Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 12-Jan-2022| Report No: PIDC33521

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Brazil	P177632	BR State of Goias Sustainable Recovery DPF (P177632)	
Region	**Estimated Board Date**	**Practice Area (Lead)**	**Financing Instrument**
LATIN AMERICA AND CARIBBEAN	Apr 13, 2022	Macroeconomics, Trade and Investment	Development Policy Financing
Borrower(s)	**Implementing Agency**		
Secretaria da Economia	Secretaria de Estado de Agricultura, Pecuária e Abastecimento (SEAPA), Secretaria Estadual de Meio Ambiente e Desenvolvimento Sustentável de Goiás (SEMAD)		

Proposed Development Objective(s)

The Program Development Objective of this DPF is to (i) improve fiscal sustainability; and (ii) enhance climate resilience and environmental sustainability.

Financing (in US$, Millions)

SUMMARY

Total Financing	500.00

DETAILS

Total World Bank Group Financing	500.00
World Bank Lending	500.00

Decision

The review did authorize the preparation to continue

B. Introduction and Context

Country Context

Goiás is facing a weakened fiscal position and significant environmental sustainability challenges that are limiting its ability to pursue a sustainable post COVID-19 recovery. The State fell into fiscal distress prior to the pandemic given rapidly growing personnel spending and high debt service costs, and its finances were further impacted by the COVID-19 crisis. Goiás is also facing significant climate change and environmental sustainability challenges, with growing Greenhouse Gases emissions between 2009 and 2020, mainly, in the Agriculture Sector. This Sustainable Recovery Development Policy Financing (DPF) will support the State in dealing with these challenges by strengthening its fiscal and environmental management frameworks for a more sustainable and climate friendly recovery.

Despite some fiscal relief in 2021 related to higher tax collections, structural fiscal challenges persist and require substantive reforms to tame Goiás spending growth. In 2021, fiscal challenges reemerged once the extraordinary federal assistance of 2020 was not extended in 2021, and debt repayments were reinstated despite an estimated increase of 20 percent in tax revenues caused by the rebound of economic activity and higher inflation. As Goiás is very dependent on its agriculture sector, the booming commodities market in 2021 also played a decisive rule to improve the State's revenues. However, these factors are conjunctural and their revenues growth impacts are not expected to last. These conditions, along with the fiscal difficulties experienced on the spending side prior to the pandemic, motivated the State to pursue a fiscal adjustment path by adhering to the Federal Government Fiscal Recovery Regime Program (FRR), a federal program that supports States in re-establishing fiscal sustainability.

Overall Brazil's macroeconomic policy framework is deemed adequate for this proposed operation. Brazil successfully mitigated the impact of the pandemic on the poor and achieved high vaccination rates by end 2021. These efforts increased fiscal pressures and raised debt, including a further risk of additional demand for social transfers in 2022 as growth slows and the electoral cycle advances. Public debt rollover risks are also significant, as the amount of debt payments within one year is projected to stay above 35 percent of GDP in the next years. However, fiscal adjustment has advanced at a robust pace over the past year despite the high costs of the pandemic. Moreover, the authorities have already budgeted for an increase in social transfers in 2022 and remained committed to observing the spending cap as the main anchor for fiscal framework going forward. Compliance with the spending cap will be supported by the constitutional pension reform adopted in 2019, a civil service pay freeze, and tight control of discretionary spending, including at the sub-national level. Also, the Central Bank independency approved in February 2021 will ensure that monetary policy decisions will be made without political influence. This is helping anchor inflation expectations for 2023 and 2024. Reforms approved in the financial sector in recent years to boost competition and market access will contribute to reduce private borrowing cost and incentivize investments, while the labor market reform implemented in 2017 should contribute to boost employment as the economy grows. In the medium-term, additional structural measures will be required to comply with spending cap, keep the fiscal adjustment on track (such as the already submitted administrative reform or the reframe of inefficient expenditure programs) and boost potential GDP growth.

Relationship to CPF

The proposed DPF is fully aligned with the World Bank Group's Country Partnership Framework (CPF) for the period FY2018–23.[1] The World Bank Group FY18-23 CPF for Brazil (Report no. 113259-BR, discussed by the Executive Directors on July 13, 2017) was prepared against the backdrop of the deep 2014–16 economic recession that led to a fiscal crisis and increased unemployment and poverty levels. The main premise of the CPF was the need to revisit the country's growth model to improve its sustainability and inclusiveness. The CPF is built on three pillars: (i) fiscal consolidation and government effectiveness; (ii) private sector investment and productivity; and (iii) equitable and sustainable development. In line with the CPF, this proposed operation is part of a series of subnational DPFs to support fiscal adjustment and sustainable low-carbon and climate-resilient development in subnational entities. The proposed operation is the third under this framework, following the Mato Grosso Fiscal Adjustment DPF (P164588) and the First Amazonas Fiscal and Environmental Sustainability Programmatic DPF (P172455). The Mato Grosso DPF aimed to support the State to implement of institutional reforms for fiscal sustainability; and consolidate efforts to protect forest assets

