**PROGRAM INFORMATION DOCUMENT (PID)**
**APPRAISAL STAGE**

November 16, 2016
Report No: 111025

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| **Operation Name** | Supplemental Financing for the Fiscal Consolidation Support Grant |
| **Region** | AFRICA |
| **Country** | Chad |
| **Sector** | |
| **Operation ID** | P162548 |
| **Lending Instrument** | Development Policy Lending |
| **Borrower(s)** | REPUBLIC OF CHAD |
| **Implementing Agency** | Ministry of Economy and Finance |
| **Date PID Prepared** | November 16, 2016 |
| **Estimated Date of Appraisal** | |
| **Estimated Date of Board Approval** | December 21, 2016 |
| **Corporate Review Decision** | Following the corporate review, the decision was taken to proceed with the preparation of the operation. |

## I. Country and Sector Background

The Fiscal Consolidation Program Support Grant (FCPSG) was approved by the Board in December 2015 and aimed to maintain macroeconomic stability, protect critical government programs and set the basis for medium term reforms in the context of the oil price shock. During 2016 the price oil shock deepened much more than expected causing an economic recession and a severe fiscal crisis. Chad's situation is exacerbated by a complex set of circumstances, including the country's fight against regional terrorism, the hosting of a large refugee population, drought and the economic crisis in Nigeria. As a result, the objectives of the FCPSG are jeopardized and supplemental financing is needed to help attain them. The proposed operation will also help address the unanticipated financing gap caused by the shocks while preserving core development spending in the 2016 budget. Chad meets the eligibility criteria for the IDA Crisis Response Window (CRW) given that the current crisis is caused primarily by an exogenous shock and GDP has is projected to decline by more than 3 percent.[1]

**The economic impact of the oil shock is of unprecedented magnitude and severity**. Since June 2014, oil prices have decreased by about 70 percent with the price of Chadian crude oil dropping from an average of US$100 in 2013-14 to US$34 in 2016. The oil price shock has had dramatic consequences as oil accounts for 63 percent of fiscal revenue and 85 percent of exports, and contributes to 20 percent of GDP with substantial inter-sectoral linkages. The impact of the crisis in 2016 is significantly worse than what was projected at the time of FCPSG approval. The expected growth recovery has not materialized. Instead, the severe recession is reversing the

[1] CRW support would be triggered by evidence of a crisis that is caused by an exogenous shock which affects a significant number of IDA countries. All IDA countries are in principle eligible for CRW support. A year-on-year decline of GDP growth of 3 percentage points or more would be the threshold to identify countries that could be eligible for CRW support.

progress made through hard-won and recognized reform efforts. The depth of the crisis and the related financing needs are greater than originally expected.

**The proposed operation meets the key conditions for the use of quick disbursing Supplemental Financing.** The oil crisis is exceptional and its magnitude is unexpected. The FCPSG is being implemented in compliance with the provisions of the Financing Agreement, and the program remains largely on track. Chad has exhausted its statutory and exceptional advances from the regional Central Bank, BEAC, and is unable to obtain sufficient funds from other creditors on reasonable terms and in a reasonable time. The time available is also too limited to prepare a free-standing operation given the urgent need to reduce the 2016 financing gap**.**

## II. Operation Objectives

The development objectives supported through the proposed Supplemental Development Policy Financing are to help maintain stability on the fiscal and macroeconomic fronts including to protect critical Government's programs and set the basis for medium term reforms. This is being achieved by: (a) broadening the tax base; (b) improving the rationalization of public spending and transparency in public resource management; and (c) improving new business registration.

## III. Rationale for Bank Involvement

The proposed Supplemental Financing meets Bank requirements for Supplemental Financing under OP 8.60 as follows:

**The oil crisis is exceptional and its deep magnitude is unexpected, beyond the control of the authorities, threatening original program objectives of the FCPSG absent a supplemental source of financing.** While the oil shock started in end-2014, against a more positive projection, it has intensified in 2016, leading to an unprecedented magnitude of revenue shortfall and an urgent and unanticipated financing gap that is jeopardizing the Government's reform and development spending program. The oil shock aggravates the negative impact of El Niño, the economic and fiscal cost of regional security measures and of hosting a large refugee population.

**The program is being implemented in compliance with the provisions of the Financing Agreement:** Chad is currently implementing the FCPSG reform program in full compliance with all covenants embedded in the Legal Agreement for the financing of the FCPSG (Financing Agreement Number D0970-TD between the Association and Chad dated November 2, 2015). As discussed in Section B, achieving some of the targets of the FCPSG would require financing the budget[2] and more pronounced fiscal rationing would weaken progress towards some other objectives.[3]

**The borrower is unable to obtain sufficient funds from other lenders on reasonable terms and in a reasonable time.** The funding for the 2016 budget already includes contributions from

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[2] For example the regularization of the exceptional expenditures and the matching of the census of enterprises and the Tax directorate database.

