Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 03-May-2024 | Report No: PIDPC00085

BASIC INFORMATION

A. Basic Program Data

Project Beneficiary(ies)	Region	Operation ID	Operation Name
Ukraine	EUROPE AND CENTRAL ASIA	P505616	Resilient, Inclusive and Sustainable Enterprise Project
Financing Instrument	Estimated Appraisal Date	Estimated Approval Date	Practice Area (Lead)
Program-for-Results Financing (PforR)	16-Jul-2024	31-Oct-2024	Finance, Competitiveness and Innovation
Borrower(s)	Implementing Agency		
Ministry of Finance	Ministry of Economy		

Proposed Program Development Objective(s)

Improve the enabling environment for a sustainable private sector-led recovery in Ukraine.

COST & FINANCING (US$, Millions)

Maximizing Finance for Development

Is this an MFD-Enabling Project (MFD-EP)? Yes

Is this project Private Capital Enabling (PCE)? Yes

SUMMARY

Government program Cost	**1,900.00**
Total Operation Cost	**1,530.00**
Total Program Cost	1,499.89
IPF Component	30.00
Other Costs (Front-end fee,IBRD)	0.11
Total Financing	**480.00**
Financing Gap	**1,050.00**

FINANCING

Total World Bank Group Financing	**450.00**
World Bank Lending	450.00
Total Non-World Bank Group Financing	**30.00**
Trust Funds	30.00

Concept Review Decision

The review did authorize the preparation to continue

B. Introduction and Context

Country Context

1. **While Ukraine's economy shows signs of a modest recovery, Russia's invasion of Ukraine continues to impose an immense human and economic toll.** As of February 2024, at least 10,582 civilians, including 587 children, have been killed and 19,875 have been injured since February 24, 2022. To date, over 5.9 million people have fled abroad and millions remain internally displaced (according to the UNHCR). Loss of private sector jobs and income, high inflation, and asset losses have reversed 15 years of poverty reduction. Based on the global line of US$6.85 a day (2017 PPP), poverty is estimated to have increased from 5.5 percent to 24.1 percent in 2022, pushing 7.1 million more people into poverty. While Ukraine's economy contracted by 28.8 percent in 2022, it has shown signs of a modest recovery in 2023, growing by 5.3 percent.

2. **Ukraine's policy framework is at an inflection point, transitioning from a focus on short-term macro stabilization towards a medium-term focus on resilience, growth, and sustainability.** Ukraine has been able to maintain macroeconomic stability since February 2022, controlling inflation, maintaining a stable currency, financing critical expenditure, and accumulating over US$ 40 billion in foreign exchange reserves. The receipt of significant external aid - US$42.5 billion in 2023 – was instrumental to this achievement. At the same time, as the magnitude and timing of external aid inflows is becoming increasingly uncertain, Ukraine seeks to reduce its aid dependence and use existing aid inflows to stimulate growth and generate real and productive resource transfers. A renewed focus on reforms that encourage capital accumulation, strengthen productivity, help close the output gap by enabling access to external markets, and alleviate critical institutional growth constraints is critical.

3. **Successful recovery and reconstruction, and progress toward EU standards, will require significant institutional reforms that both strengthen public sector capacity and facilitate a competitive private sector**. Implementation of extensive reforms—both prior to the invasion and during the past two years— has played a major role in enabling the government to deliver on its core functions and initiate recovery. But further changes are needed. Experience from other post-war situations highlights the central role of government in managing resource allocation and ensuring coordination during the reconstruction process. Moreover, given the scale of financing needs and the capacity of the Ukrainian private sector, there is a significant opportunity and need to take full advantage of the potential for the

private sector to finance and execute recovery and reconstruction investments. In this context, the Ukraine Plan — which includes economy-wide and sectoral reforms, increasing the capacity to absorb investment, and crosscutting issues such as European integration, digital transformation, green transition, environmental protection, as well as human capital— plays a critical role over the coming years.

4. **The National Economic Strategy (NES) (2021-2030), the Ukraine Plan (2024-2027) and Ukraine's Reforms Matrix 2024 lay out key reforms to support SMEs and stimulate business activity.** Key relevant reform areas of the NES focus on entrepreneurship development, regulatory environment, investment attractiveness and international economic policy and trade. The recently adopted Ukraine Plan (2024-2027) focuses on three key directions as regards to the private sector reform agenda: improving the regulatory environment, facilitating access to finance and markets, and harmonizing Ukrainian legislation and standards with the EU with the transition to a green, digital, and inclusive economy being stipulated as cross-cutting themes. Relevant reforms are also outlined in Ukraine's Reforms Matrix's pillar on economic competitiveness.

