Combined Project Information Documents / Integrated Safeguards Datasheet (PID/ISDS)

Appraisal Stage | Date Prepared/Updated: 02-Nov-2017 | Report No: PIDISDSA23210

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Cabo Verde	P163015	Cabo Verde: Access to Finance for MSMEs	
Region	**Estimated Appraisal Date**	**Estimated Board Date**	**Practice Area (Lead)**
AFRICA	13-Nov-2017	15-Feb-2018	Finance & Markets
Financing Instrument	**Borrower(s)**	**Implementing Agency**	
Investment Project Financing	Ministry of Finance	Ministry of Economy and Jobs	

Proposed Development Objective(s)

The development objective is to increase access to finance for micro, small and medium sized enterprises.

Components

Partial Credit Guarantee Fund to Enhance MSME Finance
Technical Assistance for MSMEs
Upgrades to Improve Credit Information Systems
Institutional Capacity Building and Project Implementation

Financing (in USD Million)

Financing Source	Amount
International Development Association (IDA)	15.00
Total Project Cost	**15.00**

Environmental Assessment Category

F - Financial Intermediary Assessment

Decision

The review did authorize the preparation to continue

Other Decision (as needed)

B. Introduction and Context

Country Context

1. **Cabo Verde is an archipelago of ten islands, nine of which are inhabited, located 500 kilometers off the west coast of Africa with an estimated population of 540,000.** Only 10 percent of its territory is classified as arable and the country possesses limited mineral resources. The country is vulnerable to climate change, rising sea levels, and natural disasters including an active volcano on the island of Fogo that last erupted in November 2014. Despite the arid climate and mountainous terrain, Cabo Verde has developed rapidly, in large part thanks to its sizeable tourism industry, and attained lower middle-income country status with a GNI per capita income of USD 2,970 in 2016.

2. **Cabo Verde's economic growth over the past decade has resulted in poverty reduction**. Using a national poverty line of USD 5.4 per person per day, poverty fell from 58 percent in 2001 to 35 percent in 2015 while extreme poverty, defined as PPP USD 2.9 in 2015, fell from 30 to 10 percent. Over the same period, the share of income of the bottom 40 percent increased from 12.4 percent to 15.3 percent.[1] Unemployment was 15 percent in 2016. Cabo Verde outperforms its peers on most non-monetary dimensions of poverty, including life expectancy, maternal mortality, net primary school enrolment, and access to an improved water source. Cabo Verde's average life expectancy, estimated at 73 years of age, is the highest in Sub-Saharan Africa. Similarly, education outcomes put Cabo Verde at the top of Sub-Saharan Africa: the adult literacy rate is estimated at 87 percent, although disparities continue to persist between men and women.

3. **Economic activity in Cabo Verde is mostly conducted by small, mostly informal, firms**. In 2015, the business sector was comprised of 9,357 formal firms providing 52,783 jobs and approximately 33,000 informal firms providing close to 40,000 jobs. Micro, small, and medium-sized enterprises (MSMEs) as defined by the 2014 Special Legal Regime for Micro and Small Enterprises, constitute 98 percent of firms operating in Cabo Verde, providing more than 40 percent of jobs and a significant share of the economy (when informal businesses are included).[2] About two thirds of formal firms are located on the islands of Santiago and São Vicente. In 2014, 19 out of 100 adults were business owners.[3] This rate was higher for men (21.8 percent) than for women (16.1 percent). One in ten entrepreneurs (either new, young, or established) closed, suspended, or gave up of a business that they owned or managed in the last 12 months.

4. **The economy is based on services, particularly wholesale and retail trade, as well as tourism, mainly for European markets**. Canned fish (using fish caught by foreign vessels) dominates the manufacturing sector, which comprises 15 percent of GDP. Construction plays an important role in the economy and represented 9 percent of GDP between 2011–15. Over the last decade, the share of the primary sector in GDP has been relatively stable, reaching 9.1 percent in 2015. The main export is tourism for European markets; other exports include fuels, lubricants, and fish.

[1] The Government expects to publish updated poverty figures in late 2017 analyzing data from a comprehensive household income expenditure survey conducted in 2016.

[2] Staff calculations based on data of the National Statistics Institute. According to the Special Legal Regime for Micro and Small Enterprises enacted in 2014, a micro enterprise has up to five employees and/or annual revenues of less than CVE 5 million (about USD 54,000). A small enterprise has between six and ten employees and/or annual revenues in between CVE 5 million and CVE 10 million (about USD 54,000-108,000). The National Statistics Institute categorizes a medium-size enterprise as one with annual revenues of less than CVE 150 million (about USD 1,600,000).

[3] Established business ownership rate is the percentage of adult population who are currently owner-manager of an established business, i.e., own and manage a running business that has paid salaries, wages, or any other payments to the owners for more than 42 months.

