July 2006
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Grenada: Request for a Three-Year Arrangement Under the Poverty Reduction and Growth Facility—Staff Report; and Press Release on the Executive Board Discussion

In the context of a request for a three-year arrangement under the Poverty Reduction and Growth Facility, the following documents have been released and are included in this package:

- the staff report for a Request for a Three-Year Arrangement Under the Poverty Reduction and Growth Facility, prepared by a staff team of the IMF, following discussions that ended on December 7, 2005, the officials of Grenada on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on March 31, 2006. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a Press Release summarizing the views of the Executive Board as expressed during its April 17, 2006 discussion of the staff report that completed the request and or review.

The documents listed below have been or will be separately released.

Interim Poverty Reduction Strategy Paper
Joint Staff Advisory Note of the Interim Poverty Reduction Strategy Paper
Letter of Intent sent to the IMF by the authorities of Grenada*
Memorandum of Economic Policies by the authorities of Grenada*
Technical Memorandum of Understanding*
*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

GRENADA

Request for a Three-Year Arrangement Under the Poverty Reduction and Growth Facility

Prepared by Western Hemisphere Department
(In consultation with other departments)

Approved by José Fajgenbaum and Matthew Fisher

March 31, 2006

- **Context**. Grenada is recovering from the devastating effects of Hurricanes Ivan (September 2004) and Emily (July 2005). Economic developments prior to Ivan and the changes in policies and priorities that it engendered are discussed in the July 2005 Staff Report for the Article IV consultation: http://www.imf.org/external/pubs/ft/scr/2005/cr05290.pdf.
- **Use of Fund Resources.** In support of their economic and financial policies, the Grenadian authorities are requesting a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF). Access under the arrangement is proposed at 90 percent of quota. An initial disbursement of SDR 1.56 million becomes available on approval of this request.
- **Recent Fund Support**. Two purchases under the Fund's policy on emergency assistance for natural disasters of SDR 2.9 million (25 percent of quota) each were approved in January 2003 (following tropical storm Lili) and November 2004 (following Hurricane Ivan).
- **Discussions**. Staff visited St. George's in October and December, 2005 and met with Prime Minister Keith Mitchell, Deputy Prime Minister Gregory Bowen, Minister of Finance Anthony Boatswain, incoming and outgoing Permanent Secretaries in the Ministry of Finance (respectively) Lennox T. Andrews and Timothy N. J. Antoine, other senior officials and representatives of the banking and business communities as well as trade union officials.
- **Staff**. The mission team comprised Abebe Aemro Selassie (Head), Rishi Goyal, and Werner Keller (all WHD), Prakash Loungani (EXR), David Hofman (PDR), Yu Ching Wong (FIN), and Timothy Muzondo (FAD). Paul Jenkins (OED) and staff of the ECCB and CDB also participated in the discussions. Ratna Sahay attended the final discussions.
- **Exchange Regime.** Grenada is a member of the Eastern Caribbean Currency Union (ECCU), which has a common currency, the Eastern Caribbean dollar, that has been pegged to the U.S. dollar at US$1=EC$2.70 since July 1976. The country has accepted the obligations of Article VIII, Sections 2, 3 and 4, and maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.

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EXECUTIVE SUMMARY

Background. A modest economic recovery is underway from the devastating effects of Hurricanes Ivan (September 2004) and Emily (July 2005). Economic growth rebounded to an estimated 1½ percent, after a drop of 3 percent in 2004, with brisk activity in the construction sector offsetting the slowdown in agriculture and tourism. Near-term growth prospects are good, reflecting ongoing construction activity and the expected recovery in tourism. Following a 45 percent increase in domestic fuel prices, inflation reached 6 percent at end-2005. Second-round price increases have, however, been limited, and inflation is expected to decline in the coming months.

The Authorities' Program. The authorities have used the 2006 budget to launch a comprehensive medium-term economic reform program, with the following key objectives:

- ***Fiscal adjustment***. The program aims to sharply reduce public debt from its present inordinately high level (128 percent of GDP at end-2005). To this end, a primary surplus of 2½ percent of GDP is targeted by 2008, requiring an underlying primary adjustment of some 4½ percentage points of GDP. This shift in the fiscal stance will be phased in over the next three years to accommodate the large reconstruction-related spending needs in 2006 and 2007, and will be underpinned by structural fiscal measures already identified in the program.

- ***Structural policies***. The first year of the program targets measures to improve the investment climate, and the second and third years are expected to focus on removing policy-induced distortions in the labor and financial markets.

- ***Reducing vulnerabilities***. The authorities are committed to reducing vulnerabilities from extreme weather events and weaknesses in the regulatory framework of the financial sector.

- ***Social development agenda***. The fiscal measures under the program make room for increased social spending. The authorities have prepared a poverty eradication strategy, being submitted to the Boards of the Fund and Bank as the country's Interim-PRSP.

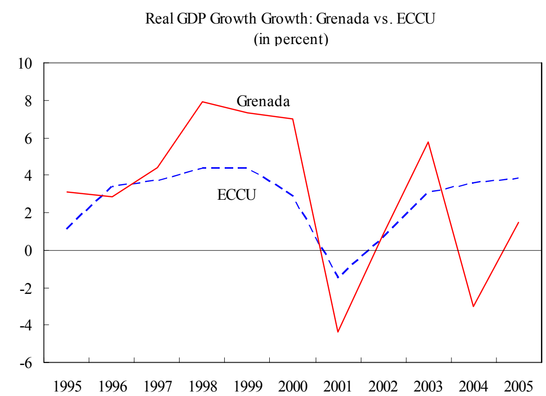
Risks. The main risks to the program relate to the outlook for the external accounts, policy slippages, higher output growth failing to materialize, and weak implementation capacity. These risks are addressed through the program's focus on reducing vulnerabilities.

Assessment. Much now depends on the implementation of the agreed policies. Providing the reforms are advanced, the program should help improve the economy's resilience to shocks and restore debt and fiscal sustainability.

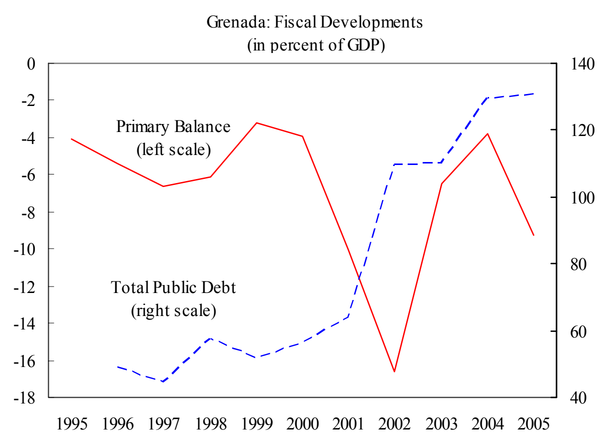
Arrangement. Access under the arrangement is proposed at 90 percent of quota. An initial disbursement of SDR 1.56 million becomes available on approval of this request.

I. Context for Reform

1. **Grenada has been buffeted by a series of exogenous shocks in recent years**. In September 2004, Hurricane Ivan caused unprecedented damage of 200 percent of GDP. And the recovery from the devastation wrought by Ivan was set back by the impact of Hurricane Emily in July 2005, which caused additional damage (mainly in rural areas) estimated at 12 percent of GDP (Box 1). In conjunction with earlier shocks—the September 11 attacks in the United States (which caused a sharp drop in tourism) and tropical storm Lili in 2002 (which depressed agricultural exports)—these events have hampered effective policy implementation and caused output to fluctuate sharply in recent years (Table 1 and Figure 1). The recent increase in international oil prices has caused further hardship.



2. **The shocks have exacerbated the already tenuous fiscal situation, and amplified the need for reforms to reduce vulnerabilities.** Hurricanes Ivan and Emily hit the island against the backdrop of large (albeit narrowing) fiscal imbalances and a growing public debt burden—in part a legacy of expansionary fiscal policies in the aftermath of earlier shocks (Tables 2a and 2b). Consequently, the large-scale physical reconstruction effort currently underway needs to be accompanied by fiscal consolidation to reduce public indebtedness. Reforms are also needed in other areas to reinvigorate growth (sustained private sector growth has been elusive); introduce social safety nets (poverty and underemployment in the agricultural sector have risen sharply in the wake of the hurricanes); and strengthen fiscal institutions (tax concessions have significantly eroded the tax base).



3. **To address these challenges, the government has launched a comprehensive economic reform program, outlined in the attached letter of intent (LOI)**. The program's strategic objectives are fourfold: promoting sustained high economic growth, restoring fiscal and debt sustainability, reducing vulnerabilities, and alleviating poverty. In light of the adverse impact of recent shocks on social indicators, the social development agenda is particularly important—as highlighted in the government's Poverty Eradication Strategy (www.imf.org) which is being submitted to the Executive Boards of the World Bank and Fund as an Interim-Poverty Reduction Strategy Paper.

Box 1.Weather-Related Vulnerabilities

Grenada has traditionally been considered to lie south of the Atlantic hurricane belt. Prior to hurricane Ivan in 2004, Grenada had not been hit by a major hurricane since 1955, and served as a safe heaven for yachts and other inter-island passenger/cargo ships during the hurricane season.

But possibly reflecting recent warming of sea surface temperatures, the intensity of hurricanes has increased and their paths have become less predictable. Ivan killed 39 people and caused damage in Grenada in excess of 200 percent of GDP.[1/] This is among the highest estimated loss from an incident of natural disaster. Productive sectors, particularly agriculture and tourism were severely damaged, and over 80 percent of the housing stock was affected, with 30 percent completely destroyed. The bulk of the damage from Hurricane Emily was to the agriculture sector (banana production, which farmers had turned to following the devastation to the mainstay crops nutmeg and cocoa, was hit badly) and rural infrastructure (houses, roads, and bridges).

Reconstruction is proceeding well. By end-2005, it is estimated that about 60 percent of the damaged houses had undergone repairs. More than two-thirds of the pre-Ivan industrial and hotel room capacity had also been restored.

1/ By comparison, the damage caused by Hurricane Katrina in South Eastern United States last summer is estimated to be some 2 percent of GDP.

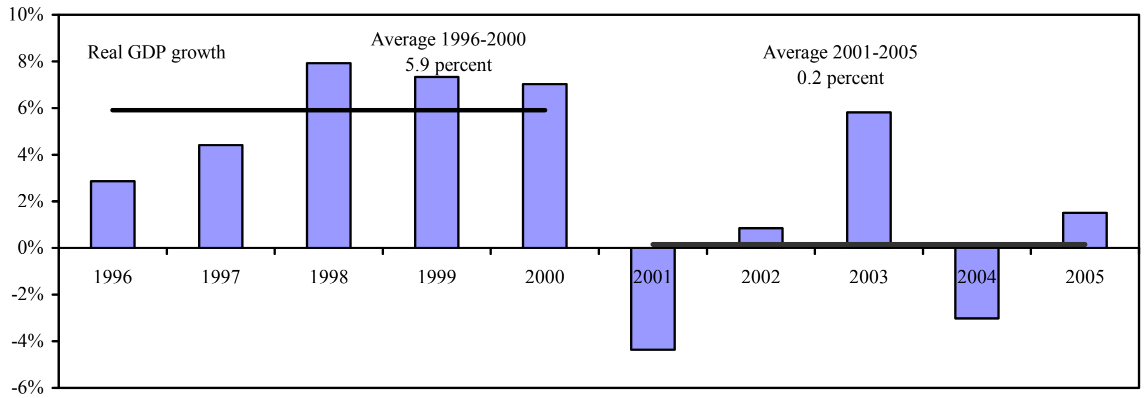
4. **In support of their reform program, the Grenadian authorities request Fund support under the Poverty Reduction and Growth Facility (PRGF)**. Access under the arrangement is proposed at the norm for first time users of 90 percent of quota (SDR 10.53 million). The Fund has already provided extensive support to the authorities' recovery efforts in recent years, including two purchases under the Fund's policy on emergency assistance for natural disasters.[1]

5. **The political context for reform is difficult, but the authorities are determined to push ahead with their reform agenda**. The government has a slim (one-vote) majority in the 15 member Parliament. It has sought to build consensus for reforms, but has at times found it difficult to garner broad support. Most recently, despite modification to address some concerns, trade unions have voiced strong opposition to the National Reconstruction Levy (NRL) introduced by the government in the 2006 budget. The situation is likely to remain difficult ahead of the general elections which have to be held before March 2009.

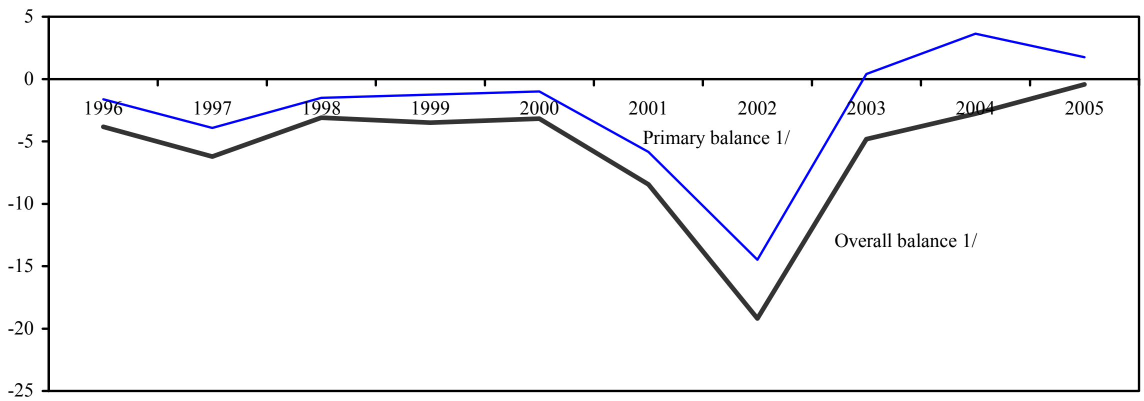
[1] The two purchases were each in the amount of SDR 2.9 million (25 percent of quota). The first purchase was approved in January 2003 (following tropical storm Lili) and the second in November 2004 (following Hurricane Ivan).

Figure 1. Grenada: Macroeconomic Developments, 1996–2005
(In percent of GDP, unless otherwise denoted)

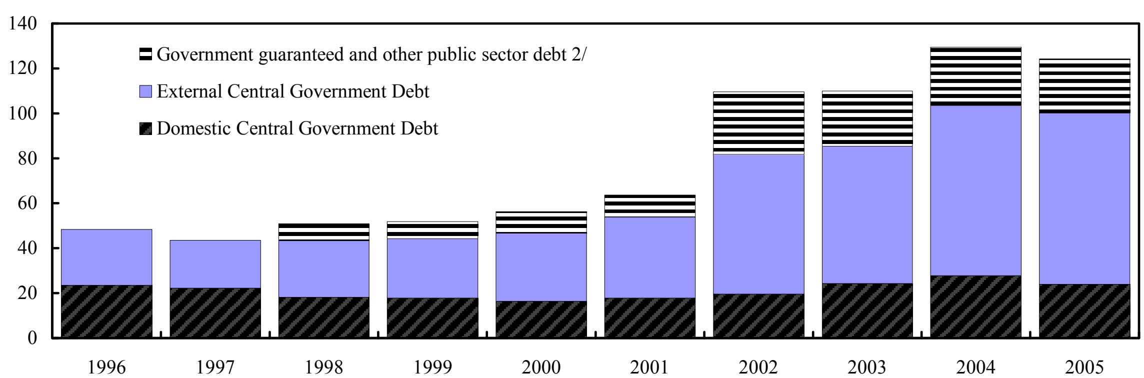
Exogenous shocks have increased growth volatility in recent years...



...fiscal balances had deteriorated, but have improved since 2003…



...and public debt, especially external and government guaranteed debt, have reached high levels.



Sources: Grenadian authorities; and Fund staff estimates.

1/ Includes 11.4 percent of GDP paid in 2002 to extinguish lease arrangements.
2/ Data on government-guaranteed and other public sector debt before 1998 are not available.

II. Recent Developments and Outlook

6. **Brisk activity in the construction sector led to a modest recovery in 2005**. The influx of insurance proceeds and donor support helped finance rebuilding. Activity in agriculture and tourism, the mainstays of the economy, however, remained weak. The agriculture sector was dealt a further blow when much of the short-cycle crops planted by farmers in the wake of the destruction to nutmeg and cocoa trees from Ivan were destroyed by Hurricane Emily. Tourism activity was also subdued in 2005, as it was only in late December (the start of the tourist season) that 70–80 percent of the pre-Ivan hotel room capacity was restored. The sharp spike in construction activity nonetheless offset weak conditions in agriculture and tourism, leading real GDP to expand by around 1½ percent in 2005 after contracting 3 percent in 2004.

7. **Inflation rose to 6 percent during 2005 reflecting shortages and a 45 percent adjustment in domestic petroleum prices in October**. Prior to this adjustment, inflation had risen to 4.2 percent year-on-year in September, owing to increases in prices of food (in part because Hurricane Emily destroyed crops), construction material, and electricity.[2] Second-round price increases in the wake of the fuel price adjustment have so far been limited, and inflation is expected to drop back to historical rates in 2006.

8. **The impact of the hurricanes on the financial sector has been modest.**

- *Domestic commercial banks were in a relatively strong financial position, providing them room for maneuver when Ivan struck*. Further, liquidity increased as insurance proceeds (some of which were used to repay loans) and higher remittances were deposited with the banks. Banks raised their loan-loss provisioning and granted a three-month blanket moratoria on servicing loans. More recently, however, NPL ratios have increased marginally and the capital adequacy ratio for locally incorporated banks declined to 15 percent in December 2005.

Grenada: Selected Financial Soundness Indicators, June 2004–December 2005

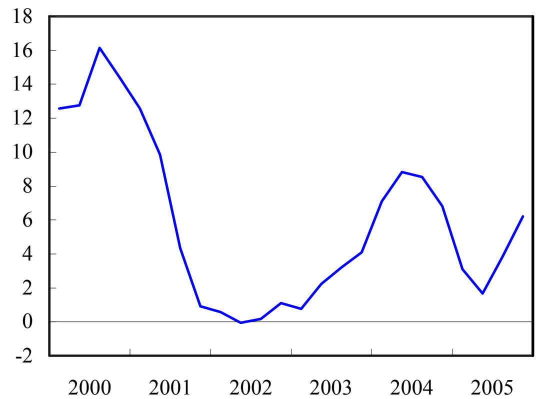
	2004			2005	
	Jun-04	Sep-04	Dec-04	Jun-05	Dec-05
Capital adequacy ratio (total capital over risk weighted assets)	17.2	16.4	14.9	17.7	15.0
NPLs/total loans	5.9	6.2	6.0	5.0	5.5
Locally incorporated banks	7.6	7.6	7.1	4.7	6.8
Foreign banks	3.5	4.1	4.4	5.5	3.5
Loan loss provision/NPLs	42.9	67.1	81.9	93.5	78.9
Locally incorporated banks	45.2	79.9	63.0	88.2	60.0
Foreign banks	36.0	32.3	127.8	100.4	134.6
Liquid assets/current liabilities	34.6	38.6	42.9	40.8	30.6
Gross government claims/total assets	14.6	13.5	11.3	11.7	11.2
Government deposits/total deposits	7.7	8.1	8.4	9.6	8.7
Foreign currency deposits/total deposits	6.9	6.6	5.6	7.1	7.8
Contingent liabilities/capital (indigenous banks)	54.6	60.3	67.7	69.9	81.0
(Pre-tax) return on average assets	0.6	(0.6)	(0.1)	0.4	0.3

Source: Eastern Caribbean Central Bank

[2] The electricity pricing mechanism has a component which is adjusted automatically to reflect changes in international fuel prices. Domestic fuel prices had not been adjusted since late 2000.

- *Encouragingly, growth in private sector credit has also started to recover* (Table 3).

Grenada: Credit to Private Sector
(Quarterly percentage change)



1/ End-December figure is proxied by the average of end-October and end-November figures.

- *Some insurance companies have, however, been under strain*. The settlement of Hurricane Ivan's insurance claims has been mostly completed, with an estimated EC$416 million paid to about 5,000 claimants as at end-June 2005. However, a few small insurance companies have had difficulties making timely payment to policy holders apparently due to insufficient provisioning and reinsurance, leading to the government closure of one insurance company in December 2005.

9. **The immediate fiscal shortfall, including the large financing gap in 2005, has been addressed through a tripartite burden-sharing arrangement: fiscal adjustment, donor support, and commercial debt restructuring**.

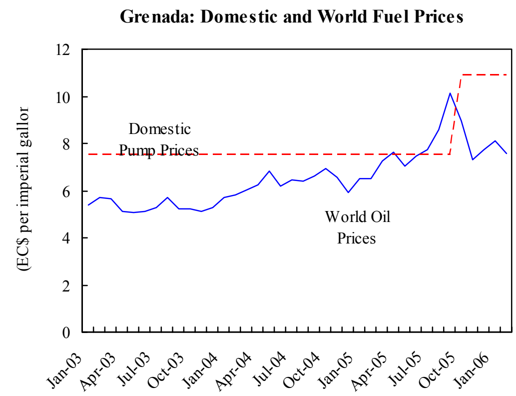
- *The fiscal accounts were in broad balance in 2005*. Revenues were quite buoyant (Tables 2a and 2b), partly reflecting one-off factors (arrears collection and the boost to trade taxes from higher imports of construction material). The adjustment of petroleum prices also helped eliminate the subsidy that the government was providing as world oil prices increased sharply.[3] Spending was also quite restrained, with primary expenditures kept 4½ percentage points of GDP below the allocation in the budget.

Fiscal Developments 2004–05

(In percent of GDP)

	2004	Budget 2005	Est. 2005
Total revenues and grants	**33.1**	**41.6**	**39.1**
Of which			
Tax revenues	23.6	22.6	26.9
Grants	7.5	16.8	11.0
Total expenditures	**35.9**	**47.3**	**38.9**
Primary expenditures	29.5	41.3	36.7
Of which			
Capital expenditures	8.0	18.4	15.4
Primary balance (excluding grants)	-3.8	-16.5	-8.6
Overall balance	**-2.8**	**-5.6**	**0.2**

[3] The delay in adjusting oil prices had however led to the accumulation of liabilities in the order of 2 percent of GDP to the oil importing companies.



- *Donors have been supportive.* Grants to the tune of 11 percentage points of GDP were disbursed in 2005 to help finance the government's current and capital expenditures.

- *A successful commercial debt restructuring process provided substantial near-term cash-flow relief* (Box 2). Following Ivan, the authorities indicated that they would not be able to service their debt and would seek a collaborative restructuring of outstanding claims. The debt exchange offer, eventually launched in September 2005, helped restructure more than 90 percent of eligible commercial debt (accounting for about 45 percent of total public sector debt). The exchange did not involve any reduction of principal, but the lower interest rates in the near to medium term that the new bonds carry, nonetheless imply that creditors accepted a haircut in NPV terms of some 40–45 percent.

10. **The external current account deficit widened sharply in 2005** (Table 4). Reflecting high reconstruction material imports and low tourism and agriculture export receipts, the current account deficit widened from 13½ percent of GDP to 37 percent in 2005. With much of Grenada's nutmeg and cocoa trees destroyed, merchandise exports, remain depressed—a condition likely to prevail until newly planted trees start to bear fruit in about five years time.

Outlook for 2006 and beyond

11. **Prospects for near-term output growth are good.** Reflecting ongoing reconstruction activity, preparations for and the eventual hosting of the 2007 Cricket World Cup, and an anticipated recovery in tourism, real GDP growth should rise to above 5 percent in 2006 and 2007. Beyond 2007, however, growth is likely to slip back as agriculture activity and exports, in particular, are likely to remain depressed for some time. The tourism sector, the mainstay of foreign currency earnings, is also unlikely to expand strongly absent new investment. Consequently, staff and the authorities were of the view that fiscal consolidation would be important to reduce the policy uncertainties caused by the current high level of public debt, and improvements to the investment climate would be needed for the economy to revert to its long-term potential growth rate. The planned reforms are expected to raise the real GDP growth rate to a sustainable 4 percent—the long-run average.

Box 2. Grenada's Commercial Debt Restructuring Process

Grenada started incurring arrears on most of its commercial debt after authorities declared public debt to be unsustainable after Hurricane Ivan struck in September 2004. Almost a year after Ivan, Grenada launched an exchange offer for its commercial debt. The offer covered about half of the country's total public sector debt, and sought to restructure approximately US$190 million of external debt (including one global bond of US$100 million) as well as US$86 million of domestic debt. (The eligible debt included claims by domestic banks of about US$17 million for which the authorities reached a separate settlement in October, ahead of the closing of the general offer.)

