DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

DOMINICAN REPUBLIC

IDB COUNTRY STRATEGY
2010-2013

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ELECTRONIC LINKS

ABBREVIATIONS

AECID	Agencia Española de Cooperación Internacional para el Desarrollo [Spanish Agency for International Cooperation and Development]
BCS-DR	Bank's country strategy with the Dominican Republic
CAASD	Corporación de Acueducto y Alcantarillado de Santo Domingo [Santo Domingo Aqueduct and Sewerage Corporation]
CDEEE	Corporación Dominicana de Empresas Eléctricas Estatales [Dominican Corporation of State-owned Electricity Companies]
CI	Contingency instrument
CPAR	Country Procurement Assessment Review
DGII	Dirección General de Impuestos Internos [Internal Revenue Office]
ENCOVI	Encuesta Nacional de Condiciones de Vida [National Survey of Living Conditions]
ENDESA	Encuesta Demográfica y de Salud [Demographic and Health Survey]
GCPS	Gabinete de Coordinación de Políticas Sociales [Social Policy Coordination Cabinet]
GDP	Gross domestic product
IF	Insurance facility
IMF	International Monetary Fund
INAPA	Instituto Nacional de Aguas Potables y Alcantarillados [National Water and Sewer Institute]
IRI	International roughness index
JICA	Japan International Cooperation Agency
MDGs	Millennium development goals
MIF	Multilateral Investment Fund
NFPS	Nonfinancial public sector
NSG	Non-sovereign guaranteed
OECD/DAC	Development Assistance Committee of the Organisation for Economic Co-operation and Development
OFID	OPEC Fund for International Development
OPRET	Oficina de Planificación y Reordenamiento del Transporte [Transportation Planning and Reorganization Office]
OVE	Office of Evaluation and Oversight
PEFA	Public expenditure and financial accountability
PRODEV	Program to Implement the External Pillar of the Medium-term Action Plan for Development Effectiveness
PTMC	Programa de Transferencias Monetarias Condicionadas [Conditional Cash Transfer Program]
R&D	Research and development
RF	Reserve fund
SBA	Stand-by arrangement
SEA	Secretaría de Estado de Agricultura [Ministry of Agriculture]
SECCI	Sustainable Energy and Climate Change Initiative

SECMCA	Secretaría Ejecutiva del Consejo Monetario Centroamericano [Executive Secretariat of the Central American Monetary Council]
SECTUR	Secretaría de Estado de Cultura y Turismo [Ministry of Culture and Tourism]
SEE	Secretaría de Estado de Educación [Ministry of Education]
SEH	Secretaría de Estado de Hacienda [Ministry of Finance]
SEOPC	Secretaría de Estado de Obras Públicas y Comunicaciones [Ministry of Public Works and Communications]
SET	Secretaría de Estado de Trabajo [Ministry of Labor]
SIGEF	Sistema Integrado de Gestión Financiera [Integrated Financial Management System]
SIUBEN	Sistema Único de Beneficiarios [Single System of Beneficiary Selection]
UEPEX	Unidades Ejecutoras de Préstamos Externos [Execution Units of External Loans]
UNDP	United Nations Development Programme
USAID	United States Agency for International Development
WEF	World Economic Forum
WEO	World Economic Outlook
WTO	World Trade Organization

EXECUTIVE SUMMARY

The Dominican Republic has had one of the fastest-growing economies in Latin America in the past 20 years. It has significantly reduced its poverty rates and has a high degree of political and social stability. Still, despite this progress, the Dominican economy faces challenges.

The global economic crisis adversely affected growth in 2009, with significant impacts on the country's fiscal position and external financing. In response, the Government of the Dominican Republic designed and implemented a countercyclical macroeconomic program in late 2009, aimed at restoring growth and returning to a primary fiscal surplus in coming years, which will ensure stabilized debt levels. This program is backed by the International Monetary Fund (IMF) through a stand-by arrangement.

In this setting, actions should be aimed at promoting a recovery of economic growth in a fiscally stable climate in the Dominican Republic. To achieve stability in public finances in the short term, transfers to companies in the electricity sector and nontargeted subsidies must be reduced, and tax revenues must increase. To resolve long-term fiscal problems and create an environment conducive to economic growth, spending—especially on infrastructure—must become more efficient. Infrastructure services must also be improved to raise the country's productivity and support the economic recovery. In view of the competitive weakening of the tourism sector and the decline of the textile maquiladora industry, the productive sectors should be developed, without expanding the use of tax exemptions, in order to promote a recovery of economic growth. Lastly, spending in the social sector must be made more efficient, mainly by targeting transfer programs and making social services more efficient. Not only will this support the accumulation of human capital and avoid potential constraints on long-term growth, but it will also resolve a short-term expenditure problem.

The Bank's country strategy with the Dominican Republic (BCS-DR) for the 2010-2013 period will focus on the following areas: (i) public finances; (ii) social protection; (iii) education; (iv) labor intermediation; (v) electricity; (vi) transportation; (vii) water and sanitation; (viii) agriculture; and (ix) tourism. The BCS-DR will support the objectives of the Dominican government as set in the National Development Strategy for these areas.

The lending framework for <u>sovereign guaranteed</u> approvals in the 2009-2013 period ranges from US$1.445 billion in the base scenario to US$1.9 billion in the high scenario. This framework of approvals, together with the existing portfolio, would allow for resources to be disbursed during the BCS-DR period to meet the objective of covering some 20% of the country's external financing.

The main risk faced by the Dominican economy is that the global economic crisis will continue, which would lead to slower economic growth and could create a gap in the lending program. Under these circumstances, the Bank could enlarge its lending framework in order to partially bridge this gap.

RESULTS MATRIX

Objectives of the National Development Strategy (****)	IDB sectors for intervention	IDB strategic objectives	Projected outcomes of the country strategy	Indicators	Baseline (Source) (*)	Targets (**)
To strengthen the sustainable management of public finances, allocating resources according to National Development Strategy priorities, and more equitably distributing national revenue		To increase tax revenue levels	Increased tax revenues	Income tax revenues as % of GDP	2009: 4.1% (SEH)	2013: 4.6% or greater
				Sales tax revenues on goods and services as % of GDP	2009: 4.3% (SEH)	2013: 4.8% or greater
			Reduced tax exemptions and incentives (tax expenditures)	Tax expenditures as % of GDP	2009: 6% (SEH)	2013: 4%
	A. Public finances	To make public spending more efficient	Reduced transfers to electricity sector	Transfers to electricity sector as % of GDP	2008: 2.7% (SEH)	2013: 0.5% or less
To develop a regulatory environment that ensures a procompetitive investment and business climate			Targeting of electricity subsidy	% of beneficiary families receiving targeted electricity subsidy through SIUBEN-Solidaridad	2009: Electricity = 0% (GCPS)	2013: Electricity = 100%
To develop an effective national system for comprehensive risk management with active community participation			More efficient coordination of institutions for productive development (competitiveness, science and technology, professional development)	Indicator of cluster development (prevalence of well-developed clusters)	2009: 3.5 (WEF) (1 = none; 7 = extensive)	2013: 3.9
				Indicator of industry/academia collaboration on research and development (extent to which businesses and universities are collaborating in R&D)	2009: 3.3 (WEF) (1= no collaboration; 7 = extensive collaboration)	2013: 3.7
			Increased ex ante financial and fiscal coverage of risks of emergencies caused by natural disasters	Total amounts covered by: Reserve fund (RF) Contingency instrument (CI) Insurance facility (IF)	2008: RF: US$95 million CI: US$0 IF: US$0 (SEH)	2013: RF: US$135 million CI: US$100 million IF: US$100 million

To reduce and alleviate extreme poverty through an effective, efficient social protection system	**B. Social protection**	To make the social safety net more effective and efficient	Improved levels of nutrition, health, and education among children in the poorest families	Prevalence of chronic malnutrition among children 0-2 years of age among SIUBEN-1 households	2007: 11.6% (ENDESA 2007)	2013: 10.5%
				Percentage of fully vaccinated children 18-24 months of age in SIUBEN-1 households	2007: 38.2% (ENDESA 2007)	2013: 60%
				Percentage of children 14-16 years of age completing at least 6 years of basic education	2007: 38.9% (ENDESA 2007)	2013: 49%
			Reduce administrative costs of the social safety net	Administrative costs of the Solidaridad program as a percentage of the total Solidaridad budget	2008: 19% (GCPS)	2013: 12%
Objectives of the National Development Strategy	**IDB sectors for intervention**	**IDB strategic objectives**	**Projected outcomes of the country strategy**	**Indicators**	**Baseline (Source) (*)**	**Targets (**)**
To implement a quality education system that teaches continuous learning, promotes human development, and fosters a responsible citizenry	**C. Education**	To improve the quality of basic and secondary education in low-income areas	Reduced overcrowding of school infrastructure in basic and secondary education	Average number of students per section in the 150 most crowded basic and secondary schools out of the universe of schools with 500 students or more	2008: 47.1 basic students 45 secondary students (SEE)	2013: 43 basic students 40 secondary students
			Improved effective promotion rates in basic and secondary education	Effective promotion rates in the first cycle of basic education at schools where interventions occur	2008: 1st: 70%; 2nd: 68%; 3rd: 67% (SEE)	2013: 1st: 73.5%; 2nd: 71.4%; 3rd: 70.3%
				Average effective promotion rates in secondary education at the 150 most crowded schools out of the universe of schools with 500 students or more	2008: 80.1% (SEE)	2013: 84.1%
			Improved learning in reading, writing, and math in 4th grade	Results of national tests on 4th grade reading, writing, and math in schools where interventions occur	2010: to be determined at the start of the intervention (SEE)	2013: positive change in achievement of students in 4th grade reading, writing, and math in schools where interventions occur

To strengthen the Continuing Vocational Training and Development System	**D. Workforce integration**	To improve the positioning in the labor market of young people in low-income areas	Increased probability of finding a job for young people	Percentage of young people trained by the Bank's intervention employed at a rate that is 10% higher than the control group, 6 to 12 months after completing training	2010: to be determined during design of intervention (SET)	2013: to be determined during design of intervention
				Percentage of young people trained by the Bank's intervention who have a job 6 months after completing their training and who work in the field in which they were trained	2010: to be determined during design of intervention (SET)	2013: to be determined during design of intervention
Objectives of the National Development Strategy	**IDB sectors for intervention**	**IDB strategic objectives**	**Projected outcomes of the country strategy**	**Indicators**	**Baseline (Source) (*)**	**Targets (**)**
To ensure a reliable supply of electricity at competitive prices under financially and environmentally sustainable conditions	**E. Energy**	To promote the operational and financial sustainability of the electricity sector	Reduced energy losses and improved collection rates at the three public distribution companies	Percentage of energy losses Percentage of collections out of amounts billed	2009: 28.1% 2009: 94.8% (CDEEE)	2013: 12% 2013: 97.3%
			Strengthened corporate management and internal efficiency at the three public electricity distribution companies	Number of customers per employee at distribution companies (total customers/total employees)	2009: 221 (CDEEE)	2013: 300 or greater
				Electricity sold per employee at distribution companies (billed MWh/total employees)	2009: 1105	2013: 1500 or greater
To expand the coverage and improve the quality and competitiveness of transportation and logistics infrastructure and services	**F. Transportation**	To improve the quality and management of the road system and the urban transportation system in Santo Domingo	Improved systems for reconditioning and maintaining the road system on circuits where interventions occur	Kilometers of highways under a reconditioning and maintenance plan to ensure an average international roughness index of 2.5 or less on circuits where interventions occur	2008: 0 km (SEOPC)	2012: 180-200 km under a rehabilitation and maintenance plan that ensures an average IRI of 2.5 or less on circuits where interventions occur
			Increased number of passengers using the subway as a result of the integration of feeder routes	Percentage of subway passengers using feeder routes, according to OPRET statistics	2009: 0% (OPRET)	2013: 20%

