Program Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 27-Aug-2019 | Report No: PIDA26922

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Vanuatu	P168749	Vanuatu Disaster Risk Management Development Policy Grant with a Catastrophe-Deferred Drawdown Option (CAT-DDO) (P168749)	
Region	**Estimated Board Date**	**Practice Area (Lead)**	**Financing Instrument**
EAST ASIA AND PACIFIC	30-Oct-2019	Urban, Resilience and Land	Development Policy Financing
Borrower(s)	**Implementing Agency**		
Republic of Vanuatu	Ministry of Finance and Economic Management, Department of Strategic Policy, Planning and Aid Coordination		

Proposed Development Objective(s)

The Program Development Objective (PDO) is to enhance the Recipient's regulatory framework and institutional capacity to: (i) manage and reduce the risks from natural disasters and climate change; and ii) manage public debt.

Financing (in US$, Millions)

SUMMARY

Total Financing	10.00

DETAILS

Total World Bank Group Financing	10.00
World Bank Lending	10.00

Decision
The review did authorize the team to appraise and negotiate

B. Introduction and Context

Country Context

The proposed SDR yy million (US$10 million equivalent) stand-alone Disaster Risk Management (DRM) Development Policy Grant with a Catastrophe-Deferred Drawdown Option (CAT-DDO) supports the Government of Vanuatu's (GoV) program to reduce disaster and climate risk and better manage the socioeconomic and fiscal impacts of natural disasters. Disasters in recent years (e.g. 2015 Tropical Cyclone Pam) have shown the need for a comprehensive disaster risk management framework, with well-defined institutional roles and responsibilities for preparedness, *ex ante* risk reduction, and management of impacts. At the same time, the rapid growth of population and assets in hazardous areas necessitates stronger disaster risk reduction policies and regulations for resilient land and settlement development throughout the country.

As a very small remote economy that is highly vulnerable to climate change, disasters and external shocks, Vanuatu is subject to many of the constraints facing other Pacific island countries. The 279,000 residents of the Republic of Vanuatu live on an archipelago of 83 volcanic islands (72 of them inhabited) with approximately 12,200 square kilometers land area, dispersed over an exclusive economic zone of about 827,000 square kilometers. The economy is characterized by a formal sector driven by tourism and agriculture, and informal subsistence activity outside the main urban centers of Port Vila and Luganville. The small size of the domestic economy (GDP was estimated at US$880million in 2017) and its remoteness from major markets push up the costs of economic activity, as economies of scale cannot be realized in domestic production and transport costs significantly increase the cost of trade. Relatively fast population growth (due to high fertility rates and limited international migration opportunities) has meant that average annual per capita GDP growth has only been marginally positive over the past decade, with GDP per capita estimated at US$3356 in 2017.

Vanuatu is exposed to a variety of both hydrometeorological and geophysical disasters due to its location in the South Pacific tropical cyclone basin and the Pacific Ring of Fire. Hydrometeorological hazards include tropical cyclones, floods, and droughts, whereas geophysical hazards include volcanic hazards, earthquake-related hazards, and tsunamis. During the period 1980 to 2012, Vanuatu experienced approximately 53 disaster events (earthquakes - 46 percent, tropical cyclones - 35 percent) that affected around 300,000 people[1]. As at 2014, the cumulative effect of disaster loss on fixed capital was estimated at approximately 24 per cent of capital investment since 1970[2]. In March 2015, the Category 5 Cyclone Pam struck 22 islands of Vanuatu, causing estimated economic impacts in the amount of US$ 450 million, equivalent to 64 percent of GDP.[3] Catastrophe modeling conducted in 2010 estimated that, on a very long-term annual average, the country faces US$48 million per year in risk to assets from earthquakes and tropical cyclones alone. In the next 50 years, Vanuatu has a 50% chance of experiencing a loss exceeding US$330 million, and a 10% chance of experiencing a loss exceeding US$540 million.[4]

The macroeconomic policy stance is adequate overall, though there are a number of important risks that will be mitigated in part by the policy reforms supported by this operation. Growth is expected to remain broadly resilient in the medium term and despite projections of moderate fiscal deficits in the years ahead, the risk of debt distress in Vanuatu is assessed as remaining moderate, in contrast to several other Pacific island countries. Nevertheless, there are two overarching (and related) macroeconomic risks in the medium term: the risk of another large natural disaster, and the risk that new public debt is accumulated at a pace inconsistent with overall fiscal sustainability. These risks are