5. **The economy has limited productive capabilities and its global competitiveness is low**. While there is potential for agribusiness and fisheries, the limited level of processing of agricultural products and the lack of food and handling safety certifications remains a constraint. MSMEs are not well connected to tourism supply chains, which are dominated by large international resorts located in the islands of Boa Vista and Sal and based on an all-inclusive model that obtains most of their goods and services abroad. A weak transport sector results in poor inter-island connectivity, which limits tourism's inclusiveness. The small size of the domestic market imposes limitations to economies of scale. From 2011–16, the current account deficit was 9 percent on average. The Global Competitiveness Report ranks poor financial sector development as one of the most problematic factors, after a small market size, an inefficient labor market, and the macroeconomic environment.[4] Enterprise surveys consistently rank limited access to finance as the most significant constraint for businesses.

6. **Cabo Verde's economic growth slowed down significantly due to the global financial crisis, which was primarily transmitted to Cabo Verde by the Eurozone crisis**. During 2010–15, average real GDP growth fell to 1.8 percent relative the 7.1 percent average growth achieved from 2005–09. Foreign direct investment (FDI) fell to 6.7 percent of GDP from 10.4 percent of GDP over the same periods. Growth was mainly driven by public expenditure financed with external debt. The economy recovered in 2016 with an estimated real GDP growth of 3.8 percent supported by FDI, domestic demand, and tourism, which benefitted from the economic recovery in Europe. The economy is still vulnerable to external shocks, notably from Europe, the main source of tourism, FDI, and remittances.[5]

7. **The macroeconomic situation is challenging with public debt at 132 percent of GDP at the end of 2016**. The slow pace of public financial management reforms and weak fiscal discipline—particularly in the state-owned enterprise (SOE) sector—has undermined macro-economic resilience. The current account deficit has been mostly financed by external debt, which increased from 42.8 percent of GDP in 2009 to 97.4 percent of GDP in 2016. Public debt is likely to continue to increase given government liabilities associated with largely insolvent SOEs. The latest debt sustainability analysis found Cabo Verde to be at a high risk of debt distress, although baseline debt service indicators remain at comfortable levels. While most of this debt is concessional, gross financing needs are increasing, limiting the ability of the government to use fiscal policy to absorb shocks. Episodes of debt distress could affect confidence levels and bring shocks to the economy, including through the financial system, particularly given the limited monetary and fiscal space available to the government. The government has invested heavily in the country's infrastructure in recent years. The challenge now is to wind down the public investment program and enable businesses to utilize the new infrastructure for growth, job creation, and poverty reduction.

Sectoral and Institutional Context

8. **The size of the financial sector is significant and larger than what would be expected given the country's level of economic development.** As of end-2016, financial sector assets were estimated at 139 percent of GDP (approximately USD 2 billion) and have increased by about two thirds since 2010. Domestic credit provided by the financial sector is estimated at about 86 percent of GDP as of end-2016, which compares well with regional and income group comparators as well as other small island states. Financial assets are largely denominated in the local currency and the sector has benefited from the confidence provided to investors by the stable currency peg to the Euro.

[4] World Economic Forum. *Global Competitiveness Report 2017-2018*.
[5] After a decline during 2006–2010, remittances from migrants have picked-up and increased to 13.6 percent of GDP in 2016 from 7.9 percent of GDP in 2010.

9. **The financial sector in Cabo Verde is dominated by banks, which are liquid but risk averse**. The banking sector, which has more than 85 percent of total financial sector assets, is highly concentrated with two out of seven licensed banks dominating the credit and deposit markets with a combined market share of almost 70 percent. Bank liabilities are predominantly deposits from residents, migrants, and government.

10. **Banks struggle with low asset quality, low profitability, and limited capital buffers**. The economic downturn's impact on tourism and real estate caused the level of non-performing loans (NPLs) to increase to 15.5 percent of total loans as of end-2016.[6] Average return on assets from 2011-16 was only 0.3 percent. Capital was only 7.7 percent of total assets at end-2016 and varies by bank. Some banks have experienced capital constraints. In March 2017, BCV took measures to resolve an insolvent state-owned bank (Novo Banco) established in 2010 to support MSME finance and low-income housing.[7] To mitigate risks, BCV is reinforcing its banking supervision team, increasing the frequency of on-site audits, and encouraging banks and corporates to recognize and address NPLs while rebuilding capital buffers.[8]

11. **Access to finance is a significant constraint.** Domestic credit to the private sector has declined as banks increased the share of their assets deposited with the central bank and lent to the government and SOEs. This reflects both a higher risk aversion by banks and the lack of viable investment opportunities. Despite progress, in 2015 there were only 189 commercial bank borrowers per 1,000 adults. Lending rates are also high in real terms.

12. **The average cost of finance is high with lending rates for loans of up to one year of about 10 percent in real terms.**[9] In 2016 the average interest rate spread (lending minus deposit rates) was 7.0 percent in line with low middle-income economies and slightly above middle-income economies (6.4 percent). This is due to inefficient banking and capital allocation—as evidenced by high NPLs and high level of reserves at the central bank—, but also to high operating costs due in part to the nature of operating bank branches on an archipelago and lack of sufficient economies of scale. Cost-to-income ratios are very high (an average of 69 percent over the last five years), indicating room for improvement in banking sector efficiency.

