Project Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 13-Mar-2023 | Report No: PIDA35595

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Rwanda	P179999	ADDITIONAL FINANCE-ACCESS TO FINANCE FOR RECOVERY AND RESILIENCE PROJECT (AFIRR)	P175273
Parent Project Name	**Region**	**Estimated Appraisal Date**	**Estimated Board Date**
Access to Finance for Recovery and Resilience Project	EASTERN AND SOUTHERN AFRICA	29-Mar-2023	15-May-2023
Practice Area (Lead)	**Financing Instrument**	**Borrower(s)**	**Implementing Agency**
Finance, Competitiveness and Innovation	Investment Project Financing	Ministry of Finance and Economic Planning	Development Bank of Rwanda, Business Development Fund

Proposed Development Objective(s) Parent

The Project Development Objective (PDO) is to increase access to finance and support recovery and resilience of businesses affected by the COVID-19 pandemic.

Components

Component 1 – Liquidity and Recovery Facility
Component 2 – Risk Sharing Facility
Component 3 – Institutional Strengthening and Implementation Support

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Project Cost	320.00
Total Financing	320.00
of which IBRD/IDA	100.00
Financing Gap	0.00

DETAILS

World Bank Group Financing

International Development Association (IDA)	100.00
IDA Shorter Maturity Loan (SML)	100.00
Non-World Bank Group Financing	
Commercial Financing	220.00
Unguaranteed Commercial Financing	220.00

Environmental and Social Risk Classification

Substantial

Other Decision (as needed)

B. Introduction and Context

Country Context

1. **Rwanda is managing a strong recovery from the pandemic, amidst inflationary pressures and downside effects of the ongoing Ukraine war.** Rwanda's economy experienced a remarkable recovery in 2021, with 10.9 percent GDP growth compared to its 3.4 percent contraction during the pandemic. Building upon decades of robust growth, the government strategy is shifting towards private sector and sustainability-focused development. However, inflationary pressures have been mounting, driven mainly by domestic food and utility prices, and on average, inflation increased to 13.9 percent in December 2022 compared to 0.8 percent in 2021. The war in Ukraine has increased global commodity prices, and higher oil prices are expected to raise international transport costs, and increase the cost of imports, including food items. The National Bank of Rwanda (BNR) tightened its monetary policy[1] to curb the inflationary pressures after keeping it at historic low of 4.5 percent—for 22 consecutive months—first to mitigate the impact of COVID-19 on the economy and then to support the economic recovery.

2. **Economic recovery has been supported by industrial activities benefitting from government support of the manufacturing and construction sectors, as well as a gradual recovery of tourism activities.** Growth is expected to be moderate over the next two years, with downside risks including a potential pandemic resurgence, vulnerability to weather and climate shocks, and the potential for the increasing fiscal deficit to limit the GoR's fiscal consolidation. Rwanda's general government gross debt is estimated at around 68.1 percent of GDP at the end of 2022, up from 44.9 percent of GDP at the end of 2018, prior to the pandemic[2]. As the COVID-19 crisis dissipates, the authorities are committed to putting in place a credible fiscal consolidation package to reduce Rwanda's public debt and to meet the debt convergence criterion of the East African Community and restore fiscal buffers. The ability of the Rwandan

[1] The Central bank rate was raised to 7 percent in February 2023, from the 6.5 percent in effect since November 2022.
[2] IMF. (October 2022). World Economic Outlook. Database.

government to support the country's development and tap into new sources of funding through mobilizing private capital will be instrumental to finance Rwanda's development strategy.

3. **Rwanda continues to be among the most vulnerable countries to weather and climate shocks, which are a key risk to the continuation of economic recovery.** The impact of risks of climate change could be consequential for Rwanda's growth given the reliance of the economy on climate sensitive sectors. The increasing frequency of weather and climate shocks (e.g., drought and floods) could lower agriculture output and thereby impact many farms and households. On the steep slopes that dominate much of the country, floods, landslides, and soil erosion already impact agriculture, infrastructure, and services[3]. The associated long-term risks from climate change underscore the need for the GoR and private sector to invest in resilience, including through financing instruments that help mitigate associated risks.

4. **Vision 2050 sets an ambitious goal to eliminate poverty in the country supported by economic transformation and private sector led growth.** Under this focus, Vision 2050 prioritizes considerations of a diversified economy, universal access to financial services, competitive manufacturing and export sectors, export oriented services and sustainable tourism, along with smart and green cities, sustainable supply of and demand for energy for sustainable growth. Considering the current global and national fiscal context, finding the right balance between development and climate action will be instrumental for Rwanda to sustain its impressive growth rates and deliver its national development plan Vision 2050.

Sectoral and Institutional Context

5. **The private sector represents a small, but growing, share of overall jobs**. Like many other low-income countries, Rwandan firms, for the most part, are young and informal.[4]Most firms have experienced weak employment growth, and more than 90 percent of firms have failed to increase employment numbers after entry. With an estimated 230,000 young Rwandans entering the labor force every year, there is a pressing need to create productive jobs to drive inclusive economic transformation. Enhancing growth opportunities for firms will be critical in creating productive employment opportunities.