Sectoral (or multi-sectoral) and Institutional Context of the Program

5. **Businesses, in particular SMEs[1] – the cornerstone of the Ukrainian economy, have been greatly affected by Russia's invasion of Ukraine.** Since February 2022 the number of active enterprises fell by 15 percent, to about 760,000 entities, most (86 percent) of which were micro or small enterprises, with fewer than 50 employees. The war impacted Ukraine's private sector through various transmission channels: first, through demand shocks, which were driven by reduction in domestic consumer spending, loss of access to crucial export markets, and heightened uncertainty about sales outlook, and second, through supply shocks, which encompassed damage, labor and input shortages, logistical disruptions, and limited access to financing. The extent of these impacts varies depending on firms' sector, location, market presence, and size. The latest Rapid Damage and Needs Assessment of February 2024 (RDNA3) estimates the damages sustained by the private sector at US$15.6 billion, a 43 percent increase above the estimate of US$10.9 billion reported in RDNA2 for the previous year. Around 21 percent of firms experienced war-related damage, with an average 53 percent drop in sales across firms of all sizes and sectors, a 25 percent reduction in employment, and a dramatic 76 percent fall in investment (80 percent decline for medium sized firms). Around 15 percent of all firms and up to 20 percent of manufacturing firms experienced power outages.[2] A total of 2.4 million jobs, or 15.5 percent of the total, were lost in 2022. [3]

6. Ukraine's economic recovery is dependent on harnessing the dynamism of the private sector, which has shown remarkable resilience through the war. Many Ukrainian firms that continued operation after the invasion have adapted their business strategies proactively and resiliently. They continued operating at a lower capacity (44 percent average capacity utilization, with two-thirds of manufacturing enterprises managing to operate at 75 percent of capacity or higher), sought new customers and markets (36 percent), leveraged digital tools (41 percent), changed their product/services mix (17 percent), and adopted supply chain optimization techniques (12 percent).[4] Foreign investors and multinational corporations (MNCs) also stayed the course in Ukraine, with only 10 percent reducing productive capacity and almost no divestment of local subsidiaries. Many MNCs even expanded their investment by purchasing new fixed assets (30 percent), repairing or renovating existing assets (40 percent), or even acquiring new subsidiaries (3 percent).

[1] SMEs account for two-thirds of total value added and over 80 percent of private sector jobs.
[2] World Bank, "Ukraine: Firms through the War," November 2023, Link.
[3] International Labour Organization "Care at Work in Ukraine" Brief, November 2023.
[4] World Bank, "Ukraine: Firms through the War," November 2023, Link

7. **Improving the business environment is crucial for Ukraine's private sector-led economic recovery**. An ineffective business environment, characterized by pervasive regulation and overlapping state controls, remains a fundamental structural challenge to harness for the economic recovery the dynamism and resilience shown by firms since the invasion. Despite the recent progress made by the GoU in simplifying business regulation, complex, outdated, and burdensome regulations remain in effect, and stand in the way of a full harmonization with EU legal and regulatory framework for firms' entry, operation, and exit. According to the Ukraine Plan 2024-2027, in 2023 there were 84 areas of state supervision and control and over 30 inspection bodies with duplicating functions. As of mid-2024, there are over 1000 instruments of state regulation, including 528 permits, 224 licenses, 157 approvals, 145 conclusions, 121 certificates, 55 declarations, 42 notifications, and 23 authorizations, along with hundreds of product standards. This includes old Soviet-type business regulations that stifle process and product innovation and the adoption of sustainable production practices and green technologies. Since February 2022, many companies restructured their business models with 18 percent prioritizing marketing among the business functions upgraded through new technology and processes, followed by business administration (15 percent), and 11 percent focusing on "Production" or "Service Planning" functions. The persistence of burdensome and outdated regulation will continue to restrain the proactive adoption of new business models and strategies by firms, with simplification of regulation ranked as a top priority by 76 percent of firms as of March 2024. The GoU is committed to improve the business environment through a systemic regulatory simplification and full digitalization of government-to-business (G2B) services, as a top policy priority of the National Economic Strategy (NES) (2021-2030) and the Ukraine Plan (2024-2027).

