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Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 26-Jul-2019| Report No: PIDC27231

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
St Maarten	P171291	Sint Maarten First Public Finance, Social Insurance and Resilience Development Policy Operation (P171291)	
Region	**Estimated Board Date**	**Practice Area (Lead)**	**Financing Instrument**
LATIN AMERICA AND CARIBBEAN	Aug 30, 2019	Macroeconomics, Trade and Investment	Development Policy Financing
Borrower(s)	**Implementing Agency**		
Ministry of Finance	Ministry of Health, Social Affairs and Labor, National Recovery Program Bureau, Ministry of Finance		

Proposed Development Objective(s)

To support the Government of Sint Maarten in: (i) strengthening domestic resource mobilization and public financial management; (ii) improving the financial sustainability of the social insurance system; and (iii) boosting resilience to natural disasters.

Financing (in US$, Millions)

SUMMARY

Total Financing	15.00

DETAILS

Total Non-World Bank Group Financing	15.00
Trust Funds	15.00

Decision

The review did authorize the preparation to continue

B. Introduction and Context

Country Context

Sint Maarten, a constituent country of the Kingdom of the Netherlands in the Caribbean, faces a major challenge of reconstruction and economic recovery after hurricanes Irma and Maria hit the island in September 2017, causing damages and losses amounting to approximately 260 percent of GDP. Economic activity is estimated to have contracted during 2017-2018 by an estimated 12.5 percent compared to its pre-hurricane (2016) level, leading to significant public-sector deficits. In 2016, the tourism sector directly accounted for 45 percent of GDP and 73 percent of its foreign exchange earnings. Damages from the hurricane to the airport, hotels, and firms engaged in the tourism sector have had a significant negative economic impact. While the economy is expected to bounce back in 2019, fiscal deficits are expected to be incurred through at least 2020. The major part of these deficits can be attributed to the fall in tax revenue – primarily in wage, turnover and profit taxes – following the downturn in economic activity.

Fiscal consolidation will be needed to ensure debt sustainability and build additional resilience. The fiscal framework, in combination with a debt restructuring of the former Netherlands Antilles in 2010, led to a moderate level of public debt prior to the hurricanes. In addition to borrowings from the Netherlands, the government has financed itself by incurring arrears mainly with the civil servants' pension fund (APS) and the Implementing agency for the Social Insurances (SZV). Liquidity support provided by the Netherlands, borrowings for capital expenditures, an EIB loan for the government to on-lend for the reconstruction of the airport, and domestic arrears, are significantly increasing the gross debt-to-GDP ratio, currently projected to reach nearly 60 percent by 2022-2023. The level and rapid increase in the gross debt-to-GDP ratio calls for ambitious fiscal consolidation, based on both revenue and expenditure measures, to moderate financing needs and accommodate additional debt service and fiscal resilience requirements

Relationship to CPF

The Sint Maarten Recovery, Reconstruction and Resilience Trust Fund, administered by the World Bank and financed by the Netherlands, supports the objectives of Sint Maarten's National Recovery and Resilience Plan (NRRP) to restore economic, community and governance infrastructure as well as service delivery. The Steering Committee of the Trust Fund (composed of the Government of Sint Maarten, the Government of the Netherlands and the World Bank) allocated US$30 million to support a a Development Policy program in the form of two Development Policy Operations (DPOs) of US$15 million each.

C. Proposed Development Objective(s)

To support the Government of Sint Maarten in: (i) strengthening domestic resource mobilization and public financial management; (ii) improving the financial sustainability of the social insurance system; and (iii) boosting resilience to natural disasters.

Key Results

Actions within **pillar A (strengthening domestic resource mobilization and public financial management)** will support the modernization of the tax administration and improvement of tax compliance and collection. Enhanced public financial management (PFM) capacity is expected to lead to a better tracking, monitoring, and promptly respond to identified gaps. **Pillar B (improving the financial sustainability of the social insurance system) is expected to** improve the financial sustainability of the public pension and health system though an increase of the retirement age from 62 to 65 years of age, a systematic switch to generic medicines, and a revamping and streamlining of the medical referral process. **Pillar C (boosting resilience to natural disasters)** will support the adoption of a comprehensive Disaster Risk Management policy, including an ex-ante Disaster Risk Financing strategy consisting of disaster risk insurance and contingency fund instruments.

