

**CARIBBEAN DEVELOPMENT BANK**



**SPECIAL DEVELOPMENT FUND (UNIFIED)**

**SDF 7: A STRATEGIC PERSPECTIVE**

**July 2008**

## ABBREVIATIONS

AsDB	-	Asian Development Bank
BMCs	-	Borrowing Member Countries
Bn	-	billion
BNTF	-	Basic Needs Trust Fund
CARICOM	-	Caribbean Community
CDB	-	Caribbean Development Bank
CDM	-	Comprehensive Disaster Management
CPAs	-	Country Poverty Assessments
CSPs	-	Country Strategy Papers
CSO	-	Civil Society Organisation
CTCF	-	Canadian Technical Cooperation Fund
CTCS	-	Caribbean Technological Consultancy Services
DRM	-	Disaster Risk Reduction
EVI	-	Economic Vulnerability Index
GDP	-	Gross Domestic Product
GPRS	-	Growth and Poverty Reduction Strategy
HRD	-	Human Resource Development
ISF	-	Interest Subsidisation Fund
MDBs	-	Multilateral Development Banks
MDGs	-	Millennium Development Goals
MfDR	-	Managing for Development Results
NPRSs	-	National Poverty Reduction Strategies
OCR	-	Ordinary Capital Resources
OECS	-	Organisation of Eastern Caribbean States
p.a.	-	per annum
PBL	-	Policy-Based Loans
PBG	-	Policy-Based Guarantees
PCRs	-	Project Completion Reports
PPMS	-	Project Portfolio Management System
PRS	-	Poverty Reduction Strategy
RPGs	-	Regional Public Goods
SDF	-	Special Development Fund
SDF 6	-	Special Development Fund (Sixth Cycle)
SDF 7	-	Special Development Fund (Seventh Cycle)
SDF (U)	-	Special Development Fund (Unified)
SFR	-	Special Funds Resources
SMEs	-	Small- and Medium-Size Enterprises
SwAPS	-	sector-wide approaches
TA	-	Technical Assistance
\$		US dollar (unless otherwise specified)

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## EXECUTIVE SUMMARY

1. The Special Development Fund (Seventh Cycle) (SDF 7) strategy is anchored in the Caribbean Development Bank's (CDB) Strategic Plan 2005-2009 and developed within the context of the regional economic and social environment, the impact of global trends on this regional environment and the lessons learned from the Bank's experiences in the Special Development Fund (Sixth Cycle) (SDF 6) and earlier Special Development Fund (SDF) cycles (i.e. the Strategic Context). The strategy is, therefore, built around the Millennium Development Goals (MDGs), the international economic context and the major transition challenges facing the Caribbean. In addition, the SDF 7 strategy is aligned with the themes and objectives of the new Strategic Plan that is under preparation.

2. The economic and social environment and the challenges facing Caribbean economies define the context within which the strategy for SDF 7 is crafted. Poverty, inequality and social exclusion remain defining features of the economic and social reality of the Region and constitute important targets for development intervention. Increasing the rate of economic growth and reducing the volatility of that growth, are major macroeconomic objectives. Underlying growth performance is the issue of competitiveness. The Region's vulnerability to economic shocks and natural disasters and the need for adaptation to, and mitigation of climate change, are also critical issues. Fiscal and debt performance are also important determinants of growth performance and must be addressed if sustainable growth is to be achieved. All of these issues need to be approached in the context of the threat of a global recession and the reality of sharply rising commodity and food prices, with their implications for growth, employment and poverty reduction in the Caribbean. CDB's own capacity and the lessons learned when implementing SDF 6 and earlier cycles of SDF also influence the nature of the SDF 7 strategy. The Caribbean MDGs and the related Caribbean-specific targets will remain as the basis for the overall monitoring of progress towards reducing poverty.

### **Strategic Themes**

3. Contributors have agreed on the following four core themes for the replenishment of SDF 7, with **gender equality** as a cross-cutting theme:

- ***strengthening poverty reduction and human development***, including the Bank's strategic response to the challenge of providing effective and meaningful assistance to Haiti, and supporting the MDGs and Caribbean-specific MDG targets in the Bank's Borrowing Member Countries (BMCs);
- ***supporting environmental sustainability and advancing the climate change agenda***, including addressing the vulnerability of the Bank's BMCs to environmental risks and climate change mitigation and adaptation;
- ***supporting regional cooperation and regional integration***, including an appropriate operational framework to support priority needs of the Caribbean Community (CARICOM) and its members and the provision of regional public goods (RPGs); and
- ***further enhancing development effectiveness***, including Managing for Development Results (MfDR) and application of the Paris Declaration on Aid Effectiveness, and including strengthening of the Bank's human resources and institutional capacity.

## **Poverty Reduction and Human Development**

4. The reduction of poverty remains the core value pursued by the Bank in all of its BMCs. The strategic levers of the Bank's Poverty Reduction Strategy (PRS): *Capability Enhancement, Vulnerability Reduction and Good Governance*, facilitates the effective targeting of the Bank's poverty reduction efforts. Within the framework of these strategic levers, it is recognised that rapid, broad-based economic growth is critical for sustaining poverty reduction. Addressing issues of poverty, at the national level, will thus continue to require actions on:

- promoting the economic opportunities and productive capabilities of the poor through action affecting the human, physical and natural assets of poor people;
- facilitating the development of the private sector by supporting an enabling environment and contributing to financial sector development;
- targeting vulnerabilities that affect the poor – or those at risk of becoming poor – resulting from personal risks (e.g. health) or national risks (e.g. economic shocks, natural disasters) by reducing macro risks and establishing/enhancing social protection mechanisms; and
- promoting good governance by:
  - improving access to, and delivery of, services that benefit the poor and vulnerable;
  - promoting sound policy and equitable resource allocation, i.e. sound macroeconomic management; and
  - encouraging increased citizen/stakeholder participation in the decision-making processes and in policy, programme and project implementation.

## **Environmental Sustainability and Climate Change**

5. It is proposed that the focus of the Bank's operational strategy on environmental sustainability and climate change during SDF 7, should be to assist BMCs to design and implement interventions that promote environmental sustainability in areas that:

- (a) widen the options for sustaining the livelihoods of the poor and vulnerable through improved protection and sustainable management of natural resources;
- (b) improve coverage of the population with access to improved water and sanitation services to reduce pollution and improve the health and productivity of the poor;
- (c) reduce BMCs' vulnerability to natural hazards and improve resilience and adaptation to climate change; and
- (d) strengthen the capacities of regional and national institutions capacity for improved environmental and natural resource management.

6. Given resource limitations, however, the areas for CDB's interventions will need to be carefully selected using the following criteria:

- (a) provide opportunities for significant beneficial impacts for the poor and vulnerable;

- (b) contribute to BMCs stated BMC environment priorities;
- (c) offer opportunity to significantly improve environmental benefits and natural resource management in areas where CDB has experience, credibility and comparative advantage; and
- (d) offer potential for synergies with other CDB areas of the Bank's operations and those of other development partners.

7. CDB's interventions should, therefore, target protected areas management; improved water, sanitation and solid waste management systems; disaster risk reduction; and the climate change agenda. In relation to the latter area, particular attention should be focused on climate change mitigation and adaptation measures. Mitigation will require additional support for policy, regulatory and governance mechanisms so that renewable energy sources and energy efficiency measures can be fully exploited. Assistance will be provided to BMCs to integrate climate change adaptation measures into their agendas for sustainable development and poverty reduction as well as for sectoral policies. The most vulnerable group likely to be impacted by climate change are the poor, thus targeted measures that help to build community resilience to climate change will be implemented, together with the Basic Needs Trust Fund (BNTF) and other programmes. Support will be provided to regional institutions to strengthen and advance the Caribbean knowledge base about climate change and to monitor adaptation measures. BMCs will also be assisted in accessing innovative climate change funding mechanisms.

### **Regional Cooperation and Integration**

8. CDB recognises that its BMCs have entered a critical phase of the integration process, one that will determine not only how well the objectives set out in the Preamble to the Revised Treaty of Chaguaramas are achieved, but whether the centripetal forces are strong enough, with coordinated development partner support, to overcome the genuine fears that accompany the eventual subsuming of the individual sovereignty of small states into a larger, more flexible and responsive entity, better able to cope with the demands of a new global reality. In SDF 7, CDB will continue to focus its project interventions in developing common structures and processes in its borrowing members, based on best practices. This approach will facilitate coordination and mutual support among officials and stakeholders in the BMCs themselves, both generally, and in specific areas of activity and operations. Support for RPGs' initiatives will be an important element in the Bank's support for regional cooperation and integration.

### **Gender Equality**

9. Improving gender equality stands on its own merits as a development objective. The primary rationale for addressing gender equality in the CDB's programming is the strong link between gender inequality and poverty in the region, in both rural and urban contexts. To effectively address poverty, the Bank will continue to utilise strategic entry points for integrating gender issues into existing Bank processes. At the same time, it proposes to be more systematic in the way the effort to achieve gender equality is mainstreamed. Further, in order to strengthen the performance of the Bank in its policy dialogue with BMC officials on economic management and to assist the Bank in being more efficient in the use of its investment resources in a development context, it needs a framework to improve analytic and sector work. It also needs a methodology for designing loans and grants that exhibit a greater responsiveness to the priority development needs related to gender equality issues of BMCs and the region. The development of a gender policy and strategy is therefore critical.

## Development Effectiveness

10. As in the case of most developing countries and other development agencies, managing for development results (MfDR) and increasing development effectiveness at CDB are a work in progress, and further steps need to be taken in SDF 7. Increasing development effectiveness is a shared objective, with roles and responsibilities for both the Bank and BMCs. There are factors beyond the Bank's control that need to be addressed by BMCs, as well as other development partners. The Bank's agenda, therefore, addresses those steps that the Bank itself can take, including, where appropriate, supporting BMCs in their MfDR and development effectiveness agendas, and working with other development partners towards increased harmonisation and alignment. The agenda has been developed to be capable of implementation with modest resources and within the overall demands of CDB's work programme, including that expected to be set for SDF 7.

11. The Bank's MfDR agenda will be paralleled by a results monitoring framework, which will be similar to that adopted by other Multilateral Development Banks (MDBs) in recent replenishment discussions, although incremental and adapted to CDB's particular circumstances, operational priorities and capacities. The results framework will be linked to the MDGs, particularly those that are most relevant to the Bank's operational programme, and will include more consistent identification, monitoring and reporting of results at various levels. It will include performance indicators to measure progress in terms of institutional and operational effectiveness.

## Operationalising the Strategy

12. The mix of measures adopted to operationalise the strategy is determined by the availability of human and financial resources, the Bank's own capacity, and on the institutional capabilities of the different BMCs. It also depends on the effectiveness of the partnerships that can be built with other development agencies operating in the Region. The Bank's interventions need to become more finely focused so that they are consistent with its capabilities, and this underscores the importance of partnerships. Country-level interventions need to be complemented by regional public action to deal with areas where externalities or public good characteristics at the regional level have a direct or indirect impact on poverty reduction. The approach to different countries may be differentiated depending on country conditions and capabilities. It is envisaged that the Bank will increasingly rely on local capacity for analysis and will adapt its modalities to reflect these changes. The Bank's result-based country strategy will be the basis on which the Strategy will be operationalised in each BMC.

13. The instruments that will be used to operationalise the strategy are the standard MDB products, but designed with increased flexibility to allow greater responsiveness to the dynamic environment. For CDB, these instruments include:

- **Investment Loans** – either Special Funds Resources (SFR) alone or blended with Ordinary Capital Resources (OCR). OCR could involve use of the Interest Subsidisation Fund (ISF).
- **Technical Assistance (TA) Loans and Grants** – in the case of TA loans, these could involve SFR, SFR/OCR blend, OCR or OCR/ISF. Grants will be funded from SDF and, when appropriate, specific SFR resources such as the Canadian Technical Cooperation Fund (CTCF) or the China Fund.
- **Policy-Based Loans (PBLs)/Policy-Based Guarantees (PBGs)** – PBLs and PBGs are usually part of a broader assistance strategy to improve a country's debt dynamics, enhance public sector management systems, foster fiscal sustainability and improve

overall macroeconomic fundamentals. PBLs usually involve SFR/OCR blending. Country eligibility and resource availability would determine use of ISF resources.

- **Contingently Recoverable Loans** – especially in instances where there is considerable uncertainty regarding the viability of the investment or the ability of the investment to be financed.

14. The strategic levers of the Bank’s PRS: *Capability Enhancement, Vulnerability Reduction and Good Governance*, can be used to identify the modalities used in operationalisation of the SDF 7 Strategy. The categorisation of modalities under these strategic levers is not rigid because most interventions contribute to more than one area. These are, essentially, the same modalities used in SDF 4, 5 and/or 6, and are not exhaustive.

15. The modalities are as follows:

### **Capability Enhancement**

- Solid Waste Management
- Student loans Scheme
- Technical and Vocational Education [including sector-wide approaches (SwAPs)]
- Tertiary Education (including SwAPs)
- Natural Resource Management/Ecotourism Development
- Rural Enterprise Development Projects
- Essential Infrastructure and Services
- Rehabilitation/Expansion of Productive Capabilities
- Micro and Small Enterprise Development – Especially the Caribbean Technological Consultancy Service (CTCS).

### **Vulnerability Reduction**

- Natural Disaster Response:
  - Immediate Response
  - Rehabilitation
  - Risk Reduction and Management
- Climate Change Mitigation and Adaptation
- Renewable Energy and Energy Efficiency
- Social Investment Funds
- Basic Needs Trust Fund (BNTF)
- Low-income Housing
- Shelter Development
- Early Childhood Education (including SWAPs)
- Basic Education (including SWAPs)

### **Good Governance**

- Institutional Strengthening Technical Assistance (TA)
- Public Sector Reform
- Policy-based Interventions

16. SDF 7 would, therefore, employ essentially the same modalities as before and this is reflective of the need for the Bank to maintain strategic focus especially in the areas where it has competitive advantage. In applying these modalities, CDB would emphasise reinforcement of the strategic framework

already developed, consolidation of changes already in train and setting more realistic and achievable targets that allow sufficient time for transformational change. In particular, managing for development results (MfDR) is vital to future success in addressing most of the deficiencies described and will be strengthened and deepened as a central process in all future interventions. Towards this end, more effort and resources would be invested in a strategic and systematic way to develop the policies, institutions, human resources, information systems and tools required to design and manage projects for development results and to sustain project benefits. CDB is already making interventions in this direction. These interventions would be designed to be more strategic, integrated and systematic. SDF 7 would support a comprehensive strategy and programme to build vital capacity at the national, sub-regional and regional levels. This would form the core of the TA programme. CDB would also address issues such as inflexibility, human resource limitations and inadequate supervision which make MfDR difficult or impossible. A stronger commitment by BMCs to MfDR and to engage in the transformation processes required is imperative to the success of SDF interventions.

## 1. INTRODUCTION

1.01 SDF<sup>1/</sup> is a partnership between countries of the Caribbean, both borrowing and non-borrowing, and countries from outside the region. SDF provides a major element of the resources of CDB and allows a range of operations that would not otherwise be possible, including operations in the poorest, most vulnerable and most highly indebted countries among the Bank's membership. It plays a critical role in the international effort to achieve poverty reduction, the MDGs, and major economic adjustment in the Caribbean.

1.02 This role has become increasingly important as poverty reduction efforts and targeting of the MDGs have become more focused and based on a deeper understanding of the poverty and economic vulnerability in Caribbean countries. The SDF mandate has expanded with a doubling of the number of persons in its client base and a greater increase still in the number of the poor that it is intended to help, and as the economic challenges and potential have become clearer. It is also becoming increasingly effective, with better information, more effective instruments, learning through the evaluation of past experience, and a focus on MfDR and cooperative partnerships as part of the international Harmonisation and Alignment agenda. A stronger framework for targeting and measuring results has also been provided by the Caribbean MDGs, developed with CDB's leadership and support.

1.03 Progress and achievements under SDF 6 to date have been reported to Contributors and discussed both at a Preparatory Meeting in December 2007, at the First Negotiation Meeting held in Belize in early April 2008 and at the Second Negotiation Meeting held on May 27, 2008 in Halifax, Canada<sup>2/</sup>. The SDF 6 cycle covers the period 2005-2008, with a revised programme level of \$238.5 million (mn), of which \$224 mn is expected to be committed by the end of 2008. This leaves some \$14.5 mn to support planning and operations in the early part of 2009, when the SDF 7 replenishment will need to be put in place to support continued operations of the SDF 7 partnership.

1.04 The present paper provides an overview of the strategy for planning and implementation of SDF 7. It is based on *A Strategic Framework for SDF 7: Discussion Outline* (the Framework Paper), presented at the May 2008 Meeting of Contributors and it draws on a Background Paper - *Context And Issues For SDF 7: Economic Performance and Prospects in the Caribbean* which is attached to this Paper (See Attachment A).

