Public Disclosure Authorized

Program Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 25-Oct-2019 | Report No: PIDA27903

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BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Grenada	P167748	Grenada Second Fiscal Resilience and Blue Growth Development Policy Credit (P167748)	P164289
Region	**Estimated Board Date**	**Practice Area (Lead)**	**Financing Instrument**
LATIN AMERICA AND CARIBBEAN	17-Dec-2019	Macroeconomics, Trade and Investment	Development Policy Financing
Borrower(s)	**Implementing Agency**		
Grenada	Ministry of Finance, Planning, Economic Development & Physical Development		

Proposed Development Objective(s)

The series' Program Development Objectives are to: (i) support long-term fiscal sustainability and strengthen fiscal resilience; and (ii) support Grenada's transition to a Blue Economy by strengthening marine and coastal management, marine ecosystem health, and climate resilience.

Financing (in US$, Millions)

SUMMARY

Total Financing	20.00

DETAILS

Total World Bank Group Financing	20.00
World Bank Lending	20.00

Decision

The review did authorize the team to appraise and negotiate

B. Introduction and Context

Country Context

Grenada has made significant progress towards achieving fiscal sustainability and the country's macroeconomic framework is adequate for the budget support operation. The global financial crisis and the subsequent recession in many high-income countries affected Grenada's economic performance through the strong reliance on the tourism sector, resulting in steep declines in real GDP, which combined with a sustained pro-cyclical fiscal policy stance led to an abrupt rise in public debt. The subsequent adjustment program, focused on significant fiscal consolidation in the absence of independent monetary policy, helped to stabilize the economy. Successful debt restructuring and consistent primary balances averaging about 5 percent of GDP for four consecutive years have caused the public debt stock to drop from 107 percent of GDP in 2013 to 63 percent in 2018. With the fiscal adjustment program largely completed, there is a need to consolidate the hard-won fiscal gains and strengthen institutions to continuously promote fiscal sustainability and diversify sources of growth. The currency peg to the U.S. Dollar emphasizes the importance of prudent fiscal policy. In this context, the fiscal rule adopted in 2015 is expected to provide a critical anchor for macroeconomic sustainability in the context of frequent shocks. While Grenada's macroeconomic outlook is generally positive, the exogenous macroeconomic risks are tied to Grenada's small economy, which is highly vulnerable to shifts in external demand, and to its geographical location, which exposes it to very high risks of extreme climate and weather-related shocks.

Grenada's economic performance in the last two decades highlights the importance of transitioning to a new blue growth model while strengthening resilience to shocks, including those resulting from climate change. The size of the country and its geographic location expose it to high volatility stemming from the external environment both in terms of macroeconomic risks as well as weather and climate-change related events. Grenada is a small island economy with a population of around 107,000 people and GDP per capita of around US$10,517. Its marine and coastal ecosystems provide a wide array of goods and services that contribute to the country's economy. In addition to facing pressure from natural forces and human activities, the impacts of climate change, in particular sea level rise, inundation, erosion, and storm surge will magnify pressures on Grenada's marine and coastal ecosystems. For example, Hurricane Ivan in 2004 and Hurricane Emily in 2005 caused damages estimated at 148 percent and 30 percent of Gross Domestic Product (GDP), respectively.

The proposed Development Policy Credit (DPC) is the second operation in a programmatic series of two, aimed at supporting Grenada's efforts to advance the country's fiscal resilience and blue growth. The operation supports the implementation of policy and institutional reforms set out in the Government's long-term development strategy, the New Economy Plan (NEP), the Growth and Poverty Reduction Strategy (GPRS) for 2014-18, and Grenada's Blue Growth and Coastal Master Plan. The Government's programs prioritize fiscal sustainability, strengthening resilience against natural disasters, and harnessing the economy as a way to fuel blue growth.

Relationship to CPF

The proposed DPC is aligned with key policy and institutional reforms defined in the Government's development strategies and plans. It is also aligned with the World Bank's OECS Regional Partnership Strategy (RPS), and the priorities and recommendations of the WBG Small States Roadmap, including the predictability of affordable financing, measures to support debt sustainability and access to new climate financing, and diversification of small states' economies.

C. Proposed Development Objective(s)

The series' Program Development Objectives are to: (i) Support long-term fiscal sustainability and strengthen fiscal resilience; and (ii) Support Grenada's transition to a Blue Economy by strengthening marine and coastal management, marine ecosystem health, and climate resilience.

Key Results

The fiscal measures supported by the DPC are expected to ensure continued adherence to the fiscal rules and improve fiscal resilience to shocks. The DPC helps to ensure compliance with the fiscal rule on public sector wage bill ceiling, leads to efficiency improvements in post-clearance audits and other customs procedures, as well as enhanced transparency and accountability of the state-owned-enterprise sector. Measures supporting climate resilience and blue growth are expected to help restore the health and management of the marine and coastal areas and help to address the harmful effects of non-biodegradable products on the marine and coastal environment.

D. Project Description

The DPC is the second in a series of two lending operations aimed at supporting Grenada's efforts to maintain fiscal discipline and support the transition to a blue growth model. The DPC series builds on the success of the Government's reform efforts to regain fiscal discipline and macroeconomic stability, and to strengthen long term macroeconomic and fiscal sustainability. In this context, the reforms foreseen in the DPC2 constitute the continuation of the fiscal reform agenda by putting emphasis on consolidating the gains of fiscal adjustment and supporting implementation of the effective fiscal framework. In addition, this series supports critical policy and institutional reforms to help Grenada harness the potential of its blue economy in ways that promote economic growth, social inclusion, and the preservation or improvement of livelihoods while at the same time ensuring environmental sustainability of the oceans and coastal areas.

