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FUND FOR SPECIAL OPERATIONS

REVIEW OF THE IMPLEMENTATION OF THE DEBT SUSTAINABILITY FRAMEWORK AND ENHANCED PERFORMANCE-BASED ALLOCATION

2013-2014

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ABBREVIATIONS

CDB	Caribbean Development Bank
CIPE	Country Institutional and Policy Evaluation
CPIA	Country Policy and Institutions Assessment
CIRR	Commercial Interest Reference Rates
DSA	Debt Sustainability Analysis
DSF	Debt Sustainability Framework
EPBA	Enhanced Performance-Based Allocation
FSO	Fund for Special Operations
GCI-9	Ninth General Increase in Resources of the Inter-American Development Bank
GDP	Gross Domestic Product
GNI	Gross National Income
IDA	International Development Association
IMF	International Monetary Fund
MDB	Multilateral Development Bank
MDRI	Multilateral Debt Relief Initiative
MFI	Multilateral financial institution
NSG	Non-Sovereign Guaranteed Operations
OC	Ordinary Capital
OECD	Organization for Economic Cooperation and Development
OECS	Organization of Eastern Caribbean States
OVE	Office of Evaluation and Oversight
PBA	Performance-Based Allocation
PBL	Policy-Based Loan
PMR	Progress Monitoring Report
PPMR	Project Performance Monitoring Review
PTI	Poverty Targeted Investment
RES	Research Department
SCF	Single Currency Facility
SEQ	Social Equity
SG	Sovereign Guaranteed
SI	Synthetic Indicator
SPD	Office of Strategic Planning and Development Effectiveness
ULB	Undisbursed Loan Balances
WB	World Bank

I. INTRODUCTION

A. Objective

1.1 On March 15, 2007, the Board of Governors approved Resolution AG-03/07, which states that every two years there shall be a review of implementation of the Debt Sustainability Framework and Enhanced Performance-Based Allocation (DSF/EPBA). Management has presented three reviews for consideration of the Board of Executive Directors (Board) and subsequent distribution to the Board of Governors for information at the IDB Annual Meeting: (i) in 2009 (Documents GN-2442-17 and AB-2646); (ii) in 2011 (Documents GN-2442-34 and AB-2646-1); and (iii) in 2013 (Documents GN-2442-44 and AB-2646-2).

1.2 The purpose of this document is to submit for the consideration of the Board Management's fourth review of the implementation of the DSF/EPBA framework. Management also requests that the Board authorizes transmission of this report for information to the Board of Governors.

B. The Debt Sustainability Framework and Enhanced Performance-Based Allocation

1.3 On February 21, 2007, the Board approved document GN-2442 "Implementation of multilateral debt relief and concessional finance reform at the IDB. Proposal for the implementation of a Debt Sustainability (DSF) and Enhanced Performance-Based Allocation (PBA) framework", which presented an enhanced performance-based allocation (EPBA) system for the distribution of Fund for Special Operations (FSO) resources, under a structure that blends FSO and OC resources (blended structure), based on the DSF/EPBA criteria. Total allocation of concessional resources under the DSF/EPBA is determined by a combination of country needs and performance, which determines the allocation of FSO resources (first step); and the risk of debt distress, which defines the appropriate blend of Ordinary Capital (OC) resources (second step). The DSF/EPBA aims to ensure a link between concessional resource allocation and absorption capacity, while preserving debt sustainability.

1.4 The EPBA for FSO resources has two major elements: (i) needs and economic strength, comprised of population and GNI per capita; and (ii) performance, estimated as the weighted average of portfolio performance (30%) and the quality of the institutional and policy framework (70%), as measured by the Country Institutional and Policy Evaluation (CIPE). Each of these variables in the allocation formula has a defined exponent for the calculation of the distribution coefficient as determined in document GN-2442.

1.5 The DSF defines the risk of debt distress (low, moderate or high), which in turn determines the appropriate level of concessionality for each country through the blended structure.

II. UPDATE OF DEBT SUSTAINABILITY AND SELECTED INDICATORS OF D2 COUNTRIES

A. Debt Sustainability

2.1 For the 2013-2014 allocation cycle, the blend of FSO and OC resources remained unchanged compared to the first DSF/EPBA allocation in 2007 for Guyana, Honduras and Nicaragua. The FSO/OC blend applicable to Bolivia had been modified from

30%/70% to 25%/75% for 2011 and, subsequently, to 20%/80% for 2012 (Document GN-2442-39). The 20%/80% blend was applied also to the allocation to Bolivia for 2013-2014.

2.2 Although the lending blends for the four countries in 2013-2014 remained the same as the blends prevailing in 2012, the estimated *ex-post* or realized concessionality of blended loans decreased in 2013-2014, continuing a trend since 2010 (Table 1). For example, a lending blend of 50% FSO/50% OC is estimated to have had a concessionality of approximately 58% in 2012, 56% in 2013 and 49% in 2014.[1] The decline in concessionality was due to: (i) a reduction in the discount rate used to assess present value, which has the effect of increasing the present value of future streams of debt service; and (ii) an increase in the weighted average lending rate applicable to OC resources because of a change in the composition of the outstanding OC loan balances. The share of OC Fixed SCF loan balances (which carried an average interest rate of 4.3% as of December 2014 versus 1.12% for the OC Libor Single Currency Facility [SCF]) rose from zero in 2010 to approximately three-quarters of the FSO-IV countries' total OC outstanding loan balances by 2014.

Table 1. Risk of Debt Distress and Level of Concessionality Ex-Post

				2010	2011	2012	2013	2014
Country	Risk of Debt Distress	FSO Interest rate		0.25%	0.25%	0.25%	0.25%	0.25%
		Average Effective OC rate		1.27%	2.78%	2.82%	2.91%	3.54%
		Ex-ante discount rate		6.80%	6.50%	6.50%	5.90%	5.90%
		Ex-post discount rate		6.37%	6.00%	5.70%	5.44%	5.00%
		FSO	OC	Concessionality				
Bolivia	Low	30%	70%	61.6%				
Bolivia	Low	25%	75%		46.6%			
Bolivia	Low	20%	80%			43.9%	39.6%	31.0%
Guyana	Moderate	50%	50%	69.1%	60.4%	58.4%	58.2%	48.0%
Honduras	Low	30%	70%	61.6%	50.9%	42.4%	39.2%	33.7%
Nicaragua	Moderate	50%	50%	69.1%	56.5%	57.2%	54.5%	49.0%

Source: VPC based on OECD grant element calculator, OECD differentiated discount rates.