13. **Micro and small enterprises, in particular, face significant financing constraints.** Total domestic bank credit to MSMEs in Cabo Verde is estimated to be about US$ 320 million. Banks do not segment their customers by size and as a result bank staff have an incentive to focus on larger customers. Micro and small enterprises receive only 58 percent of the number of bank loans, despite representing 90 percent of the number of firms in the economy. Businesses in Cabo Verde tend to source their external financing from informal investors (24%), family and friends

[6] A significant share of asset quality issues pertains to large tourism real estate exposures, which consist of residential real estate property developments targeted to foreigners funded by local banks. As the global crisis unfolded, key projects ceased to be viable and companies (mostly foreign-owned) went bankrupt.

[7] In March 2017, the BCV transferred all Novo Banco's deposit liabilities to Caixa Económica de Cabo Verde together with some assets (collateralized loans, cash, government securities) and restricted Novo Banco from taking deposits or extending credit. BCV withdrew Novo Banco's license in June 2017. The government estimates this resolution will cost US$ 17 million or about 1.0 percent of GDP.

[8] In 2014, the BCV approved a gradual increase of the minimum capital requirements from 10 to 12 percent of risk-weighted assets: the minimum capital requirement will increase to 10.5 percent on 1 January 2018, 11.25 percent on 1 January 2019, and 12 percent on 1 January 2020. In 2015, the BCV increased to five years the time limit for banks to sell their real estate assets received as payment for NPLs during 2013–2016.

[9] Deflation has hardly reacted to the BCV's program of monetary easing of February 2015, which signals problems in the transmission mechanism of monetary policy and could be linked to the illiquid interbank money market. In June 2017, the BCV introduced more aggressive monetary stimulus measures, reducing the benchmark interest rate from 3.50 to 1.50 percent.

(24%), banks (22%), and microcredit institutions (14%).[10] On average, MSMEs have credit with only one bank (versus an average of two banks, in the case of large enterprises). This signals limited competition in the credit market for MSMEs and is likely due to MSMEs lacking fixed assets (e.g. real estate) to offer as collateral.

14. **The microfinance sector is small and comprised mostly of non-profit institutions with social objectives that rely primarily on donor funding and are not financially sustainable**. The sector's total loan portfolio is USD 6 million distributed across 11,000 borrowers (for an average loan size of USD 545) located mostly on the islands of Santiago and Fogo. Funding from commercial banks is limited by the amount of real estate guarantees provided by microfinance institutions.

15. **Inadequate financial infrastructure undermines credit allocation by financial institutions.** A weak insolvency regime, the absence of large-scale financial reporting, and an inefficient credit reporting system results in sub-optimal credit allocation. This partly explains why commercial banks primarily provide asset-based lending and offer little cash-flow-based lending or start-up financing, and why small-scale borrowers receive limited credit from financial institutions.

16. **A mutual credit guarantee system was launched in in 2010 but has been highly ineffective.** The system is based on mutual guarantee companies that provide guarantees directly to MSMEs and benefit from a counter-guarantee from a public fund. CVGarante is the only mutual guarantee company operating in Cabo Verde. An assessment of the system conducted by the Bank in August 2016 found that its governance, institutional structure, and design had rendered it unattractive for banks as a risk sharing mechanism.[11] The public counter guarantee also introduced uncertainty around claim payout given the requirement of board approval rather than well-defined criteria.

17. **CVGarante does not meet many of the *Principles for Public Credit Guarantee (PCG) Schemes*.**[12] Since inception, CVGarante has issued only seven guarantees on loans equivalent to US$ 250,000 of which banks have disbursed funds from only two loans given the low credibility of the fund.[13] Guarantee approvals were unnecessarily cumbersome and redundant as they duplicated the review conducted by the lending institution without any value addition or expertise in credit risk. The rejection rate was high and processing slow (paper-based and manual) with much of the information required by CVGarante being unnecessary to make decisions on guarantees. Fees were high and unattractive to banks. Given the size of the fund and volume of business, the assessment concluded that the operation was not financially sustainable. In other countries, well-functioning PCG schemes increase bank's risk appetite to lend to MSMEs. Particularly for financial systems characterized by high liquidity and risk aversion, mechanisms like a well-designed PCG help banks move to higher risk client segments. International experience suggests that key factors determining PCG success include governance, coverage, management of claims, and pricing.

18. **Financial reporting and auditing practices are absent in most firms.** Two thirds of registered firms do not have proper accounting.[14] This creates obstacles to accessing bank credit: according to a recent BCV study, 92.5 percent of businesses with bank credit had organized accounting. Although those registered firms with organized

[10] Based on an unpublished study on entrepreneurship commissioned by the Ministry of Economy that conducted a survey of 2,200 adults in Cabo Verde in December 2014.
[11] World Bank, *Cabo Verde: Partial Credit Guarantee Scoping Report,* August 2016
[12] World Bank Group; FIRST Initiative. 2015. *Principles for public credit guarantee schemes for SMEs*. Washington D.C.
[13] CV Garante was established in 2013 by four of the largest banks and with the support of Government.
[14] Instituto Nacional de Estatística. 2017. *Estatísticas de Empresas. Inquérito Anual às Empresas.*

accounting represent 96 percent of total turnover, banks believe that most of these financial reports are not credible as they are not properly audited and are prepared primarily for tax purposes. Confusion between personal and business accounts and financial flows is common. Accounting standards are not enforced.