The exchange of commercial debt was successfully completed on November 15, 2005, and has several noteworthy features:

- ***The authorities sought a co-operative solution with their creditors***. Together with their advisors, the authorities met individually and in groups with creditors and, in response to creditor's suggestions, adjusted the structure of the offer while maintaining consistency with the overall financing envelope (the coupon structure was raised slightly, resulting in a lowering of the NPV haircut by about 5 percentage points). There were especially close consultations, but not formal negotiations, with a creditor committee which represented about 70 percent of the eligible external debt.

- ***Participation was high***. Overall participation reached 91 percent of eligible claims, or about US$237 million (see table below for a comparison with other recent sovereign debt restructurings). Participation was especially high on the external side, reaching 93 percent. Participation among domestic creditors exceeded 86 percent.

- ***The exchange entails significant, and front-loaded, cash flow relief to the government***. It provides an 83 percent reduction in Grenada's commercial debt service costs between 2005 and 2008 and a reduction of 73 percent between 2009 and 2012.

- ***Creditors accepted a substantial net present value (NPV) reduction***. The debt exchange did not involve any write down of principal, and past-due interest was fully capitalized. The new bonds have a 20-year maturity and interest rates of 1 percent for the first three years, which gradually increase thereafter. For creditors, on average, this implies an NPV haircut of 40–45 percent for exit yields in the 9–10 percent range.

- ***Credit rating has improved following the restructuring***. The new bonds issued in the debt exchange have received a B- minus rating from Standard and Poors, thereby lifting Grenada from the Sovereign Default status it had since the end of 2004. The current rating, however, falls still short of the BB- rating Grenada enjoyed before Ivan struck.

Recent Debt Restructurings: A Comparison

	Participation Rate	NPV-Haircut (Actual Exit Yields) (In percent)	NPV-Haircut (Uniform 10% Discount Rate)
Grenada	91	40–45	45
Argentina	76	75	75
Dominican Republic	91	1	1
Russia	99	45–60	44
Dominica	72	50	...
Uruguay	93	20	8
Ukraine	97	30	5
Ecuador	97	25	25

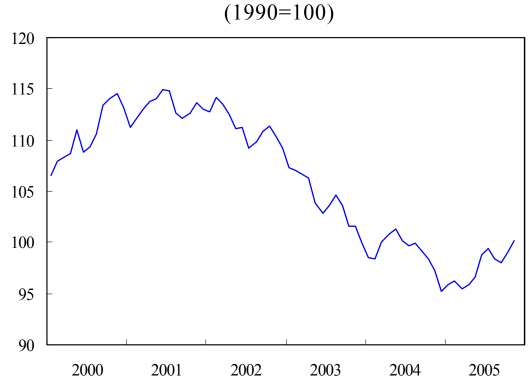
Source: Fund staff estimates.

12. **The external outlook is subject to some uncertainty**.

- *The current account deficit is projected to narrow very gradually.* With merchandise exports only expected to recover in the medium term, and imports set to remain high with continued reconstruction activity, the trade balance is expected to remain at recent levels through the program period. But as more hotel rooms come back on stream, higher tourism earnings should contribute to a decline in the current account deficit—from the current level of 37 percent of GDP to about 27 percent by 2008.

- *With one-off factors dominating the external accounts, competitiveness is hard to gauge*. In contrast to the evolution in the current account, indirect indicators point to an improvement in competitiveness. The Eastern Caribbean dollar has depreciated markedly in real effective terms since the beginning of 2002 mirroring the depreciation of the U.S. dollar to which it is pegged. Tourism based indicators also suggest that competitiveness is adequate. Grenada's market share of Caribbean stay-over tourist arrivals improved somewhat during 1999–2003, although visitor numbers have been substantially lower after Ivan reflecting the temporary reduction in hotel room capacity.

Grenada: Real Effective Exchange Rate
(1990=100)



III. The Authorities' Program for 2006–08

The authorities' reform program is an outgrowth of work initiated before Hurricane Ivan struck. In 2003, the primary balance (including grants) registered a small surplus—for the first time in a decade—as the authorities sought to keep in-check public debt which had risen to inordinately high levels. And in mid-2004, the authorities were considering how best to make the improvement in the fiscal stance permanent when Ivan struck. Policies and priorities changed considerably thereafter. The debt burden increased further even as debt servicing capacity weakened and pressing spending needs emerged. The government remained committed to reform, and the policy dialogue with Fund staff deepened while donors were approached for support. Discussions on possible Fund-support intensified after the authorities developed a home-grown reform program in mid-2005.[4]

[4] This program was prepared under the auspices of the Structural Adjustment and Technical Assistance Program (SATAP). SATAP was set-up by CARTAC in response to a request from the ECCB's monetary council to enable country authorities to implement home-grown adjustment programs.

A. Overall Strategy

13. **With reconstruction activity broadly on-track, the Grenadian authorities have turned their attention to the longer term challenges that the country faces—a timely shift in emphasis that staff strongly welcomed**. The authorities' program aims at re-establishing the basis for high, sustained growth, and is accordingly based on four pillars: (i) reducing fiscal imbalances; (ii) wide-ranging reforms to reinvigorate economic growth; (iii) steps to reduce vulnerabilities; and (iv) advancing social development. There was agreement that progress in these areas would improve the economy's resilience to shocks.

14. **Fiscal reforms are at the heart of the authorities' program.** There was broad agreement that reducing the debt stock from 130 percent of GDP at end-2004 to a more prudent level had to be the central objective of fiscal policy and that fiscal consolidation needed to be initiated promptly. Without fiscal measures, huge financing gaps would have emerged. Against this backdrop, the approach adopted has the following elements:

- **Debt restructuring**. The authorities noted soon after Ivan struck that it had limited the scope for fiscal adjustment, and that a restructuring of Grenada's public debt burden would be unavoidable. In the event, private creditors have been very responsive, and official creditors have been approached for comparable debt relief to that provided by commercial creditors (Table 5).

- **Fiscal adjustment**. By the same token, the authorities recognized that they needed to do their part—consistent with the burden-sharing approach—by improving the fiscal stance and thus eliminating remaining financing gaps. To this end:

  - The authorities' program targets a central government primary surplus (excluding grants) of 2½ percent of GDP—a target that would enable the debt-to-GDP ratio to decline to 60 percent (in keeping with the ECCB's recommendation) by 2015 (Box 3).[5]

  - The 4½ percentage points of GDP improvement in the primary balance[6] (excluding grants) that this requires will be phased in through 2008—consistent with the need to avoid fiscal retrenchment becoming a drag on the recovery and accommodate the large capital spending needs in 2006 and 2007 to rehabilitate public infrastructure and buildings.[7]

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[5] However, when the ECCB adopted this benchmark in 1998 it was with a view to it being reached by 2007.

[6] This adjustment is relative to the current underlying or structural primary balance—a deficit of around 2 percent of GDP. The actual primary deficit is much larger reflecting one-off capital expenditures.

[7] The country is one of the host nations of the 2007 Cricket World Cup. A grant from the People's Republic of China is being used to finance a new Cricket Stadium to replace the one destroyed by Ivan.

- ➢ The measures required to generate this shift in the fiscal stance will be initiated early in the program period—so the adjustment can be completed by 2008.

- **Structural fiscal policies**. The shift in the fiscal stance will be underpinned by reforms to improve the efficiency of the tax system and effectiveness of public spending.

15. **Fiscal consolidation will be bolstered by policies to foster higher economic growth and reduce vulnerabilities**. In light of the need for a quick pay-off in the form of higher investment, structural reforms in the first year of the program focus on measures to improve the investment climate. In the second and third years of the program they will focus on removing constraints on growth stemming from the labor and financial markets. The durability of the ongoing recovery also depends on mitigating vulnerabilities. To this end, the program includes a number of initiatives to improve preparedness for extreme weather events as well as to address weaknesses in the financial sector.

B. Towards Sustainable Public Finances

The composition of fiscal adjustment will be evenly distributed between revenue and expenditure measures to affect the 4½ percentage points of GDP improvement in the primary balance by 2008. Two important revenue measures (a levy on personal incomes and an automatic fuel pricing mechanism) are being implemented in the context of the 2006 budget. A VAT will also be introduced by 2008. Expenditure reforms are also being initiated early in the program period, particularly the rationalization of the public sector investment program.

16. **The authorities are committed to a primary surplus (excluding grants) of 2½ percent of GDP as the main anchor for fiscal policy over the medium term, and have used the 2006 budget to initiate the fiscal consolidation program**. With capital outlays on reconstruction, in particular, needing to be maintained at high levels through next year, the emphasis in the 2006 budget, approved by Parliament in mid-February, is on the revenue side. It introduced the National Reconstruction Levy (NRL) on personal incomes first mooted in the 2005 Budget as well as an automatic fuel pricing mechanism. Current spending is also set to decline by about 1 percentage point of GDP relative to last year. All told, the measures announced in the budget are expected to limit the primary deficit (excluding grants) to 7¾ percent of GDP, down from 8½ percent of GDP in 2005. As the largely one-off capital expenditures in 2006 and 2007 are completed and the fiscal reforms being implemented bear fruit, the primary balance (excluding grants) should swing to a surplus of 2½ percent of GDP by 2008.

Fiscal Developments 2005–08
(In percent of GDP)

	Est. 2005	Proj. 2006	Proj. 2007	Proj. 2008
Total revenues and grants	**39.1**	**36.1**	**31.5**	**31.9**
Of which				
Grants	11.0	8.0	2.7	2.5
Total expenditures	**38.9**	**38.1**	**31.6**	**28.8**
Primary expenditures	36.7	35.7	29.4	26.8
Of which				
Capital expenditures	15.4	15.4	10.0	8.2
Primary balance (excluding grants)	-8.6	-7.7	-0.6	2.5
Overall balance (excluding grants)	-10.8	-10.1	-2.8	0.5

Box 3. Grenada: Medium-Term Fiscal Consolidation

The fiscal program has been designed to ensure that public debt is reduced markedly. The program's debt objective is the ECCB's established benchmark—a debt to GDP ratio of 60 percent—to be reached by 2015.

To reach this objective, a primary surplus of 2½ percent of GDP has been targeted for 2008. This target is based on the following considerations:

- **Total public sector debt** (including government-guaranteed debt and nonguaranteed public sector debt) at end-2005 was about 128 percent of GDP. About 17 percent of GDP is in the form of guaranteed debt. It is, however, debatable whether permanent fiscal adjustment is needed for such contingent liabilities. Nonetheless, under the program it is assumed that half of these contingent liabilities could be called upon. Accordingly, the starting debt-to-GDP ratio for the purposes of estimating the appropriate primary surplus is assumed to be 120 percent of GDP.

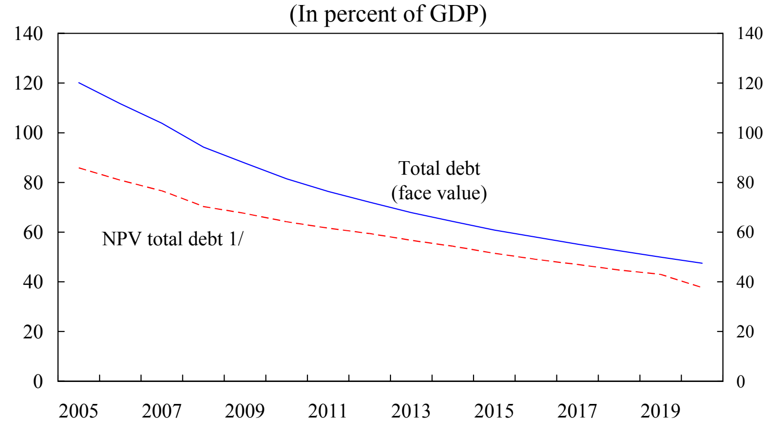
- **Interest rates** on Grenada's restructured claims step up gradually from 1 percent over the next three years to over 8 percent after ten years.

- **Real GDP** is assumed to expand by 4 percent a year over the medium term.

The underlying or structural primary deficit is now estimated at 2 percent of GDP. To arrive at this figure, the one-off factors that have dominated the fiscal account in recent years were purged. Consequently, staff and the authorities estimate that the revenue effort (tax plus nontax) on current policies is of the order of 27 percent of GDP, current primary expenditures are about 21 percent of GDP (the average over 1990–2002), and capital expenditures are 8 percent of GDP—a level that should be consistent with the medium-term growth target.

Consequently, the medium-term primary surplus target requires a fiscal adjustment of around 4½ percentage points of GDP. The revenue measures envisaged under the program coupled with administrative reforms are expected to allow the revenue-to-GDP ratio to increase to 29¼ percent by 2008 (from the current underlying level of 27 percent). On the expenditure front, current primary spending is expected to decline to below 19 percent of GDP (from 21 percent) over the same period.

Grenada: Public Debt-to-GDP Ratio 2005-2020
(In percent of GDP)



1/ Discount rate used for external debt is 9 percent. Domestic debt is not discounted.

The improvement in the fiscal stance will help lower public debt significantly. With GDP growth rates of around 4 percent and a substantial turnaround in the primary balance, low interest rates in the initial few years should allow a rapid decline in the debt-to-GDP ratio. When interest rates step up, however, the rate of decline in the debt ratio slows, unless primary surpluses rise above 2½ percent of GDP (see debt sustainability analysis in Annex I).

17. **The levy on incomes is being introduced in the face of opposition from the trade unions** (¶17).[8] The authorities noted that they had delayed the introduction of the NRL in the hope of securing broad national support for the measure. Following consultations with the Trade Union Congress (TUC), a number of deductions from the tax base were introduced to ameliorate impact on homeowners in particular.[9] While this did not prove sufficient to win the backing of the unions, the government has proceeded with the collection of the levy. At the same time, discussions with the trade unions are continuing. The government has not ruled out further modification to the levy, but has stressed that any such changes would have to be consistent with the objective of collecting EC$10½ million (¾ percent of GDP).

18. **Expenditure measures will focus on streamlining the public sector investment program and wage restraint**.

- On the **public sector investment program** (PSIP), the authorities recognize that project selection is haphazard, and the PSIP tends to be dominated by projects for which external financing is readily available rather than by projects with higher social and economic rates of return. Accordingly, the authorities intend to improve project screening with the assistance of CDB and the World Bank (¶21). They also intend to limit PSIP envelope to around 8 percent of GDP—a level that should be consistent with the expected GDP growth rate of 4 percent over the medium term—once reconstruction is completed. While 8 percent may appear relatively large, the authorities stressed that capital spending is important to spur growth in small-island economies with limited private investment opportunities. The authorities also noted that a higher PSIP envelope could be considered should higher grants become available. Going forward, the authorities will also seek to keep nonconcessional financing to a minimum.

- **Public sector wages** have in recent years increased well ahead of inflation and productivity. This has led to an increase in the wage bill from 10½ percent of GDP in 2000 to 11¾ percent of GDP in 2005. While this is not far from the average level in other countries in the region, it belies the fact that there has been extensive outsourcing of government services in Grenada in recent years. Against this backdrop, wage restraint is expected to contribute to the adjustment effort. To this end, the authorities intend to keep wages constant in real terms through 2008, thereby reducing the wage bill by about 1¼ percentage points of GDP. These reforms will be underpinned by broader public sector reforms (¶28).

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[8] Paragraph numbers refer to the Memorandum of Economic Policies (Annex II).

[9] Mortgage interest payments and certain outlays on education are allowed to be deducted from the tax base starting July 1, when the levy increases from 3 to 5 percent on monthly incomes of EC$1,001 to EC$5,000.

19. **These fiscal measures make room for increased social spending**. The mission supported the authorities' plans to increase financial support to those affected hardest by the rise in fuel prices. The 2006 budget includes an increase in monthly transfers to needy elderly persons, mainly in rural areas, from EC$100 to EC$135 at an estimated annual cost of about 0.3 percentage points of GDP. In addition, the budget includes a significant allocation for low-income housing projects and support for farmers whose livelihoods have been severely affected by the hurricanes.

20. **The program envisages comprehensive reforms to tax policy and administration, geared towards improving the efficiency and effectiveness of the tax system**.

- **VAT**. The authorities are committed to introducing a value-added tax by January 1, 2008, to replace the current narrowly based general consumption tax (¶25). Notwithstanding the preparatory work that had been undertaken before Hurricane Ivan struck, the authorities wanted to proceed cautiously, particularly in light of the limited implementation capacity and the administrative problems that scuttled an earlier VAT introduced in the 1980s.

- **Tax administration**. Improvements in tax administration will include enhancements to work practices at Customs and the auditing capacity of the Inland Revenue Department (¶19).

- **Tax incentives**. The current system of tax incentives has proved ineffective at promoting investment (see below), imposes a heavy burden on public finances, and is very cumbersome to administer.[10] Reforms are accordingly planned to improve the predictability and transparency of the tax system (¶26), including the repeal of legislations that provide wide discretionary powers to grant tax concessions.

- **Corporate income tax**. Reductions in the CIT rate will be considered as the revenue situation permits.

21. **Staff supported the ambitious fiscal objectives at the central government level, but highlighted the need to closely monitor developments in the rest of the public sector**. Preliminary work by staff suggests that the rest of the public sector is in broad balance. However, the balance sheets of some public enterprises have been strained by the recent hurricanes, while some other enterprises harbor ambitious investment plans—plans that require close screening to ensure that they are financially viable. Against this backdrop, the authorities have agreed to require public enterprises to submit quarterly accounts to the Ministry of Finance. They also intend to avoid providing guarantees to public enterprises.

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[10] Revenues foregone on account of tax concessions are estimated to be over 10 percentage points of GDP per year.

22. **The authorities are working to finalize the debt restructuring process**. With respect to the few remaining nonparticipating commercial creditors, the authorities continue to make good faith efforts towards reaching a collaborative settlement. About half of the nonparticipating eligible external claims pertain to a single creditor with whom the authorities have established contact and who they continue to offer a settlement on the same terms as the participants in the exchange have received. The other half pertains to about 5 percent of holders of a US$100 million international bond issued in 2002. In this case, the identity of the nonparticipating creditors is unknown and the authorities are making efforts to find and engage these creditors. The authorities have also approached official creditors for rescheduling of their outstanding obligations.

C. Improving the Investment Climate

Major relative price distortions and institutional weaknesses are not evident in Grenada, so discussions focused on policies that would be more supportive of higher private investment.

23. **The paucity of new private investment—particularly in the tourism sector—is a major concern for the authorities**.[11] The few tourism projects that have been initiated in recent years have entailed considerable government financial involvement. Moreover, a number of these projects had stalled. Beyond such direct financial involvement, as noted above, the government has tended to provide generous income tax holidays to most new investment initiatives. But, again, this practice too has failed to elicit much new investment; creating instead a cycle of dependency with well-established firms being repeatedly granted extensions of concessions. The authorities argued that, absent such interventions, there would have been even less investor interest. While not discounting the importance of incentives, staff argued that there are more efficient tax incentives that should be considered in lieu of tax holidays. Ultimately, it was the limited success of the current approach that prompted action.

24. **Against this backdrop, structural policies will focus on eliminating policy-induced distortions that have inhibited higher private investment**. In particular:

- **Land**. The three public entities currently involved in determining land use and management will be merged by end-2006 to facilitate investor access to land (¶14). All major divestment of public properties will take place through well-advertised public auctions to attract the widest possible investor interest.

[11] National account data on private investment are derived as a residual and are thus subject to significant measurement errors. The absence of much new investment is confirmed by survey data, including a recent diagnostic review of the investment climate in Grenada by the World Bank's Foreign Investment Advisory Service (FIAS) which reveals that new business activity has been in decline in recent years, with most existing firms having been in operation for more than ten years.

- **Investment promotion**. The government agency responsible for investment promotion, Grenada Industrial Development Corporation (GIDC), will be strengthened and made to focus on investment promotion, rather than its current focus of screening requests for tax incentives (¶14).

- **Investment code**. A new investment code will be legislated by September 2006, clearly laying out investor rights and obligations (¶14).

- **Tax incentives**. The current system of tax holidays will be replaced by end-June 2006 with a system of accelerated depreciation and time-limited loss carry forward provisions (¶26).

25. **There was broad recognition that improvements in the investment climate, while important, may not prove sufficient for increased private investment**. Consequently, there was agreement that future program reviews would address other possible hindrances to higher economic growth as they are identified. Further, staff and the authorities will also look at the need to enhance the flexibility of labor and product markets, in the second and third years of the program, respectively. The sequencing of reform is also motivated by limited implementation capacity.

D. Reducing Vulnerabilities

The program seeks to reduce vulnerabilities from extreme weather events and weaknesses in the regulatory framework of the financial sector. The recent hurricanes suggest that steps are required to better enforce building standards as well as increase insurance coverage. In the financial sector, while the banking system appears to have coped with recent shocks, this needs to be confirmed by a closer look at banks' balance sheets.

26. **The authorities' strategy to reduce vulnerabilities to future hurricanes has the following key elements**:

- **Building code**. The authorities consider the current code's requirement that newly built structures be able to withstand hurricanes of up to Category 3 strength to be adequate. They, however, note that the code is not evenly enforced, and will seek to address this weakness in the coming months.

- **Insurance**. A new Insurance Act will be enacted to help improve confidence in the sector, improve contract certainty, and better protect policy holders. The Act is expected to strengthen insurance supervision, which currently does not involve any on-site inspections. The authorities will also look into other ways to encourage greater insurance coverage, although they note that the destruction caused by Ivan has increased demand for housing insurance.

- **Regional initiatives**. The government is also looking to participate actively in regional initiatives to pool insurance risk, including the World Bank's Catastrophic Insurance Project.

27. **The authorities noted that the banking system had coped with the impact of the recent hurricanes** (Table 6). However, the increase in the share of nonperforming loans in recent months is a concern. Further, the authorities and staff reached understandings that in light of the damage caused by Ivan to a large swath of the country's capital stock and the high share of mortgages in total lending (close to 40 percent), it would be beneficial to have an on-site inspection of the banking system. Accordingly, the authorities have asked the ECCB, which is responsible for bank supervision, to conduct such an inspection, expected to be initiated by mid-2006.

28. **Staff also stressed the need to strengthen the financial sector's regulatory framework**. Weaknesses in this area have allowed a small domestic bank to operate without supervision. The authorities explained that their ability to ascertain that this bank is complying fully with regulatory and prudential norms is constrained because of an ongoing court case regarding the validity of its banking license. Further, they noted that the bank's ongoing operations posed limited risk to the rest of the financial sector, given that it has been kept outside the formal clearing system as well as its relatively minor role in the financial system (accounting for less than 2 percent of the banking system's total assets). Nonetheless, the authorities are committed to strengthening their relationship with the ECCB regarding licensing practices and the development of strategies to address problems which may arise in banks. Relatedly, to help strengthen supervision of the nonbank financial sector, the government is committed to ensuring passage of the Grenada Authority for the Regulation of Financial Institutions (GARFIN) Act, that would establish a single supervisory agency.

E. Social Development

Grenada is considered to be broadly on track to meet the MDGs. The most pressing near-term social challenges relate to the dislocation caused by the hurricanes. For the longer term, reducing poverty is contingent on reducing unemployment.

29. **Near-term social needs arising from the impact of recent hurricanes are being addressed through a range of programs**. In rural areas where dislocation has been greatest because of the extensive damage to nutmeg and cocoa trees, programs include efforts to provide farmers with soft loans to rehabilitate farms and, with a more longer-term focus, rehabilitation of a large number of rural roads. Another area of concern has been the damage to the housing stock. Work here includes a program to contribute building materials to the needy to allow them to rebuild their dwellings. Beyond this, the government is preparing an ambitious program to build several hundred (low-income) housing units to be financed by external grants.

30. **Staff noted that it would be important to embed these and other social programs in a broader national strategy to alleviate poverty.** In recent years a number of documents

have been prepared to identify needs and advance the social development agenda. These include the Poverty Eradication Strategy initially prepared in 2004 and updated in late 2005, a Core Welfare Indicator Questionnaire Survey prepared in 2005, an assessment of progress towards the MDGs (Table 7), as well as a Macro-Socio-Economic Assessment of Damage by Hurricanes Ivan and Emily. But the recommendations of these initiatives have not been fully costed. Staff noted that the forthcoming PRSP would be a good occasion to integrate and prioritize the social development agenda. The government is presently considering the appropriate modalities to outline this agenda in a comprehensive poverty reduction strategy paper.