[1] Countries with the same lending blend, such as Guyana and Nicaragua for the period 2013-2014, may have slightly different realized concessionality due to differences in the dates on which they contract OC liabilities and the differences in the proportions of OC Fixed SCF/ OC Libor SCF debt in their outstanding loan balances. For the FSO portion of blended loans, there is no variation over time in the interest rates applicable (0.25%).

Discount rates used to estimate concessionality

The grant element or concessionality of a loan is defined as the difference between the loan's nominal value (face value) and the sum of the discounted future debt-service payments (present value), as a percentage of the loan's face value. Whenever the interest rate on a loan is lower than the discount rate, the loan is concessional. Consequently, the discount rate used to estimate the present value of a loan has an important impact on the loan's concessionality.

Until October 2013, the International Monetary Fund (IMF)/World Bank (WB) DSF used different discount rates to calculate the concessionality of loans and to calculate present value in the debt sustainability analyses for low income countries. Despite differences in methodology to calculate the discount rates, all discount rates were linked to the Organization for Economic Cooperation and Development's (OECD) Commercial Interest Reference Rates (CIRRs) [i.e. market-based interest rates]. For the purposes of estimating concessionality for loans with a maturity greater than 15 years, the IMF/WB DSF used a 10-year average CIRR (to smooth out volatility) and updated the discount rate annually.

In October 2013 the IMF and WB Executive Boards approved a proposal to unify the discount rates used for all operational purposes. The unified discount rate was initially set at 5%, with a review of the rate scheduled for 2015.

The biannual FSO allocation documents always base *ex-ante* concessionality estimations on the discount rate prevailing at the time of allocation. However, since the discount rate in the IMF's Concessionality Calculator used to be updated annually, the actual discount rates in the two years of an allocation period could deviate from the rate prevailing at the time of the allocation.

2.3 The realized or *ex-post* concessionality was greater than the *ex-ante* concessionality projected in FSO biannual allocation proposals prior to 2012. However, during the 2013-2014 period the realized concessionality fell 1.8 percentage points below the projected level (Table 1 and Annex I), due particularly to the adoption of a discount rate below that assumed in 2012. Barring an increase in OC lending rates, *ex-post* concessionality is unlikely to decline further during the 2015-2016 period because the trends weighing on concessionality appear to have come to an end. The IMF is expected to review the unified discount rate of 5% in 2015 but the 10-year average of the U.S. dollar commercial interest reference rate has not changed significantly since 2013. Furthermore, the share of OC Fixed Rate SCF in total FSO-IV OC debt appears to have converged to a natural ceiling already.

2.4 Under the DSF, debt sustainability indicators have largely continued to improve or been maintained following multilateral debt relief at the beginning of 2007.[2] The burden of debt service with respect to both exports and government revenues declined from 2007-2013 for all FSO-IV countries except Guyana. The FSO-IV simple average debt service-to-export ratio declined from 4.0% in 2007 to 2.3% in 2013, while the average debt

[2] For reasons of data availability as well as avoiding noise caused by changes in discount rates, ratios in this paragraph and in Annex II refer to nominal rather than present value terms.

service-to-government revenue ratio declined from 6.2% in 2007 to 4.1% in 2013.[3] Trends regarding the stock of public external debt with respect to GDP, exports and government revenues between 2007 and 2013 have been more mixed (Annex II). Debt stock indicators improved significantly in the case of Nicaragua and were broadly unchanged in the cases of Bolivia and Guyana (Table 2).[4] However, in the case of Honduras, the stock of public external debt rose: from 16.7% of GDP in 2007 to 27.3% in 2013; from 31% of exports in 2007 to 57% in 2013; and from 68% of government revenues in 2007 to 120% in 2013. The FSO-IV simple average debt-to-GDP ratio rose marginally from 30.0% in 2007 to 31.6% in 2013; the debt-to-export ratio declined from 73% in 2007 to 66% in 2013; and the debt-to-revenue ratio increased from 117% in 2007 to 125% in 2013.

Table 2. Change in Debt Sustainability Indicators Between 2007 and 2013 (nominal terms)

	Debt stock indicators	**Debt service indicators**
FSO IV	No significant change	Strengthened
Bolivia	No significant change	Strengthened
Guyana	No significant change	Weakened
Honduras	Weakened	Strengthened
Nicaragua	Strengthened	Strengthened

Source: VPC based on Annex II.
Note: "No significant change" is defined as a majority of indicators in 2013 are within 7% of their 2007 value.

2.5 **Collaboration with the World Bank and the IMF**. The Bank has continued its collaboration with the WB and the IMF in the preparation of debt sustainability analyses. During 2013 and 2014, the Bank continued to participate in the annual MDB/MFI Technical Meeting on Performance Based Allocation (PBA) Systems, in which various aspects of concessional financing are discussed among multilateral development banks (MDBs) and other multilateral financial institutions.

B. Enhanced Performance-Based Allocation Indicators

B.1. Country Institutional and Policy Evaluation

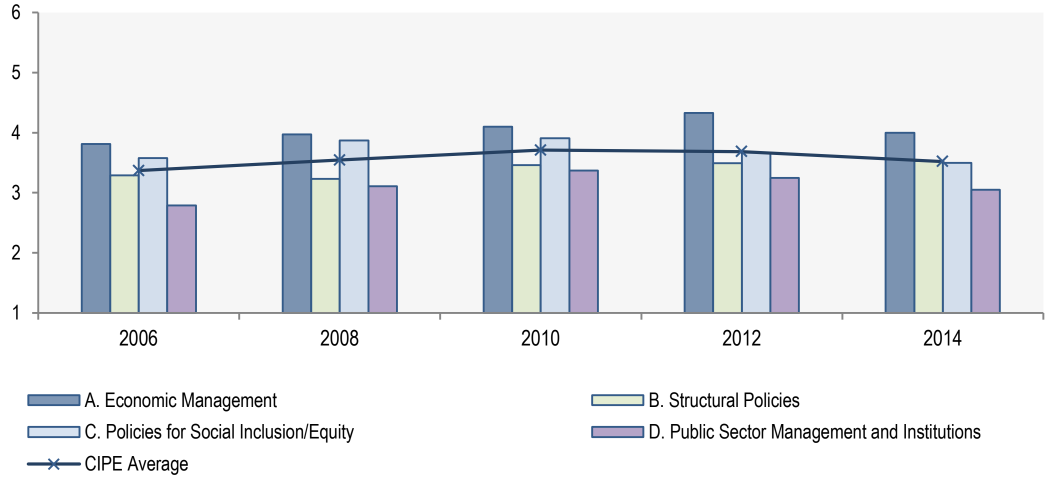
2.6 The CIPE assesses the quality of a country's present policy and institutional framework. A CIPE update was approved by the Board in 2012 for the 2013-2014 allocation, consistent with the revisions to International Development Association's (IDA) "Country Policy and Institutions Assessment" (CPIA) (Document GN-2442-42). No changes to the CIPE were made in 2014 for the 2015-2016 allocation.