19. **The central bank maintains a public credit registry, but it is only used by banks and the percentage of the population covered is low, mainly because the only source of information is solely bank credits. Coverage has fallen slightly from 23 percent in 2009 to 20 percent in 2016.** Banks receive limited information from the credit registry. Banks note that: (i) credit references are not available for everyone, particularly for small businesses that do not have bank credit; (ii) the absence of information about other type of arrears, such as tax, social security, customs, and utilities; and (iii) identification of borrowers is sometimes difficult due to duplication of names, and given the lack of a standardized, generalized and unequivocal identification system in Cabo Verde.

20. **In 2016, BCV developed a plan to upgrade the registry based on a diagnostic of the IT architecture, data quality, communication processes, and sharing information sharing capabilities.** The plan includes enhancements to the regulatory framework and to the IT architecture and software solution. BCV is recruiting a full-time IT staff for its credit registry team, which currently does not have any full-time IT staff. The upgrade will improve the quality and reliability of information but will not necessarily increase financial inclusion. The PCR holds data about a population that is already "banked" and will improve credit risks reviews for clients with an existing credit history, but will not incorporate alternative data (e.g. from mobiles) that is one of the best mechanisms to enlarge financial inclusion.

21. **The credit registry has positive and negative information about borrowers' credits from banks that are more than CVE 1,000.** Available information includes type of credit (utilized vs available), type of borrower (individual vs legal entities; resident vs non-resident), address, loan maturity (short, medium, and long-term), guarantees (assets vs personal), and credit quality (performing, non-performing, in judicial process, write-off, and restructured). BCV aims to expand the type of information available, including the loan modality, lending rate, currency denomination, and gender-disaggregated data. BCV is expected to improve its reporting templates for banks for regular reporting of loans outstanding (by number and value) among corporate, household and public sector, and within its corporate category for MSMEs. Reporting requirements for microfinance institutions will also be modified to capture the number and value of loans to MSMEs.

22. **A private credit bureau was established in 2013 but is not currently operating and was constrained by the lack of coordination and the absence of a conducive regulatory environment.** The bureau was established by the chambers of commerce in Cabo Verde and an international partner, to offer full and semi-full credit reports for both consumers and businesses. Financial institutions are yet to join the bureau.

23. **Determining the creditworthiness of small businesses is challenging and costly, and therefore banks require small firms to provide higher levels of collateral** (an average of 201 percent of the loan, against an average of 176 percent for all firms).[15] Banks rely on real estate, cash deposits, and third-party guarantees (*aval*) as collateral for loans, since these receive a reduced risk weight for the purposes of calculating regulatory solvency ratios. Banks do not tend to lend against inventory or make use of cash-flow-based financing. There is no movable collateral registry and no leasing industry, although some banks engage in sporadic leasing activities.

[15] Enterprise Surveys. 2009. (http://www.enterprisesurveys.org/data/exploreeconomies/2009/cabo-verde#finance)

24. **There is limited institutional capacity to facilitate greater provision of bank credit to MSMEs.** Public support programs and agencies have some capacity to support development of small enterprises but their activities remain modest. In 2017, the government established ProEmpresa to support capacity building for MSMEs, in partnership with existing business incubators and business associations that will be responsible for implementation of the programs.[16] ProEmpresa will be funded by the state budget.

25. **MSMEs are critical for economic growth and development.** They create jobs, alleviate poverty and raise the standard of living and play an important role in service, export, and tourism value chains. One of the major impediments to access to finance has been the high collateral requirement demanded by lending financial institutions. The majority of MSMEs are unable to provide sufficient or acceptable collateral to obtain finance, leaving them underserved. Governments have undertaken numerous initiatives to create a conducive environment that would facilitate access to finance in a manner that is sound and protects the stability of the financial system. Financial intermediation such as an efficient and streamlined PCG scheme play an important role in facilitating access to finance and supporting MSMEs to grow and create employment. PCG schemes have proved their effectiveness in attaining this goal, given the right structure and support.

C. Proposed Development Objective(s)

Development Objective(s) (From PAD)

The project development objective (PDO) is to increase access to finance for micro, small and medium sized enterprises.

Key Results

26. A stable, competitive, and inclusive financial system capable of providing affordable financial services supports economic growth, employment, and shared prosperity: (i) establishment of a permanent PCG Fund, compliant with all World Bank fiduciary requirements, to enhance MSME finance; (ii) improved MSME's ability to generate and share business and financial information (including preparation of loan applications with financial institutions and improved quality of financial statements; and (iii) Central bank's (Banco de Cabo Verde) credit registry information upgraded and expanded in terms of coverage and depth, in line with the General Principles for Credit Reporting.

D. Project Description

27. **The proposed Project will have the following three main components:** (i) PCG fund to enhance MSME finance; (ii) technical assistance to MSMEs; and (iii) upgrades to improve credit information systems. These components would complement access to finance reforms supported by the CTD Project (insolvency reforms and introduction of a framework for secured transactions).