[1] Pacific Disaster Net. 2013. www.pacficdisaster.net.
[2] *Global Assessment Report on Disaster Risk Reduction 2015: Making Development Sustainable: The Future of Disaster Risk Management*. Geneva, Switzerland: United Nations International Strategy for Disaster Reduction, 2015.
[3] World Bank Group, 2015. Tropical Cyclone Pam Post Disaster Needs Assessment.
[4] PCRAFI Country Risk Profiles, September 2011.

mitigated by the DRM reforms supported by this operation, which should help facilitate ex ante measures to reduce the costs associated with natural disasters. They are also mitigated by the introduction of a revised Debt Management Strategy, which is a key component of the government's overall plans to consolidate its public finances and rebuild the fiscal buffers it needs to respond to disasters and other external shocks.

Relationship to CPF

This program is consistent with the World Bank Group's Pacific Islands - Regional Partnership Framework (FY17-FY21) [Report 120479] covering nine Pacific island countries, including Vanuatu. Specifically, it is in line with Focus Area 3: Protecting incomes and livelihoods, through its contribution to the achievement of Objective 3.1: Strengthened resilience to natural disasters and climate change. The program supports the World Bank Group's twin goals of ending extreme poverty and boosting shared prosperity. Poorer people are typically disproportionately affected by disasters for several reasons: (i) the poor and "bottom 40 percent" typically have inadequate financial means to deal with disaster events, (ii) in the face of more 'immediate' challenges (access to food, water, or livelihood), poor people have limited settlement options and are forced to live in lower-value hazard prone areas, and (iii) people just above the poverty line and vulnerable populations (children, women, elderly) can be pushed into transient poverty when a disaster hits. Accordingly, the contingent financing can be expected to benefit the most vulnerable and impoverished communities by strengthening the financial capacity of the government to respond and recover in a timely manner following a disaster, thus allowing poor communities to recommence their livelihood activities sooner.

The program will also complement recently completed and active DRM and climate adaptation projects and technical assistance activities in Vanuatu. These include investment projects such as the: (i) Mainstreaming Disaster Risk Reduction Project (P129376 – closed 2017), which supported hazard and risk mapping in the Greater Port Vila and Luganville areas, (ii) Increasing Resilience to Climate Change and Natural Hazards Project (P112611 – closed 2018), which supported community-based disaster risk management and the review of the National Disaster Act of 2000, (iii) Pacific Resilience Program (P155256 – active), which funded Vanuatu's catastrophe insurance premia from 2015-2018, and (iv) Vanuatu Infrastructure Reconstruction and Improvement Project (P156505 - active), which is reconstructing and upgrading public facilities and infrastructure in provinces affected by Cyclone Pam, as well as the Vanuatu Enabling Affordable and Resilient Settlements ASA (P157414 - closed).

C. Proposed Development Objective(s)

The proposed development objective is to enhance the Recipient's regulatory framework and institutional capacity to: (i) manage and reduce the risks from natural disasters and climate change; and (ii) manage public debt. This objective will be achieved through reforms under Pillar A: Managing and Reducing Disaster and Climate Risk, and Pillar B: Managing Public Debt.

Key Results

The main results expected from the operation are:

(i) a fundamental reorientation of the Government of Vanuatu's regulations and institutional system toward the full cycle of effective disaster risk management, shifting the focus from emergency management and response, to risk reduction, climate adaptation, and longer-term recovery;

(ii) the development of land and creation of new settlements to ensure affordable, resilient, environmentally and socially sustainable development and an improved quality of life for residents with minimum standards of disaster risk reduction; and

(iii) strengthened debt policy and management to assist in consolidating Vanuatu's public finances over the medium term, thereby rebuilding its capacity to respond to future natural disasters and external shocks.

