

INVESTMENT SECTOR REFORM PROGRAM

(BA-0012)

EXECUTIVE SUMMARY

BORROWER AND GUARANTOR: The Government of Barbados

EXECUTING AGENCY: The Ministry of Finance and Economic Affairs

AMOUNT AND SOURCE: IDB: US\$35 million

FINANCIAL TERMS AND CONDITIONS:

Amortization period:	20 years
Disbursement period:	3 years
Interest rate:	variable
Inspection and supervision:	1%
Credit fee:	0.75%

OBJECTIVES: The Investment Sector Reform Program (ISRP) will increase the competitiveness of the barbadian economy and improve the climate for private sector investment.

DESCRIPTION: The ISRP is a fast-disbursing operation in the amount of US\$35 million to be released in three tranches, over a period of approximately 24 months. The first tranche will include the resources for the technical support component and will total US\$15 million. The second and third tranches will be each US\$10 million. Disbursement of each tranche is contingent upon compliance of tranche-specific conditionality and maintenance of an appropriate macroeconomic framework.

To support the growth-oriented macroeconomic framework recently adopted by the GOB, the IDB will assist the Government in addressing distortions in areas that pose significant obstacles to new private investment in Barbados: (i) the financial sector, (ii) land-use policy, and (iii) the enabling environment for private sector investors. Inefficiencies in each of these sectors significantly raise transaction costs for new investments.

ENVIRONMENTAL CLASSIFICATION: The environmental brief for the ISRP was considered by the Environmental Committee on May 11, 1995. The operation was classified as a category III. The CMA reviewed and approved the Environmental Summary on September 14, 1995. The environmental measures contained in the ISRP are consistent with those in other Bank projects, such as Coastal Conservation and

Solid Waste. Furthermore, completion of the institutional arrangements for the environmental management unit will be accomplished by second tranche.

BENEFITS:

The beneficiary of the ISRP will be the private sector, especially small and medium enterprises, in Barbados. At the conclusion of the loan program, Barbados will enjoy a financial sector capable of providing a wide range of modern financial services to a growing, diversifying private sector. Land-use policy and administration will, subject to environmental considerations, water resource constraints, the GOB macroeconomic strategy, and the GOB overall settlement policy, permit the rapid shift of land resources into new sectors and economic activity. Finally, the process of registering and starting new businesses will be faster and less costly.

RISKS:

The GOB medium-term macroeconomic policy framework calls for a contraction in domestic demand and an increase in productivity to check inflation and maintain a sustainable balance of payments position. Since the use of the exchange rate as a policy instrument has been ruled out, the GOB strategy will require fiscal austerity and an incomes policy. Such a strategy will require the full support of the social partners and if such does not materialize in full measure, the barbadian economy will be very vulnerable to external shocks.

Several of the policy measures identified in this project will involve changes to the legal and regulatory system which only Parliament has the authority to approve and enact. The project team believes this risk can be well managed considering that the long gestation period for this project has allowed the issues to be thoroughly vetted throughout the government and the private sector in Barbados.

**THE BANK'S
COUNTRY AND
SECTOR STRATEGY:**

Bank strategy for Barbados is set out in the Country Paper now under review. This strategy identifies increasing efficiency throughout the economy as an important priority. Accordingly, this operation is consistent with Bank strategy.

POVERTY TARGETING:

As a policy based operation, this project is not expected to have a direct impact on poverty in Barbados.

**SPECIAL
CONTRACTUAL
CONDITIONS:**

The program will be governed by a loan contract. The special contractual conditions are set forth in Annex IV.

I. INTRODUCTION

- 1.1 The Investment Sector Reform Program (ISRP) is a fast-disbursing operation in the amount of US\$35 million to be released in three tranches, over a period of approximately 24 months. Disbursement of each tranche is contingent upon compliance of tranche-specific conditionality and maintenance of an appropriate macroeconomic framework.
- 1.2 The most important objective for economic and social development in Barbados is to restore sustained growth in the economy. Without a resumption of economic growth, living standards would deteriorate and resources would be unavailable for the pressing social problems that would inevitably follow in the wake of economic stagnation. Bank analysis has revealed that the path to sustained growth is through improved export performance. Achieving this will require the government to maintain external competitiveness by means of policy measures designed to increase investment in tradable goods industries.
- 1.3 In accordance with this strategy, the Bank will assist the Government of Barbados (GOB) in building a policy framework conducive to long-term economic growth and development. The World Bank has recently graduated Barbados and is unable to implement an adjustment program for the country. However, with periodic IMF consultations, supplemented by World Bank technical assistance, the GOB will soon put into place a medium-term adjustment program that will stimulate investment in export industries, as well as in efficient import-substitution industries, in which Barbados enjoys a comparative advantage.
- 1.4 The ISRP will complement and support the government's macroeconomic adjustment program by strengthening private sector development, the engine for future growth. With the ISRP, the Inter-American Development Bank (IDB) will assist the GOB in addressing several major distortions in the financial sector, in land markets and in the enabling environment for new investors, each of which now significantly raises transaction costs for private investment. At the conclusion of the loan program, Barbados will enjoy a financial sector capable of providing a wide range of modern financial services to a growing, diversifying private sector. Land-use policy and administration will permit the rapid shift of land resources into new sectors of economic activity. Finally, the process of registering and starting a new business will be faster and less costly.

II. FRAME OF REFERENCE

A. Macroeconomic framework

- 2.1 Barbados is a small, densely populated, tropical island nation, with two major distinctive assets: its natural beauty and its highly educated population. These two assets were the chief factors responsible for its generally successful development performance from independence in 1966 to the end of the 1980s. In 1966-89 the country's real GDP posted an average growth rate of 3.2% per annum, which implied per capita real growth of 2.7% per year, as the economy evolved from one largely dependent on sugar, to one based on tourism, manufacturing, and information and financial services. By 1989 per capita GDP had reached a nominal \$6,708, second highest among IDB borrowing countries, inflation was low, and external debt levels were modest by Latin American standards. Steady economic growth permitted the development of an extensive and generous social services system, a consequence of which is that Barbados ranks first among developing nations in the U.N.-defined Human Development Index.
- 2.2 In the course of the 1980s, however, the Barbadian economy's competitive edge gradually eroded due to internal and external factors, such as high domestic costs in manufacturing and tourism and fierce price competition from other Caribbean destinations. In the second half of the decade private investment fell, manufacturing output declined and the sugar sector's long-term slide worsened, despite a massive effort by the government, through the Barbados National Bank (BNB), to shore it up financially. Fiscal policy, combined with the bargaining power of labor unions, tended to artificially, but effectively, counteract declining real economic performance by cushioning its impact on private consumption, which did not decline.
- 2.3 The slowdown in investment in the 1980s can be attributed mostly to the decline in competitiveness and consequent deterioration of profitability in tourism and manufacturing. The major causes of the decline in competitiveness included the following:
 - a. The maintenance of a fixed nominal exchange rate combined with macroeconomic policies that accommodated inflation and wage settlements exceeding productivity gains have lead to a real appreciation of the currency, especially in relation to Caribbean competitors.
 - b. Manufacturing was heavily protected by tariffs and non-tariff barriers which, combined with tax increases, made many inputs for tourism more expensive than imported ones. This lowered profits and thus acted as a disincentive to investment in improvement and expansion of the hotel plant.

- c. Labor market institutions and policies were obstacles to labor productivity and mobility, thus increasing the cost of labor for the private sector. Collective bargaining agreements imposed restrictive work rules which limit the most efficient use of labor resources. Moreover, the severance system discourages the movement of workers between employers and sectors.
 - d. Land-use policy limits the efficiency of land markets. Rigid restrictions are placed on the sale of agricultural land for other than its historical agricultural use and exceptions to these restrictions are applied in a non-transparent manner. Current land-use policy, therefore, creates disincentives for investment in new land-intensive economic activities, such as tourism and residential development.
- 2.4 With these adverse trends already in motion, a large drop in stopover tourism in 1990-91 coincided with very high external debt service obligations. The ensuing foreign exchange scarcity triggered the country's worst economic crisis since independence. In the 1990-92 triennium real GDP dropped by 12%, the unemployment rate shot up from 15 to 25% (in 1993), and net international reserves became negative in September/October, 1991. Investment coefficients fell to very low levels, during the 1990-92 economic crisis and its aftermath, auguring ill for future growth.
- 2.5 The authorities responded to this crisis in the latter part of 1991, by adopting a comprehensive adjustment program that was supported by a stand-by arrangement with the IMF. The initial, stabilization phase of that program was designed to stem the reserve drain without recourse to currency devaluation. This required drastic cuts in aggregate demand, which were effected primarily by harsh fiscal measures, supported by tight monetary policies and a general wage-price freeze. The stabilization program was a success in that, by 1993, the fiscal deficit was virtually eliminated, international reserves substantially increased and inflation was reduced to practically nil. However, economic contraction continued and unemployment remained at record high levels. Economic activity experienced a recovery in 1994 -- real GDP grew 4% -- due mainly to a strong upswing in tourism, but that upswing was based primarily on external, non-recurrent events. Indeed the economy was expected to grow at less than 1% in 1995.
- 2.6 Since the end of the stabilization program in 1993, macroeconomic policy in Barbados has focussed on stimulating a recovery of economic activity, mainly by prudently relaxing fiscal policy, while simultaneously building up net international reserves to a level that would provide adequate protection for the existing fixed exchange rate parity with respect to the U.S. dollar. The authorities have been aware of the potential conflict between their main policy aims and consequently acted with considerable caution. Thus, they have restored the 8% cut in public sector wages and the duty exemptions on imported inputs for agriculture and manufacturing,

which were imposed under the stabilization program; but they also have firmly adhered to the existing wage-price freeze protocol, and supplemented net current foreign exchange earnings with foreign borrowing. The fiscal deficit which had been virtually eliminated in 1993, rose to 1.8% of GDP in 1994, but the situation has been reversed in 1995, as a small fiscal surplus was posted for the first half of the year. Net international reserves have steadily increased and stand close to their desired level of three months of imports.

