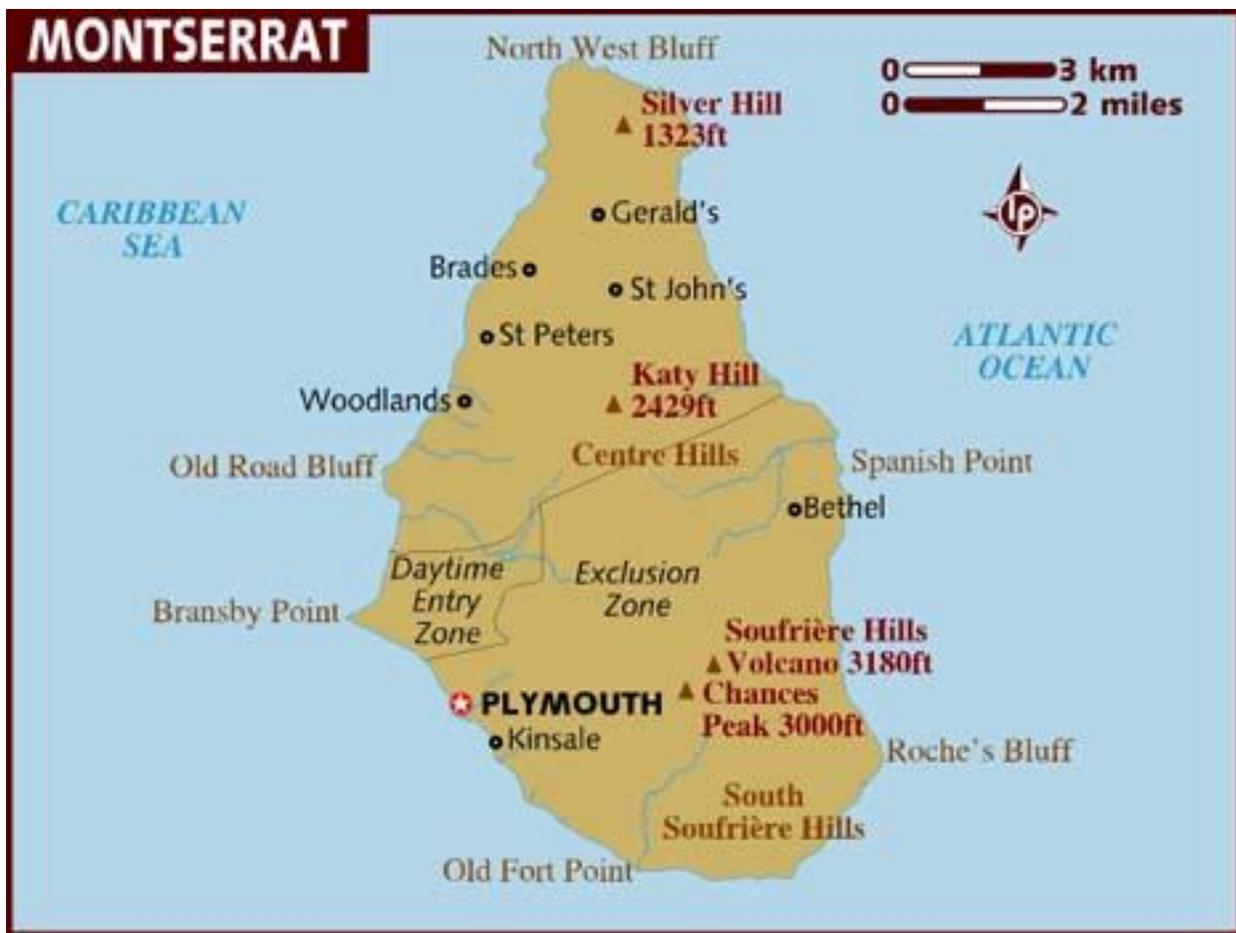




# Single Programming Document of Montserrat

## 10<sup>th</sup> European Development Fund



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## **PART A: COOPERATION STRATEGY**

### **LIST OF ABBREVIATIONS**

ACP	African Caribbean and Pacific
BNTF	Basic Needs Trust Fund
CARICOM	Caribbean Community
CDB	Caribbean Development Bank
CDERA	Caribbean Disaster and Emergency Response Agency
CEDA	Caribbean Export Development Agency
COTGAR	Caribbean Overseas Territories Government Accounting Reform
CPP	Country Policy Plan
CSME	Caribbean Single Market and Economy
CTO	Caribbean Tourism Organisation
CXC	Caribbean Examinations Council
DfID	Department for International Development
EBAS	European Business Assistance Services
ECCB	Eastern Caribbean Central Bank
ECTEL	Eastern Caribbean Telecommunications
EC\$	East Caribbean Dollar
EDF	European Development Fund
EPA	Economic Partnership Agreement
EU	European Union
EUR	EURO Currency
FCO	Foreign and Commonwealth Office
GDP	Gross Domestic Product
ICT	Information and Communications Technology
IMF	International Monetary Fund
MCCI	Montserrat Chamber of Commerce and Industry
MDC	Montserrat Development Corporation
MDG	Millennium Development Goals
MTB	Montserrat Tourist Board
MVO	Montserrat Volcano Observatory
NGO	Non-Government Organisation
NTSP	National Tourism Strategy and Plan
OCT	Overseas Countries and Territories
OECD	Organisation for Economic Co-operation and Development
OECS	Organisation of Eastern Caribbean States
PEFA	Public Expenditure and Financial Assessment
PDP	Physical Development Plan
PPA	Participatory Poverty Assessment
PSD	Private Sector Development
PSF	Petroleum Stabilisation Fund
SDP	Sustainable Development Plan
SPD	Single Programming Document

TSSP	Trade in Services Support Programme
UK	United Kingdom
UWI	University of the West Indies
WTO	World Trade Organisation

The Government of Montserrat and the European Commission hereby agree as follows:

- 1) The Government of Montserrat (represented by the Premier of Montserrat, Mr. Reuben Meade), and the European Commission, (represented by Mrs. Jolita Butkeviciene, Director of Latin America and Caribbean Directorate of the Directorate-General for Development and Cooperation – Europaid), hereinafter referred to as 'the parties', held discussions with a view to determining the general approach to cooperation between Montserrat and the European Union.

During these discussions this Single Programming Document was drawn up in accordance with the provisions of the association of the Overseas Countries and Territories with the European Union, as provided for in the treaty on the Functioning of the European Union, in particular Article 198, as well as the council decision 2011/822/EC of 27 November 2001 on the association of the Overseas Countries and Territories with the European Union.

- 2) The agreement of the two parties on this Single Programming Document, will be regarded as definitive within eight weeks of the date of the signature, unless either party communicates the contrary before the end of this period.

Done at Brussels

For the Government of Montserrat

For the European Commission

Date

Date

Place

Place

## EXECUTIVE SUMMARY

### **National development strategy**

Montserrat is a United Kingdom Overseas Territory in the Caribbean and since the start of the volcanic crisis Montserrat has relied on and benefited from budgetary aid from the UKG. The Sustainable Development Plan (SDP), the Sustainability Roadmap and the Country Policy Plan (CPP) - which sets out how the UK will contribute to achieving policy objectives and promote development in Montserrat - make up the framework for development assistance and cooperation between the Government of Montserrat and the Government of the United Kingdom and that framework informs the Cooperation Strategy between the EU and Montserrat.

### **EU response strategy**

Based on the analyses of Montserrat's challenges, the government's development strategy, and programmes by other international development partners, in particular DFID and taking into account the EU's comparative advantages and strengths, the EU response was drawn up and intends to continue to focus on the following area of support:

**General Budget Support** is the program to be implemented under the 10th EDF allocation, which amounts to EUR 15.66 million. It is highly complementary with the EU financed programmes under the 9th EDF allocation, as well as with DFID's framework of assistance. The **overall objective** of this general budget support programme is to support implementation of Montserrat's Sustainable Development Plan (SDP) and the Sustainability Roadmap thus contributing to the recovery and sustainable development of Montserrat. The specific objectives are (i) to support creation of an environment that fosters prudent economic management, sustained growth, a diversified economy and the generation of employment opportunities; (ii) to support development of an efficient, responsive and accountable system of governance and public service.

Through the 10th EDF allocation for Montserrat, the EU is supporting a 12-year strategy (Montserrat's Sustainable Development Plan lasts from 2008 until 2020), which is formulated on the basis of previous support focused on physical improvements and developments. The aim of this programme is on the improvement of the public administration, without which the long term strategy cannot be fully implemented.

The programme will also have a Technical Assistance (TA) component supporting implementation of Public Finance Management and Civil Service reforms.

## Chapter 1: EU cooperation objectives

In accordance with Article 198 of the Treaty on the Functioning of the European Union (TFEU), the purpose of the association between the European Union and the Overseas Countries and Territories shall be *“to promote the economic and social development of the countries and territories and to establish close economic relations between them and the Union as a whole”*. These objectives have been confirmed and further developed in the consecutive Council Decisions on the association of the overseas countries and territories (OAD) with the European Community<sup>1</sup>.

Since 2007 the European Union and the OCTs have been engaged in a reflection process, with a view of modernising the OCT-EU association. The purported aim of this process, which should culminate in a revised OAD, to be implemented as of 1 January 2014 onwards, is to define a partnership based on mutual interests, reciprocity, rights and obligations. This implies that one moves away from the classic development cooperation approach to adopt a reciprocal partnership in support the OCTs' sustainable development, and whereby OCTs are expected to contribute to the promotion of European values in the wider world.