Component 1: Partial Credit Guarantee Fund to Enhance MSME Finance (USD 10.7 million)

28. **Under this component, the proposed Project will finance activities to support the establishment and operationalization of a PCG fund to improve access to finance for MSMES,**[17] **through *inter alia***: (i) the

[16] In June 2017, the Government created *ProEmpresa* which resulted from the merger of two government-backed institutions—the small-business promotion agency (ADEI) which was responsible for technical assistance to businesses and the Sociedade de Desenvolvimento Empresarial (SDE)—that operated in this area but were uncoordinated and had minimal results.
[17] MSMEs, as defined by the National Statistics Institute (INE), in all sectors will be eligible to receive guarantees, if determined

development of its business plan, financial model, and operational policies and procedures; (ii) undertaking of PCG fund-related outreach and communication activities targeting Participating Financial Institutions (PFIs) and MSMEs; (iii) training to PFIs on accessing the PCG fund; and (iv) capitalization of the PCG fund. The scheme will apply the Principles for Public Credit Guarantee Schemes.

29. **Implementation of this component will proceed in two phases.** The initial phase will involve establishing a pilot PCG fund administered by an independent firm (Fund Manager) responsible for developing the business plan, financial model, operational policies and procedures including the selection criteria for PFIs. The Fund Manager will be selected through an international competitive bidding process. The Fund Manager will have a performance-based contract that will balance outreach and sustainability.

30. **The Fund Manager will define strategies, policies and action plans to promote the use of the resources of the PCG fund.** The Fund Manager will select PFIs based on financial and prudential indicators and minimum performance ratios. PFIs must maintain adequate prudential ratios relating to capital adequacy, asset quality, and liquidity to be considered eligible. Only PFIs licensed and supervised by the BCV will be eligible to participate. The selected PFIs should have and use internal Environmental and Social Safeguards systems that comply with the national and World Bank's environment and social policies. PFI selection will be subject to non-objection by the World Bank.

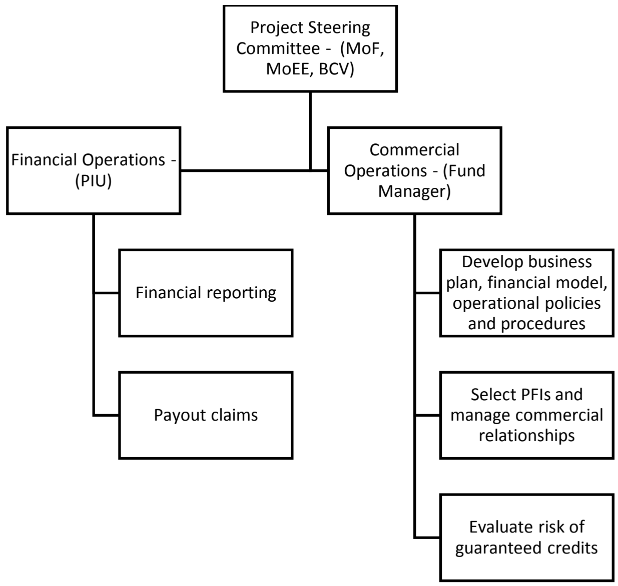
31. **The Fund Manager will determine the conditions of operation with PFIs, and define information requirements and support systems for the institutions that utilize the fund.** The Fund Manager will develop actions to evaluate and measure the risk of guaranteed credits; exercise control on all operations arising from the administration of the PCG fund; ensure compliance with the regulations governing the PCG fund; study and propose regulatory and administrative changes that help optimize the use of the PCG fund; develop commercial dissemination functions and train financial institutions, MSME and others in order to increase take up of the fund.[18] It will provide legal, operational, and commercial advice to PFIs in their effort to serve MSMEs.

32. **The Project Implementation Unit (PIU) will manage the fiduciary aspects related to application of guarantees financed by the PCG fund**. The PIU will be responsible for matters related to the preparation of financial statements and accounts, evaluation of systems and operational risk (e.g. cash flow), and payment of claims as directed by the Fund Manager. The Fund Manager will provide the necessary information to manage these fiduciary aspects. The Project Steering Committee will provide overall guidance and oversight of project implementation as outlined in the figure below.

creditworthy by a PFI. All MSMEs with annual sales of less than CVE 150 million (equivalent to about USD 1.6 million), in line with INE's definition, will be eligible. MSMEs must have been in operation for at least two years. Start-ups with less than 1 year of operation are eligible, but the guarantee will be capped at CVE 2.5 million.

[18] The Fund Manager will sign umbrella contracts with each PFI, defining terms and conditions for individual guarantees. The Fund Manager would also approve a limit for each PFI for the total number of guarantees for a certain period (e.g., 1 year). The PFI would then decide which MSME loans will be covered by a guarantee, as long as the loan meets the eligibility criteria, and reflect this in each MSME loan contract. In this model, there is no individual certificate of guarantee, as the guarantee is reflected in each loan contract. The PFI submits a list of guaranteed MSME loans to the Fund Manager. Payouts are made on an individual basis (not on a portfolio basis).