- 2.7 This policy approach has been basically incorporated into the GOB's comprehensive medium-term economic strategy (MTES) for the 1995-98 period. Under this strategy, the fixed exchange parity is to be maintained by low fiscal deficits supported by monetary and incomes policies. The restoration of growth itself is expected to follow upon structural reforms already underway, which constitute the second part of the comprehensive adjustment program adopted in late 1991. These reforms were designed mainly to improve the economy's competitiveness, thus providing a strong stimulus for the increase in private investment required to restore sustained growth. Private investment, both domestic and foreign, and especially in the exportables subsectors, is expected to play the central role in the country's return to sustained growth.
- 2.8 The barbadian authorities have made very considerable progress to date in implementing the structural reform program. Key measures already adopted include: (i) tax policy; the direct tax system has been simplified, especially corporate and property taxes, and many distortions eliminated; (ii) financial policy; selective credit controls have been largely eliminated, as was the fixing of interest rates by the Central Bank. Most interest rates are now market-determined; (iii) foreign trade policy; the CARICOM Common External Tariff reductions are being gradually implemented, according to the agreed timetable. Most non-tariff barriers have been eliminated and replaced by temporary ad valorem tariff surcharges; and (iv) gradual privatization of state enterprises has taken place.
- 2.9 Excluding reforms that will be put in place supported by the ISRP, the key remaining elements of structural reform are: (i) a new indirect tax policy, existing consumption taxes, stamp duties and other minor taxes would be replaced by a value added tax (VAT), thus eliminating most of the anti-export bias in the tax system and encouraging private investment in exportables. Implementation is scheduled for April 1, 1996 (with technical assistance under an IDB program); (ii) labor market reform. Labor costs are intended to be lowered and efficiency in labor markets improved by revising the severance pay scheme and other labor regulations. In fact, incomes policies in effect since 1993 have prevented significant wage increases in that period.

B. Bank lending strategy

- 2.10 The most important objective for economic and social development in Barbados is to restore sustained growth in the economy. Without a resumption of economic growth, living standards would deteriorate and resources would be unavailable for the pressing social problems that would inevitably follow in the wake of economic stagnation. Bank analysis has concluded that the path to sustained growth is reversing the decline in external competitiveness. This will require the implementation of a comprehensive adjustment program to improving the incentives for investing in tradable goods industries, eliminating factor market imperfections, and rationalizing the public sector role in the economy.
- 2.11 Over the 1995-1997 period, the Bank's lending program will support this strategy. Projects in multisector credit, tourism development and the expansion of the Bridgetown port will improve the competitiveness of those sectors of economic activity in which Barbados enjoys a comparative advantage. Project activities in solid waste management, coastal conservation and management and west coast sewerage will assist the GOB to reverse and avoid potential environmental degradation. A project to rationalize health services will improve the efficiency and delivery of social services, while meeting the special needs of the adjustment process.

C. Relations with other multilateral organizations and external creditors

- 2.12 The IDB is the major assistance agency with an extensive and comprehensive program in Barbados. It is now by far the main source of multilateral development finance for the country. The World Bank has "graduated" Barbados. The Caribbean Development Bank has approved to date \$90.3 million in loans to the country, and plays an expanding role in cofinancing with the IDB, particularly in the Solid Waste projects. The US Agency for International Development has a Caribbean regional program that indirectly benefits Barbados. The European Community, mainly through its lending arm, the European Investment Bank has small programs, mainly in technical assistance focused on tourism training and the productive sectors.

III. THE SECTOR PROGRAM

- 3.1 The macroeconomic program adopted by the GOB, and supported by periodic IMF staff consultations, will address the major structural impediments to renewed growth in the economy of Barbados. The initiatives contained in that program will complement the ongoing stabilization effort and stimulate investment in export industries, as well as in efficient import-substitution industries, in which Barbados enjoys a comparative advantage.
- 3.2 To support this growth-oriented macroeconomic framework, the IDB will assist the GOB in addressing several major distortions that pose significant obstacles to new investment in Barbados. Over the past several years the Bank and the GOB conducted several diagnostic studies in order to identify opportunities for appropriate policy reform to complement those already being addressed in the macroeconomic program. These analyses ranged over the entire spectrum of options normally considered in the context of an ISRP: privatization, utility regulation, labor market policies and the like. Our studies revealed three priority areas which were not being addressed in other project activities and where policy adjustment would impact favorably on private sector investor decisions: (i) the financial sector, (ii) land-use policy, and (iii) the enabling environment for investors. The financial sector is not capable of providing the range of financial services that will be in demand from private sector investors rapidly diversifying into new business activities. Second, land-use policy, as well as the administration of that policy, does not permit the speedy shift of land resources into new sectors of economic activity. Lastly, the enabling environment for new investors is very inefficient; it is very costly to register and begin a new business enterprise in Barbados.

A. Macroeconomic policy framework

- 3.3 Over the next four years, the government will confront the task of implementing the Medium-Term Economic Strategy discussed in the above sections. Higher expenditures and lower than anticipated revenues have caused the fiscal position of the government to deteriorate since 1993, and the authorities will be struggling to maintain the stabilization targets in the Strategy. The recently concluded Prices and Incomes Protocol will help in this regard. With respect to taxes, the implementation of the direct tax reform enacted in July 1992 is now virtually complete and on schedule. In addition, a value-added tax system has been designed to replace the myriad of consumption and stamp duties, and it will be laid before Parliament this year. The new CARICOM External Tariff schedule is being implemented and the authorities have removed many non-tariff barriers.

- 3.4 Proposed Action. The success of the ISRP in developing a more dynamic incentive structure for private sector investment in Barbados will depend in large part on the complete and prompt implementation of the GOB economic strategy. For this reason, the IDB will support the efforts of the GOB in this endeavor, and its progress, especially in the areas of stabilization, incomes policy and trade and tax reform, will be carefully monitored. The implementation of tax reform will be aided by the technical cooperation between the GOB and the IDB. It is anticipated that the IMF will assist in monitoring the stabilization effort through frequent staff consultations with the government.

B. The financial sector

- 3.5 The financial sector in Barbados can not respond adequately to a growing private sector demand for financial services. The most serious problem is systemic risk; the weak financial condition of two state-owned banks places a severe drain on the entire financial system. Furthermore, there are gaps in supervision and regulation. Finally, the securities market is underdeveloped.

1. Removing systemic risk

- 3.6 The weak financial position of the BNB poses the greatest obstacle to the growth and development of the financial sector in Barbados, and, consequently, to the growth of financial services to the private sector. The BNB plays an important role as both a commercial and to a lesser extent development bank. As a commercial bank it has a 67% market share of time deposits, and it holds approximately 25% of the liabilities and 30% of all assets of commercial banks in Barbados. As a development bank, it was the government's main instrument for supporting the sugar sector. During the preparation of the ISRP, the single largest threat to the solvency of the bank was eliminated when non-performing loans to this sector were removed from the books of the BNB and transferred to a specialized work-out agency (the Barbados Agricultural Credit Trust) in 1993. The year prior to this transfer, the outstanding balance of nonperforming loans of this bank was equivalent to 12% of GDP. Although this sugar-debt workout initiative has substantially improved the BNB balance sheet, non-performing and poorly performing loans still represented, as of mid 1995, 40% of loans outstanding of the BNB. As part of the Investment Sector Reform Program, BNB management will complete a work-out plan for all delinquent loans, and priority will be given to restoring them to fully performing status. To assure that arrearage rates on future loans are maintained at or below acceptable levels, a number of organizational and procedural changes will be carried out by the BNB Board of Directors and management, as noted below.
- 3.7 The BNB's deposit base is comprised primarily of small accounts and, although traditionally stable, there is no assurance that significant withdrawals would not occur in the face of diminished

public confidence. As mentioned above, the bank has followed practices which could raise just such doubts. Poor loan administration has allowed arrears to remain uncorrected over extended periods of time, even in those cases where the borrower was capable of servicing the debt promptly; unpaid interest and principal have been capitalized resulting in a misleading picture of portfolio performance. Contributing to these bad practices has been poor head-office supervision of the branch offices. The trend in net interest margin between 1993 and the first quarter of 1995 is downward, going from 3.0% of average assets to 1.6% (annualized) respectively. Net earnings and cash flow are substantially negative and projected to remain so. The BNB lacks a strategic focus which is compounded by a transaction, rather than a customer/service, mentality. Reform of the BNB will promote a more healthy financial sector in general and will make more loan funding available to well qualified private sector investments as its loan decisions are increasingly made solely on the basis of their commercial merit.

- 3.8 Proposed Action. In response to the current weak position of the BNB and to the mutually agreed objective of restructuring it as a commercial bank, the IDB and GOB authorities propose a number of reforms which will be carried out during the execution of the sector loan. The first important task will be to improve its financial position. To this end the BNB will carry out an internal review of all loans greater than B\$50,000 (US\$25,000) and initiate a work-out plan for those which are found to be delinquent. Once this is accomplished, the institution will be able to increase loan loss reserves sufficient to cover potential losses from troubled loans and, if necessary, prepare a plan for recapitalization of the bank in light of the Basle capital adequacy standards. In addition, the government will increase the interest paid on GOB securities delivered to the BNB in exchange for the non-performing sugar and other parastatal assets which have been divested by the BNB to specialized work-out entities. A detailed list of the actions to be taken are available in the project files and will be included in the minutes of negotiation.
- 3.9 The next step for the BNB will be to strengthen its internal management and controls. A policy statement on BNB governance will be approved and implemented by the board; a recently established asset-liability management committee will better match and supervise bank risk on both sides of the balance sheet; management will train staff in new credit policies and procedures; the internal audit function will be substantially strengthened; and the BNB will regularly subject itself to the external audit standards established for commercial banks by the Financial Intermediaries Regulatory Act. Also the BNB will gain more effective control over its subsidiary mortgage bank, Barbados Mortgage Finance Corporation (BMFC), and initiate an internal review of this institution.
- 3.10 Once the financial position of the BNB has been improved, its internal management has been strengthened, and the bank has been

rechartered under FIRA, the GOB will proceed to privatize the bank. The BNB will be rechartered under the legislation governing commercial banks. Subsequently, at least 51% of the ownership will be brought to point of sale. Subsequently the GOB may further reduce its equity in the bank. As the only major commercial bank which is owned domestically, the strategy of restructuring the BNB first and then selling a majority stake has been designed to assure that majority control be diversified as widely as possible while remaining predominantly in Barbadian hands.