A first highlight was the publication in June 2008 of a Commission Green Paper on the future of the OCT-EU relations, followed by a Commission Communication in November 2009 regarding key elements of the future OCT-EU relations.<sup>2</sup> The latter identifies three central objectives for the renewed OCT-EU association:

- 1) to enhance OCT competitiveness;
- 2) to strengthen OCT resilience and reducing their vulnerability;
- 3) to promote cooperation.

The Communication also indentified five intertwined principles and axes for cooperation:

- a) to stimulate OCT development as centres of excellence and expertise;
- b) to stimulate the upgrading of OCT legislation in relevant policy fields as well as to encourage convergence with EU rules and standards;
- c) to assist the OCTs in the formulation and development of environmental and disaster risk reducing policies;
- d) to help OCTs with linking up to the outside world and improve their accessibility by upgrading their infrastructures;
- e) to continue to offer the OCTs a favourable access to the EU market and assist them in their adjustment to the changing global trade and economic environment.

The OCT/EU association framework and the territorial policy agenda presented in Chapter 3 constitute the starting point for this Single Programme Document, in accordance with the principle of territorial ownership of development strategies. 10<sup>th</sup> EDF aid to Montserrat aims to provide support to the implementation of Montserrat's Sustainable Development Plan (SDP) and the Sustainability Roadmap thus contributing to the recovery and sustainable development of

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<sup>1</sup> The Decision currently in force is Decision 2001/822/EC of the Council of 27 November 2001 on the association of the overseas countries and territories with the European Community, OJ L 314, 30.11.2001, p. 1. Decision as amended by Decision 2007/249/EC (OJ L 109, 26.4.2007, p. 33).

<sup>2</sup> Commission Green Paper COM (2008) 383 final of 25 June 2008 on Future Relations between the EU and the Overseas Countries and Territories; and Communication COM (2009) 623 final of 6 November 2009 from the Commission to the Parliament, the Council, The European Economic and Social Committee and the Committee of the Regions, Elements for a new partnership between the EU and the overseas countries and territories (OCTs).

Montserrat. The specific objectives are (i) to support creation of an environment that fosters prudent economic management, sustained growth, a diversified economy and the generation of employment opportunities; (ii) to support development of an efficient, responsive and accountable system of governance and public service.

According to Article 4(3) of Implementing Regulation No 2304/2002<sup>3</sup> EU support to OCTs is in principle given in the form of budget support, except for exceptional and duly justified cases. Montserrat fulfils all the necessary eligibility conditions for budget support: (1) the existence of a territorial development plan which has been adopted and in the course of implementation; (2) a stable macro-economic framework; and (3) a credible program of public finance management.

## **Chapter 2: Assessment of the political, economic, social and environmental situation**

### *2.1 Political situation*

Montserrat is an internally self-governing Overseas Territory of the United Kingdom. Montserrat is a stable parliamentary democracy and its system of governance rests on three pillars – executive, legislative and judicial. There is an Executive Council, presided over by the Governor and comprising the Governor, the Chief Minister, and three other ministers, as well as the Attorney-General and the Financial Secretary, who serve as *ex-officio* members. The Legislative Council is made up of nine elected members and a Speaker. The Attorney-General and the Financial Secretary also sit on the Legislative Council.

Montserrat continues its tradition of free and fair multi-party elections with the active participation and success of independent candidates. The most recent general elections were held on September 9, 2009, where the nine seats for the Legislative Council were contested by three parties and 3 independent candidates. A government was formed under the Movement for Change and Prosperity (MCAP) led by Chief Minister Reuben Meade.

Montserrat, whose legal system is based on English common law, is one of the jurisdictions that share the Eastern Caribbean Supreme Court headquartered in St. Lucia. Montserrat shares a Resident High Court Judge with Anguilla, although other Judges are available for sittings when the circumstances warrant. Appeals from the High Court are heard by the Eastern Caribbean Appeals Court with the final appeal to the Privy Council in London.

### *2.2 Economic situation*

#### 2.2.1 Economic structure and performance

Montserrat is an open and dependent micro-economy with few natural resources. Its current population of 5,039 represents a market size that is too small to stimulate significant local production for mainly local consumption and therefore the country relies on imports to meet

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<sup>3</sup> Commission Regulation (EC) of 20 December 2002 implementing Council Decision 2001/822/EC on the association of the overseas countries and territories with the European Community (OJ L 348, 21.12.2002), as amended by Commission Regulation (EC) No [1424/2007](#) of 4 December 2007 amending Regulation (EC) No [2304/2002](#) implementing Council Decision [2001/822/EC](#) on the association of the overseas countries and territories with the European Community and allocating the indicative amounts under the 10th European Development Fund (OJ L 317, 5.12.2007).



**Table 1a: Montserrat**  
**Rate of growth of gross domestic product at basic prices in constant prices**

SECTOR	2003	2004	2005	2006	2007	2008	2009
Agriculture	(0.84)	(18.64)	(12.50)	15.48	2.68	24.47	30.11
Crops	(14.29)	(30.56)	(8.00)	69.57	(46.74)	12.75	55.00
Livestock	4.08	(15.69)	(58.14)	0.00	170.10	43.73	33.00
Forestry	0.00	0.00	0.00	0.00	0.00	0.00	2.00
Fishing	13.04	(11.54)	65.22	(7.89)	(27.97)	1.82	5.00
Mining & Quarrying	0.00	80.00	88.89	276.47	158.75	(5.07)	0.50
Manufacturing	0.00	0.00	44.23	(10.00)	0.50	6.56	1.50
Electricity & Water	3.45	(2.67)	10.96	2.47	0.99	1.14	(0.00)
Construction	(15.68)	2.36	1.06	(33.77)	(11.72)	3.30	7.00
Wholesale & Retail Trade	(3.42)	0.35	2.83	(1.72)	(6.32)	22.54	(7.50)
Hotels & Restaurants	(31.58)	33.85	31.03	(7.89)	13.40	9.46	(22.00)
Transport	6.78	3.17	(0.22)	7.19	(1.23)	5.09	(6.33)
Road Transport	11.31	8.20	(0.61)	9.15	0.28	3.59	(2.00)
Sea Transport	1.63	(9.60)	(4.42)	(3.70)	(8.59)	11.25	(18.00)
Air Transport	(31.25)	9.09	50.00	36.78	7.95	3.25	(20.00)
Communications	(1.41)	1.64	(1.81)	0.82	4.63	1.57	(1.00)
Banks & Insurance	8.76	10.18	9.38	(3.28)	21.89	7.40	1.00
Real Estate & Housing	4.47	1.68	2.01	5.57	0.83	1.02	2.00
Government Services	3.96	5.23	(4.92)	4.47	6.83	5.37	2.00
Other Services	(0.64)	8.60	4.75	(0.57)	6.19	6.12	1.00
Less Imputed Service Charge	(3.40)	1.76	18.04	4.23	32.26	6.16	1.00
TOTAL	(0.92)	4.45	(0.35)	(3.99)	2.92	5.41	0.99



### National output

As illustrated in Table 1, the economic performance of Montserrat continues on a slow path of recovery following more than 10 years of volcanic activity. Prior to the start of the volcanic crisis in 1995 Montserrat had a balanced and sustainable economy with growth rates averaging 5% in the early 1990s. Since the volcanic crisis, economic growth has been uneven. The Montserrat economy experienced a long period of decline during the second half of the 1990s and recorded positive growth for the first time in six years in 2002. This was followed by another decline in 2003, growth in 2004 and again by declines in 2005 and 2006. However, economic activity picked up in 2007 and 2008 but slowed to an increase of 1% (constant dollars) in 2009, underpinned by lower construction activity in both the public and private sectors. For the past ten years, Government services and construction has dominated economic activity in Montserrat. These two sectors now account for approximately 37% and 11% of GDP, respectively.

### Tourism

The tourism sector is seen as contributing to GDP growth, employment generation and foreign exchange earnings. However, tourism (hotels and restaurants), which was once the mainstay of the economy, accounted in 2009 for only 1.6% of GDP as compared to 20% in the pre-volcanic crisis period, significantly reducing revenue gains from this sector. Tourism still depends largely on the rental of vacation homes and there are presently 65 rental villas available. Hotel accommodation once also formed an important part of Montserrat's tourism but there is now only one 18-room hotel in operation along with 3 guest houses.

The number of stay-over visitors in 1994, before the volcanic crisis, was 21,000. After a significant decline in the late 1990s, the tourism sector began to recover. Tourist arrivals in 2002 numbered approximately 15,000. However, there was a setback due largely to the uncertainty of volcanic activity and the limited access to the island when the ferry service ended in 2005. These factors along with the onset of the global recession in 2008, may explain why visitor arrivals declined to below 10,000 between 2005 and 2009.

### Agriculture

Agriculture in Montserrat involves small-scale production of fruits, vegetables, eggs and meat for the local market and it now accounts for only 2.53% of GDP. The area of land under cultivation was drastically reduced after the volcanic crisis and activity is now concentrated in the north. Most of the food in Montserrat is imported which contributes to the negative trade balance.

### Mining and quarrying

As there is an abundance of sand and gravel in Montserrat, businesses are able to supply these materials to meet local and overseas demands. In fact, due to ongoing construction activity and the volcanic crisis, the mining and quarrying sector has assumed growing importance in recent years. The data on mining and quarrying activity indicates that the sector grew from a negligible 0.1% of GDP in 2002 to approximately 2.48% of GDP in 2009. However, owing to the world economic crisis, growth in the sector slowed to 0.5% in 2009 after registering triple digit growth in 2008.