To ensure universal access to clean drinking water and sanitation services	**G. Water and sanitation**	To improve the coverage and management of water and sanitation services in low-income rural and periurban areas	Increased coverage of uninterrupted water service in areas served by INAPA	Percentage coverage of uninterrupted water service users registered by INAPA	2009: 36% (INAPA)	2013: 42%
			Increased coverage of sewer and/or sanitation service in areas served by INAPA	Percentage coverage of users of sewer and/or sanitation services registered by INAPA	2008: 5% (INAPA)	2013: 8%
			Strengthened technical and business capacity of the Santo Domingo Aqueduct and Sewerage Corporation (CAASD)	Percentage of registered customers in CAASD business systems	2009: 60% (CAASD)	2013: 70%
				Percentage of registered CAASD customers with customer metering	2009: 27% (CAASD)	2013: 40 %
				Percentage of water unaccounted for by CAASD	2009: 63% (CAASD)	2013: 50%
			Increased coverage of uninterrupted water service in areas served by CAASD	Percentage coverage of users of CAASD uninterrupted water service	2009: 89% (CAASD)	2013: 91 %
			Increased coverage of sewer service in areas served by CAASD	Percentage coverage of users of CAASD sewer service	2009: 19% (CAASD)	2013: 40%
Objectives of the National Development Strategy	**IDB sectors for intervention**	**IDB strategic objectives**	**Projected outcomes of the country strategy**	**Indicators**	**Baseline (Source) (*)**	**Targets (**)**
To improve the productivity, competitiveness, and environmental and financial sustainability of agricultural productive chains, thereby contributing to food security, jobs, and income for rural residents	**H. Agriculture**	To increase productivity in the agricultural sector	Increased output of production units through incentives for agricultural innovation	Percentage output of participating units of production receiving incentives, compared to control group (*****)	2009: to be determined in design of intervention (SEA)	2013: to be determined in design of intervention
			Reduced rejection rate of exports due to agricultural safety problems	Percentage of rejected exports of fresh produce due to pesticide residues (rejected containers as % of total exported containers)	2008: 1% (SEA)	2013: 0.5% or less

To support competitiveness, diversification, and sustainability in the tourism sector	**I. Tourism**	To support diversification of the tourism sector	Increased capacity of the sector to offer tourism products in the colonial area of Santo Domingo	Percentage of tourist attractions in the colonial area conditioned for tourism with access services, safety, basic services, facilities, signage and interpretation, etc. (tourist attractions where interventions occur/total attractions selected in the colonial area) (***)	2009: to be determined in design of intervention (SECTUR)	2013: to be determined in design of intervention

(*) Numerical indicators are currently monitored by various agencies in the Dominican Republic and are updated on at least an annual basis.

(**) Targets will be revised or replaced, as appropriate, through programming documents to be developed during the country strategy period.

(***) This is a midterm product indicator, since outcomes of these interventions will extend beyond the country strategy period. The specific unit of measurement of the indicator and the different categories of services to be developed are established in the relevant country program document.

(****) The National Development Strategy is a proposal, and therefore a preliminary document in the process of being explained, publicized, and discussed nationally. It is therefore subject to change.

(*****) The specific unit of measurement of the indicator and the different categories of services to be developed are established in the relevant country program document.

I. COUNTRY CONTEXT

1.1 The Dominican Republic's economy has been one of the fastest-growing in Latin America in recent years (6% average growth year-on-year between 1991 and 2008). In the past 20 years, this growth has been based on export activity, such as tourism and light assembly in export processing zones (primarily textile maquiladoras), for which the leading market is the United States economy.[1] The country has also attained a high degree of political and social stability, partly as a result of a reduction in the poverty rate from 43.4% in 2004 to 35.2% in 2008.

1.2 In the past two years, with the onset of the global economic crisis, the Dominican Republic has found itself in difficult economic curcumstances. As a result of reduced flows from abroad, the worldwide crisis caused a downturn in economic growth and a drop in fiscal revenues equivalent to 3.6% of cumulative GDP between 2007 and 2009, which took a significant toll on the fiscal balance. In January 2009, sovereign risk indicators increased significantly to about 1,800 basis points, hindering access to international financial markets. In response, the Dominican government designed a countercyclical macroeconomic program aimed at restoring economic growth and generating the primary fiscal surplus needed to ensure stabilized debt levels. This program began in late 2009 and is supported by the IMF through a stand-by arrangement.

1.3 The state of public finances poses a threat to macroeconomic stability in the short term, due to decreased fiscal revenues and substantial transfers to the electricity sector, while inefficient spending on infrastructure and poor service quality are compromising the ability to restore economic growth and fiscal health over the long term. The country is also exposed to frequent and costly natural disasters, which have a recurring impact on public expenditure and economic growth.

1.4 The country's competitiveness has been adversely affected by the quality of infrastructure. The poor quality and high cost of electricity service has negative impacts on business productivity, living standards, and public expenditure. There are additional weaknesses in road maintenance and in water and sanitation service coverage.

1.5 The economic slowdown since 2007 has revealed the competitive weakening of textile maquiladoras and tourism, which had been the leading growth sectors in recent decades. The textile maquiladora sector is in decline[2] due to the massive influx of Asian competitors to the United States market, while the tourism sector copes with maturation of the "sun and sand" tourism market in the Caribbean region.

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[1] The United States, as the Dominican economy's leading partner for trade and finance, receives about 70% of all Dominican exports; in addition, more than one third of all tourists visiting the Dominican Republic, more than one third of all foreign direct investment, and 70% of all remittances (accounting for 7% of GDP) originate in the United States.

[2] Exports from Dominican textile maquiladoras, as a percentage of all clothing imports to the United States, have steadily decreased (from 6.5% in 1996 to about 1% in 2008).

In addition, the policies used to promote production have come at a high fiscal cost with limited impact.

1.6 Poverty, though reduced in recent years, still affects more than one third of the population, and there is a risk that it will increase in coming years due to the economic slowdown. This will strain the social safety net and require better targeting of public expenditure in this area, as well as more effective social services.

1.7 In the latter half of 2009, the Government of the Dominican Republic developed the proposed National Development Strategy[3] and carried out significant efforts to modernize the electricity sector.[4] These actions are aimed tackling the long-term problems currently facing the country.

II. PRIORITY AREAS FOR THE BANK 2010-2013

2.1 To address these challenges, integrated action should be pursued in several different sectors, with the aim of promoting a recovery of economic growth within a fiscally stable environment.

2.2 To create conditions conducive to an economic recovery, public finances must be strengthened, in both the short term and long term, to make macroeconomic conditions stable and favorable to growth. In the short term, transfers to companies in the electricity sector and untargeted electricity subsidies must be reduced, while tax receipts are increased and tax exemptions decreased.

2.3 To strengthen public finances in the long term, spending must be made more efficient in the energy, transportation, and water and sanitation sectors—with special emphasis on the electricity sector—as well as in efforts to promote productive development. Meanwhile, the quality of services in these sectors must be improved to make the country more productive and to support the economic recovery.

2.4 To promote the economic recovery, and amid the competitive weakening of the tourism sector and the decline of the textile maquiladora sector, support must be provided for development of the productive sectors without expanding the use of tax exemptions. Opportunities have been identified in the agricultural sector and in a diversified tourism sector. The Dominican government also needs support to efficiently design productive development policies and minimize the fiscal impact of development interventions.

2.5 Lastly, to address the impact of the economic slowdown on the most vulnerable sectors of the population, spending in the social sector must be made more efficient and effective, mainly by targeting social transfer programs and enhancing the quality and efficiency of social services. Not only will this support the accumulation of

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[3] The National Development Strategy is a proposal, and therefore a preliminary document in the process of being explained, publicized, and discussed nationally. It is therefore subject to change.

[4] The Dominican government requested that the IDB and the World Bank prepare the Action Plan for Modernizing the Electricity Sector in the Dominican Republic , which is monitored periodically by senior government officials.

human capital and prevent potential constraints on long-term growth, but it will resolve a problem related to efficiency in social spending in the short term.

2.6 The Bank's country strategy with the Dominican Republic (BCS-DR) for the 2010-2013 period will focus on the sectors described below, which were identified in conjunction with the Government of the Dominican Republic. These sectors fall under the development objectives set preliminarily in the National Development Strategy (see Results Matrix and Annex II); they address the aforementioned challenges; and they were selected on the basis of the diagnostic assessments and the Bank's experience.[5] The new BCS-DR will leverage the comparative advantages gained by the Bank in recent years, which will allow for effective positioning in key sectors.[6]

A. Public finance

2.7 Revenue. The tax ratio in the Dominican Republic grew until 2007, when it peaked at 16% of GDP. It is currently at 14% of GDP, slightly below the average for Latin America, which indicates weaknesses in tax policy and in tax and customs administration.[7] Also, the Government of the Dominican Republic must establish a new tax incentive system for export processing zones by 2015, to comply with World Trade Organization agreements. Foregone tax revenue from tax exemptions and tax incentives was an estimated 6% of GDP in 2009.

2.8 The Bank's interventions will be aimed at increasing tax receipts by: (i) strengthening policies and practices for the oversight of the tax administration agency (Internal Revenue Office [DGII]);[8] (ii) providing technical support for tax policy to improve the sales tax and reduce income tax exemptions; (iii) providing technical support to establish a new tax incentive system to replace the system of export processing zones; (iv) reducing tax exemptions and tax incentives; and (v) providing technical support to modernize and professionalize customs administration. Since this area is strictly public in nature, non-sovereign guaranteed (NSG) interventions are not expected to occur.

2.9 The main risk is that of resistance to possible further reforms in tax administration and tax policy. To mitigate this risk, specific interventions will include components for negotiation, communication, and reorganization management, and international best practices will be implemented in policy and tax administration design.

2.10 Expenditure. Public expenditure is characterized by large transfers to companies in the electricity sector, which accounted for about 3% of GDP in 2008, and by the use of untargeted subsidies for electricity. Also, the actions of the various regulatory

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5 The strategic alignment of each area and sector, and the rationale for the Bank's intervention, are described in detail in the Challenges, Alignment, and Strategic Rationale Matrix.

6 The Bank's new interventions will adopt a programmatic approach aimed at providing stability and continuity in support initiatives, with an emphasis on programs rather than projects (see OVE RE-342-1, paragraph 3.63).

7 The rate of sales tax evasion is estimated at 35%.

8 Most of these activities only require administrative actions or tax administration decisions. For technical support, negotiation components will be included to make the proposed reforms viable.

bodies working to encourage production have been largely ineffective and poorly coordinated, and their policies have been weak, especially with the extensive use of tax exemptions. Lastly, a lack of planning in risk management for recurring or catastrophic natural disasters heightens the country's fiscal vulnerability and increases the cost of emergencies caused by natural disasters.[9]

2.11 The Bank's interventions will be aimed at making public spending more efficient by: (i) promoting the reforms needed to reduce transfers to the electricity sector; (ii) targeting the electricity subsidy;[10] (iii) strengthening technical and coordination capacities to improve efficiency and reduce the use of tax incentives among entities working in productive development related to competitiveness, science and technology, and professional development; and (iv) providing technical support to improve fiscal programming over the medium term.[11] The Bank will also support the country in designing and providing ex ante instruments to improve financial and fiscal coverage of risks related to natural disasters. Since this area is strictly public in nature, NSG interventions are not expected to occur.

2.12 The main sector-specific risk is that of potential operational delays in implementing plans for reducing transfers and targeting subsidies, and this may prevent a short-term reduction in spending in this area. To mitigate this risk, the Bank is providing technical support to make rapid progress in designing and implementing these plans.