2. Development finance

- 3.11 The Barbados Development Bank (BDB) traditionally has provided the small business and service sectors term financing under favorable conditions. Due to difficult economic conditions and lax loan recovery practices, almost two thirds of the US\$37.5 million loan portfolio is in non-performing status. Recent loans are doing better, but the rate at which older loans have been falling into default has been increasing since 1990. The bank has accumulated losses of at least US\$23.5 million and a negative net equity of approximately US\$6.8 million. Cash flow and earnings are substantially negative, and projected to remain so. Without additional sources of funds, the institution will soon be starved of operating resources.
- 3.12 The problems of the BDB relate principally to the provision of development finance in Barbados. Since the BDB does not have a local deposit base, it does not pose the same risk to the financial system as does the BNB. However, its poor financial record suggests that it has outlived its usefulness in providing finance to emerging businesses in Barbados.
- 3.13 Proposed Action. The BDB will terminate new lending operations and initiate a wind-up of the institution. Non-performing assets will be divided into two groups and transferred to specialized loan work-out entities created for this purpose. Performing assets will be disposed of prior to second tranche at which time the BDB will formally go out of existence. A detailed list of the actions to be taken are available in the project files and will be included in the minutes of negotiation.
- 3.14 The first group of non-performing assets consists of loans to certain unprofitable South Coast hotel properties which are seen as having potential for rehabilitation. To this end a single purpose GOB-owned corporation will be established to attempt to restore these properties to profitability within a fixed period of time and a fixed government budgetary commitment. For the second group of non-performing assets, a separate single-purpose corporation will be created to liquidate these prior to third tranche disbursement.
- 3.15 In order to develop a plan for the future of development finance in Barbados, an assessment of alternatives, sponsored by the Caribbean Development Bank (CDB), will be carried out by an international

consulting firm. Earlier studies have suggested that private financial intermediaries may well be able to meet the demand for development finance if technical assistance were provided and the second-tier term financing facility were improved. Once the CDB sponsored study is completed (expected by first quarter, 1995) these results as well as those of the earlier studies will be reviewed by the GOB and Bank, and a plan of action will be agreed upon prior to first tranche release. A key criterion for determining the course of action to take will be the expected impact on private sector investment. If this plan were to include provision for a new first-tier Development Finance Institution (DFI), it would be essential that it not fall into the same difficulties as the BDB. To this end guidelines have been established and are included in the policy matrix regarding governance and operating modalities of any possible future DFI in Barbados. These include minority government ownership to be reduced over time, assumption of entire credit risk by the DFI on its loans, and charging of market rates on all lending. In the event that a DFI were to be created, compliance with these guidelines would be monitored prior to second and third tranche releases.

3. Regulation and supervision

- 3.16 In 1992, the GOB strengthened the legal basis for supervision and regulation of the banking system in Barbados by approving a new Financial Intermediaries Regulatory Act (FIRA). However, this does not provide for assigned capital for branches of foreign commercial banks operating in Barbados. Moreover, the FIRA contains provisions that limit the effectiveness of the Supervision Department of the Central Bank in dealing with the problem of insolvent banks. These and related deficiencies would be rectified by passage of a proposed "Financial Institutions Act" which is currently under consideration by Cabinet for subsequent presentation to Parliament. As it is expected that this legislation will be approved prior to effectiveness of the ISRP, the GOB requires no further assistance in this regard.
- 3.17 The GOB believes that improvements to the regulatory environment especially in regard to non-bank financial intermediaries may be needed. Well defined and administered regulations bring about more transparent and reliable intermediation which in turn increases private investors confidence in and use of the financial system. In addition to commercial banks, there are several categories of financial institutions in Barbados, including credit unions, insurance companies, securities brokers, pension funds, etc. which are presently regulated by a variety of unrelated government oversight agencies, or not regulated at all (e.g. the securities market). These agencies have varying capabilities to detect and take action on potentially serious problems within the institutions they respectively supervise.

- 3.18 Proposed Action. As part of the ISRP technical support component, a study will be carried out of the current regulatory environment for all finance-related institutions in Barbados leading to recommendations and appropriate actions for reform.

4. Government securities market

- 3.19 The securities markets in Barbados has several deficiencies. In particular, although contractual saving and insurance schemes are widespread and represents a major source of long-term resources, most of these funds are invested in government paper which is held to maturity. This results from an essentially non-existent secondary market in government securities. The creation of such a market would reduce intermediation costs and facilitate the flow of capital to its most productive uses, thus facilitating private investment. While the market would initially trade in government securities exclusively, it would set benchmarks and provide experience in trading methods which could subsequently be helpful in expanding the market for corporate paper. Central Bank of Barbados (CBB) and Bank sponsored analysis has established the feasibility of establishing such a market on a largely over-the-counter basis.

- 3.20 Proposed Action. Consistent with this analysis, an expert will be hired to work with the CBB to initiate operations in the government securities market. The technical support component of the ISRP will provide financing for the honorarium and related expenses of this expert.

5. Secondary mortgage market

- 3.21 During the 1980s the government and private sector expressed interest in creating a market in which home mortgage instruments could be traded among financial agents. Studies were carried out; however no action was taken, and at present banks and other institutions granting mortgage loans hold them in portfolio until maturity. Development of this market would facilitate the further growth of contractual and other long-term savings by way of offering a more diversified range of instruments in which to invest these resources. Recently there has been renewed high-level interest in creating a secondary mortgage market Barbados, due in part to the success of a second-tier mortgage bank in Trinidad and Tobago and recent initiatives to create a similar institution in the Eastern Caribbean States.

- 3.22 Proposed Action. Drawing lessons as appropriate from the Trinidad experience, background studies and initial implementation of a second-tier mortgage bank would be carried out as part of the technical support component of the ISRP.

C. Land-use policy

- 3.23 The development of efficient land markets is crucial to the long-term growth and development of Barbados. For over 300 years the pattern of land-use has been dominated by plantation agriculture. Now, as the economy adjusts to a new structure of production and exports under the medium-term adjustment program, new land-intensive activities, such as new tourist products, will emerge. Land-use policy and administration in Barbados could more efficiently accommodate these demands through reformed regulation and guidance which also addresses environmental concerns, and which preserves some land for the provision of public goods that would meet recreational and aesthetic needs.
- 3.24 The current land-use policy in Barbados, as expressed in the Physical Development Plan, and as reflected in day-to-day administrative decisions, applies highly restrictive controls to the transfer of land to alternative uses. Complicating the problem of land-use policy is the legal and financial situation facing many of the sugar estates. Until these problems are resolved, transfers of sugar lands to alternative uses will be difficult. Each of these issues is discussed in more detail below.
- 3.25 The Town and Country Planning Act vests considerable discretionary authority with the Minister and the Chief Town Planner. The law gives to the authorities the power to grant approval to development projects "in special circumstances." Neither the law nor the regulations attempt to define these circumstances. Such an exercise of authority, without clearly defined and well-publicized land-use principles, creates uncertainty in land markets and acts as a constraint to the development of a more rational structure of production.
- 3.26 A fundamental problem also exists with the "National Land-Use Policy" which is contained in the Physical Development Plan. This policy, simply stated, divides Barbados into an "urban zone" and an "agricultural zone". Urban development is to be concentrated in the urban zone and prohibited or discouraged in the agricultural zone. While exclusive agricultural zoning is conceptually sound and commonly applied in other countries, the existing zoning pattern should be revised to reflect current needs and changing economic structures, as is the practice elsewhere.
- 3.27 Numerous deficiencies found in the staff structure and operations of the Town Planning Office hampers the regulatory process and results in slow processing of planning applications. There is an inconsistent and irregular flow of information among government departments involved in land-use issues. There is a virtually no public discussion and review of planning decisions. There is a lack of normative standards, such as building codes and environmental criteria. Finally, regulation is impeded by limited staff and other resources.

- 3.28 Finally, the more efficient operation of land markets in Barbados is hampered by financial problems in the sugar sector. This sector, accounting for about 50% of agricultural output and arable land under cultivation, is in a particular state of crisis. Returns to sugar were low through the decade of the 1980s, and declining capital investment has led to falling production and rising per unit fixed costs until the industry now is one of the least efficient in the world. And yet, because of the role the sugar industry plays in the ecology and economy of the country, successive governments have been reluctant to allow the sector to collapse completely, and have retained land-use policies that were designed to protect and preserve the amount of land under cultivation.
- 3.29 Proposed Action. The GOB has agreed to begin implementing a four-part program to effectively address the problems now affecting the functioning of land markets in Barbados. These are: (i) revisions to the Physical Development Plan (PDP) providing Barbados with a policy framework for land-use planning and the issuance of planning permissions; (ii) strengthening the Office of the Chief Town Planner; (iii) a plan for the diversification of land-use on the sugar estates and other rural areas; and (iv) a reform of planning permission procedures. These actions are interrelated and focus upon the principal economic, environmental, and demographic issues that are likely to affect land-use in the future and the key legal and institutional aspects of land-use planning.
- 3.30 The government has already made significant progress in resolving probably the most vexing problem facing land-use planning in Barbados, the restructuring of the financially troubled sugar estates and production facilities. A fiduciary agency, Barbados Agricultural Credit Trust (BACT), has been created to take title to the security interest in the insolvent, indebted sugar mills and estates, which were transferred from the BNB after an independent audit of their performance. The BACT and its operating arm, the Barbados Agricultural Management Company (BAMC), have temporary charters, and are organized and managed specifically to insure the speedy and orderly disposition of these sugar lands and related assets with minimum disruption of sugar production and export. Those assets (estates and mills) that can not be restructured and placed on a commercial basis will be liquidated by the agency in an orderly, but expeditious manner.
- 3.31 In order to give land-use planning a more flexible and robust policy framework, the government has decided to revise the Physical Development Plan. This will provide for more flexibility in allocating land between agricultural and nonagricultural uses. Once revised, the PDP will be established, through amendments to the Town and Country Planning Act, as standing policy. The GOB has already prepared a TOR for the revision and these have been agreed to between the government and the Bank.

- 3.32 The new policies regarding land-use will operate within the context of environmental and water resource constraints, the GOB macroeconomic strategy, and the GOB overall settlement policy. This will be achieved through an environmental planning review which, during the revision of the Physical Development Plan, will identify any adverse environmental impacts resulting from future land-use. Furthermore, to insure that environmental considerations are met in any land-use allocation, an environmental regulatory framework will be created. An environmental management unit will be empowered under law to draft environmental regulations and will be given powers of enforcement and sanction.
- 3.33 The existence of the BACT offers a unique opportunity to strengthen the PDP with an area development plan focusing on the land-use issues inherent in the overall problem of the heavily indebted estates, as well as in other rural areas. This task will be a cooperative effort of government, landowners and the BACT/BAMC. This will allow a more rational allocation of land resources now in the rural sector in the context of a sustainable agriculture base, resource conservation, and the financial obligations of the heavily indebted estates. The area development plan will be adopted following preparation of Draft Physical Development Plan, and consistency between the two Plans will be assured.
- 3.34 The Town and Country Planning Act will be amended to give higher policy standing to the PDP. The amendments to the Town and Country Planning Act will specify the procedures whereby plan amendments are proposed, reviewed and adopted, and will provide for formal opportunities for technical and public review.
- 3.35 At the same time that a stronger land-use policy framework is being put in place, the GOB will move to strengthen the administration of that policy. The first step in that direction will be to augment the Office of the Chief Town Planner in order to provide for quicker regulatory response. Based on a comprehensive audit of the Town Planning Office, staffing and budget requirement will be adjusted to increase capabilities to review and process planning applications. This task is already well advanced with Terms of Reference (TOR) and recommendations already agreed to between the GOB and the Bank.
- 3.36 The second, and probably the most crucial, step in augmenting regulatory response will be in amendments to the Town and Country Planning Act providing for revised administrative procedures for granting land-use permits. The most important changes to current procedures will be to add institutional depth to the review process; to reform the planning permission process to incorporate up-dated and publicized procedures, and to permit public participation in the process. Under these revised procedures:
- a. Planning applications, if found consistent with standing policy and/or regulations, will be approved by administrative action of the Chief Town Planner. The statutory consultations and

recommendations that accompany the decision will be accessible to the applicant and general public in the case of any planning decision.