1.05 The Framework Paper indicated that an SDF 7 strategy must be anchored in CDB's Strategic Plan 2005-2009 and developed within the context of the regional economic and social environment, the impact of global imbalances on this regional environment and the lessons learned from the Bank's experiences in SDF 6 and earlier SDF cycles (i.e. the Strategic Context). The strategy must, therefore, be built around the MDGs, as these have been adjusted for the Caribbean, the international economic context and the major transition challenges facing the Caribbean, including the nature and extent of poverty in the Bank's BMCs, and the issues of vulnerability to economic shocks and natural disasters and adaptation to and mitigation of climate change. In addition, the SDF 7 strategy must be aligned with the themes and objectives of the new Strategic Plan that is under preparation.

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<sup>1/</sup> All references to the Special Development Fund are to the Unified Special Development Fund [SDF (U)] established in 1983.

<sup>2/</sup> Status Report on the Special Development Fund – Sixth Cycle, SDF 7/1-NM-2, Rev.1, May 2008

**FIGURE 1: THE STRATEGIC FRAMEWORK**



## **2. THE STRATEGIC CONTEXT**

2.01 The economic and social environment and the challenges facing Caribbean economies define the context within which a strategy for SDF 7 must be crafted. Poverty, inequality and social exclusion remain defining features of the economic and social reality of the Region and constitute important targets for development intervention. Increasing the rate of economic growth and reducing the volatility of that growth, are major macroeconomic objectives. Underlying growth performance is the issue of competitiveness. Fiscal and debt performance are also important determinants of growth performance and must be addressed if sustainable growth is to be achieved. All of these issues need to be approached in the context of the threat of a global recession and the reality of sharply rising commodity and food prices, with their implications for growth, employment and poverty reduction in the Caribbean. CDB's own capacity and the lessons learned when implementing SDF 6 and earlier cycles of SDF also influence the nature of the SDF 7 strategy. The Caribbean MDGs will remain as the basis for the overall monitoring of progress of implementation of SDF 7 programmes. Figure 2 illustrates the strategic context.

### **THE ONGOING CHALLENGE OF POVERTY AND INEQUALITY**

2.02 Country Poverty Assessments (CPAs), surveys of living conditions and household budgetary surveys conducted in many Caribbean countries between 1998 and 2005 provide the basis for assessing the incidence, poverty and economic vulnerability in the Region. Looking at the Region as a whole, the results confirm that, despite significant gains in all areas of social life, poverty is very much present in the Caribbean, and has taken new forms and dimensions such as the growth of urban poverty, new types of rural poverty and poverty arising from the impact of HIV/AIDS and the ageing of the population. Poverty, inequality and social exclusion thus remain frustrating features of the economic and social development of the Region.

2.03 Several complex, interrelated factors have contributed to offsetting and sometimes erasing previous gains in the levels of living in the Caribbean. These include the slowing down of economic growth, the decline in growth of single crops or sectors on which strong reliance had been placed, the impact of natural disasters, and diminishing real public expenditures essential for access to vital social services such as education, health and sanitation. Other compounding factors contributing to the level of indigence and poverty include the economic disparities within countries and communities<sup>3/</sup>, the decline in family income as a result of economically debilitating health challenges arising from both chronic and communicable diseases, environmental degradation, urgent problems of food price inflation and food security, and weakening of the traditional family as an institution.

**FIGURE 2: THE STRATEGIC CONTEXT**



**ECONOMIC GROWTH PERFORMANCE**

2.04 The rate of economic growth is a major factor impacting on the level of poverty. As indicated by the experience of some of the Asian economies, high, relatively stable growth rates over extended periods can reduce poverty levels substantially. These very successful economies have been able to sustain growth rates of between 8% and 10% per annum (p.a.) for an extended period. Such growth rates have allowed, for example, Singapore to reduce its poverty level from 31% in 1970 to 10% in 2003; China from 30.7% in 1978 to 9.1% in 2003; South Korea from 39.6% in 1990 to 13.4% by 1999.

2.05 Real income growth for CDB’s BMCs averaged 3% over the period 1990-2007, and with considerable variability. The average reached 3.8% during 2002-2007, or 3.4% excluding the very strong performance of Trinidad and Tobago of approximately 9%. During the periods 1992-96 and 1997-2001, growth averaged 2.2% and 2.9% (2.7% without Trinidad and Tobago). In the 1992-96 period, the Region began to feel the effects of the diminution of European trade preferences. During the 1990s also,

<sup>3/</sup> 12 of the 14 BMCs that reported on income distribution exhibited Gini Coefficients greater than 0.35. This compares with only 5 of the top 20 countries on the UN HDI exhibiting Gini Coefficients in excess of 0.35.

several regional economies (Guyana, Jamaica and Trinidad and Tobago) underwent structural adjustment programmes with the international financial institutions, of which an important component was the opening up of these economies to international trade. The second period also includes the impact of 9/11.

2.06 Additionally, the considerable variability of growth performance was highly problematic for most countries. Estimates of the coefficient of variation (the ratio of the standard deviation to mean growth) of growth performance for several countries was greater than 1, underscoring the vulnerability of regional economies to exogenous shocks. A coefficient of variation of 1 implies that a shock such as a hurricane or an event such as 9/11 can throw an economy completely off its trend growth rate and into a recession, depending on the severity of the shock.

2.07 The substantial vulnerability of Caribbean economies to economic shocks and natural disasters has particular implications for the poor and the vulnerable, and especially the latter, which represent a significant proportion of the population. These persons can be pushed into poverty because of economic shocks and/or natural disasters. Meanwhile, the lot of the poor is also made worse. This is a very important characteristic of the poverty landscape in the Caribbean that needs to be understood and considered in designing of poverty reduction interventions in BMCs.

**BOX 1: VULNERABILITY INDEX**

In 2006, an earlier study on deriving an economic vulnerability index (EVI) for CDB’s BMCs was updated. The 2006 study included an additional variable that captured the “quality of the insertion of nation states into the global economy by evaluating the type of exports of goods and services. The study shows that countries exporting goods and services with low income and/or price elasticity are more vulnerable than those that engage in products that are technologically dynamic and have high price and income elasticities.

**EVI SCORES AND RANKING**

<b>Country Groups</b>	<b>EVI</b>	<b>Ranking</b>
All Countries	0.50	6
Caribbean	0.62	4
Islands	0.63	3
Landlocked	0.50	6
Large States	0.36	10
Medium States	0.50	6
Micro States	0.68	1
Non-Small States	0.44	9
SIDS	0.64	2
Small States	0.62	4

The Caribbean ranked fourth in economic vulnerability. Nine of CDB’s BMCs are among the most vulnerable countries and 12 are among the 36 most vulnerable. One of the major vulnerabilities is the exposure to natural disasters, which are frequent and often devastating. Every BMC has been affected in some way and several have suffered more than one such event in the 1998-2007 period. The estimated cost of these events over this period is \$9.2 billion (bn), not including the economic output foregone.

## **FISCAL AND DEBT PERFORMANCE**

2.08 A significant number of BMCs are in fiscal and debt difficulties, thereby compromising their ability to address the problems of poverty and vulnerability. During 2002-06, six BMCs averaged fiscal deficits of more than 5% of Gross Domestic Product (GDP). By the end of 2007, five BMCs had ratios of public sector debt to GDP of more than 100% and all were facing problems of fiscal and debt sustainability. Others, while not as heavily indebted, are substantially above what has emerged as the prudential norm internationally, i.e. a public sector debt to GDP ratio of no more than 60 % of GDP.

2.09 The ratios of debt servicing to recurrent revenue, reflects the considerable burden on the budget in the heavily indebted countries of the Region. In many of these countries, the substantial portions of recurrent revenue dedicated to debt servicing underscore the high opportunity cost of significant debt accumulation in terms of expenditure foregone on education, health, housing, water, sanitation and other services that are critical to empowerment and welfare enhancement of the poor and vulnerable

## **THE ECONOMIC CHALLENGES**

2.10 The openness of Caribbean economies makes them particularly vulnerable to terms of trade and other shocks from the external environment. The current international environment is very unstable, with several dangers looming for the Caribbean. Arguably, the greatest threat is the possibility of a global recession. The effects of such an event on the Caribbean could be very destabilising, depending on its severity and duration. With the concomitant expectation of lower export levels for both goods and services and reduced growth and employment in the Region, the impact on the poor and vulnerable is potentially devastating.

2.11 Another significant threat to the Region is the upward trend in inflation. Estimates of inflation in the Caribbean during the period 2003 to 2007 indicate that in a significant proportion of countries, the rate of inflation is increasing, driven by imported inflation, essentially from rising oil and food prices, which account for 50% or more of the rise in prices. The consequent erosion in the standard of living is leading towards a tense political and industrial climate in which unions are pressing for higher wages, sometimes from governments that are already fiscally challenged. In those countries where governments have taken action to protect their populations from spiraling inflation through the foregoing of tax revenues on imports of food and oil, or have eliminated or reduced certain border taxes, there have been significant fiscal costs.

2.12 Independently of the impact on inflation, rising food prices, given the heavy dependence of the Caribbean on food imports, are of major concern to the Region. Regional food imports, including for Suriname and Haiti, amount annually to more than \$2 bn. Between 1994 and 2004, regional food imports grew in real terms by 2.4% p.a. In some countries, food dependence, defined by the ratio of food imports to consumption in volume terms, is already close to or more than 80%.

2.13 In the absence of strong energy conservation initiatives, the development of alternative sources of energy, or significant oil discovery, the vulnerability to oil shocks will continue and likely intensify. This will fuel inflationary pressures; reduce growth rates, and increase unemployment and poverty. Increasing raw material demand, related to strong economic growth in East Asia, China and India, however, will continue to benefit regional producers of mining products - Trinidad (oil), Guyana (bauxite) and Jamaica (bauxite and alumina). These countries are likely to experience improved terms of trade, growing trade surpluses, improved current account balances, and an accumulation in reserves. But it must be remembered that the quality of growth is also important. Unsustainable extraction of resources, for example, undermines environmental sustainability and compromises future growth.

## **LESSONS FROM SDF 6 AND EARLIER CYCLES**

2.14 One of the principal assessments of SDF performance will be the multi-cycle evaluation of SDF that is currently underway and for which some preliminary findings are now available. Although this is focussed primarily on the two most recently completed cycles of SDF (SDF 4 and SDF 5), for which outcomes and performance can be better assessed, the evaluation is expected to put its findings in the context of more recent developments during SDF 6. The multi-cycle evaluation follows on from the SDF Performance Review in 2000, which assessed the response of SDF to new directions set by Contributors. Other important contributions to the lessons learned include the SDF 6 Mid-Term Review/Evaluation, the Evaluation of the Bank's TA Operations and the Mid-Term Evaluation of BNTF 5.

2.15 The detailed findings have been or will be reported in the individual review/evaluation reports and summarised in a separate paper.<sup>4/</sup> For present purposes, however, it is useful to identify those lessons that are likely to have *strategic significance* in the context of SDF 7. The lessons identified here are, therefore, those that focus on the broad design of SDF 7 and not on individual modalities or interventions.

### **Overall Performance and Effectiveness**

- The Bank needs to sharpen its focus on its poverty reduction mission, by expanding its use of MfDR, and other management improvement initiatives where appropriate.
- There is a priority need for the Bank to strengthen its results orientation. An outcomes-oriented culture needs to be more deeply imbedded.
- The Bank needs to establish priorities, consistent with its capacity and capabilities. CDB needs to focus and avoid new commitments that may lead to unreasonable expectations on the part of Contributors.
- Human resource constraints have become a chronic issue at the Bank and affected the Bank's performance in SDF 5. For example, there is an urgent need to improve the level and type of supervision required, particularly in multidisciplinary projects.
- In a small organisation like CDB, giving effect to policy shifts and programme improvements in a four-year time frame - the SDF Cycle - is a significant challenge.
- Greater effort needs to be placed in the development of partnerships and collaboration with other development actors.
- More resources need to be directed to improving the policy and institutional frameworks for supporting project interventions in BMCs.

### **TA Operations**

- CDB's TA programme needs to more strategic and focussed.
- There is a need for a central focal point for TA operations and a greater level of training should be provided to Operations staff.
- Mechanisms need to be put in place to ensure access to specialised TA experience and skills.

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<sup>4/</sup> Performance and Results Analysis: Lessons Learned from use of Various Modalities in SDF Operations and Implications for SDF 7, SDF 7/3 NM-2

### **Basic Needs Trust Fund**

- The foundations of the social orientation of BNTF should be strengthened.
- BNTF should enhance and further define its strategic partnerships with government ministries, non-governmental organisations, and other development partners.
- BNTF should continue its shift from one-off subprojects in the community to a more integrated and comprehensive targeted approach to poverty reduction.
- The programme should enhance integration of the cross-cutting themes that are directly relevant to BNTF, such as Gender and the Environment.

2.16 During discussion on the Framework Paper, Contributors also identified a number of features that should guide strategy formulation for SDF 7:

- The importance of economic growth as a central component of the strategy.
- The continuing importance of poverty reduction, environmental sustainability, climate change and regional integration in regional development (i.e. the Strategic Themes).
- The significance of the current global environment – economic slowdown, rising commodity and food prices – in strategy formulation.
- The critical importance of a well-developed results framework to measure and monitor performance.
- The need to build in flexibility in strategy implementation.
- The importance incorporating institutional capacity-building in BMCs as an element of the Strategy.

### **3. THE SDF 7 STRATEGY**

3.01 The SDF strategy is an important sub-set of the Bank's overall strategy and must be built around this strategy. In a real sense, the strategy for SDF 7 would be a continuation of SDF 6, but with changing emphases. Significantly, the SDF 7 themes (outlined below) are consistent with the current Strategic Plan. The themes reinforce the linkages between the Bank's Mission Statement, the Strategic Plan, and other guiding documents such as the Resolution and Report of Contributors to the SDF (U), PRS, and other thematic and sector policies and strategies. It should be noted that 2008 is the mid-point of the period set for the achievement of the MDGs and that the seventh cycle (2009-2012) of the SDF is the last full cycle before the MDG target date of 2015. This cycle and its action plans and programmes should provide the momentum for BMCs to achieve these goals.

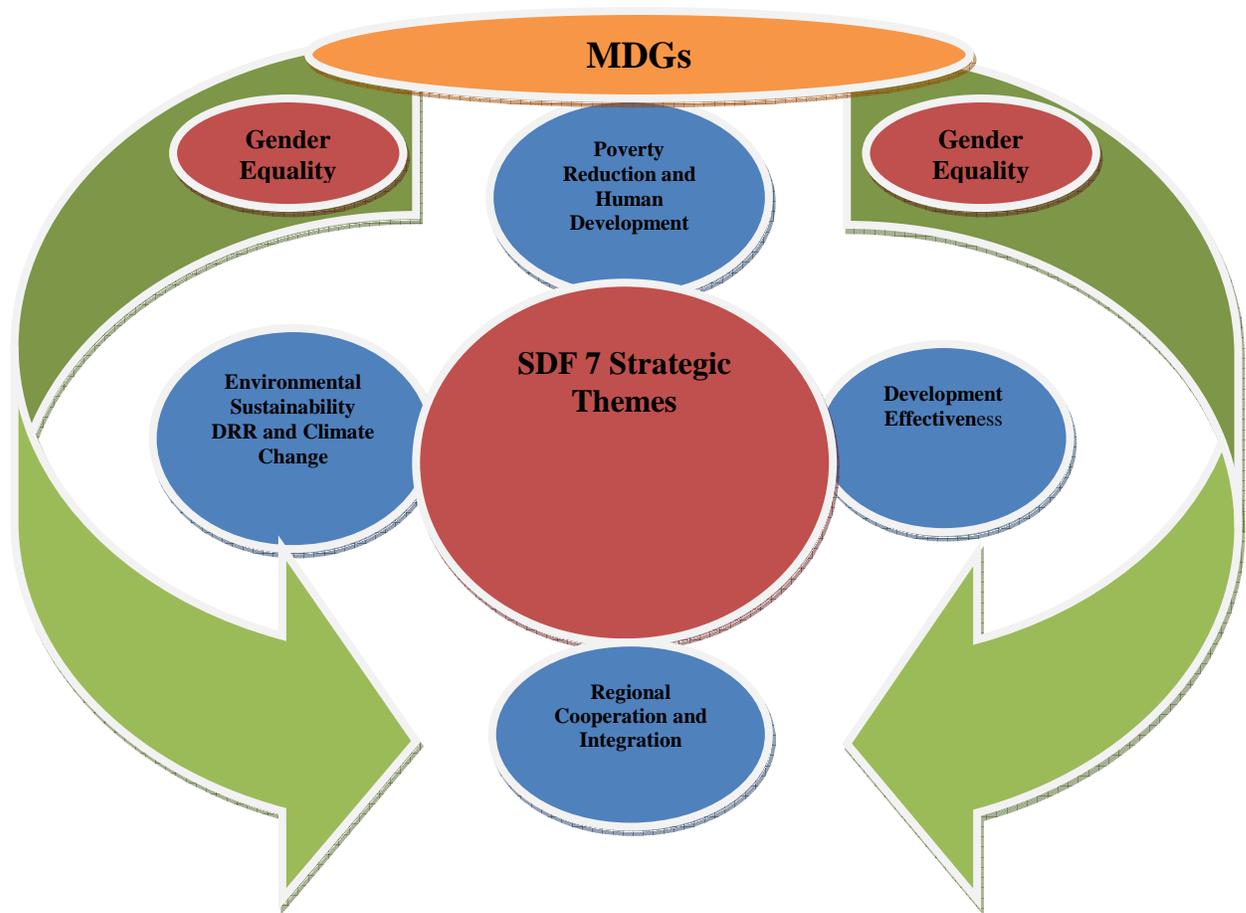
#### **Strategic Themes**

3.02 Contributors have agreed on the following four core themes for the replenishment of SDF 7, with *Gender Equality* as a cross-cutting theme:

- *strengthening poverty reduction and human development*, including the Bank's strategic response to the challenge of providing effective and meaningful assistance to Haiti, and supporting the MDGs and Caribbean-specific MDG targets in the Bank's BMCs;

- **supporting environmental sustainability and advancing the climate change agenda**, including addressing the vulnerability of the Bank’s BMCs to environmental risks and climate change mitigation and adaptation;
- **supporting regional cooperation and regional integration**, including an appropriate operational framework to support priority needs of CARICOM and its members, and the provision of RPGs; and
- **further enhancing development effectiveness**, including MfDR and application of the Paris Declaration on Aid Effectiveness, and including strengthening of the Bank’s human resources and institutional capacity.

