Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 03-Jun-2019| Report No: PIDC27059

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Cabo Verde	P171080	CABO VERDE SECOND STATE-OWNED ENTERPRISES FISCAL MANAGEMENT DEVELOPMENT POLICY FINANCING (P171080)	P165631
Region	**Estimated Board Date**	**Practice Area (Lead)**	**Financing Instrument**
AFRICA	Mar 19, 2020	Macroeconomics, Trade and Investment	Development Policy Financing
Borrower(s)	**Implementing Agency**		
Ministry of Finance	Ministry of Finance		

Proposed Development Objective(s)

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

Financing (in US$, Millions)

SUMMARY

Total Financing	15.00

DETAILS

Total World Bank Group Financing	15.00
World Bank Lending	15.00

Decision

The review did authorize the preparation to continue

B. Introduction and Context

Country Context

The administration which took office in April 2016 has reiterated its commitment to create space for the private sector to lead growth, while putting debt on a sustainable declining path. The administration inherited a middle-income country with one of the highest per capita incomes in Sub-Saharan Africa (SSA) but with a public debt ratio to Gross Domestic Product (GDP) twice the average of small island developing states, and significant contingent liabilities from the state-owned enterprises (SOEs) sector. Immediate efforts were launched to create the conditions for private-sector led growth, through a new partnership between the State and the private sector in delivering key services, notably in infrastructure. Building on this agenda, the government has been acting to stabilize and reverse the rapid public debt accumulation.

The macroeconomic policy framework in Cabo Verde is deemed adequate for the proposed operation. GDP growth has accelerated recently, and the outlook is positive, driven by ongoing structural reforms to improve connectivity and boost private sector investment. With limited pressure on the peg, monetary policy has been supportive of growth. The government has also demonstrated its ability to implement fiscal consolidation, including SOE reforms, since taking office and has expressed a strong commitment to putting debt decisively on a downward trajectory. Furthermore, while external vulnerabilities are significant given the high level of the current account deficit, foreign direct investment (FDI) is projected to be sustained, and international reserves remain at a comfortable level. The authorities have reached out to international financial institutions and other partners for technical and financial support to implement their program, and the proposed operation supports substantial reforms underpinning the economic outlook. Sustained political will to implement difficult and sensitive reforms will be a crucial ingredient for the success of this operation.

Relationship to CPF

The programmatic DPF series for Cabo Verde is aligned with the preliminary objectives and proposed outcomes of the Fiscal Year 2020 -2025 CPF under preparation. This upcoming World Bank Group CPF is being prepared on the findings of the Systemic Country Diagnostic. It identified high debt and fiscal risks in the SOEs sector, weak government effectiveness and limited inter-island connectivity among the list of binding constraints for growth, reduced poverty and shared prosperity. The proposed operation will advance reforms to address some of these constraints, reinforcing the country's fiscal position as it seeks to adjust its development model to allow greater private sector participation in the transport, housing and energy sectors.

C. Proposed Development Objective(s)

The program development objectives (PDO) in this operation are (i) reducing fiscal risks from SOEs while improving service delivery in infrastructures, and (ii) strengthening accountability and effectiveness in fiscal management. The PDO remains unchanged from the first operation in the series.

Key Results

The measures to reduce fiscal risks from SOEs while promoting private-sector led provision of key services are expected to lead to a reduction in financial support to SOEs from the budget, increased international air traffic and inter-island cargo and passenger movement, and strengthened financial performance of the energy utility. The DPF program targets a reduction in financial support to the national airline from 4.8 percent of GDP in 2018 to zero by GDP 2021. Support for the social housing project should also decline by a full percentage point. The volume of maritime passenger traffic is expected grow 10 percent in 3 years to 537, 000. On the other hand, cargo could increase from 481,00 tons to 528 000 tons by 20201. It is also expected that by the end of this series the energy utility will register an improved financial position. The wholesale cost to information, communication and technology companies should also be substantially lower. The measures to strengthen accountability and effectiveness in fiscal management should improve the government fiscal targets (primary balance from a deficit of 0.2 percent of GDP in 2018 to a surplus of 0.4 percent of GDP or higher by the end of the series).

