Public Disclosure Authorized

Public Disclosure Authorized

97468

Guatemala Cat DDO

DRFIP

DISASTER RISK FINANCING & INSURANCE CASE STUDY

Providing Countries with Rapid Access to Funds after a Natural Disaster

Highlights

- The DPL with Cat DDO provides immediate access to liquidity following a declaration of emergency.
- Guatemala, one of the top five high-risk countries in the world in terms of vulnerability to three or more hazards, requested and received a DPL with a Cat DDO that complements other financial instruments and disaster risk management measures in place in the country.
- Guatemala disbursed the full value of its DPL with Cat DDO following two major adverse natural events that struck the country in 2010, using the funds to finance reconstruction and other expenses.

Background

Guatemala, one of the largest economies in Central America, has made significant progress in achieving macroeconomic and democratic stability after a 36-year civil war. Prudent macroeconomic management enabled an annual average growth of 4.2% between 2004 and 2007. The global economic crisis of 2008-09, however, had a significant impact on the country. Remittances — a key driver of Guatemala's economy — dropped by 9.5% in 2009, and exports to the US, its main trade partner, also fell. Guatemala is also challenged by significant exposure to natural disasters. Between 1902 and 2005, the country experienced 62 natural disasters, which affected approximately six million people.

Since 1969, Guatemala has been building institutions in order to better respond to events affecting its macroeconomic stability. From 2005, the country has taken significant steps to move from a reactive to a proactive approach to addressing disaster risk by investing in risk mitigation measures.

Objective

Disasters from adverse natural events often force the government to divert resources from important long-term development projects, which can seriously inhibit the country's progress on its development goals. The Government of Guatemala wanted to ensure immediate access to funds following a natural disaster while other sources of financing (i.e., concessional funding, bilateral aid, and reconstruction loans) were being mobilized. Immediate liquidity would allow the government to respond quickly to emergency needs without hampering the continuity of development programs.

Structure

Guatemala decided to strengthen its response capacity with the help of a Development Policy Loan (DPL) with a Catastrophe Deferred Drawdown Option (Cat DDO), a form of contingent financing offered by the World Bank that provides countries with access to immediate liquidity at cost-effective levels following the declaration of a natural disaster. To qualify for the Cat DDO, Guatemala had to have an adequate macroeconomic framework in place and its disaster risk management program will be periodically reviewed by the World Bank. In April 2009, Guatemala requested and received a US$85 million Development Policy Loan (DPL) with a Cat DDO.

The Cat DDO provides immediate liquidity up to US$500 million or 0.25% of GDP (whichever is less) to IBRD member countries in the event of a natural disaster. Funds may be disbursed (partially or in full) when a state of emergency is declared by the government. The Cat DDO has a revolving feature, that is, amounts repaid prior to the closing date of the project are available for subsequent disbursements. Guatemala has the flexibility to change the repayment schedule for each new drawdown before it is disbursed, which allows it to balance its need for a grace period and with timing the loan's final payment maturity.

Outcome

The Cat DDO allowed the government to quickly respond to the damages caused by the eruption of the Pacaya volcano and the Agatha tropical storm in May 2010. The cost of the two disasters was US$982 million, approximately 2.6% of the 2009 GDP. In June 2010, the government disbursed the full balance of the Cat DDO to obtain liquidity and finance part of the reconstruction and other expenses.