IV. Program Modalities

31. **The program is structured and will be monitored as follows**:

- **Access and phasing**. In view of the remaining large reconstruction needs, the country's high level of indebtedness, and its request for concessional treatment from both commercial and official creditors, staff supports the authorities' request for the full access to come from PRGF resources at the norm for first-time uses of 90 percent of quota. The phasing would be front loaded (Table 8): 40 percent in the first year when the financing need is the highest, and 25 percent each in the second and third years of the arrangement.

- **Capacity to repay the Fund**. Grenada's capacity to repay the Fund is favorable. Debt service to the Fund is projected to peak at a modest 1.3 percent of exports of goods and services during 2006–09 when the ENDA purchases are to be repaid (Table 9). During 2011–18, when the PRGF disbursements would be repaid, debt service is not expected to exceed 1 percent of exports of goods and services.

- **Program monitoring**. Program reviews will be on a semiannual basis, linked to the end-June and end-December test dates. Indicative targets will be established for end-March and end-September to allow quarterly assessment of progress under the program.

- **Quantitative performance criteria** will apply to: the primary balance of the central government excluding grants;[12] nonaccumulation of domestic arrears (continuous basis); nonconcessional public external borrowing up to a certain limit;[13] zero short-term external debt ceiling (continuous); and nonaccumulation of external arrears (continuous).

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[12] An adjuster would allow the government to spend any additional grant proceeds. Shortfalls in external financing will also be accommodated up to a limit of EC$25 million.

[13] Nonconcessional borrowing of up to US$16 million is allowed to accommodate official bilateral loans which have a grant element slightly short of the 35 percent threshold.

- **Structural benchmarks** are proposed in the following areas:
    - Reach agreement on public sector wage path for 2006–08 (end-April 2006);
    - Initiate implementation of reforms at Customs Authority (end-August 2006);
    - Initiate work to strengthen PSIP planning and implementation (end-June 2006);
    - Amend Income Tax Act to adopt a system of accelerated depreciation and time-bound loss carry-forward provisions (end-June 2006);
    - Repeal the Investment Code Incentives Act, Qualified Enterprises Act, and elements affecting tax policy in other legislations including the Hotels Act and Fiscal Incentives Act (end-June 2006);
- **Debt restructuring**. The authorities have indicated that they will continue to make good-faith efforts towards reaching a collaborative settlement with nonparticipating creditors from the November 2005 commercial debt exchange. This is consistent with the Fund lending into arrears policy.
- **Financing assurances**. Approval of the program should pave the way for a restructuring of debts owed to Paris Club creditors. Notwithstanding arrears to bilateral creditors (including Belgium and Taiwan Province of China), the Paris Club has provided financing assurances for Grenada during its March 7 meeting.

V. RISKS

32. **In the staff's view, the risks to the program relate to the outlook to the external accounts, policy slippages, higher output growth failing to materialize, and weak implementation capacity**. Of course, there is also the ever-present specter of another Ivan-strength hurricane. Such an event would significantly delay the achievement of fiscal and debt sustainability.[14] Given its location, Grenada can best prepare for such an event by reducing vulnerabilities—the unifying theme of the authorities' program.

- **Financing of the external current account deficit is subject to some uncertainty**. In addition to projected Fund financing, donor support as well as the beneficial effects of the recent commercial and prospective official debt restructurings, higher private inflows are expected to be forthcoming to finance the large current account deficits expected to prevail in the next few years. However, should this not occur, it would likely lead to lower imports, in turn constraining output growth.

[14] In particular, another hurricane would likely cause large financing gaps—gaps which are likely to prove difficult to bridge.

- **Implementation risks related to the envisaged demanding set of fiscal reforms are also considerable**. Some of these reforms are likely to face stiff resistance, although the authorities have so far shown their readiness to tackle such resistance.

- **The pick-up in real GDP growth expected under the program could fail to materialize**. This could in turn undermine the fiscal effort.

- **Finally, the limited implementation capacity could delay the completion of some reforms or give rise to slippages in data reporting**. Mindful of this, staff has sought to sequence the reforms and has closely defined conditionality to those areas where reporting is strongest.

VI. Staff Appraisal

33. **Grenadians are to be commended for their efforts to quickly recover from the devastating effects of Hurricane Ivan**. And despite the set back that Hurricane Emily dealt to the ongoing recovery from Ivan, rebuilding has persisted and the economy is getting back on its feet. This is a strong testament to the population's resilience and fortitude.

34. **The proposed program should help address the formidable challenges that the country still faces**. These challenges include public finances that are on an unsustainable trajectory, weak prospects for sustained high growth, and heightened vulnerability to shocks. Absent a change in direction, the country's ability to bounce back quickly from further shocks is uncertain. Accordingly, staff strongly welcomes the government's decision to put the ongoing recovery on a firmer footing by adopting a medium-term reform program. The comprehensive nature of the program—focusing not just on fiscal consolidation, but also fostering higher growth, alleviating poverty and reducing vulnerabilities—should also ensure its success.

35. **Fiscal consolidation is the centerpiece of the reform program**. The adjustment is phased to allow the authorities to use the breathing room provided by the commercial debt restructuring to implement the fiscal measures that they have identified. Indeed, the program is based on a gradual improvement in the primary balance (excluding grants) to 2½ percent of GDP by 2008. This together with the debt restructuring should allow public debt to decline to some 60 percent of GDP by 2015. But this will require strict adherence to the fiscal program and readiness to adopt corrective action to address any important deviations. Close monitoring of developments will therefore be critical to the successful implementation of the fiscal program.

36. **The fiscal reforms that have been initiated need to be seen in a broader context**. Beyond eliminating the financing gaps the country would otherwise face, the planned reforms should also serve to bolster investor confidence by eliminating the economic uncertainty that the weakness in public finances has engendered. This includes uncertainty about future levels of taxation, path of expenditures, and the government's ability to abide by the contracts that it engages in. Further, the fiscal reforms should also

contribute towards the continued stability of the monetary union. Staff welcomes the important structural measures that the authorities have selected to ensure that the envisaged fiscal improvement is durable.

37. **Implementation of the planned tax reforms will be important to minimize distortions and improve the efficiency of the tax system**. The wholesale tax exemptions provided as incentives under the present tax regime are not closely aligned with the amount of ongoing investment that firms are undertaking, and lead to a higher tax burden on businesses that are not granted similar tax relief. Accordingly, the authorities' decision to move to a system that allows accelerated depreciation for investments—thus more directly relating incentives to investment—is an important initiative. Also significant is the authorities' plan to replace the present general consumption tax with a broad-based value-added tax. Staff commends these decisions. To compliment the tax policy changes that are to be implemented under the program, staff also urges the government to consider reductions to the corporate income tax rate in a phased manner provided the fiscal situation permits. Beyond simplifying the tax system, these policy changes should help simplify tax administration.

38. **Staff welcomes the authorities' plans to introduce an automatic fuel pricing mechanism**. Going forward, it will be important to insulate government revenues from changes in world market prices as well as allow demand to respond to price changes. To this end, the price build-up formula should include a specific tax element as well as frequent adjustments to reflect world market prices.

39. **The success of fiscal reforms will also depend critically on spending restraint and improvements in the screening of public investment projects**. Staff supports the authorities' intention to maintain public sector wages unchanged in real terms. There would otherwise not be much room, without savings being generated elsewhere in the budget, to accommodate real wage increases over the program period. Accordingly, it will be important to reach quickly an agreement with the civil service unions along these lines. Relatedly, staff welcomes the decision to reorient the process of selecting public investment projects to those with the highest rates of return and to limit the overall PSIP envelope to around 8 percent of GDP once reconstruction is completed. Given the limited room for maneuver elsewhere in the budget, absent such reforms to the investment budget, the intended fiscal consolidation is unlikely to bear fruit. Accordingly, staff encourages the authorities to initiate reforms in this area promptly.

40. **Improvements to the investment climate will be important to raise growth and reduce the unemployment which underlies poverty in Grenada**. In the near term, the authorities are aware of the need to focus on increasing the level of private investment. To this end, they are focusing on the need to put in place a transparent and investor-friendly framework in which investors can operate, simplifying the process through which land is made available to investors, and removing other regulatory hurdles. Staff commends these initiatives.

41. **The program is subject to a number of risks**. Perhaps the most potent of these would be a hurricane of the same (or greater) strength than Ivan. But, as noted above, the authorities' program is very much centered on reducing vulnerabilities by improving the country's ability to cope with future shocks. In particular, the fiscal room that is being created by reducing public debt will provide the country with flexibility in the event of further shocks. Other elements of the program are even more directly focused on reducing vulnerability. Risks related to program financing—given the external payments arrears to external creditors—will be addressed through financing assurances reviews for each disbursement under the arrangement until outstanding arrears are eliminated. Staff commends the authorities' efforts to reach a collaborative agreement with creditors in the context of the recently completed commercial debt restructuring process—a process that has been consistent with the Fund's lending into arrears policy. It also strongly encourages them to continue working with nonparticipants with a view to reaching agreement.

42. **All in all, staff believes the proposed program will help address the many economic and social challenges that Grenada faces and recommends approval of the authorities' request for an arrangement under the PRGF**.

Table 1. Grenada: Selected Economic and Financial Indicators, 2003–08

Rank in UNDP Human Development Index out of 177 countries (2004)	66	Infant mortality rate per '000 births (2003)	18
		Adult illiteracy rate in percent (2001)	4
Life expectancy at birth in years (2003)	65	Poverty headcount index (2000)	32
GDP per capita in US$ (2004)	4,620		

	2003	2004	Est. 2005	Projections 2006	2007	2008
(Annual percentage change; unless otherwise specified)						
National income and prices						
Real GDP	5.8	-3.0	1.5	6.5	5.0	4.0
GDP deflator	1.3	2.7	3.5	4.6	2.0	2.0
Consumer prices						
End-of-year	1.6	2.5	6.0	2.0	2.0	2.0
Period average	2.2	2.3	3.5	4.6	2.0	2.0
External sector						
Exports, f.o.b.	7.1	-24.8	-14.6	0.6	-8.2	16.7
Imports, c.i.f.	25.9	3.3	22.6	-3.4	4.2	5.7
Export volume 1/	-2.0	-25.6	-23.5	-0.6	-10.0	17.1
Import volume 1/	11.6	-8.6	11.7	-5.0	4.3	5.7
Current account balance (including grants; in percent of GDP)	-33.2	-13.5	-37.1	-32.8	-28.0	-26.7
Terms of trade (deterioration -)	-3.2	-10.6	1.7	-0.5	2.0	-0.4
Real effective exchange rate (end of period, depreciation -)	-8.5	-4.6	5.2	...	...	...
Banking system						
Net foreign assets 2/	5.8	17.9	-19.4	-2.2	-2.0	-2.5
Net domestic assets 2/	2.2	-0.2	19.0	10.1	7.7	7.3
Of which						
Credit to public sector (net) 2/	2.3	-6.7	-0.8	0.0	0.0	0.0
Credit to private sector 2/	3.1	5.0	6.2	8.5	7.7	7.7
Money and quasi-money (M2)	8.0	17.7	-0.4	7.8	5.7	4.8
Weighted deposit rate (in percent per year) 3/	3.4	2.8	2.8	...	...	...
Weighted lending rate (in percent per year) 3/	12.4	10.0	10.2	...	...	...
(In percent of GDP)						
Central government finances						
Total revenue and grants	34.5	33.1	39.1	36.1	31.5	31.9
Of which						
Grants	6.9	7.5	11.0	8.0	2.7	2.5
Total expenditure	39.3	35.9	38.9	38.1	31.6	28.8
Current expenditure	24.3	27.9	23.5	22.7	21.6	20.6
Of which						
Salaries and allowances	10.9	12.7	11.8	11.7	11.1	10.6
Capital expenditure	15.0	8.0	15.4	15.4	10.0	8.2
Primary balance (after grants)	0.4	3.7	2.4	0.3	2.1	5.0
Current balance	3.2	-2.4	4.6	5.3	7.2	8.6
Overall balance (after grants)	-4.8	-2.8	0.2	-2.0	-0.1	3.0
Public sector total debt (end-period) 4/	110.0	129.5	128.0	126.7	117.8	107.3
(In millions of U.S. dollars; unless otherwise specified)						
Gross international reserves of the ECCB, end-of-period	539.9	632.4	600.7	...	...	...
In percent of broad money in all ECCU countries	19.8	20.4	20.1	...	...	...
Nominal GDP	443.7	436.8	474.0	519.3	558.9	596.5

Sources: Ministry of Finance; Eastern Caribbean Central Bank; United Nations, Human Development Report 2004; World Bank, WDI 2005; and Fund staff estimates and projections.

1/ Does not include goods procured in ports by carriers.
2/ As a percent of broad money at the beginning of the year.
3/ Break in the data series in 2003.
4/ Includes central government debt, government-guaranteed debt, and nonguaranteed public enterprise debt.

Table 2a. Grenada: Medium-Term Central Government Finances, 2003–08 1/

(In millions of EC dollars, unless noted otherwise)

			Est.	Projections		
	2003	2004	2005	2006	2007	2008
Total revenue and grants	**413.2**	**390.7**	**500.7**	**505.6**	**475.7**	**513.0**
Total revenue	330.3	302.5	360.1	392.8	434.7	472.0
Current revenue	330.0	301.2	359.7	392.3	434.2	471.4
Tax revenue	298.3	278.8	343.8	362.1	400.0	434.8
Taxes on income and profits	47.5	43.0	57.7	67.2	72.5	77.4
Taxes on property	17.0	16.4	15.3	17.1	22.5	23.9
Taxes on domestic goods and services	59.0	52.4	60.0	69.0	76.7	90.2
Taxes on international transactions	174.8	167.1	210.8	208.9	228.4	243.2
Nontax revenue	31.8	22.3	15.9	30.1	34.2	36.7
Capital revenue	0.3	1.3	0.4	0.5	0.5	0.6
Grants	82.9	88.2	140.6	112.8	41.0	41.0
Total expenditure	**470.8**	**423.4**	**497.7**	**534.2**	**476.6**	**464.4**
Current expenditure	291.6	329.6	301.1	318.1	325.7	332.3
Current primary expenditure	229.2	253.8	273.3	285.1	293.2	300.3
Personnel emoluments	130.4	150.3	150.9	164.1	167.4	170.7
Wages and salaries	118.4	135.0	135.2	145.2	148.1	151.0
Personnel allowances	12.0	15.3	15.7	18.9	19.3	19.7
Goods and services	40.5	48.0	67.8	58.4	59.6	60.8
Interest	62.5	75.8	27.8	33.0	32.5	32.0
Domestic	17.2	21.1	13.9	9.3	9.3	9.2
Foreign	45.2	54.7	13.9	23.7	23.2	22.8
Transfers and subsidies	58.3	55.5	54.6	62.6	66.2	68.8
Statutory authorities and state enterprises	0.0	0.0	0.0	0.0	0.0	0.0
Private enterprises	6.5	0.0	0.0	0.0	0.0	0.0
Grants and subventions	19.7	17.8	21.4	27.9	30.9	32.7
Transfers abroad (contributions)	6.5	5.2	4.4	4.6	4.6	4.7
Transfers to Statutory Boards	0.5	0.8	0.6	0.6	0.6	0.6
Transfers to households	25.1	31.8	28.2	29.5	30.1	30.7
Capital expenditure	179.1	93.8	196.6	216.1	150.9	132.1
Grant-financed capital expenditure	82.9	30.1	96.5	112.8	41.0	41.0
Current balance	38.4	-28.4	58.6	74.2	108.5	139.1
Primary balance (excluding grants)	-78.0	-45.0	-109.8	-108.5	-9.4	39.6
Primary balance (including grants)	4.9	43.1	30.8	4.4	31.6	80.6
Overall balance (excluding grants)	-140.5	-120.8	-137.6	-141.5	-41.9	7.6
Overall balance (including grants)	-57.6	-32.7	3.0	-28.7	-0.9	48.6
Statistical discrepancy 2/	-56.0	-19.1	0.0	0.0	0.0	0.0
Financing	**113.5**	**51.8**	**-3.0**	**28.7**	**0.9**	**-48.6**
Net external financing	39.7	67.9	27.7	61.1	27.7	11.9
Net amortisation	39.7	111.7	14.2	61.1	27.7	11.9
Disbursments	66.6	157.5	34.8	83.2	47.3	35.3
Amortisation	-26.9	-45.9	-20.6	-22.0	-19.6	-23.4
Change in government assets	0.0	-43.7	13.5	0.0	0.0	0.0
Net domestic financing	73.6	-38.1	-30.7	-32.5	-26.9	-60.5
Divestment/privatization proceeds	0.3	0.0	0.0	0.0	0.0	0.0
Arrears	0.0	22.0	0.0	0.0	0.0	0.0
Financing gap	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Memorandum items:						
Total public sector debt 3/	1,318.2	1,527.6	1,637.8	1,776.1	1,776.9	1,728.3
Nominal GDP (market prices)	1,198.1	1,179.4	1,279.7	1,402.2	1,508.9	1,610.5
Real GDP growth (percent change)	5.8	-3.0	1.5	6.5	5.0	4.0
CPI (average, percent change)	2.2	2.3	3.5	4.6	2.0	2.0

Sources: Ministry of Finance; and Fund staff estimates and projections.

1/ After debt restructuring in 2005.

2/ Difference between overall balance and identified financing.

3/ Includes central government debt, government-guaranteed debt, and nonguaranteed public enterprise debt. In 2005, past due interest has been capitalized.

Table 2b. Grenada: Medium-Term Central Government Finances, 2003–08 1/

(In percent of GDP, unless noted otherwise)

			Est.	Projections		
	2003	2004	2005	2006	2007	2008
Total revenue and grants	**34.5**	**33.1**	**39.1**	**36.1**	**31.5**	**31.9**
Total revenue	27.6	25.6	28.1	28.0	28.8	29.3
Current revenue	27.5	25.5	28.1	28.0	28.8	29.3
Tax revenue	24.9	23.6	26.9	25.8	26.5	27.0
Taxes on income and profits	4.0	3.6	4.5	4.8	4.8	4.8
Taxes on property	1.4	1.4	1.2	1.2	1.5	1.5
Taxes on domestic goods and services	4.9	4.4	4.7	4.9	5.1	5.6
Taxes on international transactions	14.6	14.2	16.5	14.9	15.1	15.1
Nontax revenue	2.7	1.9	1.2	2.1	2.3	2.3
Capital revenue	0.0	0.1	0.0	0.0	0.0	0.0
Grants	6.9	7.5	11.0	8.0	2.7	2.5
Total expenditure	**39.3**	**35.9**	**38.9**	**38.1**	**31.6**	**28.8**
Current expenditure	24.3	27.9	23.5	22.7	21.6	20.6
Current primary expenditure	19.1	21.5	21.4	20.3	19.4	18.6
Personnel emoluments	10.9	12.7	11.8	11.7	11.1	10.6
Wages and salaries	9.9	11.4	10.6	10.4	9.8	9.4
Personnel allowances	1.0	1.3	1.2	1.3	1.3	1.2
Goods and services	3.4	4.1	5.3	4.2	4.0	3.8
Interest	5.2	6.4	2.2	2.4	2.2	2.0
Domestic	1.4	1.8	1.1	0.7	0.6	0.6
Foreign	3.8	4.6	1.1	1.7	1.5	1.4
Transfers and subsidies	4.9	4.7	4.3	4.5	4.4	4.3
Statutory authorities and state enterprises	0.0	0.0	0.0	0.0	0.0	0.0
Private enterprises	0.5	0.0	0.0	0.0	0.0	0.0
Grants and subventions	1.6	1.5	1.7	2.0	2.0	2.0
Transfers abroad (contributions)	0.5	0.4	0.3	0.3	0.3	0.3
Transfers to Statutory Boards	0.0	0.1	0.0	0.0	0.0	0.0
Transfers to households	2.1	2.7	2.2	2.1	2.0	1.9
Capital expenditure	15.0	8.0	15.4	15.4	10.0	8.2
Grant-financed capital expenditure	6.9	2.5	7.5	8.0	2.7	2.5
Current balance	3.2	-2.4	4.6	5.3	7.2	8.6
Primary balance (excluding grants)	-6.5	-3.8	-8.6	-7.7	-0.6	2.5
Primary balance (including grants)	0.4	3.7	2.4	0.3	2.1	5.0
Overall balance (excluding grants)	-11.7	-10.2	-10.8	-10.1	-2.8	0.5
Overall balance (including grants)	-4.8	-2.8	0.2	-2.0	-0.1	3.0
Statistical discrepancy 2/	-4.7	-1.6	0.0	0.0	0.0	0.0
Financing	**9.5**	**4.4**	**-0.2**	**2.0**	**0.1**	**-3.0**
Net external financing	3.3	5.8	2.2	4.4	1.8	0.7
Net amortisation	3.3	9.5	1.1	4.4	1.8	0.7
Disbursments	5.6	13.4	2.7	5.9	3.1	2.2
Amortisation	-2.2	-3.9	-1.6	-1.6	-1.3	-1.5
Change in government assets	0.0	-3.7	1.1	0.0	0.0	0.0
Net domestic financing	6.1	-3.2	-2.4	-2.3	-1.8	-3.8
Divestment/privatization proceeds	0.0	0.0	0.0	0.0	0.0	0.0
Arrears	0.0	1.9	0.0	0.0	0.0	0.0
Financing gap	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Memorandum items:						
Total public sector debt 3/	110.0	129.5	128.0	126.7	117.8	107.3
Nominal GDP (market prices, EC$ millions)	1,198	1,179	1,280	1,402	1,509	1,611
Real GDP growth (percent change)	5.8	-3.0	1.5	6.5	5.0	4.0
CPI (average, percent change)	2.2	2.3	3.5	4.6	2.0	2.0

Sources: Ministry of Finance; and Fund staff estimates and projections.

1/ After debt restructuring in 2005.

2/ Difference between overall balance and identified financing.

3/ Includes central government debt, government-guaranteed debt, and nonguaranteed public enterprise debt. In 2005, past due interest has been capitalized.

Table 3. Grenada: Summary Accounts of the Banking System, 2003–08

	2003	2004	2005	Projections 2006	2007	2008
(In millions of Eastern Caribbean dollars, end of period)						
I. Consolidated Banking System						
Net foreign assets	**395.1**	**620.8**	**333.5**	**300.5**	**268.9**	**226.9**
Net domestic assets	**865.3**	**862.6**	**1,143.9**	**1,292.7**	**1,415.4**	**1,537.5**
Net credit to the public sector	65.1	-19.6	-32.0	-32.0	-32.0	-32.0
Central government	126.6	71.7	15.1	15.1	15.1	15.1
Nonfinancial public enterprises 1/	-61.4	-91.3	-47.1	-47.1	-47.1	-47.1
Credit to private sector	933.0	996.4	1,088.3	1,214.3	1,337.0	1,467.2
Other	-132.8	-114.3	87.5	110.3	110.3	102.3
Liabilities to private sector (M2)	**1,260.4**	**1,483.4**	**1,477.4**	**1,593.1**	**1,684.4**	**1,764.4**
Money	241.1	340.2	325.1	330.5	355.6	376.2
Quasi-money	1,019.3	1,143.1	1,152.3	1,262.6	1,328.7	1,388.2
II. Eastern Caribbean Central Bank						
Imputed net international reserves	224.7	328.6	254.4	264.4	274.4	279.4
Net domestic assets	9.4	-1.1	-1.7	-1.7	-1.7	-1.7
Base money	**234.1**	**327.6**	**262.4**	**262.7**	**272.7**	**277.7**
Currency held by the public	84.7	102.1	115.0	100.3	107.9	111.8
Commercial bank reserves	149.4	225.5	147.5	162.4	164.8	165.9
III. Commercial Banks						
Net foreign assets	170.4	292.2	79.1	36.0	-5.5	-52.6
Net claims on ECCB	147.6	237.6	148.2	162.4	164.8	165.9
Net domestic credit	**857.7**	**848.2**	**1,135.1**	**1,294.4**	**1,417.1**	**1,539.2**
Net credit to the public sector	55.7	-18.5	-30.3	-30.3	-30.3	-30.3
Credit to private sector	933.0	996.4	1,088.3	1,214.3	1,337.0	1,467.2
Other	-131.0	-129.7	77.0	110.3	110.3	102.3
Liabilities to the private sector	1,175.7	1,381.3	1,362.4	1,492.8	1,576.4	1,652.6
(12-month change in percent of M2 at the beginning of the period)						
Consolidated banking system						
Liabilities to private sector	8.0	17.7	-0.4	7.8	5.7	4.8
Net foreign assets	5.8	17.9	-19.4	-2.2	-2.0	-2.5
Net domestic assets	2.2	-0.2	19.0	10.1	7.7	7.3
Credit to private sector	3.1	5.0	6.2	8.5	7.7	7.7
Memorandum items:						
Loans/deposits ratio (in percent)	68.1	57.6	58.1	...	...	...
Net liquid assets/total deposits (in percent)	33.4	39.9	36.2	...	...	...