**FIGURE 3: STRATEGIC THEMES**



3.03 Separate papers have been prepared for each of the strategic themes. The sections that follow summarise the core elements of the themes to underscore their relevance in the context of the Region’s development options and challenges.

## Poverty Reduction and Human Development

3.04 The reduction of poverty remains the core value pursued by the Bank in all of its BMCs. The strategic levers of the Bank's PRS: *Capability Enhancement, Vulnerability Reduction and Good Governance*, facilitates the effective targeting of the poverty reduction efforts. Within the framework of these strategic levers, it is recognised that "rapid, broad-based economic growth is the single most important factor in sustaining poverty reduction."<sup>5</sup> Appendix 1 outlines the Caribbean-specific MDG targets for the relevant poverty and human development MDG goals (Goals 1, 2 and 3). Addressing issues of poverty, at the national level, will thus continue to require actions on:

- promoting the economic opportunities and productive capabilities of the poor through action affecting the human, physical and natural assets of poor people;
- facilitating the development of the private sector by supporting an enabling environment and contributing to financial sector development;
- dealing with vulnerabilities that affect the poor – or those at risk of becoming poor – resulting from personal risks (e.g. health) or national risks (e.g. economic shocks, natural disasters) by reducing macro risks and establishing/enhancing social protection mechanisms;
- promoting good governance by:
  - improving access to, and delivery of, services that benefit the poor and vulnerable;
  - promoting sound policy and equitable resource allocation i.e. sound macroeconomic management ; and
  - encouraging increased citizen/stakeholder participation in the decision-making processes and in policy, programme and project implementation.

### **BOX 2: HAITI**

Haiti poses additional challenges to CDB. As a fragile state, Haiti has especially difficult development challenges and greater needs. Haiti accounts for almost 60% of the population of BMCs and 70% of Haitians are living below the poverty line. The country exhibits weak institutional capacity and governance such that the capacity of the state to deliver basic social and infrastructure services is seriously undermined. As noted in CDB's operational strategy for Haiti, the Bank's interventions in Haiti will be guided by the country's development priorities outlined in the recently approved Growth and Poverty Reduction Strategy (GPRS), the proposed interventions of other development partners, and CDB's own capacity and areas of strength. Consistent with this approach, the Bank is developing a results-based country assistance strategy which would take account of the development objectives and modalities outlined in Haiti's GPRS. Efforts to support Haiti must continue to involve close collaboration with development partners, increasing field presence and building on lessons learned from successful interventions. The instruments and modalities used by the Bank will need to be flexible and adapted to reflect the realities of the Haitian environment.

<sup>5</sup> Enhancing the fight against poverty in Asia and the Pacific: the PRS of the Asian Development Bank (AsDB), December, 2004.

3.05 Translating these objectives into actual interventions will result in operations in the following areas:

- Economic Growth – especially through increased support for economic and social infrastructure;
- Human Resource Development (HRD) - to increase and broaden equitable access to educational opportunities, improve efficiency and effectiveness of the educational system, strengthen the system’s institutional capacity and enhance technological capacity;
- Agriculture and Rural Development – to remove the constraints to food production and to facilitate sustainable livelihoods in rural areas;
- CPAs and National Poverty Reduction Strategies (NPRSs);
- Direct Poverty Reduction including Social Protection; and
- Civil Society Organisation (CSO) Capacity-Building.

### **Environmental Sustainability and Climate Change**

3.06 The regional economies have made progress with respect to the basic targets and indicators of Goal 7 “Environmental Sustainability” of the MDGs, in areas such as coverage of the population with access to improved water and sanitation and the coverage of areas given protected status. However, these indicators mask deeper concerns related to effective and sustainable management of these resources. In addition, the fundamental inter-linkages between poverty and environmental degradation, which result in the loss of these resources to the poor or the exploitation and unsustainable use by those better off, appears not to be well understood. High rates of soil erosion, degradation of watersheds, and loss of habitats of both precious terrestrial and marine resources are significant environmental and natural resource management issues. Large segments of the rural population still remain dependent for their livelihoods on natural resources and ecosystems, even in the face of their rapidly degrading and diminishing productivity.

3.07 CPAs of nearly all BMCs of CDB consistently show that rural areas usually have the highest incidence of poverty. In many BMCs, issues of land rights and security of tenure still remain obstacles and prevent many of the poor from responding to economic programmes which might offer the possibility of improving their livelihood options. The urban poor live just as precariously as the rural population and are as vulnerable to natural hazards, and external economic shocks. They are also just as likely to contribute significantly to pollution and environmental degradation and stress ecosystems because of limited or no access to basic infrastructure, service utilities (water, sanitation, electricity, fuel) and are often unemployed or underemployed.

3.08 BMCs have been slow to respond effectively to the many environmental challenges facing them. This has been due to a seeming disconnect between environment and natural resource management concerns and wider development policies and programmes. They have been unable to adapt administrative and legislative frameworks to reflect changing needs and priorities. Fiscal constraints and overall limited financial resources have severely impacted capacity of environmental institutions. They remain understaffed and limited in terms of the depth of technical expertise and experience. Very few countries have even rudimentary technical support systems such as databases with natural resource inventories, environmental monitoring reporting systems and laboratories.

3.09 BMCs cannot easily achieve environmental sustainability without addressing fundamental issues of poverty, and the adoption of an approach to environmental and natural resources management, which

encourages the participation and inclusion of all stakeholder groups. This is an approach that is in keeping with the CDB's mandate of poverty reduction.

3.10 It is proposed that the focus of the Bank's operational strategy on environmental sustainability and climate change during SDF 7 should be to assist BMCs to design and implement interventions that promote environmental sustainability in areas that:

- (a) widen the options for sustaining the livelihoods of the poor and vulnerable through improved protection and sustainable management of natural resources;
- (b) improve coverage of the population with access to improved water and sanitation services to reduce pollution and improve the health and productivity of the poor;
- (c) reduce BMCs' vulnerability to natural hazards and improve resilience and adaptation to climate change; and
- (d) strengthen the capacities of regional and national institutions' capacity for improved environmental and natural resource management.

3.11 Given resource limitations, however, the areas for CDB interventions will need to be carefully selected using the following criteria:

- (a) provide opportunities for significant beneficial impacts for the poor and vulnerable;
- (b) contribute to BMCs-stated BMC environment priorities;
- (c) offer opportunity to significantly improve environmental benefits and natural resource management in areas where CDB has experience, credibility and comparative advantage; and
- (d) offer potential for synergies with other CDB areas of the Bank's operations and those of other development partners.

3.12 CDB interventions should, therefore, target protected areas management; improved water, sanitation and solid waste management systems; disaster risk reduction; and the climate change agenda. In relation to the latter area, particular attention should be focused on climate change mitigation and adaptation measures. Mitigation will require additional support for policy, regulatory and governance mechanisms so that renewable energy sources and energy efficiency measures can be fully exploited. Assistance will be provided to BMCs to integrate climate change adaptation measures into their agendas for sustainable development and poverty reduction as well as for sectoral policies. The most vulnerable group likely to be impacted by climate change are the poor, thus targeted measures that help to build community resilience to climate change will be implemented, together with BNTF and other programmes. Support will be provided to regional institutions to strengthen and advance the Caribbean knowledge base about climate change and to monitor adaptation measures. BMCs will also be assisted in accessing innovative climate change funding mechanisms. Appendix 3 outlines the proposed SDF 7 contribution to MDG outcome targets for Environmental Sustainability (MDG Goal 7).

## **Regional Cooperation and Integration**

3.13 While CDB's interventions in its BMCs will, of necessity, involve project implementation at the national level, the overall context of intervention will increasingly be regional in design and conceptualisation. This is in keeping with the decisions of BMC governments to achieve economic and social development through a process of intensification of economic integration and functional cooperation. The approach on the part of regional governments has its genesis in the widespread acceptance that, individually, most if not all of the BMCs do not have the capacity to provide for their populations the range of services that are currently demanded of a modern state. Further, the small size of each country and its resource endowments limit the capacity to provide exportable output at globally competitive prices with the flexibility required of constant changes in product demand and the need for continuous improvement in living standards.

3.14 CDB recognises that its BMCs have entered a critical phase of the integration process, one that will determine not only how well the objectives set out in the Preamble to the Revised Treaty of Chaguaramas are achieved, but whether the centripetal forces are strong enough, with coordinated development partner support, to overcome the genuine fears that accompany the eventual subsuming of the individual sovereignty of small states into a larger, more flexible and responsive entity, better able to cope with the demands of a new global reality. In SDF 7, CDB will continue to focus its project interventions in developing common structures and processes in its borrowing members, based on best practices. This approach will facilitate coordination and mutual support among officials and stakeholders in BMCs themselves, both generally, and in specific areas of activity and operations. Support for RPGs initiatives will be an important element in the Bank's support for regional cooperation and integration.

## **Gender Equality as a Cross-Cutting Issue**

3.15 Improving gender equality stands on its own merits as a development objective. The primary rationale for addressing gender equality in CDB's programming is the strong link between gender inequality and poverty in the region, in both rural and urban contexts. To effectively address poverty, the Bank will continue to utilise strategic entry points for integrating gender issues into existing Bank processes. At the same time, it proposes to be more systematic in the way the effort to achieve gender equality is mainstreamed. Further, in order to strengthen the performance of the Bank in its policy dialogue with BMC officials on economic management, and to assist the Bank in being more efficient in the use of its investment resources in a development context, it needs a framework to improve analytic and sector work. It also needs a methodology for designing loans and grants that exhibits a greater responsiveness to the priority development needs related to gender equality issues of BMCs and the region.

3.16 The Bank is, therefore, in the process of developing a gender policy and the related implementation framework. This will be based on CDB's mandate, strategic objectives and the three strategic levers of the poverty reduction and governance strategies. The Policy will incorporate a results-based approach and will establish links between overall policy and programming priorities and gender equality. The Policy will be able to respond to BMCs priority needs related to gender and development

3.17 The core issues that will be incorporated include:

- (a) analysis of the economic and social dimensions of gender issues and efforts to address the issues integrated into all CDB policies, programmes and projects. In this sense, all CDBs' interventions should contribute to gender equality;
- (b) integrating approaches to address undesirable current gender-related outcomes into all policies, programmes and practices of BMCs. In the medium to long term, such

integration will support sustainable development, good governance and reduce poverty and vulnerability; and

- (c) developing approaches to gender equality through the creation of partnerships between women and men, thereby supporting both women's empowerment and men's inclusion.

3.18 The development of the gender policy will be consultative in nature and will draw on the experiences of other MDBs such as the African Development Bank and AsDB as well as regional and international development agencies. This is to ensure, not only the quality of the policy but to dialogue on issues of implementation such as human resource and skills development and to establish effective gender management systems for accountability and oversight monitoring. CDB will ensure that gender issues are included in planned Country Strategy Papers (CSPs), CPAs, and in social and economic analyses for the design of project interventions, including gender-related indicators.

3.19 In order to address issues of internal capacity, equipping Bank staff with gender analysis capability will be a starting point. The Bank will also draw on external gender expertise to support loan and sector operations as required. The Bank will also have to commit more resources to complement country processes of producing reliable social and gender statistics and disaggregated data in order to identify gender gaps and inequalities, as well as provide support for BMC gender policy formulation.

3.20 In alignment with CDB's harmonisation processes with a range of development partners, CDB will explore the potential of working with partners and research institutions in collaborative sector work, gender research and in specific areas of programming such as gender budgeting. Donor coordination on gender will continue to ensure consistency of approaches and avoid duplication of effort in working with BMCs and to report on good practice in gender mainstreaming among other MDBs.

## **DEVELOPMENT EFFECTIVENESS**

3.21 Development effectiveness - the extent to which the policies and programmes of developing countries contribute to the achievement of important social and economic development outcomes, and the extent to which external development agencies help to achieve those outcomes - has long been the objective in the development assistance relationship. It is also recognised that addressing development priorities at the country level requires a long-term and holistic vision or strategy, to which a range of different actions can contribute most effectively. Country ownership of that strategy and a country-led partnership with agencies supporting a country's development efforts is critical to successful outcomes.

3.22 As in the case of most developing countries and other development agencies, MfDR and increasing development effectiveness at CDB are a work in progress, and further steps need to be taken in SDF 7. Increasing development effectiveness is a shared objective, with roles and responsibilities for both the Bank and BMCs. There are factors beyond the Bank's control that need to be addressed by the BMCs, as well as other development partners. The Bank's agenda, therefore, addresses those steps that the Bank itself can take, including, where appropriate, supporting BMCs in their MfDR and development effectiveness agendas, and working with other development partners towards increased harmonisation and alignment.

3.23 The MfDR Agenda builds on progress to date and steps are already underway, as well as setting out additional measures. Taken together, the elements of the MfDR agenda, including the incentive structure built into new performance indicators, should make a significant difference over the next four years. The Agenda is formulated in terms of the Bank's work priorities. It responds to key findings in

recent evaluations that have helped to identify weaknesses in current processes and in results orientation.<sup>6</sup> The Agenda has been developed to be capable of implementation with available resources and within the overall demands of CDB's work programme, including that expected to be set for SDF 7.

3.24 The Bank's MfDR agenda will be paralleled by a results monitoring framework, which will be similar to that adopted by other MDBs in recent replenishment discussions, although incremental and adapted to CDB's particular circumstances, operational priorities and capacities. The results framework will be linked to the MDGs, particularly those that are most relevant to the Bank's operational programme, and will include more consistent identification, monitoring and reporting of results at various levels. It will include performance indicators to measure progress in terms of institutional and operational effectiveness. Appendix 3 summarises the proposed results framework.

#### **4. OPERATIONALISING THE STRATEGY**

4.01 The mix of measures adopted to operationalise the strategy is determined by the availability of human and financial resources, the Bank's own capacity, and on the institutional capabilities of the different BMCs. It also depends on the effectiveness of the partnerships that can be built with other development agencies operating in the Region. The Bank's interventions need to become more finely focused so that they are consistent with its capabilities, and this underscores the importance of partnerships. Country-level interventions need to be complemented by regional public action to deal with areas where externalities or public good characteristics at the regional level have a direct or indirect impact on poverty reduction. The approach to different countries may be differentiated depending on country conditions and capabilities. The modalities of CDB's intervention will need to evolve over time as countries develop greater institutional capacity. It is envisaged that the Bank will increasingly rely on local capacity for analysis and will adapt its modalities to reflect these changes.

##### **Results Framework**

4.02 The overall results framework, outlined in Section 3, is the focus for operationalisation of the SDF 7 Strategy. With regard to **country and regional level outcomes** it is proposed to track 18 selected indicators under those MDGs and Caribbean-specific targets that are likely to be most significant for SDF 7 operations and CDB's overall strategic goals. All of the indicators, except for one additional indicator related to regional integration, are included in the CMDG framework, with some adjustments recently proposed by Caribbean statisticians. Tracking the indicators should, therefore, help to reinforce the use of the same indicators by BMCs and avoid the need for additional work in an area that already presents a number of capacity challenges.

4.03 Another set of indicators will track progress on practical steps to strengthen **operational effectiveness** as well as on the operational response to key themes and priorities for SDF 7. The number of indicators is deliberately kept small, to provide a clear focus on strengthening incentives and systems for a limited number of measures that will drive operational improvements and results. The list, therefore, is not exhaustive, as complementary improvements will be undertaken as appropriate and necessary. The measures selected are those that are most likely to make a significant difference over the next four years. As already noted, it is expected that each year's annual results framework report will also include qualitative reporting similar to some of the non-quantitative indicators in the COMPAS reporting of the larger MDBs. Some of the performance indicators will track progress in improving accountability for results and strengthening the opportunities for institutional learning. All of them will highlight important areas for progress during SDF 7.

