

International Monetary Fund

[Grenada](#) and the IMF

Press Release:
[IMF Executive Board
Concludes Second
Review under the
PRGF Arrangement
with Grenada and
Approves US\\$3.66
Million Disbursement](#)
December 12, 2008

Grenada: Letter of Intent, Supplementary Memorandum of Economic Policies, Supplementary Technical Memorandum of Understanding, and Supplementary Letter of Intent

November 26, 2008

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The following item is a Letter of Intent of the government of Grenada, which describes the policies that Grenada intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Grenada, is being made available on the IMF website by agreement with the member as a service to users of the [IMF](#) website.

St. George's, Grenada
November 26, 2008

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Strauss-Kahn:

Our government, which took office in July 2008, has a strong commitment to the PRGF-supported program. The attached Supplementary Memorandum of Economic Policies (SMEP) reviews the progress under the PRGF-supported program implementation, and outlines the government's policies and objectives and macroeconomic framework for the remainder of 2008 and beyond. It emphasizes putting our debt on a sustainable trajectory, undertaking reforms to improve the business environment, and reforming our capacity for fiscal management.

Owing to negative shocks and spending pressures in the run up to the July elections, we were unable to meet two out of six of the quantitative performance criteria (on the primary balance excluding grants and external arrears) for the second review. We have taken strong remedial measures to address the fiscal slippages and to bring down the stock of domestic arrears by issuing in September a finance circular (a prior action for completion of the second review) that would sharply restrict capital spending in the fourth quarter of the year. We have also recently selected an expert with professional experience to head the new Debt Management Unit in the Ministry of Finance. Reflecting overruns in the first half, we have revised our end-2008 program targets for the primary balance excluding grants and for domestic arrears. On this basis, we request waivers for the missed performance criteria.

We are making progress with the resolution of a small unregulated bank and in September 2008 revoked its license and reappointed the receiver under a different section of the Banking Act. On November 13, we petitioned the High Court to liquidate the bank at the recommendation from the receiver and following consultation with the ECCB.

We have made limited progress with other structural reforms. We signed a memorandum of understanding on information sharing between the Customs and Inland Revenue Departments in November 2008. There were delays in developing an action plan to improve Doing Business Indicators, and obtaining Cabinet approval for reforms to investment incentives, and developing and implementing a customs Fraud Control Plan. Looking forward, we intend

to submit investment incentives reforms and new VAT and Excise bills to Parliament, and to establish the Debt Management Unit.

With regard to the proposed large loan from the Export-Import Bank of China to build a port and marina, we are proceeding cautiously and would consider a loan of around US\$5 million for a small marina project, but the project will not go forward in the first half of 2009. We have maintained our best efforts to complete the restructuring of our bilateral debt. We will continue good faith efforts to reach collaborative agreements with the few remaining nonparticipating commercial creditors. We have approached our Paris Club creditors to seek debt relief for 2009 in line with the debt relief that the Paris Club extended in 2006–08.

Proposed quantitative performance criteria and indicative targets are indicated in Table 1 of the SMEP; the proposed structural benchmarks and performance criteria are indicated in Table 2. We are committed to working to achieve these program targets, including the fiscal targets. On this basis, the Government of Grenada hereby requests the completion of the second review under the PRGF arrangement and financing assurances review and the release of the associated disbursement in an amount equivalent to SDR 2.41 million. We also request revision of the end-December targets for the primary balance excluding grants and for domestic arrears.

The government will continue to provide the Fund with such information as the Fund may request in connection with progress in implementing the economic and financial policies. The government believes that the policies and measures set forth in our previous MEP and the attached SMEP will achieve the program's objectives. The government also stands ready to take additional policy measures as appropriate to ensure the attainment of these objectives. We will consult with the Fund on the adoption of these measures, and in advance of revisions to the policies contained in the MEP and SMEP, in accordance with the Fund's policies on such consultations. The fourth review under the PRGF arrangement is expected to be completed by October 15, 2009 and the fifth review by March 31, 2010.

The government authorizes the Fund to make public the contents of this letter and the attached SMEP, as well as the accompanying staff report, to facilitate wider access to our policies and to signal the seriousness of our commitment to the program to civil society and the international community.