Sources: Eastern Caribbean Central Bank; and Fund staff estimates and projections.

1/ Includes the National Insurance Scheme.

Table 4. Grenada: Summary Balance of Payments, 2003–08

	2003	2004	Projections 1/ 2005	2006	2007	2008
(In millions of U.S. dollars)						
Current account balance	**-147.4**	**-59.0**	**-175.7**	**-170.5**	**-156.4**	**-159.1**
Exports (f.o.b.)	45.5	36.9	31.5	31.7	29.1	33.9
Imports (f.o.b.)	226.4	235.4	288.6	278.6	290.4	307.1
Services (net)	47.1	61.1	29.8	40.3	70.3	73.0
Of which						
Travel (net)	95.3	73.9	71.8	98.1	131.7	137.8
Income (net)	-50.1	-43.2	-40.7	-43.9	-42.6	-42.6
Transfers (net)	36.5	121.5	92.3	80.1	77.2	83.6
Capital and financial account	**127.1**	**94.0**	**79.5**	**148.4**	**142.1**	**143.9**
Capital account (transfers)	41.5	33.2	58.8	65.9	41.0	42.9
Financial account	85.6	60.8	20.7	82.5	101.1	101.0
Of which						
Public sector net borrowing 2/	39.1	44.2	-19.7	10.8	4.1	-1.2
Direct investment (net)	89.2	54.0	49.6	83.2	95.7	107.4
Portfolio investment (net)	29.1	40.4	6.3	0.0	0.0	0.0
Other investments (net)	-32.6	-33.6	-35.2	-0.7	5.4	-6.4
Net errors and omissions	3.4	7.1	17.0	0.0	0.0	0.0
Overall balance	-16.9	42.2	-79.2	-22.0	-14.3	-15.2
Available financing	16.9	-42.2	79.2	12.5	11.8	12.7
Change in imputed reserves	4.6	-38.5	27.5	-3.7	-3.7	-1.9
IMF reserve liabilities (+ is purchase)	4.1	4.3	0.0	3.1	2.4	1.7
Exceptional financing 3/	0.0	8.1	46.7	13.1	13.1	12.9
Financing gap 4/	**0.0**	**0.0**	**0.0**	**9.6**	**2.5**	**2.4**
Memorandum item:						
External public sector debt	355.8	415.6	436.6	459.2	469.5	473.9
(In percent of GDP)						
Current account balance	**-33.2**	**-13.5**	**-37.1**	**-32.8**	**-28.0**	**-26.7**
Trade balance	-40.8	-45.4	-54.2	-47.6	-46.8	-45.8
Exports of goods	10.3	8.5	6.6	6.1	5.2	5.7
Imports of goods	51.0	53.9	60.9	53.7	52.0	51.5
Service, income, and transfers	7.5	31.9	17.2	14.7	18.8	19.1
Of which						
Travel (net)	21.5	16.9	15.1	18.9	23.6	23.1
Capital and financial account	**28.6**	**21.5**	**16.8**	**28.6**	**25.4**	**24.1**
Capital and financial account, including errors and omissior	29.4	23.2	20.4	28.6	25.4	24.1
Public sector net borrowing 2/	8.8	10.1	-4.1	2.1	0.7	-0.2
Direct investment	20.1	12.4	10.5	16.0	17.1	18.0
Overall balance	-3.8	9.7	-16.7	-4.2	-2.6	-2.5
External public sector debt	80.2	95.1	92.1	88.4	84.0	79.5
(Annual percentage change)						
Exports of goods	10.0	-18.9	-14.7	0.6	-8.2	16.7
Imports of goods	25.1	3.9	22.6	-3.4	4.2	5.7
Travel (net)	17.2	-22.5	-2.9	36.7	34.2	4.6

Sources: Eastern Caribbean Central Bank (ECCB); Ministry of Finance; and Fund staff estimates and projections.

1/ Debt service is shown according to the original schedule, above the line, with a contra-entry under "exceptional financing" reflecting the effect of the debt restructuring, below the line.

2/ Government and government guaranteed debt.

3/ Exceptional financing refers to arrears on amortization and interest as well as debt service flow relief provided by commercial creditors in the 2005 debt exchange.

4/ Under the program, the financing gap is expected to be filled by debt service relief provided by Paris Club creditors and Taiwan Province of China.

Table 5. Grenada: Public Sector Debt, 2005

(Year end, in millions of U.S. dollars)

	Stock	Percent of Total Debt	Percent of GDP
Public sector debt 1/	606.6	100.0	128.0
Central government debt	524.1	86.4	110.6
Central government guaranteed debt	62.0	10.2	13.1
Other public sector debt	20.5	3.4	4.3
External debt	436.6	72.0	92.1
A. Central government	382.5	63.1	80.7
1. Multilateral	116.9	19.3	24.7
CDB	71.2	11.7	15.0
IDA	22.9	3.8	4.8
IBRD	10.1	1.7	2.1
IMF	8.4	1.4	1.8
Other multilateral	4.4	0.7	0.9
2. Official bilateral	66.2	10.9	14.0
Paris Club 2/	8.5	1.4	1.8
France	4.1	0.7	0.9
United States	2.8	0.5	0.6
United Kingdom	1.6	0.3	0.3
Other	57.8	9.5	12.2
Taiwan Province of China	20.3	3.3	4.3
Kuwait	18.7	3.1	3.9
Trinidad and Tobago	13.1	2.2	2.8
Other bilateral	5.8	1.0	1.2
3. Commercial, total	199.4	32.9	42.1
Restructured bonds	193.5	31.9	40.8
Unrestructured bonds	5.8	1.0	1.2
B. Central government guaranteed	33.6	5.5	7.1
Of which			
Paris Club	15.2	2.5	3.2
C. Other public sector	20.5	3.4	4.3
Domestic debt	170.0	28.0	35.9
A. Central government	141.7	23.4	29.9
Restructured bonds	68.1	11.2	14.4
Restructured commercial bank loans	14.9	2.5	3.1
Unrestructured bonds	11.0	1.8	2.3
Treasury bills	25.5	4.2	5.4
Compensation claims	14.8	2.4	3.1
Liability to oil companies	6.7	1.1	1.4
Other	0.6	0.1	0.1
B. Central government guaranteed	28.4	4.7	6.0
C. Other public sector	0.0	0.0	0.0
Memorandum items:			
Nominal GDP	474.0		

Sources: Grenadian authorities; and Fund staff estimates.

1/ Includes central government liabilities to the National Insurance Scheme.
2/ In addition, Russia put forward a claim of US$260,000, which the authorities intend to reconcile.

Table 6. Grenada: Indicators of Financial and External Vulnerability, 2001–06

	2001	2002	2003	2004	Est. 2005	Proj. 2006
Real sector indicators						
Real GDP growth (percent)	-4.4	0.8	5.8	-3.0	1.5	6.5
CPI inflation (period average, in percent)	1.7	1.1	2.2	2.3	3.5	4.6
Financial sector indicators						
Capital adequacy ratio (locally incorporated banks)	14.1	15.6	17.7	14.9	15.0	…
Nonperforming loans/total loans	5.9	5.8	4.5	6.0	5.5	…
Locally incorporated banks	9.3	9.0	7.2	7.1	6.8	…
Foreign banks	1.4	1.3	0.6	4.4	3.5	…
Loan loss provision/NPLs	43.6	45.6	61.7	81.9	78.9	…
Locally incorporated banks	40.6	39.3	49.5	63.0	60.0	…
Foreign banks 1/	71.1	106.9	301.3	127.8	134.6	…
Gross government claims/total assets	14.3	15.6	13.9	11.3	11.2	…
FX deposits/total deposits	7.3	6.9	7.3	5.6	7.8	…
Net foreign currency exposure/capital (locally incorporated banks)	49.8	78.7	116.4	221.4	142.4	…
Contingent liabilities/capital (locally incorporated banks)	74.0	73.2	55.5	67.7	81.0	…
(Pre-tax) return on average assets	2.4	2.3	2.8	0.5	0.7	…
Broad money (percent change, 12-month basis)	10.6	7.1	8.0	17.7	-0.4	7.8
Private sector credit (percent change, 12-month basis)	0.9	1.1	4.1	6.8	9.2	11.6
US treasury bill rate (percent per annum)	3.5	1.6	1.0	1.4	3.2	…
Treasury bill rate (percent per annum) 1/	7.0	7.0	6.0	6.0	6.0	…
External sector indicators						
Exchange rate (per US$, end of period)	2.7	2.7	2.7	2.7	2.7	2.7
REER appreciation (percent change on 12-month basis, end of period)	-0.1	-3.4	-8.5	-4.6	5.2	...
Exports of goods (percent change, 12-month basis)	-23.3	-34.9	10.0	-18.9	-14.7	0.6
Imports of goods (percent change, 12-month basis)	-10.9	-7.8	25.1	3.9	22.6	-3.4
Travel receipts (gross, percent change, 12-month basis)	-9.9	6.7	16.5	-19.6	-1.8	33.1
Current account balance (percent of GDP)	-26.6	-32.0	-33.2	-13.5	-37.1	-32.8
Capital and financial account balance (percent of GDP)	22.7	33.2	28.6	21.5	16.8	28.6
FDI inflows (percent of GDP)	15.4	14.9	20.4	12.7	10.8	16.3
Gross international reserves of the ECCB (in US$ millions)	446.0	504.8	539.9	632.4	600.7	...
Gross international reserves in months of current year imports in ECCU countries	4.1	4.6	4.6	4.5	4.5	...
Gross international reserves to broad money in ECCU countries (percent)	19.1	20.2	19.7	19.2	19.2	...
Private external debt (percent of GDP)	...	...	...	...	...	...
Public gross external debt (in US$ million)	179.7	340.5	355.8	415.6	436.6	459.2
Public gross external debt to exports of goods and services (percent)	91.2	197.9	196.9	215.5	261.1	261.6
Public gross external interest payments to exports of goods and services (percent)	4.1	11.3	12.6	14.0	15.4	16.0
Public gross external amortization payments to exports of goods and services (percent	4.1	6.1	6.3	10.8	25.5	11.8
Public gross external interest payments to fiscal revenue (percent)	7.6	17.8	18.7	26.7	21.4	21.2
Public gross external amortization payments to fiscal revenue (percent)	7.6	9.7	9.3	18.7	31.9	14.2
Gross external financing requirement (in percent of GDP) 2/	28.8	35.0	36.4	20.1	46.0	36.8
(In percent of GDP)						
Public sector indicators						
Central government overall balance (after grants) 3/	-8.5	-19.2	-4.8	-2.8	0.2	-2.0
Central government current account balance	2.5	0.6	3.2	-2.4	4.6	5.3
Public sector gross external debt	44.0	83.6	80.2	95.1	92.1	88.4

Sources: Ministry of Finance; Eastern Caribbean Central Bank; and Fund staff estimates and projections.

1/ Rate on three-month treasury bills for 2000, on one-year treasury bills for 200–05.
2/ Defined as external current account deficit plus external amortization.
3/ Includes 11.4 percent of GDP paid in 2002 to extinguish lease arrangements, and reflected in capital expenditures.

Table 7. Grenada: Millennium Development Goals, 1990–2003

	1990	1994	1997	2000	2003
Goal 1. Eradicate extreme poverty and hunger					
Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than $1 a day.					
Population below $1 a day (percent)	...	...	...	...	...
Poverty gap at $1 a day (percent)	...	...	...	...	...
Percentage share of income or consumption held by poorest 20 percent	...	...	...	...	...
Target 2: Halve, between 1990 and 2015, the proportion of people who suffer from hunger.					
Prevalence of child malnutrition (percent of children under 5)	...	...	...	...	...
Population below minimum level of dietary energy consumption (percent)	...	...	...	...	...
Goal 2. Achieve universal primary education					
Target 3: Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling.					
Net primary enrollment ratio (percent of relevant age group)	...	...	...	84.2	...
Primary completion rate, total (percent of relevant age group)	...	...	...	80.0	...
Percentage of cohort reaching grade 5 (percent)	...	...	...	79.0	...
Youth literacy rate (percent ages 15–24)	...	...	...	...	...
Goal 3. Promote gender equality					
Target 4: Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education no later than 2015.					
Ratio of girls to boys in primary and secondary education (percent)	...	...	...	...	...
Ratio of young literate females to males (percent ages 15–24)	...	...	...	...	...
Share of women employed in the nonagricultural sector (percent)	38.4	...	...	...	...
Proportion of seats held by women in national parliament (percent)	...	...	20.0	27.0	27.0
Goal 4. Reduce child mortality					
Target 5: Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate.					
Immunization, measles (percent of children under 12 months)	85.0	87.0	92.0	92.0	99.0
Infant mortality rate (per 1,000 live births)	30.0	26.0	...	21.0	18.0
Under 5 mortality rate (per 1,000)	37.0	33.0	...	26.0	23.0
Goal 5. Improve maternal health					
Target 6: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.					
Maternal mortality ratio (modeled estimate, per 100,000 live births)	...	...	...	...	...
Births attended by skilled health staff (percent of total)	...	...	99.0	99.0	...

Table 7. Grenada: Millennium Development Goals, 1990–2003 (Concluded)

	1990	1994	1997	2000	2003
Goal 6. Combat HIV/AIDS, malaria and other diseases					
Target 7: Have halted by 2015, and begun to reverse, the spread of HIV/AIDS.					
Prevalence of HIV, total (percent ages 15–49)	...	...	...	...	...
Contraceptive prevalence rate (percent of women ages 15–49)	...	...	54.0	...	...
Number of children orphaned by HIV/AIDS	...	...	...	...	...
Target 8: Have halted by 2015, and begun to reverse, the incidence of malaria and other major diseases.					
Incidence of tuberculosis (per 100,000 people)	6.1	5.7	5.4	5.2	4.9
Tuberculosis cases detected under DOTS (percent) 1/	...	...	...	...	...
Goal 7. Ensure environmental sustainability					
Target 9: Integrate the principles of sustainable development into country policies and programs and reverse the loss of environmental resources.					
Forest area (percent of total land area)	14.7	...	...	14.7	...
Nationally protected areas (percent of total land area)	...	...	...	...	...
GDP per unit of energy use (PPP $ per kg oil equivalent)	...	...	...	...	...
CO2 emissions (metric tons per capita)	1.3	1.7	2.0	2.1	...
Target 10: Halve, by 2015, the proportion of people without sustainable access to safe drinking water.					
Access to an improved water source (percent of population)	...	...	...	...	95.0
Target 11: By 2020, to have achieved a significant improvement in the lives of at least 100 million slum dwellers.					
Access to improved sanitation (percent of population)	97.0	...	...	...	97.0
Access to secure tenure (percent of population)	...	...	...	...	...
Goal 8. Develop a global partnership for development					
Target 12: Develop and implement strategies for decent and productive work for youth.					
Youth unemployment rate (percent of total labor force ages 15–24)	27.0	...	...	...	...
Target 13: Make available the benefits of new technologies, especially information and communications.					
Fixed line and mobile telephones (per 1,000 people)	178.3	242.3	301.1	377.6	666.7
Internet users (per 1,000 people)	0.0	0.0	11.0	43.6	169.0
Personal computers (per 1,000 people)	...	...	108.3	127.1	132.1

Source: World Development Indicators database, April 2005.

1/ DOTS detection rate is the percentage of estimated new infectious tuberculosis cases detected under the directly observed treatment, short course case detection, and treatment strategy.

Table 8. Grenada: Reviews and Disbursements Under the Three-Year PRGF Arrangement, 2006–09

Date	Conditions	Disbursement	Percent of Quota
March 2006	Board approval of PRGF arrangement	SDR 1.56 million	13.33
September 2006	Observance of end-June 2006 performance criteria and completion of first review	SDR 1.56 million	13.33
March 2007	Observance of end-December 2006 performance criteria, completion of second review and adopt conditions for second year of the arrangement	SDR 1.56 million	13.33
September 2007	Observance of end-June 2007 performance criteria and completion of third review	SDR 1.46 million	12.50
March 2008	Observance of end-December 2007 performance criteria, completion of fourth review and adopt conditions for third year of the arrangement	SDR 1.46 million	12.50
September 2008	Observance of end-June 2008 performance criteria and completion of fifth review	SDR 1.46 million	12.50
March 2009	Observance of end-December 2008 performance criteria, completion of sixth review	SDR 1.46 million	12.50
Total		SDR 10.53 million	90.00

Table 9. Grenada: Indicators of Capacity to Repay the Fund, 2004–10 1/

			Projections				
	2004	2005	2006	2007	2008	2009	2010
Outstanding Fund credit							
In millions of SDRs	5.9	5.9	7.9	9.4	10.5	10.5	10.5
In millions of U.S. dollars	9.0	8.5	11.5	13.7	15.3	15.4	15.3
In percent of:							
Quota	50.0	50.0	67.5	80.3	89.7	90.0	90.0
GDP	2.1	1.8	2.2	2.4	2.5	2.4	2.2
Government revenues 2/	6.2	4.6	6.1	7.8	8.1	8.0	7.5
Exports of goods and nonfactor services	4.7	5.1	6.5	6.6	6.9	6.1	5.4
Net imputed international reserves	7.4	8.3	10.8	12.4	13.6	13.4	13.2
Public and publicly guaranteed debt	1.6	1.4	1.9	2.3	2.6	2.7	2.7
Debt service to the Fund							
In millions of SDRs	0.1	0.1	1.1	1.5	1.8	1.5	0.1
In millions of U.S. dollars	0.1	0.1	1.6	2.2	2.6	2.2	0.1
In percent of:							
Quota	0.8	0.5	9.4	12.8	15.4	12.8	0.7
GDP	0.0	0.0	0.3	0.4	0.4	0.3	0.0
Government revenues 2/	0.1	0.0	0.9	1.2	1.4	1.1	0.1
Exports of goods and nonfactor services	0.1	0.1	0.9	1.0	1.2	0.9	0.0
Net imputed international reserves	0.1	0.1	1.5	2.0	2.3	1.9	0.1
Public and publicly guaranteed debt	0.0	0.0	0.3	0.4	0.5	0.4	0.0

Source: Fund staff estimates and projections.

1/ Assuming access of 90 percent of quota under the PRGF, with the first disbursement in 2006, and debt service according to the obligations schedule. Further assuming disbursements under the Fund's emergency assistance policy for natural disasters as scheduled and debt service according to the obligations schedule.

2/ Including grants.

Medium-Term Outlook and Debt Sustainability

43. This section assesses the sustainability of Grenada's domestic and external public debt under the program and alternative scenarios.

44. **Under the program scenario, public debt is reduced from 120 percent of GDP in 2005 to close to 60 percent of GDP in 2015** (Table A1a).[15] A large part of this adjustment is achieved during the program period, so that by end-2008 public debt will amount to less than 95 percent of GDP. This sharp decline is largely a function of the sharp improvement in the primary balance during 2006–08 and a pick-up in GDP growth.

45. **In net present value (NPV) terms, public debt is at lower levels and also set to decline more modestly.** In NPV terms, total public debt falls from above 85 percent of GDP in 2005 to about 70 percent by end-2008 and to just above 50 percent by 2015. The NPV calculation takes into account the effects of the restructuring of Grenada's commercial debt, which implied a haircut of 40–45 percent on the NPV of future debt servicing flows (for exit yields in the 9–10 percent range), while leaving the face value of debt unchanged.[16]

46. **In addition to the recent commercial debt restructuring, rescheduling by official creditors is expected to lower debt servicing**. In particular, the program scenario assumes that eligible commercial creditors that did not participate in the recent debt restructuring will settle their claims in 2006 on the same terms as the recent debt exchange. In addition, it is assumed that Paris Club debt will be rescheduled on the basis of Houston terms and that the bilateral debt to Taiwan Province of China is restructured on terms comparable to those of the commercial debt exchange.

47. **Alternative scenarios underline the importance of the envisaged fiscal adjustment and measures to foster growth** (Table A1b, Figure 1). Keeping the primary deficit at its ten-year historical average of 2 percent of GDP, while also assuming GDP growth in line with the historical average (Alternative Scenario A1) would cause the NPV of government debt to rise to over 100 percent of GDP by 2015. With the program's fiscal adjustment achieved, but GDP growth rates permanently lower than assumed under the program scenario (Alternative Scenario A2), the NPV of debt would initially fall only to rise rapidly after 2010. Bound tests indicate considerable sensitivity to external shocks—in particular with respect to lower GDP growth in 2006/2007, which could bring the NPV of debt-to-GDP ratio on an unsustainable trajectory.

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[15] At the end of 2005, public debt amounted to 128 percent of GDP. However, total debt comprises contingent liabilities in the form of government-guaranteed debt, amounting to about 13 percent of GDP. It is debatable whether permanent fiscal adjustment is needed for all of the contingent liabilities. Against this background, it is assumed for the purpose of this exercise that only about half of these guarantees will be called. This assumption implies a starting debt-to-GDP ratio of 120 percent of GDP in 2005.

[16] See Box 2 in the main text of this report.

48. **The program scenario would allow for a considerable reduction of external vulnerability** (Table A2a). With the fiscal adjustment envisaged under the program, external public debt would fall from almost 85 percent of GDP at end-2005 to below 50 percent of GDP by 2015. In NPV terms, it would fall from almost 50 percent of GDP to below 40 percent over the same period. Bound tests suggest significant sensitivity to short-term shocks, but these effects peter out with time (Table A2b, Figure 2).

49. **All told, the adjustment envisaged under the program would bring public debt on a sustainable path**. As shown above, however, accomplishment of both fiscal and growth objectives are crucial to obtain this result. Failure to adhere to program targets would rapidly result in an unsustainable debt trajectory. And, unfortunately, a significant external shock, such as another major hurricane, could have a similar adverse effect.

Table A1a. Grenada: Public Sector Debt Sustainability Framework, Program Scenario, 2002–2025

(In percent of GDP, unless otherwise indicated)

	Actual				Estimate	Projections								
	2003	2004	Historical Average 5/	Standard Deviation 5/	2005	2006	2007	2008	2009	2010	2005-10 Average	2015	2025	2011-25 Average
Public sector debt 1/	110.0	129.5			120.1	111.7	103.8	94.3	87.8	81.5		60.8	33.3	
Of which: foreign-currency denominated	80.2	95.1			84.3	81.3	77.4	73.2	69.1	65.2		48.7	26.5	
Change in public sector debt	0.4	19.5			-9.4	-8.4	-7.8	-9.6	-6.5	-6.3		-3.5	-3.0	
Identified debt-creating flows	-5.3	3.5			-6.4	-10.3	-7.3	-8.9	-6.5	-6.3		-3.5	-3.0	
Primary deficit	-3.5	-5.5	2.0	4.7	-3.3	-1.1	-2.8	-5.5	-4.0	-3.8	-3.4	-2.7	-2.6	-2.6
Revenue and grants	39.5	42.9			49.1	47.1	43.5	44.9	43.5	43.4		42.3	42.3	
Of which: grants	6.9	7.5			11.0	8.0	2.7	2.5	1.2	1.1		0.0	0.0	
Primary (noninterest) expenditure	36.0	37.4			45.8	46.0	40.8	39.3	39.5	39.6		39.6	39.7	
Automatic debt dynamics	-1.8	9.0			-3.1	-9.3	-4.6	-3.4	-2.5	-2.5		-0.8	-0.3	
Contribution from interest rate/growth differential	-1.1	9.0			-2.2	-7.3	-4.6	-3.4	-2.5	-2.5		-0.8	-0.3	
Of which: contribution from average real interest rate	4.9	5.6			-0.3	0.0	0.8	0.6	1.1	0.9		1.6	1.1	
Of which: contribution from real GDP growth	-6.0	3.4			-1.9	-7.3	-5.3	-4.0	-3.6	-3.4		-2.5	-1.4	
Contribution from real exchange rate depreciation	-0.7	0.0			-0.9	-2.0	0.0	0.0	0.0	0.0		...	...	
Other identified debt-creating flows	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	5.7	16.0			-3.0	1.9	-0.5	-0.6	0.0	0.0		0.0	0.0	
NPV of public sector debt	...	84.6			85.9	80.9	76.6	70.3	67.5	64.2		51.5	28.9	
Of which: foreign-currency denominated	0.0	50.2			50.0	50.5	50.2	49.3	48.9	47.9		39.3	22.2	
NPV of contingent liabilities (not included in public sector debt)	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	8.2	16.9			7.1	8.7	6.0	3.0	4.9	4.2		4.9	5.7	
NPV of public sector debt-to-revenue ratio (in percent) 3/	...	197.1			174.8	172.0	176.1	156.7	155.3	147.9		121.7	68.3	
Of which : external	...	43.3			37.7	39.8	42.7	40.7	41.6	40.9		34.4	19.4	
Debt service-to-revenue ratio (in percent) 3/ 4/	12.3	29.1			10.1	10.1	9.5	9.2	11.0	9.5		11.1	16.0	
Primary deficit that stabilizes the debt-to-GDP ratio	-3.9	-25.0			6.1	7.4	5.1	4.1	2.5	2.5		0.8	0.3	
Key macroeconomic and fiscal assumptions														
Real GDP growth (in percent)	5.8	-3.0	3.2	4.3	1.5	6.5	5.0	4.0	4.0	4.0	4.2	4.0	4.0	4.0
Average nominal interest rate on forex debt (in percent)	6.7	5.7	6.4	2.5	1.6	2.6	2.4	2.3	2.9	2.9	2.5	4.5	5.0	5.0
Average real interest rate on domestic currency debt (in percent)	5.1	10.2	5.9	3.4	1.6	-1.1	1.5	1.3	2.2	2.0	1.2	3.4	3.6	3.7
Real exchange rate depreciation (in percent, + indicates depreciation)	-0.9	0.0	-0.2	1.3	-1.0	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	2.9	2.7	2.2	1.3	3.5	4.6	2.0	2.0	2.0	2.0	2.7	2.0	2.0	2.0
Growth of real primary spending (deflated by GDP deflator, in percent)	-15.8	-0.5	6.3	13.6	28.4	5.1	-6.5	1.0	4.4	4.2	6.1	4.0	4.0	4.0
Grant element of new external borrowing (in percent)	...	...	...	... ...	...	...	...	...	...	...	...	...	...	...