8. **Access to international markets and enhanced export competitiveness of Ukrainian firms, enabled by a progressive harmonization and integration with the European Union (EU), are key drivers of a sustainable export-led recovery.** World Bank and NBU estimates suggest that Ukraine's output gap – the difference between what the economy can theoretically produce and actual output – currently stands at between 20 and 25 percent of actual output.[5] Closing this gap by facilitating access to export demand is thus an immediate opportunity to accelerate growth. The war caused a significant drop in exports, with 95 percent of firms exporting to the Russian and Belarusian markets suffering a complete halt, and 75 percent of firms exporting to other markets experiencing sharp declines. Supply chain disruptions hindered exports for around 80 percent of large firms and 70 percent of small firms. Approximately 65 percent of firms faced shortages of imported raw materials or intermediate inputs, which resulted in sales cancellations for more than one-fourth of firms. At the same time, the loss of traditional CIS export markets accelerated the ongoing transition towards the EU market, with the share of Ukrainian exports to the EU jumping from around 32 percent in 2020 to around 44 percent in 2022. Aligning legislation and regulation with EU trade framework, strengthening the competitiveness of Ukrainian exporters through greater access to export credit and war risk insurance, and harmonizing Ukrainian National Quality Infrastructure (NQI) with the EU, including product quality, safety, energy efficiency, environmental, and overall sustainability standards, are top policy priorities of the Government of Ukraine to lay the foundations for an export-led recovery.

9. **Priority recovery and reconstruction needs for firms in 2024 amount to US$ 5.8 billion, and the public sector can help jump-start private sector-led recovery efforts.** According to the RDNA3 priority needs include financing for investments in new equipment, improved processes, repair of buildings, creation of new businesses, as well as working capital. Most firms, even those that suffered no physical damage, have seen revenue fall due to disrupted infrastructure and electricity blackouts, contracting domestic markets, and broken supply chains. The private sector has also incurred costs for service delivery restoration via introduction of new business models, asset relocation and other working capital needs, training and reskilling of employees, and investments to meet EU and other international standards. Firms also need support to address their constrained access to finance. Bank lending has been subdued as a result of the war—performing corporate loans in UAH have declined by 8 percent (as of end 2023) compared to

[5] NBU 2023.

prewar levels —but demand for financing remains high. Some 84 percent of firms face constraints in accessing finance, in part because of high interest rates. Although firms will bear the cost of most investments, public sector support is vital to help firms survive and make the investments needed to continue operating during the war and be ready for the recovery.

10. **Firm support programs have become an important lifeline for SMEs, and businesses in general, but require strategic re-focusing and optimization in line with international best practices.** Firm support programs deployed by the Government of Ukraine (GoU) in the immediate aftermath of Russia's invasion show a significant potential for revamping and rationalization. Only 8 percent of firms participated in support programs, with a lower rate of 6 percent among SMEs. The lack of awareness, access and eligibility impacted the use of these programs, with only 26 percent of firms aware of them, and 15 percent of firms unable to find a suitable program. At the same time, participating firms performed better than non-beneficiaries in terms of sales (-8 percent vs. -15 percent), employment retention (-2 percent vs. -4 percent), and investment (+124 percent vs. +22 percent) as of March 2024, showing the potential benefits of revamped firm support programs also in accelerating the adoption of EU climate and environmental standards. The Government of Ukraine is committed to improve the efficiency, effectiveness, and sustainability of public policies and programs supporting the private sector, starting with a multiphase Policy Effectiveness Review (PER) of the overall policy mix and program portfolio of the Ministry of Economy in support of SMEs, and with the institutionalization of systemic monitoring and evaluation and policy recalibration mechanisms related to the private sector.

Relationship to CAS/CPF

11. **RISE is part of the WBG effort to support the people of Ukraine which has mobilized over US$41 billion since February 2022**. The World Bank engagement is guided by the Ukraine Country Program Update, submitted to the Board in June 2023, which identifies maintaining essential public services and relief efforts, supporting repair and reconstruction of core infrastructure, sustaining the private sector, and supporting key reforms for sustained economic growth when the war ends as priorities for the period from June 2023 to June 2024. This operation focuses on the last two of these objectives. Other operations directly complement this PfoR through support to related areas, such as the Ukraine Agriculture Recovery Inclusive Support Emergency (ARISE) project that supports the 5-7-9 program in the agricultural sector. Similarly, RISE supports critical implementation steps that complement the private sector reforms supported in DPOs.