Yours sincerely,

_____/s/_____
Honorable Nazim Burke
Minister of Finance, Planning, Economy,
Energy, Foreign Trade and Cooperatives

SUPPLEMENTARY MEMORANDUM OF ECONOMIC POLICIES

1. **Our economic strategy aims at promoting sustained high economic growth** by putting public finances on a sustainable trajectory; improving the climate for private investment; reducing vulnerabilities; and alleviating poverty through more effective social safety nets. This supplement to our Memorandum of Economic Policies dated March 21, 2006 MEP sets forth these economic objectives in greater detail and our plan for achieving them.

I. RECENT DEVELOPMENTS

2. **The economic outlook has deteriorated reflecting the global slowdown.** Growth is expected to slow to 1.6 percent during 2008. Inflation has been on an upward trend, reaching 8.2 percent in the 12 months to September 2008, mainly reflecting the impact of rising world fuel and food prices. Excluding food and fuel, inflation was 2.3 percent in the same period.

3. **External conditions are placing pressure on the balance of payments.** Stayover arrivals declined by 4.4 percent during January–September 2008 after strong Cricket World Cup-related performance in the first half of 2007, and are expected to slow further in the fourth quarter. Work on several FDI-financed tourism projects has been put on hold, due to financing difficulties. A U.S. airline began providing daily direct service to Grenada from Miami in November, and we have made some progress in attracting new airlines to take the place of two airlines that collapsed.

4. **The banking sector, which is dominated by subsidiaries of international banks which pool resources, is expected to remain resilient** notwithstanding the closure of the unregulated bank, the freezing of assets of an unregulated investment scheme, and adverse global conditions. Private sector credit growth has declined in recent months reaching 9 percent through September 2008, partly reflecting the slowdown in economic activity and remittances.

II. PROGRAM PERFORMANCE

5. **Reflecting the negative external shocks, spending pressures in the run up to the July elections, and unbudgeted retroactive wage payments, fiscal performance in the first half of 2008 deviated from the program projections.** The end-June primary deficit excluding grants (below-the-line) was 3.6 percent of annual GDP, exceeding the program target (reflecting adjustors) of 2.8 percent of GDP. Divestment proceeds financed most of the overall deficit.

- **Capital expenditure of 7.6 percent of annual GDP was significantly higher than the programmed 5.1 percent of GDP.** The overrun mainly reflected pre-election spending pressures, and included many nonrecurrent spending programs in the capital budget. Expenditure on some projects exceeded annual budgeted amounts.
- **The outturn for the current balance was slightly worse than programmed.** The first half-year revenue outturn exceeded projections by 0.6 percent of GDP. This was

largely due to overperformance on the consumption tax, which offset the impact of the reduction in May 2008 of the specific tax on gasoline from EC\$3 to EC\$2 per gallon. Current expenditure exceeded projections by 0.8 percent of GDP, due to unbudgeted retroactive wage payments and higher-than-expected transfers and subsidies.

- **Several small external debt service payments were paid with a slight delay, due to administrative difficulties.** These late payments breached our continuous zero ceiling on external payment arrears.

6. **We have made less progress with structural reforms than expected, and the implementation of most of our structural benchmarks for the second review will be delayed.** These delays largely reflect the change in government and schedule slippages by external consultants.

- On **customs reforms**, we signed a memorandum of understanding on information sharing between Customs and Inland Revenue in November 2008. This will facilitate implementation of the planned VAT. We have yet not developed and implemented a Fraud Control Plan, due to difficulties with external consultants.
- We are working to complete an **action plan to improve Doing Business Indicators**.
- We have been unable to develop **planning regulations** by the scheduled date, given problems with securing technical assistance. Given these difficulties and the improvement in construction practices since Hurricanes Ivan and Emily in 2004–05, we propose to drop this benchmark from the program.
- On the **investment incentives legislation**, a new Investment Policy Review Committee, approved by Cabinet and comprised of representatives from the GIDC, private sector, and the government, will review policy issues for the new Investment Code. Some revisions may result, but the main aspects of the framework—provision of capital write-offs rather than tax holidays as a transparent, nondiscretionary process for granting incentives—will remain. We have requested technical assistance from the IMF Legal Department—which is planned for December—in drafting sections of the new Investment Code.
- Furthermore, we reduced the fixed fuel tax from EC\$3 to EC\$2 per gallon in May 2008 and did not employ the automatic fuel price adjustment mechanism in July and September 2008. As a result, the government accumulated arrears to fuel price importers whose margins were eroded.