Sources: Country authorities; and Fund staff estimates and projections.

1/ Includes central government and central government guaranteed debt as well as debt of public enterprises. In 2005, part of the government guaranteed debt is excluded from the debt stock (see explanation in the text of the DSA annex)

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues including grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table A1b. Grenada: Sensitivity Analysis for Key Indicators of Public Debt 2005-2025

	Est.	Projections						
	2005	2006	2007	2008	2009	2010	2015	2025
NPV of Debt-to-GDP Ratio								
Program Scenario	86	81	77	70	68	64	51	29
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	85	86	87	87	90	92	103	129
A2. Permanently lower GDP growth 1/	86	82	80	75	75	74	80	124
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2006-2007	86	90	94	91	93	94	103	126
B2. Primary balance is at historical average minus one standard deviations in 2006-2007	86	88	91	84	82	80	70	53
B3. Combination of B1-B2 using one half standard deviation shocks	86	90	95	88	86	83	74	56
B4. One-time 30 percent real depreciation in 2006	86	103	99	93	91	89	79	63
B5. 10 percent of GDP increase in other debt-creating flows in 2006	85	89	84	78	75	72	60	38
NPV of Debt-to-Revenue Ratio 2/								
Program Scenario	175	172	176	157	155	148	122	68
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	172	182	199	193	206	211	243	304
A2. Permanently lower GDP growth 1/	173	175	182	167	172	171	189	292
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2006-2007	175	188	215	202	213	215	243	298
B2. Primary balance is at historical average minus one standard deviations in 2006-2007	173	186	209	188	189	183	167	126
B3. Combination of B1-B2 using one half standard deviation shocks	173	190	216	195	197	191	174	133
B4. One-time 30 percent real depreciation in 2006	173	218	226	206	209	204	187	149
B5. 10 percent of GDP increase in other debt-creating flows in 2006	172	189	193	173	173	166	142	89
Debt Service-to-Revenue Ratio 2/								
Program Scenario	10	10	9	9	11	9	11	16
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	10	10	12	15	21	20	27	54
A2. Permanently lower GDP growth 1/	10	11	10	11	14	13	21	51
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2006-2007	10	11	13	15	19	19	27	52
B2. Primary balance is at historical average minus one standard deviations in 2006-2007	10	11	16	19	17	14	16	26
B3. Combination of B1-B2 using one half standard deviation shocks	10	11	15	18	17	15	17	28
B4. One-time 30 percent real depreciation in 2006	10	12	12	12	15	14	17	27
B5. 10 percent of GDP increase in other debt-creating flows in 2006	10	10	17	13	14	12	13	20

Sources: Country authorities; and Fund staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of 20 (i.e., the length of the projection period).
2/ Revenues are defined inclusive of grants.

Table A2a. Grenada: External Debt Sustainability Framework, Program Scenario, 2002–2025 1/
(In percent of GDP, unless otherwise indicated)

	Actual		Historical	Standard	Est.	Projections								
	2003	2004	Average 6/	Deviation 6/	2005	2006	2007	2008	2009	2010	2005–10 Average	2015	2025	2011–25 Average
External government debt (nominal) 1/	**80.2**	**95.1**			**84.3**	**81.3**	**77.4**	**73.2**	**69.1**	**65.2**		**48.6**	**26.4**	
Change in external debt	-3.4	15.0			-10.8	-3.0	-3.9	-4.1	-4.1	-3.9		-2.8	-2.6	
Identified net debt-creating flows	6.3	2.4			22.0	9.1	4.9	3.8	2.0	0.8		-4.5	-3.9	
Noninterest current account deficit	**26.9**	**5.3**	**19.0**	**7.2**	**32.8**	**28.7**	**24.0**	**22.6**	**21.6**	**19.6**		**11.2**	**9.9**	12.1
Deficit in balance of goods and services	30.2	31.4			48.0	39.8	34.2	33.6	30.3	27.2		19.6	19.4	
Exports of goods and services	40.7	44.1			35.3	33.8	37.4	37.3	39.7	42.3		45.6	45.8	
Of which : goods	10.3	8.5			6.6	6.1	5.2	5.7	6.1	6.6		6.6	6.6	
Imports of goods and services	70.9	75.6			83.2	73.6	71.6	70.8	70.0	69.5		65.2	65.2	
Net current transfers (negative = inflow)	-8.2	-27.8	-9.0	7.7	-19.5	-15.4	-13.8	-14.0	-12.6	-10.6		-10.8	-11.0	-10.8
Other current account flows (negative = net inflow)	4.9	1.7			4.3	4.3	3.6	3.1	3.8	3.0		2.4	1.5	
Net FDI (negative = inflow)	**-20.1**	**-12.4**	**-13.2**	**3.4**	**-10.5**	**-16.0**	**-17.1**	**-18.0**	**-18.3**	**-18.3**		**-16.4**	**-14.9**	-16.1
Endogenous debt dynamics 2/	**-0.4**	**9.5**			**-0.3**	**-3.6**	**-1.9**	**-0.9**	**-1.2**	**-0.4**		**0.7**	**1.1**	
Contribution from nominal interest rate	6.4	8.2			1.0	1.4	1.8	2.0	1.5	2.2		2.7	2.2	
Contribution from real GDP growth	-4.5	2.5			-1.3	-5.0	-3.8	-2.9	-2.7	-2.6		-1.9	-1.1	
Contribution from price and exchange rate changes	-2.4	-1.2			…	…	…	…	…	…		…	…	
Residual (3–4) 3/	**-9.7**	**12.6**			**-32.9**	**-12.1**	**-8.8**	**-7.9**	**-6.2**	**-4.8**		**1.7**	**1.4**	
Of which : exceptional financing	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
NPV of external debt	...	48.4			48.3	48.8	48.4	47.9	47.5	46.5		39.1	22.1	
In percent of exports	...	109.7			136.8	144.3	129.5	128.6	119.6	110.0		85.9	48.2	
NPV of PPG external debt 4/	**...**	**48.4**			**48.3**	**48.8**	**48.4**	**47.9**	**47.5**	**46.5**		**39.1**	**22.1**	
In percent of exports	...	109.7			136.8	144.3	129.5	128.6	119.6	110.0		85.9	48.2	
Debt service-to-exports ratio (in percent)	49.8	64.3			7.5	9.0	8.8	10.0	8.1	8.4		10.8	17.0	
PPG debt service-to-exports ratio (in percent)	49.8	64.3			7.5	9.0	8.8	10.0	8.1	8.4		10.8	17.0	
Total gross financing need (billions of U.S. dollars)	120.0	93.2			118.2	81.6	56.6	49.9	40.8	32.2		-2.6	44.3	
Noninterest current account deficit that stabilizes debt ratio	30.2	-9.7			43.6	31.7	27.9	26.8	25.7	23.5		14.0	12.4	
Key macroeconomic assumptions														
Real GDP growth (in percent)	5.8	-3.0	3.2	4.3	1.5	6.5	5.0	4.0	4.0	4.0	4.2	4.0	4.0	4.0
GDP deflator in US dollar terms (change in percent)	2.9	1.5	1.5	1.0	6.9	2.9	2.5	2.6	2.0	2.0	3.2	2.0	2.0	2.0
Effective interest rate (percent) 5/	8.3	10.1	10.2	2.1	1.2	1.8	2.4	2.8	2.2	3.3	2.3	5.5	8.2	5.8
Growth of exports of goods and services (U.S. dollar terms, in p	5.0	6.8	6.0	17.0	-13.3	5.0	19.0	6.5	13.0	12.8	7.2	7.7	6.1	6.7
Growth of imports of goods and services (U.S. dollar terms, in p	15.3	5.0	6.9	10.5	19.5	-3.1	4.6	5.7	4.8	5.3	6.1	4.8	6.1	5.6
Grant element of new public sector borrowing (in percent)	...	...	...	...	39.0	42.9	39.9	38.0	37.2	36.1	38.8	24.9	12.4	19.9
Memorandym item:														
Nominal GDP (billions of US dollars)	443.7	436.8			474.0	519.3	558.9	596.5	632.5	670.9		902.0	1,630.7	

Source: Fund staff simulations.

1/ Data on private sector external debt is not available.
2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.
3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
4/ Based on a discout rate of 9 percent and assumes that NPV of private sector debt is equivalent to its face value.
5/ Current-year interest payments devided by previous period debt stock.
6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table A2b. Grenada: Sensitivity Analyses for Key Indicators of Public and Publicly Guaranteed External Debt, 2005-25
(In percent)

	Est.	Projections						
	2005	2006	2007	2008	2009	2010	**2015**	2025
NPV of Debt-to-GDP Ratio								
Program Scenario	48	49	48	48	48	46	**39**	22
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2006-25 1/	48	46	46	47	50	54	**81**	121
A2. New public sector loans on less favorable terms in 2006-25 2/	48	50	50	50	50	49	**44**	33
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2006-07	48	53	55	55	54	53	**45**	25
B2. Export value growth at historical average minus one standard deviation in 2006-07 3/	48	53	63	62	61	59	**48**	24
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2006-07	48	50	51	50	50	49	**41**	23
B4. Net nondebt creating flows at historical average minus one standard deviation in 2006-07 4/	48	65	80	78	76	73	**57**	26
B5. Combination of B1–B4 using one-half standard deviation shocks	48	63	82	81	79	76	**60**	28
B6. One-time 30 percent nominal depreciation relative to the baseline in 2006 5/	48	69	68	68	67	66	**55**	31
NPV of Debt-to-Exports Ratio								
Program Scenario	137	144	129	129	120	110	**86**	48
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2006-25 1/	137	135	122	127	126	127	**178**	264
A2. New public sector loans on less favorable terms in 2006-25 2/	137	147	134	134	125	116	**97**	72
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2006-07	137	144	129	129	120	110	**86**	48
B2. Export value growth at historical average minus one standard deviation in 2006-07 3/	137	184	267	264	243	222	**166**	82
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2006-07	137	144	129	129	120	110	**86**	48
B4. Net nondebt creating flows at historical average minus one standard deviation in 2006-07 4/	137	191	213	210	191	173	**125**	56
B5. Combination of B1–B4 using one-half standard deviation shocks	137	188	256	253	231	210	**154**	72
B6. One-time 30 percent nominal depreciation relative to the baseline in 2006 5/	137	144	129	129	120	110	**86**	48
Debt Service Ratio								
Program Scenario	8	9	9	10	8	8	**11**	17
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2006-25 1/	8	9	9	7	7	8	**18**	49
A2. New public sector loans on less favorable terms in 2006-25 2/	8	9	8	8	8	8	**9**	18
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2006-07	8	9	9	9	8	8	**10**	15
B2. Export value growth at historical average minus one standard deviation in 2006-07 3/	8	11	15	19	20	20	**21**	25
B3. U.S. dollar GDP deflator at historical average minus one standard deviation in 2006-07	8	9	9	9	8	8	**10**	15
B4. Net nondebt creating flows at historical average minus one standard deviation in 2006-07 4/	8	9	11	17	18	18	**17**	17
B5. Combination of B1–B4 using one-half standard deviation shocks	8	10	14	19	21	20	**20**	22
B6. One-time 30 percent nominal depreciation relative to the baseline in 2006 5/	8	9	9	9	8	8	**10**	15
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	22	22	22	22	22	22	**22**	22

Source: Staff projections and simulations.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

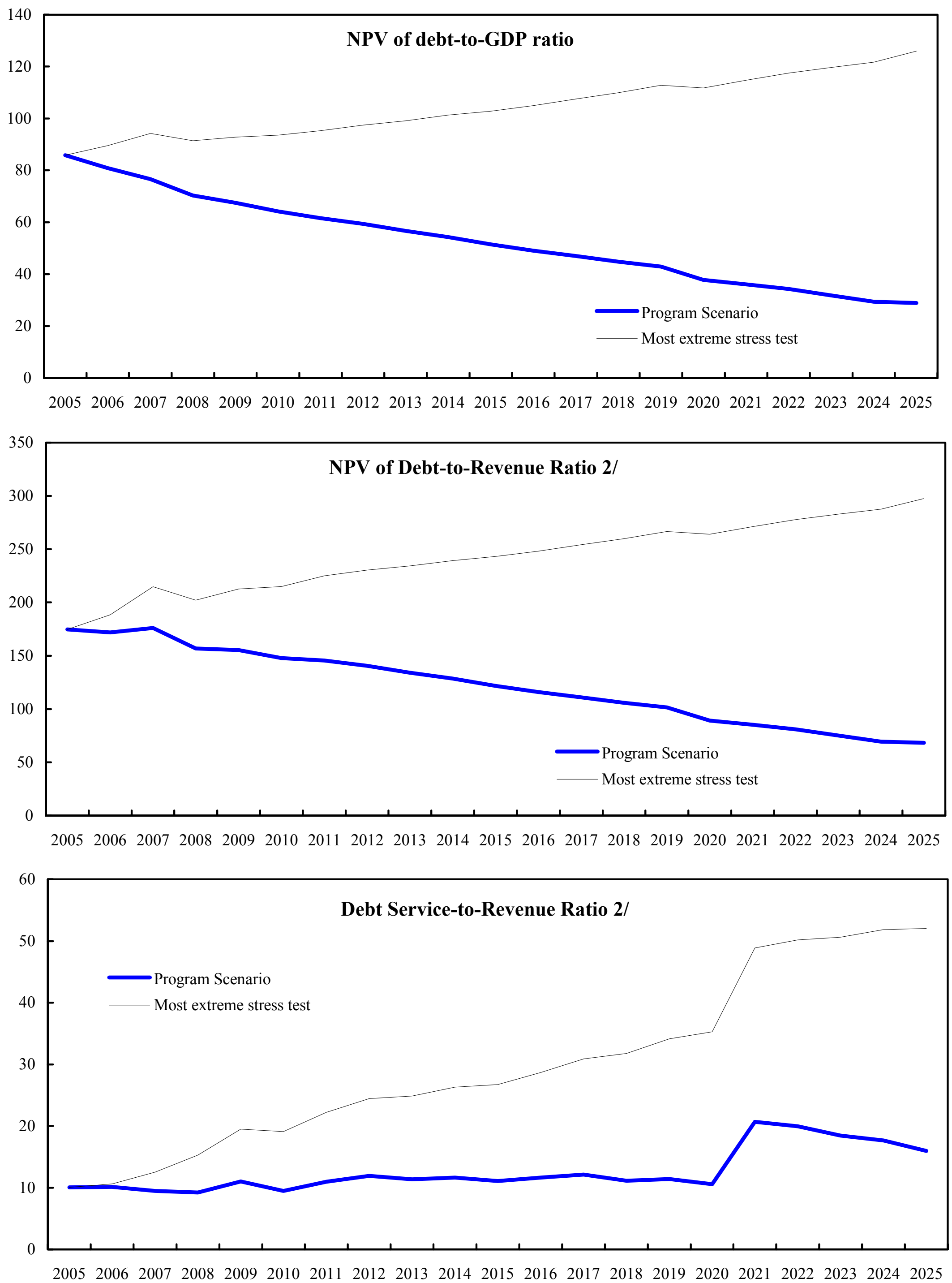
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

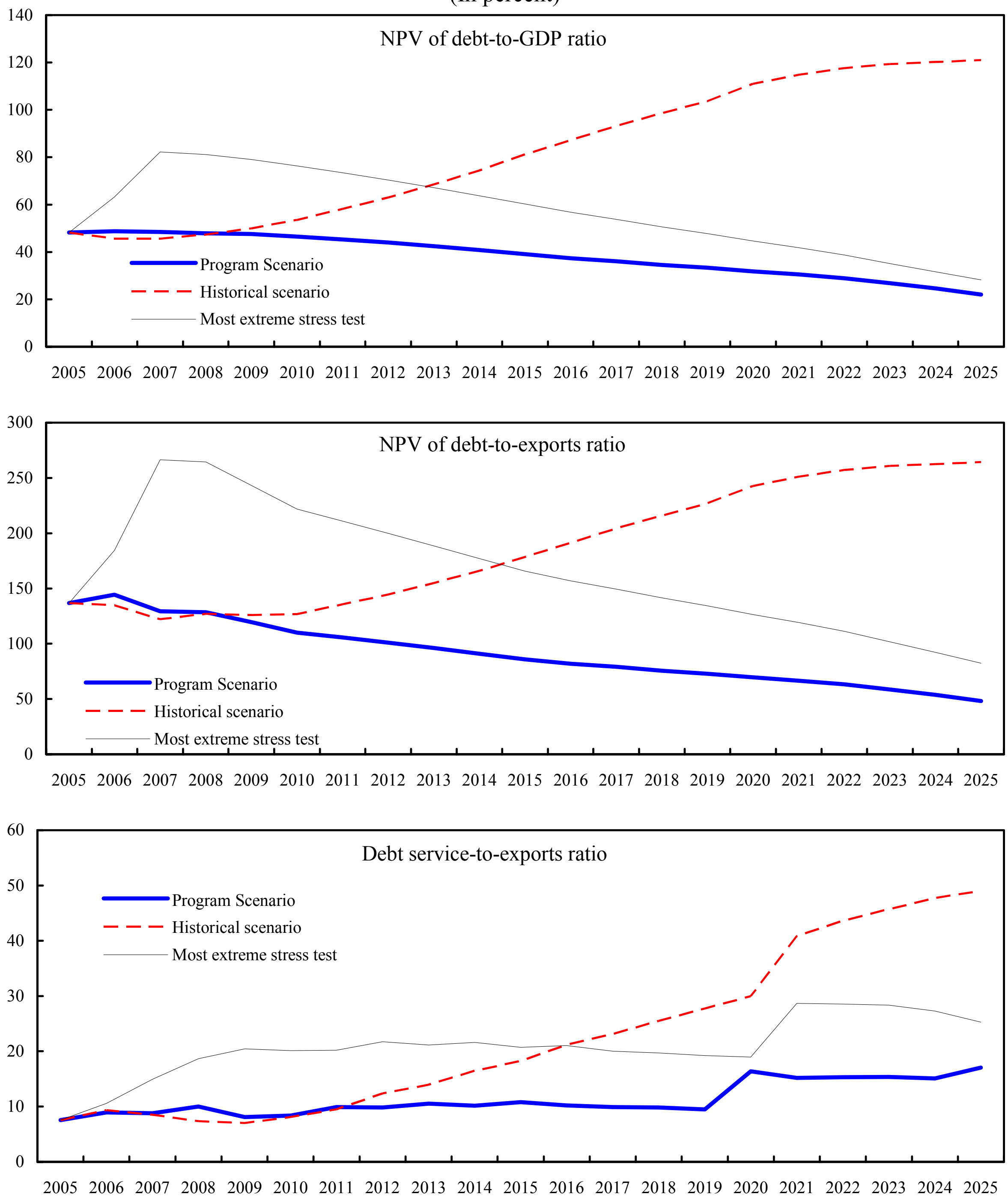
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Figure 1.Grenada: Indicators of Public Debt Under Alternative Scenarios, 2005-2025 1/



Source: Fund staff projections and simulations.
1/ Most extreme stress test is test that yields highest ratio in 2015.
2/ Revenue including grants.

Figure 2. Grenada: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2005–2025
(In percent)



Source: Fund staff projections and simulations.

Grenada—Relations with the Fund
(As of January 31, 2006)

I. Membership Status: Joined: August 27, 1975; Article VIII.

II. General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	11.70	100.00
Fund Holdings of Currency	17.56	150.05
Reserve Position	0.00	0.00

III. SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	0.93	100.00
Holdings	0.02	2.62

IV. Outstanding Purchases and Loans:	**SDR Million**	**Percent of Quota**
Emergency Assistance	5.86	50.04

V. Financial Arrangements: None

VI. Projected Obligations to Fund
(SDR Million; based on existing use of resources and present holdings of SDRs)

	Forthcoming				
	2006	**2007**	**2008**	**2009**	**2010**
Principal	1.10	1.47	1.83	1.46	
Charges/Interest	0.28	0.22	0.14	0.07	0.03
Total	1.38	1.69	1.97	1.54	0.03

VII. Implementation of HIPC Initiative: Not Applicable

VIII. Safeguards Assessment:

Under the Fund's safeguards assessment policy, the Eastern Caribbean Central Bank (ECCB), of which Grenada is a participating government, is subject to a full safeguards assessment. The on-site safeguards assessment was completed on February 20, 2003, and concluded that the ECCB has in place appropriate mechanisms to manage resources, including Fund disbursements and that the vulnerabilities that remain do not present an undue risk. The safeguards assessment proposed specific measures to address these vulnerabilities, which have been substantially implemented by the ECCB.

IX. Exchange Arrangement:

Grenada is a member for the Eastern Caribbean Central Bank (ECCB), which manages monetary policy and the exchange system for its eight members. The common currency, the Eastern Caribbean dollar, has been pegged to the U.S. dollar at the rate of EC$2.70 per U.S. dollar since July 1976. In practice, the ECCB has operated like a quasi-currency board, maintaining foreign exchange backing of its currency and demand liabilities of close to 100 percent. Grenada accepted the obligations of Article VIII, Sections 2, 3, and 4 in January 1994. It maintains an exchange system free of restrictions on payments and transfers for current international transactions.

X. Article IV Consultation:

Grenada is on the standard 12-month consultation cycle. The last Article IV consultation was concluded by the Executive Board on July 13, 2005 IMF Country Report No. 05/290.

XI. FSAP Participation:

Grenada participated in the regional ECCU FSAP conducted in September and October 2003. The Financial System Stability Assessment is http://www.imf.org/external/pubs/ft/scr/2004/cr04293.pdf.

XII. Technical Assistance:

MFD is providing assistance in banking supervision via a peripatetic advisor since 2005.

An FAD mission visited Grenada in April 2004 to provide assistance in the preparations to implement a VAT.

An LEG mission visited Grenada in October 2003 to assist the authorities in drafting VAT and other tax legislation.

An MAE mission visited Grenada in September 2003 as part of the regional FSAP covering the members of the Eastern Caribbean Currency Union.

An FAD mission visited Grenada in October 2002 to provide assistance in tax policy and administration.

An MAE mission visited Grenada in September 2001 to evaluate the Module I self-assessment of the offshore financial sector.

An MAE mission visited Grenada in January 2001 to assist the authorities in preparing self-diagnostic exercises to assess the regulatory framework and operations of the offshore financial sector.