[3] While there are reasonable grounds to expect this trend to continue, possible increases in international interest rates in might slow future progress.

[4] A rebasing of the national accounts in 2010 for Guyana and 2012 for Nicaragua led to upward revisions in the estimated GDP.

2.7 Although revisions/updates to the CIPE in 2010 and 2012 complicate comparisons over time, at the aggregate level, CIPE scores have maintained a broadly similar level from 2006 through 2014 (Figure 1). However, the unweighted average total CIPE score in 2014 declined slightly relative to 2012, in part because of a decline in the CIPE scores for the Economic Management policy cluster.[5] Nevertheless, the Economic Management policy cluster remains the cluster with the highest scores. Annex III presents detailed information on 2014 CIPE and Annex IV presents the evolution of total CIPE scores.

Figure 1. Average CIPE Ratings for FSO-IV Countries



Sources: VPC based on GN-2442-46, GN-2442-41, GN-2442-32, GN-2442-16, GN-2442.

2.8 During 2013-2014 period, the impartial review of CIPE scores and justifications by the Research Department (RES) and Office of Strategic Planning and Development Effectiveness (SPD) continued to provide a useful role in terms of quality control and ensuring equality of treatment across countries. The introduction of widely-used quantitative indicators to increase the objectiveness of the CIPE assessment, as recommended by OVE (document RE-376) for the 2011-2012 cycle, appears to have provided an additional useful input to and cross-check on the potential subjectivity of the qualitative assessment. For the 2014 CIPE the qualitative scores are positively correlated with their respective quantitative indicator, at a 95% confidence level[6], suggesting that qualitative assessments do not suffer from significant biases that would affect relative rankings.

B.2. Portfolio Performance

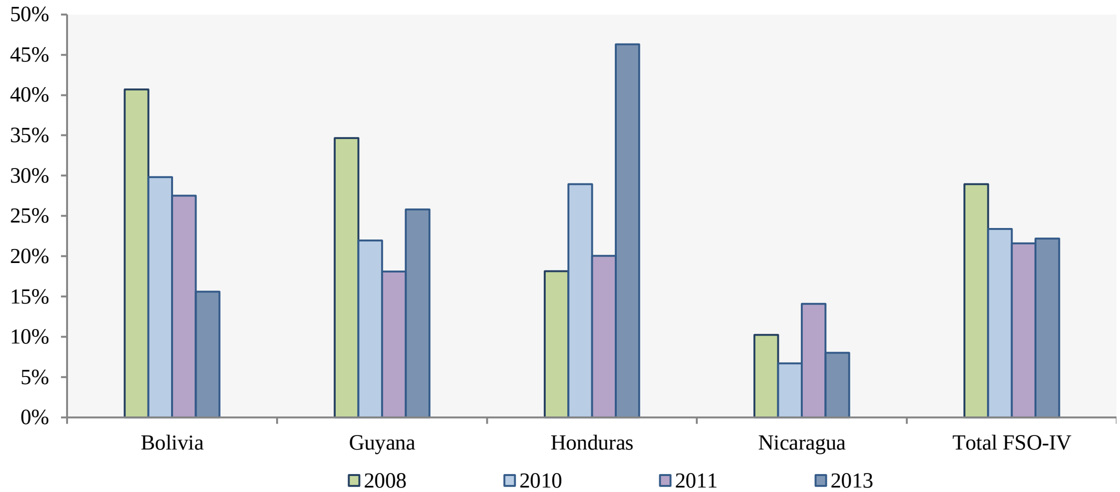
2.9 Portfolio performance is assessed as the percentage of undisbursed loan balances (ULB) represented by projects classified as “problem” and “on alert”. For the 2015-2016 allocation, the portfolio performance indicator was modified to incorporate the methodological changes introduced to the classification of projects in the Bank’s updated

[5] Notwithstanding that the CIPE tries to measure the quality of policies, inevitably to some degree it captures outcomes, particularly through the quantitative indicator components. Economic outcomes in 2014 were generally less favorable than in 2012.

[6] Pearson correlation coefficient, two-tailed test.

Progress Monitoring Report (PMR).[7] Additionally, since time-elapsed indicators in the new PMR are measured against an intra-country historical benchmark, for the purposes of the FSO allocation, projects are also evaluated by comparing them against Bank-wide benchmarks, in order to measure for relative performance among countries (Document GN-2442-46).[8]

Figure 2. "Problem" and "on Alert" Project Classification for the EPBA (as % of ULB)



Sources: VPC based on GN-2442-46, GN-2442-41, GN-2442-32, GN-2442-16, GN-2442.

2.10 Portfolio performance has improved since the adoption of the DSF/EPBA, suggesting that the performance incentives imbedded in the framework produce favorable outcomes. At the aggregate level for the FSO-IV countries, unsatisfactory projects (those "on alert" or with "problem" status) have declined from 28.9% of total ULB in 2008 to 22.2% in 2014, albeit with a slight deterioration (0.6 percentage points) from 2012 to 2014.[9] While Nicaragua consistently had the lowest balance of "on alert" and "problem" projects among the FSO IV-countries from 2008 to 2013, Bolivia experienced a notable reduction of these balances over the period. In the case of Guyana, portfolio performance deteriorated from 18.1% in 2012 to 25.8% in 2014, after experiencing systematic improvements in past exercises (Annex V). For Honduras, portfolio performance was

[7] As part of the recent GCI-9 evaluation (RE-425-4), OVE reviewed the PMR methodology and found that, among other things, having the PI as the only indicator to determine project classification was limited and could create false positive cases. In view of this and other lessons learned, a review to the PMR and the respective proposal for adjustments was approved in December 2013 (OP-1072-1). The new PMR captures different dimensions of projects' performance. Different indicators are measured at each stage of the project's life cycle, that is: (i) after Board approval and before reaching eligibility; (ii) between eligibility and up to 95% disbursement; and (iii) between 95% disbursement and project closure. A synthetic indicator (SI), reflecting a weighted average of the indicators used for rating the project's execution performance, serves as the basis of the project classification after the projects become eligible for disbursements.