[1] The CPF was endorsed by the World Bank's Board of Executive Directors on July 13, 2017 (Report no. 113259-BR).

while promoting agricultural productivity in line with the State's development strategy. The Amazonas DPF supported fiscal discipline, climate-informed decision making, and an integrated approach to forest conservation and development to help the State improve its recovery after COVID-19 and protect the Amazon forest. The operation is fully aligned with CPF objectives 1.1 (Strengthening Fiscal Management) and 1.2 (Increasing Fiscal Sustainability) under CPF Pillar 1, which supports an incentive mechanism for subnational borrowers to address their structural fiscal challenges early on, thus reducing the risk of their finances becoming unsustainable. The operation is also aligned to CPF objectives 3.1 (Supporting the Achievement of Brazil's NDC with a Particular Focus on Land Use) and 3.3 (Promoting Socioeconomic Development of Small Rural Producers and Protecting Vulnerable Groups) under CPF Pillar 3, by focusing particularly on land-use planning, deforestation, environmental compliance, and payment for environmental services in a State that is critical to Brazil's climate mitigation commitments. This pillar is also consistent with the WBG Climate Change Action Plan 2016–2020[2] and 2050 targets to step up climate action so as to support countries in delivering and exceeding their Paris commitments.

C. Proposed Development Objective(s)

The Program Development Objective of this DPF is to (i) improve fiscal sustainability; and (ii) enhance climate resilience and environmental sustainability.

Key Results

This operations is expected to contribute to improve Goiás' fiscal sustainability and enhance its climate resilience. With the implementation of fiscal reforms that restrict recurrent spending growth, the State expects to improve its primary balance and clear its arrears over the coming years, allowing it to fully meet its financing needs. Coupled with the compliance with the Fiscal Responsibility Law limit for personnel spending, the State will recover its credit rating, allowing it to access new credit lines and become eligible to receive federal government's guarantees. The State also expects to shift its agriculture production to a more climate friendly and inclusive path through more sustainable management of its natural resources. In doing so, the State expects to help steer its agricultural sector towards practices that increase carbon storage, reduce GHG emissions and foster adaptation to climate change.

D. Concept Description

Goiás is prioritizing fiscal reforms that restrict recurrent spending growth and would allow it to adhere to the Federal Fiscal Recovery Regime (FRR). These reforms includes: (i) adopting a spending cap rule as medium-term fiscal anchor; (ii) consolidating the cost of civil service pensions; and (iii) consolidating civil service benefits. Goiás is committing to a forward-looking fiscal adjustment plan that sets fiscal targets for the primary balance and the clearance of arrears over the coming years. The fiscal plan also sets personnel spending targets, including limits to salary adjustments and new hires, that will help it to comply with the State's spending cap and recover its credit rating, allowing it to access new credit lines and become eligible to receive federal government's guarantees.

The State also expects to shift to a more climate friendly and inclusive path through more sustainable management of its natural resources. State's sustainable challenges stem mainly from deforestation and land degradation pressures

[2] World Bank, IFC, and MIGA. 2016. World Bank Group Climate Change Action Plan 2016–20: https://openknowledge.worldbank.org/handle/10986/24451.

linked to farming in its Cerrado biome. To revert this, Goiás is adopting a package of reforms includes measures to promote the adoption of bio-inputs in agricultural production to increase soil carbon capture. The package also promotes remediation of deforested and degraded lands to help reverse Goiás' legacy of deforestation and sharpens the climate focus of the State's environmental licensing systems. Finally, it also supports land tenure regularization for smallholders through updated regulations that are environmentally inclusive and recognize women's land title rights. In doing so, the State expects to help steer its agricultural sector towards practices that increase carbon storage, reduce GHG emissions and foster adaptation to climate change.

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

Poverty and Social Impacts

The reforms implemented by Goiás and supported by this DPF are expected to contribute to have positive social impacts and reduce poverty in the State. The policy measures supported under the first pillar (Regaining Fiscal Sustainability) aim to open more fiscal space for public spending social and economic priorities, as well as improving the State's creditworthiness in the medium-term, increasing its access to resources for investment and are expected to have positive indirect poverty and social impacts. The policy changes supported under the second pillar (Enhancing Climate Resilience and Environmental Sustainability) are expected to support a better business environment in Goiás, thus contributing to growth and job creation in the State, having positive effects on rural incomes and having direct poverty and social impacts among certain subgroups of the rural population.

Environmental, Forests, and Other Natural Resource Aspects

The prior actions included in the DPF are likely to result in positive effects on the environment, including natural habitats, biodiversity and quality of natural resources. The actions expected in fiscal pillar represents low potential for negative effects on the environment, but a certain degree of risk cannot be totally discarded, as but both public sector compensation reform and the adoption of the spending rule, if poorly conducted, can pressure the already weakened capacity of the State to manage natural resources. Environmental enforcement, investment in protected areas and fire brigades already suffer from staff reductions and investment limitations. On the other hand, environmental licensing is being reformulated, and may open opportunities to direct human resources to inspection. It is recommended that the fiscal adjustment not affect investments in enforcement, conservation units and firefighting.

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APPROVAL

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