B. Social protection

2.13 The portfolio of social assistance programs in the Dominican Republic has been historically characterized by diffusion, low degrees of targeting, and a lack of information needed to evaluate their effectiveness. Streamlining these programs has been on the country's reform agenda since 2000, and the Dominican government has made progress, such as by creating the Single System of Beneficiary Selection (SIUBEN) and the Conditional Cash Transfer Program (PTMC, or "Solidaridad"), and by shifting from across-the-board subsidies to targeted transfer programs. Challenges remain, however, in the process of making social spending more efficient, streamlining assistance programs, and locking in the gains achieved thus far. In particular, improvements are needed in the SIUBEN's methodology for selecting beneficiaries;[12] coordination of Solidaridad's operations and policies with the health care and education sectors needs strengthening, to make them more relevant and increase their impact on indicators in those sectors, as well as to reduce administrative costs, which are currently at about 19%; and mechanisms for

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[9] In the past six years, estimated expenditures on natural disasters (storms, flooding, etc.) have ranged from 0.6% to 1.6% of GDP. The largest events of the past 30 years represented 16.1% to 18.4% of GDP.

[10] These targeting activities require only administrative actions within the Dominican government, not legislative changes.

[11] After the high cost of the financial crisis of 2003, analyzing the possible fiscal impacts of the financial sector has become increasingly important. In late 2009, the IMF and the World Bank completed an update of the Financial Sector Assessment Program. The Dominican government is currently working to determine the areas where technical support is needed to follow the recommendations in the report. Once these areas are determined, the IDB will work with the Dominican government to identify the necessary technical support.

[12] An estimated 21% of households classified as poor by the Quality of Life Index are not selected as beneficiaries.

monitoring and evaluating social assistance/protection programs need to be strengthened to improve the accountability process and report on cost-effectiveness, with the aim of making these programs more cost-effective.

2.14 The Bank will focus its interventions on making the social safety net more effective and efficient by: (i) providing support to adjust approaches in transfers and coresponsibilities, in order to more effectively promote behavioral changes in nutrition, health, and education; (ii) increasing operational coordination between the Solidaridad program and the health and education sectors, in order to make the social safety net more efficient; and (iii) strengthening the management mechanisms of Solidaridad by developing a monitoring and evaluation system. NSG interventions are not expected to occur in this sector.

2.15 The main risk is that of delay in operational improvements and interagency coordination, both within the social protection program and with the health and education sectors. Inter- and intraagency coordination are key to enabling Solidaridad to effectively and efficiently promote the accumulation of human capital. To mitigate this risk, the Bank's interventions will promote the creation of coordination mechanisms and the development of management tools, as a way of reducing transaction costs and encouraging sector entities to work together.

C. Education

2.16 The biggest gap in social services lies in the quality of education. Though the country has made progress—with nearly universal coverage at the basic level and high enrollment at the secondary level[13]—repetition rates are high and learning achievement is low. This is partly due to poor teacher quality and classroom overcrowding.

2.17 The Bank's activities will be aimed at improving the quality of primary and secondary education in low-income areas. The Bank's intervention will focus on: (i) improving training and assistance for teachers; (ii) promoting completion of the class schedule and school calendar; and (iii) building and renovating schools. NSG interventions are not expected to occur in this sector.

2.18 The main risk is that the cost of building and renovating schools will increase. To mitigate this risk, specific interventions will budget for such contingencies.

D. Workforce integration

2.19 As a consequence of poor quality in education, young people completing secondary school have a hard time entering the job market, which leads to a slow and costly transition from formal education to employment. This reflects shortcomings in vocational training and labor intermediation, and is evidenced by the higher unemployment rate among country's youngest workers (16.6% for people 20-30 years of age, compared to 10% overall).

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[13] Coverage of basic education was 92.3% and of secondary education was 49.5% in 2008. However, only half of all students are in the grade appropriate to their age.

2.20 The Bank's activities will be aimed at helping young people in low-income areas enter the workforce. They will focus on: (i) redesigning and expanding vocational training programs; and (ii) increasing the number of employment offices and other comprehensive labor intermediation services. NSG interventions are not expected to occur in this sector.

2.21 The main risk is that economy may not grow fast enough to create enough jobs to absorb the beneficiaries of workforce integration programs. This is a macroeconomic risk, and therefore constitutes an overall risk for the country strategy.

E. Energy

2.22 As a result of the high cost and poor reliability of electrical service—with 18% of demand subject to rationing in the form of blackouts—the electricity sector is the primary obstacle to competitiveness. Also, due to the inefficiency of companies in the sector and high levels of technical and business losses (32% of all energy in 2008 went unbilled), combined with a culture of nonpayment and rising oil prices, public resources have had to be transferred in significant amounts to the sector, and this has become a serious problem for public finances. Meanwhile, 86% of all generated electric power is thermal, meaning that the energy sector is highly concentrated in fossil fuels.

2.23 The Bank's activities in this sector will focus on promoting operational and financial sustainability in the electricity sector. The Bank's actions will be aimed at: (i) supporting investments to improve and rehabilitate distribution networks; (ii) strengthening corporate management and internal efficiency at companies in the electricity sector; and (iii) making the public sector more energy-efficient. The Bank's financial support for new investments (sovereign guaranteed or NSG) in generation, transmission, and distribution with public companies will be subject to the progress shown by the Dominican government toward the financial and operational recovery of companies in the sector.[14] To support the diversification of the energy sector, NSG interventions are expected for the generation of wind-powered energy, solar energy, and bioenergy. These interventions will sell electric power to private distribution companies or to public distribution companies after progress is shown in corporate management of the public electricity sector. Meanwhile, NSG operations are expected to occur in fuel storage and transportation, which will also help make the country's fuel supply less costly and more reliable.

2.24 The primary risk is that of delays in modernizing corporate management, which could postpone the Bank's support for new action areas in the sector. The Bank's technical support and the continuous monitoring of the action plan for the electricity sector, in conjunction with the Dominican government and other multilateral institutions, will be aimed at mitigating this risk.

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[14] They will be monitored through operational and financial audits, through the hiring of specialized managers, and through reduced energy losses as described in the Action Plan for Modernizing the Electricity Sector in the Dominican Republic.

F. Transportation

2.25 The condition of the highways has deteriorated as a result of poor maintenance, cutting their lifetime in half, increasing the cost of future road reconditioning efforts, and making it more expensive to transport goods and services.[15] Institutional weakness has translated to a lack of effective planning and a failure to integrate infrastructure works such as the Santo Domingo subway system with other modes of transportation, thus compromising the efficiency of investment spending in the sector.

2.26 The Bank will seek to improve the quality and management of the road system and of urban transportation in Santo Domingo. Interventions will focus on: (i) designing and implementing plans to recondition and maintain the road system; (ii) strengthening management and planning capacity in the transportation sector; and (iii) designing and implementing feeder routes and efficient urban transportation programs in Santo Domingo. NSG interventions are expected to occur in the transportation sector, especially in the form of concessions for highway construction, operation, and maintenance, since the Dominican government will be using this method to a greater extent.

2.27 The main risks lie in budgeting for road maintenance and in the agreements that must be reached with carriers to make progress on feeder roads. Both risks will be mitigated in the course of specific interventions through the Bank's financial support and technical support to develop strategies for negotiating with the carriers.

G. Water and sanitation

2.28 While a low average rate of coverage (only 42.2% of households have running water) and poor quality of water service are nationwide phenomena, the coverage rate in rural and periurban areas, home to about 50% of the country's population, is at critical levels, with barely one third of households covered. Also, management and planning weaknesses in the sector's leading entities (Santo Domingo Aqueduct and Sewerage Corporation [CAASD] and National Water and Sewer Institute [INAPA]) hamper efficiency in public spending in the sector and are an obstacle to investment with the swiftness necessary to improve service quality.

2.29 The Bank's interventions will be aimed at improving the coverage and management of water and sanitation service in rural and low-income areas. The Bank's activities will focus on: (i) supporting investments to expand coverage and improve service quality in low-income rural and periurban areas; and (ii) strengthening the technical and management capacity of INAPA and the CAASD. NSG interventions are expected to occur in the provision of water and sanitation services for tourist areas, in the form of public-private partnerships.

2.30 The primary risk is that strengthening of the CAASD and INAPA may be delayed. To mitigate this risk, specific interventions will include initial components for technical and management strengthening.

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15 Seventy-three percent of the highway system is in fair or poor condition, which translates to a 12% to 18% increase in the cost of transporting goods and services.

H. Agriculture

2.31 The Bank's diagnostic assessment and the actions of the Dominican government show tremendous potential in the agricultural sector. For example, the National Competitiveness Council is actively working with productive clusters raising mangos, Oriental vegetables, avocados, bananas, specialty coffees, pineapples, and other produce. However, it has been noted in the sector that the increase in output is due to an expansion of the area under cultivation, not to improved crop yield, which indicates a productivity problem related to farmers' lack of access to technological innovation. In addition, agricultural exports are frequently rejected on phytosanitary grounds due to poor pesticide management.

2.32 The Bank's interventions will be aimed at making the agricultural sector more productive, with a focus on: (i) implementing direct support for small-scale farmers to encourage the use of new production technologies; and (ii) improving the quality of sanitation services and agrifood safety. Given the opportunities that will open up with the productive clusters, NSG operations are expected to be in the agribusiness sector, to promote the integrated production of local crops, which enjoy a competitive advantage, and to promote the subsequent sale of such crops to local and export markets.[16] NSG operations in this sector will be financed both directly and indirectly through financial intermediaries.

2.33 The main risk in the agricultural sector is related to the impact of the international crisis on demand for agricultural products. If the worldwide crisis deepens, the expected outcomes in terms of output will not be attained despite efforts to prop up supply. This is part of the macroeconomic risk, and affects the BCS-DR as a whole.

I. Tourism

2.34 The average stay has decreased from 10 to 9.2 nights in the past 10 years, and average daily spending per tourist is low, at about US$103. Growth in international arrivals has slowed in the past 10 years, falling from an 11% average annual increase in the late 1990s to just 5% between 2004 and 2007, due to widespread availability of "sun and sand" offerings in the rest of the Caribbean. With the global economic crisis, tourist arrivals stagnated in 2008 and 2009. A coordinated public-private effort to identify and develop sustainable diversification opportunities, on both the environmental and social levels, has been notably lacking. Still, the country has opportunities to diversify its tourism sector by turning to activities with potential such as cultural tourism and ecotourism.

2.35 The Bank's interventions will be aimed at supporting the diversification of tourism. Actions in the sector will focus on: (i) supporting investments in tourism in the colonial area of Santo Domingo; and (ii) carrying out activities to strengthen tourism management, including participation of the municipal government, local business leaders, and civil society. NSG operations are expected to occur in this sector,

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16 NSG support for the agricultural sector will be coordinated with complementary interventions of the Inter-American Investment Corporation and the Multilateral Investment Fund, targeting small and medium-sized enterprises.

specifically in sustainable tourism, through initiatives to support tourism development and in regions where this sector is still under development.[17] NSG operations in this sector will be financed both directly and indirectly through financial intermediaries.

2.36 The main risk in the tourism sector is related to the impact of the international crisis on tourism-related demand. If the crisis continues, the expected outcomes in terms of diversification will not be attained despite efforts to prop up supply. This is part of the macroeconomic risk and affects the BCS-DR as a whole.

III. LENDING FRAMEWORK[18]

3.1 To cope with the economic slowdown of 2009, the Government of the Dominican Republic began implementation of a fiscal stimulus policy aimed at achieving a 3.5% growth rate in 2010, and a 6% growth rate from 2011 onward. While the nonfinancial public sector posted a deficit equivalent to 3.1% of GDP in 2009, this deficit is projected to decrease to 2.5% in 2010, and by one percentage point of GDP starting in 2011. The medium-term gross financing requirement (fiscal deficit plus amortizations) for the country's NFPS will be on the order of US$8.987 billion for the 2010-2013 period. Of that amount, US$6.983 billion is expected to come from external resources, and US$2.005 billion from internal sources (see Annex III).