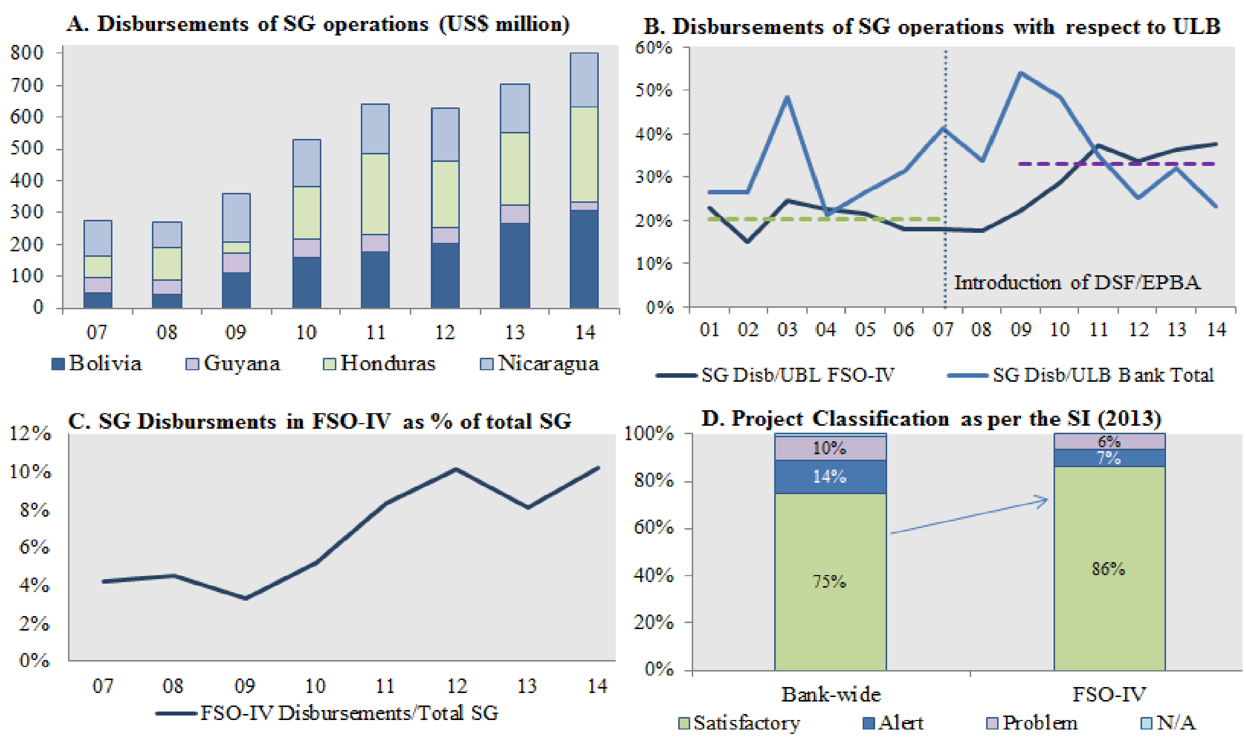
[8] These indicators measure the time elapsed from: (i) approval of the loan operation until signature of the corresponding loan contract, for those countries in which ratification of loan contracts is not required; (ii) approval of the loan operation until ratification of the corresponding loan contract, for those countries in which ratification of loan contracts is required; (iii) legal effectiveness to eligibility; and (iv) extensions of the final disbursement date.

[9] A comparison with previous years is not entirely adequate given the revisions/updates to the PMR methodology.

affected by one loan whose ULB comprised almost 60% of all the unsatisfactory loan balances.[10]

2.11 Hand-in-hand with execution improvements as measured by the portfolio performance indicator of the EBPA, the pace of disbursements has accelerated in FSO-IV countries since the adoption of the DSF/EPBA. Sovereign Guaranteed (SG) disbursements in FSO-IV countries almost tripled, from US$273 million per annum on average during 2007-2008, to US$754 million on average for 2013-2014. Although part of this increase responds to larger allocations, FSO-IV countries have been steadily increasing SG disbursements with respect to their ULB since 2007, catching up with the Bank's average in 2011 and surpassing it in 2012 (Figure 3.B).[11] As a result, the share of the Bank's annual SG disbursements by FSO-IV countries has also increased, reaching 10.2% in 2014 (Figure 3.C). Furthermore, FSO IV-countries have a larger share of projects with a satisfactory PMR classification than the Bank average (Figure 3.D).

Figure 3. Selected Indicators of Execution in FSO-IV Countries after Approval of the DSF/EPBA



Sources: VPC based on IDB FIN LMS Reports; PMR Report for 2013 (OP-1072-1).

[10] HO-L1037, with US$135 million available by the cut-off date Dec 31, 2013, was classified as a "problem" project by the PMR (according to the first phase indicator "time elapsed between effectiveness and eligibility") and also flagged when compared against the Bank-wide benchmark. The project achieved eligibility in May 2014 and is currently in the disbursing phase.

[11] For the FSO-IV countries, the mean of disbursements with respect to ULB in 2008-2014 is significantly different from the mean for 2001-2007 at a 95% confidence level. The Bank-wide mean was not significantly different between the two periods.

III. FSO ALLOCATIONS IN 2013-2014

A. FSO Allocations under the DSF/EPBA in 2013-2014

3.1 Annual allocations for 2013 and 2014 were calculated according to the exponential formula of the EPBA methodology set forth in document GN-2442. A total of US$275.6 million in FSO resources per year was allocated among the FSO-IV countries, for a total amount of allocated blended resources of US$941.1 million. The total amount of FSO resources allocated among FSO-IV countries was 19% higher than during 2011-2012.

3.2 **C and D1 countries**. FSO eligibility for C and D1 countries is based on a per-capita income threshold that is periodically revised to reflect changes in economic conditions. For the 2013-2014 allocation, Guatemala and Paraguay were eligible, with a total annual allocation of US$30 million of FSO resources.[12] The blend applied to C and D1 countries was set at 20% FSO: 80% OC, as per Document CA-474-2.