Figure 1: Project Implementation Structure



33. **Capitalization of the PCG fund will take place in tranches. The first tranche will be disbursed upon the adoption of the following disbursement conditions**: (i) adoption of operational lending guidelines for the PCG fund; (ii) adoption by the fund of corporate governance instruments including a separate external audit for the fund; and (iii) and internal and external controls for the fund satisfactory to the Bank. Further disbursements will be based on demand for PCGs.

34. **The subsequent phase will involve the establishment of a permanent PCG Fund that would combine the functions currently split between the Fund Manager and the PIU.** The World Bank has provided recommendations to the Government for establishing a permanent fund administration. During project implementation, the Ministry of Finance will decide on the best legal and institutional approach for a permanent PCG Fund. This phase would commence following the adoption of a legal framework and management structure capable of administering the operational and the fiduciary functions of the PCG fund. The permanent PCG Fund would have to comply with all World Bank fiduciary requirements in order to administer the funds. If the Recipient assesses that establishment of a permanent PCG Fund is viable and sustainable, then a transition road map would be developed to transfer resources from the Fund Manager and the PIU to the permanent PCG Fund. The permanent PCG Fund would need to be established legally with fiduciary and operational responsibility for administering credit guarantees.

Component 2: Technical Assistance for MSMEs (USD 3.0 million)

35. **Under this component, the Project will finance activities to support MSMEs in generating and providing business and financial information to financial institutions in the context of their loan applications,** including through, inter alia, the provision of accounting and auditing services to MSMEs and support in the preparation of business plans and feasibility studies for new ventures. This will include support to MSMEs for preparation of loan applications with financial institutions in a clear and complete manner, including improved quality of financial statements. This component is critical to improve credit demand, as banks' current business model requires MSMEs to have proper accounting: according to a recent BCV study, 92.5 percent of businesses that received bank credit had organized accounting. Therefore, this component complements Component 1.

36. **This component will be managed by a professional service provider that will be selected through an international competitive bidding process.** Its design is simple, focused on consulting services that are relatively standard, and the selection procedure is fairly automatic. It benefits from knowledge developed in the Bank for designing these programs, including in Cabo Verde. In particular, the project follows the findings of a 2016 IEG evaluation that highlighted the positive impacts of a Bank project that supported a similar facility for technical assistance services in Cabo Verde, which helped enhance the capacity of private operators (especially MSMEs). It will partner with government agencies with a mandate to support MSMEs and private sector stakeholders, including the chambers of commerce, which have experience in this area. The service provider will request feedback from financial institutions regarding the loan applications and share information with the PCG fund manager that will provide technical assistance to PFIs.

37. **This component will help address market failures in Cabo Verde's MSMEs credit market, which suffers from risk aversion as financial institutions lack information to appraise MSME creditworthiness.** It will support utilization of the PCG fund and other credit enhancement mechanisms, which needs to be complemented by improved financial reporting capacity of MSMEs as well as better business and financial plans and models. Implementation on this component will involve the provision of professional accounting and auditing services to improve financial statements and will provide an incentive for MSMEs to formalize.

Component 3: Improve Credit Information Systems (USD 0.8 million)

38. **This component will support an upgrade and expansion of the coverage and depth of information contained in the central bank's credit registry, in line with the General Principles for Credit Reporting**.[19] It will also support measures to establish effective oversight of credit reporting systems, including of a system where the public registry complements the provision of credit information by private bureaus. The project will assist the Recipient in producing more detailed data to better inform policy interventions to support access to finance by MSMEs. Specifically, the project will finance the following:

i. Consulting services to the BCV to assess gaps in its existing registry and opportunities for upgrades including by expanding data availability (e.g., connecting with other databases, such as tax administration, social security, and customs, and by providing gender disaggregated and geo-located data), improving the client interface, providing new value-added services, and workshops designed to build consensus on required actions to improve the credit reporting system in Cabo Verde;

ii. Hardware and software development for the public credit registry, as identified by the needs assessment;

iii. Consulting services to improve reporting templates for commercial banks for regular reporting of loans outstanding (by number and value) among corporate, household and public sector, and within its corporate category for MSMEs. This could also entail modifications to reporting requirements for microfinance institutions to capture the number and value of loans to MSMEs; and

iv. Consulting services for the design and implementation of an electronic database for collection and processing of economic and financial data of non-financial corporations (*Central de Balanços*) to enable a more efficient collection of financial statements to be used by the tax and statistical

[19] The World Bank. 2011. *General Principles for Credit Reporting*. Washington D.C.

authorities.

39. **Credit reporting systems are a crucial component of the financial infrastructure that promotes access to finance and financial stability.** Comprehensive and well-functioning credit reporting reduces information asymmetries, supports efficient credit allocation, and strengthens credit risk management. It enables lenders to make better credit decisions and the BCV to better supervise the financial system. The credit reporting system should be safe and efficient, and fully supportive of data subject/consumer rights. It should be complemented by efforts to increase financial inclusion and the number of individuals and firms with access to credit.