III. POLICIES FOR THE REMAINDER OF 2008 AND THROUGH 2009

7. **We are committed to strong, sound economic and fiscal management.** We intend to work to reduce our high public debt levels, through a determined effort, particularly at fiscal consolidation. Enhancing the business and investment environment, in partnership with the private sector is a key objective. We are committed to achieving these objectives,

including through implementation of our PRGF-supported program. The institutional framework to support reforms and changes in the culture of economic management are being supported by a major restructuring in the Ministry of Finance. The restructuring will include establishing Debt Management Unit, a Waste Reduction Unit, a Public Procurement Authority, and an Office of Private Sector Development.

Program Objectives for the Third Review

8. We have undertaken strong remedial measures to address the fiscal slippages and accumulation of domestic arrears in the first half of 2008.

- The Ministry of Finance, with approval from Cabinet, issued a finance circular in September 2008 that would limit capital expenditure in the second half of 2008 to EC\$50 million (2.8 percent of GDP), including through delaying until 2009 large locally-funded projects.
- We brought forward to September 20 the date after which no new commitments for nonessential expenditure items can be made.
- In October 2008, we also reinstated the EC\$3 per gallon fuel tax and resumed full passthrough of world fuel prices using the automatic mechanism. As a consequence, domestic retail gasoline prices increased from EC\$13.26 to EC\$15.65 per gallon.
- We have decided to resolve Capital Bank in a way that limits direct costs to the budget, and will not use the bank restructuring reserve of EC\$27 million (1.5 percent of GDP).

While these measures imply substantial adjustment in the second half, given expenditure overruns by the previous government, our target for the primary deficit (excluding grants) will be increased to EC\$110 million (6.2 percent of GDP). This implies a relaxation of EC\$36 million (2.0 percent of GDP) relative to the original program target, also adjusting for lower-than-expected bank restructuring costs and higher-than-expected grants. We are committed to meeting our revised program target and will take offsetting measures as needed in case of shortfalls in revenue and grants.

9. Nevertheless, recurrent expenditures for the second half are expected to remain high relative to the program target, on account of:

- The projection for payments for salaries and allowances in the second half has been raised to reflect retroactive payments to teachers of EC\$10.3 million.
- The projection for transfers and subsidies has been revised upward to reflect the impact of retroactive wage increases on pensions, and the difficulty of tightening social programs while the cost of living was rising rapidly.

10. Within the budget envelope described above, we have undertaken urgent measures to mitigate the rising costs of living. Households will be allowed to import two

barrels of foodstuffs duty-free until end-December 2008 with expected foregone revenue of EC\$2.6 million (0.1 percent of GDP). We have also introduced a free textbook program at a cost of EC\$5 million (0.3 percent of GDP) (classified under capital expenditure).

11. **We plan to reduce the large stock of domestic arrears older than 60 days.** These arrears declined from EC\$27 million (1.5 percent of GDP) at end-2007 to EC\$12 million (0.7 percent of GDP) at end-June 2008, but rose back to EC\$29 million (1.6 percent of GDP) at end-September 2008. We intend to reduce these arrears to EC\$25 million by end-2008. We have accumulated arrears to fuel importers resulting from incomplete passthrough of world fuel prices during recent years and have reached an agreement with these importers under which we agreed to remit back 50 percent of the fuel tax to reduce these claims, which we expect to clear in 2009. We do not expect to accumulate further arrears to importers in light of full passthrough of world fuel prices.

12. **We intend to proceed with introduction of a VAT.** We have reconstituted the VAT team and resumed preparatory work. We plan to announce in the December budget speech an introduction date that will allow sufficient time to allow businesses, consumers and government to prepare. The introduction date will be within the period October 2009 to February 2010. We will submit VAT and Excise bills to Parliament by April 2009 and recruit and begin training staff and adopting transitional procedures for bonded warehouses by May 2009. These will constitute structural benchmarks for the third and fourth reviews respectively. We have asked CARTAC to provide technical assistance building on earlier work.