Table 3. Annual Allocations to eligible countries, 2013-2014 (US$ million)

	Risk of Debt Distress (DSF)	Blend		DSF-EPBA Yearly Allocation		
		FSO	OC	FSO	OC	Total
Bolivia	Low	20%	80%	71.3	285.2	356.5
Guyana	Moderate	50%	50%	14.1	14.1	28.1
Honduras	Low	30%	70%	64.5	150.5	215.0
Nicaragua	Moderate	50%	50%	95.8	95.8	191.5
Total D2				245.6	545.5	791.1
Guatemala	n/a	20%	80%	15.8	63.4	79.2
Paraguay	n/a	20%	80%	14.2	56.6	70.8
Total D1-eligible				30.0	120.0	150.0
Total Financing				275.6	665.5	941.1

Sources: VPC based on GN-2442-41.

3.3 **Special support for eligible non-IDB member countries of the Organization of Eastern Caribbean States (OECS).** As established in the Report on the Ninth General Increase in the Resources of the Inter-American Development Bank (Document AB-2764), the Board approved in 2010 a special allocation of FSO resources to the Caribbean Development Bank (CDB) for on-lending to the IDA-eligible OECS Countries (Document GN-2593). The Board approved a total amount of US$6 million for the 2011-2012 allocation period with a blend of resources of 30% FSO and 70% OC, for a total amount of US$20 million in blended resources. As of December 2014, US$15.7 million (78%) of the Global Loan had been committed -- as three sub-projects for St. Vincent and the Grenadines, the Commonwealth of Dominica, and Grenada – and US$6 million had

[12] Since the estimated per capita GDP (average 2012-2013) for Guatemala and Paraguay exceeded the per-capita income threshold, these countries were determined ineligible for FSO lending during the 2015-2016 FSO allocation period (GN-2446-46).

been disbursed. The remaining 22% of the Global Loan is expected to be committed by the end of June 2015, for a project in St. Lucia. In view of the execution status, no additional allocation for the IDA-Eligible OECS countries was considered for the 2013-2014 allocation period.

B. Approvals in 2013-2014

3.4 A total of 30 operations with blended resources amounting to US$1.9 billion were approved during 2013-2014, of which US$551.3 million corresponded to FSO resources. For the two years, investment loans accounted for 70% of the FSO resources while 30% were policy based loans (PBLs). Table 4 presents detailed approvals by country and by source of fund.

Table 4. Operations Approved by Country, 2013-2014 (US$ million)

	2013			2014		
	FSO	**OC**	**Total**	**FSO**	**OC**	**Total**
	D2 Countries					
Bolivia	**75.7**	**302.8**	**378.5**	**66.9**	**267.6**	**334.5**
Investment	54.5	218.0	272.5	45.7	182.8	228.5
PBL	21.2	84.8	106.0	21.2	84.8	106.0
Guyana	**8.5**	**8.5**	**16.9**	**19.7**	**19.7**	**39.5**
Investment	0.0	0.0	0.0	19.7	19.7	39.5
PBL	8.5	8.5	16.9	0.0	0.0	0.0
Honduras	**57.0**	**133.1**	**190.1**	**72.0**	**167.9**	**239.9**
Investment	57.0	133.1	190.1	33.0	76.9	109.9
PBL	0.0	0.0	0.0	39.0	91.0	130.0
Nicaragua	**95.8**	**95.8**	**191.5**	**95.8**	**95.8**	**191.5**
Investment	73.3	73.3	146.5	73.3	73.3	146.5
PBL	22.5	22.5	45.0	22.5	22.5	45.0
Subtotal FSO IV	**236.9**	**540.1**	**777.1**	**254.4**	**551.0**	**805.4**
Investment	184.8	424.3	609.1	171.7	352.7	524.4
PBL	52.2	115.8	167.9	82.7	198.3	281.0
	D1 Countries					
Guatemala	**0.0**	**0.0**	**0.0**	**31.7**	**126.7**	**158.4**
Investment	0.0	0.0	0.0	1.2	4.7	5.9
PBL	0.0	0.0	0.0	30.5	122.0	152.5
Paraguay	**14.2**	**56.6**	**70.8**	**14.2**	**56.6**	**70.8**
Investment	14.2	56.6	70.8	14.2	56.6	70.8
PBL	0.0	0.0	0.0	0.0	0.0	0.0
	Regional					
CDB	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Investment	0.0	0.0	0.0	0.0	0.0	0.0
PBL	0.0	0.0	0.0	0.0	0.0	0.0
Grand Total	**251.1**	**596.7**	**847.9**	**300.2**	**734.4**	**1,034.6**
Investment	198.9	481.0	679.9	187.0	414.1	601.1
PBL	52.2	115.8	167.9	113.2	320.3	433.5
PBL as % Total	21%			38%		

*Excludes NSG operations and operations funded exclusively with OC resources.

Source: VPC based on IDB's OPS Analyzer.

3.5 In terms of sector distribution, on a biannual basis, 47% of projects were in the Infrastructure and Environment sector, an increase relative to the previous cycle, in which 41% of the blended resources were used in infrastructure projects. The Social Sector and Institutions for Development followed with 31% and 22%, respectively. About 18% of the total blended resources were approved in projects classified as poverty targeted investments (PTI) or aimed at improving social equity (SEQ). Table 5 presents the total amounts approved by sector and by country.

Table 5. Operations Approved by Sector, 2013-2014 (US$ million)

	2013				2014			
	Sector			Social Equity / Pov.Target	Sector			Social Equity / Pov.Target
	*Inst. for Development	Infrastructure & Environment	Social Sector		*Inst. for Development	Infrastructure & Environment	Social Sector	
Bolivia	153.0	225.5	0.0	*47.0*	0.0	291.5	43.0	*43.0*
Guyana	0.0	16.9	0.0	*0.0*	30.1	9.3	0.0	*0.0*
Honduras	0.0	40.1	150.0	*50.0*	130.0	0.0	109.9	*0.0*
Nicaragua	65.0	91.5	35.0	*35.0*	45.0	61.5	85.0	*85.0*
Total D2	218.0	374.1	185.0	*132.0*	205.1	362.3	237.9	*128.0*
Guatemala	0.0	0.0	0.0	*0.0*	0.0	5.9	152.5	*0.0*
Paraguay	0.0	70.8	0.0	*0.0*	0.0	70.8	0.0	*70.8*
Total D1	0.0	70.8	0.0	*0.0*	0.0	76.7	152.5	*70.8*
Regional	0.0	0.0	0.0	*0.0*	0.0	0.0	0.0	*0.0*
Total	**218.0**	**444.9**	**185.0**	***132.0***	**205.1**	**439.0**	**390.4**	***198.8***
% Total	25.7%	52.5%	21.8%	*15.6%*	19.8%	42.4%	37.7%	*19.2%*

*Includes Trade and Integration.