6. **Women-led firms play an important role in the economy and faced additional increased challenges during the pandemic**. Women head 42 percent of enterprises and comprise 58 percent of enterprises in the informal sector, which accounts for 30 percent of GDP. National surveys indicate that women entrepreneurs also have an impact on job creation, with many hiring between 3 and 5 employees in their businesses. Their contributions, however, are not without challenges, facing difficulties in access to three important factors: (a) information, (b) business skills training and development, and (c) finance. They grapple with issues such as high taxes and transportation costs as well as discrimination in property ownership which in turn constrains their ability to offer collateral for access to finance. According to the 2019 Enterprise Survey, 26.5 percent firms have female participation in ownership, slightly below the

[3] There is increasing concern in rapidly growing urban areas about water shortages during longer dry spells and the impact of flooding and landslides on expanding informal settlements in risk-prone areas like steep slopes and flood plains.

[4] Country Private Sector Diagnostic (CPSD), March 2019.

regional average of 28 percent. Nearly 14 percent of firms have majority female ownership, which is above the regional average of 13 percent.

7. **Access to finance is among key constraints for firm growth and survivorship**. Micro, Small, and Medium Enterprises (MSMEs) play an important role in the economy, contributing 55 percent of total GDP and accounting for over 95 percent of businesses and more than 70 percent of in-establishment employment in Rwanda. According to the World Bank Enterprise Survey 2019, 31 percent of (formal) small and medium enterprises (SMEs) perceived access to finance as their biggest obstacle to operations, well above that for large firms (12 percent) and above the average for Sub-Saharan African countries (around 22 percent).

8. **MSMEs face severe constraints to accessing finance, in part due to their exposure to climatic shocks.** Access to credit for MSMEs is low in Rwanda, with exposure to climatic shocks being a key inhibitor**.** Extending credit to the built environment in Rwanda is constrained by the country's vulnerability and exposure to floods and landslides. Interviews with PFIs highlight their aversion to extending credit to investments in built structures with high flood exposure, impacting access to credit for multiple sectors of the economy. When structures are not built adequately, flood events can cause severe damage, limiting the ability of the debtor to repay their loan[5]. Production of electricity is also at risk from increased flood damage to dams and turbines, reservoir siltation, and river flow variability during longer dry spells. A study by the IFC[6] finds that climate change is a key risk to the SME sector[7] that inhibits job creation in the private sector. PFIs limit their lending and apply exposure limits when lending to climatic shock exposed sectors. The resulting lack of access to finance for MSMEs prevents them from investing in climate mitigation and adaptation activities (for example drought resistant seeds, irrigation, rainwater harvesting, terracing, crop rotation, water conservation, invasive species control, etc) leaving the most vulnerable acutely exposed to climatic shocks.

9. **The financial sector has supported economic recovery in the post pandemic period.** Banks continued to provide credit to the private sector at an improved pace in line with liquidity buffers. Generally, the improved growth of lending mainly reflected the increased credit demand and lower risk perception by banks consistent with the resumption of businesses. Outstanding credit grew by 16 percent in June 2022 albeit lower than 18.6 percent registered in June 2021, largely due to the slowdown of new lending and write offs. The banking sector remains adequately capitalized (CAR: 22.1 percent as of June 2022), liquid and profitable (ROE: 16.5 percent; ROA: 2.8 percent) despite the withdrawal of COVID-19 forbearance measures.

10. **The concentration of credit to vulnerable sectors poses elevated credit risk in the financial sector[8].** The disruption in global supply chain is continuing to cause vulnerabilities to the manufacturing sector. Due to the adverse global supply shock associated with the Ukraine war, banks' exposure to manufacturing sector is at risk due to the sector's heavy usage of energy and other imported inputs that

[5] Rwanda Climate Change and Environment Risk Profile, UNDP, 2021.
[6] Creating Markets in Rwanda, WB, 2019.
[7] Climatic shocks impact MSMEs in Rwanda through multiple channels, including reducing farm yields, destroying key infrastructure (e.g., bridges and roads critical for accessing markets), interruptions in electricity supply, destruction of key assets such as storage facilities, shops.
[8] BNR, Financial Stability Report (Dec 2022).

are currently subject to strong increase in prices. The shortages of input materials may substantially slow up and complicate manufacturing processes, and increase production costs, thereby weighing on the revenues of manufacturers. The asset quality in the manufacturing sector remains healthy, though it slightly deteriorated during the last year (3.1 percent in June 2022). The growth in commercial real estate lending picked up in recent years making banks more vulnerable to adverse development in the real estate market. Banks' exposure to the commercial real estate sector constitutes around 9.1 percent of total outstanding loans s (RWF 272.4 billion), 12.8 percent of total corporate loans, and accounted for around 14 percent of the growth of bank loans over the past five years.

11. **Short-term resources also limit banks' ability to provide credit in the long term.** As of June 2022, around 65 percent of banks' deposits were demand deposits. The term deposits held by banks represent 35 percent of total deposits out of which, 92 percent hold a maturity of less than one year. With this funding structure, banks are exposed to a funding risk related to excessive maturity transformation. MFIs face similar challenges to those of banks, with the limited access to liquidity and stable sources of funding being more acute.