- b. The Policy Advisory Committee (PAC), which now exists but is inactive, will assume a stronger role in planning decisions. The exact nature of that role, along with procedures for its implementation, shall be the subject of an in-depth review. The study could recommend that the PAC should review those applications that, in the opinion of the Chief town Planner fall on the threshold of current policy.
- c. There will be a transparent and more rigorous appeals process. To further this objective, appeals panelists will be more carefully selected and training will be provided to enable them to render more careful and considered opinions.
- d. The current right of the Minister to call in and determine categories of applications arbitrarily will be modified. The Minister will be able to call in applications on an individual basis only, after due gazetting and publication in at least one daily newspaper. All material relating to the Minister's decision will be available to the public.

D. The enabling environment for private sector investment

- 3.37 The private investor faces a myriad of obstacles in starting a new business enterprise in Barbados. To begin with, there is no single convenient and effective entry point through which to channel prospective investors wishing to survey the business climate. Furthermore, given the maze of legal and regulatory obstacles, and the numerous ministries and agencies involved in the approval process, there are long delays in the start-up of new investments. Finally, there are several shortcomings in the system of copyright, trademark and patent law which do not give full protection to the intellectual property of foreign investors.
- 3.38 Investment and trade promotion have become very important issues for Barbados. As is the case for many developing countries, stagnant economic growth has forced the government to recognize the limitations of inward oriented development strategies and to adopt a more open economic policy framework that encourages foreign and domestic direct investment, especially in the export sector. A macroeconomic policy regime addressing trade, tax and exchange issues and laying the foundation for growth with price stability is the first important element in this regard. There will be little incentive for private sector investment in a depressed or unstable economy.
- 3.39 The second important element is a national strategy for investment promotion. The authorities in a small resource-poor economy such as that of Barbados cannot afford to take a passive stance with

respect to investment promotion. Comparative advantage must be identified and matched to appropriate investment opportunities.

- 3.40 Finally, a well-designed legal and regulatory framework must be created to serve as a catalyst for attracting quality investments. Ideally, this framework would be characterized as demand, or customer, driven, would possess a transparent regulatory environment under one authority and would serve three distinct functions: (i) investment promotion; (ii) screening investment proposals and advisory services to help entrepreneurs prepare project documentation; and (iii) investment facilitation and post-investment assistance. Under each of these functions, tailored programs are established to ease the burden for potential and existing investors to conduct business within the country. As a result, the potential investor will understand the direction of growth of the economy, and thus gear the proposed investment within that framework, and can see an environment in which the business will grow and prosper.
- 3.41 Several elements of this system already exist in Barbados. The macroeconomic policy regime is undergoing reform under the medium term adjustment program. Moreover, the Government of Barbados has begun to articulate an investment promotion strategy. A recent policy statement set priority on foreign direct investment as a principal area of focus to stimulate economic growth. Furthermore, the GOB outlined a number of strategic areas, mainly information technology, where foreign investment will be targeted. Consequently, the uncertainty and lack of confidence that marked the investment climate in the past is giving way to greater public-private cooperation in setting goals for the economy.
- 3.42 There is, however, a weak institutional framework to support investment activities. There is no single entry point or "window" through which a potential investor can obtain information. Promotion activities occur on an ad hoc basis by organizations with little coordination between them and considerable overlap in responsibilities. There are multiple windows, and the appropriate access window depends on the type of business in question. For example:
- a. The Barbados Industrial Development Corporation (BIDC) has been the first stop for investors looking into manufacturing activities in Barbados. It administers the incentives allowed under the Fiscal Incentives Act and controls access to much of the factory space required by manufacturing enterprises.
 - b. There are at least four separate organizations that may provide assistance to investors in tourism: the Board of Tourism, the Barbados Hotel Association, the Barbados Tourism Development Corporation and the Barbados Tourism Investment Corporation. Among these organizations, attention is focused more on attracting tourists than on investment in the tourism sector,

and a comprehensive package for interested investors does not seem to exist.

- c. There is no public sector organization that proactively promotes investment in offshore services. Inquires from potential investors are referred to accounting or law firms. These private sector firms are fulfilling the function of a one-stop-shop but at a fee to the investor and with limited focus.
 - d. An investor interested in an agro-processing venture is usually directed to the Ministry of Agriculture and the Barbados Agricultural Development Corporation for information. These two organizations have no clear agenda for investment promotion and offer only very limited follow-up assistance.
- 3.43 The investment approval process itself is also fragmented. Decisions on the granting of incentives, factory space, land-use permits, visas, etc., take place at several levels and within several organizations. For example:
- a. Investment incentives are governed by two separate laws, the Fiscal Incentives Act and the International Business Companies Act. The latter is administered by the B IDC with approval of the Ministry of Industry and Commerce. The former is administered by the Ministry of Finance.
 - b. Any investor, foreign or domestic, desiring factory space in one of the B IDC-managed industrial estates must get approval from the factory space allocation committee in B IDC.
 - c. Any change in land or building use, subdivision of land, or new construction must be approved by Town and Country Planning (TCP). TCP in turn requires consultation with numerous other agencies -- the Ministry of Health, the Water Authority, the Coastal Conservation Unit and the Chief Fire Officer -- to name a few. If beach or agricultural land is in question, the approval of the Minister of Housing and Lands will also be required.
- 3.44 The obvious effect of this fragmentation is the potential for considerable confusion on the part of the potential investor. The number of windows that exist increases the likelihood that initial inquiries will be met by incomplete or conflicting information. The numerous approvals that may be needed from separate agencies will increase the time needed to complete the process without any formal monitoring or control to insure that the process is completed within a reasonable time frame.
- 3.45 Related to the problem of fragmentation is the lack of transparency in the screening of project proposals. Not only does a potential investor wish to secure timely approval, but also wants to be assured of predictability and consistency in the way laws and

regulations will be applied to the project proposal. Long before the decision to invest is made, the potential investor will seek information on the eligibility criteria for incentives, criteria for approvals, and the step-by-step process the application will follow. However, among the several layers of approvals required for an investment there is little information available to ensure that an investor knows exactly what is required in an application, who will be reviewing the requirements and what the criteria for approval will be.

- 3.46 Most unsettling to a potential investor in Barbados is the perception that several points of discretionary decision making exist at the ministerial level. Within the existing system for example, direct authorization by a minister may be needed for approval of incentives (Trade and Industry or Finance), for approval in change of land or building use (Housing and Lands), or for import licenses (Finance). Although a minister may receive recommendations from highly qualified committees or boards, he is not bound by their recommendations and no objective criteria exists for his decision. A potential investor is not particularly comforted by the fact that a minister follows the committees' recommendations 90% of the time; instead he focuses on the remaining 10% and the possibility of having his investment derailed against seemingly subjective criteria.
- 3.47 Another important component of the enabling environment that will receive special attention in the project is the Intellectual Property System (IPS). Intellectual property can be thought of as a private creation, generated by invention or expression, to which the state grants the status of property through patent, copyright, trademark or the enforcement of trade secrets. Modernization of the IPS in Barbados would enhance investor appeal. Sophisticated informatics, advanced telecommunications, local music for export, and biotechnology applied to agriculture are only several examples of activities in which a more modern IPS would spur investment.
- 3.48 The Bank and the GOB conducted a comprehensive review of the IPS in Barbados. The analysis revealed that most of the elements of the IPS -- enforcement, administration and substantive law -- are on a par with the best systems in other countries. However, at the margin there are aspects of the system which should be modernized in order to avoid any deterrent to those who would consider investing in Barbados. The intellectual property registry is experiencing serious administrative problems. Even though only a decade old, the copyright act deserves modernization. The patent act needs modernization as well as adjustment to correct the impression that pattern applications are actually examined when, in fact, they are not. The trademark act is conceptually sound, but needs adjustment to aid in its administration.
- 3.49 Proposed Action. The GOB has agreed to pursue a number of policy measures to strengthen the investment enabling environment. Foreign investment promotion and facilitation activities will be

centralized and investment approval procedures will be streamlined through administrative measures. Secondly, under the direction of the Ministry of Industry, local enterprises will be strengthened through a series of training and capacity building programs. Lastly, the intellectual property system in Barbados will be strengthened. To accomplish these objectives, the GOB will initiate activities in three discrete areas: institutional strengthening, training and capacity building and legal reforms.

- 3.50 Two new units will be created within the Ministry of Trade and International Business. The first will coordinate and execute an external image building program for Barbados, as well as industry specific investment promotion programs, the second to coordinate and provide investor facilitation services to prospective foreign investors.
- 3.51 The activities of these two units will be defined by two working groups to be coordinated by the Ministry of Trade and International Business. The first group will contain representatives from government and the private sector to develop an image building program. The second group will contain representatives from all investment approval bodies. This group will define a protocol, or set of procedures, which will guide portfolio managers in their interaction with investors and among themselves in the various ministries.
- 3.52 The formation of these two groups will be supported by a training and capacity building program. Portfolio managers within the Ministry of Trade and International Business and within the various ministries that handle approvals will be trained to respond to investor inquiries and coordinate the investment approval process. A management information system will be developed to monitor and track investor inquiries. Local enterprises will also be the beneficiary of extensive training. An outreach program will provide technical input into all aspects of operating a business enterprise in Barbados, especially in the export sector.
- 3.53 The role of the Ministry of Trade and International Business in investment promotion and facilitation will be formalized through a Cabinet Paper. There will be a mandate from the government to formalize the cooperation of all relevant ministries to operationalize the portfolio manager system. Efforts will also be made to identify and implement administrative changes to simplify the investment approval process.
- 3.54 The government has agreed to take the necessary steps to modernize the IPS. Legislation will be prepared to correct the deficiencies in copyright, patent and trademark law. The basis for the draft legislation will be the recently completed Bank/GOB study. The improvement of enforcement and administration will be the subject of technical assistance. The Bank and the GOB will jointly prepare an action plan for the strengthening of the intellectual property registry.

IV. PROGRAM FINANCING AND IMPLEMENTATION

A. The borrower and the executing agency

- 4.1 The Borrower will be the Republic of Barbados and the Ministry of Finance and Economic Affairs will be the primary executing agency. The Central Bank of Barbados will be the executing agency for the Supervision and Regulation and Securities Markets programs.

