Program Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 04-Jun-2020 | Report No: PIDA27552
## BASIC INFORMATION

### A. Basic Project Data

<table>
<thead>
<tr>
<th>Country</th>
<th>Project ID</th>
<th>Project Name</th>
<th>Parent Project ID (if any)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cabo Verde</td>
<td>P171080</td>
<td>CABO VERDE SECOND STATE-OWNED ENTERPRISES FISCAL MANAGEMENT DEVELOPMENT POLICY</td>
<td>P165631</td>
</tr>
<tr>
<td></td>
<td></td>
<td>FINANCING (P171080)</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Region</th>
<th>Estimated Board Date</th>
<th>Practice Area (Lead)</th>
<th>Financing Instrument</th>
</tr>
</thead>
<tbody>
<tr>
<td>AFRICA</td>
<td>20-Jul-2020</td>
<td>Macroeconomics, Trade and Investment</td>
<td>Development Policy Financing</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Borrower(s)</th>
<th>Implementing Agency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ministry of Finance</td>
<td>Ministry of Finance</td>
</tr>
</tbody>
</table>

**Proposed Development Objective(s)**

i) Reducing fiscal risks from SOEs while improving service delivery in infrastructures; and ii) Strengthening accountability and effectiveness in fiscal management.

**Financing (in US$, Millions)**

<table>
<thead>
<tr>
<th>SUMMARY</th>
<th>DETAILS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total Financing</strong></td>
<td><strong>25.00</strong></td>
</tr>
<tr>
<td><strong>Total World Bank Group Financing</strong></td>
<td><strong>25.00</strong></td>
</tr>
<tr>
<td>World Bank Lending</td>
<td><strong>25.00</strong></td>
</tr>
</tbody>
</table>

**Decision**

The review did authorize the team to appraise and negotiate
B. Introduction and Context

Country Context

1. **Prior to the COVID19 global economic crisis, Cabo Verde was experiencing robust and accelerated economic growth on the back of strong structural reforms.** Since 2016, the Government took substantial fiscal consolidation measures to reduce the overall fiscal deficit from 3.0 percent of GDP in 2014 to 1.9 percent in 2019. Consequently, the debt-to-GDP ratio felt from 128.4 in 2016 percent in 2016 to 123.9 percent in 2019. The Government made substantial efforts to create the conditions for private sector-led growth, through a new partnership between the State and the private sector in delivering key infrastructure services. As a consequence of these reforms, economic growth reached 4.7 percent on average in 2016-2019, driven by private investment and consumption, on the demand side. On the supply side, growth increased owing to tourism activities on the back of the economic recovery in Europe and growth in domestic non-tradable services.

2. **Over the last decade, Cabo Verde has experienced significant poverty reduction in the context of broad development progress.** Using a national poverty line, the incidence of poverty declined from 45 percent in 2007 to 31.5 percent in 2019. Inequality has also fallen, with the consumption-based Gini index dropping from 47 in 2007 to 40 in 2018. While growth slowed down over the last decade, poverty declined faster in islands with the highest poverty rate, which is suggestive of a convergence in welfare across islands. Human capital achievements have been equally impressive. At 73, life expectancy is the second highest in SSA. In the global gender gap index, Cabo Verde ranks among the world’s best in the ‘health and survival’ and ‘school enrollment’ dimensions. However, poverty has a gender dimension as a large portion of the extreme poor live in households where a single mother is the breadwinner.

3. **The unfolding global COVID-19 pandemic will have extraordinary economic consequences, which will put a temporary hold on fiscal consolidation, debt decline, and poverty reduction.** The key transmission channels of external shocks are threefold. First, the tourism sector, which represents 25 percent of GDP and drives overall economic performance, would be affected by recently introduced travel restrictions affecting European tourists. Second, the delay or cancelation of planned private investment projects would reduce FDI and negatively impact economic activity. Finally, on the upside, as a net oil importer, the reduction in international prices would improve its terms of trade and support growth, fiscal, and external balances. As a result, the economy is expected to contract by 4 percent in 2020. The overall fiscal deficit will reach 9.4 percent of GDP and public debt increase to 134.4 percent of GDP. This is expected to be a temporary shock and the economy would revert to its previous medium-term path starting in 2021.