### Offshore services

The contribution of offshore services such as medical education and offshore finance which were once considered important areas of economic activity is now negligible. The regulatory framework and legislation to ensure that the industry is conducted and regulated in line with international standards remain in place. Montserrat's economy had gained tremendous benefits from the presence of an offshore medical school prior to the volcanic eruptions. Two new offshore medical schools recently obtained permission to set up but they have not yet started their operations. While the contribution of the offshore sector to the economy is currently small, the government is of the view that this sector has considerable potential for future growth.

### Information and communications technology

The communications sector averaged 8% of GDP between 2003 and 2009, driven by investment in modern communications infrastructure. The formation of the ICT Task Force and the adoption of the ICT policy have positioned Montserrat to become a competitive knowledge-based destination in a global market, serve as a catalyst for private sector growth, and meet future demand for telecoms services.

The 2001 census found that 1500 households (75%) in Montserrat have telephone connections. It is estimated that there are 400-500 mobile phone customers. The census also found that 366 households possessed a computer and 300 of these had internet access. All government offices have both telephone and computer facilities. All businesses have telephones and a high percentage of them have computers with internet connections. It is expected that these figures will show an increase when the next census is undertaken in 2011.

There are a small but growing percentage of relatively highly skilled technical personnel operating not only in the field of communication but also in the area of information technology. This represents a core group that could readily be expanded to meet the needs of a growing ICT sector in Montserrat. Such an expansion may be achieved through the recruitment of additional regional personnel as well as through the return of trained and experienced Montserratians residing overseas.

### Labour and employment

The structure of the labour force continues the change that began with the volcanic crisis. While a large number of Montserratians now rely on government for work and the government remains the island's single largest employer, the proportion of public sector employment has declined in recent years as private sector activity increases. In addition, the sizeable influx of Caribbean citizens into the labour force, together with the return of Montserratians from abroad, has shown that the potential labour force is far greater than the present actual size. This is a key factor in assessing the availability of the human resources necessary to bring about sustained economic growth in Montserrat.

It is estimated that the population of Montserrat at the end of 2009 stood at 5,039, representing a 5.6% average annual increase from 2002, while Montserrat's labour force in March 2006 grew to 3,005, an increase of 48% from 2001. It is estimated that since 2001, the unemployment rate remained fairly stable at approximately 13.7%. Even with double digit unemployment, there is

still an acute shortage of skills. This has been partly remedied by the influx of migrant workers, including from other Caribbean countries. However, it still remains an issue.

Public sector employment declined from 872 in 2001 to approximately 835 persons in 2007, about 27% of the working population. However, statistics on the government sector indicate that employment in the public sector may have increased in 2009, as government employed additional staff in some ministries. Approximately, 60% of the workforce are either employed by the private sector or are self-employed.

#### Private sector development

The growth of the Montserrat private sector and the development of tourism are inextricably intertwined and they continue to be the focus of the government's efforts to consolidate economic recovery and sustained growth. In order for this to happen, the government has been putting in place the necessary legislative and institutional framework and the physical infrastructure to support private sector led growth, especially in tourism. As such, the development of Little Bay Town Centre and the expansion of the port are seen as catalysts for private sector development.

The new airport at Gerald's should eventually have a significant impact on economic growth. However, the short-term impact of the airport has been uneven as tourist arrivals have declined and the airport has not offset the loss of visitors occasioned by the suspension of the ferry service in 2005, due to a variety of factors including natural hazards and technical constraints. The airport investment is expected in the long-term to generate increased private sector activity as well as complement and support other economic initiatives pursued by the government. Together with the development of a well organised, efficient and thriving tourism and commercial centre at Little Bay, the tourism and private sector initiatives taken together should produce improvements in economic performance over the medium to long-term. The assessment is that the Montserrat economy is likely to grow at an average of no more than 3% over the next three years. This projection is framed within the context of the current sluggish global and regional economic environment but takes into consideration a number of planned projects, primarily the Port Development Project and Little Bay Town Centre Project as well as expected growth in key sectors (construction, tourism and mining) over the next three years.

#### 2.2.2 Trade and regional integration

Montserrat is a member of the Caribbean Community and Common Market (CARICOM), the Organisation of Eastern Caribbean States<sup>4</sup> (OECS) and the Caribbean Development Bank (CDB), regional institutions that foster intra-regional integration and trade.<sup>5</sup> Montserrat's main trade partners are the United States, the United Kingdom and CARICOM countries. Prior to the volcanic crisis, Montserrat's small light manufacturing sector benefitted from the access it had to the European market as an OCT.

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<sup>4</sup> Member states include: Anguilla, Antigua & Barbuda, British Virgin Islands, Commonwealth of Dominica, Grenada, Montserrat, St. Lucia, St. Christopher (St. Kitts) & Nevis, St. Vincent & the Grenadines.

<sup>5</sup> There are in principle no restrictions to the membership in relations to the membership of CARICOM, concerning impacts on the EU trade regime.

Under Part IV of the TFEU, notably Articles 199 and 200, and the OAD, the EU offers OCTs a single, comprehensive, unilateral and asymmetric trade regime. This means that OCT exports to the EU benefit from a duty free and quota free (DFQF) access to the EU market while EU exports to OCT markets may still be subjected to both duties and quantitative restrictions. For the purposes of the OAD, all OCTs are considered to form a single customs territory.

### 2.2.3 Monetary performance

Montserrat is a member of the Eastern Caribbean Central Bank (ECCB) and therefore shares a currency union with other OECS countries. The regional currency is the Eastern Caribbean Dollar (EC\$), which is pegged to the United States Dollar at the fixed rate of EC\$2.70. The currency has maintained a strong level of stability and the exchange rate has remained the same for more than twenty-five years. The ECCB carries out monetary policy as determined by its regional Board of Governors, on which Montserrat is represented. The focus of ECCB policy is to maintain a strong currency that contributes to a stable economic and investment climate. Montserrat requires UK approval prior to undertaking internal financial commitments.

### 2.2.4 Public finances

#### *Fiscal performance*

Prior to the volcanic crisis, Montserrat managed to record strong fiscal performances. Indeed in the early 1990s, Montserrat, on average, ran an annual budget surplus of EC\$5.6 million. Since then however, it has not yet been able to fully recover its fiscal health. Montserrat's budget operations, closely monitored by the UK in conjunction with the government, are prudently managed but the circumstances in which it operates remain daunting as the government has lost its most important tax base. The UK has therefore had to finance the resulting budget deficits which in 2007 amounted to EC\$58 million or 62% of recurrent expenditure. The UK's annual budgetary support over the last 6 years averaged 64% of expenditure. Therefore, the adoption of measures aimed at reducing the budgetary deficit over time has been the dominant theme in negotiations relating to budgetary aid.

Between 2005 and 2009, the current account has averaged an annual deficit of EC\$52.6 million as the government has had to expend more on goods and services, transfers and personal emoluments. The trend has been for the deficit to increase as revenue has not kept up with expenditure. As such, the deficit is no longer expected to be substantially reduced by 2012 as was earlier thought but rather by around 2014. Nonetheless, Montserrat's public debt remains at sustainable levels and at 6.4% of GDP, it is well within the target established by the ECCB.

#### *Public finance management assessment*

In March 2010 Caribbean Regional Technical Assistance Centre (CARTAC) conducted a PEFA exercise for the Government of Montserrat. Additionally, a Fiduciary Risk Assessment, based largely on the PEFA assessment, concluded that there is a moderate to substantial risk for UK financed budget support operations.

Summary of Montserrat's PFM system, based on the 6 pillars of PEFA methodology, is provided below.

The government generally scores well on the budget credibility dimension since total spending and the composition of spending are close to the approved budget, supported by the financial discipline asserted by the Ministry of Finance and a good revenue performance. The classification of the budget is reasonably robust, but the Comprehensiveness and Transparency of the information included in the budget documents is minimal.

On Policy Based Budgeting, the budget process (recurrent and development) in Montserrat does not follow a specific invariable written calendar. However, each year the Budget Circular indicates a time schedule for the main milestones for budget preparation dictated by MOF internal management requirements. The existence of a multi-year strategic plan (SDP), including a costed Sector Investment programme, is a strong contributor to the process of strategically allocating resources.

With regards to Predictability and Control in Budget Execution, while the degree of transparency in taxpayer obligations, and effectiveness of taxpayer registration and tax assessment is good, it is recognized that these procedures could be improved by strengthened IT systems. Predictability in the availability of funds for commitment of expenditure is good. Recording and management of cash balances, debt and guarantees is fairly good. Payroll controls are effective, but procurement procedures need to be improved.

A major deficiency in the Accounting, Recording and Reporting area is the long-standing problem of producing timely annual financial statements of auditable quality. While the government has made great efforts to clear up the backlog, the bank reconciliation methodology is flawed, and further compromised by failure in the reconciliation and clearance of deposit and advance accounts, with balances outstanding for many years.

External Scrutiny and Audit functions are only partially in effect due to the delays in presentation of annual financial statements to the Auditor General. Insufficient capacity in the Office of the Auditor General to conduct regular and timely compliance and performance audits of departments means that audits are a few years behind schedule, limiting their usefulness. Partly due to the lack of timely audit reports to review, there is insufficient involvement of the Public Accounts Committee (PAC) in fulfilling its oversight of departments and other public entities. The new Public Finance Act should strengthen the PAC and allow it to better direct the work of External Audit.