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<sup>6/</sup> The Multi-Cycle Evaluation of SDF is expected to confirm some of these findings and will be taken into account in further development of the Bank's Results Agenda.

4.04 The third set of indicators relates to the **partnership, harmonisation and alignment** agenda developed in the Paris Declaration on Aid Effectiveness.

4.05 There are a number of areas in which the Bank needs to strengthen its operational monitoring and opportunities for institutional learning. This is an area for continuing review, and the areas for progress identified in the results framework are not an exhaustive list. Improved staffing in the operational divisions, together with the recent strengthening of the divisional structure, will facilitate progress, which should be relatively rapid in the period immediately ahead.

4.06 Further progress needs to be made in ensuring the timely completion of Project Completion Reports (PCRs), which need to include more systematic discussion of project outcomes and lessons learned. Improved staffing will also facilitate an increase in project supervision missions, including, as appropriate and feasible, for TA projects. Timely completion of supervision reports, with attention also to steps that might be taken to strengthen results, and the timely posting of supervision reports on the Bank's Project Portfolio Management System (PPMS), also need to be tracked more systematically.

4.07 Improvements in the user-friendliness and timeliness of PPMS will also receive attention, and together with more timely posting of reporting on results, will improve the effectiveness of PPMS as a management tool.

### **Country Strategies**

4.08 CSPs are at the core of strategy operationalisation. The CSP is prepared every 3-5 years and is developed in close partnership with development partners and stakeholders and reflects full ownership by BMC. It analyses the macroeconomic, sectoral and policy environment and identifies the development challenges facing BMC. This allows the definition and selection of the intervention modality best suited to address the issues based on the country-specific context and national strategies and priorities. The CSP incorporates a results framework which identifies how the outcomes, set within the context of the Caribbean-specific MDGs, will be monitored. By linking each intervention to one or more outcome indicators, the CSP indicates how desired outcomes are met through the country strategy.

4.09 Figure 4 outlines how the SDF 7 Strategy will be operationalised.<sup>7/</sup> Macroeconomic performance and the associated policy environment create the framework for preparation of the results-based country strategy. CPAs and the associated NPRS are critical inputs into the CSP, as are sector and thematic evaluations. The lending and non-lending interventions that are identified during the CSP process are prepared, appraised, approved and implemented. These project/programme cycle activities generate the lessons learned that supply the feedback loop to the results framework, CPAs/NPRS and CSP.

## **INSTRUMENTS AND MODALITIES**

### **Instruments**

4.10 The instruments that will be used to operationalise the strategy are the standard MDB products, but designed with increased flexibility to allow greater responsiveness to the dynamic environment. For CDB, these instruments include:

- **Investment Loans** – either SFR alone or blended with OCR. OCR could involve use of ISF;<sup>8/</sup>

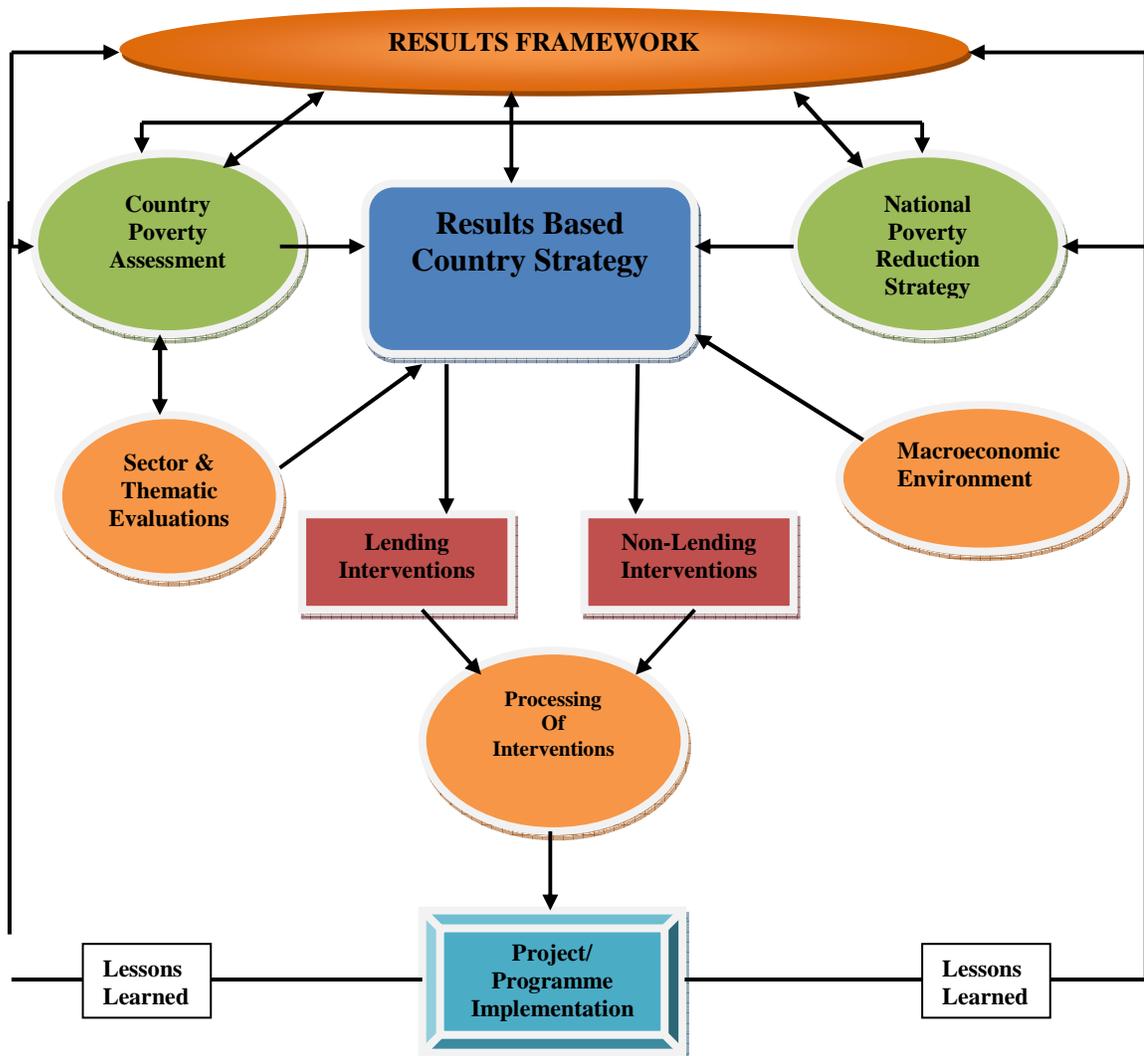
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<sup>7/</sup> Adapted from Figure 1: Operational Cycle in Enhancing the Fight Against Poverty in Asia and the Pacific: The Poverty Reduction Strategy of the AsDB, Page 14.

<sup>8/</sup> The ISF was approved in February 2007 and is used to subsidise the OCR interest rate on PBLs and Investment Loans for projects that focus on poverty reduction, address the MDGs or strengthen development effectiveness; and for specific countries – Belize, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines.

- **TA Loans and Grants** – in the case of TA loans, these could involve SFR, SFR/OCR blend, OCR or OCR/ISF. Grants will be funded from SDF and, when appropriate, specific SFR resources such as the CTCF or the China Fund;
- **PBLs/PBGs** – PBL and PBG are usually part of a broader assistance strategy to improve a country's debt dynamics, enhance public sector management systems, foster fiscal sustainability and improve overall macroeconomic fundamentals. PBLs usually involve SFR/OCR blending. Country eligibility and resource availability would determine use of ISF resources; and
- **Contingently Recoverable Loans** – especially in instances where there is considerable uncertainty regarding the viability of the investment or the ability of the investment to be financed.

**FIGURE 4: OPERATIONALISING THE STRATEGY**



## **Modalities**

4.11 The strategic levers of the Bank's PRS: *Capability Enhancement, Vulnerability Reduction and Good Governance*, can be used to identify the modalities used in operationalisation of the SDF 7 Strategy. The categorisation of modalities under these strategic levers is not rigid because most interventions contribute to more than one area. These are the same modalities used in SDF 4, 5 and/or 6, and are not exhaustive.

4.12 The modalities are as follows:

### **Capability Enhancement**

- Solid Waste Management
- Student loans Scheme
- Technical and Vocational Education
- Tertiary Education
- Natural Resource Management/Ecotourism Development
- Rural Enterprise Development Projects
- Essential Infrastructure and Services
- Rehabilitation/Expansion of Productive Capabilities
- Micro- and Small-Enterprise Development – Especially CTCS

### **Vulnerability Reduction**

- Natural Disaster Response:
  - Immediate Response
  - Rehabilitation
  - Risk Reduction and Management
- Social Investment Funds
- BNTF
- Low-income Housing
- Shelter Development
- Early Childhood Education
- Basic Education

### **Good Governance**

- Institutional Strengthening TA
- Public Sector Reform
- Policy-based Interventions.

4.13 New areas for intervention include climate change mitigation and adaptation, including renewable energy and energy efficiency and SWAPs particularly in education, and agriculture and rural development. Apart from allowing a holistic approach to sector development, SWAPs are ideal for harmonisation of development partner interventions.

4.14 Apart from these additions, SDF 7 would employ essentially the same modalities as before and this is reflective of the need for the Bank to maintain strategic focus, especially in the areas where it has competitive advantage. In applying these modalities, CDB would emphasise reinforcement of the strategic framework already developed, consolidation of changes already in train and setting more

realistic and achievable targets that allow sufficient time for transformational change. In particular, MfDR is vital to future success in addressing most of the deficiencies described and will be strengthened and deepened as a central process in all future interventions. Towards this end, more effort and resources would be invested in a strategic and systematic way to develop the policies, institutions, human resources, information systems and tools required to design and manage projects for development results and to sustain project benefits. CDB is already making interventions in this direction. These interventions would be designed to be more strategic, integrated and systematic. SDF 7 would support a comprehensive strategy and programme to build vital capacity at the national, sub-regional and regional levels. This would form the core of the TA programme. CDB would also address issues such as inflexibility, human resource limitations and inadequate supervision which make MfDR difficult or impossible. A stronger commitment by BMCs to MfDR and to engage in the transformation processes required is imperative to the success of SDF interventions.

**CONTRIBUTION TO MDG OUTCOMETARGETS FOR POVERTY AND HUMAN DEVELOPMENT (MDG GOALS 1, 2 AND 3)**

TARGET	AREAS FOR CDB INTERVENTION	CDB's CONTRIBUTION TO OUTCOMES
<p><b>Goal 1: <u>Eradicate Extreme Poverty and Hunger</u></b></p> <p><b>Target 1</b> Halve, between 1990 and 2015, the proportion of people who fall below the poverty line.</p> <p><b>Target 2</b> Halve, between 1990 and 2015, the proportion of people who suffer from hunger.</p>	<p>CPAs HRD Agriculture and Rural Development Indigenous Peoples Development Youth Enterprise Development CSOs – Capacity-Building Social Protection NPRS CTCS SLS</p>	<p>The collection and analysis of data will help with tracking changes in poverty levels.</p> <p>TA to assist with the preparation and implementation of specific policies, programmes and projects to address the poverty-related issues.</p> <p>Project financing and TAs to support policies, programmes and projects to improve household income and contribute to livelihood protection through employment creation and enterprise development for rural and urban households including youth and indigenous people.</p> <p>TA to support institutional strengthening and capacity-building of CSOs will enhance their capability to respond to the issues of poverty and deprivation.</p> <p>Improved access to quality primary and secondary education and to resources for tertiary training by young persons from low-income households will improve their life chances and help in breaking the cycle of poverty for the households.</p>
<p><b>Goal 2: <u>Achieve Universal Primary and Secondary Education</u></b></p> <p><b>Target 5</b> Ensure that, by 2015, children everywhere (boys and girls alike) will be able to complete a full course of primary and secondary schooling, up to Grade 12.</p>	<p>HRD Gender Equality NPRS SLS</p>	<p>Project financing and TA to support access to quality primary, secondary and tertiary education for males and females along with support to implementation of gender equality policies should help in reducing the disparities between males and females in the education system.</p> <p>BMCs project financing and TA to enhance access to quality primary and secondary education for boys and girls and will contribute to universal basic education.</p>

TARGET	AREAS FOR CDB INTERVENTION	CDB's CONTRIBUTION TO OUTCOMES
<p><b>Goal 3: <u>Promote Gender Equality and Empower Women</u></b></p> <p><b>Target 6</b> Eliminate gender disparity in primary and secondary education, preferably by 2005, and in all</p> <p><b>Target 7</b> Eliminate gender disparity in income and occupational opportunities at all levels and in all sectors, no later than 2015 levels of education</p> <p><b>Target 8</b> Reduce by 60% by 2015, all forms of gender-based violence no later than 2015.</p>	<p>HRD Gender Equality Social Protection NPRS CTCS SLS</p>	<p>Support to the implementation of gender equality policies in BMCs should contribute to the reduction in disparities between project financing and TA to support access to quality primary, secondary and tertiary education for males and females, support to implementation of gender equality policies in BMCs, enhanced opportunities for employment and enterprise development for men and women should together help in reducing the disparities in the labour market.</p> <p>Project financing and TA support to bring about improved educational outcomes and enhanced opportunities for employment and enterprise development for men and women should address the critical factors such as lack of education, low self esteem and inadequate skills in conflict resolution that contribute to gender based violence.</p>

**CONTRIBUTION TO MDG OUTCOME TARGETS FOR ENVIRONMENTAL SUSTAINABILITY (MDG GOAL 7)**

<b>CMDG Targets</b>	<b>AREAS FOR CDB INTERVENTION</b>	<b>CDB's CONTRIBUTION TO OUTCOMES</b>
<p><b>CMDG 7:</b> <b>Ensure Environmental Sustainability</b></p> <p><b>CMDG Target 14:</b> Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources.</p> <p><b>CMDG Target 17:</b> Construct and implement a vulnerability index for the Caribbean within the next five years, which is sensitive to economic, social and environmental threats.</p>	<p><b>Integration of Environmental Sustainability in BMCs Development Programmes</b></p> <p>Institutional strengthening and capacity-building for improved natural resources management at the regional, sub-regional, national levels through improved and strengthened administrative technical systems for disaster risk reduction, environmental management and climate change adaptation.</p> <p>Capacity-building through provision of technical training and awareness building specifically in the OECS.</p>	<p>Further integration of environmental sustainability in CDB's policy work, CSPs, Country Environmental Analysis, CPA and contributions to NPRSs.</p> <p>TA - OECS BMCs for institutional strengthening and capacity-building for improved environmental management.</p> <p>Capacity-building – technical training for environmental and natural resource management, with emphasis on the development of more robust administrative regulatory frameworks.</p> <p>Updating and refinement of CDB's Vulnerability Index.</p>
<p><b>CMDG 7:</b> <b>Ensure Environmental Sustainability</b></p> <p><b>CMDG 14:</b> Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources.</p> <p><b>CMDG Target 15:</b> Halve, by 2015, the proportion of people without sustainable access to safe drinking water and improved sanitation.</p> <p><b>CMDG Target 16:</b> Have achieved by 2020, significant improvements in the lives of at least 70% of persons living in poor communities.</p>	<p><b>Sustainable Land Management and Biodiversity Protection</b></p> <p>Investment projects that widen options for sustainable livelihoods for the poor, through improved management of natural resources and ecological services. Examples include:</p> <ul style="list-style-type: none"> <li>- Establishment and co-management of protected areas including urban revitalisation projects;</li> <li>- Land management – improved agricultural production and watershed management;</li> <li>- Increased interventions under BNTF for discrete environmental beneficial community initiatives; and</li> <li>- Financing investments in water and sanitation infrastructure to widen coverage and reliability.</li> </ul>	<p>Environmental component provided for BMCs under BNTF programme.</p> <p>Investments in water and sewerage projects with emphasis on increasing coverage and reliability for the poor in rural and urban areas.</p> <p>TAs to improve understanding of water resource management issues and strengthen management capacity of resource management institutions, and improved management of national utilities.</p>