An LEG mission visited Grenada in July 2000 to examine the tax laws and to make recommendations for increasing compliance.

An FAD mission visited Grenada in October 1999 to review the tax system and advise on the feasibility of introducing a VAT.

Caribbean Regional Technical Assistance Centre (CARTAC):

A. Medium-Term Economic Framework

As part of the Structural Adjustment Technical Assistance Program (SATAP), CARTAC assisted Grenada during 2003–04 to design measures to reduce fiscal deficits and stabilize the debt-to-GDP ratio in line with ECCB targets. The exercise was undertaken in collaboration with staff of the Ministry of Finance in an effort to enhance macroeconomic management capacity within the Ministry, including in financial programming.

Work on SATAP was interrupted by Hurricane Ivan but resumed in the summer of 2005. In the wake of the Hurricane, the Government of Grenada requested assistance in developing a Medium-Term Macroeconomic Framework, consisting of three scenarios. One was based on the existing policy framework. The second incorporated a menu of policy measures that would assist in reducing the projected financing gap. The third that incorporated the policy measures and debt restructuring. The missions took place during the third quarter of 2005.

Grenada sent one participant to a Financial Programming and Policies course that was held in November 2005 at the Eastern Caribbean Central Bank in St. Kitts.

B. Fiscal Sector

- CARTAC assisted in preparing a plan for implementing the VAT in January 2006 but it had to be put on hold as a consequence of Hurricane Ivan. The authorities are now planning to introduce the VAT program in January 2008, building on the previous work, including the draft VAT/excise laws (prepared by LEG) as well as the VAT sensitivity study and training/publicity tasks (undertaken with CARTAC/FAD assistance).

- The authorities have approached CARTAC to discuss alternative means of raising revenue in the short term, including through changes in the personal income tax threshold (PIT). The CARTAC program will assist in implementing the latter initiative, tentatively from January 2006, which Parliament passed initially in the form of a reconstruction levy.

- CARTAC provided training to Customs officers in UNIX and ASYCUDA and will assist with migration to ASYCUDA ++. The customs agency needs strengthening to ensure effective collection of tariffs and proposed import VAT and to exchange information with the inland revenue to facilitate compliance.

C. Financial Sector

- In collaboration with OSFI in 2003, CARTAC assisted in drafting legislation to establish the single supervisory agency, GARFIN.

- In 2002, a CARTAC-funded consultant conducted a feasibility study on the establishment of a single supervisory unit for all licensed financial institutions. Comments were provided on proposed changes to the Offshore Banking Act and an expert was recruited to draft revisions to the Act.

- A Corporate Governance Seminar was held for directors, auditors, and service providers in Grenada in 2002. Presentations were made by regional experts on the duties and responsibilities of directors, the application of international accounting standards, and the implementation of an effective anti-money laundering regime.

- Supervisors from Grenada have participated in CARTAC training courses covering banking, credit unions, and insurance companies.

D. Macroeconomic Statistics

CARTAC has provided substantial assistance into improve the production and dissemination of macroeconomic statistics. Many of the initiatives have been undertaken with the collaboration of the Eastern Caribbean Central Bank (ECCB), which offers substantial guidance to the member countries. The CARTAC initiatives include the following:

- Assistance to improve national accounts compilation. Two missions were fielded.

- A mission to assist a rebasing of the consumer price index.

- Initiated a program to develop export-import price indices. The program is ongoing.

- Provided training in the processing of trade data. This was essential as the Customs Department was unable to process documents in the aftermath of Hurricane Ivan in 2004 because of destruction to their computer system.

- A program to improve external sector statistics in the member countries is currently the subject of a major CARTAC/ECCB project.

- The authorities recently requested assistance in the improvement of government finance statistics. In consultation with STA, a mission may be fielded in 2006.

Grenada—Relations with the World Bank Group

(As of January 17, 2006)

In September 2005, the Eastern Caribbean Sub-Region Country Assistance Strategy (CAS) for FY06–09 was presented to the Board of the World Bank. The strategy supports the sub-region's development agenda through two main pillars: (1) stimulating growth and improving competitiveness; and (2) reducing vulnerability, by promoting greater social inclusion and strengthening disaster risk management. Recognizing the OECS countries' weakened creditworthiness due to high debt ratios, Bank activities will focus on leveraging available donor grant financing. Following the recommendations of the recently completed growth and competitiveness study for the OECS, IBRD and IDA support would focus on providing technical and financial assistance for interventions to support the two main pillars. An indicative Base Case lending scenario consists of about US$51.3 million in IDA resources for the four OECS blend countries (Dominica, Grenada, St. Lucia, and St. Vincent and the Grenadines). This number includes the estimated IDA country allocations for each of the four countries during FY06–09, and an IDA Regional allocation of US$15.2 million for two regional projects: US$12 million for Catastrophe Risk Insurance and US$3.2 million for Infrastructure and Utilities Reform. Planned lending to Grenada amounts to US$11.8 million under the Base Case lending scenario and consists of two investment projects: Public Sector Modernization Infrastructure and Utilities Reform.

A. Projects

There are five active World Bank projects in Grenada for a net commitment of approximately US$38 million as well as two Global Environmental Facility (GEF) projects with total commitments of US$8.7 million.

The Grenada **Disaster Management Project**, approved in October 2000, is part of a regional program for the OECS countries to fortify, reconstruct, and/or rehabilitate key economic and social infrastructure and facilities, in order to minimize the potential damage or disruption caused by future disasters, and to improve disaster response and emergency recovery. Of a total program size of US$34 million, Grenada's component is US$10.7 million.

In March 2002, the World Bank approved US$20.9 million in loans and credits to support **Emergency Recovery Projects** in the OECS sub-region, including in Grenada. The projects support efforts aimed at fostering recovery from the fallout of the events of September 11, 2001, including: (i) efforts to safeguard the productive capacity of the tourism sector by securing energy imports; (ii) investments to enhance security at sea ports and airports; and (iii) the development of institutional capacity for security programs as mandated by international civil aviation and maritime transport agencies. The Bank's support to Grenada under this project is for US$3.8 million.

The **Grenada Education Reform Project**, approved in June 2003 for US$8 million, is a follow-up to an earlier education project. Its objective is to build human capital, with a view to contributing to economic diversification and more sustainable growth. Key objectives are to: (i) increase equitable access to secondary education; (ii) improve the quality of the teaching and learning processes, with more direct interventions at the school level and an increased focus on student-centered learning; and (iii) strengthen management of the education sector and to improve governance of schools.

Approved in July 2002, the **HIV/AIDS Prevention and Control Program** is funded under the Multi-Country APL for the Caribbean Region. Its objectives are to: (i) curb the spread of the HIV/AIDS pandemic; (ii) reduce the morbidity and mortality attributed to HIV/AIDS; (iii) improve the quality of life for persons living with HIV/AIDS; and (iv) develop a sustainable organizational and institutional framework for managing the HIV/AIDS epidemic. The Bank's support to Grenada under this project amounts to US$6 million.

In November 2004, the World Bank approved US$10 million in emergency assistance for Grenada to respond to the effects of **Hurricane Ivan**. The project supports the recovery efforts of the government of Grenada through the financing of critical imports and rehabilitation activities in key social sectors.

Grenada is also participating in two Global Environment Facility (GEF) projects. The **Caribbean-Wide Mainstreaming Adaptation to Climate Change Project** became effective in June 2003 and aims to facilitate an enabling environment for climate change adaptation. The project components aim to: (i) build regional capacity to collect and analyze data, thereby expanding the knowledge base on climate change impacts and helping to assess the associated physical and socioeconomic vulnerabilities; and (ii) build in-country capacity to formulate and analyze adaptation policy options and finalize sectoral adaptation strategies for the countries. The project is being executed by the Caribbean Community (CARICOM) and is intended to receive financing of approximately US$10.9 million, of which US$5 million is GEF funding. The **OECS Protected Areas and Associated Alternative Livelihood** became effective December 2004. It aims to remove barriers to the effective management of protected areas, and to increase the involvement of civil society in the planning, management and sustainable use of these areas. The OECS Secretariat will execute the project and receive financing of about US$7.6 million, of which US$3.7 million is GEF funding.

B. Economic and Sector Work

The Bank has completed a series of analytical work relating to: public sector capacity in the OECS including the Institutional and Organizational Capacity Review, the OECS Procurement Assessment Review, and the OECS Financial Accountability Assessment. In conjunction with the IMF, a Financial Sector Assessment Program (FSAP) was completed in early 2004. The Bank also recently completed an OECS study on Growth and Competitiveness. Work is ongoing on a review of large scale energy options for the OECS, under the Energy Sector Management Assistance Program. Grenada also stands to benefit from ongoing Caribbean-wide work on social protection.

For Grenada specifically, the Bank recently completed an Analysis of Fiscal Issues, which examines the management and allocation of public expenditure. In June 2004, **Foreign Investment Advisory Service** (FIAS) conducted a diagnostic review with recommendations to improve the investment climate in Grenada.

Grenada will benefit from ongoing and planned analytical and advisory activities to support the new CAS' two main pillars including the following activities: Caribbean Air Transport Rationalization report, Caribbean Skills and Curriculum Study, Caribbean Recent Economic Developments in Infrastructure study, Caribbean Financial Sector and Regulation report, Caribbean Social projection strategy review, and a regional study on Crime, Violence and Exclusion.

C. Financial Relations[1]

(In millions of U.S. dollars)

Operation	**Original Principal**	**Available[2]**	**Disbursed[2]**
Telecommunications & ICT Development Project	0.54	0.56	0.01
Disaster Management Project	10.07	0.11	10.47
Emergency Recovery Project	3.80	0.46	3.87
Grenada Education Reform Project	8.00	7.45	0.76
HIV/AIDS Prevention And Control Program	6.04	6.12	0.36
Hurricane Ivan Emergency Recovery Project	10.00	6.20	3.88
Total	**38.45**	**20.90**	**19.34**

1/ Includes only IBRD and IDA funded projects and is not inclusive of the two GEF projects.
2/ Amounts may not add up to Original Principal due to changes in the SDR/US exchange rate since signing.

Disbursements and Debt Service (Calendar Year)

	Actual								**Projections**	
	1998	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**
Total disbursements	0.92	1.74	2.64	1.25	6.87	3.79	2.91	6.38	6.03	10.22
Repayments	0.07	0.06	0.07	0.06	0.07	0.10	0.39	0.77	1.44	1.6
Net disbursements	0.85	1.67	2.58	1.19	6.80	3.69	2.52	5.61	4.59	8.66
Interest and fees	0.06	0.05	0.13	0.30	0.33	0.42	0.53	0.60	0.84	1.12

Grenada: Relations with the Caribbean Development Bank
(As of December 31, 2005)

A. Projects

In 2005, Grenada received a package of soft financing from the Caribbean Development Bank (CDB) totaling US$25 million for a number of projects intended to facilitate the recovery and reconstruction process following the devastation caused by Hurricane Ivan on September 7, 2004.

Bridge and Road Improvement Project (BRIMP)

Among the projects is a Bridge and Road Improvement Project which is expected to contribute to the social and economic development of Grenada through improved road infrastructure. A loan equivalent to US$11.9 million was approved to assist the government in financing the reconstruction of approximately 2.1 kilometers of main arterial road in St. George's. The project also includes the replacement of two bridges located on the Western Main Road which have exceeded their design life and have deteriorated substantially and are no longer able to safely support existing and projected traffic. In 2001, CDB's Board of Directors approved a loan for a Bridge and Road Improvement Project, which was significantly advanced at the time Hurricane Ivan struck the island.

Hurricane Reconstruction Support

A Hurricane Reconstruction Support loan equivalent to US$5.4 million was approved to assist the Government in meeting its financial obligations in order to sustain an economic recovery programme.

Disaster Mitigation and Restoration

A loan equivalent to US$5.2 million was approved for this Disaster Mitigation and Restoration project. Grenada has a history of landslides characterized by rapid mass movement of solids on steep slopes. Financing was approved for a project designed to restore essential road infrastructure and to reduce the risk of loss of life and damage to public and private property associated with rock fall and landslip incidents. It is expected to provide cost avoidance benefits by reducing rehabilitation and road-clearing costs in the aftermath of natural hazards.

Sites and Services for Low-Income Earners

Members of low-income households, including certain households located in hazardous areas, will be the main beneficiaries of a loan to the Government equivalent to

US$1.9 million. The financing was approved to improve the shelter conditions of low-income households through the provision of 116 serviced lots at two sites—Soubise and Mount Gay—which will accommodate members of 186 households with the kind of amenities not previously available to them. Persons living in vulnerable areas along beachfronts, steep hillsides and gullies will be relocated to areas which are less susceptible to storm surges, landslides and flooding.

B. Financial Relations

(As of December 31, 2005)
(In millions of U.S. dollars)

Item	2001	2002	2003	2004	2005
Cumulative total credit approved[17]	107.8	112.8	120.7	128.8	157.1
Cumulative disbursements[18]	83.2	88.6	97.0	106.8	121.1
Disbursements					
Ordinary Capital Resources	3.3	1.0	4.7	5.8	5.6
Special Development Fund	2.3	2.5	4.3	3.5	8.0
Other Special Fund Resources	2.3	1.4	0.1	0.2	0.3
Amortization[19]					
Ordinary Capital Resources	0.9	0.7	0.8	0.3	1.3
Special Development Fund	1.4	1.7	1.7	1.7	2.0
Other Special Fund Resources	0.3	0.2	0.2	0.2	0.2
Outstanding debt (end of period)	51.3	55.7	61.2	67.1	78.5
Interest and Commitment Fees					
Ordinary Capital Resources	1.2	1.1	1.1	1.3	1.7
Special Development Fund	0.6	0.7	0.6	0.6	0.8
Other Special Fund Resources	0.1	0.2	0.2	0.2	0.2

Source: Caribbean Development Bank.

[17] Loans and grants.

[18] Including valuation adjustments.

[19] Ordinary capital resources (OCR) are loans on nonconcessional terms. Special development funds (SDF) and other special fund (OSF) resources are soft loans. Commitment fees apply only to OCR.

Grenada—Statistical Issues

Grenada participates in the Fund's General Data Dissemination System (GDDS). Its metadata are posted on the Dissemination Standards Bulletin Board, although these have not been updated recently. The metadata include short- and medium-term plans for statistical development. Improvement in several key areas are needed to facilitate effective surveillance. Some of the outstanding issues are detailed below.

A. Real Sector

There are a number of deficiencies in the real sector statistics. National accounts are provided annually. However, GDP by expenditure is available only with long lags, and real GDP by sector is not available. The estimation of gross capital formation needs to be improved and sectoral price deflators computed. There are discrepancies in the foreign trade estimates prepared by the customs department and the Central Statistical Office (CSO), and coverage, consistency, and timeliness of tourism data are limited.

Consumer prices are the only real sector data provided between missions. The basket used to compute the consumer price index was last updated in 2000. A producer price index is not available.

Labor statistics are limited and outdated, with 1998 being the most recent year for which data are available. There are no regular wage and unemployment data. Data collected during the 2001 population census are still being processed. The CSO is working with the International Labor Organization (ILO) to improve the coverage of labor market statistics.

B. Public Finances

The reporting of central government data has improved in recent years, with data being provided in Fund economic classification format with lags of about two months. However, there appear to be inaccuracies in the composition of public expenditure. Moreover, capital expenditures could include current expenditure items, and the nature of expenditures in the Public Sector Improvement Program needs to be scrutinized carefully. In addition, spending on outsourced activities is not broken down into the appropriate categories, but rather grouped into a single category.

The coverage of the rest of the public sector is very limited, and there are no consolidated public sector accounts. There is no systematic reporting of information to the Ministry of Finance. Annual statements for some public enterprises are provided during Fund missions. It would be useful to institute a mechanism for the regular reporting of financial data pertaining to the rest of the public sector.

The authorities do not report fiscal data for publication in IFS. Grenada has not provided any fiscal data, either on a *GFSM 2001* basis, or a cash basis, for presentation in the *GFS Yearbook*.

C. Monetary Accounts

The ECCB compiles monthly data on commercial banks with a lag of about two months. Information is reported on a regular basis for publication in *IFS*. The Ministry of Finance does not collect data regularly on nonbank financial institutions. Coverage of the offshore financial sector is limited.

Expanding institutional coverage to include nonbank financial institutions, such as credit unions and insurance companies, would enhance understanding of savings and credit as well as improve compilation of monetary aggregates. In addition, improved classification of financial instruments and loan categorization would enhance identification of credit flows to different sectors of the economy.

D. Balance of Payments

The ECCB compiles and reports balance of payments statistics on an annual basis, using information collected by the CSO. The latest data published in the IFS and Balance of Payments Yearbook are for 2002. The authorities and the ECCB should produce and disseminate more timely statistics.

Many of these statistics are based on information collected from surveys, and are not comprehensive. Trade statistics have traditionally been more reliable and available by SITC classification on a quarterly basis. However, reliability and detail of trade statistics have suffered considerably in the aftermath of Hurricane Ivan (September 2004) and reporting is not yet fully back on track
.
Enhanced data sources and better compilation procedures are needed to improve the accuracy of balance of payments statistics. Moreover, quarterly balance of payments statistics and international investment position data are not compiled.

E. External and Domestic Debt

The database for government external debt is quite comprehensive, and can be used to provide detailed and reasonably up-to-date breakdowns of disbursements and debt service. However, data availability on domestic debt, government-guaranteed debt, and debt of public enterprises is limited, and there is no data on private external debt.

GRENADA: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE
AS OF FEBRUARY 28, 2006

	Date of latest observation	Date received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of publication[1]
Exchange Rates[2]	NA	NA	NA	NA	NA
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[3]	Mar 2005	5/3/05	M	M, with 2- to 3-month lag	A/Q
Reserve/Base Money	Dec 2005	2/15/06	M	M, with 2- to 3-month lag	A/Q
Broad Money	Dec 2005	2/15/06	M	M, with 1- to 2-month lag	A/Q
Central Bank Balance Sheet	Dec 2005	2/15/06	M	M, with 1- to 2-month lag	A/Q
Consolidated Balance Sheet of the Banking System	Dec 2005	2/15/06	M	M, with 2- to 3-month lag	A/Q
Interest Rates[4]	Dec 2005	2/15/06	M	M, with 1- to 2-month lag	A/Q
Consumer Price Index	Apr 2005	May 2005	M	M, with 1- to 2-month lag	A/M
Revenue, Expenditure, Balance and Composition of Financing[5] – Central Government	Mar 2005	May 2005	M	Q, with 1- to 2-month lag	A
Stocks of Central Government and Central Government-Guaranteed Debt[6]	Dec 2004	Feb 2005	M/A	Q, with 1- to 2-month lag	A
External Current Account Balance	Dec 2004	May 2005	A	Article IV Mission	A
Exports and Imports of Goods and Services	Dec 2004	May 2005	A	Article IV Mission	A
GDP/GNP	Dec 2004	May 2005	A	Article IV Mission	A
Gross External Debt[7]	Dec 2004	May 2005	Q	Q, with 1- to 2-month lag	A/Semi-annual

[1] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).
[2] Grenada is a member of the Eastern Caribbean Currency Union, in which the common currency of all member states (EC dollar) has been pegged to the US dollar at US$1=EC$2.70 since July 1976.
[3] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[4] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[5] Foreign, domestic bank, and domestic nonbank financing.
[6] Including currency and maturity composition.
[7] Public external debt only.

St. George's, Grenada
March 21, 2006

Mr. Rodrigo de Rato
Managing Director
International Monetary Fund
Washington, D.C. 20431
UNITED STATES OF AMERICA

Dear Mr. de Rato:

Reconstruction activity is proceeding well following the unprecedented 200 percent of GDP damage caused by Hurricane Ivan in September 2004. Visitors to our shores cannot believe the tremendous progress that we have made in such short time, particularly in light of the additional damage and delay caused by Hurricane Emily in July 2005. This success owes much to policies that have sought to cushion the adverse impact of the hurricanes on the population, donor and creditor support, as well as the fortitude of the people of Grenada.

With reconstruction broadly on track, the government has proceeded to prepare and launch a home-grown medium-term reform programme—Enhancing Growth, Poverty Alleviation and Macroeconomic Stability. The objectives and policies the government intends to pursue during 2006–08, with particular emphasis on policies for 2006, are detailed in the attached memorandum of economic policies (MEP). The main goals of the program are to:

- Promote sustained high economic growth by improving the climate for private investment.
- Restore fiscal and debt sustainability through fiscal consolidation and reform.
- Reduce vulnerabilities by safeguarding the soundness of the financial system; and
- Reduce poverty through more effective social development programmes and safety nets.

In support of our economic policies and objectives, the Government of Grenada hereby requests a three-year arrangement under the Poverty Reduction and Growth Facility in an amount equivalent to SDR 10.53 million (90 percent of quota).

We believe that the policies and measures set forth in the attached MEP will achieve the objectives of the programme. The government also stands ready to take additional policy measures as appropriate to ensure the attainment of these objectives. The MEP reflects the objectives for poverty reduction that we outlined in our 2004 Poverty Eradication Strategy, which is being submitted to the Boards of the World Bank and IMF under separate cover as the country's Interim-Poverty Reduction Strategy Paper. Grenada will consult with the Fund on the adoption of these measures, and in advance of revisions to the policies contained in the MEP, in accordance with the Fund's policies on such consultation. We expect the first review under the arrangement to be completed by September 15, 2006 and the second review by March 15, 2007. The government authorizes you to make public the contents of this letter and MEP as well as the accompanying staff report.

Yours sincerely,

____________/s/___________
Honorable Anthony Boatswain
Minister of Finance

GRENADA—MEMORANDUM OF ECONOMIC POLICIES

I. INTRODUCTION

1. **Our country is recovering from one of the most difficult periods in its recent economic history.** Grenada has been severely affected by several external shocks in recent years: the September 11, 2001 attacks in the United States which triggered a recession in 2001–02, Tropical Storm Lili in 2002, Hurricane Ivan in September 2004 (causing an unprecedented 200 percent of GDP damage), Hurricane Emily in July 2005 (which caused additional 12 percent of GDP damage), and, more recently, high world oil prices. As a result, economic growth has fluctuated sharply since 2001, and unemployment and poverty have risen. The poverty eradication and fiscal consolidation programmes that we had initiated before Hurricane Ivan struck have also been derailed. Reconstruction needs remain substantial, while fiscal imbalances, financing gaps and the public debt burden are high.

2. **The nation has nonetheless made significant strides in recent months**. Visitors to our shores cannot believe the tremendous progress that we made in such short time. Notwithstanding the additional delay and damage caused by Hurricane Emily in July 2005, there are indications that more than 60 percent of the 28,000 housing units damaged by Ivan have had some repairs done to them—though an additional 9,000 dwellings have yet to be brought on stream. And while activity in the agriculture sector remains subdued, in the tourism sector some 85 percent of the pre-Ivan capacity had been restored by end-2005. This success owes much to policies that have sought to cushion the adverse impact of the hurricanes on the population, donor and creditor support, as well as the fortitude of the people of Grenada.

3. **We have also begun to address the fiscal challenges we are facing.** Particularly in the aftermath of Ivan, the large financing gaps that emerged have been filled with all stakeholders—donors, creditors and the people of Grenada—sharing the burden:

- There has been significant international donor pledges following Hurricane Ivan. To date, US$110 million of the US$290 million that had been pledged following Hurricane Ivan has been disbursed.

- A successful debt exchange involving our commercial creditors was concluded on November 15, 2005, resulting in substantial lowering of debt service payments for the next few years.

- To contribute our share and thereby eliminate remaining financing gaps, we have taken a number of fiscal measures, including a levy on incomes to fund the reconstruction effort and a 45 percent increase in retail fuel prices.

4. **With reconstruction broadly on track, the government is now shifting its focus to addressing the longer-term economic challenges that our country faces**. Our economy needs to be revitalized. We need to once again return to the growth and stability that

prevailed before the recent shocks. To this end, in the last several months, we have been developing a comprehensive medium-term reform programme, with the help of CARTAC. The rest of this memorandum outlines key elements of this home-grown programme for 2006–08—Enhancing Growth, Poverty Alleviation and Macroeconomic Stability. The reform programme, and in particular the fiscal reform package for 2006, has benefited from input provided during the broad-based national budget consultations held in November 2005, drawing participants from the main opposition party, trade unions, business groups, as well as members of civil society.

