Catastrophe Deferred Drawdown Option

The Development Policy Loan with a Catastrophe Deferred Drawdown Option (Cat DDO) is a contingent credit line that provides immediate liquidity to IBRD member countries in the aftermath of a natural disaster. It is part of a broad spectrum of risk financing instruments available from the World Bank Group to help borrowers plan efficient responses to natural disasters.

The Cat DDO gives a government immediate access to funds after a natural disaster, a time when liquidity constraints are usually highest. This type of financing is typically used to finance losses caused by recurrent natural disasters. It is most effective as part of a broader risk management strategy in countries highly exposed to natural disasters.

A disaster risk management strategy would involve complementing the Cat DDO with disaster risk transfer instruments (such as catastrophe risk insurance or catastrophe bonds) for high risk layers. Governments determine the mix of disaster risk financing instruments based on an assessment of risks, desired coverage, available budget, and cost efficiency.

Key Features

The Cat DDO allows borrowers to prepare for a natural disaster by securing access to a financing source before a disaster strikes. Essentially, the Cat DDO serves as bridge financing while funds from other sources (e.g., concessional funding, bilateral aid, or reconstruction loans) are being mobilized. Under the Cat DDO, borrowers can secure immediate access to financing up to US$500 million or 0.25% of GDP (whichever is less).

The Cat DDO has a "soft" trigger, as opposed to "parametric." Funds become available for disbursement after the declaration of a state of emergency due to a natural disaster.

The Cat DDO also has a revolving feature, which means that amounts repaid during the drawdown period are available for subsequent withdrawal. The three-year drawdown period may be renewed up to four times, for a maximum of 15 years in total.

In order to gain access to the Cat DDO, the borrower must implement a disaster risk management program, which the Bank will monitor on a periodic basis.

At a Glance

- A contingent loan that provides immediate liquidity following a natural disaster
- Funds become available for disbursement after the declaration of a state of emergency due to a natural disaster
- Country must have a disaster risk management program in place, which the Bank will monitor on a periodic basis

Pricing

The Cat DDO has a LIBOR-based interest rate that is charged on disbursed and outstanding amounts. The applicable interest rate is the prevailing rate for IBRD loans at drawdown. In addition, there is a front-end fee of 0.50% and a renewal fee of 0.25% on the loan amount. For current pricing information, please visit the Treasury website: http://treasury.worldbank.org/bdm/htm/ibrd.html.

The Cat DDO provides an affordable source of contingent credit for governments to finance recurrent losses caused by natural disasters. The expected net present value of the cost of a Cat DDO is at least 30% lower than the cost of insurance for disasters occurring once every three years. The cost saving can be even higher when the country's opportunity cost of capital is greater.

Disbursements

As of December 2010, three countries have secured access to funds after natural disasters by drawing down the outstanding balance on Cat DDOs. Cost Rica drew down a US$24 million Cat DDO after a 6.2 magnitude earthquake in January 2009. Guatemala accessed US$85 million—the full value of its DPL with Cat DDO—to finance reconstruction work and other expenses after two major natural disasters in 2010. Colombia also disbursed the full balance of a US$150 million Cat DDO to address a crisis caused by the worst rainy season in the country for decades.

Major Terms and Conditions	
Purpose	To enhance/develop the capacity of borrowers to manage catastrophe risk. To provide immediate liquidity to fill the budget gap after a natural disaster. To safeguard on-going development programs.
Eligibility	All IBRD-eligible borrowers (upon meeting pre-approval criteria)
Pre-approval Criteria	Appropriate macroeconomic policy framework. The preparation or existence of a disaster risk management program.
Loan Currency	EUR, JPY, and USD
Drawdown	Up to the full loan amount is available for disbursement at any time within three years from loan signing. Drawdown period may be renewed up to a maximum of four times.
Repayment Terms	Must be determined upon commitment and may be modified upon drawdown within prevailing maturity policy limits.
Lending Rate	Like regular IBRD loans, the lending rate consists of a variable base rate plus a spread. The lending rate is reset semi-annually, on each interest payment date, and applies to interest periods beginning on those dates. The base rate is the value of the 6-Month LIBOR at the start of an interest period for most currencies, or a recognized commercial bank floating rate reference for others.
Lending Rate Spread	The prevailing spread, either fixed or variable, for regular IBRD loans at time of each drawdown. 1. Fixed for the life of the loan: Consists of IBRD's projected funding cost margin relative to LIBOR, plus IBRD's contractual spread of 0.50%, a risk premium, a maturity premium for loans with average maturities greater than 12 years, and a basis swap adjustment for non-USD loans. 2. Variable, resets semi-annually: Consists of IBRD's average cost margin on related funding relative to LIBOR plus IBRD's contractual spread of 0.50% and a maturity premium for loans with average maturities greater than 12 years. The variable spread is recalculated on January 1 and July 1 of each year. The calculation of the average maturity of DDOs begins at loan effectiveness for the determination of the applicable maturity premium, but at withdrawal for the remaining components of the spread.
Front-End Fee	0.50% of the loan amount is due within 60 days of effectiveness date; may be financed out of loan proceeds.
Renewal Fee	0.25% of the undisbursed balance
Currency Conversions, Interest Rate Conversions, Caps, Collars, Payment Dates, Conversion Fees, Prepayments	Same as regular IBRD loans.
Other Features	Country Limit: Maximum size of 0.25% of GDP or the equivalent of US$500 million, whichever is less. Limits for small states are considered on a case-by-case basis.
	Revolving Features: Amounts repaid by the borrower are available for drawdown, provided that the closing date has not expired.

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