D. Project Description

This proposed Disaster Risk Management (DRM) Development Policy Grant with a Catastrophe-Deferred Drawdown Option (CAT-DDO) supports the Government of Vanuatu's (GoV) program to reduce disaster and climate risk and better manage the socioeconomic and fiscal impacts of natural disasters. Disasters in recent years (e.g. 2015 Tropical Cyclone Pam, recurring volcanic activity on Ambae, Ambrym and Tanna islands) have shown the need for a comprehensive disaster risk management framework, with well-defined institutional roles and responsibilities for preparedness, *ex ante* risk reduction, and management of impacts. At the same time, the rapid growth of population and assets in hazardous areas necessitates stronger disaster risk reduction (DRR) policies and regulations for resilient land and settlement development throughout the country. This proposed stand-alone operation aligns with the national priorities set forth in the *Vanuatu Climate Change Adaptation and Disaster Risk Reduction Policy (2016-2030)* and the objectives of the *National Sustainable Development Plan (2016-2030)*, specifically Environment Goal 3 of a strong and resilient nation in the face of climate change and disaster risks posed by natural hazards. The operation's Pillars and Prior Actions are as follows:

Pillar A: Managing and Reducing Disaster and Climate Risk

The prior actions under Pillar A, and the associated results, will fundamentally strengthen the regulatory framework and institutional capacities for multi-hazard, *ex ante* DRM at national and local levels, and provide a comprehensive approach to risk reduction and climate adaptation in future land and settlement development throughout the country. The new Disaster Risk Management Act was developed to address the evolving understanding of: (i) the impacts of climate change, and (ii) management of risk, instead of treating disasters as exogenous shocks that cannot be proactively addressed.

The National Land Use Planning Policy of 2013 calls for appropriate and effective land use planning in the face of growing population and assets in hazardous areas, compounded by the impacts of climate change, and directs that risk and vulnerability assessment methodologies and information be formally integrated into the land use planning process, particularly in determining development controls and assessing development applications. The National Land Subdivision Policy provides the regulatory framework and institutional mandates to address these priorities.

Prior Action 1: *The Recipient's Council of Ministers has approved, and submitted to the Parliament, a Bill for the Disaster Risk Management Act, which provides for an integrated approach to disaster risk reduction and climate change adaptation, disaster preparedness, response and recovery at national and local levels.*

Prior Action 2: *The Recipient's Council of Ministers has approved a National Land Subdivision Policy, which provides for risk-informed land and settlement development, with minimum standards for disaster risk reduction.*

Pillar B: Managing Public Debt

The substantial increase in public debt after Tropical Cyclone Pam in 2015 has reduced the fiscal space available to the government to respond to future natural disasters. The debt management reforms supported by this operation are a critical component of the government's overall plans to consolidate its public finances and rebuild the fiscal buffers it needs to respond to disasters and other external shocks.

Prior Action 3: *The Recipient's Council of Ministers has approved the Debt Management Strategy 2019-2022, which contains measures to minimize the costs and risks associated with the Recipient's public debt, and sets out plans to strengthen the Recipient's public debt management.*

E. Implementation

Institutional and Implementation Arrangements

The Ministry of Finance and Economic Management is the main counterpart of the World Bank for this development policy operation, while the implementation of the policy program will be coordinated and monitored by the Department of Strategic Policy, Planning and Aid Coordination attached to the Prime Minister's Office. The 3-year drawdown period will coincide with the monitoring of the operation's Policy and Results Matrix, with indicators that reflect the expected outcomes of the prior actions (in line with the monitoring and evaluation framework of the National Sustainable Development Plan).

Policy dialogue and monitoring and evaluation of the program are shared with the relevant actors under the Policy and Results framework. The government and the Bank will maintain a close policy dialogue during the program implementation period, through periodic implementation support missions that may take place at a frequency consistent with the needs of the counterparts, but no less than every 6 months. Indicators selected to monitor progress toward achievement of the PDO reflect defined areas of action and correspond to the expected outcomes of the prior actions, and are aligned with government priorities.