13. **We intend to accelerate structural reforms focusing on tax and customs reform, economic management, and laying the groundwork for a poverty reduction strategy.**

- We will begin implementing a customs Fraud Control Plan by August 2009. This will provide for risk profiles as a basis for risk-based inspections, in conjunction with the introduction of ASYCUDA World.
- We are also moving forward with our work related to the new investment legislation and in this regard we have established a new Investment Policy Review Committee to review the legislation with stakeholders.
- Completing the Country Poverty Assessment (CPA) becomes more important as we consider ways to mitigate the impact of food and fuel shocks on vulnerable groups. The CPA will provide information to help improve targeting of social programs, and to develop a poverty reduction strategy that will be reflected in a full PRSP report. We will work with the World Bank, with the aim of finalizing the full PRSP by November 2009.
- We also plan to set up a new Debt Management Unit. The unit would improve debt recording, evaluate proposed external and domestic borrowing, develop a debt management strategy and undertake debt sustainability analysis. Technical assistance on the structure and operation of the unit will be requested from the IMF.

14. **We will proceed promptly with the resolution of Capital Bank, while minimizing costs to the government.** The process has been delayed by legal challenges by the bank's owner and the High Court's decision to revoke the appointment of the receiver. On September 18, 2008, we dropped our appeal of that decision, and revoked the bank's license and reappointed the receiver under a different a section of the Banking Act on the recommendation of the ECCB. We petitioned the High Court for liquidation on November 13, acting on the recommendation of the receiver and following consultation with the ECCB. The government will not provide any cash injection during the resolution but would entertain requests by potential investors for indirect support such as tax credits or placement of government deposits.

15. **We intend to proceed cautiously regarding a possible concessional loan from the Export-Import Bank of China to build a port and marina.** The previous government had considered a proposal of up to US\$85 million (13 percent of GDP). Such a large loan could, depending on its concessionality, undermine our objective of restoring debt sustainability. We would consider a smaller loan of around US\$5 million for a small marina project which would not go forward in the first half of 2009. If we proceed we will seek a high level of concessionality and explore nonguaranteed private sector co-financing.

16. **In light of Grenada's high public debt levels, we will prudently manage PetroCaribe concessional financing.** We will set aside 35 percent of PetroCaribe financing in the special account to ensure sufficient funds for repayment, and in January 2009 will raise this share to 40 percent. The remainder would be transferred to the budget as grants. We intend to broaden the range of fuel products imported under PetroCaribe as we develop the necessary infrastructure.

17. **We have approached our Paris Club creditors to seek debt relief for 2009 in line with the debt relief that the Paris Club extended in 2006–08.** We are continuing best efforts to conclude bilateral agreements with Paris Club (the Russian Federation) and non-Paris Club (Taiwan Province of China) creditors. We are seeking an out-of court-settlement with the Export-Import Bank of Taiwan Province of China. We are pursuing good faith efforts to reach a collaborative agreement with Grenada's external commercial creditors that did not participate in the 2005 debt exchange. We have cleared or restructured all but EC\$1.1 million arrears on unstructured domestic debt to the nonbank public incurred in June 2007. However, we incurred new arrears on 90-day Treasury bills held by domestic commercial banks, which stood at EC\$3.4 million at end-October 2008, and will complete clearing these arrears by the end of 2008.

Program Objectives for the Fourth Review

18. **Our 2009 budget will continue with fiscal consolidation needed to achieve debt sustainability.** An primary deficit target of 2.2 percent of GDP would be consistent with shifting gradually to small overall surpluses, in line with the objective of securing debt sustainability. Privatization proceeds expected from the Four Seasons project (EC\$45 million or 2.3 percent of GDP) will be used to finance this deficit and to reduce expensive debt and arrears. We now expect to reach the 60 percent debt-to-GDP target by 2019, still one year

ahead of the ECCB's 2020 benchmark for the region. Our framework anticipates the following policies:

- Maintaining the fuel tax at EC\$3 per gallon and continuing application of the automatic fuel price adjustment mechanism.
- Repealing from January 2009 the National Reconstruction Levy, a levy which was put in place in 2006 for period of 3–5 years, with a cost of EC\$10 million (0.5 percent of GDP).
- Intensifying the successful program of collecting tax and nontax arrears (which is expected to yield around EC\$12 million or 0.7 percent of GDP in 2008), while providing a tax amnesty through March 2009 in tandem with strengthened powers for seizing assets, garnishing income, and linking eligibility for government services to tax compliance.
- Reaching agreement on a wage path for public service workers for 2009–11 in line with projected inflation while taking into account the loss of national income from higher world fuel and food prices. We will also utilize the findings from the 2008 pay and grade study financed by the CDB.
- Adjusting travel allowances for public service workers, which had not been adjusted since 1990, at a cost of EC\$6.5 million (0.3 percent of GDP).
- Targeting capital expenditure of EC\$175 million (9.1 percent of GDP), and minimizing use of special warrants.
- Reducing spending on goods and services to EC\$75 million (0.4 percent of GDP), through bulk procurement internally and in cooperation with other ECCU members. The new Waste Reduction Unit in the Ministry of Finance is expected to achieve savings on fuel for government vehicles, fleet insurance and electricity costs.
- Reducing spending on transfers and subsidies to EC\$87 million (0.5 percent of GDP). The first stage of rationalization of social programs would yield savings of around EC\$4 million (0.2 percent of GDP), while protecting transfers to vulnerable individuals. Any increase in the monthly transfer to the elderly from EC\$150 per month would be financed by rationalization and would not increase the total cost of the assistance.

19. **The government believes that the policies and measures set forth above will be sufficient to achieve our fiscal targets.** We would undertake contingent measures if needed to reduce spending, including limiting grants and subventions while protecting vulnerable groups, and further rationalizing capital spending.

20. Our structural reform agenda will continue to focus on improving tax revenue policy, enhancing the business environment, and upgrading public financial management.

- A key objective is to improve Grenada's Doing Business Indicators. We are developing an action plan to improve specific indicators. Three priority areas have been identified: starting a business, registering property and facilitating trade. We will use the action plan to identify specific outcome targets and add one of these as a benchmark for fourth review.
- On tax policy, preparatory steps for introducing VAT (recruiting and training staff and adopting transitional procedures for bonded warehouses) will be the focus in 2009. In addition, we will move toward introducing a market-based property tax. We will complete the cadastral survey in December 2008 as a basis for reassessing the value of property. The new valuations would be applied beginning January 1, 2010.
- We plan to establish a Public Procurement Authority by September 2009, in order to realize gains in efficiency, uniformity of procedures, and savings for government purchases. We intend to implement several pieces of public financial management legislation enacted in 2007–08, including the Integrity in Public Life, Anticorruption, Public Financial Management, Audit, and Public Procurement and Contract Administration Acts. The latter provides for the establishment of a public procurement authority that would provide a framework for the procurement of all government purchases. We will also work with the World Bank to establish bulk procurement procedures with another OECS country, extending the existing successful procedure with pharmaceuticals to other products such as textbooks, agricultural inputs, fleet insurance and tires.

Program Monitoring

21. We are improving our capability to monitor economic developments and program performance. We will designate a Ministry of Finance official as the coordinator of Grenada's PRGF-supported program, with responsibility for overseeing the monitoring of macroeconomic and structural program targets. We have put in place a system of monthly monitoring of domestic arrears and below-the-line financing of the central government overall balance, and will update this on a monthly basis.

IV. OTHER ISSUES

Reducing Financial Sector and Natural Disaster Vulnerabilities

22. The Eastern Caribbean Securities and Regulatory Commission (ECSRC) issued cease and desist orders in May against two unregulated investment schemes in Grenada, one of which was already operating. We will not compensate investors in the scheme, which has not made payments since July. The scheme invested through an offshoot of a Jamaican scheme whose assets were frozen by the Turks and Caicos law enforcement authorities in July. The Grenada Authority for the Regulation of Financial Institutions

(GARFIN) will continue efforts to advise the public to invest only with licensed institutions, and will continue to advise any new parties interested in setting up a foreign exchange trading scheme not to start operations unless they are licensed by the ECSRC.