B. Disbursement and procurement

- 4.2 Proceeds from the loan will finance the Freight on Board (FOB) cost of eligible imports, or the Cost, Insurance and Freight (CIF) cost, when freight is eligible. Disbursements of the tranches will be made against import documentation provided by the executing agency. According to Bank policy, the usual restrictions contained in a negative list will apply, excluding local currency expenses, guns and other goods used by the armed forces, luxury items, and imports financed through medium- and long-term loans.
- 4.3 Procurement of goods with funds provided by the loan will be carried out in accordance with standard Bank procedures. For amounts above US\$5 million, International Competitive Bidding (ICB) will be required. In the case of petroleum and petroleum products, imports above US\$5 million from individual suppliers may not always follow the letter of Bank procedures. However, if acceptable commercial practices are followed, and transactions are effectively at market prices, their procedures will be acceptable to the Bank, as is the case in other sector adjustment operations.
- 4.4 For amounts smaller than US\$5 million, procurement by the public sector will be done in accordance with established national procedures, provided they are consistent with the Bank's procurement policy. Procurement of smaller amounts by the private sector will be done in accordance with applicable commercial practices and, whenever possible, on the basis of quotes from suppliers from at least two Bank member countries.

C. The technical support program

- 4.5 The Government will support the implementation of the reforms contained in the ISRP with an allocation of up to US\$5 million from the resources of the ISRP. The plan for the technical support program and the specific activities to be carried out are presented in Annex III. As a separate initiative, applications could be made to the Multilateral Investment Fund (MIF) to finance one or more of these activities. In such a case, the contribution of the Government to the technical support program would be correspondingly reduced.

- 4.6 The technical support contracts will be coordinated between the Government and the Bank. Terms of reference for the hiring of consultants will be drafted with inputs from both parties. The Government will draw up a short list of candidates for each contracting, which will be given to the Bank for its approval.

D. Records, audit and control

- 4.7 For each disbursement, the Executing Agency will provide documentation showing the goods imported during each period, the country of origin, and the date and value of the transaction. For purposes of accounting and control of those transactions, the Borrower shall open a special account in the Central Bank, keep accounting records of the project, prepare and forward the applications for disbursements, present lists of the transactions considered eligible and maintain all relevant supporting documentation. The Borrower shall present to the Bank, within 90 days following the disbursement of each tranche, a statement of account for such tranche, prepared in accordance with terms of reference agreed with the Bank and certified by a firm of independent public accountants designated by the Borrower and accepted by the Bank.
- 4.8 Funds for the technical support program will be deposited in a separate US dollar account at the Central Bank of Barbados, and used to pay for goods and services in accordance with a memorandum of understanding to be negotiated with the Government. This memorandum will reflect the program set out in Annex III.

E. Environmental impact of the operation

- 4.9 The environmental brief for the ISRP was considered by the Environmental Committee on May 11, 1995. The operation was classified as a category III. The CMA reviewed and approved the Environmental Summary on September 14, 1995. The environmental measures contained in the ISRP are consistent with those in other Bank projects, such as Coastal Conservation and Solid Waste. Furthermore, completion of the institutional arrangements for the environmental management unit will be accomplished by second tranche.

F. Status of compliance

- 4.10 The GOB has initiated action in the case of most of the activities relating to financial sector conditions for first tranche disbursement. Reform of the two state-owned banks is proceeding, and in the case of the Barbados National Bank, a number of concrete measures have been initiated at the BNB level which will assure compliance with all first tranche conditions by early 1996 or before. The issue of raising interest on GOB securities held by the BNB, which is the only major condition outstanding, is the responsibility of the central government (Ministry of Finance). Regarding the Barbados Development Bank, new lending operations

have effectively been discontinued; a formal wind-up plan is in preparation; measures are underway to dispose of the performing assets in a cost-effective manner; and it is expected that the BDB will terminate all operations, except management of those performing assets not yet disposed of, by year-end 1995. The creation of the two new single-purpose companies to manage the non-performing assets will likely take place during the first quarter of 1996. Selection of a consulting firm to carry out the CDB-sponsored study of the future of development finance in Barbados is underway and the results are expected prior to year-end. With respect to the amendments to the Financial Institutions Regulatory Act, a draft of the bill is under consideration by Cabinet, and it is expected that the bill will be laid before Parliament in late November or early December.

- 4.11 The GOB has made significant progress in meeting first tranche conditionality in the land-use issue area. The TOR for the strengthening of the Office of the Chief Town Planner has been agreed to between the Bank and the GOB. Representative of the Bank and the government will soon meet to revise the TOR for the PDP to include the necessary environmental considerations, and to conclude the TOR for the environmental management unit and the environmental legal and regulatory framework. A working group has been formed to revise the framework for granting land-use permissions.
- 4.12 Considerable progress has also been made in the enabling environment for private sector investment. Most of the activities in this area fall under the Ministry for International Trade and Business. The Plan for the consolidation of the promotion and facilitation activities is in draft and will be presented to Cabinet by December. The minister has prepared action plans for the two working groups and these should be formed by year-end. The Ministers of International Trade and Business and of Industry have begun to collaborate on a program of assistance to small enterprises.
- 4.13 Considering the above, the GOB should be able to complete all actions for first tranche during February-March, 1996.

V. PROBLEMS AND RISKS

- 5.1 The GOB medium-term macroeconomic policy framework calls for a contraction in domestic demand and an increase in productivity to check inflation and maintain a sustainable balance of payments position. Since the use of the exchange rate as a policy instrument has been ruled out, the GOB strategy will require fiscal austerity and an incomes policy. Such a strategy will require the full support of the social partners and if such does not materialize in full measure, the Barbadian economy will be very vulnerable to external shocks.
- 5.2 Several of the policy measures identified in this project will involve changes to the legal and regulatory system which only Parliament has the authority to approve and enact. The project team believes this risk can be well managed. The gestation period for this project, almost three years, has allowed the issues to be thoroughly vetted throughout the government and the private sector in Barbados. Consequently, the project team feels that the political risk is tempered by the considerable consensus for change that already exists in Barbados.

PROPOSED POLICY MATRIX

SUBJECT	OBJECTIVE	ACTIONS COMPLETED	MEASURES TO BE TAKEN		
			BEFORE FIRST TRANCHE	BEFORE SECOND TRANCHE	BEFORE T
MACROECONOMIC FRAMEWORK					
Medium-term Policy Framework	A macroeconomic policy framework containing among others, measures for: stabilization, incomes policy, tax reform, trade reform.	GOB has approved Medium-Term Economic Strategy for 1995-98.	<i>Satisfactory progress in the macro-policy environment which includes implementation of CARICOM tariff schedule and adherence to incomes policy. Staff consultation with IMF completed and any stabilization issues resolved.</i> <i>1/</i>	Satisfactory progress in the macro-policy environment which includes VAT in place, Caricom tariff implementation on schedule and adherence to incomes policy.	Satisfactory p macro-policy which includ implementati and adheren policy.
THE FINANCIAL SECTOR					
Systemic Risks	Privatize the BNB	Transfer of the non-performing sugar portfolio to the BACT and bonds equal in amount to the discounted value of these assets issued to the BNB.	Initiate a restructuring of the BNB. This will include: (i) Raising interest rates on GOB securities to market rates. (ii) Initiating internal loan review process. (iii) Preparing Board policy statement. (iv) Establishing interlocking directorate with BMFC.	Complete the restructuring of BNB: (i) Completion of all internal reviews and loan workout plans. (ii) Preparation of recapitalization plan. (iii) Establish compliance with FIRA. (iv) Initiate internal review of BMFC. (v) Statement of intent to privatize BNB.	Bring BNB t (i) Complete plan. (ii) Recharte Companies A (iii) Prepare other materia of at least 51
Development Finance Policy orm	Liquidate the BDB		(i) <i>Cessation of BDB operations.</i>	(i) Formal wind-up of BDB including extinguishing of its legal person.	

ns in italics are to be completed before Board presentation.

ANNEX I

Page 2 of 5

SUBJECT	OBJECTIVE	ACTIONS COMPLETED	MEASURES TO BE TAKEN		
			BEFORE FIRST TRANCHE	BEFORE SECOND TRANCHE	BEFORE THIRD TRANCHE
	Disposition of BDB Assets: performing assets nonperforming assets (class A) nonperforming assets (class B)		Reconciliation of BDB Balance Sheet: (ii) Provision for interim management of performing assets. (iii) Creation of legal and institutional arrangements for disposition of non-performing assets (Class A and B). 2/ (iv) Agreement on framework for operating plan for class A nonperforming assets.	(ii) Liquidation of performing assets complete. (iii) Transfer of secured interest in class A and B nonperforming assets to their appropriate entities. (iv) Preparation of operating plan for class A nonperforming assets complete.	(i) Liquidation of class B nonperforming assets and dissolution of respective entities. (ii) Satisfactory management of nonperforming assets according to operating plan.
	New Strategy for Development Finance		(v) Agreement on future institutional arrangements for development finance to include the following principles if there is a DFI: -- minority GOB share -- market rates -- assume entire credit risk.	(v) Adherence to agreed principles governing development finance.	(iii) Adherence to agreed principles governing development finance.
Regulation and Supervision	Strengthen the legal framework for prudential regulations of the financial sector.		<i>Agreement on new Financial Institutions Act with respect to strengthening GOB oversight of the financial system in Barbados.</i> Bill laid before Parliament.	New FIA effective.	Maintenance
Capital Markets	Allow securities markets to play a more active role in fixed capital formation in the private sector.	Removal of quantitative and interest rate controls on Central Bank rediscount facilities.	<i>Agreement on required improvements to primary and secondary government securities market.</i>	Implementation of agreed measures.	Maintenance

1 refers to certain South Coast hotels. Class B refers to all other non-performing assets.

SUBJECT	OBJECTIVE	ACTIONS COMPLETED	MEASURES TO BE TAKEN		
			BEFORE FIRST TRANCHE	BEFORE SECOND TRANCHE	BEFORE T
LAND MARKETS					
versification of Land Use	Allow a more rational use of land resources now in the rural sector subject to constraints posed by environment and water resources.	Presentation of operational and financial plan (encompassing both sugar and non-sugar assets) for the BAMC to include: --price and incentive system; --production targets; --investment program; --financial plan.	<i>Satisfactory progress in implementation of the operational and financial plan.</i>	Satisfactory progress in implementation of the operational and financial plan.	Satisfactory p implementati operational a
nd Use Policy	Create an appropriate policy framework for the exercise of land-use policy.		Approval of TOR for area development plan for the sugar estates and other rural areas. Approval of TOR for the revision of the Physical Development Plan (PDP).	Plan complete. PDP revision complete.	Satisfactory p implementati recommenda Revised PDP new land-use
regulatory Efficiency	Improve the administration of land use policy.	Approval of TOR for strengthening of the Town Planning Office. These address: --functions and mandates; --performance targets; --staffing; --data base mgmt and mapping; and --budget requirements.		Program to strengthen Town Planning Office complete.	
			Cabinet approval of a paper on the creation of an open and transparent system for granting land-use permissions. The system will provide for stronger roles for the appeals and advisory commissions.	Material and satisfactory progress in the implementation of new policy.	Satisfactory c new policy.