F. Poverty and Social Impacts and Environmental Aspects

Poverty and Social Impacts

The disproportionate impact of natural disasters on the poor has been extensively documented in Vanuatu. The country faces long-term average annual asset risk of approximately 7 percent of GDP, consisting of the cost to repair or replace damaged assets including homes, vehicles, roads and bridges, etc. However, these aggregated asset losses do not show how people's livelihoods are affected, especially the prospects of the poorest and most vulnerable (well-being risk). For the poor, even small absolute values of asset loss can disproportionately affect livelihoods, reducing income and making it even harder to rebuild lost homes and productive assets. The poor have few assets, and little or no savings. They have little opportunity for risk diversification and restricted access to credit. Because of this, they are less able to cope with impacts on consumption or disruptions to income. Exogenous shocks like disasters can also increase poverty indirectly through the effects of lower economic growth, higher inflation (to which the poor are more vulnerable), and through resulting lower government spending for social services. Households living close to the poverty line can be pushed into poverty as a result. Prior Action 1 will strengthen the regulatory and institutional systems to enable more effective, faster recovery, which has been found to significantly reduce well-being risk in Vanuatu.[5]

One of the key principles of the National Land Subdivision Policy (Prior Action 2) is that the regulation and approval of land subdivision applications must take into consideration the affordability of (part of) the proposed development for low-income households. Provisions are made for higher-density subdivision layouts and the setting aside of land for lower-income groups to increase affordability, more cost-efficient site planning and service provision, and appropriate minimum infrastructure service standards for all subdivision developments (including those targeted to low-income households).

The poorest quintile of households in Vanuatu is more vulnerable than other quintiles to any contraction in the provision of essential public services that may result from external shocks if the government lacks adequate fiscal

[5] World Bank and Global Facility for Disaster Reduction and Recovery. World Bank 2018, *Building back better: achieving resilience through stronger, faster, and more inclusive post-disaster reconstruction. Washington, D.C.: World Bank Group.*

buffers. It is thus particularly important to poor people and vulnerable groups that the government maintains the capacity to provide public services over time, which in turn depends on the maintenance of fiscal stability. The reforms to debt management and policy supported by this operation are expected to have positive impacts on the poor, to the extent that they assist the government in its efforts to consolidate its public finances and build fiscal buffers.

Environmental Aspects

The policy actions proposed under the operation are likely to have positive effects on Vanuatu's environment, natural resources or forests, relative to the status quo. The actions, which include implementation of the Disaster Risk Management Act and application of the National Land Subdivision Policy, will improve risk reduction, preparedness, response and recovery from natural disasters and are not associated with activities that will impact the environment or natural resources. The Subdivision Policy is expected to have positive environmental impacts associated with future development, via integration of environmental considerations in the subdivision approval, design and implementation process.

The GoV has in place environment and natural resources management laws that provide for sustainable utilization and conservation of the environment and natural resources. The primary legislation is the Environmental Protection and Conservation Act, administered by the Department of Environmental Protection and Conservation. The act requires environmental assessment to be undertaken for any activity likely to impact on the environment and is referred to in the National Land Subdivision Policy. The framework for environmental assessments has been mainstreamed into the development process and for specific projects (including post-disaster reconstruction), and the Strategic Environmental Assessment (SEA) is required for sectoral plans and programs. More effective environmental management, including the adoption of eco-based adaptation and risk mitigation measures that work with natural systems, will be informed by the mainstreaming of DRM in the development process through Prior Actions 1 and 2.

G. Risks and Mitigation

The overall program risk rating is Substantial, based on substantial political and governance, macroeconomic, fiduciary, and institutional capacity risk as detailed below. Sector strategies and policies pose moderate risk, as the government has shown strong leadership by integrating the DRM and CCA agenda in the National Sustainable Development Plan and convening extensive public consultations around the prior actions. The substantial risks remain to be:

a. political risk, which has had an impact on the passage of the Council of Ministers-approved Bill for the DRM Act, due to unrelated motions of no confidence in December 2018 and June 2019. The impact of this risk on achievement of the operation's objectives will be mitigated through targeted technical assistance to support progress toward achievement of the result indicators;

b. macroeconomic risks related to future natural disasters and the public debt trajectory (to the extent that large new loans are taken on by the government at unfavorable terms);

c. fiduciary risks related to post-disaster public financial management and audits; which will be mitigated by targeted technical assistance to support the development of key guidelines for the use of post-disaster funding; and

d. the effective long-term implementation of reforms given constrained institutional capacity. This is being mitigated by the strong anchoring of the reforms in the Climate Change and Disaster Risk Reduction Policy, as well as the corporate plans of the relevant ministries. This agenda also has strong support from the Council of Ministers, and public pressure for better disaster risk management is significant due to the frequency and intensity of disasters in Vanuatu.

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APPROVAL

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