Rationale for Bank Engagement and Choice of Financing Instrument

12. **The PforR instrument is considered the most appropriate instrument to support the private sector and SME recovery agenda because it focuses on reform implementation and results, uses government systems and supports institutional strengthening**. The rationale for Bank engagement and use of the PforR financing instrument for supporting Ukraine's National Economic Strategy (NES) 2021-2030 and Ukraine Plan 2024-2027 is realistic due to its emphasis on results, flexibility, capacity building, governance, and the potential to attract further support, all of which are critical in navigating the complexities of the current country situation while laying the foundations for future recovery. The PforR complements Development Policy Operations, which focus on the development and approval of policy and regulatory framework for reforms, by supporting the implementation and application of policies and regulations. Technical assistance needs to support reform implementation will be met partly from an investment component under the PforR.

C. Program Development Objective(s) (PDO) and PDO Level Results Indicators

Program Development Objective(s)

Improve the enabling environment for a sustainable private sector-led recovery in Ukraine.

PDO Level Results Indicators

- PDO Indicator 1: number of beneficiaries participating in redesigned firm support programs
- PDO Indicator 2: number of firms benefiting from streamlined business regulation and G2B digital services
- PDO Indicator 3: amount of domestic and foreign capital mobilized, including in green economy industries
- PDO Indicator 4: increase in exports by beneficiaries of the firm support programs of the MoE

D. Program Description

PforR Program Boundary

13. **The Program will support the implementation of selected components of the Government's National Economic Strategy (NES) (2021-2030) and the Ukraine Plan (2024-2027).** The program also builds upon Ukraine's Reforms Matrix's pillar on economic competitiveness. The Government has requested the Bank support for the implementation of reforms that are critical for private sector recovery. In particular, it will support reforms in three results areas: (i) improving efficiency, effectiveness, and sustainability of state support to SMEs, with a focus on green competitiveness, (ii) improving the business environment through regulatory simplification, G2B digital services, and investment facilitation, and (iii) improving SMEs access to export markets.

E. Initial Environmental and Social Screening

14. **The environmental risks of the Program are rated Substantial (PforR component).** The Program will have a number of positive environmental effects resulting from enhancing green competitive policies (such as adoption of the National Energy and Climate Plan of Ukraine 2025-2030and ESG requirements) for financial institutions that support SMEs. At concept stage, the main potential negative environmental impacts are associated with the effects of business activities of SMEs in diverse sectors across the country supported by the Program. These activities will have potential environmental risks and impacts related to construction as well as operation-related pollution (including air, water, soil pollution; waste management), resources utilization, biodiversity impacts and cultural heritage impacts, as well as OHS and community health and safety. While the scale of business activities of SMEs is deemed relatively limited, the Program will ensure to exclude activities with significant adverse environmental impacts (such as projects impeding on critical habitats or known cultural heritage sites and sectors that could cause significant environmental hazards). While some implementing agencies have operational experience with WB E&S policies/standards under IPF and PforR (such as MoF, and BDF), the E&S systems of other institutions (such as MoE

and ECA) are broadly unknown at this stage. The ESSA will further assess the capacity of relevant institutions in addressing potential E&S risks and impacts and propose mitigation measures to address identified gaps which will be integrated as part of DLIs/verification protocols and/or PAPs.

15. **The social risks of the Program are rated Substantial (PforR component).** The Program will have positive social effects, in particular the creation of job opportunities in SMEs, which account for over 80 percent of private sector jobs, and improved labor and working conditions in such SMEs through the enhanced E&S risk management and monitoring systems of the financial institutions. At concept stage, the main potential negative social impacts associated with business activities of SMEs include (i) risks related to labor and working conditions of SMEs workers (including vulnerable groups of workers and workplace SEA/SH risks); (ii) land acquisition and resettlement of informal users (while the client government institutions will not directly acquire lands for the Program, the Program may support SMEs that could purchase lands in the market for their businesses, including the development of some industrial parks); (iii) exclusion of vulnerable groups where the business owners of SMEs have limited access to the Program (such as female business owners or those in remote areas or who have limited access to ITs). The exclusion of vulnerable stakeholders could also happen where stakeholder and citizen engagement processes are weak; (iv) social tensions or conflicts/grievances over the Program if the relevant implementing institutions have inadequate grievance redress systems; and (v) safety risks related to war hazards (such as ERW, landmines and aerial strikes) which could affect business activities. While the scale of business activities of SMEs is deemed relatively limited, the Program will ensure to exclude activities with significant adverse social impacts (for example, significant resettlement or areas with significant war hazards in de-occupied territories). The ESSA will further assess the magnitude of these potential social risks and the capacity of relevant institutions in addressing such risks, which will inform the gap filling measures.