23. **We intend to further strengthen nonbank financial sector regulation and supervision, with continued technical assistance from CARTAC.** GARFIN, which has authority over insurance, nonbank financial institutions, money services, and international financial services, is pursuing an ambitious agenda of enhancing legislation, producing regulations, and developing and implementing supervisory practices (reporting, offsite and onsite monitoring) for each type of institution. The Money Services, Insurance, and Cooperative Society Acts will be submitted to Parliament in the first half of 2009.

24. **We will continue participation in the World Bank's Caribbean Catastrophic Risk Insurance Facility.** In June 2007, we began purchasing parametric insurance that pays the government a predetermined amount in case of hurricane or earthquake. An IDA credit has financed Grenada's insurance premium in the first two years and half the premium for the next year. We intend to seek donor support for the remaining half of the premium payments beginning in June 2009.

Fiscal transparency

25. **We are continuing our efforts to improve fiscal transparency.** We will disseminate to the public quarterly information with a lag of one quarter on the overall fiscal situation and gross financing needs starting May 2009 and publish information on public enterprise finances. In line with the new Public Financial Management Act of May 2007, we will require public enterprises to submit audited financial statements four months after the close of the financial year, as required by law. We will continue to publish newly granted or extended tax concessions within a month of granting these.

Table 1. Grenada: Quantitative Performance Criteria and Indicative Targets, 2008-09

	End-June 2008			End-Sept. 2008			End-Dec. 2008		2009	
	Unadjusted Target	Adjusted Target	Prel.	Unadjusted Target 1/	Adjusted Target	Prel.	Target	Proposed	End-March Proposed 1/	End-June Proposed
<i>Performance Criteria:</i>										
(In millions of Eastern Caribbean dollars)										
Central government primary balance excluding grants (floor) 2/3/	-45.0	-49.8	-63.3	-67.5	-50.8	-84.5	-90.0	-110.0	-11.3	-22.5
Stock of central government domestic arrears (ceiling)	15.0	15.0	12.4	11.0	11.0	28.9	7.0	25.0	20.0	15.0
(In millions of U.S. dollars)										
Contracting and guaranteeing of nonconcessional external debt by the central government with maturity of at least one year (ceiling) 2/	4.0	4.0	0.0	4.0	4.0	0.0	4.0	4.0	4.0	4.0
Stock of external short term debt (ceiling) 4/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Contracting and guaranteeing of bilateral concessional external debt by the central government with maturity of at least one year (ceiling) 2/5/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Central government or guaranteed external arrears accumulation (ceiling) 4/	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<i>Indicative Target:</i>										
(In millions of Eastern Caribbean dollars)										
Change in net credit of the banking system to the public sector (ceiling) 2/3/	12.0	14.2	9.9	18.0	31.1	12.9	24.0	24.0	0.0	0.0

1/ Indicative target.

2/ Cumulative within each calendar year.

3/ See the TMU and supplementary TMU for a description of adjusters.

4/ To be monitored on a continuous basis.

5/ Excludes PetroCaribe.