3.2 The lending framework for Bank sovereign guaranteed approvals for the 2010-2013 period ranges from US$1.445 billion for the base scenario to US$1.9 billion for the high scenario (see Annex IV). This framework of approvals, together with the existing portfolio, would allow for resources to be disbursed that would maintain the IDB's share of the country's external financing at 20%, similar to historical levels. The Bank's share of the multilateral debt would decrease under both scenarios from a historical average of 73% to an average of 56% for the BCS-DR period. Meanwhile, the multilateral debt would increase as a percentage of external debt from a historical average of 29% to an average of 36% under the BCS-DR. These debt levels, along with the Bank's status as a preferred creditor, mean that the credit risk is manageable under any lending scenario (see Annex IV). In operational terms, the lending framework of the BCS-DR will pose new challenges for the project delivery capacity of the Government of the Dominican Republic and of the Bank itself. To meet these challenges, the Bank and government will work together to support strengthening of the financial management and procurement functions of the executing agencies, as described in paragraph 4.1 and Annex IX.

3.3 The transition from the base scenario to the high scenario for loans will depend on: (i) progress in reforming corporate management in the electricity sector (see

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[17] NSG interventions in the tourism sector are expected to be complemented by MIF activities for training and social development in areas where sustainable tourism projects are to be conducted. In addition to the aforementioned sectors in infrastructure, agriculture, and tourism, another possible area of NSG intervention is the development of financial and capital markets. For NSG operations with the financial sector, activities will preferably be aimed at customers working in the energy, tourism, and agricultural sectors.

[18] For more details on the financing framework and medium-term fiscal needs, see Annex III.

paragraph 2.23); and (ii) progress in reaching sector milestones and evaluating the first interventions, which will set the stage to move on to subsequent phases of programs in the public finance, social protection, education, transportation, water and sanitation, and agricultural sectors. Amounts approved for non-sovereign guaranteed interventions are expected to increase in the BCS-DR period, compared to 2009. The BCS-DR calls for knowledge generation and technical cooperation to occur simultaneously with the loan operations program, to ensure consistency with country priorities and the Bank's cycle of operations. Biannual programming for the 2009-2010 period was coordinated with the Dominican government, mobilizing technical-cooperation resources on the order of US$8.7 million. The program will be updated annually, to ensure that interventions are timely and adapted to the Bank's work cycle with the country (see Annex III).

IV. STRATEGY IMPLEMENTATION

A. Country systems

4.1 The diagnostic assessments performed on the financial management systems of the Dominican Republic between 2003 and 2007 noted weaknesses in public financial management systems.[19] The Bank is currently making only partial use of country systems in the operations it is financing (see Annex IX). In recent years, the Dominican government has made progress in reforming public financial management, mainly in developing the SIGEF Integrated Financial Management System and in establishing the legal framework needed to reform financial management. For procurement systems, the Bank is not currently using country systems in the operations it finances, and the diagnostic assessments are not up to date. They need to be updated, and the country must be supported in developing a methodology to plan, develop, and standardize bidding documents, and in evaluating and developing an electronic procurement system. For more details, see Annex IX, which describes the current state of the fiduciary systems, as well as expected actions and outcomes for the BCS-DR period.

4.2 For planning, monitoring, and evaluation, the Bank will continue to support, through PRODEV operations, the strengthening of new systems for planning and programming investments and for managing for results, which began operating in 2007 and are currently in the early stages of implementation. For statistical systems, the Dominican Government will be supported as part of the BCS-DR in the technical and institutional strengthening of the national statistics system and the agency responsible for setting policies and generating statistics.[20] For environmental systems, as part of the Country Environmental Study, the Bank completed an initial evaluation in late 2009 on the state and effectiveness of the legal and institutional framework for national environmental management. This study noted progress in environmental legislation as well as weaknesses in enforcing the legislation and complying with its provisions. It also noted weaknesses in institutional capacity at

[19] See the Technical Note on Fiduciary Strategy and Annex IX.
[20] See the Statistics Action Plan.

sector agencies, and identified priority action areas for strengthening environmental management.[21]

B. Coordination with other donors

4.3 Coordination for public finances sector will be primarily carried out with the World Bank and the International Monetary Fund (IMF); coordination in the electricity sector will occur through confinancing with the World Bank and the OPEC Fund for International Development; and coordination in the water sector will occur through cofinancing with the Spanish Cooperation Fund for Water and Sanitation in Latin America and the Caribbean. For social issues, a significant effort to coordinate and distribute action areas will be carried out with the World Bank and the United Nations Development Programme for the social safety net, education, and health care. Coordination with bilateral entities will be conducted mainly through the Donors Forum, which operates on a permanent basis and includes the various bilateral and multilateral cooperation agencies in Santo Domingo. For more details, see Annex VI, which includes a summary of activities and sectors in which coordination efforts will be conducted.

V. RISKS

5.1 **Macroeconomic and fiscal risks.** The main macroeconomic risk facing the country is that the global economic crisis will continue. In view of the Dominican external sector's vulnerability to the international economic cycle, under a worldwide scenario of slow growth the country's projections for the 2010-2013 period would be overestimated, and a gap would open up in the lending program.[22] Even under these extreme assumptions, the debt would not increase significantly and would be projected to remain at sustainable levels (see Annexes VII and VIII).

5.2 **Natural disaster risk.** The country is exposed to natural disasters, and its degree of vulnerability is high. Historical costs show that a moderate to severe natural disaster can have a significant fiscal impact. To mitigate this risk, the Bank will support the country in designing and implementing a comprehensive plan to manage and mitigate natural disaster risks (see the Challenges, Alignment, and Strategic Rationale Matrix),[23] aimed at reducing and mitigating such risks. Also, interventions aimed at improving financial and fiscal coverage of disasters, as part of the BCS-DR, will seek to reduce the cost of such disasters.

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21 See the Environmental Action Plan.

22 A simulation of this impact found that the financing gap would grow from 0.4% of GDP in 2010 to around 1% of GDP in 2013. This would mean more than US$1.958 billion in additional total financing requirements for the 2010-2013 period. If the Bank covers 20% of this gap, the lending framework could expand by some US$392 million. See Annex VII, Macroeconomic Risk Analysis.

23 This plan must be in effect and progressing, as a condition reviewed annually by the Bank as part of implementation of various financial risk management instruments.

SELECTED ECONOMIC AND SOCIAL INDICATORS

Dominican Republic: Selected macroeconomic and social indicators, 2002-2009 /1

	2002	2003	2004	2005	2006	2007	2008	2009
	Real sector							
Real GDP growth (%)	5.8	-0.3	1.3	9.3	10.7	8.5	5.3	3.0
GDP at current prices (in billions of US$)	35.0	20.4	22.6	33.8	35.9	41.2	45.7	46.7
GDP per capita (US$)	2,918.0	2,344.1	2,548.0	3,739.1	3,903.9	4,404.5	4,797.8	4,815.6
	Monetary variables, prices, and exchange rate							
Consumer prices (%), end of period	10.5	42.7	28.7	7.4	5.0	8.9	4.5	5.8
Monetary base (% annual variation)	1.2	114.9	12.9	22.6	9.8	13.7	9.7	3.2
Exchange rate (DR$/US$), annual average	20.8	37	31	35	33.7	33.3	34.6	35.9
Average effective real exchange rate (index) /2	102.0	130.9	126.5	90.7	95.8	92.7	90.7	92.9
	External sector							
Current account balance (% of GDP)	-3.8	5.6	4.8	-1.4	-3.6	-5.1	-9.7	-5.0
Financial and capital account balance (% of GDP)	4.9	8.9	0.5	4.9	4.5	5.8	8.8	5.7
Foreign direct investment (% of GDP)	3.5	4.6	4.2	3.4	4.3	3.9	6.8	4.6
Gross international reserves (millions of US$)	630	279	825	1,929	2,251	2,946	2,662	3,307
Gross international reserves (% of GDP)	2.4	1.3	3.8	5.8	6.4	7.2	5.9	7.1
	Public finances /3							
Overall balance, central government (% of GDP)	-2.2	-4.5	-3.1	-0.5	-0.9	0.1	-3.3	-3.5
Overall balance, NFPS (% of GDP)	-2.3	-5.4	-2.0	-0.5	-0.9	0.1	-3.3	-3.1
Overall balance consolidated public sector (% of GDP)	-2.6	-8.1	-5.4	-3.0	-3.1	-1.7	-4.6	-4.4
Primary balance, central government (% of GDP)	…	-2.6	-1.2	0.8	0.2	1.7	-1.5	-1.6
Primary balance, consolidated public sector (% of GDP)	-1.4	-4.8	-0.1	1.0	0.4	1.8	-1.3	-0.7
Public sector debt (% of GDP) /4	26.8	55.7	51.1	36.6	39.5	35.8	35.5	39.0
Public sector external debt (% of GDP)	21.5	36.6	34.8	17.4	20.6	19.0	17.1	19.2
	Social indicators							
Population (millions)	8.2	8.3	8.4	8.5	8.7	8.8	8.9	9.0
Unemployment rate (%)	16.1	16.7	18.4	17.9	16.2	15.6	14.2	17.5
Extreme poverty rate (%)	10.7	12.2	16.5	15.0	12.9	11.9	11.7	…
Total poverty rate (%)	29.1	36	43.4	40.1	36.3	35.8	37.8	…

Notes:
1/ Sources: Central Bank, except at otherwise indicated.
2/ Source: SECMCA; values above 100 indicate depreciation in real terms.
3/ Source: Results for period: IMF, debt stock, Ministry of Finance
4/ Includes Central Bank debt.

SUMMARY OF THE NATIONAL DEVELOPMENT STRATEGY

<table>
<tr><td colspan="2">Country vision 2030: The Dominican Republic is a prosperous country in which people live in dignity, safety, and peace, with equal opportunity, in a framework of participatory democracy, responsible citizenship, and competitive positioning in the global economy; a country that makes good use of its resources to develop in an innovative, sustainable manner.</td></tr>
<tr><td colspan="2">Strategy area 1: A State with efficient, transparent institutions at the service of a responsible, participatory citizenry, which ensures security and promotes development and peaceful coexistence</td></tr>
<tr><td>General objectives</td><td>Specific objectives</td></tr>
<tr><td>1.1 An efficient, transparent, results-oriented public administration</td><td>1.1.1 To structure an efficient public administration that acts ethically and transparently, is results-oriented, and is at the service of the citizenry and national development</td></tr>
<tr><td>1.2 Rule of law and public safety</td><td>1.2.1 To ensure that the law is enforced and that crimes do not go unpunished, through a responsive, accessible, efficient judicial system
1.2.2 To build a climate of public safety based on combating the causes of crime and through a professional, efficient, and effective national police force at the service of the public</td></tr>
<tr><td>1.3 Participatory democracy and a responsible citizenry</td><td>1.3.1 To strengthen participatory democracy and the responsible exercise of citizens’ rights and responsibilities
1.3.2 To strengthen the electoral system to ensure that political parties and the National Congress act responsibly, democratically, and transparently</td></tr>
<tr><td>1.4 National security and peace</td><td>1.4.1 To ensure that Dominican national security interests are defended by strengthening the national security system
1.4.2 To strengthen international relations as a means for promoting national development, peaceful coexistence, sustainable global development, and a just world order, in accordance with democratic principles and international law</td></tr>
<tr><td colspan="2">Strategy area 2: A cohesive society with equal opportunity and low levels of poverty and inequality</td></tr>
<tr><td>General objectives</td><td>Specific objectives</td></tr>
<tr><td>2.1 Quality education for all</td><td>2.1.1 To implement a quality education system that teaches continuous learning, promotes human development, and fosters a responsible citizenry
2.1.2 To make education universal from preschool to secondary school</td></tr>
<tr><td>2.2 Comprehensive health care and social security</td><td>2.2.1 To ensure access to a comprehensive health care model with quality and compassion, which focuses on promoting health care and prevention by strengthening the national health care system
2.2.2 To make health insurance universal to ensure access to health care services and reduce out-of-pocket expenses.
2.2.3 To ensure universal, equitable, mutually supportive, and sustainable protection against the risks of aging, disabilities, and survival.</td></tr>
</table>