4. **The macroeconomic policy framework is deemed adequate for the proposed operation.** With the rapid deployment of an ample array of containment policy measures to the COVID-19 pandemic, the country has an adequate policy framework to respond to the ongoing crisis in 2020. While economically costly in the short term, these measures are aimed at mitigating the domestic outbreak and reduce long-term costs. The World Bank, through the Covid-19 Emergency response Project (P173857) and the Cabo Verde Disaster Risk Management Development Policy Financing with CAT DDO (P160628), will support the Government capacity to respond to the crisis. Growth will be restored over the medium term, driven by ongoing structural reforms to improve connectivity and boost private sector investment. The macroeconomic framework is anchored in the IMF Policy Coordination Instrument (PCI), the First Review of which was approved on March 27, 2020.
Relationship to CPF

5. The proposed operation is aligned with the objectives of the Country Partnership Framework (CPF) for Cabo Verde and the Systematic Country Diagnostics (SCD). The CPF aims to assist Cabo Verde over Fiscal Year (FY) 2020-2025 to accelerate human capital development, enhance fiscal and macroeconomic resilience, and improve the foundations for private sector-led growth. The programmatic DPF series is fully aligned with the World Bank Group twin goals of ending extreme poverty and promoting shared prosperity in a sustainable manner. The CPF was prepared based on the findings of the 2018 SCD. It identified high debt and fiscal risks in the SOEs sector, weak government effectiveness, and limited inter-island connectivity among the binding constraints to inclusive growth and shared prosperity. The proposed operation will advance reforms to address some of these constraints, reducing fiscal risks from SOEs and enhancing fiscal management. The following operations are complementing the DPF to achieve CPF outcomes: the SOE Related Fiscal Management Project; the Transport Sector Reform Project; Recovery and Reform of the Electricity Sector Project; the Catastrophe Deferred Draw-down Option DPF; Debt Management Capacity Support TA; and technical support on Transfer Pricing and Tax Expenditures.

C. Proposed Development Objective(s)

6. This programmatic Development Policy Financing series aims to support Cabo Verde’s efforts to: i) Reduce fiscal risks from SOEs while improving service delivery in infrastructures; and ii) Strengthen accountability and effectiveness in fiscal management.

Key Results

7. The DPF series supports the authorities’ transformative yet difficult reforms to break the cycle of high debt and reposition the role of the State in the economy. While acknowledging the short-term cost of the unfolding global COVID-19 economic crisis, the program promotes private sector-led provision of critical infrastructure services, and improvements in fiscal management over the medium term. The reforms supported by this operation are expected to minimize fiscal exposure to the SOE sector while improving the quality of maritime transportation and energy services. Private sector-led provision of maritime transport services leads to substantial improvements in the quality of maritime services, increased connectivity among the islands, and more efficient inter-island cargo transportation. In the energy sector, the reforms supported by this DPF would increase the affordability of energy services for low-income households and promote the use of renewable energy. Implementation of regional ICT directives would promote competition and reduce the cost of digital services. The new law package to revoke or streamline the main cost ineffective tax incentives will yield substantial fiscal savings and ensure greater transparency in fiscal management.
D. Project Description

8. This programmatic series supports a set of reforms aimed at addressing a series of binding constraints that have weighed on poverty reduction and shared prosperity in Cabo Verde. The SCD identifies poor connectivity (problematic inter-island transportation, high energy costs, and weak ICT infrastructure), risks to macroeconomic stability and fiscal sustainability, and weak public sector performance among the binding constraints to unlocking Cabo Verde’s pathways to prosperity. The DPF program is closely linked to the priorities identified under the three drivers or pillars of the SCD for sustaining poverty reduction and further enhancing shared prosperity. These are expected to promote economic growth and job creation, strengthen social inclusion, and improve resilience. Priorities include: (i) enhance human capital; (ii) address poor connectivity; (iii) tackle risks to macroeconomic stability and fiscal sustainability; (iv) enhance public sector performance; and (v) bolster resilience.