D. Concept Description

The PDO is to reduce fiscal risks and enhance fiscal management in support of sustainable private-sector led growth. The series is closely aligned with the priorities of the PEDS and complements other activities to address fiscal risks, especially those related to natural disasters. Specifically, this series supports the authorities in their efforts to stem the debt generation process and reposition the role of the State in the economy, by promoting private sector-led provision of critical infrastructure services, and to improve fiscal management for enhanced accountability and effectiveness in the use of public resources. In the short term, below-the-line support to SOEs will continue to affect financing needs and debt, but this support is expected to decline as reforms are implemented and will be complemented by positive contributions from the evolution of the primary balance and automatic debt dynamics. In parallel, attention is also specifically given to supporting quality and affordability of services for end-users. The series is structured around two interrelated policy areas:

- **Pillar A aims to reduce fiscal risks from SOEs and improve the management of public assets in the transport, energy, housing and ICT sectors while promoting private sector involvement in the delivery of these key services for enhanced performance.** Capitalization and direct subsidies and transfers to the TACV, IFH and ELECTRA fluctuate from year to year but averaged over 2 percent of GDP per year between 2014-2018. Concurrently, explicit guarantees to the same entities average 7 percent of GDP. There is also significant on-lending by the central government to ELECTRA and IFH, which is a source of contingent liabilities. The reforms supported by the series are expected to minimize fiscal exposure to these entities while improving the quality of air and maritime transportation and energy services. Overall, the program includes: (i) repositioning the role of the State in the provision of international air and maritime inter-island transportation; (ii) reducing ELECTRA's commercial losses and revisiting tariffs to improve the financial position of the utility while supporting affordability of services for low-income households; (iii) restructuring the *Casa Para Todos* (CPT) social housing program to increase its performance and reduce related debt service risks; and (iv) adopting regional directives opening access to ICT wholesale broadband infrastructure, so as to boost sound competition and reduce cost of service.

- **Pillar B support reforms which aim at strengthening accountability and effectiveness in budget and debt management.** Building on the first operation on the series, key policy actions focus on: (i) implementing new budget and debt legislation for more effective and transparent management, clearly linking the medium-term fiscal framework with fiscal and debt targets; (ii) implementing legislation which strengthens the powers of the Court of Accounts - which is the supreme audit institution (SAI) responsible for the supervision of the legality of public expenditures and the audit of public accounts; (iii) enhancing tax transparency, streamlining tax exemptions and revoking undue exemptions ; and (iv) rationalizing public investment selection.

E. Poverty and Social Impacts and Environmental Aspects

Poverty and Social Impacts

The impact of the policies supported by the proposed operation on poverty and social indicators are expected to be mostly positive in the short to longer-run. The DPF's focus on reforms of key SOEs, fiscal and debt management, public investment management, and rationalization of non-efficient tax expenditures will help to establish an enabling environment for sustainable fiscal management and economic growth over time. The operation is closely aligned with the SOE Related Fiscal Management Project approved in June 2018, which advanced reforms that are expected to offset any negative social and economic impact of the government reform in the air transport sector on both poor and non-poor households. Emphasis on increasing private-sector engagement in the delivery of key services is also expected to support sustainable growth and job creation, which will be beneficial for the poor over the medium-term. To assess the likely impact of the reforms supported by this operation, a Poverty and Social Impact Analysis is under preparation (and expected to be completed by September 2019) and will make use of the latest household income and consumption expenditure survey.

Environmental Impacts

The specific actions supported under the proposed DPF series are not likely to have any significant impact on the country's environment, forests and natural resources. It supports measures to improve public sector management and do not support direct investment in environmentally impactful investments or involve actions with significant environmental consequences. Reforms aimed at improving evaluation mechanisms for public investment projects and reforms to the energy sector will have an overall positive impact on environmental sustainability.

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APPROVAL

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