental consultants. Periodic environmental reporting by supervisory firms will be established. In addition, CDB staff will conduct periodic supervision missions during the construction phase of sub-projects likely to generate moderate to significant negative impacts.

4.13 **Legal and Institutional Framework for Environmental Management in Grenada.** The Environmental Impact Assessment process is governed by the Physical Planning and Development Control Act (2002). Section 25 of the Act makes provision for conducting EIAs. The institution with lead responsibility for EIA procedures is the Planning and Development Authority. This agency is empowered by law to require applicants to submit EIAs. At the same time that an EIA notice is issued to the applicant, the Authority must inform agencies and departments of government responsible for issuing licenses, permits, approvals, and other consents related to the proposed project. The Authority is prohibited from granting permission for the development of land for which an EIA has been requested unless it has first taken into account the EIA report. At the end of 2004, Grenada approved its first National Environmental Management Strategy

(NEMS). The country now has an institutional and legislative framework for integrating environmental management in its development agenda.

4.14 Even before the devastating impacts of Hurricane Ivan in Grenada, the Government demonstrated its commitment to develop and/or approve several critical instruments for environmental and natural hazard management. These include Parliament's enactment in 2004 of a National Building Code and Guidelines (based on the OECS code), the enactment of the Physical Planning and Development Control Act and the National Physical Development Plan, the endorsement of the Comprehensive Disaster Management Strategy and the adoption of a National Hazard Mitigation Policy and Strategic Framework (December 2004). The latter instrument, developed by CDB and the United Nations Development Program (UNDP) at the request of the Government of Grenada, provides for mainstreaming disaster risk reduction into the Post-Hurricane Ivan reconstruction process.

4.15 Although environmental management capacity is limited, the country has made progress in strengthening this capacity in recent years and continues to do so with support from CDB, CARICOM, and the UNDP through the OECS.

4.16 **Environmental and Social Management Capacity of Executing Agency.** CDB has separate procedures and instruments for the assessment and management of environmental and social impacts. For the analysis and management of environmental impacts, CDB uses the Environmental Review Guidelines, and for the review and management of social impacts, it applies the Guidelines for the Social Analysis of Development Projects. Taken together, these are consistent with IDB's Environmental Safeguards and Compliance Policy currently under review.

4.17 CDB´s environmental and social review functions are centralized in the Projects Department. Environmental and Social Project Officers are responsible for conducting, respectively, the environmental and social analysis of operations, including the review of documentation, visits to project sites, the preparation of required documentation, the contacts with project proponents, consultants, communities and NGOs, and the formulation of recommendations to Bank management on all environmental and social issues associated with operations, including loan conditionality. The supervision of the environmental and social components of projects is conducted by a separate unit of the Projects Department, with the support of Environmental and Social Project Officers and sometimes external consultants for projects likely to cause significant negative impacts. The ex-post analysis of these components is done by EOV.

E. Beneficiaries

4.18 The program will benefit Grenada by providing low-cost resources to implement socially and economically viable projects to support its economic recovery and rehabilitation. It is expected that the program will have a very strong and positive

impact in the population, particularly in the low-income segment that has been hard hit by the Hurricane, in many cases losing their jobs or revenue generating activities, and lack the means to recover their businesses or reconstruct their houses. Finally, the program ensures that strong relations are maintained between the IDB and CDB for mutual collaboration and support in the region.

F. Risks

4.19 **Credit Risk.** It is worth indicating that IDB and CDB face different types of credit risk under this program. The credit risk faced by IDB in this operation is different than those of other loans to Bank members because repayment depends on the ability of CDB, a multilateral agency currently rated AAA by Moody's and Standard & Poor's. It does not hinge on the repayment ability of a single country borrower. Given the expectation of continued prudent financial policies at CDB, these resources provide a strong level of support, to service the loan. On the other hand, CDB faces the typical country risk since all the funds will be on-lent to a single country, Grenada.[20] Furthermore Grenada has a relatively high debt burden and has experienced recent repayment problems on its commercial debt. Nonetheless, CDB officials have indicated that they are quite comfortable with the ability of Grenada to repay the loan.

4.20 **Implementation Risk.** The success of the program will hinge on the capacity of CDB and of the agencies of the Government of Grenada to carry it out. CDB will work through the appropriate Government agencies making sure that the GOGR has adequate capabilities, thus mitigating this risk. The recently created Agency for Reconstruction and Development (ARD) in Grenada should also help in this respect, as it is responsible for coordinating the reconstruction and development activities of the stakeholders. The Program does not provide financial support for strengthening the ARD, given that other donors are providing grant funding for this purpose.

4.21 **Environmental risk.** The risk associated with the limited enforcement capacity of the Planning and Development Authority is mitigated by CDB's independent oversight of the projects to be financed. In addition the Authority's enforcement capacity continues to be strengthened by international agencies including CDB, UNDP, and CARICOM.