<b>CMDG Targets</b>	<b>AREAS FOR CDB INTERVENTION</b>	<b>CDB's CONTRIBUTION TO OUTCOMES</b>
<p><b>Additional Target:</b>  <b>Environmental Protection</b>                      Achieve by 2015, a significant contribution to sustainable land management and biodiversity protection.</p>		
<p><b>CMDG 7:</b>  <b>Ensure Environmental Sustainability</b></p> <p><b>CMDG Target 14:</b>                      Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources.</p> <p><b>Additional Target:</b>  <b>Renewable Energy, Energy Efficiency and Climate Change</b>                      Increase the contribution of alternative sources of energy to at least 10% of the energy mix in BMCs by 2010.</p>	<p><b>Renewable Energy and Energy Efficiency Programme</b></p> <ul style="list-style-type: none"> <li>- Financing viable renewable energy capital projects.</li> <li>- Promoting improved national policies and regulatory framework to facilitate expansion of renewable energy and energy efficiency at the regional and national levels.</li> <li>- Resource mobilisation for innovative financing of climate change initiatives for the Region to finance renewable energy and climate change adaptation issues.</li> </ul>	<p>TAs for capacity-building and strengthening sub-regional or national regulatory framework to promote reduced dependency on fossil fuels.</p> <p>Promotion and financing of viable renewable projects.</p> <p>Mobilise support for renewable energy and climate change adaptation projects for BMCs through the carbon market.</p>
<p><b>CMDG 7:</b>  <b>Ensure Environmental Sustainability</b></p> <p><b>CMDG Target 14:</b>                      Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources.</p> <p><b>Indicators 65, 66, 67</b>                      65: Incidence of natural disasters                      66. Economic losses resulting from natural disasters                      67 Social dislocation resulting from natural disasters</p>	<p><b>Disaster Risk Management (DRM): Contribute to the Caribbean Comprehensive Disaster Management (CDM) Framework</b></p> <ul style="list-style-type: none"> <li>- Regional sustainable development is advanced and the lives of people living in poor communities are improved through disaster risk reduction and mitigation activities within the overall CDM framework.</li> </ul>	<p>Institutional support for CDM programme implementation at national and regional levels (Outcome 1 of CDM) as seen by:</p> <p>DRM policies and strategies formally adopted in all BMCs; regional and sub-regional DRM initiatives implemented with other donor/MDB partners; expansion of scope of Caribbean Catastrophe Risk Insurance Facility to include other hazards, e.g. floods.</p> <p>Capacity-building in BMCs to monitor and assess DRM achievements (Outcome 2 of CDM) as seen by:</p>

<b>CMDG Targets</b>	<b>AREAS FOR CDB INTERVENTION</b>	<b>CDB's CONTRIBUTION TO OUTCOMES</b>
<p><b>CMDG Target 16:</b> Have achieved by 2020, significant improvements in the lives of at least 70% of persons living in poor communities.</p>		<p>CDM database established and maintained; additional DRM monitoring tools developed and adopted in 50% of BMCs; consolidation of ongoing work on Caribbean Building Code and monitoring of implementation.</p> <p>Capacity-building at the national level to integrate DRM and Climate Change Adaptation into economic planning and finance sectors, environmental impact assessment procedures, and business continuity planning (Outcome 3 of CDM) as seen by:</p> <p>DRM integrated into economic planning and finance sectors in 50% of BMCs; DRM (and climate change adaptation) integrated into environmental impact assessment procedures at the national level in 50% of BMCs; business continuity planning strengthened in microfinance institutions in BMCs.</p> <p>Build local capacity in vulnerability reduction and safe building practices in low-income communities, and collaborate with BNTF programme projects (Outcome 4 of CDM) as seen by:</p> <p>Best practices in DRM shared and implemented widely in low-income communities; formal and informal DRM training programmes supported; 10 BNTF projects implemented that include specific DRM measures.</p>
<p><b>CMDG 1: Eradicate extreme poverty and hunger</b> <b>CMDG 4: Reduce child mortality</b> <b>CMDG 5: Improve maternal health</b> <b>CMDG 6: Combat HIV/AIDS, malaria and other diseases</b> <b>CMDG 7: Ensure Environmental Sustainability</b></p>	<p><b>Climate Change Adaptation</b></p> <p>Help society develop ways to live with the degree of global warming that cannot be stopped by integrating climate change adaptation measures into sustainable development and PRSs.</p>	<p>Support for the development of national climate change adaptation policies, strategies and action plans incorporating results based management as seen by:</p> <p>Climate change adaptation policies formally adopted in all BMCs; climate change adaptation plans with specific results adopted in 50% of the BMCs.</p>

<b>CMDG Targets</b>	<b>AREAS FOR CDB INTERVENTION</b>	<b>CDB's CONTRIBUTION TO OUTCOMES</b>
		<p>Support BMCs in the mainstreaming of climate change adaptation measures into sector policies and plans, especially in sectors dealing with economic planning, finance, physical planning, environment and disaster risk management as seen by:</p> <p>Climate change adaptation measures integrated into specific sector policies and plans in 50% of the BMCs.</p> <p>Build local capacity in vulnerable low-income communities, including BNTF projects, to adapt to climate change as seen by:</p> <p>Climate change adaptation incorporated into existing BNTF policies and procedures; 15 BNTF projects implemented that include specific climate change adaptation measures; CTCS expanded to include climate change adaptation, renewable energy and energy efficiency, climate-proofing buildings and projects; support for small-farmer crop insurance.</p> <p>Support regional institutions in monitoring climate change adaptation in the region, and the scientific modelling and forecasting of climate change.</p> <p>Support regional climate change funding mechanisms and collaborate with other MDBs and donor agencies in climate change adaptation as seen by:</p> <p>Establishment of a climate change adaptation database; improved climate change modelling and predictions specific to individual BMCs.</p> <p>Support regional climate change funding mechanisms and collaborate with other MDBs and donor agencies in climate change adaptation.</p>

## SDF 7 RESULTS MONITORING FRAMEWORK

### LEVEL 1: COUNTRY AND REGIONAL OUTCOMES

#### Selected Caribbean-specific Millennium Development Goals and Targets<sup>9/ 10/</sup>

##### Poverty and Human Development CMDGs

1. Proportion of population below the poverty line, by sex.
2. Proportion of population below the indigence line, by sex.
3. Proportion of population below minimum level of dietary energy consumption, by sex.
4. [Proportion of population living in inadequate housing, by sex of head of household.]<sup>11/</sup>
5. Net enrolment ratio in primary education, by sex.
6. Net enrolment ratio in secondary education, by sex.
7. Ratio of girls to boys in primary, secondary and tertiary enrolment.
8. Share of women in wage employment in the non-agricultural sector.
9. Proportion of seats held by women in national parliament.

##### Environmental Sustainability

10. Proportion of land area covered by forest.
11. Energy use (kg. oil equivalent) per \$1 GDP (PPP).
12. Proportion of population with sustainable access to an improved water source.
13. Proportion of population with access to improved sanitation, urban, rural.

##### Global and Regional Partnership for Development

14. Proportion of ODA to basic social services (basic education, primary health care, nutrition, safe water and sanitation).
15. Proportion of ODA for the environment in Caribbean Small Island States.
16. Services as a proportion of total exports of goods and services.
17. Intra-regional trade as a percentage of total regional trade.
18. Debt service as a percentage of exports of goods and services

### LEVEL 2: OPERATIONAL EFFECTIVENESS

##### Project Cycle Management

1. Number of country strategies in place with a results framework.
2. Number of new or updated country poverty assessments for CDB BMCs in the past five years<sup>12/</sup>
3. Number of national poverty reduction strategies for BMCs developed in the past five years.<sup>13/</sup>
4. Percentage of projects other than technical assistance receiving two or more supervision visits during past two years, by category.
5. Percentage of all projects with one or more supervision report on PPMS.
6. Percentage of completed projects with project completion reports that include reporting on outcomes, in past 2 years.
7. Percentage of projects receiving satisfactory or better ratings with respect to achievement of development objectives.
8. Number of project, country and programme evaluations completed during the past five years

##### Concessional Resource Allocation

9. Percentage of concessional resources allocated according to performance-related criteria, current and previous two SDF cycles.

<sup>9/</sup> MDG 8 has been extended to cover regional partnership, which is important for the Caribbean and CDB/SDF goals.

<sup>10/</sup> Indicators have been worded to reflect recommendations of the meeting of BMC statisticians on Caribbean-specific MDG targets and indicators held at CDB in January 2008 and financed by TA PRN-3357. An additional regional indicator, however, has been included.

<sup>11/</sup> Feasibility of this indicator or a relevant proxy is under consideration. Construction of a housing quality index as such will require further discussion and agreement by Caribbean statisticians.

<sup>12/</sup> Whether supported by CDB or otherwise.

**Operational Programming**

10. Number of BMCs receiving support for MfDR.
11. Number of BMCs receiving support for direct poverty reduction programming.
12. Number of BMCs receiving support for environmental sustainability and climate change.
13. Number of investment projects or TA operations for regional public goods and significant regional initiatives.
14. Number of projects with explicit consideration of gender issues in project design.
15. Number of projects with good governance and capacity development components.

**LEVEL 3: PARTNERSHIP, HARMONIZATION AND ALIGNMENT**

1. Number of BMCs with operational national development strategies, such as a national poverty reduction strategy.
2. Percentage of CDB country strategies with explicit consideration of other agency programming in areas in which CDB/SDF may provide support.
3. Number of capacity development interventions provided through coordinated programmes.
4. Number of project interventions provided through common arrangements or procedures such as programme-based approaches (PBAs), SwAps or joint operations with other agencies.
5. Number of cases of joint or shared analytic work with other agencies, such as joint field missions or joint diagnostic reviews.
6. Percentage of BMCs for which there is an explicit results-based framework at (a) country level or (b) programme or sector level.
7. Number of aid coordination initiatives led by CDB during the past two years.

**CONTEXT AND ISSUES FOR SDF 7: BACKGROUND PAPER ON  
ECONOMIC PERFORMANCE AND PROSPECTS IN THE CARIBBEAN**

**1. INTRODUCTION**

1.01 Over the last three decades, and particularly during the last decade-and-a-half (1993-2008), the Caribbean has had to confront the major challenges of trade liberalisation and globalisation.<sup>13/</sup> This has meant an intensification of international competition resulting from the growing integration of markets stimulated by rapid technological change, a significant reduction in transportation costs internationally, and new directions in national and international policy focused essentially on the freeing up of markets.

1.02 For the Caribbean, trade liberalisation has had among its consequences the diminution of preferences for major exports such as bananas and sugar, on which the Caribbean has depended for decades, as the European Union (EU) moved towards the development of its Single Market in the early nineties. Likewise, on the import side, the liberalisation of trade has led to the contraction or elimination of uncompetitive domestic and regional industries geared largely to the domestic and regional markets. The overall result has been a slowing of economic growth, and the persistence of high unemployment and poverty.<sup>14/</sup> In fact, the average real Gross Domestic Product (GDP) growth for the Caribbean was 2.8% during 1990 to 2005 compared to growth of 3.5% for all small states [states with a population equal to or less than 1.5 million (mn)] and 4.2% for all developing countries.<sup>15/</sup>

1.03 While freer trade offers greater international access to markets far and wide, thus being a conduit for economic growth and development, financial resource and other constraints (narrow resource base, limited skills development, limited institutional capacity in both the public and private sectors, etc.) have made it very difficult to effect the transition to new competitive industries. Without considerable external assistance, the adjustment period for Caribbean economies can be long and difficult. Navigating the adjustment process remains one of the Region's enduring challenges. For many countries, the limited availability of financial resources on appropriate terms has been a major constraint on beneficial participation in the new world trading order, creating indecision and delays in the adjustment process.

1.04 While it is true that the Caribbean has been a significant beneficiary of Foreign Development Investments (FDI) and donor inflows, the fact is that the distribution in both cases has been skewed in favour of a few countries. Between 1997 and 2006, for example, 70% to 80% of net FDI inflows have gone consistently to three countries – Trinidad, Jamaica and The Bahamas.<sup>16/</sup> An analysis of the sectoral distribution of FDI inflows also indicates significant gaps in the agriculture and manufacturing sectors, which have borne the brunt of the trade liberalisation process and are in dire need of resources for economic adjustment and transformation. Indications are that a similarly skewed distribution characterises the inflow of concessional resources.

**2. REGIONAL VULNERABILITIES**

2.01 Small states such as those in the Caribbean bring certain weaknesses to the globalisation process making them highly vulnerable to external shocks. Common weaknesses include a small resource base in terms of both skills and natural resources; limited institutional capability within both the public and

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<sup>13/</sup> The beginning of the current period of globalisation is generally dated from 1980, coincident with the beginning of the administrations of Ronald Reagan (1981-89) and Margaret Thatcher (1979-90).

<sup>14/</sup> For a discussion of the high levels of unemployment in the Region, see the Caribbean Trade and Investment Report, 2005, p.381.

<sup>15/</sup> Commonwealth Secretariat and World Bank (WB) (2006), p.3.

<sup>16/</sup> UNECLAC, Foreign Investment in Latin America and the Caribbean, 2006, p.59.

private sectors; small domestic markets inhibiting the realisation of economies of scale; remoteness (lying outside of established trading routes, making international transportation very costly); proneness to natural disasters; environmental fragility; high export dependence, and particularly dependence on a small number of exports (export concentration) and a limited number of markets (market concentration); high import dependence including, in particular, dependence on imported energy; and limited access to capital markets.<sup>17/</sup> In the Commonwealth Secretariat and WB study in 2000 on vulnerability of states within the Commonwealth,<sup>18/</sup> ten Caribbean countries were categorised as highly vulnerable and three exhibited high to medium vulnerability.<sup>19/</sup>

2.02 The Caribbean Development Bank (CDB) in 2006<sup>20/</sup> updated an earlier CDB study on economic vulnerability.<sup>21/</sup> The 2006 study included an additional variable that captured the “quality of the insertion of nation states into the global economy.”<sup>22/</sup> This variable evaluates the type of exports of goods and services. The study points out that countries exporting goods with low income and/or price elasticity are more vulnerable than those that engage in products that are technologically dynamic and have high price and income elasticities.

**TABLE 1: EVI SCORES AND RANKING**

Country Groups	EVI (SERU, 2006)	Ranking
All Countries	0.50	6
Caribbean	0.62	4
Islands	0.63	3
Landlocked	0.50	6
Large States	0.36	10
Medium States	0.50	6
Micro States	0.68	1
Non-Small States	0.44	9
SIDS	0.64	2
Small States	0.62	4

2.03 In the 2006 study, the Caribbean ranked fourth in terms of economic vulnerability. There was a small marginal reduction in vulnerability of Caribbean countries with the EVI declining to 0.62 in the 2006 study from 0.64 in the 1999 study. The 2006 study reported that the Caribbean had performed somewhat better with respect to vulnerability except for the indicator relating to the number of deaths from natural disasters. The main reason given for the reduced vulnerability was lower freight cost compared with medium-sized states and landlocked countries. The study concluded, nevertheless, that “9 of CDB’s Borrowing Member Countries (BMCs), including Haiti, are among the most vulnerable countries and 12 are among the 36 most vulnerable.”<sup>23/</sup> Table 1 shows the EVI scores and the rankings based on the 2006 study.

2.04 One of the major vulnerabilities of the Caribbean is the exposure to natural disasters, which are frequent and often devastating. They include hurricanes, which are the most common, as well as floods;

<sup>17/</sup> Briguglio, 1995; Crowards, 1999; Downes and Mamimigi, 2001.

<sup>18/</sup> Commonwealth Secretariat and World Bank (2000), p. 22.

<sup>19/</sup> These results for the Caribbean were very similar to those of Briguglio (1995).

<sup>20/</sup> CDB, SERU, 2006.

<sup>21/</sup> Crowards, 1999. This was the study drawn on for the analysis of vulnerability presented to SDF Contributors at the time of the SDF 5 and SDF 6 Replenishments and used in the construction of the formula for the SDF resource allocation system (RAS), which introduced performance-based as well as vulnerability factors for the first time into the allocation of SDF resources.

<sup>22/</sup> SERU, 2006, p.18.

<sup>23/</sup> SERU, 2006, p.22.

landslides; volcanic activity; and earthquakes. As shown in Table 2, which details major natural disasters that impacted the Region between 1998 and 2007,<sup>24/</sup> every BMC has been affected in some way. Several countries have suffered more than one such event during the period. These include Anguilla, Antigua and Barbuda, Dominica, Jamaica, St. Kitts and Nevis, St. Lucia and St. Vincent and the Grenadines. The estimated cost of these events has been USD9,200 mn.