ANNEX I

Page 4 of 5

SUBJECT	OBJECTIVE	ACTIONS COMPLETED	MEASURES TO BE TAKEN		
			BEFORE FIRST TRANCHE	BEFORE SECOND TRANCHE	BEFORE T
Investment Promotion and Facilitation	Reduce administrative barriers to new investments.	GOB investment promotion strategy approved.	Draft plan to centralize investment promotion and facilitation activities.	Approval of new institutional framework for improved investment facilitation, promotion and approval.	Centralized investment promotion and streamlined approval procedure in
	Centralize investment promotion activities within Ministry of International Trade and Business.	GOB commitment to coordinate investment promotion activities with private sector and substantive ministries.	Create Promotion Unit within Ministry of International Trade and Business.	Promotion Unit fully operational.	Satisfactory progress in implementation, building and promotion pr
	Centralize investment facilitation activities within Ministry of International Trade and Business and to streamline approval procedures through administrative measures.	Draft plans to centralize investment facilitation and approval procedures through on-line computer network.	Create Facilitation Unit within Ministry of International Trade and Business.	Facilitation Unit fully operational based on portfolio manager system and MIS for investor facilitation and approval.	Continued satisfactory operation of facilitation service portfolio man
	Strengthen local enterprise capacity for joint venture activities with foreign investors.	Review of institutional arrangements to centralize programs to assist local enterprises.	Define and approve institutional framework to centralize or coordinate local enterprise support programs.	Institutional framework and programs fully operational.	Satisfactory progress in centralizing a of local enterprise programs.

SUBJECT	OBJECTIVE	ACTIONS COMPLETED	MEASURES TO BE TAKEN		
			BEFORE FIRST TRANCHE	BEFORE SECOND TRANCHE	BEFORE THIRD TRANCHE
B. Intellectual Property Rights	Bring intellectual property system compatible with international standards.		Approval of proposed modifications to the IPR law in: --copyright; --patent; and --trademark.	Draft legislation laid before Parliament.	New IPR law in force.
V. TECHNICAL SUPPORT COMPONENT	Assist the GOB in the implementation of policy measures contained in the ISRP.		Approval of action plan to strengthen Intellectual Property Office (Registry). Special account at Central Bank established.	Action plan implemented. Satisfactory progress in execution of the TS component.	Satisfactory operation of the IPO. Satisfactory progress in execution of the TS component.



THE PRIME MINISTER'S OFFICE
BRIDGETOWN, BARBADOS

TEL: 809-426-3179

October 16, 1995

Mr. Enrique V. Iglesias
President
Inter American Development Bank
Washington D.C. 20577
U.S.A.

Dear Mr. Iglesias,

The Government of Barbados is undertaking a programme of policy reforms designed to create a strong foundation for private sector led growth. The purpose of this letter is to describe this programme and to place it in the context of our achievements and goals for the future. Several important policy measures have already been taken. The Government of Barbados is now formally requesting the assistance of the Inter-American Development Bank in carrying out the remaining measures.

BACKGROUND

The Government will continue to implement a comprehensive economic adjustment programme to lay the foundation for sustained real growth with price stability. The stabilisation phase of this programme will continue to manage aggregate demand through appropriate fiscal and monetary policies. These policies will be supported by an incomes protocol designed to reduce the real cost structure facing domestic economic activities and improve international competitiveness, by relating increases in employee compensation to measures of productivity and enterprise profitability. The National Productivity Board will give technical support to this process.

The stabilisation phase will be complemented by comprehensive and far-reaching structural reforms aimed at restoring sustained growth in the Barbadian economy. This is to be accomplished through measures that will increase efficiency in the economy and strengthen public finances. Tax reform is high on our agenda. Changes in the direct tax structure were approved in

Mr. Enrique V. Iglesias

October 16, 1995

July, 1992. Now with technical assistance from the IMF, World Bank and the IDB the GOB will move forward to implement a value added tax to replace the current ad hoc system of indirect taxes. Further progress in trade liberalisation is also important. The Government has prepared a comprehensive package which includes a phased reduction of import tariffs to a range of 5-20%, the removal of non-tariff barriers, and adjustments in tariff exemptions and other trade concessions. Finally, the Government will rationalise public sector operations. There will be a review of public sector current and capital expenditures. The programme targeting public sector enterprises for privatisation, rehabilitation or liquidation, will continue.

The adjustment programme should allow the economy in the medium term to achieve real growth of about 3-3.5% with inflation of below 2%.

THE INVESTMENT SECTOR REFORM PROGRAMME

We realise that a successful macroeconomic adjustment programme will provide only the foundation for private sector led growth. Further efforts, sector specific measures to improve efficiency are also required. To this end, the Government has targeted three broad areas of policy reform: the financial sector, land-use and the enabling environment for private investment.

1. *The Financial Sector.* Priorities for the Government in this sector are eliminating the risks posed by the two publicly owned banks, the BNB and BDB, to the financial system, further improvements to the regulatory environment, and innovation in securities markets.

The weak financial position of the Barbados National Bank (BNB) poses the greatest obstacle to the growth and development of the financial sector in Barbados, and, consequently, to the growth of financial services to the private sector. I am pleased to report however that the single largest threat to the solvency of the bank was eliminated when non-performing loans to the sugar sector were removed from the books of the BNB and transferred to a specialised work-out entity in 1993. The year prior to this transfer, the outstanding balance of non-performing loans of this bank was equivalent to 12% of GDP. Nonetheless non-performing and poorly performing loans still represent, as of mid 1995, 40% of the BNB portfolio. This situation represents a threat to our government, which, either directly or through the

Mr. Enrique V. Iglesias

October 16, 1995

Central Bank of Barbados, may be forced to provide financial assistance to the BNB. Such assistance would imply a considerable social cost, as it would constrain the fiscal and monetary policies of our Government.

In response to the current weak position of the BNB and to the government's commitment to restructure it as a commercial bank, we propose a number of reforms which will be carried out during the execution of the sector loan. The first important task will be to improve its financial position. To this end the BNB will carry out an internal review of all loans greater than B\$50,000 (US\$25,000) and initiate a work-out plan for those which are found to be delinquent. Once this is accomplished, the institution will be able to increase loan loss reserves sufficiently to cover potential losses from troubled loans and provide for the necessary recapitalisation in light of the Basle capital adequacy standards. In addition, the government will increase the interest paid on GOB securities delivered to the BNB in exchange for the non-performing sugar and other parastatal assets which have been divested by the BNB to specialised work-out entities.

The BNB intends to strengthen its internal management and controls. It will gain more effective control over its subsidiary mortgage bank (BMFC), and initiate an internal review of this institution. The management of the BNB has established a functioning asset liability management committee. Finally, a policy statement on governance will also be prepared. Once the financial position of the BNB has been improved and its internal management has been strengthened, the government will proceed to privatise the bank. The BNB will be incorporated under the Companies Act. Subsequently, at least 51 percent of the ownership will be brought to point of sale.

In the area of development finance the government has traditionally relied upon the Barbados Development Bank to provide the small business and service sectors with term financing under favourable conditions. However more recently, due to difficult economic conditions and lax loan recovery practices, almost two thirds of the BDB's loan portfolio is in non-performing status. Cash flow and earnings are substantially negative, and projected to remain so. Without additional sources of funds, the institution will soon be starved of operating resources.

The BDB has ceased new lending operations and has initiated wind-up

Mr. Enrique V. Iglesias

October 16, 1995

proceedings. Non-performing assets will be divided into two groups and transferred to specialised loan work-out entities created for this purpose. Performing assets will be disposed of at which time the BDB will formally go out of existence.

The first group of non-performing assets consists of loans to certain unprofitable South Coast hotel properties which are seen as having potential for rehabilitation. To this end a single purpose government-owned corporation will be established to attempt to restore these properties to profitability within a fixed period of time and a fixed budgetary commitment. A separate single purpose corporation will be created to liquidate the remaining non-performing assets prior to third tranche disbursement.

As there is some question regarding the nature of a successor to the BDB, or even whether there should be any such institution at all, an assessment of the future directions for development finance in Barbados will be carried out by an international consulting firm under the sponsorship of the Caribbean Development Bank (CDB). The results of the study will be reviewed and a plan of action will be agreed upon. At the present it is not possible to specify this plan of action, however the following points will be considered.

Preliminary studies indicate that the private financial intermediaries may be able to meet the demand for development finance if technical assistance were provided and the second-tier term financing facility were improved. The government is prepared to give full consideration to this option. On the other hand, if a new first-tier development finance institution (DFI) were to be created, it would be essential that it not fall into the same difficulties as the BDB. To this end the government would insist upon certain guidelines regarding the governance and operating modalities of any possible future DFI in Barbados. These would include, not be limited to, minority government ownership to be reduced over time, assumption of entire credit risk by the DFI on its loans, and charging of market rates on all lending.

In the area of regulation and supervision, the government strengthened the legal basis with the passage of the Financial Intermediaries Regulatory Act (FIRA) in 1992. However, there are certain areas where the act is deficient, such as assigned capital for branches of foreign banks and the authority of the Supervision Department of the Central Bank in dealing with the problem of insolvent banks. These and related deficiencies are to be rectified with the

Mr. Enrique V. Iglesias

October 16, 1995

passage of a proposed "Financial Institutions Act" which will be presented to Parliament shortly.

Bank and non-bank financial intermediaries, such as credit unions, insurance companies, securities brokers, pension funds, etc. are presently regulated by a variety of unrelated government oversight agencies, or not regulated at all (e.g. the securities market). These agencies have varying capabilities to detect and take action on potentially serious problems within the institutions they respectively supervise. With assistance from outside consultants, we intend to carry out a full review of the current regulatory environment for all finance related institutions in Barbados leading to recommendations and appropriate actions for reform.

The securities market in Barbados has several deficiencies, particularly as regards its term structure. Interest rate controls, resulting in negative real rates in some years (particularly the latter half of the 1980s), and institutional restrictions have limited the development of the long-term debt market. Contractual saving is widespread and represents a major source of long-term resources; however most of these funds are invested in government paper which is held to maturity, as the secondary market is poorly developed. Based on studies already completed, we propose that a secondary market in government securities be developed largely on an over-the-counter basis and that an expert be hired to work with the Central Bank of Barbados to initiate operations in the government securities market.

The secondary market for mortgage instruments is virtually non-existent in Barbados, as banks and other institutions granting mortgage loans hold them in portfolio until maturity. We have noted with interest developments in other eastern Caribbean countries such as Trinidad and Tobago and more recently the OECS where a second-tier mortgage bank has been created. Based on these experiences, the government plans to carry out the necessary background studies and, if found feasible, to engage in a pilot project to establish a second tier bank which would purchase mortgages from commercial banks and hold them in its portfolio. It is anticipated that if its initial operations are successful, the second-tier bank could subsequently securitise these instruments and sell them in a secondary market.