The government of Montserrat is pursuing a number of on-going reforms that directly impact the PFM system, including strengthening the legislative basis for these reforms:

- A new Public Finance Management and Accountability Act and Regulations were promulgated in 2009 to address the perceived shortcomings in the 2001 Finance Act.
- The existing 1989 Constitution was revised, with the modified sections on PFM to include specific provisions for strengthening the Public Accounts Committee and greater independence for external audit.
- A revised Audit Act has been elaborated to make this function more consistent with international standards.

- New procurement regulations have been elaborated. The principle underpinning them is the "pursuit of best value for money".
- An accounting manual has been prepared. It includes procedures for strengthening internal controls and accounting practices with respect to commitments.
- Since end-2007/start-2008, with the financial assistance of DfID, procedures for and training in internal audit within the MOF has been undertaken. The ultimate objective is to establish an operational internal audit unit.
- Code of Ethics for government officers has been finalized and has been introduced into the General Orders in 2009. A Code of Consultation has also been prepared, governing officers' interaction with the public. A Register of Interests Act is in the process of being finalized that will address a gap in anti-corruption legislation.

Additionally, recent PEFA assessment resulted in government's decision to develop a comprehensive PFM reform Action Plan developed with assistance of CARTAC and approved in June 2010. Prepared with a wide participation of government's officials, it confirms government's willingness to address weaknesses of the PFM system and assures government's ownership of the reform agenda.

### *2.3 Social situation*

The government is committed to the Millennium Development Goals (MDGs) and it has already surpassed most of the targets. Nonetheless, the MDGs together with their associated targets and indicators do provide a valuable framework within which the government will work to ensure the overall development of Montserrat.

The volcanic crisis significantly altered the social situation in Montserrat. The disruptions had a severely negative impact on employment and the means of livelihood, family life, housing, health care, benefits for the poor and vulnerable groups, and other elements of the social fabric. GoM has since used various assessments and surveys like the Montserrat Social Survey, the Social Welfare Review, the Participatory Poverty Assessment, and a national census, which were undertaken subsequent to the crisis, as the basis of its social policies and programmes.

A comprehensive system of social safety nets has now been built in a society that previously had a very low level of vulnerability and dependency. Today, the government supports direct welfare assistance, housing and rental assistance, three homes for the elderly, and a warden supported apartment for elderly persons, all in an effort to maintain a humane quality of life for its citizens. Data gaps though continue to plague Montserrat's ability to put into place safety nets for those at risk. However, the recently conducted Country Poverty Assessment (2009) is expected to help fill this gap and to provide the baseline information for support of much needed targeted interventions<sup>6</sup>. In an effort to complement social protection, GoM has built social capital through the construction of social infrastructure projects such as health clinics, early childhood centres and community markets, which have been financed through the CDB's Basic Needs Trust Fund (BNTF). The share of the budget allocated to social expenditure ranged from 23% in 2005 to an allocation equivalent to 19% in 2009.

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<sup>6</sup> The CPA report as at March 2011 was not available. Indications are that the report will be available by end of 2011.

### Health care

The standard of health care in Montserrat remains good. There is one 30-bed hospital that serves Montserrat's 4,819 residents. The hospital is equipped with an operating theatre, a laboratory, a pharmacy and a casualty department. Montserrat has one doctor for about every 1000 persons and this number includes a surgeon and an anaesthesiologist. Regular clinics are held by doctors visiting from overseas. Local nurses are trained at the Montserrat Community College. There are four health centres around the island providing primary care. The government provides assistance for those needing specialised care not locally available to receive that care overseas. Government health expenditure ranged from 12.9% to 14.1% of the budget between 2005 and 2009 with healthcare spending trending upwards. Life expectancy in Montserrat is 78 years.

### Education

Education in Montserrat returned to pre-volcanic levels with the completion of the EU-funded Montserrat Community College. This institution complements the services offered by the Montserrat Secondary School and University of the West Indies Open Campus. The integrated tertiary institutions offer a wide range of academic and a limited number of technical subjects. Secondary and primary education is free and enrolment at both levels is 100%. There are three primary schools and four early childhood centres. Montserrat's literacy rate is 97%. Government expenditure on education ranged from 5.6% to 4.5% of its budget between 2005 and 2009 with the latest trend showing increases in spending. The major challenges in the education sector include low teacher-student teacher ratios in the secondary schools and the ability to finance higher fees associated with secondary exams. The low teacher-student ratio has been tackled through the recruitment of teachers from overseas. The latest data from GoM reflects an improvement in the sector, with the teacher-student ratio now at approximately 1:12 across the system. The Montserrat Community Services Department provides some assistance to persons who face hardship and a few students in the system are assisted by private sector donations. Generally, these challenges have not had notable negative effects on education as students in Montserrat perform well on the regionally administered secondary school leaving Caribbean Examinations Council (CXC) examination.

### *2.4 Gender*

As a UK OCT, Montserrat is guided by the international conventions and practices on the rights of women adopted by the UK. Montserrat practices gender equity in most aspects of life in the country even though like the developed world, female wage levels are still below their male counterparts. In the decision making arena, three of the nine members of the Legislative Council and four of the six permanent secretaries in government are women.

### *2.5 Environmental situation*

The impact of the volcano on the southern half of the island remains the main environmental consideration for Montserrat. While the northern half remains mostly unaffected except for the occasional ash clouds, air quality is regularly assessed.

Environmental awareness among the population in general has been heightened by the volcanic activity and more specifically the need to preserve the remaining land and sea resources is better appreciated.

Montserrat now has a very strong environmental protection programme in place; it has implemented a comprehensive disaster management plan, become a leader in regional disaster preparedness mitigation and collaborates closely with the Caribbean Disaster Emergency Response Agency (CDERA) - the body responsible for coordinating disaster management in the region.

In particular, Montserrat has been working on enhancing the Department of Environment and the DMCA. This has involved securing adequate facilities and equipping the Department of Environment and the DMCA as well as identifying, recruiting and training staff of these departments. The Government has also enacted and enforced policy and legislation to ensure effective environmental and disaster management. Other ongoing work in the area include: protection and conservation of biodiversity and other natural resources through monitoring of invasive species and the implementation of species and habitat action plans and strengthening the capacity of national and community-level entities and key personnel engaged in the mitigation, management or coordinated response to natural disasters.

## *2.6 Sustainability and medium term challenges*

The main hurdle to the accomplishment of Montserrat's targets in the medium term as well as its overall sustainability will be overcoming the underachievement on the SDP and the Sustainability Roadmap to date, which has been driven primarily by exogenous factors.

### *Economic challenge*

The most important economic challenge facing Montserrat over the next three years will be managing the effects of the global financial and economic crisis, although less vulnerable to the downturns in tourism and the financial sector than many of its neighbours, as a result of its dependence on budgetary aid from the United Kingdom. A significant fall in activity in both public and private sector construction and a number of other areas such as mining depressed the Montserrat economy over the first three quarters of 2010. As a result, GDP is estimated to have declined by 4.4% in 2010. The Sustainable Development Plan 2008-2020 suggests that 4%-7% growth in GDP would be necessary to keep pace with the various development needs of Montserrat. This would be a challenge because it means that funding would need to be available for the implementation of key government projects such as the Little Bay Town Centre, the port expansion and the new tourism development project. These are the minimum requirements if Montserrat is to experience this kind of growth and fully resuscitate the tourism sector.

The government has continued to focus on how to ensure sustainable output expansion through growth in the tourism sector and has begun to target further private sector investment. In that regard, the implementation of SDP phase II, which focuses on capacity building for the sector and marketing the product, helps to meet the challenge of developing the tourism sector. The challenge is to speed up the process.

Another major challenge facing Montserrat in its efforts to revive economic growth over the medium term is the question of access to and from the island. The new airport at Gerald's has not

yet had the anticipated impact in terms of increased visitor traffic. Increasing airlift *still* remains a challenge while Montserrat awaits the completion of the port expansion project.

#### Population growth challenge

Montserrat's population, which currently stands at approximately 5, 000, is too small to meet its development objects and the population shortage remains a major challenge to its prospects for sustainable economic growth. The exodus of Montserratians after the volcanic crisis disproportionately included young people with skills and this has resulted in a demographic profile where 16% of the population is over 65 years of age, while the birth rate is almost the same as the death rate, which means Montserrat effectively has a zero population natural growth rate.

The fact remains that Montserrat wants service workers but it does not have enough people. The government therefore has to encourage Montserratians to return home by creating incentives that are attractive, such as adequate and affordable housing. Montserrat also has the challenge of dealing with a shortage of skilled technical labour. The challenge now is meeting the 5% growth in the indigenous population as Montserrat was not able to meet that target.

#### Budgetary challenge

Reducing the annual budget deficit and dependence on UK budgetary assistance remains a challenge and a constraint for the government. Since the government recognises that aid dependence is unsustainable over the long-term, the challenge for Montserrat over the medium-term is to accelerate its activities geared towards generating additional revenues.

#### Public financial management

In the light of the weaknesses and challenges identified in the recent Fiduciary Risk Assessment (FRA) and the report of the Public Expenditure and Financial Accountability (PEFA), the government has taken measures to strengthen public financial management. An action plan has been developed and is being implemented by the Ministry of Finance.