16. **An ESSA will be prepared by the Bank team by appraisal as required**. Based on the defined Program boundaries, the ESSA will: (a) further assess the different environmental and social effects associated with the Program's activities, including direct, indirect and cumulative effects; (b) assess the capacity of Government institutions in addressing relevant E&S risks and identify any gaps in implementing E&S measures; (c) compares the borrower's E&S systems—laws, regulations, standards, procedures, and implementation performance—against the PforR core E&S principles to ensure its consistency with the PforR policy; and (d) formulate recommended measures to address any identified gaps and strengthen the borrower's system to manage E&S risks and impacts of the Program. The ESSA will be consulted on-line with different stakeholders including representatives of potential vulnerable groups, taking into consideration the martial law restrictions. The feedback of stakeholders will be incorporated in the ESSA. The ESSA will be disclosed by appraisal.

17. **The Environmental and Social Risk Rating for the IPF component is considered Moderate**. The IPF component will provide the Government with TA activities (Type 2 and 3 TA activities). The potential project-related E&S risks and impacts from such TA activities are not likely to be significant. More details are provided in the Concept stage E&S Review Summary (C-ESRS).

Legal Operational Policies

	Triggered?	
	Last approved	**Current**

Projects on International Waterways OP 7.50	No
Projects in Disputed Area OP 7.60	No

Summary of Screening of Environmental and Social Risks and Impacts of the IPF Component

The Environmental Risk Rating for the IPF component is considered Moderate. The proposed project is an IPF component of a broader Program for Results (PforR) operation. The IPF activities focused on operational support to implementing agencies and change management primarily aim to strengthen institutional capacities and facilitate capacity building. These activities involve engaging consultants and potentially recruiting new government staff. The potential risks include lack of adherence to fair labor practices and unsafe working conditions. In addition, given the context of Ukraine, potential risks include community health and safety concerns related to war hazards, such as explosive remnants of war and aerial strikes. The TA on developing a green regulatory framework to align SMEs with the European Green Deal objectives would result in significant environmental benefits. However, the transition process (from their current state of operations to a more improved, energy efficient and sustainable state that aligns with the European Green Deal) may also result in some adverse impacts. These negative impacts may typically arise from the implementation of new technologies and changes to the existing infrastructure needed to achieve these goals as well as handling of obsolete equipment, systems and materials. The activities related to IT solutions and development of digital platforms require energy use and generate electronic waste that require diligent handling. Giving the existing practices relating to the reuse and recycle of such wastes, the envisaged quantity of e-wastes that will be generated will be small and relatively easy to manage in a manner that is consistent with the ESF and other international conventions, such as the Basel convention on the trans-boundary movement of hazardous substances. The potential project-related risks and impacts on the environment from TA activities are likely to be site-specific, moderate in scale and can be mitigated in a predictable manner. The Program will ensure incorporation of proper safety measures in line with national legislation and War-Hazard Emergency Preparedness and Response Guidance into all envisaged activities requiring physical presence of people on site. Also, the ESCP for the project will specify that the terms of reference and outputs of technical assistance, such as on developing a green regulatory framework, shall be conducted in a manner consistent with the ESF. During project preparation, when the nature and scope of the activities which will be supported by the TA are known, they will be screened for potential environmental risks and impacts, and environmental risk rating will be revised if needed. The Social Risk Rating for the IPF component is considered Moderate. While the proposed TA activities themselves will carry limited social risks or impacts, there are potential risks for the project workers (PCU staff and other consultants engaged for TA activities) regarding the labor and working conditions (including fair treatment, non-discrimination and equal opportunities, SEA/SH risks at workplace and access to grievance mechanism), in addition to the safety risks stemming from war hazards (as highlighted in the environmental risk rating section). Other social risks relate to potential inadequate inclusion of vulnerable groups in capacity building and stakeholder engagement activities while the Program is nationwide in geographic scope and takes place within the context of the Russian invasion of Ukraine. Subject to overriding security concerns and the implications of martial law, the project will ensure transparency and accessibility to TA activities through stakeholder participation, public information disclosure and grievance mechanism through the use of IT tools (online consultations etc.). While the SEA/SH risk rating for this IPF component is considered Low, it will implement relevant mitigation measures including

SEA/SH code of conduct to manage relevant risks during the TA activities, as per the Good Practice Note on managing SEA/SH risks.

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