Supporting fiscal measures and compliance with the Fiscal Responsibility Law is a key Government priority. In the absence of monetary policy, the issues related to fiscal sustainability are of critical importance. While Grenada has successfully stabilized the economy and maintained fiscal discipline over the past few years, the question of sustainability over the medium and long term remains critical. In this context, the reform measures supported by the DPC2 are geared towards strengthening systems and institutions for fiscal sustainability. Specifically, reforms aim to build fiscal buffers against natural disasters through the operationalization of the contingency fund; strengthen wage bill sustainability through a new wage negotiation framework that incorporates principles of fiscal sustainability and budget affordability; improve customs and excise operations; and strengthen transparency and risk monitoring of the SOE sector.

Further progress towards growing a blue economy, by strengthening marine and coastal management and climate

resilience is crucial for Grenada's development. Grenada's extensive coastline and sea area offer significant resources for driving economic growth. The marine and coastal ecosystems provide a wide array of goods and services – such as seafood, tourism and recreation, transportation, and coastal protection – that contribute to fuel the country's economy, to reduce the country's vulnerability to natural disasters, and to promote sustainable livelihoods. However, those assets are undermined by unsustainable practices, including poorly planned coastal development, land-based and marine pollution, and unsustainable fishing, agriculture, energy and unplanned and unregulated tourism and construction activities. Climate change impacts, such as sea level rise, storm surges and increased occurrences of extreme weather events, exacerbate the pressures on marine and coastal ecosystems. Extreme weather events, particularly hurricanes and tropical storms, also disrupt livelihoods and economic production, destroy physical infrastructure, and impose high public and private costs for reconstruction and rehabilitation. Moreover, most development and infrastructure in Grenada are concentrated on the coast, and significant populations live in low-lying coastal areas. In this context, the Government has embarked on various reforms to ensure sustainable use of natural resources, while increasing adaptation and resilience to the impacts of climate change.

E. Implementation

Institutional and Implementation Arrangements

Monitoring of the operation will be conducted by the Ministry of Finance, Planning, Economic Development & Physical Development (MOF). The World Bank will support the monitoring through the supervision missions embedded in the ongoing policy dialogue. The Ministry, through the Office of the Permanent Secretary and the Macro Policy Unit, has adequate capacity and is responsible for monitoring the program and all associated outcome indicators. In addition, selected components of the DPC program will be supported through the technical assistance engagement.

F. Poverty and Social Impacts and Environmental Aspects

Poverty and Social Impacts

The poverty and social impact of the policy measures supported by this DPC is expected to be neutral in the short term and positive in the medium term. Prior actions under Pillar 1 are not expected to have direct impacts on poverty. However, the policies are expected to have positive indirect impacts on poverty through accountability in fiscal management. Prior actions under Pillar 2 are expected to have positive impacts on the poor and the vulnerable by promoting sustainability of marine ecosystem. In addition, policies aimed at decreasing contamination from plastic and Styrofoam are expected to improve the welfare of Grenadians, particularly in coastal communities.

Environmental Aspects

Policies supported by the proposed DPC are not expected to have significant negative effects on the environment, forests and natural resources. Policies under Pillar 1 are expected to lead to a more efficient use of public resources, particularly through enhanced tax collection and compensation systems and more resilient public finances. In combination with improved management of fiscal risks stemming from natural hazards, these are expected to have positive, albeit difficult to quantify, effects on the environment. Under Pillar 2, policies aimed at supporting Grenada's transition to a blue economy by strengthening marine and coastal management, marine ecosystem health, and climate resilience are expected to have significant positive environmental effects.

G. Risks and Mitigation

Risks to achieving the program objectives are considered substantial. Macroeconomic risks are related to Grenada's small economy, which is highly vulnerable to shifts in external demand, which exposes it to very high risks of extreme climate and weather-related shocks. While Grenada's institutional and technical capacity is relatively robust by regional standards, a limited number of technical experts in core ministries, and scarce fiscal resources may pose risks to implementing the reforms supported by the DPC series. Stakeholders risks are also elevated, given that some of the DPC policy measures are politically sensitive and may get influenced by the ongoing discussions between the Government and the trade unions. Finally, Grenada is inherently vulnerable to natural disasters and climate change, which could have adverse effects on certain aspects of the program. The high costs of disaster mitigation and response could strain the public resource envelope, delaying the country's progress toward fiscal sustainability and diverting scarce financing away from long-term development objectives, or increasing indebtedness. The Government has been proactive in mitigating these risks. The rules-based fiscal policy framework enshrined in the law and a fiscal council for further oversight are important elements of fiscal architecture. Ex ante disaster risk financing through the Contingency Fund and arrangements for the Bank's contingent credit line provide a fiscal buffer, while the inclusion of natural disaster clauses in the debt restructuring agreements should help mitigate the risk to fiscal stability in the event of natural disasters. Ongoing capacity building initiatives and the technical assistance are aimed to help mitigate the institutional capacity risks, while stakeholders risks are being addressed through the consultative reform process in Grenada and the commitments under the Social Compact.

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APPROVAL

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