#### International and regional challenges

The current forecast is that food prices will continue to rise substantially over the medium-term and those territories like Montserrat with high food import bills will suffer the consequences and experience the effects of the upward movement on prices of basic foodstuff on the world market. This represents a serious challenge and its implications for Montserrat will have to be studied in more detail. The other major exogenous factors posing a challenge to the sustainability of Montserrat's economic growth would be the possibility of a double dip recession in Montserrat's major tourism markets in North America as many economists are predicting. Regionally, it would be too soon to measure the precise nature of the challenge posed by the EPA recently signed by CARICOM and the EU, but trade liberalisation, including the implementation of the CET and the CSME, could have an impact on Montserrat as the government depends on custom duties and other trade taxes for 40% of its current revenue.

## **Chapter 3: Policy agenda of Montserrat**

### *3.1. Introduction*

Montserrat's policy response to these challenges is embodied in the Montserrat Sustainable Development Plan (SDP) 2008-2020 as well as in the Montserrat Sustainability Roadmap. These documents also provide the blueprint for Montserrat's longer term objectives and development. The SDP represents an agreed and coherent policy framework over the 12 year period, outlining national development priorities and providing a framework for resources allocation towards the development of the island. In addition, the SDP sets out the essential elements of National Policy in a comprehensive and integrated agenda. The policy framework was agreed to after extensive consultations with all the various stakeholders in Montserrat. In particular, the SDP sets out the 5 major strategic objectives in the areas of: Economic management; Human development; Environmental management and Disaster mitigation; Governance; Population growth. In an effort to achieve these objectives, the SDP identifies the entities responsible for implementing the strategic actions as well as the expected timeframe for implementation and the measurable outcome indicators. Moreover, to contribute to a more effective implementation of the long-term strategic goals of the SDP, the document incorporates a Medium-term Strategy and Action Plan for 2008-2012.

On the other hand, the Sustainability Roadmap is a medium term strategy complementing, cutting across and developing certain aspects of the SDP, aimed at enabling Montserrat to move towards sustainability and achievement of the longer term goal of eliminating dependence on budgetary aid. It is considered that the successful implementation of this strategy is a prerequisite for success of the SDP long-term goals. The Roadmap focuses on a transformation of government administration in order to increase its efficiency and effectiveness, various revenue enhancement measures, capital investments needed to kick-start economic regeneration as well as creating a policy environment conducive to growing the island's population back to sustainable levels.

Apart from a response to short-term challenges, the SDP and Roadmap serve as core elements of Montserrat's overall policy framework. The documents provide the guidance for Montserrat's long-term and overall development in all areas, from which the other key plans are framed.

### *3.2 Overall policy framework*

The overall policy framework has the primary focus of bringing the recurrent deficit down to sustainable levels through increased tourism receipts, while maintaining macroeconomic stability and social expenditure at a reasonable level. The rationale behind this strategy is that lower deficits should result in reduced pressure on social expenditure and less dependence on grant support. Additionally, this policy framework is expected to create a stable environment conducive to private sector growth and a balanced budget.

This policy framework is outlined in the:

- Sustainable Development Plan (SPD) 2008-2020
- Sustainability Roadmap 2009-2014
- The Country Policy Plan (CPP)

- The National Disaster Plan
- Budget Speech and Estimates of Revenue and Expenditure
- Physical Development Plan for North Montserrat

The SDP and Roadmap are as described above, while the Country Policy Plan (CPP) sets out the strategy for the United Kingdom support to Montserrat, to help the island achieve its objectives. This is usually set in the overall context of the UK's evolving constitutional and governance relationship with Montserrat, and in coherence with Montserrat's own development plans. However, since 2002, the UK development assistance to Montserrat has been based on the SDP and Sustainability Roadmap rather than on the traditional CPP.

The National Disaster Plan - The Disaster Management Coordination Agency (DMCA) is the designated agency with a mandate for disaster/emergency planning and response. It embraces the concept of comprehensive disaster management which seeks to address all hazards during the various phases of the disaster cycle by involving all relevant sectors and levels of the community in preparing for and responding to hazard impacts. Additionally the DMCA is the identified coordinating agency for disaster management in Montserrat. The DMCA maintains updated guidelines (various disaster plans) that will ensure the departments effectiveness prior to, during and after a disaster.

Budget Speech and Estimates of Revenue and Expenditure – The budgets set out the focus of government resources and initiatives for a given financial year. It allocates resources to the programmes and projects necessary in the achieving of Montserrat's overall goals outlined in the SDP in that year. It allows the civil service to be aware of the path the government wishes to take and develop their annual plans around it in order to attain the benchmarks laid out in the SDP. Furthermore the private sector is made aware of where government is focusing and are able to adjust their own plans to take advantage of the opportunities that will arise as a result of the programmes and projects to be implemented.

Physical Development Plan - The Physical Development Plan (PDP) is developed as a result of extensive consultation between government departments, the private sector, NGOs and the community both on the island and overseas. The plan is based on a fundamental principle of making the island attractive for people to return to, and encourage population growth. An overall target of 10,000 persons is considered realistic in terms of the carrying capacity of the northern part of the island. The plan specifies the land requirements and development projects necessary to attract and accommodate the population at each phase without indicating when these population levels are intended to be reached. The approach necessitates careful and continual monitoring but makes the plan both robust and flexible, which is particularly important in conditions of uncertainty.

The next plan is being developed based on the goals outlined in the Sustainable Development Plan and the vision outlined for what the North will look like at the end of the 2008-2020 period. The previous PDP (2000-2009) was based the earlier versions of the SDP. The next PDP will be developed based on the map outlined in the SDP and will provide the infrastructural development that will facilitate private sector lead growth and economic sustainability. It will be

the catalyst to the initiation of several government projects and programmes that hope to generate economic activity in various sectors on the island such as Tourism and Agriculture.

### *3.3 Other policy initiatives*

The government has in its mandate to increase the population and size of the work force through overseas recruitment and recruitment of returned Montserratians. Such recruitment would require the government to establish the necessary package of incentives for attracting these skills to the island. However, the Government's constant need to reduce recurrent expenditure has prevented the establishment of a fully fledged overseas recruitment program. In some cases the government has provided incentives including: housing and competitive salaries to fill vacant posts but there is no concrete policy for overseas recruitment at this time.

A comprehensive National Tourism Strategy and Plan (NTSP) produced a strategic framework that incorporates a private sector development strategy. A Tourism Development Project (TDP), which involves tourism capacity development, tourism activities, and tourism marketing forms part of the NTSP and is administered by the Montserrat Tourist Board (MTB). A key feature of the NTSP is the setting up of a Tourism Challenge Fund under the TDP to encourage institutional and business ideas for private sector tourism development.

The National Tourism Strategy Paper identified the need for a high level of investment in Montserrat tourism, at both the institutional and infrastructure levels. This has received support from all major donors (DFID and the EU) who have agreed to contribute to the financing of vital tourism infrastructure.

The Montserrat Development Corporation (MDC) was created to oversee the development of Little Bay Town Centre and port expansion. A Loan Guarantee Fund was also established under the MDC to support private sector investment in tourism. The government is also seeking to access EU-funded private sector initiatives such as INTERREG III, PROINVEST and Caribbean Export.

In terms of trade policy, due to its status as a UK overseas territory, Montserrat cannot participate in Economic Partnership Agreements (EPAs). However, the government is hoping to use its special relationship with the EU to encourage domestic and foreign investors to become more active in the export sector.

## **Chapter 4: Assessment of past and ongoing EU cooperation**

The EU has been providing support to Montserrat under various conventions since 1976. Through this partnership, grant resources have been provided in the areas of economic infrastructure for water, roads, seaport, airport, and after funds were reprogrammed, for housing and tourism under various conventions and agreements. The total development cooperation under the 4<sup>th</sup> to the 8<sup>th</sup> EDF has been valued at EUR 32 million.

Under the 9<sup>th</sup> EDF, the Montserrat initially received EUR 11 million in the focal sector of Trade in Services (TSSP). This sum was increased to EUR 17.2 million after a positive mid-term budget review. Unlike under previous protocols where financial support was provided as project

support, Montserrat under the 9th EDF opted to use a new form of support, budget support. Budgetary support is being implemented in 5 tranches of which the first tranche of EUR 3 million was disbursed in 2007, the second of EUR 4 million in 2009 and the third tranche of EUR 6.4 million in 2010. The remaining 2 tranches will be disbursed after meeting agreed upon targets.

#### *4.1. Lessons learnt*

Montserrat has also benefited from EU humanitarian assistance since the volcanic crisis began in 1995. In addition, the recently completed housing project, funded under the 8<sup>th</sup> EDF helped to resettle displaced residents after the volcanic crisis.

The EU remains Montserrat's second largest development partner after the UK. The EU development cooperation programme in Montserrat is both consistent with the priorities of the government and complements the policies of the other international and regional development partners.

Under the 9<sup>th</sup> EDF, mid-term budget reviews conducted by both EU and DFID concluded that varying levels of progress were achieved by the government in meeting its budgetary targets. While there were delays in the start of the tourism development programme, the period also witnessed improved donor coordination.

Important lessons learned from past experience in Montserrat relate to the need of: assuring greater predictability of disbursements in order to avoid budgetary distortion in the context of important aid dependence; defining a clear strategy supported by the budget support programme, contributing to a more realistic determination of conditions and targets for variable tranches; establishing a clear correlation between the calendar of disbursements and the timing of availability of supporting evidence for general conditions and variable tranche indicators; assuring a greater balance between the variable and fixed tranches; understanding of budget support modality as such by main stakeholders; strengthening of coordination with DFID in assessment of general conditions of the programme.

#### *4.2. Programmes of EU Member States and other donors*

The UK is the largest development partner for Montserrat followed by EU and the CDB. There are no other member states or development partners providing assistance to Montserrat. The framework for development assistance co-operation is reflected in the SDP and the CPP.