2.3 Equal opportunity and low poverty levels	2.3.1 To build a culture of equality and equity between men and women 2.3.2 To raise human and social capital and create economic opportunities for people living in poverty 2.3.3 To reduce and alleviate extreme poverty through an effective, efficient social protection system 2.3.4 To protect those living in vulnerable conditions and promote their social inclusion 2.3.5 To control migration flows in accordance with development needs 2.3.6 To promote and protect the rights of Dominicans living abroad
2.4 Territorial cohesion	2.4.1 To promote local development by strengthening the administrative capacities of municipios and coordinating with other levels of government 2.4.2 To incorporate the concept of territorial cohesion in designing and managing public policy 2.4.3 To reduce the urban/rural disparity in access to services and economic opportunity, and to promote orderly, inclusive territorial development 2.4.4 To promote sustainable development in the border region
2.5 Decent housing in a healthy environment	2.5.1 To ensure sustainable, socially integrated human communities with effective risk management 2.5.2 To facilitate people's access to decent housing, with legal security 2.5.3 To ensure universal access to clean drinking water and sanitation services
2.6 Culture, recreation, and sports for human development	2.6.1 To recover, develop, and promote cultural and artistic processes that contribute to human development and national identity 2.6.2 To promote a culture of regular physical exercise and sport activities
Strategy area 3: A coordinated, innovative, and sustainable economy with a productive structure that generates solid, sustained growth with decent jobs, and which positions itself competitively in the global economy	
General objectives	**Specific objectives**
3.1 Macroeconomic stability conducive to sustained economic growth	3.1.1 To ensure macroeconomic stability 3.1.2 To strengthen the sustainable management of public finances, allocating resources according to national development priorities and equitably distributing national revenue 3.1.3 To strengthen an efficient, solvent, and deep financial system that supports the generation of savings and the allocation of savings to productive development
3.2 Reliable, efficient energy	3.2.1 To ensure a reliable supply of electricity at competitive prices under financially and environmentally sustainable conditions 3.2.2 To ensure a reliable, diversified, and environmentally sustainable fuel supply at competitive prices

3.3 An environment conducive to competitiveness and innovation	3.3.1 To develop a regulatory environment that ensures a procompetitive investment and business climate 3.3.2 To strengthen a quality higher education system that addresses the nation's development needs 3.3.3 To promote the development of research, science, technology, and innovation 3.3.4 To achieve universal access and the productive use of information and communication technologies 3.3.5 To expand coverage and improve the quality and competitiveness of transportation and logistics infrastructure and services 3.3.6 To turn the country into a regional logistics hub, leveraging its favorable geographic location
3.4 Decent employment	3.4.1 To promote higher levels of investment, both domestic and foreign, in activities with high value added and the capacity to create decent jobs 3.4.2 To strengthen the Continuing Vocational Training and Development System 3.4.3 To improve the efficiency, investment capacity, and productivity of small and medium-sized enterprises
3.5 A productive structure coordinated and integrated competitively with the global economy	3.5.1 To promote the development of exports on the basis of competitive positioning in international markets 3.5.2 To improve the productivity, competitiveness, and environmental and financial sustainability of agricultural productive chains, thereby contributing to food security, jobs, and income for rural residents 3.5.3 To develop a manufacturing sector that coordinates the national productive system and is integrated with global markets 3.5.4 To support the competitiveness, diversification, and sustainability of the tourism sector 3.5.5 To promote the development of the culture industry 3.5.6 To strengthen an environment that can effectively encourage investment for sustainable development of the mining sector
Strategy area 4: Sustainable management of the environment and effective adaptation to climate change	
General objectives	**Specific objectives**
4.1 Environmental sustainability	4.1.1 To protect and use natural resources in a sustainable manner and improve the quality of the environment 4.1.2 To manage water resources efficiently and sustainably
4.2 Effective risk management	4.2.1 To develop an effective national system for comprehensive risk management with active community participation
4.3 Adaptation to climate change	4.3.1 To make progress in adapting to the effects of climate change and mitigating its causes

Source: Government of the Dominican Republic.
The shaded specific objectives are those targeted by the BCS-DR to support the Dominican government. See Results Matrix.

LENDING FRAMEWORK OF BCS-DR 2010-2013

1.1 **Fiscal position and external financing.** To cope with the economic slowdown of 2009,[24] the Government of the Dominican Republic began implementation of a fiscal stimulus policy aimed at achieving a 3.5% growth rate in 2010, and a 6% growth rate from 2011 onward. While the nonfinancial public sector (NFPS) posted a deficit equivalent to 3.1% of GDP in 2009, this deficit is projected to decrease to 2.5% in 2010, and by one percentage point of GDP starting in 2011, as a result of the recovery of economic growth and the structural measures that the Dominican government will implement in the electricity sector and tax administration. These improved economic prospects and stronger fiscal performance of the nonfinancial public sector (NFPS) will help the country stabilize its debt levels starting in 2011 and generate a primary fiscal balance consistent with the fiscal sustainability analysis.[25]

1.2 **Medium-term financing requirements.** To implement the countercyclical fiscal policy and the structural adjustments envisioned by the Dominican government, the medium-term gross financing requirement (fiscal deficit plus amortizations) for the country's NFPS are projected to be on the order of US$8.987 billion for the 2010-2013 period. Of that amount, US$6.983 billion is expected to come from external resources, and US$2.005 billion from internal sources. Sixty percent of these financing requirements are for 2010 and 2011, due to the effects of the global financial crisis on the country's fiscal position. In 2009 these financing requirements were largely covered by multilateral organizations (World Bank, IDB, IMF), and in April 2010 the country regained access to international capital markets with a successful bond issue of US$750 million on favorable terms in 2010.

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[24] According to preliminary estimates by the Central Bank of the Dominican Republic, growth in 2009 was around 3.5%. However, the IMF's stand-by arrangement as of end-October 2009 estimates growth in the range of 0.5% to 1.5%.

[25] See Annex VIII, Public Debt and Fiscal Sustainability Analysis. The projected primary fiscal balance of the NFPS as of 2011 is consistent with a sustainable debt.

Dominican Republic
NFPS fiscal balances and financing needs (2009-2013)

Item	2009	Estimates 2010	2011	2012	2013
Fiscal balance (% of GDP)					
Total revenues, central government	13.7	14.3	15.3	15.7	16.0
Tax revenues	13.1	13.8	14.7	15.1	15.4
Total expenditures, central government	17.2	16.7	16.9	16.3	16.5
Primary expenditure	15.3	14.5	14.7	14.1	14.1
Interest	1.9	2.2	2.2	2.2	2.4
Fiscal balance, rest of NFPS	0.4	-0.1	0	0	0
Primary balance, NFPS	-1.2	-0.4	0.6	1.6	1.9
Overall balance, NFPS	-3.1	-2.5	-1.6	-0.6	-0.5
Financing (millions of US$)					
Gross financing requirements	2,676	3,060	2,375	1,710	1,843
Overall balance, NFPS	1,448	1,262	868	345	305
Amortizations /1	1,228	1,798	1,507	1,365	1,538
Gross financing sources	2,676	3,060	2,375	1,710	1,843
External	1,717	2,135	1,780	1,540	1,527
Internal /2	959	925	595	169	316

Source: Ministry of Finance, IMF stand-by arrangement.
1/ Includes other short-term assets.
2/ Includes REFIDOMSA net credit and net financing with the electricity sector.

1.3 **IDB financing.** As for the Bank, the lending framework for sovereign guaranteed approvals in the 2009-2013 period ranges from US$1.445 billion in the base scenario to US$1.9 billion in the high scenario (see Annex IV). This framework of approvals, together with the existing portfolio, would allow for resources to be disbursed that would maintain the IDB's share of the country's external financing at 20%. This will help maintain the Bank's share of the country's external debt and total debt at the historical averages for the 2005-2008 period (21% and 17%, respectively). As for multilateral debt, the Bank's share under both scenarios would decrease from a historical average of 73% to an average of 56% in the BCS-DR period. Meanwhile, multilateral debt as a percentage of external debt would rise from a historical average of 29% to an average of 36% under the BCS-DR.

1.4 The transition from the base scenario to the high scenario for loans will depend on: (i) progress in reforming corporate management in the electricity sector (see paragraph 2.23); and (ii) progress in achieving sector milestones and evaluating the first interventions, which will help programs in various sectors (public finances, social protection, education, transportation, water, and agriculture) move on to subsequent phases. As for non-sovereign guaranteed approvals, the amounts approved for the new BCS-DR period are expected to increase from 2009 (when US$62 million was approved).

1.5 The BCS-DR calls for knowledge generation and technical cooperation to occur simultaneously with the operational loan program to ensure consistency with country priorities and the Bank's cycle of operations. Biannual programming for the 2009-2010 period was coordinated with the Dominican government, mobilizing technical-cooperation resources on the order of US$8.7 million. This program's activities will focus on infrastructure (energy, water and sanitation, transportation), social issues (education, social safety net, labor markets), production (agriculture, tourism), and public finances (strengthening of fiscal programming, financial management of disasters). The program will be updated annually to ensure that interventions are timely and adapted to the Bank's work cycle with the country.

Dominican Republic
2005-2009 period and new country strategy 2010-2013
Scenarios of loan flows and net flows

Base scenario	2005	2006	2007	2008	2009	2010	2011	2012	2013
Approvals	250.0	181.0	80.5	40.0	730.0	309.0	160.0	446.0	530.0
Disbursements	135.7	118.1	109.5	137.4	485.5	406.1	189.6	520.7	628.3
Repayments	67.0	75.5	171.7	167.4	134.3	88.7	84.1	310.8	390.8
Net lending flow	68.7	42.6	-62.2	-30.0	351.2	317.4	105.5	209.9	237.5
Interest and fees	59.8	68.2	67.9	62.3	51.4	45.4	42.1	39.0	35.7
Net resource flow	8.9	-25.6	-130.1	-92.3	299.8	272.0	63.4	170.9	201.8
High scenario	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Approvals	250.0	181.0	80.5	40.0	730.0	309.0	295.0	646.0	650.0
Disbursements	135.7	118.1	109.5	137.4	485.5	406.1	194.5	556.6	664.7
Repayments	67.0	75.5	171.7	167.4	134.3	88.7	84.1	310.8	390.8
Net lending flow	68.7	42.6	-62.2	-30.0	351.2	317.4	110.4	245.8	273.9
Interest and fees	59.8	68.2	67.9	62.3	51.4	45.4	42.1	39.0	35.7
Net resource flow	8.9	-25.6	-130.1	-92.3	299.8	272.0	68.4	206.8	238.3

Dominican Republic
2005-2009 period and new country strategy 2010-2013
Exposure indicators (%)