40. **The main utilization of the PCR will be for internal purposes.** This includes utilizing credit reporting data for micro and macro-prudential supervision, monetary policy, statistics, trends, and risk management, particularly on large borrowers and significant banks. In practice, the PCR should be a data-warehouse supplied by different sources among which the banks provide regular updates, allowing data extraction and dynamic reporting to any central bank departments.

Component 4: Project Implementation (USD 0.5 million)

41. The project will cover the project implementation costs (i.e., coordination, procurement, financial management, monitoring, and evaluation).

E. Implementation

Institutional and Implementation Arrangements

42. **The Ministry of Finance will oversee project implementation. The Implementation of Special Projects Unit (*Unidade de Gestão de Projetos Especiais*—UGPE) will be the PIU within the Ministry of Finance and will be responsible for implementing the project with full fiduciary responsibility.** UGPE will have responsibility for the day-to-day project management and coordination of project-related activities, including overall responsibility for, *inter alia*: (a) ensuring timely implementation of the project in accordance with the Project Implementation Manual (PIM); (b) overseeing project activities under its direct responsibility and of project-related activities to be carried-out by other entities; (c) managing Project finances and maintaining consolidated project accounts; (d) developing and maintaining a system for monitoring the project performance indicators; and (e) preparing progress reports, including updates to the Results Framework, budgets, and Procurement Plan. A dedicated Project Manager (PM) may be appointed within UGPE, with responsibility for day-to-day implementation and management of the Project. The PM would be selected competitively on the basis of qualification and experience through procedures acceptable to the Bank.

43. **To ensure proper coordination and supervision of the project, the Financial Reforms Committee chaired by the Minister of Finance will serve as the Project Steering Committee, conduct oversight on project implementation, and provide overall policy guidance to the PIU and the Fund Manager.** In addition to the Ministry of Finance (MoF), the committee includes representatives from the Ministry of Economy and Employment (MoEE) and the Bank of Cabo Verde (BCV).

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F. Project location and Salient physical characteristics relevant to the safeguard analysis (if known)

The specific location of the individual MSMEs to be financed under the Project are not known at this time. They could be located anywhere in Cabo Verde where the project will be implemented. The type and scale of activities may vary widely across the geographic and environmental landscapes of the archipelago of islands that constitutes Cabo Verde.

G. Environmental and Social Safeguards Specialists on the Team

Alexandra C. Bezeredi, Social Safeguards Specialist
Medou Lo, Environmental Safeguards Specialist
Mame Safietou Djamil Gueye, Social Safeguards Specialist

SAFEGUARD POLICIES THAT MIGHT APPLY

Safeguard Policies	Triggered?	Explanation (Optional)
Environmental Assessment OP/BP 4.01	Yes	The project triggers Safeguards Policy OP/BP 4.01 (Environmental Assessment) and is classified as category FI project given the potential negative environmental and social impacts associated with the Partial Credit Guarantee (PCG) funds, which is expected to be financed by the project (component 1) and used to guarantee private bank loans to MSMEs. Specific MSME activities and location are not yet defined, but they are expected to be largely related to small and medium scale projects in agriculture, small scale light manufacturing, construction & real estate development, and tourism that will require environmental assessment to ensure that potential adverse effects are mitigated. These could include loss of vegetation due to land clearing, soil degradation due to civil works, nuisance caused by dust and noise from construction activities, risks of injury, increased prevalence of HIV/AIDS and other STDs due to workers potentially coming from other cities/villages, etc. For Component 2 (Technical Assistance to MSMEs), there are no environmental and social risks foreseen. Component 3 (Credit

		Registry Enhancement) only involves IT equipment and TA, which is not expected to generate negative environmental and social impacts. An ESMF has been prepared by the borrower, consulted upon and disclosed both in-country and at the Info Shop before appraisal. The ESMF includes appropriate screening and standard mitigation measures to effectively manage the potential negative impacts.
Natural Habitats OP/BP 4.04	No	The PCG will not guaranty activity that can lead to conversion or degradation of Natural Habitats. The ESMF includes preventive measures for avoiding encroachment or negative leakage on natural habitats.
Forests OP/BP 4.36	No	It is not expected that the guaranteed MSMEs will invest physically in forest ecosystem. However, their agricultural activities may induce indirect deforestation. The ESMF provides guidance to prevent such risks.
Pest Management OP 4.09	No	The project will not support any activity that would require usage of pesticides; therefore, OP 4.09 is not triggered. It is reflected in the ESMF that the project the project will exclude sub-projects intended to finance the purchase of hazardous pesticides, and subprojects that may to lead to substantially increased pesticide use.
Physical Cultural Resources OP/BP 4.11	Yes	The policy for Physical Cultural Resources (OP/BP 4.11) has been triggered because of the prevalence of ecotourism-related MSMEs in Cabo Verde, which can negatively affect national heritage sites. The ESMF includes a Chance-Find Procedures' to be incorporated into all contracts related to civil works.
Indigenous Peoples OP/BP 4.10	No	This policy is not triggered because there are no Indigenous Peoples present in the Project area.
Involuntary Resettlement OP/BP 4.12	No	The World Bank (WB) Policy on Involuntary Resettlement, OP 4.12, will not apply to the Cabo Verde: Access to Finance Project. The financing activities are focused on existing MSMEs. No land take is expected for the project and the PCG will not guarantee investments or activities that result in land acquisition leading to economic or physical displacement. This restriction will be part of the exclusion list in the ESMF and Operations Manual, including a rigorous screening process for potential future investments.
Safety of Dams OP/BP 4.37	No	The ESMF includes an exclusion list for activities

		involving dams.
Projects on International Waterways OP/BP 7.50	No	Subprojects which could potentially affect international waterways will be excluded in the ESMF.
Projects in Disputed Areas OP/BP 7.60	No	In Cabo Verde there is no disputed area as defined under OP 7.60.