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[20] With the exception of participation in the credit line component of financial institutions from Caribbean countries other than Grenada, in which case the credit risk is not concentrated exclusively in Grenada.

LOGICAL FRAMEWORK
GRENADA RECONSTRUCTION, RECOVERY AND DEVELOPMENT PROGRAM (RG-L1006)

	NARRATIVE	OBJECTIVE VERIFIABLE INDICATORS	MEANS OF VERIFICATION	ASSUMPTIONS
GOAL	Support economic reconstruction, recovery and development of the public and private sector in Grenada, in the aftermath of Hurricane Ivan.	- Subprojects financed by the CDB-managed program will, by the time they are completed (no later than five years after project initiation), have contributed to improved income and employment in Grenada. - Completed subprojects will prove to be technically, socially, economically, financially and environmentally viable and sound.	- CDB and Government of Grenada economic performance reports and Country Strategy Papers. - Reporting from CDB Project Performance Evaluation System scores, annual supervisory reports, project completion reports.	- Macroeconomic and political environment on Grenada conducive to economic growth. - No additional external shocks to the country.
PURPOSES	The program will achieve one or more of the following three purposes: (i) improve infrastructure and social sector services, (ii) repair or mitigate damage caused by natural disasters; and (iii) reactivate private economic activity.	- Subprojects to be financed by the loan will meet at least one of these three purposes 2 – 3 years after completion of works. Measurable performance indicators (including baseline data, and project implementation and completion targets) will be defined to verify achievement of these purposes. (Loan resources will be committed three years after Board approval)	- CDB Subproject Appraisal Reports, including Logical Frameworks. - CDB Supervisory Reports and mid-term evaluation report(s).	- The Government of Grenada maintains the political will and interest to implement the program as agreed between IDB and the CDB. - The ARD and executing agencies in Grenada are respectively provided the required resources to coordinate and implement the various subprojects. - Strong collaboration between CDB and Government of Grenada to design and implement the subprojects. - ARD is able to provide acceptable standardized reports on a timely basis.
OUTPUTS	Specific development subprojects (approved and financed by CDB) in the areas of (i) housing infrastructure (sites and services) on properties with clear land titles; (ii) environmental and public infrastructure reconstruction;	- Subprojects will be consistent with (a) the Operating Regulations agreed between the IDB and CDB and (b) the priorities established jointly between CDB and the Government of Grenada. - Subprojects will have been adequately appraised. All loan resources will be committed by the end of year three of project execution. - By year three, subprojects representing half of loan	- CDB Subproject Appraisal Reports - CDB monitoring reports and mid term evaluation report(s) to the IDB. - IDB project monitoring system reports. - Annual report of the CDB.	- Demand for public sector resources remains high in Grenada. - Demand for medium/long-term financing remains high from commercial banks and their private entrepreneur clients for the purpose of

	NARRATIVE	OBJECTIVE VERIFIABLE INDICATORS	MEANS OF VERIFICATION	ASSUMPTIONS
	and (iii) financing through first tier commercial banks for business revitalization activities that are technically, socially, economically, financially and environmentally viable and sound.	fund resources will have reached their mid-term execution point; at this stage, the subprojects will have met project implementation benchmarks, or agreements have been reached between the CDB and sub-borrower to ensure completion through remedial measures.		reactivating/rehabilitating their businesses. - CDB and the local executing agencies have the capabilities and resources to design, implement and monitor the execution of the subprojects.
I N P U T S	- Program resources (IDB loan to CDB) to finance (a) acquisition of works(?), goods and services, &/or (b) a line of credit. - Staff time, direct costs, external advice and overhead of the CDB and executing agencies in Grenada for the design and implementation of subprojects.	- Subprojects budgets by activities - Disbursements of program resources - Dedication of CDB staff and administrative budget resources. - Subproject teams formed and working on at four sub-loans within 12 months after IDB Board approval.	- Disbursement reports. - CDB sub-project appraisal and interim progress reports. - Detailed accounting reports compiled by the ARD and maintained in its consolidated data base.	- Timely availability of program financing. - Consistent funding for GOGR administrative and technical staff responsible for sub-project execution.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-___/05

Regional. Loan____/SF-RG to the Caribbean Development Bank
Grenada Reconstruction, Recovery and Development Program

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 Caribbean Development Bank, as Borrower, for the purpose of granting it a financing to cooperate in the execution of the Grenada reconstruction, recovery and development program. Such financing will be for an amount of up to US$10,000,000, or its equivalent in other currencies, which is part of the resources of the Bank's Fund for Special Operations ("FSO"), and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

LEGIII/RG-539956-05
RG-L1006