Sources: VPC based on data provided by SPD.

IV. GRANT LEVERAGE MECHANISM[13]

4.1 In September 2013 Governors approved a Grant Leverage Mechanism (GLM) with the purpose of leveraging grant resources from bilateral and multilateral donors with resources from the OC to finance investment operations in shared priority areas, thereby increasing the concessional resources available for the recipient countries (FSO D2 countries). The lending blend follows established FSO/OC percentages for each country, thereby providing a level of concessionality consistent with the countries' debt sustainability. A total of US$100 million in OC resources were approved for this pilot program.

4.2 During 2014, the first two projects of the program were approved. [14] Both projects were for Guyana and, combined reached the US$30 million OC cap established per country. The two operations were approved for the sectors of energy and water and sanitation[15]

[13] Document GN-2711-1.
[14] Projects GY-L1040 and GY-L1041. Project documents: PR-4167 and PR-4166, respectively.

with donors' resources coming from the European Union Caribbean Investment Fund (EU-CIF).

V. CONCLUSIONS

5.1 Under the DSF, debt sustainability indicators have largely continued to improve or been maintained following multilateral debt relief at the beginning of 2007. The burden of debt service declined from 2007-2013 for all FSO-IV countries except Guyana. At the same time, on average there has been no significant change in debt stock indicators for the FSO-IV, over a period when the debt stock has grown in many non-FSO IV countries. The blended lending structure has provided the Bank and the countries with the flexibility to adjust concessionality levels and the total amount of allocated resources by altering the proportion of FSO and OC over time, in accordance with the countries' changing debt sustainability situations and risks of debt distress

5.2 Although the lending blends for the four countries in 2013-2014 remained the same as the blends prevailing in 2012, the estimated *ex-post* or realized concessionality of blended loans decreased in 2013-2014, continuing a trend since 2010. Nevertheless, barring an increase in OC lending rates, *ex-post* concessionality is unlikely to decline further during the 2015-2016 period because the trends weighing on concessionality appear to have come to an end.

5.3 Portfolio performance has improved in the FSO-IV since the adoption of the DSF/EPBA, suggesting that the performance incentives imbedded in the framework has produced favorable outcomes. The proportion of the FSO-IV's undisbursed loan balances pertaining to projects classified as "on alert" or having "problem" project status has declined since 2007 and the proportion of "satisfactory" projects was higher in the FSO-IV than for the Bank as whole at December 2014. Similarly, the pace of disbursements has accelerated in the FSO-IV countries. Although the pace of FSO-IV disbursements from undisbursed SG loan balances was only half that of non-FSO-IV countries at the end of 2007, it has exceeded non-FSO countries every year from 2011-2014.

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[15] Both sectors are in line with Guyana's Country Strategy for the period 2012-2016 (GN-2690).

ANNEX I

BLENDED STRUCTURE AND EX-ANTE LEVEL OF CONCESSIONALITY

Blended Structure		Concessionality				
FSO	**OC**	**Allocation 2007-2008**	**Allocation 2009-2010**	**Allocation 2011-2012**	**Allocation 2013-2014**	**Allocation 2015-2016**
Discount rate:		7.2%	6.8%	6.5%	5.9%	5.0%
100%	0%	90.0%	89.3%	88.4%	86.0%	81.5%
75%	25%	71.3%	70.1%	69.4%	70.2%	64.7%
70%	30%	67.5%	66.2%	65.6%	67.1%	61.3%
50%	50%	52.5%	50.8%	50.4%	54.5%	47.9%
40%	60%	45.0%	43.1%	42.7%	48.2%	41.2%
35%	65%	41.3%	39.3%	38.9%	45.0%	37.9%
30%	70%	37.5%	35.4%	35.1%	41.9%	34.5%
25%	75%	33.8%	31.6%	31.3%	38.7%	31.2%
20%	80%	30.0%	27.7%	27.5%	35.6%	27.8%
15%	85%	26.3%	23.9%	23.7%	32.4%	24.5%
10%	90%	22.5%	20.0%	19.9%	29.3%	21.1%
0%	100%	15.0%	12.3%	12.3%	23.0%	14.4%

Notes:

1) Source: VPC based on GN-2442-46. GN-2442-32, GN-2442-16.

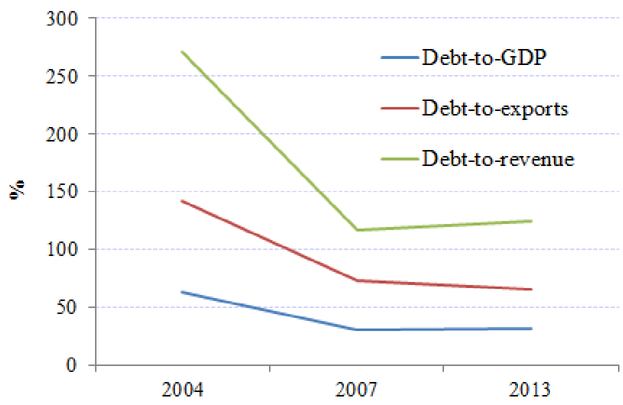
2) FSO portion is a 40-year bullet repayment loan, with a 0.25% fixed lending rate.

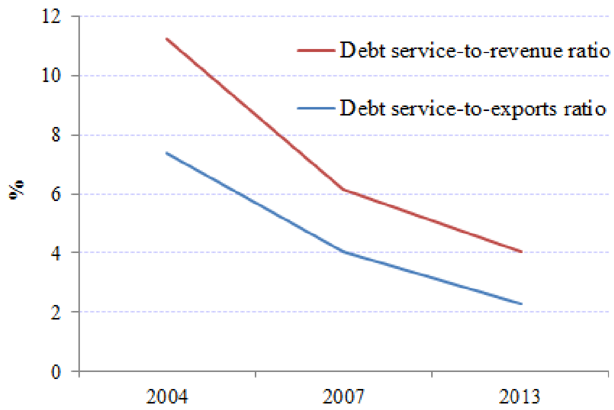
3) OC portion is 30-year maturity and 5.5-year grace period loan.