2. Land-use Policy and Administration. The Government believes that

Mr. Enrique V. Iglesias

October 16, 1995

the development of efficient land markets is crucial to the long-term growth and development of Barbados. For over 300 years the pattern of land use has been dominated by plantation agriculture. Now, as the private sector adjusts to a new structure of production and exports under the medium-term adjustment programme, new land-intensive activities, such as new tourist products, will emerge. Land use policy and administration in Barbados will accommodate these demands, within the context of water availability, environmental constraints, the macroeconomic policies and the national settlement strategy.

Recognising the need for greater land market efficiency, the Government will embark on a programme to reform land use policy and to strengthen the administration of that policy. We have already made significant progress in resolving probably the most vexing problem facing land-use planning in Barbados, the restructuring of the financially troubled sugar estates and production facilities. A fiduciary agency (The Barbados Agricultural Credit Trust (BACT) has been created to manage the insolvent, indebted sugar mills and estates. These assets were purchased from the BNB after an independent audit of their performance. The BACT and its operating arm, the Barbados Agricultural Management Company (BAMC), have temporary charters, and are organised and managed specifically to insure the speedy and orderly disposition of these sugar lands and related assets with minimum disruption of sugar production and export. Those assets (estates and mills) that cannot be restructured and placed on a commercial basis will be liquidated by the agency in an orderly, but expeditious manner.

We intend to build on this success and begin implementing a three-part programme to effectively address the problems now affecting the functioning of land markets in Barbados. These are : (i) revisions to the Physical Development Plan (PDP) - supplemented by an area development plan focusing on the diversification of land-use on the sugar estates and other rural areas - providing Barbados with a new policy framework for land-use planning and the issuance of planning permissions; (ii) strengthening the Office of the Chief Town Planner; (iii) a reform of planning permission procedures. The fundamental principles that will guide these reforms are transparency in the formulation of land-use policy and openness in the application of that policy.

Mr. Enrique V. Iglesias

October 16, 1995

In order to give land-use planning a more flexible and robust policy framework, the government has decided to revise the Physical Development Plan. This will provide for more flexibility, in allocating land between agricultural and non-agricultural uses. Once revised, the PDP will be established, through amendments to the Town and Country Planning act, as standing policy. The Government has already prepared terms of reference (TOR) for the revision and these have been agreed to between us and the IDB.

The policies and strategies outlined in the physical development plan will be complemented by the preparation and adoption of a detailed area development plan. This will be initiated for the sugar estates and other rural areas, involving cooperative effort of Government, landowners and the Barbados Agricultural Credit Trust/Barbados Agricultural Management Company. The purpose of this planning exercise is to allow a more rational allocation of land resources now in the rural sector in the context of a sustainable agriculture base, resource conservation, and the financial obligations of the heavily indebted estates. The area development plan will be adopted following preparation of the draft Physical Development Plan, and consistency between the two will be assured.

The Government intends to review, and if necessary revise, the previously stated policy of reserving 45,000 acres of agricultural land when the Physical Development Plan and the Area Development Plans have been completed and adopted. A new allocation will be determined based on the long-term future of agriculture. The revised PDP shall identify a set of policy guidelines for the use, development and management of any excess lands.

In order to give a high policy standing to the PDP, we intend to introduce amendments to the Town and Country Planning Act. These will specify new procedures whereby Plan amendments are proposed, reviewed and adopted, and will provide for formal opportunities for technical and public review.

At the same time that a new land-use policy framework is being put in place, we will move to strengthen the administration of that policy. The first step in that direction will be to augment the Office of the Chief Town Planner. Based on a comprehensive audit of the Town Planning Office, staffing and budget requirement will be adjusted to increase capabilities to review and process planning applications. This task is already well advanced with terms of

Mr. Enrique V. Iglesias

October 16, 1995

reference and recommendations already agreed to between the Government and your institution.

The second, and probably the most crucial, step in improving land-use administration will be in several amendments to the Town and Country Planning Act providing for revised administrative procedures for granting land-use permits. The most important changes to current procedures will be to add institutional depth to the review process, to improve transparency, and permit a greater degree of public participation in the process of determining planning applications. We anticipate that many planning applications, if found consistent with standing policy and/or regulations, will be routinely approved by administrative action of the Chief Town Planner. Unlike current procedure, however, the statutory consultations with recommendations that accompany such decisions will be accessible to the applicant and general public. The Government is considering having the Planning Advisory Committee (PAC) assume a stronger role in planning decisions. The exact nature of that role, along with procedures for its implementation, shall be the subject to an in-depth review. Finally, there will be a transparent and more rigorous appeals process. To further this objective, appeals panelists will be more carefully selected and training will be provided to enable them to render more careful and considered opinions.

These reforms will necessarily change the role which the Minister plays in the administration of land-use policy. Since governance in a small island nation has a very personal character, we feel that the minister should play a strong role. At the same time, however, the current right of the Minister to call in and determine categories of applications should be modified. In the future, the Minister will be able to call in applications on an individual basis only, after due gazetting, and the reasons for the Minister's decision as well as the comments from statutory consultations will be available to the public.

3. Environmental Management. We wish to strongly emphasise at this point that the new policies regarding land-use will operate within the context of environmental and water resource constraints, the macroeconomic policy of government, and the national settlement strategy for the Island. This will be achieved, partly, through an environmental planning review which, during periodic revisions of the Physical Development Plan, adverse environmental impact resulting from future land use will be identified and addressed.

Mr. Enrique V. Iglesias

October 16, 1995

Furthermore, to insure that environmental considerations are met in any land-use allocation, we intend to create, with technical assistance provided by your institution, an environmental regulatory framework. An environmental management unit will be empowered under law to draft environmental regulations and will be given powers of enforcement and sanction.

4. Enabling Environment for Private Sector Investment. The Government recognises the very important role that trade and investment policy will play in the long-term growth and development of Barbados. Indeed, our medium-term adjustment programme lays the foundation for an open economy. Our intention is now to create more efficient institutional arrangements to attract foreign investors and stimulate national investment. Several important steps have already been taken in this regard. A new ministry, the Ministry of International Trade and Business, has been established. Recently, the Government issued a policy statement setting priority on foreign direct investment as a principal area of focus to stimulate economic growth and outlining a number of strategic areas, mainly information technology, where foreign investment will be targeted. We feel that much of the uncertainty and lack of confidence that marked the investment climate in the past has given way to greater public-private cooperation in setting goals for the economy.

Our next goal is to establish a more robust institutional and regulatory framework to support investment activities. The ultimate objective is to possess a transparent regulatory environment under one authority serving all functions relating to new investments: (i) investment promotion; (ii) investment facilitation such as screening investment proposals and advisory services to help entrepreneurs prepare project documentation; and (iii) post-investment assistance such as helping the new investor secure the many required approvals. During the next several years we intend to take several significant steps in this direction. First, two units will be created within the new Ministry of International Trade and Business, the first to create an external image building programme for Barbados, the second to provide facilitation services to prospective investors. This latter unit will contain portfolio managers who will interact with prospective investors, as well as with their counterparts in the various agencies and ministries that grant approvals, all with the purpose of guiding the new investor through the many stages to final start-up of the new business. Second, a management information system will be developed to monitor and tract investor activities. Next, under the

Mr. Enrique V. Iglesias

October 16, 1995

direction of the Ministry of Industry, we will develop a programme to strengthen local businesses to make them more attractive partners for foreign investors. Lastly, we plan to review the laws and regulations governing investment with an eye to simplification and streamlining. Working groups will be established from among the relevant ministries to devise the appropriate protocols.

Another important component of the enabling environment is the intellectual property rights system. Modernisation of this system through appropriate legislative changes, and improvements in institutional arrangements will enhance Barbados' investor appeal.

We understand that a technical support component will be included in the Investment Sector Reform Programme to provide us with the assistance that we require in carrying out the activities that are discussed above. We welcome this support, and are committed to the execution of this component in a timely fashion so as not to delay the implementation of the schedule of policy reform.



Owen Arthur

Prime Minister

Minister of Finance and Economic Affairs

TECHNICAL SUPPORT FOR THE INVESTMENT SECTOR REFORM PROGRAM

I. INTRODUCTION

During the execution of this operation, it will be necessary to provide the GOB with technical support in order to meet the objectives of the program. For this purpose the Government will require US\$5.0 million to finance the contracting of consulting services. The funding for these activities is contained in the proposed loan. The Central Bank of Barbados will be the executing agency for those activities relating to regulation and supervision and securities markets. The Ministry of Finance and Economic Affairs will be the executing agency for all others.

The financial resources for technical support (US\$5.0 million) will be transferred to the GOB as part of the first tranche disbursement. These monies will be deposited in an escrow account at the Central Bank of Barbados for the use of the Central Bank and the Ministry of Finance in carrying out the activities outlined in this annex. Before these are drawn down, however, there will be prior agreement in each instance between the GOB and the IDB. The Public Investment Unit at the Ministry of Finance, or the respective department at the Central Bank, will present to the Country Office the TOR, budget and the short list of eligible consultants. Once these are approved by the Bank, written correspondence to that effect, and authorizing the disbursement of funds from the escrow account, will be sent to the GOB.

II. DESCRIPTION

The following areas will receive support under technical assistance:

A. Macroeconomic monitoring

The Statistical Services Department will be strengthened to insure that information is available on a timely basis for policy formulation and, important for this project, for monitoring performance under the medium-term adjustment program.

B. Financial sector

1. Restructuring the BNB

The BNB will be restructured into a viable commercial bank. A thorough review of all loans will be made. Management will be strengthened through the establishment of an asset/liability committee and the development of new internal procedures. The Bank will be recapitalized and brought to point of sale.

2. New directions for development finance

The BDB will initiate wind-up procedures for the permanent closure of the institution. Performing assets will be managed and eventually sold. Non-performing assets relating to the South Coast hotels will be placed in a management unit. Other non-performing assets will be placed in a work-out unit. A series of studies will be performed to determine the best direction for development finance.

3. Regulation and supervision

A study will be initiated to determine the best manner to bring non-bank financial intermediaries under the regulatory regime.

4. Securities markets

Consultants will assist the Central Bank in designing an over-the-counter market for government securities. The best manner for developing a secondary mortgage market will also be studied.

C. Land-use planning and administration

1. Environmental management

A legal and regulatory framework for environmental management will be established. Based on a national database of natural resources policy priorities will be formulated. A legislative and administrative framework for environmental management will be created for substantive law, regulations and effective enforcement. Finally, the environmental management unit will be strengthened.

2. National park system

A comprehensive development and management plan for a national park system will be established. The plan will specifically address land based parks on the north, east and southeast coasts, along with a national marine park.

2. Land-use policy and planning

Technical assistance will be provided to develop a revised framework for land-use policy and planning. The new framework will seek to make environmental impact evaluations an integral part of physical development projects. A new Physical Development Plan, supplemented by an area development plan for the rural areas, will be prepared. The Office of the Chief Town Planner will be strengthened.