Base scenario	2005	2006	2007	2008	2009	2010	2011	2012	2013
Debt with IDB	1,374.0	1,428.2	1,378.7	1,347.4	1,698.6	2,016.0	2,121.5	2,331.4	2,568.8
Service on debt with IDB/Service on total debt (30%)	6.5	6.3	11.9	13.0	8.1	5.2	4.5	12.4	13.3
Debt with IDB/External debt	23.0	22.3	20.8	18.4	20.3	20.8	19.7	19.7	20.0
Debt with IDB/Multilateral debt	75.2	74.6	72.6	71.0	56.7	56.9	54.4	53.5	57.3
Weighted debt/GDP	17.0	15.7	14.1	18.0	21.1	21.6	22.7	23.0	24.1
Multilateral debt/External debt	30.7	29.9	28.6	26.0	35.9	36.5	36.3	36.9	34.9
Service on debt with IDB/Exports (8%)	2.1	2.2	3.3	3.6	3.1	2.1	1.8	4.5	5.0
Service on external debt/Exports	12.5	21.2	20.0	16.0	19.8	18.9	21.4	19.0	18.8
Exposure of IDB portfolio (18%)	2.3	2.5	2.5	2.3	2.8	3.3	3.5	3.8	4.1
Debt with IDB/GDP	4.5	4.0	3.4	3.0	3.6	4.0	3.9	4.1	4.2
High scenario	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Debt with IDB	1,374.0	1,428.2	1,378.7	1,347.4	1,698.6	2,016.0	2,126.4	2,372.2	2,646.2
Service on debt with IDB/Service on total debt (30%)	6.5	6.3	11.9	13.0	8.1	5.2	4.5	12.4	13.3
Debt with IDB/External debt	23.0	22.3	20.8	18.4	20.3	20.8	19.8	20.0	20.5
Debt with IDB/Multilateral debt	75.2	74.6	72.6	71.0	56.7	56.9	54.4	53.9	58.0
Weighted debt/GDP	17.0	15.7	14.1	18.0	21.1	21.6	22.7	23.1	24.2
Multilateral debt/External debt	30.7	29.9	28.6	26.0	35.9	36.5	36.3	37.1	35.3
Service on debt with IDB/Exports (8%)	2.1	2.2	3.3	3.6	3.1	2.1	1.8	4.5	5.0
Service on external debt/Exports	12.5	21.2	20.0	16.0	19.8	18.9	21.4	19.0	18.8
Exposure of IDB portfolio (18%)	2.3	2.5	2.5	2.3	2.8	3.3	3.5	3.8	4.2
Debt with IDB/GDP	4.5	4.0	3.4	3.0	3.6	4.0	3.9	4.1	4.3

RECOMMENDATIONS OF THE COUNTRY PROGRAM EVALUATION (OVE)
According to the draft Country Program Evaluation, January 2010

Recommendations of the Country Program Evaluation	Incorporation into BCS-DR 2009-2012
Recommendation 1: The experience of the previous strategy suggests the need to develop a new country strategy for the 2009-2012 period, in order to update and incorporate into the programming the basic contextual restrictions in terms of borrowing limits, fiscal headroom for investments, restrictions on the balance to allocate, and changes in the scope of competence of the institutional and political interlocutors.	The new BCS-DR explicitly considers the fiscal leeway available to the Government of the Dominican Republic under the stand-by arrangement with the IMF for the programming of Bank financial support (paragraphs 3.1 and 3.2, Annex III). It also factors in the government's medium-term fiscal programming and borrowing schedule, as well as potential macroeconomic risks (paragraph 5.1 and Annex VII). In terms of changes in institutional competencies, the new BCS-DR establishes the principle of "programmatic focus" as a strategic element for interventions during the country strategy period. This focus is especially important in a country like the Dominican Republic, since it will lend stability and consistency to support initiatives so that they can outlast turnovers of administrations or political parties (paragraph 2.6, footnote 5).
Recommendation 2: Steps should be taken to ensure that the Bank's program helps to strengthen the government's medium- and long-term planning so that it becomes a guiding framework for the implementation of its programs and for allocation of the budget based on results. In particular, the Bank should focus on the country's long-term challenges and vulnerabilities, supporting the planning and implementation of economic and social policies to strengthen a social safety net that will mitigate the effects of external shocks on the most vulnerable groups.	The new BCS-DR is particularly aligned with the country's National Development Strategy as a way of ensuring greater effectiveness of the Bank's program in support of the country's initiatives. The BCS-DR places special emphasis on the social sector, where reforms and investments are identified to strengthen the social safety net based on targeted interventions and expanded availability of quality essential services (education and vocational services). This includes interventions under way or to be approved as part of the new BCS-DR, as well as coordination of interventions with the World Bank for the social safety net, education, and health care (paragraphs 2.13 to 2.21).
Recommendation 3: Activities should be pursued that allow for more efficient interaction between the national economic planning systems and the budgeting, investment, and public credit systems, in order to align spending in a fiscal stabilization framework with the expected results of the country's strategic planning. In order to increase the use of country systems, they will have to be strengthened to meet quality standards. The Bank should continue to support strengthening of the country's systems with technical cooperation instruments and nonfinancial products to identify the basic failures of the system of incentives inherent to these functions.	The new BCS-DR pays special attention to the development of country systems, particularly the systems related to financial administration, budget management, and public investment. The Bank will support the Dominican government with nonfinancial products and knowledge products to achieve progress in these areas, following the action plans for their strengthening. Through PRODEV, the Bank is already providing significant support in results-based management, planning, and public investment (paragraphs 4.1 and 4.2, Annex IX).
Recommendation 4: The Bank should set its financial parameters in the design of the strategy and ensure that the flows of benefits produced by Bank-supported programs exceed their financial costs. If periods of negative net flows arise again in the future, the Bank should also guarantee that there is value added in the form of knowledge. Particularly during periods of limited fiscal leeway for borrowing, the Bank should invest nonreimbursable resources to ensure the development of technical policy proposals that address the country's long term challenges.	The lending scenarios are designed with positive flows during the BCS-DR period. Various supports are also projected in the form of nonfinancial products and knowledge products to support and compensate the country in the event that negative net flows arise (paragraphs 3.1 to 3.3, Annex IV).

Recommendations of the Country Program Evaluation	Incorporation into BCS-DR 2009-2012
<u>Recommendation 5:</u> The Bank should ensure that the conditions attached to reform and budget support programs (PBLs) support real policy reform processes in the framework of the agreements negotiated by the country, contributing technical value added to the detailed reform plans and acting as real incentives to make the necessary reforms under enforceable parameters.	Under the stand-by arrangement with the IMF, in late 2009 the Bank supported an emergency loan (Fiscal Strengthening Program, loan DR-L1043) with major reforms in the electricity sector and fiscal area. The new BCS-DR calls for the Bank to continue working in these very important areas for the country's economy and macroeconomic stability (paragraphs 1.2, 2.7 to 2.12, and 2.22 to 2.24). The Bank will also work to support significant changes in the financial management, purchasing and procurement systems and in the environmental systems (paragraphs 4.1 and 4.2).
<u>Recommendation 6:</u> Given the limited predictability and efficiency of the program, the Bank should establish a new relationship with the country based on shorter portfolio approval, ratification, and execution periods. It should develop alternative scenarios based on these restrictions, while aligning flows to the country with financing needs. It should also ensure that the active portfolio during the strategy period addresses the long-term objectives identified in the strategy.	The new BCS-DR makes a particular effort to ensure strategic consistency between the active portfolio and the objectives and outcomes to be attained, specifically regarding the timeline for approval and execution, given that a number of the Bank's and the country's strategic objectives are aligned with operations already in the portfolio (see electronic link 1, Challenges, Alignment, and Strategic Rationale Matrix). Current operations (especially those recently approved) are key in the new BCS-DR to achieving objectives and results, which will be essential to making timely progress toward outcomes. Additionally, the "programmatic focus" will lend stability and continuity to support initiatives (paragraph 2.6, footnote 5).
<u>Recommendation 7:</u> The Bank should make its full complement of financial and nonfinancial instruments available to the country, to help the government strengthen its capacity to provide public services and regulate private services for the economy and society, ensuring that quality and targeting remain independent from the political cycle and guaranteeing these basic services for the most vulnerable groups.	The use of financial and nonfinancial products to support the government in providing public services and regulating private services is clearly developed in the new BCS-DR, especially in the electricity sector. The Action Plan for Modernizing the Electricity Sector in the Dominican Republic is more than just an example of a highly effective nonfinancial product, it is an example of coordination and working together with the World Bank (paragraphs 2.22 to 2.24, 2.28 to 2.30).
<u>Recommendation 8:</u> The Bank should advance the environmental vulnerability prevention and reduction agenda for the island with various instruments based on the needs and interests of the stakeholders, including technical assistance, knowledge transfers, and grants. Specifically, in order to prompt the adoption of prevention-oriented policies, efforts should be made to identify the political economic factors that have led to the government's de facto adoption of rehabilitation-oriented policies. In addition, the Bank should continue to invest in knowledge by building on the studies conducted in 2005 to identify policy options.	As the new BCS-DR begins, conditions are very favorable for progress in disaster prevention (paragraph 2.11). Startup of the financial strategy for disaster risk management has been the framework to align the various government players and create a technical committee of staff from the finance and planning ministries. Thus, as part of the country's eligibility for the contingent facility for disaster risks, in the short term a comprehensive plan to manage natural disaster risks, focused mainly on prevention, will be prepared and kept up-to-date (paragraph 5.2).
<u>Recommendation 9:</u> Given the increase in basic poverty levels, the Bank should place priority on the targeting of social assistance programs that comprise a social safety net and for which full-scale targeting would produce a demonstrable impact on the reduction of extreme poverty. To that end, the Bank's new programs should condition support on the consolidation of an effective system for fully targeting financing to the poorest groups and establishing an adequate supply of quality social services to expand their opportunities.	In public finance and the social sector, the new BCS-DR establishes the principle of targeting subsidies both in the electricity sector and in social assistance programs, defining them as an efficiency parameter for the design of social protection programs and subsidies (paragraphs 2.10, 2.11, 2.13, 2.14).

DONOR COORDINATION SUMMARY

1.1 The Bank coordinates closely with multilateral institutions, such as the IMF, the World Bank, and the OPEC Fund for International Development (OFID). In coordination efforts with the IMF[26] and World Bank, the Dominican Republic Workgroup meets monthly to monitor the stand-by arrangement (SBA) and the Action Plan for Modernizing the Electricity Sector in the Dominican Republic. Coordination with the OFID occurs through annual meetings, which lead to project-specific activities and eventually to cofinancing actions. Coordination activities with bilateral organizations occur mainly through the Donors Forum which operates permanently between the various bilateral and multilateral agencies in Santo Domingo.

1.2 In public finances, fiscal support for the Dominican government as part of the SBA was closely coordinated with the IMF and World Bank through the Dominican Republic Workgroup. This group jointly established policy measures, financial flows, and macroeconomic conditions so that the SBA could become a comprehensive, coordinated effort of all multilateral institutions.

1.3 In social issues, coordination is based on specific projects and activities (joint missions, technical meetings). For the World Bank, coordination activities have allowed for responsibilities to be distributed efficiently between both institutions: the IDB will focus its work on the education sector, the World Bank will focus on health care, and both institutions will coordinate efforts to support the social safety net. While this does not mean these areas will be addressed exclusively, this does allow for a concentration and specialization of both institutions' efforts.

1.4 For infrastructure, the process of modernizing the electricity sector has been carried out in close technical and financial coordination with the World Bank and the IMF. The IDB and the World Bank jointly developed the Action Plan for Modernizing the Electricity Sector in the Dominican Republic, which has become the action guide for the Dominican government in its efforts to reform the sector. As for financial support, the IDB, World Bank, and OFID designed a joint project to reduce losses and rehabilitate electricity distribution companies. Also, as part of the SBA with the IMF, structural measures related to the electricity sector have been closely coordinated on a technical level with the World Bank and the IDB. In transportation and electricity, significant coordination work has culminated in successful confinancing operations with the OFID. In water and sanitation, significant coordination work has been carried out with the Spanish Agency for International Cooperation and Development (AECID), which has allowed for confinancing operations to be programmed with the Spanish Cooperation Fund for Water and Sanitation in Latin America and the Caribbean.

[26] The IDB, the World Bank, and the OFIC are financing joint activities to reduce losses and rehabilitate distribution companies. Also, within the framework of the stand-by arrangement with the IMF, a number of structural measures related to the electricity sector are closely coordinated at the technical level with the World Bank and the IDB.