Table 2. Grenada: Structural Measures

	Target Date	Comment	Macroeconomic Criticality
Second Review			
Issue a finance circular reducing capital expenditure to EC\$184 million.	September 2008	Prior action. Met	To address fiscal slippages in the first half of 2008
Develop an action plan to improve Doing Business Indicators	August 2008	Benchmark. Not met	To create a more enabling environment for doing business by first identifying key steps to reduce bottlenecks identified in the World Bank's 2007 Doing Business Indicators
Bring into force new planning regulations, as a first step toward giving the Building Code force of law	July 2008	Benchmark. Not met	To reduce the vulnerability of the economy to natural disasters
Develop and begin implementing a customs Fraud Control Plan and sign an MoU on information sharing between customs and Inland Revenue	September 2008	Benchmark. Partially met. MoU signed November 2008	To enhance customs administration and revenue collection for sustainable financing of the budget
On Investment Act, amended Income Tax Act, and drafts to repeal tax incentives legislation, update with final policy decisions and obtain Cabinet approval	September 2008	Benchmark. Not met	To improve the investment climate and to reform the tax concessions regime
Third Review			
Reorganize or initiate liquidation of Capital Bank	November 2008	Performance criterion. Met	To increase confidence in the financial system by having a clear bank resolution strategy
Submit to Parliament the Investment Act, the amended Income Tax Act, and repeal of tax incentives	December 2008	Benchmark	To improve the investment climate and reform the tax concessions regime
Complete the Country Poverty Assessment	December 2008	Benchmark	To strengthen the ability of the government to develop effective and well-targeted poverty reduction measures
Establish a Debt Management Unit at the Ministry of Finance	February 2009	Proposed benchmark	To enable more effective debt management including better monitoring of payment obligations and effective debt sustainability analysis
Submit new VAT and Excise bills to Parliament	April 2009	Proposed benchmark	To increase the efficiency and effectiveness of revenue collection
Fourth Review			
Recruit and begin training staff and adopt transitional procedures for bonded warehouses	May 2009	Proposed benchmark	To ensure smooth implementation of the VAT
Develop and begin implementing a customs Fraud Control Plan	August 2009	Proposed benchmark	To enhance customs administration and revenue collection for sustainable financing of the budget
Establish a Public Procurement Authority	September 2009	Proposed benchmark	To enhance transparency and governance in procurement and facilitate donor monitoring
Implement a measure to be identified from the Action Plan to improve Doing Business Indicators 1/	To be specified	Benchmark to be specified	To further improve the investment climate

1/ Three priority areas have been identified. Once specific outcome targets (for example reducing by a specified amount the number of steps required to start a business) have been identified, a specific benchmark will be proposed at the time of the third review as a benchmark for the fourth review.

**SUPPLEMENTARY TECHNICAL
MEMORANDUM OF UNDERSTANDING**

The Technical Memorandum of Understanding (TMU) associated with the LOI and MEP of March 21, 2006, as modified by the Supplemental TMU of June 20, 2008, remains the operative document for monitoring and reporting requirements and for defining how the quantitative performance criteria and indicative targets, specified in Table 1 of the supplementary MEP, will be interpreted, except for the specific changes in the following:

Section II. Replace paragraph 10 with “The floor on the central government primary balance excluding grants will be adjusted as follows:

- (i) downward¹ to the extent that grants exceed programmed amounts, as specified in Table 1 below.
- (ii) upward to the extent that grants fall short of the programmed amounts, as specified in Table 1 below, by more than EC\$10 million through end-June or after.
- (iii) downward to the extent that concessional financing from multilateral development banks exceeds programmed amounts, as specified in Table 1.
- (iv) upward by an amount equivalent to 50 percent of the shortfall of divestment proceeds from the programmed amount, as specified in Table 1.
- (v) downward by an amount equivalent to 50 percent of divestment proceeds in excess of EC\$45 million, with a maximum adjustment of EC\$32 million. The remaining excess divestment proceeds will be used to pay down debt, targeting more expensive debt first.
- (vi) downward to the extent that bank restructuring costs exceed the programmed amount, as specified in Table 1, with a maximum adjustment of EC\$7 million.”

Section III. Replace paragraph 12 with

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

- (i) Upward to the extent that grants fall short of programmed amounts in Table 1 up to a limit of EC\$10 million;
- (ii) Upward to the extent that concessional financing falls short of programmed amounts in Table 1.”

Section IV. Replace the last sentence of paragraph 14 with

¹ Downward adjustment means a higher deficit; upward implies a lower deficit.

“The performance criterion on domestic arrears older than 60 days will not be monitored continuously but on an outstanding stock basis at the specified test dates.”