9. Specifically, the DPF supports a program of two pillars:

- Pillar I on reducing fiscal risks from SOEs while improving service delivery in infrastructures supports:
  (i) the implementation of a strategic partnership with the private sector for improved quality and financial sustainability of inter-island maritime transportation; (ii) strengthening the position of the public energy utility while improving the affordability of electricity and fostering energy efficiency and the use of renewables; (iii) enhancing fiscal transparency and increase inclusiveness of the social housing program; (iv) addressing anti-competitive practices in the Information and Communication Technologies (ICT) sector through effective implementation of relevant regional regulations.

- Pillar II on strengthening accountability and effectiveness in fiscal management supports:
  implementation of the recently approved legal framework for budget and debt management; strengthening the medium-term fiscal framework; and streamlining tax expenditures.

The DPF series is closely linked to the development priorities of the Government as reflected in the National Development Plan for 2018-2021. The plan aims to position the country as a ‘Hub in the mid-Atlantic’. The objectives include: (1) transforming the country into a maritime and air transport hub providing services to freighters, cruise and other ships as well as connecting the islands and neighboring countries; (2) ensuring economic stability and sustainability; (3) enhancing social inclusion; and (4) strengthening sovereignty and valuing democracy. The strategy highlights the need for a major shift in the country’s development model, addressing macroeconomic stability, fiscal risks in the SOEs sector and from natural disasters, and broadening Cabo Verde’s economic base. The focus on private sector-led growth represents a major shift from previous strategies where state-led investments were more dominant. The design of the DPF reflects implementation capacity constraints and the difficult global environment related to the COVID-19 pandemic. This operation builds on the 2019 First SOE and Fiscal management DPF.

E. Implementation

Institutional and Implementation Arrangements
11. The Ministry of Finance (MOF) is leading the effort in coordinating the overall implementation of the DPF. The MOF has experience and is conversant with World Bank policies and procedures through DPF, project lending and TA operations. The SOE Related Fiscal Risk Management Investment financing project, approved by the Board in June 2018, is providing institutional capacity building on effective implementation of the medium-term fiscal framework. The SOE project is also providing technical capacity building to strengthen the SOE Ownership Unit at the Ministry of Finance to closely monitor SOE financial and operational performance. Technical assistance was also given to the Government to adopt a formal benchmark model to systematically evaluate and publish all tax incentives. The World Bank DPF team continues to support the Government in monitoring reform progress. The MOF has assigned multi-sector focal points (including from the Ministry of Industry, Commerce, and Energy) for coordination on the reform program under the leadership of the Directorate of Planning at the Ministry of Finance. Most of the data for tracking progress is available within the MOF, on the websites of relevant ministries, and/or provided by the MOF upon request.

F. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts

12. The DPF program supports policy reforms of key SOEs, the ICT sector, fiscal and debt management, and rationalization of non-efficient tax expenditures. The policies supported by the proposed operation are expected to have broadly positive impact on poverty and social indicators. The support to the concession of inter-island maritime transportation to reduce fiscal risks and enhance service delivery has positive effects. The reforms have already led to a substantial improvement in maritime services which will have indirect positive effects on poverty in the medium term through improved service delivery and higher economy-wide productivity. In the energy sector, the expansion and accelerated implementation of the social tariff for low-income households will have a positive impact on the poor. The reform ensures an alignment of the beneficiaries with the social cadaster and the automatically enrollment of eligible households into the social tariff scheme. When the reform is in effect, the poverty impact would be significant: the median disposable income that would be released for alternative uses ranges from an equivalent of 1.1 percent of total annual household expenditures in Santiago island to 1.94 percent in Santo Antão. This reform will particularly benefit women as a large portion of the extreme poor (43 percent) live in households where a single mother is the only breadwinner. The COVID-19 crisis and associated containment measures are expected to cause a direct and severe income shocks particularly for those that are engaged in the travel and tourism industry through loss of employment and reduction in domestic remittances.