1.5 In the productive area of tourism and agriculture, activities are coordinated mainly with bilateral institutions that belong to the Donors Forum.

SUMMARY OF DONOR COORDINATION
Number of interventions by area and agency

Areas	Issues	AECID	AFD	IDB	WB	EC	JICA	PAHO	UNDP	UNFPA	UNICEF	USAID	Total
Social cohesion	Education	1	3	3	1	1	1				1	3	14
	Health care	1	1	1	2	1	1	3	5	6	2	3	26
	Transfers and subsidies				2								2
	Employment	1		1	1			1					4
	Food security	1	1		1			1					4
	Vulnerable groups				1						1		2
Macroeconomic stability, competitiveness, and productive development	Energy				2		1		1				4
	Banking		1	1	1								3
	Fiscal policy			2	1								3
	Agriculture	1	2	2			1					1	7
	Environment	1	1			1	1	1	5			1	11
	Water and sanitation	1		1	1	1	1	1	1			1	8
	Disaster mitigation	1		2	1	1	1	2		1	1		10
Institutional development and quality in public spending	Justice	1		1							1	1	4
	Democratic governance	1			1	2			8	1	1		14
	Migration					1				1			2
	Gender	1						1	1	2			5
	Human rights					1		1		1	1		4
	Inst. development & RBM			2		1		1	2				6
	Social auditing			1		1						1	3
	Control mechanisms				1	1					1	1	4
Other	Culture and development	3											3
	Community				1								1
	Economic competitiveness					1							1
	Bilateral cooperation Haiti-DR					2							2
	Sustainable tourism						1						1
	Competitiveness						1		1				2
	Millennium Development Goals								1				1
	Total	14	9	17	17	15	9	12	25	12	9	12	151

Priority issues of the BCS-DR 2009-2012

MACROECONOMIC RISK ANALYSIS

1.1 The main macroeconomic risk facing the Dominican economy during the period of the new BCS-DR is that the global economic crisis will continue. Given the vulnerability of the Dominican external sector to the international economic cycle (due to its strong dependence on flows from the United States economy) and its high exposure to external shocks (fuel prices, capital flows), a continuation of the global economic crisis from 2010 onward could have additional effects on economic growth and fiscal revenues beyond those estimated in the stand-by arrangement (SBA). In such a scenario, the SBA's growth projections could prove to be overestimated, which would have an adverse effect on projected tax revenues and open up a gap in the lending program.

1.2 A simulation of the impact of a slowdown in the growth rates estimated in the SBA (assuming that growth only recovers to half of the estimate for the 2010-2013 period) found that the financing gap could grow from 0.4% of GDP in 2010 to around 1% of GDP in 2013. This would represent slightly more than US$1.958 billion in additional financing requirements during the period (about 3.5% of GDP). In this situation, the Bank could cover 20%[27] of the gap, increasing its lending framework to accommodate roughly an additional US$392 million (about 0.7% of GDP).

Dominican Republic
NFPS fiscal balance and financing needs (2010-2013)
Macroeconomic risk scenario

	Preliminary	Estimates			
Items	**2009**	**2010**	**2011**	**2012**	**2013**
Estimated fiscal balance (% of GDP)					
GDP growth rate	3.5%	2.0%	3.0%	4.0%	4.0%
Total revenues, central government	13.7	13.9	14.2	14.6	15.1
Primary spending, central government	15.3	14.5	14.7	14.1	14.1
Balance, rest of NFPS	0.4	(0.1)	-	-	-
NFPS primary balance	(1.2)	(0.7)	(0.5)	0.5	1.0
NFPS overall balance	(3.1)	(2.9)	(2.7)	(1.7)	(1.4)
Estimated financing (millions of US$)					
Gross financing needs	2,676	3,267	2,961	2,316	2,401
NFPS overall balance	1,448	1,469	1,455	952	863
Amortization	1,228	1,798	1,507	1,365	1,538
Increase in financing needs	-	207	587	607	558
Additional IDB financing	-	41	117	121	112
Increase in financing needs (% of GDP)	0.0%	0.4%	1.1%	1.1%	0.9%
Additional IDB financing (% of GDP)	0.0%	0.1%	0.2%	0.2%	0.2%

Source: Own calculations and data of the Ministry of Finance and IMF stand-by arrangement.

27 Replicating the Bank's share in the country's external financing requirements (paragraph 3.2, section III).

1.3 Any support of this type, which increases the lending framework to support the Dominican government in its additional financing requirements, should be closely linked to the implementation of policies aimed at ensuring fiscal sustainability over the medium term. In a scenario of a continued worldwide recession such as the one described above, the country should adjust its public finances in view of that fact that new levels of worldwide growth are permanent in nature. Such an adjustment would require additional actions in tax policy and tax administration to generate new revenues, as well as additional spending actions to reduce the financial deficit of the electricity sector, more quickly than set forth in the Action Plan for Modernizing the Electricity Sector of the Dominican Republic.

1.4 <u>Even under these extreme assumptions, the medium-term projections and sustainability analysis show that debt remains remain at sustainable levels.</u> Based on the sustainability analysis presented in Annex VIII, and the medium-term fiscal projections developed under the SBA, the country will move gradually toward fiscal results consistent with the stabilization of debt levels. With implementation of the policy measures proposed by the Government of the Dominican Republic, as reflected in the SBA projections, the country can be expected to generate positive primary balances from 2011 onward.

PUBLIC DEBT AND FISCAL SUSTAINABILITY ANALYSIS

Public debt

1.1 In view of the fiscal position of the Dominican Republic in 2009 and the SBA's projections for 2010, total public debt (including the debt of the Central Bank of the Dominican Republic [BCRD]) will continue to grow until 2011 and then will begin to stabilize. The distribution of total public debt among the various types of creditors is steadily changing. Especially noteworthy, as of 2008, is the increase in debt to bilateral creditors, which has grown at a more than 20% rate (reflecting the increase in amounts owed in connection with the agreement with Petrocaribe). Indebtedness to multilateral organizations (IDB, World Bank, IMF, Andean Development Corporation) began to rise in 2009, and will increase by more than US$1 billion (2.4% of GDP). In addition, indebtedness to private creditors shows an increase in 2010, given bond issues on the international market. After the SBA begins to yield results in terms of economic growth and fiscal strengthening, however, fiscal needs will decrease significantly and the nonfinancial public sector (NFPS) will begin to generate a primary surplus starting in 2011.

1.2 The internal debt has continued to grow in 2009, largely as a result of bonds to recapitalize the BCRD. Since 2008, internal debt amounts have increased significantly, reflecting the use of internal financing to meet financing requirements in general and to recapitalize the BCRD in particular. During 2009, some US$900 million (2.0% of GDP) in treasury bonds were issued for recapitalization.

Table 1. Public debt
Debt of the nonfinancial public sector
(Stock in millions of US$)

SOURCE OF DEBT/CREDITOR	2005	2006	2007	2008	2009	2010	2011	2012	2013
EXTERNAL DEBT	**5,963.5**	**6,393.0**	**6,636.6**	**7,313.4**	**8,357.8**	**9,708.7**	**10,746.0**	**11,815.0**	**12,551.1**
official creditors:	***4,151.7***	***4,517.1***	***4,817.1***	***5,624.6***	***6,829.5***	***7,525.0***	***8,106.6***	***8,659.5***	***8,976.0***
Multilateral debt:	**1,828.0**	**1,914.3**	**1,900.0**	**1,899.0**	**2,996.8**	**3,543.7**	**3,902.2**	**4,356.6**	**4,482.0**
IDB	1,374.0	1,428.2	1,378.7	1,347.4	1,698.6	2,016.0	2,121.5	2,331.4	2,568.8
World Bank	403.1	432.6	468.2	448.9	801.1	895.2	1,048.4	1,191.0	1,237.7
IMF	0.0	0.0	0.0	0.0	300.0	75.0	107.0	130.7	138.3
CAF	0.0	0.0	0.0	55.4	75.4	467.7	467.7	467.7	248.9
Other	51.0	53.5	53.2	47.3	121.6	89.9	157.7	235.9	288.2
Bilateral debt:	**2,323.7**	**2,602.8**	**2,917.1**	**3,725.6**	**3,832.7**	**3,981.3**	**4,204.3**	**4,302.9**	**4,494.0**
Petrocaribe agreement	159.5	448.8	707.2	1,250.9	1,456.3	1,689.0	1,837.0	1,965.1	2,059.4
Private creditors:	***1,811.9***	***1,875.9***	***1,819.5***	***1,688.8***	***1,528.3***	***2,183.7***	***2,639.4***	***3,155.5***	***3,575.1***
Bonos	1,149.3	1,496.0	1,389.8	1,283.7	1,178.2	1,822.1	2,216.6	2,716.6	3,189.0
INTERNAL DEBT	**974.9**	**1,111.3**	**1,002.6**	**4,000.4**	**4,899.5**	**4,992.5**	**5,775.0**	**5,848.1**	**6,232.3**
TOTAL PUBLIC DEBT	**6,938.4**	**7,504.3**	**7,639.2**	**11,313.8**	**13,257.2**	**14,701.2**	**16,521.0**	**17,663.2**	**18,783.4**
% OF GDP	**22.5**	**20.9**	**18.8**	**24.9**	**28.4**	**29.0**	**30.5**	**30.7**	**30.8**
CENTRAL BANK DEBT	**4,437.6**	**4,750.2**	**5,318.8**	**5,926.5**	**4,180.8**	**4,506.2**	**3,959.9**	**3,718.4**	**3,718.4**
% GDP	**14.4**	**13.21**	**13.06**	**13.03**	**9.0**	**8.9**	**7.3**	**6.5**	**6.1**
TOTAL PUBLIC DEBT + CB	**11,376.0**	**12,254.5**	**12,958.0**	**17,240.3**	**17,438.0**	**19,207.4**	**20,480.9**	**21,381.6**	**22,501.8**
% OF GDP	**36.9**	**34.1**	**31.8**	**37.9**	**37.3**	**37.8**	**37.8**	**37.2**	**36.9**

Source: Ministry of Finance. Preliminary projections.
The projected stock of IDB debt corresponds to the base scenario of the BCS-DR.

Fiscal sustainability

1.3 <u>The country should make significant efforts in fiscal sustainability, especially in the current state of the world economy.</u> The outcomes attained by implementing the Bank's debt sustainability analysis[28] show that the sustainable primary balance (under a scenario with roughly a 5% economic growth rate[29]) for the nonfinancial public sector is 0.61% of GDP. In view of the situation at the close of 2009 (primary NFPS deficit equivalent to 1.2% of GDP in 2009), getting on the road to sustainability would require a fiscal adjustment of about 1.8% of GDP over the short term, which would help stabilize public debt at about 30% of GDP in 10 years. Under the government's macroeconomic program, the nonfinancial public sector is expected to post a primary surplus near that range starting in 2013.

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[28] This analysis is performed using various methodologies agreed upon with RES (Research Department) and CID (Country Department of the Central American Isthmus, Mexico, and the Dominican Republic).

[29] Under a scenario with a 3% growth rate, the required average primary surplus is 1.4% of GDP. Under a scenario with a 2% growth rate, the required average primary surplus is 1.8% of GDP. If growth rates in the Dominican economy drop to these levels, the fiscal adjustment needed in the public sector would be 2.6% of GDP in the former scenario and 3% of GDP in the latter scenario.