D. Concept Description

The first pillar will support the Government's efforts to strengthen domestic resource mobilization and public financial management. This is key to creating the fiscal space necessary to gradually achieve a balanced budget, and eventually a moderate surplus, to reduce the public debt burden. Increased fiscal space is also essential for building fiscal buffers over the medium term to face recurrent natural disasters. In light of the major fiscal challenges, it is crucial to modernize the tax system and to improve compliance and collection as enhanced tax revenues provide a base for expanded social services and greater resilience. Another objective of the government recovery and resilience process is to strengthen public financial management (PFM) capacity to better track and monitor spending, and promptly respond to identified gaps.

The second pillar will support the Government's efforts to improve the financial sustainability of the social insurance system. Demographic ageing and epidemiological transition are compromising the financial sustainability of traditional social insurance schemes, necessitating parametric adjustments to contributions, benefits or both. Many countries have adopted phased increases in retirement ages, for example, while other parametric adjustments may include moving from a final salary to average salary basis for the calculation of pension benefits. With increased longevity and more sophisticated medical treatments, medical cost inflation has followed a rising trajectory in recent decades. Substantial financial savings in the purchase of pharmaceuticals can be made through the systematic switch to generic medicines, where they are available. Like other small jurisdictions, Sint Maarten is not of sufficient scale to be able to provide a full universe of medical treatments efficiently within its own borders, relying instead on medical referrals abroad where necessary. There is evidence that significant savings can be made through the revamping and streamlining of the referral process.

The third pillar will support the Government's efforts boost resilience to natural disasters. Due to its geography, Sint Maarten will continue to suffer periodic, and sometimes catastrophic, natural disasters. It is critically important that its finances and its processes are built to withstand future disasters. There is an opportunity for Sint Maarten to avail itself of pooled catastrophic disaster risk insurance through the Caribbean Catastrophic Risk Insurance Facility (CCRIF). As well as improving its public finances to create fiscal space to react to a future natural disaster in a general sense, governments may also choose to self-insure through the establishment of an emergency response fund. The importance of contingency funds has been demonstrated in other national contexts in building a fiscal framework that is able to generate savings that can later be used when shocks materialize. Finally, it is advisable to have in place a comprehensive Disaster Risk Management policy, including an ex-ante Disaster Risk Financing strategy, so that the governance processes and institutional and financial architecture are already in place before the next significant natural disaster. Additional measures to boost resilience may also be supported.

E. Poverty and Social Impacts and Environmental Aspects

Poverty and Social Impacts

Poverty and social impacts of the policy measures supported by this programmatic DPO are expected to be positive on balance. Reforms supported under Pillar A are not expected to have significant short term positive or negative effects on poverty, social outcomes or income distribution. In the medium term however, a potential positive effect can be expected as improved revenue mobilization generates fiscal space to increase public spending on poverty reduction, income redistribution and on the provision of public goods. Measures introduced under Pillar B can be expected to have a mixed social impact. Increasing the retirement age should allow for the maintenance or improvement of pension benefits while making the pension system overall more financially sustainable. This should serve to reduce poverty among the elderly, particularly among women who are less likely to have alternative income sources. Cost control measures in the health system are likely to reduce somewhat the choice available to doctors and their patients but are not expected to materially impact on health outcomes. Reforms supported by Pillar C could have positive effects. For example, to the extent that residents rely on the country's infrastructure and natural environment for their livelihoods, such as in the tourism sector, policies such as disaster risk management and financing that serve to protect natural and physical capital may have positive employment, poverty reduction and distributional effects.

Environmental Impacts

Reforms supported by Pillars A and B will have no negative environmental effects, while those under Pillar C have the potential to be positive. Measures supported under Pillars A and B do not include policy reforms or any measures that could reasonably be expected to impact the environment and natural resources. Under Pillar C, elaborating a comprehensive Disaster Risk Management (DRM) policy will not have an immediate direct impact on the environment. However, the medium-to-long term impact of this measure should be positive insofar as the Disaster Risk Financing (DRF) strategy component incorporates risk-retention and risk-transfer mechanisms that will ensure resources are set aside or otherwise made available, for timely and appropriate responses to extreme weather events. The negative repercussions of such events on the environment can become aggravated if left unaddressed. Furthermore, the DRM policy should be elaborated with a view to maximizing climate change resilience

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APPROVAL

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