D. The enabling environment for private sector investment

1. Training and capacity building

Investment promotion techniques will be strengthened within the Ministry of Trade and International Business. A system of portfolio managers will be introduced into the Ministry of Trade and International Business as well as into the ministries and agencies that process approvals for new investments. A management information system will be installed in the Ministry of Trade and International Business to track and monitor prospective foreign investors. An outreach service for SME development will be established in the Ministry of Industry.

2. Administrative and Regulatory

Administrative and Regulatory changes to expedite the investment approval process will be identified.

TECHNICAL SUPPORT PROGRAM SUMMARY			
AREA OF REFORM	OBJECTIVE	BUDGET ESTIMATES	\$ TOTAL
Macroeconomic Monitoring	Support the strengthening of the Statistical Services Department.	Three information specialists	100,000
BNB restructuring	Support the transformation of the BNB into a viable commercial bank.	Portfolio review--350,000 Work-out plan--100,000 Develop credit policy and manuals--50,000 Privatization plan--100,000	600,000
Wind-up of BDB	Support the orderly closure of BDB and the disposition of its assets.	Disposition of performing assets--100,000 Disposition of non-performing assets, class A--300,000 Disposition of non-performing assets, class B --300,000 New directions in development finance--400,000	1,100,000
Regulation and Supervision	Diagnosis of future needs of the regulatory regime.	Study of non-bank financial intermediaries	400,000
Capital Markets	Support new features to the securities market.	Government securities market--250,000 Secondary mortgage market--300,000	550,000
Land-use Policy and Planning	Strengthen the Office of the CTP and revise PDP.	Urban planning-- 200,000 Resource surveys--150,000 Coastal surveys--150,000	500,000
Natural Resource Management	Support plan for public use of lands and the execution of the area development plan.	Parks planning--300,000, Coastal conservation--200,000 Agricultural resource survey'--300,000	800,000
Legal and Institutional Framework	Support the development of environmental law and the strengthening of the environmental management unit.	Legal drafting--150,000 Environmental management--325,000	475,000
Enabling Environment for Private Sector Investment	To consolidate investment promotion and facilitation and to simplify the approval process.	Institutional strengthening--125,000 Training and capacity building--300,000 Legal reform--50,000	475,000
TOTAL			5,000,000

SPECIAL CONTRACTUAL CONDITIONS

Set forth below is a list of conditions which are to be fulfilled by the Borrower to the Bank's satisfaction prior to the release of the indicated tranches.

The policy conditions prior to Board Presentation are:

A. The Macroeconomic Framework

Performance under the Medium Term Macroeconomic Policy Framework of the Borrower is consistent with the objective of the program. This will include adherence to the agreed CARICOM tariff implementation schedule and to the incomes protocol currently in effect.

B. The Financial Sector

1. All BDB credit operations have ceased.
2. The draft Financial Institutions Bill to repeal and replace the existing Financial Institutions Regulatory Act has been prepared for presentation to Cabinet. This draft includes *inter-alia* the following provisions: (1) assigned capital of branch banks; (2) empowering CBB to initiate winding up provisions; (3) allowing CBB to intervene troubled institutions without time limits.
3. Agreement has been reached on improvements to the primary and secondary government securities markets.

C. Non-Financial Sector

Satisfactory progress has been achieved in the implementation of the operational plan (encompassing both sugar and non-sugar assets) for the BAMC.

Policy Conditions to be completed for the first tranche disbursement are:

D. The Macroeconomic Framework

1. Performance under the Medium Term Macroeconomic Policy Framework of the Borrower is consistent with the objectives of the Program. This will include adherence to the agreed CARICOM tariff implementation schedule and to the incomes protocol currently in effect.

E. The Financial Sector

1. The restructuring of the Barbados National Bank (BNB) has been initiated.
2. The interest rates on Government of Barbados (GOB) securities in BNB asset portfolio have been raised to market rates.
3. The BNB internal loan review process has been initiated.
4. A policy statement to guide BNB Board procedures has been prepared.
5. An interlocking directorate between the BNB and the Barbados Mortgage Finance Corporation (BMFC) has been established.
6. All Barbados Development Bank (BDB) credit operations have ceased.
7. Provisions are in place for management of all BDB performing assets.
8. The legal and institutional arrangements have been made for disposition of the BDB non-performing assets relating to South Coast hotels, including agreement on the operating plan for the management of these properties. A commitment by the Government to limit expenditure to an agreed level has been made.
9. The legal and institutional arrangements for disposition of all other BDB non-performing assets are in place.
10. An agreement has been reached on future institutional arrangements for development finance.
11. The Financial Institutions Bill to repeal and replace the existing Financial Institutions Regulatory Act has been laid before Parliament. This bill will include *inter-alia* the following provisions: (1) assigned capital of branch banks; (2) empowering the Central Bank of Barbados (CBB) to initiate winding up provisions; (3) allowing the CBB to intervene troubled institutions without time limits.
12. An agreement has been reached on improvements to be made to primary and secondary government securities markets.

F. Non-Financial Sectors

1. Satisfactory progress has been made in the implementation of the operational plan (encompassing both sugar and non-sugar assets) for the Barbados Agricultural Management Company (BAMC) to include *inter-alia*: (1) a price and incentive

system; (2) production targets; (3) an investment program; and (4) a financial plan.

2. An agreement has been reached regarding the terms of reference (TOR) for an area development plan for the sugar estates and other rural areas.
3. An agreement has been reached regarding the TOR for the revision of the Physical Development Plan (PDP).
4. An agreement has been reached regarding the TOR, and referenced studies have been initiated, for the creation of a more open and transparent system for granting land-use decisions providing for stronger roles for the Appeals and Advisory Commissions, with specific recommendations for their prompt implementation.
5. A draft plan has been completed to centralize foreign investment promotion and facilitation activities in the Ministry of International Trade and Business.
6. A foreign investment promotion unit has been created within the Ministry of International Trade and Business.
7. A foreign investment facilitation unit has been created within the Ministry of International Trade and Business.
8. An institutional framework has been created to coordinate local enterprise support programs.
9. A draft bill for the revision of intellectual property rights (IPR) legislation has been approved for introduction to Parliament.
10. An action plan to strengthen the intellectual property registry has been approved.
11. A special account has been established for the management of the Technical Support Component.

G. The Policy Letter. Satisfactory progress in meeting terms of the Policy Letter.

Policy Conditions to be completed for the second tranche disbursement are:

H. The Macroeconomic Framework

Performance under the Medium Term Macroeconomic Policy Framework continues to be consistent with the objectives of the Program. This will include adherence to the agreed Caricom tariff implementation schedule, adherence to the current incomes protocol and implementation of the Value Added Tax (VAT).

I. The Financial Sector

1. All internal reviews and loan workout plans for the BNB have been completed.
2. A recapitalization plan for the BNB has been prepared.
3. Negotiations have been completed regarding timing of BNB compliance with the new Financial Institutions Act (FIA).
4. The internal review of the BMFC has been initiated.
5. A statement of intent to privatize the BNB has been made.
6. The loan loss reserves of the BNB are sufficient to cover potential losses from troubled loans.
7. Written responses have been prepared by the BNB management for its Board on internal and external audits.
8. The formal wind-up of the BDB has been completed including its dissolution.
9. All BDB performing assets have been sold.
10. All categories of the BDB non-performing assets (including corresponding security interest thereto) and liabilities have been transferred to the respective entities.
11. The operating plan for South Coast hotels continues to be implemented satisfactorily.
12. The agreed principles governing the future of development finance continue to be followed.
13. The new FIA has entered into force.
14. The agreed measures strengthening primary and secondary government securities markets have been implemented.

J. Non-Financial Sectors

1. Satisfactory progress continues to be made in the implementation of the operational plan (encompassing both sugar and non-sugar assets) for the BAMC.
2. The area development plan for sugar estates and other rural areas has been completed.
3. The first draft of the revised PDP has been completed.
4. The strengthening of the Town and Country Planning Development Office has been completed.

5. Satisfactory progress has been made in the development of a new policy for making land-use decisions.
 6. The Cabinet has approved the new institutional framework for foreign investment promotion, facilitation and approval.
 7. The promotion unit within the Ministry of International Trade and Business has become fully operational.
 8. The facilitation unit in the Ministry of International Trade and Business has become fully operational.
 9. The institutional framework and programs for local enterprise development have become fully operational.
 10. The draft IPR legislation has been laid before Parliament.
 11. The action plan to strengthen the intellectual property registry has been implemented.
- K. The Policy Letter. Satisfactory progress continues in meeting the terms of the Policy Letter.

Policy Conditions to be completed for the third tranche disbursement are:

L. The Macroeconomic Framework

Performance under the Medium Term Macroeconomic Policy Framework continues to be consistent with the objectives of the Program. This will include adherence to the agreed Caricom tariff implementation schedule, adherence to the current incomes protocol and implementation of the Value Added Tax (VAT).

M. The Financial Sector

1. The following actions to bring the BNB to point of sale have been achieved: (1) complete recapitalization plan; (2) incorporation of the BNB under the Companies Act; (3) preparation of a prospectus and other material for divestiture of at least 51% of ownership.
2. The liquidation and/or sale of all the BDB nonperforming assets other than those relegated to the South Coast hotel management group has been completed.
3. Satisfactory progress continues in the management of the South Coast hotel assets.
4. The new FIA and its associated regulations remain in force.
5. The agreed performance targets relating to government securities markets have been achieved.

N. Non-Financial Sectors

1. Satisfactory progress has been achieved in the implementation of the operational plan (encompassing both sugar and non-sugar assets) for the BAMC.
 2. Satisfactory progress has been achieved in the implementation of the area development plan recommendations.
 3. The revised PDP has been adopted under the Town and Country Planning Act.
 4. Satisfactory compliance has been achieved with the new policy for making land-use decisions.
 5. The approved policy centralizing investment promotion, and facilitating and streamlining approval procedures, has been put into effect.
 6. The operation of the investor facilitation unit continues to be satisfactory.
 7. Progress in implementing local enterprise support programs continues to be satisfactory.
 8. New intellectual property rights legislation and associated regulations have become effective.
 9. Satisfactory operation of the intellectual property registry continues.
0. The Policy Letter. Satisfactory progress continues in meeting the terms of the Policy Letter.

PROPOSED RESOLUTION

BARBADOS. LOAN ____/OC-BA TO THE REPUBLIC OF BARBADOS
(Investment Sector Reform 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 Republic of Barbados, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a Investment Sector Reform Program. Such financing will be for the amount of up to US\$35,000,000 or its equivalent in other currencies, except that of Barbados, which are part of the Ordinary Capital resources of the Bank, and will be subject to the "Special Contractual Conditions" and the "Terms and Financial Conditions" of the Executive Summary of the Loan Proposal.