13. Improving fiscal transparency and promoting of social inclusion in the social housing program has a positive social effect through better access to housing for the disadvantage people. Access to affordable housing for people with disabilities and the youth is expected to decrease social inequalities, reduce physical deprivations, and improve socio-economic conditions of low-income populations. The reforms on the non-transport SOE sectors are designed to create fiscal space for development spending, which should contribute to poverty reduction and social progress. This is also applicable to the reforms on fiscal and debt management and to some extent to those in the ICT sector.
Environmental, Forests, and Other Natural Resource Aspects

14. Some of the policy reforms supported by this DPF operation are expected to have significant positive environmental effects, while provisions to ensure environmental and social due diligence are in place in relevant sectors. An increase in the share of renewable energy (Prior Action 3) and the promotion of energy efficiency (Prior Action 4) can bring environment benefits. The strategic plan fostering the use of renewable energies, which identified solar and wind resources as a priority source of energy to attain the targets in the National Power Sector Master Plan, will guide stakeholders in how to develop sub-sector plans that meet the country’s energy and development needs. The implementation of this plan will reduce the use of fuel fossil for power generation. In line with Cabo Verde contribution to the Paris Agreement on Climate change, the National Power master plan seeks to generate 30 percent of Energy from renewable resources in 2025. Additionally, the national labelling system for electrical products will promote the energy efficiency. In the maritime sector, the concession contract includes provisions on the obligations of the Concessionaire regarding environmental and social issues, including occupational health and safety, and refers to the relevant national and international regulations. In terms of the environmental and social impacts of renewable energy infrastructure projects, the implementing central agency—Special Project Management Unit (UGPE)—is well experienced and equipped to manage the environmental and social impacts of World Bank projects. Nonetheless, given the scale of the planned projects UGPE would benefit from technical assistance. The rest of the reform actions supported by this operation are policy-oriented and are not likely to have negative impacts on natural assets.

G. Risks and Mitigation

39. The overall risk rating for the DPF series is substantial. Macroeconomic risks are high. These are primarily associated with a potential delay in fiscal consolidation and SOE reforms due to adverse economic impacts of COVID-19. A sharper economic slowdown could cause reversal of the gains in fiscal and debt sustainability achieved in recent years. The government has shown a strong commitment to fiscal consolidation and strengthen SOE governance. To mitigate these risks, the reform measures supported in the DPF have been selected considering areas where the Government has already initiated reforms and have been the object of support from other Bank projects. Risks related to the implementation capacity of sector strategies and policies are substantial. Cabo Verde has made important strides in raising the capacity of the public service. However, significant deficiencies exist in some areas. The proposed operation seeks to mitigate capacity risks by: (i) concentrating on policy reforms that have benefitted from or are the subject of ongoing policy dialogue with the WBG; (ii) supporting policy reforms that leverage other WBG operations; and (iii) providing TA either directly or jointly with other development partners in selected areas. Institutional capacity risks are high. The government in power since April 2016 has shown its commitment to the DPF-supported reform agenda. However, the effectiveness of this commitment and the government’s ability to manage political and institutional pressures going forward are not assured. The reforms undertaken by the government may be politically sensitive. To mitigate this risk, the Bank is supporting reforms which, while difficult, benefit clearly from strong
CONTACT POINT

World Bank
José Daniel Reyes, Fiseha Haile Gebregziabher, Maimouna Mbow Fam
Senior Economist

Borrower/Client/Recipient
Ministry of Finance

Implementing Agencies
Ministry of Finance
Gilson Pena
National Director of Planning
carla.cuz@mf.gov.cv

FOR MORE INFORMATION CONTACT
The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 473-1000
Web: http://www.worldbank.org/projects

APPROVAL

Task Team Leader(s):
José Daniel Reyes, Fiseha Haile Gebregziabher, Maimouna Mbow Fam

Approved By
Country Director: 21-Mar-2020