**TABLE 2: NATURAL HAZARDS IMPACTING BMCs, 1988-2007**

Hazard	Year	Magnitude	Estimated Cost	Countries Affected
Hurricane Gilbert	1988	Category 5	USD1.1 bn, 65% of GDP	Jamaica
Hurricane Hugo	1989	Category 5	USD3.6 bn, 200% of GDP for Montserrat	Antigua and Barbuda, St. Kitts and Nevis, Montserrat, British Virgin Islands
Tropical Storm Debby	1994	n.a.	USD79 mn, 18% of GDP	St. Lucia
Hurricanes Iris/ Marilyn/Luis	1995	Iris (cat. 3/4) Marilyn (cat. 1) Luis (cat. 3)	USD700 mn	Anguilla, Antigua and Barbuda, Dominica, Montserrat, St. Kitts and Nevis
Hurricane Georges	1998	Category 3	USD450 mn (not including Dominica)	Antigua and Barbuda, Dominica, St. Kitts and Nevis
Hurricane Floyd	1999	Category 4	n.a.	Bahamas
Hurricane Lenny	1999	Category 4/5	USD274 mn	Anguilla, Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines
Tropical Storm Lili	2002	n.a.	XCD21 mn XCD26 mn	Grenada St. Vincent and the Grenadines
Tropical Storm Earl	2004	n.a.	n.a.	St. Vincent and the Grenadines, Grenada
Hurricanes Charley/ Frances/ Ivan/ Jeanne	2004	Charley/ Frances (cat. 4) Ivan (cat. 5) Jeanne (cat. 4)	USD150 mn	The Bahamas, Cayman Islands, Grenada, Jamaica, St. Lucia, St. Vincent and the Grenadines, Trinidad and Tobago
Hurricane Emily	2005	Category 5	USD75.5 mn	Grenada
Hurricane Dean	2007	Category 5	USD90 mn (initial estimate of damage to infrastructure for Dominica and Belize)	Belize, Dominica, Grenada, Jamaica, St. Lucia, St. Vincent and the Grenadines
<b>OTHER EVENTS</b>				
Volcano	1995 to present	-	1995 negative growth - 7.61%, 1996 negative growth - 20.15%	Montserrat
Landslides	2002	-	USD116 mn	Jamaica
Floods	2005	-	USD2.6 bn	Guyana

Source: Caribbean Disaster Emergency Response Agency (CDERA)

2.05 The estimates include only the cost of damage, and do not include economic output foregone as a result of a natural disaster. The economic effects of a natural disaster can last for several years. In the case of Montserrat, the effects will last for decades, if not centuries. The replacement cost of

<sup>24/</sup> Excluding Haiti.

infrastructure, crops and other assets is very high, and is one of the major economic burdens of these economies, which have had in some cases to replace the same infrastructure several times.

2.06 Given all of the abovementioned weaknesses and vulnerabilities of the Region, integration into the world economy on the basis of international competitiveness is extremely difficult. While some of the vulnerabilities, such as high export and market concentration, can be reduced as a result of trade liberalisation, other vulnerabilities, such as a small resource base or susceptibility to natural disasters, remain. In fact, current predictions with respect to global warming are that the frequency and the intensity of natural disasters are likely to increase. Also, in the globalised economic environment, new vulnerabilities have emerged, particularly the risk of financial crisis/contagion and increased exposure to fiscal instability with greater integration into global financial markets. This is discussed below.

### **3. ECONOMIC GROWTH PERFORMANCE**

3.01 The rate of economic growth is a major factor impacting on the level of poverty. As indicated by the experience of the East Asian tigers (Hong Kong, Singapore, South Korea and Taiwan), together with China, high, relatively stable growth rates over extended periods can reduce poverty levels substantially. These very successful economies have been able to sustain growth rates of between 8% and 10% per annum (p.a.) (even higher in the case of China) for an extended period. For example, Singapore was able to reduce its poverty level from 31% in 1970 to 10% in 1985.<sup>25/</sup> In China, it is estimated that the level of poverty declined from 30.7% in 1978 to 9.1% in 2003.<sup>26/</sup> Between 1990 and 1999, South Korea was able to reduce its poverty level from 39.6% to 13.4%.<sup>27/</sup>

3.02 Real income growth for CDB's BMCs averaged 3% over the period 1990-2007, with considerable variability, as shown in Table 3. The average reached 3.8% during 2002-07, or 3.4% excluding the very strong performance of Trinidad and Tobago of approximately 9%. Table 3 also indicates the difficulties confronted by the Caribbean, particularly during the periods 1992-96 and 1997-2001, when growth averaged 2.2% and 2.9% (2.7% without Trinidad and Tobago). During 1992-96, the Region began to feel the effects of the diminution of European trade preferences. During the 1990s also, several regional economies (Trinidad and Tobago, Guyana and Jamaica) underwent structural adjustment programmes with the international financial institutions, of which an important component was the opening up of these economies to international trade. The second period also includes the impact of 9/11.

3.03 While average growth performance improved gradually during 1990-2007, it can be considered moderate at best and was below the average for all small states for most of the period. For six of the countries in Table 3, growth rates were below 3% for the most recent period (2002-07), and for three of them, it was at 2% or less. It can be argued that perhaps only four countries in recent years have posted growth rates that might have had a significant positive impact on poverty levels. These were Antigua and Barbuda (6.4%), The Bahamas (4.8%), Belize (5%) and Trinidad and Tobago (8.9%). But even in these faster growing economies, with the exception of Trinidad and Tobago, the unemployment rate, which impacts on poverty levels, has remained stubbornly persistent at high levels, and even increased in the case of The Bahamas and Belize.<sup>28/</sup>

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<sup>25/</sup> Quibria (2002), p.9

<sup>26/</sup> "Poverty Statistics in China," Rural Survey Organisation of National Bureau of Statistics, China, 2004

<sup>27/</sup> Poverty Equivalent Growth Rate with Applications to Korea and Thailand, WB, Poverty Net Library

<sup>28/</sup> For a discussion of the high levels of unemployment in the Region, see the Caribbean Trade and Investment Report, 2005, p.381.

**TABLE 3: CARIBBEAN GROWTH RATES, 1990-2007**

	ANT	BAH	BAR	BZ	DOM	GRE	GUY	Haiti	JAM	SKN	St.L.	SVG	T&T	
1990	2.5	1.1	-4.8	10.6	5.3	5.2	-3.0	-0.1	4.2	2.3	23.5	5	1.5	
1991	2.0	-2.7	-2.9	11.6	0.6	2.3	6.0	4.2	4.8	0.4	2.7	0.6	2.7	
1992	0.8	-2.0	-5.0	11.9	2.0	-0.3	7.8	-13.2	2.0	3.3	7.0	7.5	-1.6	
1993	5.4	1.9	1.0	6.2	1.7	-2.6	8.2	-2.4	9.4	6.7	2.6	0.2	-1.4	
1994	6.3	0.3	4.0	0.3	1.4	2.8	8.5	-8.3	1.4	5.1	1.4	-3	3.6	
1995	-4.2	0.3	1.5	0.3	2.0	2.5	5.0	-4.0	2.3	3.7	3.3	1	4	
1996	6.7	4.2	1.8	1.7	2.6	4.1	7.9	4.1	-0.1	6.5	1.4	1.3	3.9	
1997	4.9	3.3	6.4	3.6	1.5	4.6	6.2	2.7	-1.1	6.8	0.6	3.2	2.7	
1998	4.4	3.0	4.1	3.7	5.0	6.5	-1.7	2.2	-0.2	1.1	4.7	5.2	7.8	
1999	4.1	5.9	2.6	8.4	0.7	10.1	3.0	2.7	0.7	5.2	2.9	3	4.4	
2000	3.3	5.0	2.3	12.3	0.7	7.6	-1.4	0.4	0.6	2.8	5.0	2	6.1	
2001	0.4	0.4	-2.6	4.9	-3.8	-4.9	2.2	-1.0	1.4	2.0	-5.5	-0.1	4.1	
2002	2.5	13.5	-0.5	5.1	-4.0	1.6	1.1	-0.3	1.6	0.9	2.4	1.4	7.9	
2003	5.2	5.2	2.0	9.3	2.2	7.1	-1.0	0.4	2.7	0.8	3.0	1.5	13.5	
2004	7.2	1.2	3.7	4.6	6.4	-5.7	3.3	-3.5	1.1	8.8	5.8	9.1	6.5	
2005	5.3	2.6	4.1	3.1	3.4	11.0	-2.2	1.8	1.8	4.1	5.8	2.2	7.9	
2006	12.2	3.4	3.9	5.6	4.6	-2.4	5.1	2.3	2.5	4.0	5.6	6.7	12.2	
2007	6.0	3.1	4.3	2.0	1.6	3.1	5.4	n.a.	1.4	3.5	3.0	6.9	5.5	
<b>Averages:</b>														<b>Overall Average</b>
2002-2007	6.4	4.8	2.9	5.0	2.4	2.5	2.0	0.1	1.9	3.7	4.3	4.6	8.9	<b>3.8</b>
1997-2001	3.4	3.5	2.6	6.6	0.8	4.8	1.7	1.4	0.3	3.6	1.5	2.7	5.0	<b>2.9</b>
1992-1996	3.0	0.9	0.7	4.1	1.9	1.3	7.5	-4.8	3.0	5.1	3.1	1.4	1.7	<b>2.2</b>

Source: CDB

3.04 The growth performance of several regional countries was significantly below the average. For Haiti, the average growth rate for the period 1990-2006 was 0.7%, and during 2002-2007 was 0.1%. In the case of Barbados (whose performance improved significantly towards the middle and end of the period), the average was 1.3%. Average growth for Barbados during 1992-96 was only 0.7%. Other countries registering growth of 2% or less for the period were The Bahamas and Dominica.

3.05 Additionally, as shown in Table 4, the considerable variability of growth performance was highly problematic for most countries. Estimates of the coefficient of variation (the ratio of the standard deviation to the mean) of growth performance for several countries was greater than one, underscoring the vulnerability of regional economies to exogenous shocks. A coefficient of variation of one implies that an economic shock such as a hurricane or an event such as 9/11 can throw an economy temporarily off its trend growth rate and into a recession, depending on the severity of the shock.

3.06 Of course, the coefficient of variation gives no information with respect to the duration of the effects of the shock on economic activity, which may last for several years, such as, for example, the case of Hurricane Ivan in Grenada. Also, the higher the coefficient of variation, the higher the level of economic instability. Thus, while the Caribbean in recent years has averaged approximately 3% growth, this is by no means stable growth. For the period 1990 to 2006, the coefficient of variation was greater than 1 for seven of the 13 countries in Table 4.

3.07 For Haiti, the coefficient was 16.4, with an average growth rate of less than 1%, underscoring the tremendous challenges that Haiti, with a poverty level estimated at 65%, is facing. Given current predictions on the effects of global warming, including an increase in the frequency and intensity of climatic events and the possible flooding of low-lying areas, the Caribbean seems likely to witness even greater variability in economic performance.

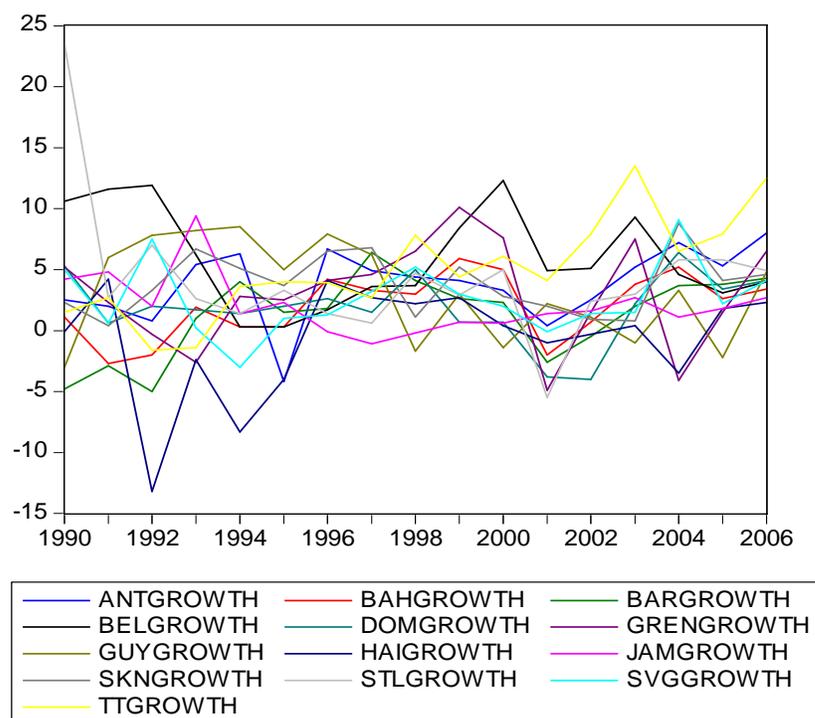
**TABLE 4: AVERAGE GROWTH RATES AND COEFFICIENTS OF VARIATION (CV) 1990-2006**

	Average Growth	CV	Average Growth	CV	Average Growth	CV	Average Growth	CV
	1990-2006	1990-2006	1992-96	1992-96	1997-2001	1997-2001	2002-2006	2002-06
	%		%		%		%	
Antigua and Barbuda	3.8	0.79	3.0	1.55	3.4	0.52	5.6	0.38
Bahamas	2.0	1.31	0.9	2.40	3.0	1.01	3.1	0.52
Barbados	1.3	2.60	0.7	5.10	2.6	1.29	2.7	0.74
Belize	6.0	0.68	4.1	1.23	6.6	0.57	5.2	0.46
Dominica	1.9	1.47	1.9	0.23	0.8	3.82	2.4	1.61
Grenada	3.0	1.41	1.3	2.10	4.8	1.21	2.6	1.80
Guyana	3.2	1.24	7.5	0.19	1.7	1.98	1.2	2.40
Haiti	0.7	6.50	-4.8	-1.36	1.4	1.17	0.1	16.4
Jamaica	2.1	1.14	3.0	1.23	0.3	3.42	2.0	0.35
St. Kitts and Nevis	3.8	0.64	5.1	0.31	3.6	0.66	3.8	0.85
St. Lucia	4.2	1.36	3.1	0.73	1.5	2.79	4.4	0.36
St. Vincent and the Grenadines	2.6	1.13	1.4	2.72	2.7	0.73	3.7	0.88
Trinidad and Tobago	5.1	0.81	1.7	1.72	5.0	0.39	9.7	0.32

Source: WB, *World Development Indicators*, and CDB Estimates

3.08 The substantial vulnerability of Caribbean economies to economic shocks has particular implications for the poor and the vulnerable, and especially the latter, who represent a significant proportion of the population, and who can be and are pushed into poverty because of economic shocks. Meanwhile, the lot of the poor is also made worse. This is a very important characteristic of the poverty landscape in the Caribbean that needs to be understood and considered in the crafting of any poverty reduction strategy for the Region.

**FIGURE 1: CARIBBEAN GROWTH PERFORMANCE, 1990-2006**



#### 4. FISCAL AND DEBT PERFORMANCE

4.01 Another area of macroeconomic performance that impacts on the level of poverty is fiscal and debt performance. Governments can use expenditure policy as a means of reducing income inequalities through transfers. Governments can also use their financial resources to provide housing, health, education and other services to improve the welfare and life chances of the poor and disadvantaged. Furthermore, governments in a strong fiscal position (that is, with overall surpluses and/or small budgetary deficits and relatively low debt ratios) are best placed to help the vulnerable in an economic crisis. For these reasons, a review of the fiscal and debt performance is important in evaluating the policy environment with respect to the poverty reduction capacity of BMC governments.

4.02 A significant number of BMCs are in fiscal and debt difficulties, thereby compromising their ability to address the problems of poverty and vulnerability. During 2002-06, six BMCs averaged fiscal deficits of more than 5% of GDP – Belize, Grenada, Guyana, Jamaica, St. Kitts and Nevis and St. Lucia. By the end of 2007, five BMCs had ratios of public sector debt-to-GDP of more than 100%. These were Antigua and Barbuda, Grenada, Guyana, Jamaica and St. Kitts and Nevis, all facing problems of fiscal and debt sustainability (see Table 5). Others, while not as heavily indebted, are substantially above what has emerged internationally, as the prudential norm, i.e. a public sector debt-to-GDP ratio of no more than 60% of GDP. These are Barbados, Belize, and, to a lesser extent, St. Vincent and the Grenadines.

**TABLE 5: RATIO OF TOTAL PUBLIC DEBT TO GDP (%)**

	ANG	ANT	BAH.	BAR	BZ	BVI	TCI	DOM	GRE	GUY	JAM	SKN	St L	SVG	T&T
2001	17.0	137.7	46.6	72.3	51.9	4.3	9.7	100.1	77.1	209.1	130.3	132.3	47.2	71.2	37.0
2002	20.2	137.7	51.3	79.8	62.4	4.4	8.5	115.9	102.6	211.5	137.3	152.3	53.5	72.3	56.8
2003	20.2	138.9	54.6	75.4	81.7	5.2	9.0	112.5	100.5	188.9	140.0	193.6	59.4	75.4	49.9
2004	23.6	158.4	54.0	75.1	100.2	12.9	9.3	94.7	118.2	179.0	140.9	178.8	65.9	79.4	44.6
2005	25.4	123.9	53.9	80.2	98.4	3.8	9.6	99.9	109.7	173.8	135.0	178.3	64.1	84.3	37.6
2006	21.9	109.7	37.3	n.a.	92.1	4.4	8.5	98.5	113.6	125.8	132.4	178.7	65.8	89.2	30.5
2007	21.8	101.4	38.1	90.0	90.2	n.a.	n.a.	95.0	113.2	125.8	128.1	n.a.	68.2	77.0	28.3

Source: CDB

4.03 Table 6, which presents the ratios of debt servicing to recurrent revenue, reflects the considerable burden on the budget in the heavily indebted countries of the Region. In Jamaica, debt servicing, though declining, has been more than 100% of recurrent revenue for almost a decade. In Belize, the ratio of debt service to recurrent revenue breached the 80% mark several times during 2002-07. In St. Kitts and Nevis, the ratio averaged between 40% and 50% during 2002-07. The substantial portions of recurrent revenue dedicated to debt servicing underscore the significant opportunity cost of high debt accumulation in terms of expenditure foregone on education, health, housing, water, sanitation and other services that are critical to empowerment and welfare enhancement of the poor and vulnerable. For example, during 2001 to 2005, recurrent expenditure on health as a percentage of GDP by five of the most indebted countries for which data are readily available (Antigua and Barbuda; Belize; Dominica; Jamaica and St. Kitts and Nevis) averaged 3.3% compared to 4.3% for countries that were not similarly indebted (The Bahamas, Barbados, St. Lucia, St. Vincent and the Grenadines, Trinidad and Tobago). Similarly, during 1997 to 2006, recurrent expenditure on education as a percentage of GDP averaged 4.7% for the first group compared to 5.4% for the second group. Lack of access to quality education by the poor and vulnerable because of high debt servicing can doom large segments of the population to remain in poverty because of the inability to obtain the necessary skills and income for the purchase of basic necessities and for upward economic mobility in a globalised knowledge economy.