KEY SAFEGUARD POLICY ISSUES AND THEIR MANAGEMENT

A. Summary of Key Safeguard Issues

1. Describe any safeguard issues and impacts associated with the proposed project. Identify and describe any potential large scale, significant and/or irreversible impacts:

The potential negative environmental and social negative impacts and risks of the proposed project are associated with the implementation of Component A, which is designed to support a Partial Credit Guarantee Fund (PCG) to enhance MSME Finance. These are expected to be moderate to low, mostly site-specific and easily manageable to an acceptable level. The specific location of MSME activities to be financed under the Project are not known at this time, an Environmental and Social Management Framework (ESMF) was developed by the borrower. It includes a list of transactions that are not eligible for financing under the Project:

No large-scale or irreversible adverse impacts and risks are expected

2. Describe any potential indirect and/or long term impacts due to anticipated future activities in the project area:

No potential indirect and/or long term environmental and social impacts are expected.

3. Describe any project alternatives (if relevant) considered to help avoid or minimize adverse impacts.

N/A

4. Describe measures taken by the borrower to address safeguard policy issues. Provide an assessment of borrower capacity to plan and implement the measures described.

The proposed project will be implemented by the Ministry of Finance, through its Unit for the Implementation of Special Projects (Unidade de Gestão de Projetos Especiais - UGPE), which has implemented several development projects since it was established in 1999. To address issues related to
the safeguard policies triggered, the Government of Cabo Verde (GoCV) has prepared an ESMF.

The ESMF sets forth the principles and guidelines to be followed by the borrowers to comply with the requirements of the triggered policies. It includes a mechanism to review and conduct an environmental screening to avoid and mitigate the environmental and social impacts and risks of potential subprojects eligible for financing by the Participating Financial Institutions (PFIs) that have access to the PCG. Provisions are being made in the ESMF to address issues related to Physical Cultural Resources (OP/BP 4.11).

To mitigate this risk, the PCG Management will include a part-time environmental and social safeguards specialist to adequately handle the implementation of environmental recommendations. The ESMF includes an allocation of USD

70,000 for its implementation.

5. Identify the key stakeholders and describe the mechanisms for consultation and disclosure on safeguard policies, with an emphasis on potentially affected people.
The key stakeholders of the proposed project include government agencies with a mandate to support MSMEs, the MSME borrowers, their creditors (Partner Financial Institutions), and the chambers of commerce. The preparation of this ESMF has followed a consultation process and a one day workshop has been held for discussion among stakeholders, including commercial banks. As this is an interactive process, further consultations will be done throughout project implementation.

B. Disclosure Requirements

Environmental Assessment/Audit/Management Plan/Other

Date of receipt by the Bank	Date of submission for disclosure	For category A projects, date of distributing the Executive Summary of the EA to the Executive Directors
23-Oct-2017	02-Nov-2017	

"In country" Disclosure

Cabo Verde
30-Oct-2017

Comments

The ESMF has been disclosed in country in the Sistema de Informação Ambiental web page (www.sia.cv)

C. Compliance Monitoring Indicators at the Corporate Level (to be filled in when the ISDS is finalized by the project decision meeting)

OP/BP/GP 4.01 - Environment Assessment

Does the project require a stand-alone EA (including EMP) report?
Yes
If yes, then did the Regional Environment Unit or Practice Manager (PM) review and approve the EA report?
Yes
Are the cost and the accountabilities for the EMP incorporated in the credit/loan?
Yes

OP/BP 4.11 - Physical Cultural Resources

Does the EA include adequate measures related to cultural property?
Yes
Does the credit/loan incorporate mechanisms to mitigate the potential adverse impacts on cultural property?

Yes

The World Bank Policy on Disclosure of Information

Have relevant safeguard policies documents been sent to the World Bank for disclosure?
Yes
Have relevant documents been disclosed in-country in a public place in a form and language that are understandable and accessible to project-affected groups and local NGOs?
Yes

All Safeguard Policies

Have satisfactory calendar, budget and clear institutional responsibilities been prepared for the implementation of measures related to safeguard policies?
Yes
Have costs related to safeguard policy measures been included in the project cost?
Yes
Does the Monitoring and Evaluation system of the project include the monitoring of safeguard impacts and measures related to safeguard policies?
Yes
Have satisfactory implementation arrangements been agreed with the borrower and the same been adequately reflected in the project legal documents?
Yes

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