The CPP is the UK-Montserrat negotiated strategy paper which has strengthened the partnership approach to development cooperation with Montserrat. The UK funds are managed by DFID and account for an average of 60% of total revenue. These funds support both the development programme and short falls in the government budget. EU funds are used strategically to enhance DFID support or fill any gaps in DFID contribution. UK funds implemented through DFID have supported housing development with the EU, as well as essential transport services.

The CDB has focused its efforts at financing social infrastructure throughout the country under the BNTF programme including the new public market.

The implementation of the Montserrat SDP will touch upon cross cutting issues with environment, biodiversity and private sector growth. The major development plans will require an environmental impact assessment; therefore, efforts are made to eliminate or minimize adverse effects to the environment. The port landside development is expected to result in some loss of vegetation but it is considered to be of low conservation or biodiversity value. The overall development of the Little Bay area has plans for improvement to waste water treatment and use of renewable energy sources. Noise emissions will increase during redevelopment and subsequent operation. Nonetheless, there are only a small number of residential properties in the vicinity of the port. In addition, the development of the port will encourage private sector involvement in the development of direct and indirect port related services. The government will ensure that equal opportunities are available. No negative effects are expected in the areas of good governance and human rights.

## **Chapter 5: Response strategy**

This chapter outlines the EU response strategy for Montserrat for the period 2008-2013 and is based on the country diagnosis and preliminary findings of the EU mid-term budget review. It also considers Montserrat's needs and progress made so far towards meeting the goals of the SDP and the government's commitment to achieving them. Finally, due consideration is given to the relative magnitude of financial and administrative resources to be made available by the EU for development cooperation with Montserrat in 2008-2013, as well as their potential impact.

The principles upon which the strategy was decided include: the alignment with key strategies of the government, in particular the SDP and NTSP; complementary synergies with the actions of DFID and CDB in Montserrat; and maximising effectiveness by focusing on interventions which respond to key needs and opportunities for progress, playing to the EU's comparative advantage.

### **Key objective, main areas for community action**

- The key objective of EU cooperation in 2008-2013 will be the promotion of sound economic management and sustained growth by supporting Montserrat in reaching its goals outlined in the SDP and the Sustainability Roadmap. The EU Country Strategy for 2008-2013 will concentrate on supporting the government's SDP through the aid modality of general budget support

In coherence with the EU Response Strategy, the overall objective of this general budget support (GBS) programme, which will absorb 100% of 10<sup>th</sup> EDF allocation, is to support implementation of the Sustainable Development Plan and Sustainability Roadmap, in order to contribute to the recovery of Montserrat by facilitating improved economic, social and environmental conditions for sustainable development.

The specific objectives are (i) to support creation of an environment that fosters prudent economic management, sustained growth, a diversified economy and the generation of employment opportunities; (ii) to support development of an efficient, responsive and accountable system of governance and public service.

### **Relevance and sustainability of the support strategy**

Under the 9<sup>th</sup> EDF the EU based its strategy on economic recovery and sustained growth. This strategy is still relevant as the economy continues on a slow upward trajectory. However, contrary to 9<sup>th</sup> EDF where a sector budget support was chosen as the implementation instrument, it is proposed that the support strategy employs available resources under the 10<sup>th</sup> EDF for General Budget Support towards the achievement of the objectives inscribed in the SDP and the Sustainability Roadmap. The GBS programme thus explicitly targets overarching objectives of EU development policy, such as poverty reduction and prevention, good governance and integration into the world economy. It also complements other development approaches (DFID and CDB), facilitating donor coordination and bolstering the effectiveness and sustainability of the EU response.

### **Coherence with other EU policies and cross cutting issues**

The suggested strategy is fully compatible with other EU policies. Where relevant, the EU policies and strategies on cross-cutting issues such as the protection of the environment, gender, governance and poverty alleviation have been taken into consideration. This includes the building of strategic and operational links between inter-related aspects of Montserrat's development. In addition, through EU budget lines, funding continues to be available mainly for environmental and governance projects.

Montserrat's economic industry and infrastructure has a high vulnerability to the increasing frequency and intensity of natural hazards, including tropical storms and hurricanes, flooding, droughts and earthquakes. Montserrat is also vulnerable to the impact of climate change including rising sea levels, increased temperatures, ocean acidification, changing precipitation patterns and an increase in the magnitude and frequency of extreme events.

Montserrat's location, geography and the concentration of its tourism plant in the coastal zone, makes it extremely vulnerable to coastal erosion, hurricanes and to the long-term risks associated with rising sea levels and climate change. Sea level rise, accompanied by increases in storm surge and wave run-up will heighten risks faced, as will destruction of reefs and protective environmental systems.

Montserrat is faced with growing problems of solid waste management, degradation of coastal and marine resources, beach erosion, pollution threat to critical groundwater resources and the degradation and loss of valuable biodiversity and biological resources.

The Government is through the National Disaster Plan, addressing the need for disaster/emergency planning and response. The aim is to ensure comprehensive disaster management, responding to all hazards, involving all relevant sectors and levels of the community. As mentioned above, the population of Montserrat is aware of environmental issues and more specifically the need to preserve the remaining land and sea resources.

Furthermore, the government has enacted and enforced policy and legislation to ensure effective environmental and disaster management. Moreover, it has initiated work in the areas of

protection and conservation of biodiversity and other natural resources, through monitoring of invasive species and the implementation of species and habitat action plans.

### **The indicative volume of funds available – principle of concentration**

The EU is the second largest grant provider to Montserrat after the UK. The total funds earmarked for EU Budget Support to Montserrat under the 10 EDF are EUR 15.66 million. EU assistance in 2009 was the equivalent of 36% of Government of Montserrat capital budget and came to EUR 794 for each Montserratian.

The implementation period for the Trade in Services Programme (9 EDF) is ongoing and is anticipated to be extending beyond the second quarter of 2011. The fourth tranche is expected to be partially disbursed in 2011 (EUR 1.6 million) with the possibility of a 5<sup>th</sup> tranche (EUR 2.1 million) to be disbursed at a later stage.

### **Budget support eligibility**

Montserrat currently fulfils the budget support eligibility criteria of a relevant development strategy, a stable macro environment and progress in PFM reform.

The Sustainable Development Plan and Sustainability Roadmap provide for a credible strategic framework guiding Montserrat's political and financial priorities. The monitoring framework for their implementation is functioning well and provides sufficient information on yearly progress achieved as well as the necessary corrective measures. Moreover, there is a strong commitment by the government to reform and considerable buy-in from most stakeholders to the Country Strategy and achievement of long-term objectives. Despite the recent macroeconomic challenges and territory's overall dependence on budgetary aid, Montserrat leads a prudent macroeconomic and fiscal policy and is thus considered eligible for budget support modality. This is reflected in its short-term response to the crisis as well as in progress made on the country's Sustainability Roadmap which provides a response to aid dependency in the medium term perspective.

The analysis of the public finance management criterion shows that the government has established a relevant programme of improvement in public financial management and that the evidence from the PFM diagnostic and the PFM reform process shows that trends in PFM justify the use of budget support as an implementation modality.

### **Complementarity with other donor assistance**

Coordinating support with other donor agencies, such as those already providing support to Montserrat in the development of sector reforms and action plans (DFID and CDB), is one of the objectives of the Paris Declaration. The EU and DFID, in particular, have made significant progress with respect to these efforts. The EU currently participates in DFID's annual and mid-year budget reviews and information sharing is supported by both agencies. Budget support programmes are closely coordinated and this helps to align indicators for performance evaluation & monitoring and to enhance budget reviews.

The EU's prior experience in Montserrat with cooperation in the Trade in Services sectors, its past and its current intense collaboration and coordination with DFID augurs well for the future. Furthermore, EU intervention in Montserrat would build upon its prior efforts at supporting

tourism infrastructure development, private sector growth and ICT under previous EDF allocations at the national and regional levels.

### **Risks**

The main risk for the government stems from the challenging global macroeconomic environment. The implementation of the Sustainability Roadmap and continued financial and TA from the UK during the implementation of the programme, however, should address this risk.

Administrative capacity risks are probable given the Montserrat administration relatively small size, which influences the capacity of the administration to implement the SPD and to adopt international PFM standards. It is expected that provision of TA support under this and other on-going budget support programmes will mitigate this risk.

Montserrat receives a significant level of budgetary support in the areas of rehabilitation and reconstruction as a result of its inability to generate sufficient revenue to finance its recurrent operations or its capital programme. Montserrat is faced with a relatively small tax base of just over 4,800 people, approximately 2,500 of which are economically active. As just under 1,000 of this proportion is employed by the government, reducing staff levels is a significant policy challenge as there is no viable private sector to absorb any redundancies. Therefore, private sector development continues to be fundamental to ensure sustained future economic growth.

Volcano related risks are a constant concern. Further volcanic activity as in the past, is the greatest threat to the success of any development programme. However, recent scientific reports have given residents reason to be optimistic about the future low levels of volcanic activity. Notwithstanding the above, careful selection of “safe areas” and the “Medium Investment” option in the National Tourism Strategy, with public sector investment kept to a minimum and private sector activity funded from internal and external sources greatly mitigates this risk.

Finally, the continued threat posed by hurricanes is the greatest barrier to the success of any development programme.