II. Recent Developments and Outlook

5. **Economic recovery is underway:**

- With the reconstruction activity proceeding well, output is estimated to have recovered by around 1½ percent in 2005 after contracting 3 percent in the previous year. Conditions in agriculture and tourism remained weak, although activity has resumed in some areas.

- Average inflation is estimated 3½ percent for 2005, although inflation was higher at the end of the year, reflecting the recent increase in fuel prices.

- Fiscal performance in 2005 benefited from one-off factors that have boosted revenues, including from the high levels of imports of reconstruction materials, while current spending was lower than budgeted.

- Prudential indicators for the banking system showed relative stability through the first half of the year, although there was a marginal deterioration in the third quarter. Meanwhile, credit growth to the private sector recovered modestly in 2005.

- The external current account deficit is estimated to have widened sharply to about 37 percent of GDP on account of high reconstruction material imports and low tourism receipts.

6. **Growth is expected to recover in 2006 reflecting continued reconstruction activity, preparations for the hosting of the World Cricket Cup in 2007, and a pick-up in tourism.**

- Real GDP growth of 6–6½ percent is projected for 2006. Beyond 2006–07, growth of 4 percent would need to be sustained through growth-enhancing reforms.

- Average inflation for 2006 is expected to be 4½ percent, on account of the recent fuel price increase, although by year-end inflation should decline to 2 percent. Beyond 2006, inflation of 2 percent is projected.

- Fiscal measures and reforms will cover a financing gap of over 5 percent of GDP (EC$70 million) for 2006, because external grants are expected to decline and expenditure to remain high. The gaps would have increased in the outer years.

- The external current account deficit is expected to narrow in 2006 to some 33 percent of GDP. While exports are likely to remain broadly unchanged, imports are expected to decline marginally and tourism earnings to recover somewhat. The deficit is expected to be financed partly by foreign direct investment and capital grants.

III. Objectives of the Reform Programme

7. **The strategic objectives of our reform programme for 2006–08 are fourfold—sustained high economic growth, restoring fiscal and debt sustainability, reducing vulnerabilities, and alleviating poverty**. These objectives are essential for the improvement of our economic circumstances and our aspirations of higher standards for Grenadians. They also need to be advanced in tandem given the interlinkages among them. High economic growth is necessary to allow rapid poverty reduction and ease the burden of fiscal consolidation. Fiscal reform, in turn, is required to ensure that public debt sustainability is achieved in an orderly manner and maintained, fiscal imbalances do not become a drag on growth, and to help pay for initiatives to alleviate poverty. Reducing vulnerabilities, including by safeguarding the soundness of the financial sector, is essential to ensure the durability of growth. Finally, alleviating poverty is the imperative that motivates our social development agenda.

Sustained high economic growth

8. **As our Poverty Eradication Strategy highlights, improving the standard of living of our citizens is the overriding objective of government's economic policies.** This in turn requires sustained high economic growth (at least 4 percent), with the private sector playing a more vibrant role than in the past. To this end, the near-term focus of our structural reforms will be to put in place a policy environment that is much more conducive to private investment. This will include steps to ensure that Grenada Industrial Development Corporation (GIDC), our investment promotion agency, starts to play a more prominent and proactive role in promoting the country as an attractive investment destination, improving the manner in which land can be acquired by investors, as well as comprehensive reforms to improve the tax system's transparency and predictability. The planned Public Sector Modernization Project will also serve to make the rest of the public sector more efficient, customer oriented and productive. Reforms in the second and third years of our programme will focus on measures to enhance labor and product market flexibility, respectively.

Restoring fiscal and debt sustainability

9. **We recognize that, in the absence of reforms, Grenada's fiscal and public debt situation is unsustainable**. The public debt stock is very high at 130 percent of GDP—or some EC$15,000 for each Grenadian. Without fiscal consolidation, by about 2010, virtually

all of the tax revenues that the government collects would be spent on civil service salaries and interest payments, leaving little room for outlays on goods and services or transfer to households, much less capital investment.

10. **Accordingly, an important element of our reform programme is to restore debt and fiscal balances**. We have designed and phased our fiscal programme so that it will sustain the current economic recovery. In particular, the programme will facilitate the capital investment required in 2006 and 2007 to ensure that the ongoing reconstruction effort and preparations for the 2007 Cricket World Cup can be completed successfully. At the same time, with the adoption of a number of important revenue and expenditure measures, the fiscal reform package will allow the fiscal accounts to swing gradually from an underlying primary deficit of 2 percent in 2005 to a primary surplus of 2.5 percent of GDP in 2008. Providing the surplus is kept at this level thereafter, our public debt will decline sharply to the more prudent—although still high—level of 60 percent of GDP by around 2015.

Reducing vulnerabilities

11. **The durability of the current recovery also depends on attenuating vulnerabilities to natural disasters and safeguarding the soundness of the financial sector.** Grenada has traditionally been considered to be outside the hurricane belt. But recent events suggest that this may no longer be the case, and accordingly our preparedness for extreme weather events needs to be strengthened considerably. To this end, our programme aims to improving adherence to the building code and encouraging citizens to acquire insurance. Our reform programme also aims to address other sources of vulnerability for our economy, including by safeguarding the soundness of the financial sector.

Reducing poverty

12. **Social development, particularly by alleviating poverty, is the other important programme objective**. Social conditions have deteriorated in the aftermath of Hurricane Ivan. The unemployment rate stood at 19 percent in July, and was especially high among women (more than 25 percent) and youth (more than 30 percent). While data collection on social indicators needs strengthening, preliminary indications are that the poverty rate is likely to have risen. To reverse these trends and guide our social development agenda in the coming years, we will start preparing in the coming months a comprehensive poverty reduction strategy paper (PRSP), which will update and expand the Poverty Eradication Strategy prepared in 2004. The 2006 budget will also focus on introducing social safety nets for the poor and vulnerable of our society, particularly those worst hit by the increase in domestic fuel prices to world market levels in October.

IV. FOSTERING ECONOMIC GROWTH

13. **To promote private sector activity and achieve high economic growth rates and better employment prospects over the medium term, our reform programme envisages several measures to improve the investment climate**. Higher private investment is critical to sustain growth beyond 2007, once the positive effects on output from the ongoing

reconstruction activity and hosting of the 2007 Cricket World Cup subside. The economy has, traditionally, been well diversified, and we want to maintain this feature of our economy. To this end, increased investment in and a recovery of, in particular tourism and agriculture, is needed.

14. **To address these challenges and improve the investment climate, the following measures are envisaged for 2006**. These measures will complement intended reforms to the tax incentives regime and our continued commitment to ensuring the soundness of the financial sector (see below):

- ***Strengthening investment promotion***. We intend to review the role of Grenada Industrial Development Corporation (GIDC) with a view to improving its effectiveness in promoting new investment. Over the years, GIDC's focus has shifted to one of screening requests for tax incentives, reflecting the limited resources available to the agency as well as the high administrative cost associated with the current tax incentive system. But with the planned simplification and rationalization of the tax incentive regime (see below), GIDC should be able to focus on its core mandate: promoting Grenada as a favorable investment destination, including in the tourism sector. This should include steps to turn GIDC into a one-stop shop for investors. In a similar vein, the due diligence process for new investments will be strengthened, so as to allow for better assessments of the viability of projects.

- ***Investment code***. The government is in the process of preparing a new investment code to be legislated by September 2006. This code will, inter alia: improve and clarify the legal system for investment in Grenada; outline investor rights and obligations; detail investment procedures; and the means to access fiscal incentives.

- ***Facilitating land transactions***. To facilitate private investment and improve the efficiency of land use, the following initiatives are planned:

  - A project has been initiated to upgrade the land registry with a view to enhancing the accessibility of the records therein to the public, including with respect to information on leaseholds of public lands granted by our government, the duration of these leaseholds, and to whom they have been granted. This project will be completed by end-2006.

  - Second, a new executive agency to manage issues related to land use will be established by end-2006, pulling together the valuation section of the Ministry of Finance, the land and surveys division of the Ministry of Agriculture and the Registry at the Supreme Court.

  - Third, all significant future divestments of public properties will take place through well advertised international auctions, so as to attract the widest possible range of investors and enhance transparency.

- ***Simplifying customs clearance.*** The envisaged reforms at the Customs Authority (see below), will seek to reduce the amount of paper work and time (currently as much as four days) needed to clear imports through the ports.

- ***Implementing export strategy***. We have recently initiated preparations for a National Export Strategy (NES). This initiative, which is being carried out in close partnership with private sector stakeholders and NGOs, seeks to support and promote existing and potential export sectors through a comprehensive and consistent set of policies. These policies pertain in particular to the general business environment, training, trade liberalization, trade promotion, the reduction of transaction costs (including through customs reform), and the institutional strengthening of the "trade support network" that comprises various relevant public and private sector bodies. The strategy will also seek to exploit possibilities for the creation of support industries around specific clusters of activity—in particular around tourism. We will seek to complete the NES by mid-2006.

15. **Beyond the measures slated for 2006, our reform program envisages action in several other areas over the next three years**. In particular, to enhance labor market efficiency and flexibility, we will launch a review to assess the effectiveness of the market. Measures are also envisaged to tap the large expatriate community of our country, including in the areas of skills development and training, investments (especially in entrepreneurship and small businesses) and finance. Furthermore, to foster the functioning of markets and efficient allocation of productive resources, we plan to abolish most of the small number of price controls except on a few essential items. And finally, we will explore the role of the financial sector in enhancing small business development.

V. Restoring Debt and Fiscal Sustainability

16. **The fiscal measures we have undertaken over the past year, coupled with reforms discussed below, will help restore debt and fiscal sustainability.** A critical mass of these measures have been undertaken in the context of the 2006 budget and early in the programme period. The fiscal programme is also consistent with the goals of improving the structure and efficiency of public finances; reducing poverty, including to achieve the Millennium Development Goals; and enhancing the investment climate. It comprises revenue and expenditure measures, structural reforms, and a debt strategy.

A. Fiscal Measures

Revenues

17. **In light of the need for additional revenues to finance the reconstruction effort, we have introduced a national reconstruction levy on wages and salaries for a period of three to five years.** The levy has been approved by Parliament, and collections will commence on income earned starting on January 1, 2006. The levy is 5 percent (3 percent during January 1 to June 30, 2006) for those earning salaries of EC$1,001–5,000 per month, EC$225 per month for those earning between EC$5,001 and EC$9,000 per month, and

EC$350 per month for those earning above EC$9,000 per month. While the levy entails an additional burden on the population, it is necessitated by the large financing gaps the government faces. The design of the levy takes into account the fact that personal incomes below EC$5,000 per month are exempt from income taxes. To ensure that the levy is collected promptly and efficiently, we have provided additional resources to the Inland Revenue Department (IRD) and put in place a software module that will help with the management of the levy. Our aim is to collect EC$10.5 million per year, about ¾ percent of GDP.

18. **Having kept domestic petroleum prices unchanged for sometime to ease the burden on the public following Hurricane Ivan, we adjusted domestic prices in October to reflect developments in world market prices, and will introduce an automatic fuel price mechanism shortly**. We raised domestic fuel prices by over 45 percent on October 1, 2005, which has helped to eliminate the subsidy that resulted in the build-up of about 2 percent of GDP in liabilities to the oil importing companies. We are now in the process of introducing a transparent, automatic fuel pricing mechanism which includes a total tax element of at least EC$2 per gallon. This measure could generate EC$16–20 million per year. To mitigate the adverse effect of the recent price adjustment on vulnerable groups, we are putting in place social safety nets (see below). To facilitate transparency, we have cleared all outstanding obligations to one of the oil importing companies, and reached agreement on a repayment schedule with the other company. The outstanding liabilities have also been added to our debt stock.

19. **In addition, we will undertake administrative improvements, collect on tax arrears, and revise property valuations.**

- *Improving tax administration.* We will seek further technical and financial assistance to strengthen administration at the Customs and Excise Department, including possibly by hiring specialized private firms with experience in helping other countries improve customs revenue collections procedures. We will also seek assistance in strengthening the audit capacity at Customs and in the Inland Revenue Department, and tightening enforcement, including by introducing systems to enhance information exchange between the departments. We plan to commence formulating and implementing reforms in these areas in the second half of 2006.

- *Nontax revenues.* The project planned to upgrade the land registry should help to boost the collection of fees and arrears related to leaseholds. Plans are also underway to improve collection of company registration fees by end-2006, and we are in the process of examining the need to adjust other fees and charges that have remained unchanged for long periods. These initiatives will be complemented by administrative steps that we are taking to improve the collection of nontax revenues.

- *Property taxes.* Property taxes on buildings are paid on values as at 1994. Consequently, work needs to commence on a comprehensive cadastre that will allow us to revalue all land and property to reflect current market values. We will also examine the possibility of making legislative changes to allow the Inland Revenue Department greater leeway in using alternatives to property-by-property inspections in determining the value of these assets.

Spending reform

20. **In light of the destruction and suffering caused by Hurricane Ivan, compressing public wages is not an option and accordingly the programme will try and protect real wages**. To this end, we will seek early agreement with the civil service unions on the wage path for 2006–08 in line with the projected evolution of average annual inflation, following discussions in the context of the multipartite committee that has been established. Provided growth accelerates, the wage-to-GDP ratio should decline, helping reverse the recent rapid increase in the wage bill (by about 35 percent in the last five years).

21. **We will also strengthen PSIP planning and implementation so as to undertake only projects with high social and economic rates of return.** We will seek the assistance of the international donor community, specifically the Caribbean Development Bank and the World Bank, to screen all projects above EC$5 million. This will result in a streamlined and effective capital expenditure programme to meet the needs of the economy. Moreover, the PSIP would be made consistent with the objectives for poverty reducing to be laid-out in the forthcoming poverty reduction strategy paper. Once the reconstruction and the World Cup Cricket related projects are completed, the capital budget would decline to about EC$130 million, or 8 percent of GDP, by 2008. A higher capital budget will depend on higher grants and concessional financing being available.

22. **We are undertaking additional measures to control and lower expenditures.** These include:

- *Goods and services spending*: subjecting government procurement to competitive bidding, including for outsourced services. With assistance from the World Bank, we will strengthen procedures for monitoring and reviewing contracted services to ensure that they are delivered as contracted. Together with further control on other spending, potential savings are expected to be about ½ percent of GDP by 2008.

- *Transfers and subsidies:* in light of the dislocation that the sharp increase in oil prices is likely to have caused, we have made provision for well-targeted social safety nets for the elderly poor and needy students of about EC$5 million in the 2006 budget.

23. **In sum, by implementing the above measures, we have targeted about one-quarter of the underlying medium-term fiscal consolidation in the 2006 budget.** On the revenue side, the national reconstruction levy will generate around ¾ percentage points of GDP per annum. Expenditure savings would come from keeping wage increases constant in real terms. A primary deficit (excluding grants) of EC$110 million (7¾ percent of GDP) is targeted under the 2006 programme. Consistent with this, we will avoid supplementary budgets (or special warrants) that will increase spending without matching tax revenues and/or higher grants.

B. Fiscal Reforms

24. **To improve the structure and efficiency of public finances as well as to facilitate growth enhancing reforms, our programme includes comprehensive tax and civil service reform**. Widespread use of inefficient tax concession instruments has resulted in a substantial erosion of the tax base. Civil service reform is also needed to allow decompression of the wage scale and reward performance and to improve the quality and efficiency of government services. Beyond this, we will improve fiscal transparency and reporting, including for statutory bodies.

Tax reform

25. **We will introduce a value-added tax (VAT) by January 1, 2008.** Work on this had commenced before Hurricane Ivan struck, and this now needs to be revived. The VAT will replace the existing consumption tax that applies on a relatively narrow base and has multiple and varying rates for domestic and imported goods. To broaden the base, the VAT will only incorporate standard exemptions (financial, education, and health services, etc.) with a zero rate for exports and a single non-zero rate for all other goods and services. The VAT and accompanying system of excises will be calibrated to be broadly revenue neutral.

26. **The government has initiated reforms to the current costly and complex system of tax incentives.** During 2000–02, revenue forgone from import duty and consumption tax concessions was nearly 11 percent of GDP. In 2003–04, we took steps to curtail concessions, although these efforts were set back by Hurricane Ivan. Going forward, we will publish all new concessions granted on a quarterly basis starting in June 2006, with information on the beneficiaries of tax concessions, their intended purpose, and the cost of the concessions in terms of revenue foregone. Specific reforms in this area will include:

- **Income tax.** Effective January 1, 2006, the government will not grant any new tax holidays or renew expiring ones; incentives thereafter will be provided in the form of tax write-offs for investment and after June 30, 2006 through accelerated depreciation with loss carry forward provisions. We will discontinue the granting of tax holidays because they are an inefficient tool to promote higher investment, provide incentives for investors with short horizons, and continue to bestow tax relief irrespective of whether further new investments are made. In contrast, a system that relies on accelerated depreciation has the benefit of providing tax relief for those undertaking new investments. Moreover, such reforms are consistent with the new CARICOM guidelines on tax incentives. Accordingly, we will submit to Parliament amendments to the Income Tax Act by end-April to allow us to adopt a system of accelerated depreciation and five-year loss carry forward for investments. There will be no renewal of existing holidays, although holidays currently in effect will be grandfathered. Until the legislative amendments are put in place, tax incentives, where warranted, will be granted in the form of tax write-offs, as has been the practice in most instances in the last few months.

- **Consumption tax.** Reforms to concessions on consumption taxes will occur in the context of VAT introduction by January 1, 2008. All consumption taxes will be repealed and replaced with a broad-based VAT with a low rate and few exemptions. Until the introduction of the VAT, we will not renew expiring consumption tax concessions.

- **Import duties.** We will also initiate a review on options for reform of the import duty regime for completion by end-September 2006. This review will, inter alia, consider the need to provide import duty exemptions for exporters, including in the tourism sector. The objective of the review will be to reduce the scope of exemptions currently provided for in SRO/37/99.

- **We will also repeal the Investment Code Incentives and Qualified Enterprises Acts by end-June, 2006**. These little used acts will not be necessary once the new incentive regime for income taxes is put in place, and will accordingly be repealed.

27. **Beyond this, provided the revenue situation permits, we will announce a firm timetable to lower the corporate income tax in a gradual manner to promote higher private investment.** One possibility would be to lower the tax rate gradually to 25 percent over the 2007–10 period. Across the region, there has been a move towards lower corporate tax rates to encourage new business creation and expansion of existing businesses. A reduction in the rate from 30 percent to 25 percent would cost about EC$5 million per year. The tax cut would benefit small-and medium-scale enterprises and promote economic diversification.

Civil service reform

28. **We are undertaking reforms to enhance the performance appraisal system in the civil service and improve the efficiency and quality of government services, including through commercialization.** With assistance from the World Bank, we are undertaking a Public Sector Modernization Programme that will be implemented during 2006–10. We have maintained a freeze on public sector positions since 2000, although reforms are needed, given considerable outsourcing of government services in the interim. The civil service reform programme that we plan to undertake in 2007 will, inter alia, examine the need for greater flexibility in employment and separation decisions, decompression of the wage scale to reward (and retain) high performers, as well as the need to rebalance the civil service mix towards more professional and fewer clerical staff.

Fiscal transparency and institution building

29. **Improving the transparency of public finances and strengthening fiscal monitoring are important goals of our reform programme.** To this end, we will implement the following measures:

- Every quarter, we will disseminate information publicly on the overall fiscal and economic situation, possibly through press briefings or presentations in Parliament and on the government's official website.

- We will strengthen budget accountability by making the Audit Department fully operational and enforcing regular auditing procedures.

- All expenditures will be reported on the budget, including the expenditures of the Grenada Reconstruction and Development Fund and transfers to the Agency for Reconstruction and Development.

- The budget formulation will include quarterly projections of gross financing needs as well as targets and performance indicators.

- The formulation of the PSIP and reporting by line ministries of capital spending will be improved by establishing monthly reporting of capital expenditures.

- We will require public enterprises to submit audited financial statements at the close of the financial year, as stipulated by law. To facilitate close monitoring of developments in their financial accounts, we will establish a mechanism in 2006 for quarterly reporting (with a one-quarter lag), which would serve as an early warning system. The financial conditions of these entities will be reviewed and financial management guidelines will be prepared.

C. Debt Strategy and Privatization

30. **Our government's debt exchange offer has been a resounding success**. Holders of over 90 percent of eligible claims participated in the exchange, providing substantial and necessary near-term cash flow relief. We will make good faith efforts to dialogue constructively with those creditors with eligible claims that did not participate in the exchange. Wherever possible, we will reach out to them.

31. **We also intend to intensify our dialogue with official creditors and request debt relief on terms comparable to those provided under the debt exchange offer.** In keeping with best international practices, we are committed to the principle of inter-creditor equity. After seeking Fund support for our programme, we will approach our Paris Club and non-Paris Club creditors for relief.

32. **We are undertaking steps to enhance our debt management capacity and transparency.** With assistance from the Commonwealth Secretariat and the ECCB, we are upgrading the debt recording systems. We will develop further and implement a debt management strategy with a view to improving the debt profile and lowering vulnerabilities, including through retiring expensive debt with any financing surpluses that accrue and asset sales.

33. **We are considering divesting remaining government assets and using the proceeds to retire debt and to finance approved capital expenditures subject to strict rate of return analysis**. While most of the privatization and divestiture occurred in the 1990s, our government retains small share holdings. We are also in the process of acquiring assets related to government guarantees that were called. Sales of the assets will be conducted through a transparent bidding process. The proceeds from the sale will be used to reduce the high level of public debt. We will consider carefully the timing of the asset sales. While early sale of some assets is desirable to avoid damage to partially completed tourism projects to which some of the guarantees pertain, sales of too many assets at the same time could signal distress sales and depress prices.

VI. Reducing Vulnerabilities

34. **To safeguard the soundness of the financial system**, our government will:

- **Request the ECCB to undertake an on-site inspection of the banking system before end-2006**. Aggregate prudential indicators show that commercial banks are generally in good shape, with adequate capitalization and loan-loss provisioning. Nonetheless, the damage to housing stock as well as slowdown in economic activity caused by Hurricane Ivan may have placed bank balance sheets under stress, and an on-site inspection will be important to ensure that banks remain adequately capitalized going forward.

- **Enact the Grenada Authority for the Regulation of Financial Institutions (GARFIN) legislation.** To strengthen the supervision of the banking sector, we have passed a new Uniform Banking Act in August, making us one of the first countries in the region to do so. Our banks are now supervised under this new Act. To strengthen the supervision of the nonbank financial sector that includes the insurance sector, cooperatives, the offshore sector and money changers, we will introduce the GARFIN Act in Parliament in January next year, with a view to having it enacted by March. The Act would establish a single supervisory agency for the nonbank financial sector. Furthermore, we intend to increase staff resources devoted to supervising the sector.

35. **The durability of the current economic recovery also depends on our ability to diminish the impact of natural disasters**. To this end, we intend to:

- ***Enforce the building code***. We will consider whether this code should be given the force of law. Its enforcement will also be stepped-up.

- ***Strengthen the regulation of the insurance sector***. Enactment of the new Insurance Act will help ensure contract certainty, improve confidence in the sector, and better protect policyholders.

- **Participate in regional initiatives**. We will actively look to participate in the World Bank's Catastrophic Risk Insurance Project, which is designed to pool insurance risk across the countries.

VII. Social Development

36. **We are in the process of prioritizing our social development agenda, building on the extensive work that was done in recent years.** A Poverty Eradication Strategy was prepared in 2004, and more recently we have undertaken a Core Welfare Indicator Questionnaire as well as a Macro-Socio-Economic Assessment of Damage by Hurricanes Ivan and Emily. These initiatives are in addition to the many programmes already included in the 2006 budget to further social development, such as the support to farmers and construction of low-income housing units. Building on all of these initiatives, we will rely on an updated version of the 2004 Poverty Eradication Strategy as our Interim Poverty Reduction Strategy Paper (PRSP). And a full-fledged PRSP will be elaborated in 2006 through a broad consultative process. This document will aim at sharpening the focus and coherence of the poverty reduction initiatives, ensuring that scarce resources are better directed to the neediest members of society. In addition, it will link the poverty reduction objectives closely to the social development programmes in the budget, while ensuring consistency with the overall macroeconomic and fiscal objectives. More specifically, the PRSP will:

- *Adopt a forward-looking and strategic approach***,** clearly defining the goals for poverty reduction and spelling out steps needed to achieve our poverty reduction objectives, including the Millennium Development Goals (MDGs).