Table 1. Programmed Disbursements of Concessional Loans and Grants
and Bank Restructuring Costs, 2008-09
(In millions of Eastern Caribbean dollars, cumulative)

	2008	2009			
	Q4 Prog.	Q1 Prog.	Q2 Prog.	Q3 Prog.	Q4 Prog.
Concessional loans	49.0	2.4	4.7	7.1	9.4
Grants disbursements	78.2	15.5	31.0	60.6	76.1
Divestment proceeds	50.4	0.0	0.0	0.0	44.6
Bank restructuring costs	0.0	0.0	0.0	0.0	0.0

St. George's, Grenada
December 9, 2008

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Strauss-Kahn:

We have now submitted our draft 2009 budget to Parliament. Our budget speech is scheduled for December 12, and Parliament will approve the budget by the end of December. The draft budget represents an ambitious fiscal adjustment, and envisages reduction in the primary balance excluding grants from a projected 6.0 percent of GDP in 2008 to 2.7 percent of GDP in 2009. Reflecting some new information and consultations within the government that had been delayed, we have revised the draft budget relative to the parameters presented in our letter dated November 26, 2008. In particular, we have:

- Increased spending on transfers and subsidies by EC\$1.7 million to reflect recent increased demand by individuals to participate in existing government transfer programs, notwithstanding removal of ineligible persons from the transfer lists;
- Increased spending on goods and services by EC\$2.2 million, reflecting in part our plan to improve management of several large donor-financed housing programs under the new Ministry of Housing; and
- Increased capital spending by EC\$5 million in light of faster disbursements for an existing externally-financed project to build farm roads, and for new infrastructure spending to address recent damage by strong tropical rainstorms.

In addition, our more conservative projection of external grants is lower by EC\$4.8 million.

The draft budget remains consistent with our objective of undertaking fiscal consolidation to support restoration of debt sustainability, and we remain committed to achieving our program's targets.

We propose to revise our targets for 2009 on the primary balance (excluding grants) and on net credit to the public sector, as specified in the attached two tables in our Supplementary Memorandum of Economic Policies and Technical Memorandum of Understanding dated November 26.

Yours sincerely,

_____/s/_____
Honorable Nazim Burke
Minister of Finance, Planning, Economy,
Energy, Foreign Trade and Cooperatives

Table 1--SMEP. Grenada: Quantitative Performance Criteria and Indicative Targets, 2008–09

	End-June 2008			End-Sept. 2008			End-Dec. 2008		2009	
	Unadjusted Target	Adjusted Target	Prel.	Unadjusted Target 1/	Adjusted Target	Prel.	Target	Proposed	End-March Proposed 1/	End-June Proposed
<i>Performance Criteria:</i>										
	(In millions of Eastern Caribbean dollars)									
Central government primary balance excluding grants (floor) 2/3/	-45.0	-49.8	-63.3	-67.5	-50.8	-84.5	-90.0	-110.0	-14.0	-28.0
Stock of central government domestic arrears (ceiling)	15.0	15.0	12.4	11.0	11.0	28.9	7.0	25.0	20.0	15.0
	(In millions of U.S. dollars)									
Contracting and guaranteeing of nonconcessional external debt by the central government with maturity of at least one year (ceiling) 2/	4.0	4.0	0.0	4.0	4.0	0.0	4.0	4.0	4.0	4.0
Stock of external short term debt (ceiling) 4/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Contracting and guaranteeing of bilateral concessional external debt by the central government with maturity of at least one year (ceiling) 2/5/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Central government or guaranteed external arrears accumulation (ceiling) 4/	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<i>Indicative Target:</i>										
	(In millions of Eastern Caribbean dollars)									
Change in net credit of the banking system to the public sector (ceiling) 2/3/	12.0	14.2	9.9	18.0	31.1	12.9	24.0	24.0	6.2	12.5

1/ Indicative target.

2/ Cumulative within each calendar year.

3/ See the TMU and supplementary TMU for a description of adjustors.

4/ To be monitored on a continuous basis.

5/ Excludes PetroCaribe.

Table 1--STMU. Programmed Disbursements of Concessional Loans and Grants
and Bank Restructuring Costs, 2008–09

(In millions of Eastern Caribbean dollars, cumulative)

	2008	2009			
	Q4 Prog.	Q1 Prog.	Q2 Prog.	Q3 Prog.	Q4 Prog.
Concessional loans	49.0	2.3	4.7	9.3	14.0
Grants disbursements	78.2	12.9	25.7	52.7	65.5
Divestment proceeds	50.4	0.0	0.0	0.0	44.6
Bank restructuring costs	0.0	0.0	0.0	0.0	0.0