## PART B: TERRITORIAL PROGRAMME

### Chapter 6: Identification

Title/Number	Montserrat General Budget Support Programme CRIS reference: 022445		
Total cost	EU contribution: EUR 15,660,000		
Aid method / Management mode	General budget support – centralised management Complementary support - partially decentralised management		
DAC-code	51010	Sector	GBS

### Chapter 7: Rationale and country context

#### *7.1. Country context and national policy and strategy*

##### 7.1.1. Economic and social situation and poverty analysis

Historically, Montserrat's budget has been self-financing. However, in the last decade of the 20th century two successive events rendered the country's economy and government largely dependent on UK and EU financing. In 1989 Hurricane Hugo, a category 5 hurricane, destroyed over 90% of the island's infrastructure. The island recovered considerably after a few years only to be struck again in 1995 by the eruption of the Soufriere Hills volcano in the southern part of the island that had been dormant for many years. The eruptions continue today and have affected economic activities and pattern of land use. Since these developments, the focus of Montserrat's development efforts has been on reconstruction of infrastructure and services and the rebuilding of economic opportunities so that the remaining population may be retained in the territory, and as many expatriates as possible lured to return.

Development efforts have been reflected in a reduction in the poverty level, which is low by international standards. In Montserrat, the poorest households have a reasonable standard of living, good access to education and health services. In fact, many of the MDG's targets have been achieved. However, there are a number of groups that are still exposed to hardship. Those mainly at risk include: teenage mothers, the unaccompanied elderly and the working poor. Data gaps continue to plague Montserrat's ability to put into place safety nets for those at risk. However, the recently conducted Country Poverty Assessment (2009) will help to fill this gap and should provide the baseline information to support much needed targeted interventions.

##### 7.1.2. National development/cooperation policy and strategy

The development agenda in Montserrat has relied on development plans. The first one was elaborated for the period 1998-2002. A new Sustainable Development Plan (SDP) was elaborated for the period 2003-2007 and implemented. It sought to strengthen and consolidate these earlier achievements by developing Montserrat into a largely service oriented export led economy, reduce its current dependency on grant aid and ultimately achieve self-sufficiency. The

main achievements over the implementation period included: completion of crucial infrastructure - Montserrat Community College, Cultural Centre, John A. Osborne Airport; reduction of budgetary aid by 5% per annum on average and compliance with ECCB monetary policies; revision of existing constitution; completion of National Environmental Management Strategy, establishment of a Department of Environment and revision of environmental legislation.

However, a number of objectives related to increase of population, increase of tourism contribution to the GDP, increase in exports, shift in reliance on government services as the lead sector in the economy and reform of the public services were not achieved during the lifespan of the SDP 2003-2007. As a lesson learnt, in the development of a successive SDP a greater attention was placed on designing appropriate strategies leading to the achievement of main targets and outputs of the plan and to definition of achievable, from timing and resources point of view, targets. These lessons underpin the current development strategy, SDP 2008-2020 and to some extent Montserrat's Sustainability Roadmap, which was devised in 2009.

## *7.2. Eligibility for budget support*

### 7.2.1. National development or cooperation policy and strategy

The Montserrat Sustainable Development Plan 2008-2020, represents an agreed and coherent policy framework over the 12 year period, outlining national development priorities and providing a framework for resources allocation towards the development of the island. The SDP was prepared through extensive consultations involving open dialogue between key stakeholders: Ministers, Parliamentarians, non-state actors and development partners.

The strategic objectives of the SDP are as follows: Economic Management; Human Development; Environmental Management and Disaster Mitigation; Governance and Population. To contribute to a more effective implementation of the long-term strategic goals of the SDP, the document incorporates a Medium-term Strategy and Action Plan for 2008-2012. It focuses on the achievement of clearly specified medium-term objectives under each goal, identifies 'quick wins' and attributes clear responsibilities for meeting the targets.

Since its approval, the implementation of the strategy is monitored yearly by an SDP Monitoring Committee and results of the reviews are shared with the public. The 2008 and 2009 reviews noted progress achieved, with the objective 3 – Environmental management and disaster mitigation - showing most of progress in line with targets established. However, many medium term objectives initially to be achieved by end 2010 were considered overambitious and the calendar was revised accordingly, to allow for 5 year implementation period – 2008-2012. The reviews have also formulated recommendations or corrective actions to improve future performance.

In 2009 the government embarked on a development of a 'Sustainability Roadmap', a medium term strategy complementing, cutting across and developing certain aspects of the SDP, aimed at enabling Montserrat to move towards fiscal sustainability and achievement of the longer term goal of eliminating dependence on budgetary aid. It is considered that the successful implementation of this strategy is a pre-condition of success of the overall SDP long-term goals. For each of the 5 pillars of the Roadmap: Institutional Development; Economic and Financial

Management; Private Sector Development; Infrastructure and Services and Population, Capacity and Skills, a matrix of actions and a calendar has been defined for effective follow-up of implementation.

In conclusion, Montserrat is deemed to meet this eligibility criterion based on the following: i) the Sustainable Development Plan and Sustainability Roadmap provide for a credible strategic framework guiding Montserrat's political and financial priorities; ii) the monitoring framework for their implementation is functioning, providing sufficient information on yearly progress achieved and defining necessary corrective measures; iii) on the basis of recent progress reports, despite certain delays, there is an overall progress in SDP's implementation, while the Sustainability Roadmap complements and operationalises certain aspects of the SDP.

### 7.2.2. Macroeconomic situation

The basis of the yearly assessment of the macroeconomic situation and fiscal developments of Montserrat are mostly based on UK-Montserrat yearly discussions of budget estimates and policy benchmarks as well as on data published in ECCB reports. The latest UK-Montserrat discussions on budgetary assistance and related matters took place on 27-29 September 2010. The findings of the discussions included in the Aide Memoire at the end of the mission as well as reports from the ECCB are summarised below.

Although 2009 was a relatively difficult year for Montserrat, it is worthy to note that Montserrat was one of the few countries in the region estimated to have recorded positive growth in 2009. Real economic activity in Montserrat increased by just under 1 percent in 2009 after registering an expansion of 5.4 percent in 2008, marking an average annual rate of 1.5 per cent over the past five years. Growth was largely driven by three main sectors: construction, government services and banks and insurance. The rate of inflation as measured by the consumer price index (CPI) was just 2.5 percent during 2009, reflecting the low economic activity, which tempered a rebound in international commodity prices.

The fiscal operations of Central Government generated an overall surplus of \$2.4m in contrast to a deficit of \$13.5m recorded in 2008. This outturn was the result a revision in expenditure as a result of some unforeseen expenditure during the year. Revenue levels were higher than projected, that is \$100.5m against the projection of \$95.2m. Taxes on Income and Profits performed better than expected and budgetary aid levels (grant receipts) increased as a result of favourable exchange rates. On the other hand, current expenditure grew by 3.3 per cent to \$97.8m, attributed to increased outlays on transfers and subsidies and personal emoluments.

Based on the latest forecasts, however, real growth in Montserrat is projected to decline by around 4.4% in 2010 owing primarily to delays in construction projects experienced over the first eight months. Nonetheless, activity is expected to pick up modestly in the medium term, as construction activity in the public sector is likely to rebound in the fourth quarter. This output is expected to be led by public investment in roads, port and the development of the new town in Little Bay. Over the review period, inflation moderated further but revenue intake was below estimates due mainly to the decreased economic activity. Expenditure estimates on the other hand have been positive, with expenditure arrears kept close to, or even below the estimated

figures for all but a few items. The debt stock is currently less than EC\$9.0M and is being serviced in accordance with the repayment schedule.

In conclusion, despite the recent macroeconomic challenges and territory's overall dependence on budgetary aid, Montserrat leads a prudent macroeconomic and fiscal policy and is thus considered eligible for budget support modality. This is reflected in its short-term response to the crisis as well as in progress made on the country's Sustainability Roadmap which provides a response to aid dependency in the medium term perspective.

### 7.2.3. Public Financial Management

The most recent PEFA assessment was completed in March 2010. An additional source of information is DfID's Fiduciary Risk Assessment, conducted in parallel and based on the PEFA methodology.

Overall, the PEFA assessment indicates that while a fair amount of progress has been made in recent years, the existing PFM system in Montserrat is not entirely supporting the achievement of aggregate fiscal discipline, strategic allocation of resources, and efficient service delivery, which characterize a fully transparent and orderly PFM system. PEFA report, as well as the FRA provided clear evidence of progress with respect to the recent PMF related legislative and institutional reforms undertaken by the Government of Montserrat. With regard to recent achievements of the PFM reforms, since 2008 The government has improved financial regulations to make them broadly compatible with international standards; improved budget dialogue with overall sector strategic plans and embarked on capacity building within the Ministry of Finance (MoF).

In June 2010, the Government adopted an official PFM Action Plan, which will be used a baseline for measuring future progress. The plan, although ambitious, is well organized and responds to critical weakness identified in the March 2010 PEFA assessment. The plan seeks, among other things, to strengthen the legislative basis for PFM reforms (among others, Audit and Procurement legislation) and address the weaknesses at the level of the Ministry of Finance as well as at Auditor General and Accountant General Offices. Its implementation will be supported by DfID, CARTAC and EU financial and technical resources.

The analysis of the public finance management criterion shows that The government has established a relevant programme of improvement in public financial management and that the evidence from the PFM diagnostic and the PFM reform process shows that trends in PFM justify the use of budget support as an implementation modality.

### *7.3. Lessons learnt*

Under EDF 9, the Government of Montserrat is already implementing a Trade in Services Support Programme (TSSP) through GBS. The existing programme has been marked by delays in implementation. The main lessons learnt relate to the need for: further technical support to strengthen the national institutional framework; the creation of an annual budget support review process assuring greater predictability of disbursements; more realistic determination of conditions and targets for variable tranches; establishing a clear correlation between the calendar

of disbursements and the timing of availability of supporting evidence for general conditions and variable tranche indicators.