Table 2. Required primary balance

Required primary balance (% of GDP)

		Long-term GDP growth				
		3.5%	**4.5%**	**5.0%**	**5.5%**	**6.5%**
Real interest rate	**3.8%**	0.12%	-0.24%	-0.45%	-0.59%	-0.94%
	4.8%	0.48%	0.11%	-0.10%	-0.24%	-0.59%
	5.8%	0.84%	0.47%	0.26%	0.11%	-0.24%
	6.8%	1.20%	0.83%	0.61%	0.47%	0.11%
	7.8%	1.56%	1.18%	0.97%	0.82%	0.46%
	8.8%	1.92%	1.54%	1.32%	1.17%	0.81%
	9.8%	2.28%	1.90%	1.67%	1.53%	1.16%

Sudden stop

1.4 A sudden stop scenario poses greater challenges to fiscal sustainability. The Dominican Republic has relatively high levels of dollarization of its public debt (58.7%), and its exports-to-GDP ratio is moderate (26%). This combination explains the fact that, all other things equal, a change in relative prices (between nontradable and tradable goods) would lead to a 0.15% increase in the primary balance needed to stabilize the debt compared to the base scenario.[30] Under this methodology, if one also takes into account the external vulnerability of the Dominican Republic, a primary balance of up to 2.1% of GDP would be needed to protect the economy from simultaneous shocks in interest rates, relative prices, and decreased growth. Under the macroeconomic program of the Government of the Dominican Republic, the nonfinancial public sector is projected to post a primary surplus in approximately that range starting in 2013.

[30] Under the assumptions used by Calvo, Izquierdo, and Talvo (2005), the change in relative prices depends mainly on the degree of absorption of tradable goods, i.e., the current account-to-imports ratio. The degree of absorption of tradable goods may be understood as the percentage of imports not financed by the internal supply of tradable goods.

Table 3. Public debt

Sudden stop scenario		
Balances as % of GDP		
1. Base scenario	Initial debt level	35.1
	Primary balance	0.61
2. Change in relative prices	Primary balance	0.76
3. Scenario 2 + 200 bp increase in interest rate	Primary balance	1.64
4. Scenario 3 + 1% decrease in GDP growth rate	Primary balance	2.10

Source: Own calculations

Sustainability amid uncertainty

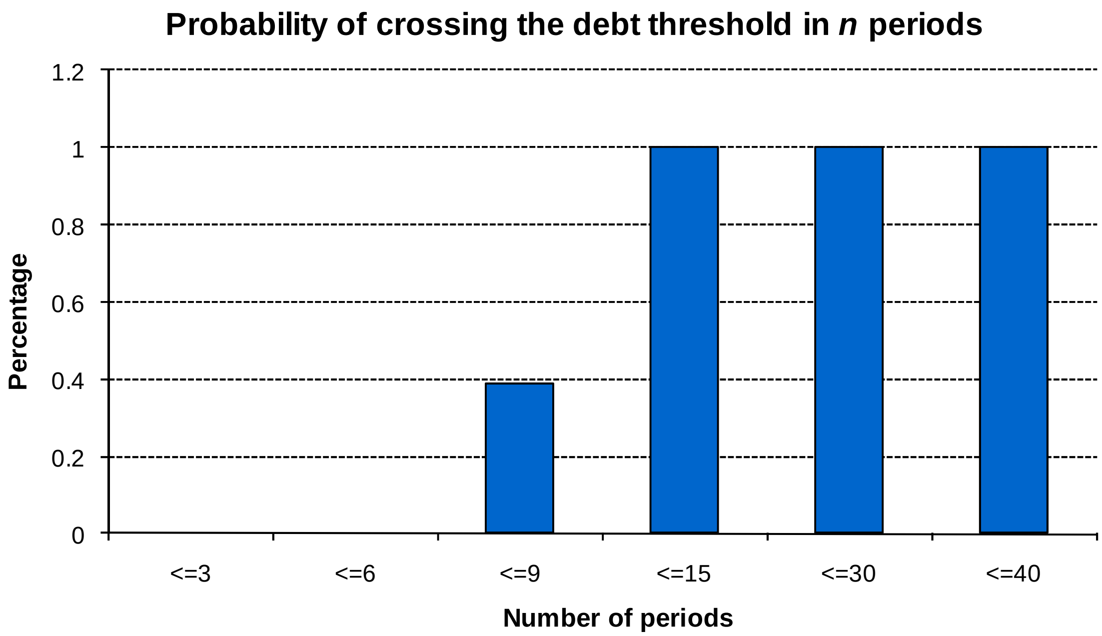
1.5 A sustainability analysis under a scenario of uncertainty poses the greatest challenges. Given a level of flexibility in public expenditure and/or revenues that allows the government the credible capacity to repay its debt,[31] the government's debt threshold[32] is projected (based on data up to 2008) at 65% of GDP—i.e., this is the maximum debt level that the government can honor under a scenario of minimum fiscal revenues. Also, assuming that the accumulated debt level is as observed up until 2008, that the government maintains spending at its historical average, and that fiscal revenues fall two standard deviations below the historical average (which constitutes a minimum-revenue scenario), there is a probability of crisis, i.e., the probability of crossing the maximum debt threshold. Assuming a maximum adjustment level of expenditure of 20% compared to a minimum-revenue scenario, the probability of crisis is less than 40% in a nine-year period.[33] A long-term "sustainable" scenario is generally assumed to be one that generates only a 20% probability of crisis over a period of about nine or ten years under a minimum-revenue scenario. This does not necessarily mean that current levels are unsustainable, but rather that these simulations give an indication that it is important to make adjustments to minimize the probability of crisis under a minimum-revenue scenario. Obviously, these adjustments cannot be made immediately, but they indicate a path for the medium term. Experience over the past three years has shown that a 3% adjustment in GDP in the fiscal balance is feasible and politically viable. However, this adjustment was achieved in a different macroeconomic environment and within a favorable international framework.

[31] The capacity of repayment is credible only if the government can pay its debt under any possible scenario. This means that the government cannot accumulate more debt than it can honor in the event of a fiscal crisis, defined as a situation in which the primary balance is at the lowest level possible.

[32] The debt threshold does not necessarily coincide with sustainable debt, which is determined by the primary balance.

[33] The degree of flexibility in spending is estimated in a manner exogenous to the model, and fluctuates on the order of 20% to 24%.

Figure 1. Probability of crisis



FIDUCIARY SAFEGUARDS AND SYSTEMS[34]

1.1 Studies of financial management systems in the Dominican Republic between 2003 and 2007[35] revealed weaknesses in the budget allocations and in public administration systems. To make management more effective, the government has made progress in carrying out a significant reform process in public administration, and the Bank has been a strategic partner in this process. Against this backdrop, progress has been made in recent years in designing, developing, and implementing the SIGEF Integrated Financial Management System and in developing and approving the legal framework needed to reform the financial administration of the State.[36]

1.2 The Bank is making partial use of national fiduciary systems. In resource management, funds from external financing are programmed into the national budget and are managed through individual fiscal accounts authorized and monitored by the Dominican treasury office, while consolidated treasury account is beginning to be implemented. In particular, the country developed an financial information, administration, and control system for the execution units of external loans (UEPEX) that allows for execution to be disaggregated from spending, budgeting, and accounting, and incorporated manually and aggregately to the SIGEF system. UEPEX is currently used on recently approved Bank operations, and also with other accounting systems developed on an ad hoc basis on older operations. The Chamber of Accounts and the Office of the Comptroller General are responsible for external and internal government oversight, respectively; however, due to technical limitations and limited resources, external audits of Bank-financed projects will be carried out by the country's leading private firms.

1.3 The Bank is not currently using national procurement systems in the operations it is financing, and diagnostic assessments need to be updated. Opportunities to improve execution have been identified,[37] such as developing a methodology for planning, development, and standardization of model bid forms, and evaluating and developing the electronic procurement system. These actions will lead to better management and tracking of procurement processes, with an impact on the efficiency, effectiveness, and transparency of public management. The current state of the systems, the amount of resources that the country will be managing,[38] and the opportunity to improve on transparency indicators[39] pose a clear challenge for the next four years. In that sense, strengthening national fiduciary systems in

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34 See the Technical Note on Fiduciary Strategy.

35 Public Expenditure Review, World Bank (2004); Country Fiduciary Assessment, World Bank (2005); Country Financial Accountability Assessment, World Bank/IDB (2005); Report on the Observance of Standards and Codes, World Bank (2004); and Public Expenditure and Financial Accountability, European Union (2007).

36 The most significant support from the Bank has been through loan 1093/OC-DR, which was completed in 2005. After this operation, support was provided through a number of technical-cooperation operations.

37 Prior reviews of 85% of the operations currently financed by the Bank.

38 See paragraph 3.1 and the first two objectives of the Results Matrix in this country strategy.

39 Transparency International, http://www.transparency.org.

accordance with international standards[40] is key. The following table shows the current state of the fiduciary sector, projected actions, and outcomes for the period covered by the country strategy.

[40] See standards for the methodology of indicators of the OECD/DAC (www.oecd.org) and PEFA (www.pefa.org).

EXPECTED OUTCOMES IN THE FIDUCIARY SECTOR

Objectives of the National Development Strategy	IDB sectors for intervention	IDB strategic objectives	Projected outcomes of the country strategy	Indicators	Baseline (Source) (*)	Targets (**)
To structure an efficient public administration that acts ethically and transparently, is results-oriented, and is at the service of the citizenry and national development	**Financial management and public procurement**	**Financial management system**				
		Use the country's SIGEF Integrated Financial Management System (budgeting, cash management, and reports subsystems), by way of the financial administration and control System for Execution Units of External Loans (UEPEX), for Bank-financed loan operations.	The country financial management system (SIGEF/UEPEX) is used for financial management of Bank-financed projects.	% of Bank-financed projects using the SIGEF/UEPEX system.	2009: 40% of Bank-financed projects use the SIGEF/UEPEX system for financial management.	2013: The SIGEF/UEPEX system is used for financial management of 100% of Bank-financed projects.
		Procurement system				
		Strengthen and gradually use the country public procurement system based on international best practices for efficiency and transparency.	Establish a set of indicators to guide the use of international best practices in the public procurement system.	Estimation of OECD/DAC indicators for public procurement systems.	**2010**: No indicators	**2013:** All OECD/DAC indicators have been estimated for the country.
			Implement international best practices in publication and standardization of procurement processes.	% of contracts with standard bidding documents.[41]	**2010**: 0% of contracts have standard bidding documents.	**2013:** 100% of contracts use standard bidding documents.
				% of Bank-financed projects under which standard bidding documents are used for all procurements and published via the country's e-procurement system.	**2009**: 0% of Bank-financed projects publish bid notices via the country's e-procurement system or use standard bidding documents for all procurements.	2013: 100% of Bank-financed projects publish bid notices via the country's e-procurement system or use standard bidding documents for all procurements.

[41] "Standard bidding documents" are documents prepared by the country and agreed upon with the Bank for bidding processes, under Bank-financed operations, to procure works and/or goods and/or nonconsulting services; price comparison processes for works and/or goods and/or nonconsulting services; and the selection of consulting firms and/or individual consultants.

DEVELOPMENT EFFECTIVENESS MATRIX (DEM)

COUNTRY STRATEGY: DEVELOPMENT EFFECTIVENESS MATRIX	
In August 2008, the Board of Directors approved the Development Effectiveness Framework (GN-2489) to increase the evaluabiliy of all Bank development products. The Development Effectiveness Matrix for Country Strategies (DEM-CS) is a checklist of the elements that are necessary to evaluate a country strategy. It is based on the evaluation criteria developed by the Evaluation Cooperation Group of the Multilateral Development Banks in the "Good Practice Standards for Country Strategy and Program Evaluation." The DEM-CS is a yes/no system with a partial score for each of the four evaluation criteria.	
	SCORE
I. RELEVANCE	10.00
A. Ownership and Alignment: establishing consistency of CS objectives with government's plans & priorities	10.00
B. Coherence: establishing (i) the definition of Country Strategy focus in terms of anticipated results and (ii) the integration across Bank instruments/products	10.00
II. EFFECTIVENESS	8.48
A. Strategy Results Framework	9.29
B. Financial Transfers	10.00
C. Build up and use of Country systems	6.16
III. EFFICIENCY	to be determined in Programming document
IV. RISKS	10.00