[3] These include procurement activities, and the support to the Court of Accounts.

the AfDB, the EU and under the IMF ECF. The Supplemental Financing is therefore critical to reduce the unanticipated fiscal gap caused by lower than expected revenues. No other concessional resources are available as Chad has already exhausted its statutory and exceptional loans with the BEAC.

**The time available is too short to prepare a free-standing operation.** Under the difficult economic downturn affecting Chad, World Bank assistance should be channeled as soon as possible, and time available is too short to prepare a self-standing program, even an emergency operation. Given the urgency, the proposed supplemental financing allows the Bank to provide support in a timely manner so that the Government can deal rapidly with the fiscal and social impact of the shock, while also ensuring that the FCPSG-supported reforms continue to be implemented.

**The reform program, supported by the FCPSG remains on track.** The Government and key implementing agencies remain committed to implementing the reform program. Rapid delivery of Bank support is therefore essential to sustain the on-going reform program and domestic demand and avoid lack of tax revenues are substituted by arrears or unsustainable rundown in foreign exchange reserves.

## IV. Tentative financing

| Source: | | ($m.) |
|---|---|---|
| BORROWER/RECIPIENT | | 0.00 |
| International Development Association (IDA) | | 50.00 |
| Borrower/Recipient | | |
| IBRD | | |
| Others (specifiy) | | |
| | Total | 50.00 |

## V. Tranches *(if applicable)*

**N/A**

## VI. Institutional and Implementation Arrangements

The Ministry of Finance and Budget (MFB) and the Ministry of Planning and International Cooperation (MPIC) will be responsible for coordinating the supervision and monitoring of the reform program. The MFB and the MPIC have experience in collaborating with the IMF and World Bank, as demonstrated by the successful achievement of HIPC completion.

## VII. Benefits, Risks and Risk Mitigation

### A. Benefits

**The proposed Supplemental Financing will be an important source of resources for the government**. It will provide financing at a time when there is an urgent need for financing unmet government expenditures, including pro poor expenditures. The proposed Supplemental Financing is quick disbursing and timely program support will assist the GoC in minimizing the risks to the overall reform program that is being supported through the current FCPSG. It will also maintain the integrity of the transition to a new reform program planned for implementation over the next fiscal year.

### B. **Risks**

**The risk assessment made for the FCPSG remains valid and the overall risk rating for the proposed operation is high.** Political and governance, macroeconomic as well as institutional capacity for implementation and sustainability risks are of particular concern.

**Many of the risks listed above cannot be mitigated by the proposed operation**. Nevertheless, supporting the authorities' efforts to enable the economic recovery, expand the revenue base and to improve the quality of PFM will reinforce macro-fiscal stability, which will be essential to managing the impact of economic, political or security-related shocks. The progress noted following the latest IMF Safeguards Assessment of the BEAC will also contribute to mitigate the fiduciary risks. Finally, the Bank team's close collaboration with the IMF and its active role in macroeconomic surveillance will enable the authorities to better anticipate and address emerging fiscal and external imbalances.

## VIII. Poverty and Social Impacts and Environment Aspects

*Poverty and Social Impacts*

**Previous assessment remains valid**. **The measures supported by the FCPSG are still expected not to have a negative impact on poverty but rather to mitigate the adverse impact of the crisis on poverty.** First, it would reduce the severity of the fiscal adjustment by providing budget support at a critical juncture. Second, it would reduce the risks of unordered adjustment that could take the form of massive arrears accumulation and severely disrupt the functioning of the urban economy. Third, the proposed operation was expected indirectly to contribute to maintaining minimum levels of security and pro-poor expenditures as budgeted in the revised Finance laws in 2016, thus reducing risks of increased fragility and disruption in basic service delivery. The proposed operation contribute to addressing the severity of the fiscal adjustment and the risk of increasing arrears. While the level of pro poor expenditures has decreased in terms of levels, they have increased in terms of share of the budget when comparing the 2016 initial budget to the revised finance Law.[4] In the longer run, measures supported by the operation are still expected to generate efficiency gains and fiscal space that could be used to strengthen the resilience of the economy against shocks and finance larger pro-poor interventions in public health, education, social protection and agriculture.

*Environment Aspects*

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[4] The share of pro poor expenditures increase from 29 percent in the 2016 initial budget to 39 percent of total expenditures in the revised finance Law. Budget execution remains to be assessed.

**Previous assessment remains valid. The measures supported by the proposed operation are not expected to have any negative impact on the environment.** None of the measures supported by the operation are expected to affect the quality of Chad's forests, fisheries, water supplies or other environmental resources. However, the operation's focus on ensuring adequate fiscal space to preserve pro-poor spending and maintain the government's capacity for effective social protection policy could indirectly support environmental objectives by mitigating the need for rural households to resort to environmentally unsustainable practices in the event of a natural disaster or a shock to agricultural production.

## IX. Contact point


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