**TABLE 6: RATIO OF DEBT SERVICE TO RECURRENT REVENUE**

	Anguil.	Antigua	Baham.	Barbada.	Belize	BVI	T.C.I.	Dominica.	Grenada.	Guyana	Jamaica	SK-N	St L.	SVG	T&T
2001	2.9	14.0	11.6	22.6	42.0	n.a.	7.3	n.a.	17.8	24.2	145.2	39.6	n.a.	17.5	8.2
2002	5.0	43.3	16.2	24.3	80.8	n.a.	8.0	20.4	31.9	18.4	138.9	45.2	n.a.	16.3	28.9
2003	7.9	32.2	37.5	22.4	60.0	n.a.	39.7	22.1	34.7	25.4	131.1	50.3	16.4	14.5	10.0
2004	7.3	41.7	9.9	22.0	81.8	1.6	5.2	20.9	61.4	20.2	140.5	50.2	18.4	16.0	14.9
2005	4.0	111.4	8.0	20.6	82.1	2.0	4.5	15.4	19.5	8.7	128.6	47.8	23.2	19.9	29.9
2006	14.8	40.7	n.a.	n.a.	n.a.	2.5	4.9	15.6	18.8	n.a.	105.3	41.6	25.4	26.6	7.5
2007	4.0	27.5	n.a.	27.7	n.a.	2.8	n.a.	15.5	20.2	n.a.	86.9	39.5	24.6	25.0	9.8

Source: CDB, International Monetary Fund (IMF)

\* External debt service only

4.04 It can be argued that slow growth and the need to restructure regional economies in the context of trade liberalisation forced several governments to take a more proactive role in investment expansion and growth stimulation. During 1992-96 (when the impact of trade liberalisation on the Caribbean accelerated with the establishment of the European Single Market in 1993 and the diminution of trade preferences for major Caribbean exports, mainly sugar and bananas), there was a general slowing of growth rates in the Region (see Table 3).

4.05 At the same time, the limited access to concessional resources, due to resource constraints of multilateral development banks and the reduced willingness of bilateral donors (because of a focus on Africa and Eastern Europe) was replaced by access to international financial markets. There were substantial capital inflows into the Caribbean in the latter half of the 1990s, even as investment was being withdrawn from East Asia in the wake of the financial crisis of 1997/98.<sup>29/</sup> Thus, the Caribbean region in the late 1990s began to participate in what was essentially a rapid acceleration in global financial activity in emerging markets. The increased availability of financial resources through the market, however, exposed new vulnerabilities in the Region.

4.06 The change from concessional to commercial debt, together with an increased debt stock, meant that interest and amortisation payments quickly became onerous. As debt repayments increased, so also did the pressure for increased borrowing. In other words, some countries soon found themselves in a vicious cycle or, more familiarly, in a debt trap. At the end of 2003, 15 Caribbean countries were among the most indebted in the world.<sup>30/</sup> Six countries in the Caribbean region were also the most severely indebted. These were countries with a public sector debt-to-GDP ratio of more than 90%. The countries were Antigua and Barbuda, Belize, Dominica, Grenada, Jamaica and St. Kitts and Nevis.<sup>31/</sup>

4.07 The greater availability of financing facilitated the postponement of fiscal adjustments. Governments were induced by relatively easy access to large loans from the external financial sector, the absence of conditionalities, reduced scrutiny in the use of funds, and the significantly reduced transactions cost in terms of time – “advantages” that were largely absent in bilateral and multilateral lending. At the same time, growth in lending to the Region was also stimulated by increased knowledge of regional economies in financial markets, as they underwent economic reviews and credit ratings by the international credit rating agencies.

<sup>29/</sup> Source of data, WB, World Development Indicators.

<sup>30/</sup> Sahay (2004).

<sup>31/</sup> Also, according to Sahay (2004), the main reason for the rapid debt accumulation during the period 1998-2002 was fiscal policy slippage as evidenced by the rise in the budgetary deficits.

4.08 The ballooning of the debt stock was to some extent facilitated by the inexperience of the newcomers, but also by the lack of appropriate institutional mechanisms and skills to carefully evaluate the terms of loans and provide the necessary checks and balances, given the incentives to borrow. Loans were at times negotiated on terms that were, in retrospect, highly disadvantageous. One key study pointed out that the interest rates paid by the Region during the period 1998-2002 were on the upswing while global interest rates were declining.<sup>32/</sup> This would certainly explain the eagerness to lend to the Region. The highly disadvantageous fiscal and debt outcomes that accompanied this foray into international financial and capital markets underscore the substantial institutional inadequacies with respect to fiscal and debt management, inadequacies that, unless addressed, will continue to limit beneficial participation in those markets and compromise the ability of governments to reduce poverty levels.

## **5. POVERTY, VULNERABILITY AND INCOME DISTRIBUTION**

5.01 Country Poverty Assessments (CPAs), surveys of living conditions and household budgetary surveys conducted in many Caribbean countries between 1998 and 2005 provide the basis for assessing the incidence of indigence, poverty and economic vulnerability in the Region.<sup>33</sup> Looking at the Region as a whole, the results confirm that, despite social gains in all areas of social life, poverty and indigence are very much present in the Caribbean, and have taken new forms and dimensions, such as the growth of urban poverty; new causes of rural poverty; poverty arising from the impact of HIV/AIDS; and the ageing of the population. For example, recent CPAs for Antigua and Barbuda and St. Lucia point to the growing urbanisation of poverty and the consequent swelling of the ranks of the working poor. Also, the removal of preferences for major agricultural exports and the lowering of trade barriers to agriculture imports have led to a substantial decline in output in certain subsectors, leading to the creation of new segments of poverty in the rural sector. Examples of this are the contraction of the banana industry in the Organisation of Eastern Caribbean States (OECS) and of the rice industry in Haiti. Also, the Caribbean has the highest incidence of HIV/AIDS outside of sub-Saharan Africa. It is estimated that in the Caribbean, 250,000 people are currently living with HIV/AIDS.<sup>34/</sup>

5.02 Poverty, inequality and social exclusion remain frustrating features of the economic and social development of the Region. Social exclusion represents a situation of chronic scarcity of access to basic and quality services; to labor and credit markets and adequate physical infrastructure.<sup>35/</sup> The most recent data on indigence, poverty and vulnerability in the Caribbean are provided in Table 7.

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<sup>32/</sup> Sahay (2004).

<sup>33/</sup> The concept of indigence is premised on the notion that every individual must satisfy certain basic nutritional requirements for survival. A basket of goods is selected so as to maximise one's nutritional intake at the lowest possible cost. Households or persons unable to meet the cost of obtaining this basket of goods are categorised as critically poor or indigent. The income line for the vulnerable is 25% above the poverty line, and helps to determine the percentage of the population that is likely to fall into poverty as a result of an economic shock.

<sup>34/</sup> "HIV/AIDS in Latin America and the Caribbean," World Bank Brief, April 2007.

<sup>35/</sup> Melville and Wint (2007).

**TABLE 7 : MAJOR POVERTY INDICATORS**

Country (in descending order of % below poverty line)	Survey Year	Below the Poverty Line		Below the Indigence Line		Poverty Gap	Gini Coefficient %	Vulnerability %
		Population %	Households %	Population %	Households %			
Haiti	1997	65.0 <sup>36/</sup>	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Suriname	2000	63.1 <sup>37/</sup>	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Guyana	1999	43.0	n.a.	28.0	n.a.	n.a.	n.a.	n.a.
Dominica	2002	39.0	29.0	15.0	11.0	10.2	35	45
St. Vincent	1995	38.0	31.0	26.0	20.0	12.6	56	n.a.
Belize	1996	33.0	25.0	13.0	10.0	8.7	51	n.a.
Grenada	1998	32.1	24.0	12.9	11.0	15.3	45	n.a.
Nevis	1999/2000	32.0	16.0	17	n.a.	2.8	37	n.a.
St. Kitts	1999	30.5	16.0	11	4.3	2.5	40	n.a.
St. Lucia	2005	28.8	21.4	1.6	1.2	N/A	42	40.3
Turks & Caicos Isl.	1999	26.0	18.3	3.2	3.0	5.7	37	n.a.
Anguilla	2002	23.0	20.0	2.0	2.0	6.9	31	n.a.
BVI	2002	22.0	16.0	1.0	1.0	4.1	23	n.a.
Tobago	2005	19.0	n.a.	n.a.	n.a.	n.a.	n.a.	3.2
Antigua & Barbuda	2006	18.3	13.4	3.7	3.1	6.3	48	10
Jamaica	2001	18.0	n.a.	n.a.	n.a.	n.a.	38	n.a.
Trinidad	2005	15.4	n.a.	1.2	n.a.	n.a.	43	9.2
Barbados	1996	14.0	9.0	1.0	1.0	2.3	39	n.a.

Sources: CPs conducted by CDB; Jamaica Annual Survey of Living Conditions (SLC); Barbados CPA (IDB); Guyana Living Conditions Survey (United Nations Development Programme); Trinidad and Tobago Household Budget Surveys; Belize SLC; Bahamas SLC.

5.03 As shown in Table 7, while the level of indigence in some countries (Anguilla, Antigua and Barbuda, Barbados, British Virgin Islands, Grenada, St. Lucia, Trinidad and Tobago) is low, in others (Belize, Dominica, Grenada, Guyana, St. Kitts and Nevis, and St. Vincent and the Grenadines), it is very high, ranging from 11% in St. Kitts and Nevis to 26% in St. Vincent and the Grenadines.<sup>38/</sup> As regards the poverty level, Haiti and Suriname (which are not included in Table 8 because of data limitations) are at the high end of the spectrum, with an estimated 65% and 63% respectively of the populations below the poverty line.<sup>39/</sup> Clustered in the 30% to 40% range are Belize, Dominica, Grenada, Guyana, St. Kitts and Nevis, and St. Vincent and the Grenadines. Countries with levels of poverty between 20% and 29% are Anguilla, British Virgin Islands, St. Lucia, Trinidad and Tobago, and the Turks and Caicos Islands. Barbados had a poverty rate of 14% in 1997, and Jamaica a poverty rate of approximately 20% in 2002.

5.04 Progress has been made in lowering poverty levels in some countries. The level of poverty in Jamaica declined from 24% in 1993 to 20% in 2002, and in Guyana from 43% in 1993 to 35% in 1999. In the case of Jamaica, this occurred at a time when official estimates of the average growth rate were approximately 1.5% p.a., suggesting either an underestimate of growth performance and/or the considerable effect of non-growth factors (such as reduction of inflation, impact of targeted poverty reduction initiatives, etc.). In Guyana's case, the reduction in poverty occurred during a period when the growth rate averaged close to 8% p.a. Since then, growth has slowed significantly (see Table 3).

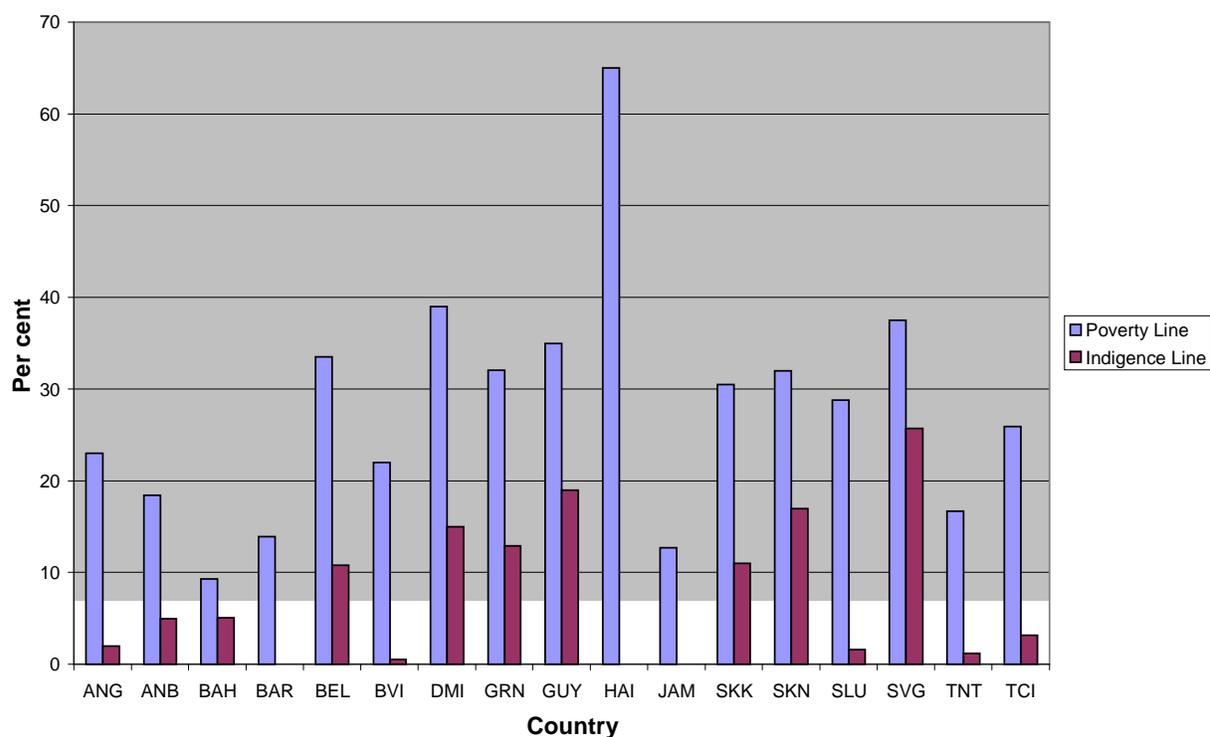
<sup>36/</sup> One more recent estimate is 80% as of 2003.

<sup>37/</sup> One more recent estimate is 70% as of 2003.

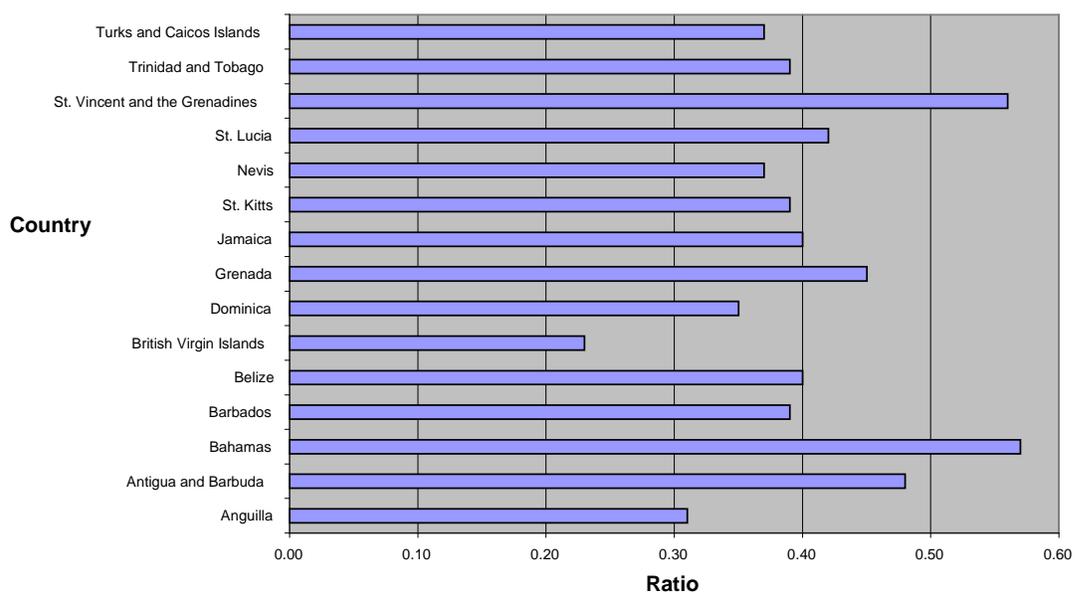
<sup>38/</sup> Probably much higher in Haiti, for which comparable data on indigence levels are not available.

<sup>39/</sup> There have also been higher estimates of 80% and 70%, respectively.