ANNEX II

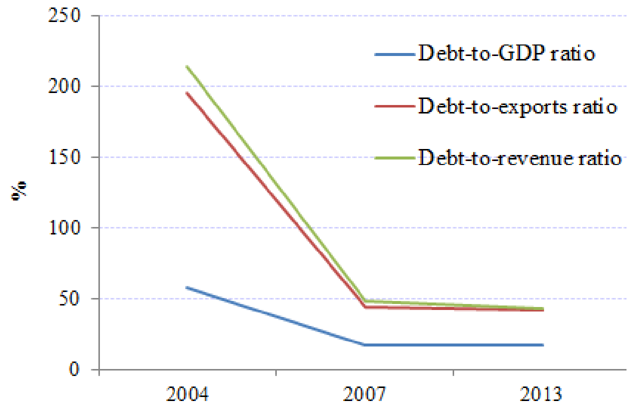
REVIEW OF DEBT SUSTAINABILITY

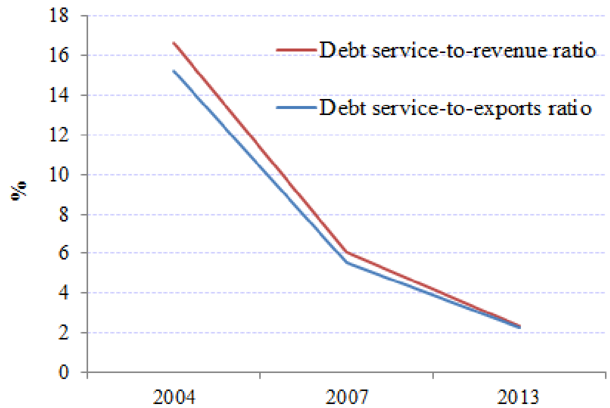
FSO IV simple average



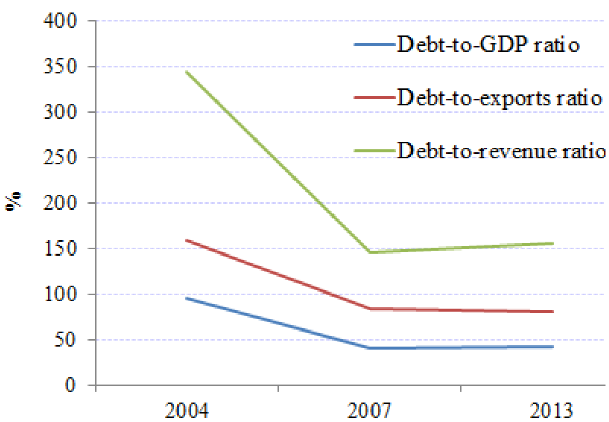


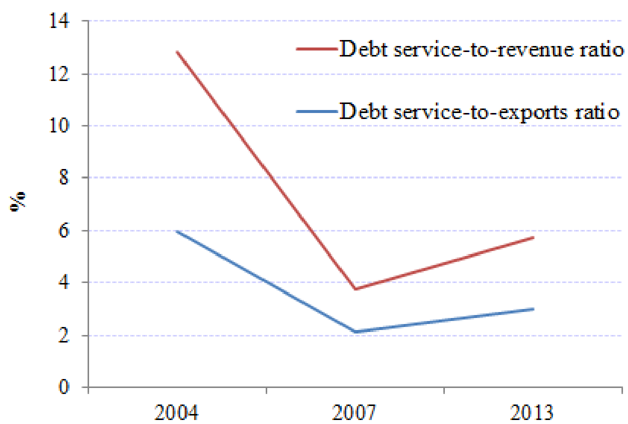
Bolivia



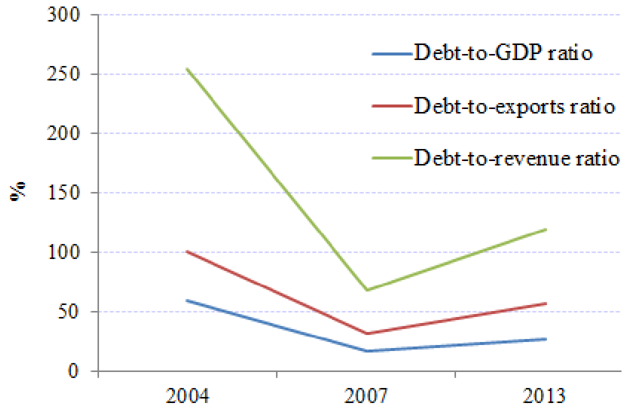


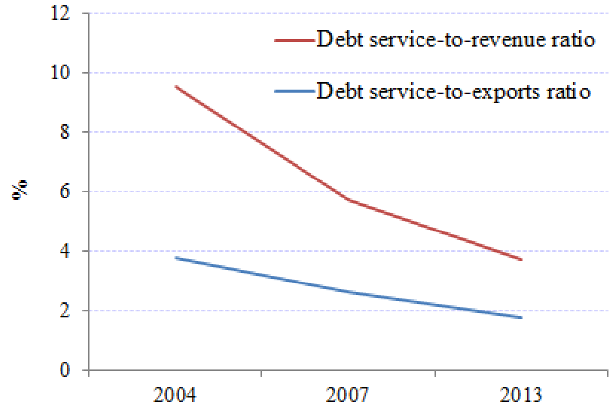
Guyana



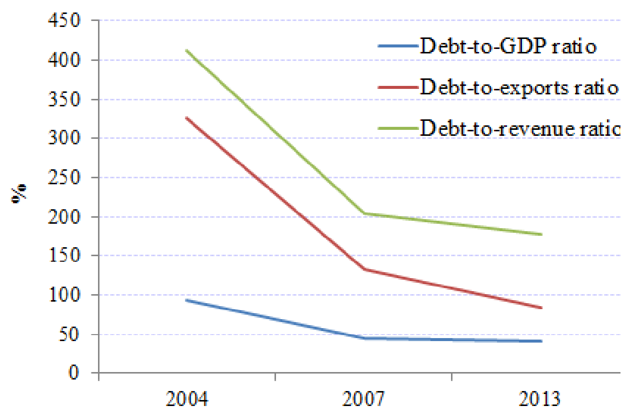


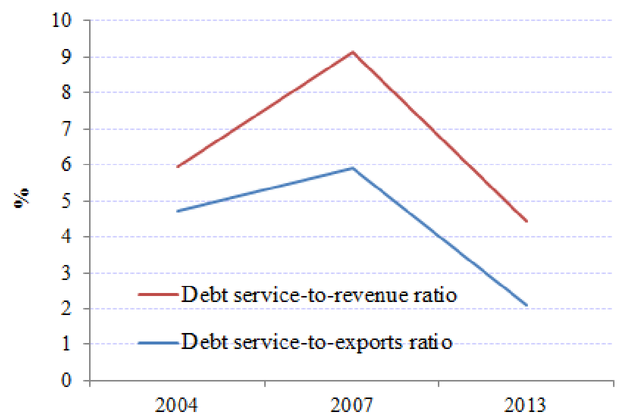
Honduras





Nicaragua





Sources: VPC based on IMF's WEO (Oct, 2014); UNCTAD; National Central Banks.

Annex III: 2014 Portfolio Performance and CIPE Scores

1. Evolution of the Percentage of Undisbursed Loan Balances (ULB) represented by projects classified as “on alert” and “problem”

Country	**2008**	**2010**	**2011**	**2013**
Bolivia	40.7%	29.8%	27.5%	15.6%
Guyana	34.7%	22.0%	18.1%	25.8%
Honduras	18.1%	28.9%	20.1%	46.3%
Nicaragua	10.2%	6.7%	14.1%	8.0%
Total FSO-IV	**28.9%**	**23.4%**	**21.6%**	**22.2%**
Guatemala	11.5%	14.0%	56.50%	-
Paraguay	17.7%	15.9%	17.70%	-
Total D1 countries	**13.5%**	**14.7%**	**38.4%**	**-**
Total	**28.9%**	**23.4%**	**21.6%**	**22.2%**

Sources: VPC based on GN-2442-46, GN-2442-41, GN-2442-32, GN-2442-16.

2. Country Institutional and Policy Evaluation 2014

A. FSO-IV Countries

Policy Cluster and Weight	Variable	BOLIVIA Score	GUYANA Score	HONDURAS Score	NICARAGUA Score
A. Economic management (15%)	1. Monetary and Exchanges Rate Policies	5.00	3.50	3.50	4.00
	2. Fiscal Policy	4.50	3.00	3.00	4.00
	3. Debt Policy and Management	5.50	3.50	3.50	4.00
	Policy Cluster A Score	**5.00**	**3.33**	**3.33**	**4.00**
B. Structural policies (20%)	4. Trade	3.71	3.33	3.94	3.58
	5. Financial Sector	4.25	3.48	3.66	3.54
	6. Business Regulatory Environment	2.77	3.33	3.29	3.28
	7. Policies and institutions for environmental sustainability	3.32	3.45	3.50	3.70
	Policy Cluster B Score	**3.51**	**3.40**	**3.60**	**3.53**
C. Social inclusion/equity policies (35%)	8. Gender equality, indigenous peoples and people of African descent	3.78	3.45	3.58	3.55
	9. Equity of Public Resource Use	3.67	3.50	3.83	3.67
	10. Building human resources	3.36	3.86	3.76	3.77