#### *7.4. Complementary actions*

The island is heavily reliant on DFID for the bulk of required investment across all sectors. The EU provides grant funding via its General Budget Support modality, while the Caribbean Regional Assistance Centre, CARTAC provides TA in the areas of macroeconomic capacity and public finance management reform process.

#### *7.5. Donor coordination*

Close coordination mechanisms were established for this programme through yearly joint budget support review missions and UK budget discussions. National responsibility for donor coordination is vested with the Ministry of Economic Development and Trade, (MOED&T). The overall framework for the consensus between government and donors on the objectives and strategy is the “Sustainable Development Plan 2008-2012”. Common performance indicators for the EU and DfID budget support programmes are being coordinated. In particular, the EU budget support performance indicators are to be aligned with UK benchmarks used in DfID yearly budget review discussions.

### **Chapter 8: Description**

#### *8.1. Objectives*

This programme is the second General Budget Support Programme (GBS) that is being provided by the European Union. In coherence with the EU's Response Strategy, the overall objective of this General Budget Support (GBS) programme is to contribute to the recovery of Montserrat by facilitating improved economic, social and environmental conditions for sustainable development. The specific objective of this General Budget Support programme is to support implementation of Montserrat's Sustainable Development Plan and the Sustainability Roadmap, with a specific focus on its economic management and governance objectives.

#### *8.2. Expected results and main activities*

The key results anticipated from the programme are:

- Improvement of the PFM system through strengthening of Government's own accountability mechanism, dialogue on conditions and indicators related to public finance management and implementation of TA component of the programme;
- Strengthening of the macroeconomic environment through dialogue and financial support;
- Increased efficiency and effectiveness of the delivery of services in the public sector through dialogue on indicators and financial support;
- Implementation of government's growth and private sector development agenda inscribed in the Sustainable Development Plan through dialogue on related indicators and financial support.

The programme activities relate to policy dialogue around the 3 eligibility criteria and fulfilment of variable tranche indicators, implementation of TA component and donor coordination. In relation to the TA, it will support government in the area of public finance management and civil

service modernisation. A detailed needs assessment will be carried out at the start-up of the programme.

### *8.3. Stakeholders*

The Ministry of Economic Development and Trade (MoED&T) is the lead ministry for the implementation of this budget support programme, with coordination and assistance of the Ministry of Finance. Monitoring of the implementation of the General Budget Support Programme will be carried out within specialised institutional structures: Inter-Ministerial Technical Committee on MTEF and Roadmap implementation; MoED&T, Aid & Project Cycle Management Unit; SDP Monitoring Committee.

### *8.4. Risks and assumptions*

**Financial and Economic Risks:** The main risk for the Government of Montserrat stems from the challenging global macroeconomic environment. The implementation of the Sustainability Roadmap and continued financial and TA from the United Kingdom during the implementation of the programme will address this risk.

**Administrative capacity risks:** Given its relatively small size, the human capacity of the administration to implement SPD and to adopt international PFM standards is challenging. Provision of TA support under this and other on-going budget support programmes will mitigate this risk.

Montserrat receives a significant level of budgetary support in the areas of rehabilitation and reconstruction as a result of its inability to generate sufficient revenue to finance its recurrent operations or its capital programme. Montserrat is faced with a relatively small tax base of just over 4,800 people, approximately 2,500 of which are economically active. As just under 1,000 of this proportion is employed by the government, reducing staff levels is a significant policy challenge as there is no viable private sector to absorb any redundancies. Therefore, private sector development continues to be fundamental to ensure sustained future economic growth.

**Volcano related risks:** Further volcanic activity as in the past, is the greatest threat to the success of any development programme. However, recent scientific reports have given residents reason to be optimistic about the future low levels of volcanic activity. Notwithstanding the above, careful selection of “safe areas” and the “Medium Investment” option in the National Tourism Strategy, with public sector investment kept to a minimum and private sector activity funded from internal and external sources greatly mitigates this risk.

**Hurricane related risks:** The continued threat posed by hurricanes is the greatest barrier to the success of any development programme.

### *8.4. Crosscutting issues*

All major development plans require an environmental impact assessment; therefore, efforts will be made to eliminate or minimize adverse effects to the environment. The port landside development will result in some loss of vegetation but it is considered to be of low conservation

or biodiversity value. The overall development of the Little Bay area has plans for improvement to waste water treatment and use of renewable energy sources. Noise emissions will increase during redevelopment and subsequent operation however there are only a small number of residential properties in the vicinity of the port. During the construction and after completion of the port facility, there will be a number of jobs available for female workers. In addition, the development of the port will encourage private sector involvement in the development of direct and indirect port related services. The government will ensure that equal opportunities are available. No negative effects are expected in the areas of good governance and human rights.

## Chapter 9: Implementation issues

### 9.1. Budget and calendar

The total amount allocated to this programme is EUR 15,660,000 from the 10th EDF, of which a maximum of EUR 15,390,000 is for budget support. The complementary support, totalling EUR 270,000 consists of EUR 170,000 for Institutional Strengthening/TA component in the area of public finance management and civil service modernisation and EUR 100,000 as provision for monitoring and evaluation.

The timetable of implementation of the budget support component covers three fiscal years over 2011 – 2014 (fiscal years are April – March in Montserrat). Operational Duration of this General Budget Support programme will be 36 months from the signature of the Financing Agreement (FA).

<b>Indicative budget</b>	
Budget Support component	EUR 15,390,000
TA/Complementary support	EUR 170,000
Monitoring & Evaluation	EUR 100,000
<b>Total</b>	<b>EUR 15,660,000</b>

<b>Indicative calendar for disbursement</b>				
	first quarter of 2012	second quarter of 2012	second quarter of 2013	<b>Total</b>
Fixed tranche	EUR5,130,000	EUR2,565,000	EUR2,565,000	<b>EUR7,695,000</b>
Variable tranche	EUR0	EUR2,565,000	EUR2,565,000	<b>EUR7,695,000</b>
<b>Total</b>	<b>EUR5,130,000</b>	<b>EUR5,130,000</b>	<b>EUR5,130,000</b>	<b>EUR15,390,000</b>

### 9.2. Budget support modalities

This direct non-targeted budget support programme will be disbursed in three instalments corresponding to fiscal years 2011/2012, 2012/2013 and 2013/2014. The funds will be accounted for in Montserrat's budget and transferred to the government's consolidated fund as revenues to support budgetary execution. Foreign-exchange transfers will be entered in the accounts under the value date of the notification of credit to the account of the Eastern Caribbean Central Bank.

The exchange rate will be the middle rate of the interbank foreign currency market on the day of the transfer. The TA component will be implemented via programme estimates under partially direct decentralised management.

### *9.3. Procurement and grants award procedures*

For complementary support like technical assistance, audit, evaluation, all contracts implementing the action must be awarded and implemented in accordance with the procedures and standard documents laid down and published by the Commission for the implementation of external operations, in force at the time of the launch of the procedure in question.

Participation in the award of contracts for the present action shall be open to all natural and legal persons covered by the financial regulations of the 10th EDF.

### *9.4. Performance monitoring and criteria for disbursement*

The fixed tranches will be disbursed in full upon fulfilment of the general conditions for budget support. So that the European Commission can evaluate the fulfilment of the general conditions, the government shall communicate at the time of disbursement request information on the following:

- (i) satisfactory progress in the implementation of the SDP and Sustainability Roadmap as evidenced by progress reports resulting from yearly SDP and Sustainability Roadmap reviews;
- (ii) satisfactory progress in the maintenance of a stability - oriented macroeconomic policy, as evidenced on the basis of UK-GOM macroeconomic and budget reviews and government's assessment in their request for tranche release;
- (iii) satisfactory progress in the implementation of its programme to improve public financial management, as evidenced by government's reports on progress achieved against targets set out in the PFM Action Plan.

The variable tranches will be disbursed upon fulfilment of the general conditions mentioned above and specific conditions in the areas of: growth and private sector development, public sector reform and public financial management.

The assessment of the general criteria for budget support will be conducted through the annual joint European Commission/DFID Budget Support review on the basis of conclusions of DfID budget discussions, the SDP and Sustainability Roadmap reviews and review of the implementation of the PFM action plan. The assessment of performance indicators will be conducted by the Delegation on the basis of proof of verification submitted by the government. On the basis of the information supplied, the European Commission shall formulate an assessment before the disbursement of all tranches of budget support.

## **Chapter 10: Evaluation and audit**

Evaluation will focus on the extent to which budget support is relevant, efficient, and effective in contributing to achieving sustainable impacts in the areas which are the focus of the objectives of budget support.

Concerning audit arrangements, the European Commission does not carry out financial audits of budget support operations. Once disbursed to the Treasury Account, funds are fungible and it is no longer possible to trace the “use” of EU funds. Audit of the national accounts is only carried out by the local Court of Auditors. Audits are however foreseen for complementary measures implemented under EDF procedures. Audit and evaluation contracts will be signed by the European Commission.

## **Chapter 11: Communication and visibility**

The Government will convene a formal high-level annual Budget Support Review of the macro-economic, fiscal and PFM situation while the programme is being implemented. This will ensure that discussions between the donors and the government take place at the appropriate level and promote high visibility of the programme. Communication and visibility activities will be coordinated by the MOED&T.