**FIGURE 1: POVERTY INDICATORS FOR SELECTED CARIBBEAN COUNTRIES (1996-2006)**



**FIGURE 2: GINI COEFFICIENT FOR SELECTED CARIBBEAN COUNTRIES**



5.05 In some other countries, poverty levels have deteriorated, largely as a consequence of severe external economic shocks and natural hazard occurrences. In fact, a salient point shown in Table 7 is the very large proportion of the population that is vulnerable in two of the five countries for which data are available. Approximately 40% of the population in St. Lucia and 45% in Dominica are considered

vulnerable, i.e., susceptible to falling into poverty because of an economic shock. If comparable data were available, similar high percentages might be the case for other countries as well.

5.06 On a more positive note, the income distribution in BMCs, while skewed, compares favourably, for example, with that of Latin America. The average of the Gini coefficient for the 16 countries in Table 7 is 38.1%, ranging from 23% for British Virgin Islands to 56% in St. Vincent and the Grenadines. The Latin American average is 50%. Still more needs to be done in a number of BMCs, however, to achieve a better income distribution as a means of reducing poverty.

5.07 Several complex, interrelated factors have contributed to poverty in the Caribbean. These include relatively poor growth performance, strong reliance on output growth of a single crop (such as bananas in the OECS) or of a sector that is in decline, macroeconomic instability, limited job growth, low productivity and low wages in the informal sector, and inadequate access to social services. Other compounding factors contributing to the level of poverty include the economic disparities within countries and communities, the decline in family income as a result of economically debilitating health challenges such as HIV/AIDS, environmental degradation, increased difficulties and uncertainties in the agriculture sector, and weakening of the traditional family as an institution, with consequent economic and social impacts on single-parent households and the elderly. Poverty in the Caribbean also results from the reduced capacity of the Region to address citizens' concerns and ambitions, thereby contributing to the migration and depletion of valuable skills from the workforce.

5.08 Common characteristics among poor households include low-quality housing, inadequate access to basic services, large family size, low levels of education, and limited access to water and adequate sanitation facilities. Issues related to food security are also of concern. Most of the poor in the Region still live in rural areas, although with rising rates of urbanisation and the high vulnerability of the urban poor to economic and social problems, urban poverty has also become a major concern.

5.09 The majority of the employed poor work in the informal sector - in rural areas as small-scale farmers or as agricultural labourers, and in urban areas as wage employees. Small farmers face a difficult period, as preferential access to markets continues to erode, and as barriers to food imports decline. It is extremely difficult for small and vulnerable agricultural economies to benefit from some of the critical gains from increased trade.<sup>40/</sup> Also, the impact of natural disasters and the ensuing devastating effects on the rural poor has been somewhat underestimated. Natural hazards, such as floods, hurricanes, and earthquakes can hit unexpectedly, and infrastructure rebuilding and recovery costs are very high.

5.10 In addition to having low incomes, the rural poor have limited access to quality health and education services, physical infrastructure, and in some cases, farmable land. Urban bias in public funding toward expensive hospital-based medical care and more elite secondary schools has channeled resources away from facilities that provide basic services in rural areas. Frequently, health centers, health posts, and schools in rural areas lack basic inputs such as medical supplies and computers, as well as trained staff.

5.11 Although unemployment rates throughout the Region are high, and thus adversely affect the poor, levels of unemployment are similar among the poor and non-poor. The duration of unemployment is, however, longer for the poor. Low wages in the informal sector, low returns to rural self-employment activities, under-employment, and, in some cases, protracted periods of unemployment, are characteristics of poverty patterns in the Region. Unemployment rates of between 10% and 20%, and even higher, are prevalent in the Caribbean.

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<sup>40/</sup> Ford *et al.*, 2007.

## **6. MEDIUM-TERM PROSPECTS**

### **External Environment**

6.01 As regards the medium term, there are several predictions that one can make with reasonable certainty. The process of trade liberalisation/globalisation will continue, as will its opportunities and challenges. The pace of trade liberalisation may be slowed somewhat as a result of the negative outcomes, or potentially negative outcomes, and resulting political opposition. Examples include the current debate over NAFTA in the United States (US) and the failure of the US, Japan and the EU to open their markets to agriculture exports, thus bringing the World Trade Organisation (WTO) negotiations to a halt. The Free Trade Area of the Americas has also stalled.

6.02 Indications are that the multilateral trade negotiation process is being overtaken by bilateral and regional trade agreements. In the Caribbean, there are special trading arrangements with Cuba, the Dominican Republic and several other Latin American countries through the Association of Caribbean States. Another important event that is expected to impact on the medium-term, though its likely impact is not yet well defined, is the Region's recently concluded Equal Partnership Agreement with the EU (see Box).

6.03 Indications are, also, that the price of oil, because of depreciation of the US dollar, capacity constraints in the industry, continuing political tensions in Middle East and in other major oil producers, and strong growth in demand from India and China, will continue to trend upwards. This is likely to continue to fan inflationary pressures globally, impact negatively on growth performance, and hence also on employment and on the level of indigence and poverty. In the US and other developed countries (Japan, the EU), this scenario is being complicated by the fallout from the sub-prime mortgage crisis, which has induced substantial turbulence and uncertainty in credit markets and compromised the availability of credit. The full effects of the crisis are still emerging, and will help determine whether the world economy in the medium term will witness an economic slowdown (with world economic growth averaging perhaps 4%), or fall into a recession or stagflation, with all of the consequent negative effects.

6.04 Another major medium-term concern will be the continuing rise in food prices as a result of the increase in energy costs and fertilizers, both related to the upward trend in oil prices. Also, production of biofuels using agriculture commodities will continue to place additional pressures on food prices. The increase in the prices of oil and food, on both of which the Caribbean is very dependent, will have a significant impact on the rate of inflation, as recent estimates already indicate. This will impact negatively on the cost of living, potentially pushing vulnerable segments of the population into poverty and poor segments into indigence.

## **THE ECONOMIC PARTNERSHIP AGREEMENT**

On December 16<sup>th</sup>, 2007 the countries of CARIFORUM and the EU concluded negotiations for an Economic Partnership Agreement (EPA) to formalise a trade regime between the two parties. Prior to the EPA, trade was conducted under a temporary regime under the Cotonou Agreement, but this was non-reciprocal in nature, and required a waiver from WTO rules. With the expiration of both the waiver and the temporary trade regime in December 2007, a new arrangement was necessary to provide predictable and preferred access to the EU while removing the threat of WTO litigation. The EPA did this, as trade will now be acceptable under the WTO's rules governing free trade areas.

Some of the more critical aspects of the EPA affect the Region's main agricultural exports (sugar, bananas and rice) which are to be afforded (with different commencement schedules) duty-free-quota-free (DFQF) access to the EU. Additional market access has also been granted for services, with some TA provisions for the important tourism sector. In total, the EU will liberalise 90% of its services sector, while CARIFORUM will liberalise between 65% and 75% of that sector. Other important aspects of the agreement include the elimination of 80% of the duty on EU imports over a period of 15 years, with some goods receiving indefinite protection, while others will have a 25-year transition period; EDF funding of €165 mn; provisions for the movement of natural persons; and provisions for the establishment of firms.

There are several significant implications for Regional economies as a result of the EPA. Firstly, there are fiscal implications, particularly for countries that rely heavily on border taxes as the main source of revenue, which in some instances may be half of tax revenues. These countries will come under increasing pressure over the medium term to implement some form of transactions-based tax to diversify the tax base and cushion some of the shock of revenue losses. Under the EPA, however, there is provision for TA with respect to fiscal reform and institutional capacity-building. On the expenditure side, consideration will need to be given to spending for any economic dislocation arising from the increase in EU imports. The EU is providing additional funding under the EPA, albeit amidst concerns on the part of CARIFORUM countries about the adequacy of such funds.

The impact of the EPA on the agricultural sector is of some concern in the face of increased competition from large producers in the Dominican Republic and also from more efficient producers in the ACP grouping. The EU, however, has committed to providing assistance to increase the sector's competitiveness; developing marketing capacity; the promotion of private investment and private-public partnerships; TA for the development of quality standards and other initiatives to strengthen sector performance. With respect to services, the EPA provides opportunities for substantial liberalisation of the EU market (and also of the CARIFORUM market, albeit to a lesser extent), thereby providing significant opportunities for the development of export services. Additionally, the Agreement provides for the temporary movement of Caribbean professionals in 29 sectors and for temporary entry by independent professionals or self-employed professionals in 11 sectors.

### **Risks and Opportunities**

#### **Risks**

6.05 Given the acute openness of Caribbean economies, they will continue to be vulnerable to terms of trade and other shocks from the external environment. The current international environment with high oil and food prices, unstable financial markets, an economic downturn in major developed countries with the possibility of a recession and even stagflation in the US, a major trading partner, presents significant challenges to the Caribbean. With the expectation of lower export levels for both goods and services, reduced growth and employment in the Region, the impact on the indigent, poor and vulnerable can be severe.

6.06 Another emerging problem for the Region is the upward trend in inflation. Estimates of inflation in the Caribbean during the period 2003 to 2007 indicate that in a significant proportion of countries, the rate of inflation is increasing, driven by imported inflation, essentially from rising oil and food prices, which account for 50% or more of the rise in prices. The consequent erosion in the standard of living is leading towards a tense industrial climate in which unions are pressing for higher wages, sometimes from governments that are already fiscally challenged. In those countries where governments

have taken action to protect their populations from spiraling inflation through the foregoing of tax revenues on imports of food and oil, or have eliminated or reduced certain border taxes, there have been significant fiscal costs in some cases and even policy reversals because of concerns about the sustainability of such action.

6.07 Independently of the impact on inflation, rising food prices are of major concern to the Region given the impact particularly on the poor who must make adjustments in their consumption pattern and nutrition intake. The balance of payments impact is also significant. Regional food imports, including for Suriname and Haiti, amount annually to more than \$2 billion (bn). In 2004, the estimate was \$2.2 bn. Between 1994 and 2004, regional food imports grew in real terms by 2.4% p.a. In some countries, food dependence, defined by the ratio of food imports to consumption in volume terms, is already close to or more than 80% (Antigua and Barbuda, The Bahamas, Barbados, St. Kitts and Nevis, St. Vincent and the Grenadines, and Trinidad and Tobago).<sup>41/</sup>

6.08 Governments in the Region will need to review their agriculture policies in order to provide the necessary food security for the population, and especially for the indigent, poor and vulnerable. This will require expanding food supply, paying particular attention to import substitution possibilities especially as regards high cost imports and to possibilities for efficiency enhancements through technological improvements. It needs to be reiterated that in the Caribbean most of the poor reside in rural areas. Hence, the rise in food prices provides an excellent opportunity to revitalise output growth and incomes in the agriculture sector.

6.09 Increasing raw material demand, related to strong economic growth in East Asia, China and India, however, will continue to benefit regional producers of mining products - Trinidad (oil), Guyana (bauxite) and Jamaica (bauxite and alumina) - as it has in Latin America, where some countries (Chile, Brazil, Venezuela and Peru) have in recent years experienced improved terms of trade and an export boom, trade surpluses, improved current account balances, and an accumulation in reserves. At the same time, however, countries dependent on energy imports will find themselves increasingly vulnerable to oil shocks, forcing the implementation of strong energy conservation initiatives; the development of alternative sources of energy and further oil exploration.

6.10 As indicated in the discussion above on fiscal and debt performance, the Region needs to be more circumspect and strategic in its engagement in financial markets, given the known dangers and imperfections (asymmetric information, currency speculation, herding behaviour, moral hazard, adverse selection, risk of contagion, the potential for excessive borrowing, etc.), and the fact that the benefits expected from such involvement are in many cases not as tangible as hoped for.<sup>42/</sup>

*“If financial integration has a positive effect on growth, there is as yet no clear and robust empirical proof that the effect is quantitatively significant.”*<sup>43/</sup>

6.11 The foregoing statement is significant, coming as it does from the IMF, which is an advocate of financial globalisation. This does not imply a recommendation for cessation of external commercial borrowing, but rather a more circumspect approach, accompanied by significantly enhanced monitoring of the financial sector. The current crisis in the US financial sector as a result of subprime mortgages shows the potential implications of lax vigilance. Also very important, given the excessive commercial borrowing that has taken place in recent years, will be strengthened fiscal and debt management institutional infrastructure to enhance the potential for improved outcomes on both counts.

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<sup>41/</sup> Kendall and Petracco, 2007.

<sup>42/</sup> IMF, 2003.

<sup>43/</sup> IMF (2003), p. 3.

## Opportunities

6.12 While trade liberalisation has presented major challenges to the Caribbean, the Region also needs to be aware of the opportunities that it presents. One notable opportunity is the possibility of increased exports, given the dynamism of the trade environment. During 1990 to 2005, growth in world trade volume (commodities and services) averaged 6.5%, significantly faster than growth in economic activity.<sup>44/</sup> Exceptional growth performance in China, East and South Asia and several other high performers among the less developed countries (e.g. Chile, Cyprus, Mauritius), in recent decades has been significantly rooted in export expansion. Indications are that, while major regional commodity exports have so far been impacted negatively by trade liberalisation, the opportunity exists, with adequate resource inflows and appropriate trade, exchange rate and other economic policies, to benefit substantially from the general “freeing up” of trade.

6.13 The challenge is the identification and exploitation of new and dynamic trading opportunities as they present themselves. This assumes the regional capacity, both in the public and private sectors, to respond effectively to these opportunities. For small island states such as those in the Caribbean, the consensus is that the export opportunities will be mainly in the service sector (tourism, financial services, offshore health care, software development and entertainment etc.), which has shown greater dynamism than merchandise trade.<sup>45/</sup>

6.14 Trade liberalisation also allows a wider array of choices in the trading arena with respect to both products and target markets, thus potentially reducing two of the major vulnerabilities of small states – product and market concentration. Additionally, remoteness and its cost implications, and indeed its implications for the Region’s competitiveness in certain sectors, are being eroded by the significant increase in communications efficiency, which is one of the hallmarks of globalisation. High transport costs of cargo, however, remain a constraining factor for continued reliance on high volume commodity exports, suggesting strongly that the Caribbean, in the context of a more competitive trading environment, has to change its trading strategy towards export services and lighter, higher value-added products.

6.15 Together with increased trade and the resulting potential for enhanced income flows, employment and poverty reduction, new prospects in specific areas or sectors have also emerged. One such area is that of corporate outsourcing. Outsourcing is defined simply as the contracting of an external supplier to carry out a specific task. It is a market that will most likely continue to grow rapidly as international competition intensifies, forcing companies, particularly in the industrialised countries, to constantly seek least cost options. From the Caribbean perspective, an important reason for exploitation of this new market opportunity is the fact that it is an export service industry, helping the Region to escape the constraints of high transport and other infrastructure costs that have compromised the Region’s competitiveness.

### **Caribbean Single Market and Economy (CSME) as a Strategy for the Emerging International Economic Environment**

6.16 In July 1989, the political leaders of the Caribbean Community decided to move the Caribbean economic integration process forward from a common market to a single market and economy. The rationale was that it was the appropriate regional response to the severe economic challenges posed by trade liberalisation and globalisation. The political leadership views CSME as moving the Region towards greater economic competitiveness in response to the new international economic order

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<sup>44/</sup> IMF, World Economic Outlook Database, April 2006.

<sup>45/</sup> Commonwealth Secretariat and World Bank Joint Task Force (2006).

dominated by marketisation and the loss of preferences. In 2006, after a period of 17 years, the single market came into effect, with the steps necessary to establish a single economy as the next stage.<sup>46/</sup>

6.17 Major policy initiatives that are intended, being implemented, or under consideration, include a common trade strategy, a Regional Development Fund (RDF), financial sector integration, integration of the regional labour market, fiscal policy integration, tax harmonisation and monetary integration. The common trade strategy – removal of barriers to regional trade, the implementation of a common external tariff, and unified positions on international trade issues through the Caribbean Regional Negotiating Machinery – has been implemented. The RDF is under implementation and is expected to become operational by July 2008. Integration of the regional labour market, one of the cornerstones of the integration process, has so far been implemented to a limited extent. However, attempts are being made to accelerate the process. Financial integration is under substantive discussion. The foregoing are all part of the first phase of the CSME implementation targeted for the period 2006-2010. The last three initiatives (tax harmonisation, fiscal policy and monetary policy integration) together with the establishment of common sectoral policies are targeted for the second phase during the period 2010-2015.

6.18 Establishment of the CSME is a substantial regional undertaking and its completion would represent a significant accomplishment. However, implementation has been slower than anticipated and hence, so far, there has been a weaker than intended impact in terms of support to the Region in its attempt to confront the challenges of trade liberalisation and globalisation. Currently an attempt is being made to reorient integration initiatives towards an increased emphasis on the production of regional public goods (technological development; enhancement of regional transportation links; human resource development etc.) as a means of strengthening and accelerating the integration process.

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<sup>46/</sup> Members of CSME comprise Antigua and Barbuda, Barbados, Belize, Dominica, Guyana, Grenada, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, and Trinidad and Tobago. The Bahamas and Haiti are members of the Common Market but not of CSME. Montserrat, which is a dependent territory, is awaiting permission from the United Kingdom to join the CSME.

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