	11. Social Protection and Labor	3.70	3.40	3.60	3.00
	Policy Cluster C Score	**3.63**	**3.55**	**3.69**	**3.50**
D. Public sector management and institutions (30%)	12. Property rights and rule-based governance	3.03	3.05	2.74	2.86
	13. Quality of budgetary, procurement and financial management	3.25	3.00	3.13	3.50
	14. Efficiency of revenue mobilization	4.25	3.50	3.25	4.00
	15. Quality of public administration	2.52	2.71	2.67	2.50
	16. Transparency, accountability and corruption in the public sector	2.87	2.39	2.61	2.38
	Policy Cluster D Score	**3.18**	**2.93**	**2.88**	**3.05**
	Total Score	**3.68**	**3.30**	**3.38**	**3.44**

Source: GN-2442-46
Note: CIPE scores and underlying write-ups were prepared by CAN, CCB, CID, and CSC, in coordination with sector specialists, and reviewed and validated by SPD and RES.

ANNEX IV: EVOLUTION OF COUNTRY INDICATORS OF THE ENHANCED PERFORMANCE-BASED ALLOCATION

	Allocation 2007-2008	Allocation 2009-2010	Allocation 2011-2012	Allocation 2013-2014	Allocation 2015-2016
		Population			
Bolivia	8,986,396	9,518,000	9,862,860	10,088,108	10,671,200
Guyana	772,056	739,000	762,498	756,040	799,613
Honduras	7,141,464	7,091,000	7,465,998	7,754,687	8,097,688
Nicaragua	5,604,000	5,605,000	5,742,800	5,869,859	6,080,478
Guatemala	12,628,480	13,348,000	14,026,947	14,757,316	-
Paraguay	5,781,569	6,120,000	6,348,917	6,568,290	-
		GNI p/c (Atlas method)			
Bolivia	960	1,260	1,620	2,040	2,550
Guyana	990	1,300	1,450	2,900	3,750
Honduras	1,030	1,600	1,820	1,970	2,180
Nicaragua	790	980	1,000	1,170	1,780
Guatemala	-	2,283	2,620	2,870	-
Paraguay	-	1,380	2,270	2,970	-
		Portfolio Performance (1-6 scale)			
Bolivia	3.27	3.97	4.51	4.63	5.22
Guyana	4.95	4.27	4.90	5.09	4.71
Honduras	4.95	5.09	4.55	5.00	3.69
Nicaragua	5.36	5.49	5.66	5.29	5.60
Guatemala	3.6	5.42	5.30	3.18	-
Paraguay	5.0	5.11	5.21	5.12	-
		CIPE (1-6 scale)			
Bolivia	3.10	3.23	3.75	3.75	3.68
Guyana	2.75	3.39	3.75	3.62	3.30
Honduras	3.85	3.95	3.72	3.58	3.38
Nicaragua	3.58	3.55	3.53	3.49	3.44
Guatemala	3.6	3.76	3.52	3.34	-
Paraguay	3.9	3.81	3.48	3.34	-

Sources: VPC based on GN-2442-46, GN-2442-41, GN-2442-32, GN-2442-16.