- *Evaluate the effectiveness of existing poverty alleviation programmes*, with a view to making better use of empirical evidence to assess programme effectiveness. In addition, it will define which institution or agency is responsible for assisting in achieving which objective; the size, financing, and duration of programmes; and the modes and timeframe of implementation.

- *Prioritize programmes and policies according to their desirability and social effectiveness*. Detailed costing—separating investment outlays from expected recurrent costs for future maintenance and operation—will be made part of the cost-benefit analysis, to facilitate the evaluation of consistency with the fiscal objectives of the macroeconomic framework, the PSIP, and available domestic and external resources.

37. **In the 2006 budget, we plan to put in place a social safety net to help the most vulnerable segments of society cope with new challenges**. Long-term social development efforts need to be supplemented by targeted social safety net measures: (i) to ensure that progress in poverty reduction is not rolled back by the effects of the hurricanes; and (ii) to protect the most vulnerable segments of the population from the side-effects of policy actions such as retail fuel price increases. In this vein, the 2006 budget will include:

- An increase in the monthly transfer to needy elderly persons, mainly in rural areas, from EC$100 to EC$135 at a budgeted annual cost of about EC$4 million; and

- A scheme to temporarily subsidize the increase in bus fares for about 2,000 tertiary students at a budgeted annual cost of EC$1–1.5 million is also being considered. Given the seemingly permanent nature of the increase in international oil prices, this subsidy will be phased out over time.

Table 1. Grenada: Structural Benchmarks for 2006

	Category	Target Date
Fiscal reforms		
Reach agreement on public service wage path for 2006–08	Benchmark	End-April 2006
Initiate comprehensive reforms to Customs administration	Benchmark	End August 2006
Initiate work to strengthen PSIP planning and implementation by seeking CDB and/or World Bank assistance in screening projects above a threshold (EC$5 million)	Benchmark	End June 2006
Publish information on all new concessions granted from January 1, 2006		End-June 2006
Stop granting new tax holidays or extending holidays		January 1, 2006
Amend Income Tax Act to adopt a system of accelerated depreciation and five-year loss carry forward	Benchmark	End June 2006
Repeal Investment Code Incentives Act, Qualified Enterprises Act, and tax components in all other incentives legislation including Hotel Aids Act and Fiscal Incentives Act	Benchmark	End June 2006

Table 2. Grenada: Quantitative Performance Criteria (PC) and Indicative Targets (IT) for 2006

	31-Mar (IT)	30-Jun (PC)	30-Sep (IT)	31-Dec (PC)
Performance Criteria:				
(In millions of EC$)				
Central government primary balance excluding grants (floor) 1/2/	-40	-60	-90	-110
Stock of central government domestic arrears (ceiling) 3/	22	22	22	22
(In millions of US$)				
Contracting and guaranteeing of nonconsessional external debt by the central government with maturity of at least one year (ceiling) 1/	16	16	16	16
Stock of external short-term debt (ceiling) 3/	0	0	0	0
Central government or guaranteed external arrears accumulation (ceiling) 3/	0	0	0	0
Indicative Target:				
(In millions of EC$)				
Change in net credit of the banking system to the public sector (ceiling) 1/ 4/	0	0	0	-33.5

1/ Cumulative.
2/ Floor will be adjusted downward to the extent grants exceed programmed amounts; and adjusted upward for shortfalls in grants exceeding EC$25 million.
3/ To be monitored on a continuous basis.
4/ Ceiling will be adjusted upward to the extent that grants fall short of programmed amounts up to a limit of EC$25 million.

GRENADA: TECHNICAL MEMORANDUM OF UNDERSTANDING

1. Grenada's performance under the Poverty Reduction and Growth Facility (PRGF), described in the letter of the Government of Grenada dated March 21, 2006, will be assessed on the basis of the observance of quantitative performance criteria as well as compliance with structural performance criteria and benchmarks. This Technical Memorandum of Understanding (TMU) defines how the quantitative performance criteria and indicative targets, specified in Table 2 of the Memorandum of Economic Policies (MEP), will be interpreted. It also lays down the monitoring and reporting requirements. The Grenadian authorities are committed to continue transmitting to the Fund staff the best data available and any revisions thereof.

2. The variables mentioned herein for the purpose of monitoring the performance criteria, which are not explicitly defined, are consistent with the Government Financial Statistics (GFS). For variables omitted from the TMU which are relevant for the program targets, the authorities of Grenada shall consult with the Fund staff on their appropriate treatment, based on GFS principles and Fund program practices.

I. GENERAL DEFINITIONS

3. For the purpose of the program, **central government** will cover all items included in the government budget, including transfers to the Agency for Reconstruction and Development.

4. The **nonfinancial public sector** is defined as the total of the central government and nonfinancial public enterprises. In addition to the Agency for Reconstruction and Development, public enterprises include: Grenada Ports Authority; Grenada Airport Authority; National Water and Sewerage Authority; Housing Authority of Grenada; Grenada Industrial Development Corporation; Grenada Solid Waste Management Authority; Gravel, Concrete and Emulsion Production Corporation; Market and National Importing Board; Grenada Postal Corporation; Grenada Board of Tourism; Grenada Bureau of Standards; Grenada Cultural Foundation; Grenada Craft Center; Grenada Commercial Fisheries Company; Grenada National Lottery Authority; Grenada National Stadium Authority; Grenada Food and Nutrition Council; National Telecommunications Regulatory Commission; and Grenada International Financial Services Authority.[20] Any new nonfinancial public enterprises that are established during the program period will normally also be covered under this definition.

[20] Excluded are the Banana, Cocoa, and Nutmeg Associations and the Minor Spices Co-operative Society as these are cooperative entities owned largely by private sector shareholders.

5. **External debt** is defined as all debt owed to creditors residing outside of Grenada, while **domestic debt** covers all debt owed to residents of Grenada. For ease of monitoring, all bonds issued at the Regional Government Securities Market (RGSM) will be regarded domestic debt.

II. Performance Criterion on the Primary Balance of the Central Government Excluding Grants

6. The **central government primary balance excluding grants** will cover the activities specified in the budget and is derived as shown in Table 1 below. Revenues will not include any proceeds from the sale of public assets exceeding EC$1 million, which will be considered as financing, below the line. Expenditure will include transfers to public enterprises.

Table 1. Performance Criterion on the Primary Balance before Grants

Revenues	a
Grants	b
Current primary expenditure	c
Capital expenditure	d
Interest payments	e
Primary Balance before Grants	**a - c - d**
Overall balance	a + b - c - d - e

7. The central government primary balance will be measured from the financing side as the sum of the net domestic financing plus net external financing plus domestic and external interest payments on a due basis minus grants.

8. **Net domestic financing** of the central government is the sum of:

(i) net domestic bank financing as measured by the change in the domestic banking system credit to the central government net of deposits, as reported by the consolidated balance sheet of the monetary authorities[21] and commercial banks, including special tranches from the ECCB;

(ii) net nonbank financing as measured by the net changes in holdings of government securities by nonbanks, and net borrowing from nonbank institutions;

[21] Consolidating the ECCB's balance sheet (excluding the government's IMF operating account) and the government's transactions with the IMF.

(iii) the change in the stock of domestic arrears of the central government defined as net changes in unpaid checks issued, unprocessed claims, pending invoices, plus accrued interest payments, and other forms of expenditures recorded above the line but not paid;

(iv) gross receipts from divestment;

(v) any exceptional financing.[22]

9. **Net external financing** of the central government is defined as the sum of:

(i) disbursements of project and nonproject loans, including securitization;

(ii) proceeds from bonds issued abroad;

(iii) exceptional financing (including rescheduled principal and interest), net changes in cash deposits held outside the domestic banking system,

(iv) net changes in short-term external debt;

(v) any change in arrears on external interest payments and other forms of external expenditures recorded above the line but not paid;

and less:

(vi) payments of principal on current maturities for bonds and loans on a due basis but excluding the use of IMF resources, and including any prepayment of external debt.

10. The floor on the primary balance of the central government before grants will be adjusted as follows:

(i) downward[23] to the extent that grants exceed programmed amounts as specified in Table 2.

(ii) upwards to the extent grants fall short of the programmed amounts as specified in Table 2 by more than EC$25 million through end-June or after.

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[22] Treasury bills will be recorded at face value, except for those held by the banking system which will be recorded on a purchase price basis.

[23] Downward adjustment means a higher deficit; upward implies a lower deficit.

(iii) downward to the extent that concessional financing from multilateral development banks exceeds programmed amounts (Table 2).

Table 2. Programmed Disbursements of Grants and Concessional Loans in 2006 (EC$ millions)

Quarter	I	II	II	IV
Grants	20	20	36.4	36.4
Concessional Loans	12.6	12.6	22.9	22.9

III. Indicative Target on the Net Credit of the Banking System to the Public Sector

11. **Net credit of the banking system** is measured as the change in credit of the domestic banking system to the public sector net of deposits, as reported by the consolidated balance sheet of the monetary authorities and commercial banks, including special tranches from the ECCB.

12. The ceiling on net credit of the banking system will be adjusted by the amount of required counterpart financing as follows:

(i) Upward[24] to the extent that grants fall short of programmed amounts up to a limit of EC$25 million through end-June or after;

(ii) Upward to the extent that concessional financing falls short of programmed amounts.

IV. Performance Criterion on the Central Government Arrears Accumulation to Domestic Private Parties and Public Enterprises

13. **Net changes in central government arrears to domestic private parties and public enterprises** is defined as the sum of all pending payments by the government for goods and services purchased from these parties, as well as pending interest and amortization payments on domestic debt, that have been outstanding for 60 days or longer. It also includes changes in arrears to the oil companies, which have resulted from the gas price subsidization arrangement, but have not been systematically recorded. The definition of domestic payment arrears excludes (i) debt claims that were irrevocably tendered in the debt exchange closed on November 15, 2005 ("the debt exchange"), and (ii) debt claims that were eligible to participate in the debt exchange but have not been tendered.

[24] Upward adjustment means higher net domestic credit to the government.

14. A ceiling is set on central government arrears to domestic private parties, equal to the stock of such arrears as per December 31, 2005 (Table 3). The ceiling will be monitored on a continuous basis.

Table 3. Stock of Domestic Arrears as per December 31, 2005
(in EC$ millions)

Unpaid checks issued	0
Unprocessed claims and Pending Invoices	2.99
Interest and amortization arrears on domestic debt	...
Arrears resulting from gas price arrangement 1/	18.15
Total stock of arrears	21.14

1/ Estimate

V. A. Performance Criterion on Nonconcessional Debt with an original maturity of At Least One Year contracted or Guaranteed by the Central Government

15. The ceiling on nonconcessional debt with an original maturity of at least one year will be applied to contracting or guaranteeing of debt by the central government .The contracting and guaranteeing of debt will be monitored and reported to the Fund staff by the Debt Unit (Economic Affairs) and the Accountant General's office on a monthly basis.

16. This performance criterion applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85) August 24, 2000) but also to commitments contracted or guaranteed for which value has not been received:

"(a) For the purpose of this guideline, the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

(i) loans, i.e., advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

(ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and

(iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lesser retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property.

(b) Under the definition of debt set out in point [16(a)] above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt."

17. Excluded from the ceiling are credits extended by the IMF and credits on concessional terms provided by multilateral development banks.

18. Concessional terms are defined as terms implying a grant element (in net present value relative to face value) of more than 35 percent, based on the currency- and maturity-specific Commercial Interest Reference Rates (CIRR), published monthly by the OECD.[25] The limit excludes the disbursements of short-term import-related debts, the use of Fund resources, and refinancing operations.

V. B. Performance Criterion on the Net Changes in the Outstanding Stock of Short-Term External Debt with Original Maturity of Less than One Year Contracted or Guaranteed by the Central Government

19. The **stock of short-term external debt outstanding** is defined as debt with original maturity of less than one year contracted or guaranteed by the central government. The term debt is defined as set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85), August 24, 2000) (see paragraph [16] above), but excludes normal import-related credits.

20. The ceiling on short-term external debt will be applied on a continuous basis to the stock of short-term external debt owed or guaranteed by the central government.

[25] For loans with a maturity of at least 15 years, the 10-year average commercial interest reference rates and for loans with shorter maturities, the six-month average CIRRs, as of August 2006 published by the OECD will be used as the discount rates. To both the 10-year and 6-month averages, the following margins for differing repayment periods will be added: 0.75 percent for repayment periods of less than 15 years; 1 percent for 15–19 years; 1.15 percent for 20–29 years; and 1.25 percent for 30 years or more.

VI. PERFORMANCE CRITERION ON NONACCUMULATION OF CENTRAL GOVERNMENT AND CENTRAL GOVERNMENT GUARANTEED EXTERNAL PAYMENT ARREARS

21. **Central government and central government guaranteed external payment arrears** are defined as overdue payments (principal or interest) on debt contracted or guaranteed by the central government. The definition of external payment arrears under the program excludes: (i) debt claims that were eligible to participate in the debt exchange but have not been tendered, and (ii) debt claims of official bilateral creditors which are under rescheduling or refinancing negotiation.

22. No external payment arrears of the central government and central government guaranteed debt, will be allowed in the program. This ceiling will be monitored on a continuous basis.

VII. PERIODIC REPORTING

23. Regular reporting on a **monthly basis** will include the following:

24. Data for monitoring the program's performance criteria and monthly indicative targets, including

Fiscal sector

(i) Central government budgetary accounts.

(ii) Central government domestic debt data.

(iii) Current grant inflows.

(iv) Stock of domestic arrears, including unpaid checks issued, stock of unprocessed claims due and invoices pending; interest and amortization on domestic debt.

(v) Capital expenditure, including revised projections for the remainder of the fiscal year. Complementing to this monthly report, a detailed overview of expenditures on a project by project basis and the composition of financing will be provided on a quarterly basis.

Financial sector

(vi) Monetary survey for Grenada as prepared by the Eastern Caribbean Central Bank.

External and real sectors

(vii) Detailed (creditor by creditor) external debt report from the Debt Unit in the Ministry of Finance, showing fiscal year-to-date disbursements, amortization, interest payments, and outstanding stocks, for the central government and public enterprises.

(viii) Total disbursements/grant receipts, monthly, disaggregated into: (a) budgetary support (by type—either loans or external "bonds" and/or other securities); (b) project loans; (c) budgetary grants; and (d) project grants.

(ix) Copies of loan agreements for any new loans contracted, including financing involving the issue of government paper, and of any renegotiated agreements on existing loans.

(x) Stock of external arrears (creditor-by-creditor)

(xi) Consumer price index.

All such information will be provided to Fund staff, to the extent possible, within three weeks of the end of each month.

25. Reporting on an **annual basis** will include the following:

Fiscal sector

26. Financial statements of the public enterprises (as listed in paragraph 4)

External and real sectors

(xii) GDP and its components.
(xiii) Balance of payments accounts.

27. **Other reporting** will include:

(xiv) Reports of legislative changes pertaining to economic matters.
(xv) Notification of any establishment of new public enterprises.

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International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$15.2 Million PRGF Arrangement for Grenada

The Executive Board of the International Monetary Fund (IMF) has approved a three-year arrangement for Grenada under the Poverty Reduction and Growth Facility (PRGF) in a total amount equivalent to SDR 10.53 million (about US$15.2 million) to support the government's comprehensive medium-term economic reform program. An initial disbursement of SDR 1.56 million (about US$2.2 million) under the arrangement will become available immediately.

The PRGF is the IMF's concessional facility for low-income countries. It is intended that PRGF-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners and articulated in a Poverty Reduction Strategy Paper (PRSP). This is intended to ensure that PRGF-supported programs are consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. PRGF loans carry an annual interest rate of 0.5 percent and are repayable over 10 years with a 5 ½-year grace period on principal payments.

Following the Executive Board discussion on Grenada, on April 17, 2006, Mr. Agustín Carstens, Deputy Managing Director and Acting Chair, said:

"A modest economic recovery is underway in Grenada from the devastating effects of Hurricanes Ivan in 2004 and Emily in 2005. Economic growth rebounded in 2005, following a decline in 2004, with brisk activity in the construction sector offsetting the slowdown in agriculture and tourism. Near-term growth prospects are encouraging, reflecting ongoing construction activity and the expected recovery in tourism. While a substantial increase in domestic fuel prices led to an increase in inflation in 2005, second-round price increases have been limited and price rises are expected to moderate in the coming months.

"With reconstruction activity broadly on-track, the Grenadian authorities have turned their attention to the longer term challenges that the country faces. These include alleviating poverty, promoting sustained high economic growth, restoring fiscal and debt sustainability, as well as reducing vulnerabilities to extreme weather events and financial sector developments. The Fund welcomes the government's commitment to address these challenges through a comprehensive medium-term reform program.

"The 2006 budget has been used to launch this reform program. The program aims to sharply reduce public debt from its present high level to some 60 percent of GDP by 2015. To this end, a primary surplus (excluding grants) of 2.5 percent of GDP will be targeted, beginning in 2008. The shift in the fiscal stance that this requires will be phased in over the next three years so as to accommodate large reconstruction-related spending needs in 2006 and 2007. The fiscal adjustment will be evenly distributed between revenues and expenditure measures. Importantly, these fiscal reforms make room for increased social expenditure, particularly with a view to addressing the social needs arising from the dislocation caused by the hurricanes and higher energy prices.

"The authorities' reform program also aims to address the other economic challenges the country faces. To raise growth potential, improvements in the investment climate are planned, including a transparent and investor-friendly framework and the removal of regulatory barriers. Relatedly, the process through which investors acquire land will be simplified greatly, by ensuring that land controlled by the government is made available through open and well-publicized auctions. To reduce vulnerabilities in the financial sector, the program includes measures to strengthen the regulatory framework.

"The authorities' comprehensive program is promising. With steadfast implementation, growth and poverty reduction will be enhanced, the resilience of Grenada's economy to shocks will improve, and debt and fiscal sustainability will be restored," Mr. Carstens said.

ANNEX

Recent economic developments

Grenada is recovering from a series of exogenous shocks in recent years. In September 2004, Hurricane Ivan caused unprecedented damage of 200 percent of GDP, and recovery efforts were set back in July 2005, when Hurricane Emily struck, causing additional damage estimated at 12 percent of GDP. In conjunction with earlier shocks—the September 11 attacks in the United States set off a sharp drop in tourism and tropical storm Lili in 2002 depressed agricultural exports—these events have hampered effective policy implementation and caused output to fluctuate sharply in recent years. High international oil prices contributed to further hardship.

Economic growth has rebounded to an estimated 1.5 percent in 2005 after a drop of 3 percent in 2004, with brisk activity in the construction sector offsetting the slowdown in agriculture and tourism. Near-term growth prospects are good with GDP potentially expanding by more than 5 percent in 2006 and 2007, reflecting ongoing construction activity and the expected recovery in tourism. Following a 45-percent increase in domestic fuel prices, inflation reached 6 percent at the end of 2005. Second-round price increases have, however, been limited and inflation is expected to decline in the coming months

The shocks have exacerbated the already tenuous fiscal situation marked by large fiscal imbalances and growing public debt, and amplified the need for reforms to reduce vulnerabilities. The large-scale physical reconstruction effort currently underway needs to be accompanied by fiscal consolidation to reduce public indebtedness.

Program summary

The government has used the 2006 budget to launch a comprehensive medium-term economic reform program with the strategic objectives to promote sustained high economic growth, restore fiscal and debt sustainability, reduce vulnerabilities, and alleviate poverty.

Fiscal reforms are at the heart of the authorities' program with the aim to sharply reduce public debt from its present inordinately high level of 128 percent of GDP at end-2005 to a more prudent level. To this end, the program targets a central government primary surplus (excluding grants) of 2.5 percent of GDP by 2008, which would enable the debt-to-GDP ratio to decline gradually to 60 percent. This shift in fiscal stance will be phased in over the next three years to accommodate the large reconstruction-related spending needs in 2006 and 2007, and will be underpinned by structural fiscal measures already identified in the program.

In regard to structural policies, the first year of the program targets measures to improve the investment climate, and the second and third years are expected to focus on improving the flexibility of the labor and financial markets.

Furthermore, the authorities are committed to reducing vulnerabilities from extreme weather events and weaknesses in the regulatory framework of the financial sector. The recent hurricanes suggest that steps are required to better enforce building standards as well as increase insurance coverage. In the financial sector, while the banking system appears to have coped with recent shocks, and there is a need to enhance the regulatory framework for non-bank financial institutions.

The fiscal measures under the program make room for increased social spending in support of the authorities' social development agenda. Although Grenada is considered to be broadly on track to meet the Millennium Development Goals, challenges remain. In the near term, a range of programs will address the social needs arising from the dislocation caused by the hurricanes. For the long term, reducing poverty is contingent on reducing unemployment, as highlighted in the government's poverty eraduication strategy, recently submitted to the Executive Boards of the IMF and World Bank as the country's interim Poverty Reduction Strategy Paper (PRSP).

Table 1. Grenada: Selected Economic and Financial Indicators, 2003–08

Rank in UNDP Human Development Index out of 177 countries (2004)	66	Infant mortality rate per '000 births (2003)	18
		Adult illiteracy rate in percent (2001)	4
Life expectancy at birth in years (2003)	65	Poverty headcount index (2000)	32
GDP per capita in US$ (2004)	4,620		

			Est.	Projections		
	2003	2004	2005	2006	2007	2008
(Annual percentage change; unless otherwise specified)						
National income and prices						
Real GDP	5.8	-3.0	1.5	6.5	5.0	4.0
GDP deflator	1.3	2.7	3.5	4.6	2.0	2.0
Consumer prices						
End-of-year	1.6	2.5	6.0	2.0	2.0	2.0
Period average	2.2	2.3	3.5	4.6	2.0	2.0
External sector						
Exports, f.o.b.	7.1	-24.8	-14.6	0.6	-8.2	16.7
Imports, c.i.f.	25.9	3.3	22.6	-3.4	4.2	5.7
Export volume 1/	-2.0	-25.6	-23.5	-0.6	-10.0	17.1
Import volume 1/	11.6	-8.6	11.7	-5.0	4.3	5.7
Current account balance (including grants; in percent of GDP)	-33.2	-13.5	-37.1	-32.8	-28.0	-26.7
Terms of trade (deterioration -)	-3.2	-10.6	1.7	-0.5	2.0	-0.4
Real effective exchange rate (end of period, depreciation -)	-8.5	-4.6	5.2	...	...	...
Banking system						
Net foreign assets 2/	5.8	17.9	-19.4	-2.2	-2.0	-2.5
Net domestic assets 2/	2.2	-0.2	19.0	10.1	7.7	7.3
Of which						
Credit to public sector (net) 2/	2.3	-6.7	-0.8	0.0	0.0	0.0
Credit to private sector 2/	3.1	5.0	6.2	8.5	7.7	7.7
Money and quasi-money (M2)	8.0	17.7	-0.4	7.8	5.7	4.8
Weighted deposit rate (in percent per year) 3/	3.4	2.8	2.8	...	...	...
Weighted lending rate (in percent per year) 3/	12.4	10.0	10.2	...	...	...
(In percent of GDP)						
Central government finances						
Total revenue and grants	34.5	33.1	39.1	36.1	31.5	31.9
Of which						
Grants	6.9	7.5	11.0	8.0	2.7	2.5
Total expenditure	39.3	35.9	38.9	38.1	31.6	28.8
Current expenditure	24.3	27.9	23.5	22.7	21.6	20.6
Of which						
Salaries and allowances	10.9	12.7	11.8	11.7	11.1	10.6
Capital expenditure	15.0	8.0	15.4	15.4	10.0	8.2
Primary balance (after grants)	0.4	3.7	2.4	0.3	2.1	5.0
Current balance	3.2	-2.4	4.6	5.3	7.2	8.6
Overall balance (after grants)	-4.8	-2.8	0.2	-2.0	-0.1	3.0
Public sector total debt (end-period) 4/	110.0	129.5	128.0	126.7	117.8	107.3
(In millions of U.S. dollars; unless otherwise specified)						
Gross international reserves of the ECCB, end-of-period	539.9	632.4	600.7	...	...	...
In percent of broad money in all ECCU countries	19.8	20.4	20.1	...	...	...
Nominal GDP	443.7	436.8	474.0	519.3	558.9	596.5

Sources: Ministry of Finance; Eastern Caribbean Central Bank; United Nations, Human Development Report 2004; World Bank, WDI 2005; and IMF staff estimates and projections.

1/ Does not include goods procured in ports by carriers.
2/ As a percent of broad money at the beginning of the year.
3/ Break in the data series in 2003.
4/ Includes central government debt, government-guaranteed debt, and nonguaranteed public enterprise debt.