12. **In April 2020, the GoR established the Economic Recovery Fund (ERF) to support the recovery of businesses hard hit by the COVID-19 pandemic.** The objective of ERF was to support businesses so that they can survive, resume operations and safeguard employment, thereby cushioning the economic effects of the pandemic. BNR was appointed as the Fund Manager.

13. **The AFIRR project was designed to further support the ERF and address binding constraints for Rwandan firms to access finance to support resilience and growth, further exacerbated during the COVID-19 pandemic**. Firms across the board were impacted due to low demand, disruption of production, markets, supply, and trade. This impacted employment as well as the continuity of their businesses. Throughout the pandemic, otherwise viable MSMEs faced shortages of working capital and access to resources to maintain their operation and basic needs. Micro and small enterprises (MSEs) suffered the most from lockdown measures and a sudden drop in demand for their products and services. Financial institutions serving MSMEs -Microfinance institutions (MFIs) and Savings and Credit Cooperatives (SACCOs)- were affected by liquidity constraints limiting their capacity to maintain lending to their clients.

14. **The AFIRR project objective is in line with the GoR's Economic Recovery Plan and complements the ERF.** BRD and the Business Development Fund (BDF) became fund managers and implementers of the project. The Ministry of Finance and Economic Planning (MINECOFIN) plays a coordinating role. AFIRR is implemented by providing lines of credit targeting affected businesses to (a) facilitate refinancing of existing debt obligations, (b) provide working capital, and (c) support investments for business adaptation and growth through the provision of long term sources of finance. The lending facility is complemented by risk sharing instruments to mitigate collateral requirements and to provide loan repayment liquidity facilities benefitting underserved segments such as MSMEs. Finally, technical assistance provided by the project is expected to facilitate increased uptake by underserved segments and the private sector more generally.

C. Proposed Development Objective(s)

15. The Project **Development** Objective (PDO) is to increase access to finance and support recovery and resilience of businesses affected by the COVID-19 pandemic.

Key Results

16. **The AF will ensure that AFIRR can continue to support sectors affected not only by the COVID-19 pandemic but also from the spillover effects from the Ukraine war and to respond to firms' long-term financing needs in support of Rwanda's economic recovery.** The AFIRR AF will scale up current support to firms and productive investments for a resilient recovery while helping develop new sources of long term funding through the mobilization of private capital. Strengthening the sustainability of development institutions implementing the project is a fundamental pillar to continue supporting economic recovery and building long-term resilience of Rwandan firms. The AF will address the growing demand for financing from project beneficiaries to cover capital expenses, as well as operating expenses and working capital in strategic and priority sectors, as well as investments in sectors with high growth potential. Diversifying sources of capital for BRD -including from the private sector- is an important element for the sustainability of ongoing programs, strengthening the institution and supporting capital market development in Rwanda.

D. Project Description

17. The PDO of the AF remains the same as the parent project, i.e., to increase access to finance and support recovery and resilience of businesses affected by the COVID-19 pandemic. The AF was requested by the GoR in September 2022 with the objective to expand current investment support to facilitate economic recovery through the provision of long-term sources of funding. The AF will address the growing demand for financing from project beneficiaries to cover capital expenses, as well as operating expenses and working capital in strategic and priority sectors, as well as investments in sectors with high growth potential. PDO indicators remain unchanged and the results framework will be updated to reflect the target numbers in light of the additional resources channeled through the project.

A. Project Components

18. **Component 1 – Liquidity and Recovery Facility (US$95 million IDA equivalent)**. Component 1 focuses on addressing firms' short- and long-term financial needs to help them withstand the crisis, grow their business and build resilience, including strengthening climate resilience. The facility will continue to provide lines of credit (LoC) to Financial Institutions (FIs) for on-lending to highly impacted and/or strategically important sectors and firms to support economic recovery and business continuity. The AF will include a new subcomponent to support BRD's mobilization of private capital.

Sub-component 1.1. Microbusinesses Credit Line (US$30million IDA equivalent)

19. **This facility provides financial support to MSEs and the informal sector.** Proceeds of the LoC will be on-lent by BDF through MFIs, mainly SACCOs, to final beneficiaries. Project flexibility allows for both working capital and investment loans. The LoC will support purchase of small capital assets to support business activity. SACCOs, particularly those in rural areas, serve the most vulnerable segments and have become increasingly short on liquidity to continue lending to their clients. To protect those businesses and jobs and to stimulate consumption of households, the sub-component support MSEs through SACCOs.

Sub-component 1.2. Refinancing Credit Line (US$10.5 million IDA equivalent)

20. **The LoC supports refinancing of existing loans in priority sectors as determined by the GoR.** BRD will lend to banks, MFIs (banks and limited companies) to support enterprises through refinancing of existing financial commitments to ease hardship caused by the pandemic. Target beneficiaries include all firms in priority sectors affected by the pandemic. Similar to other components, there is a specific focus on refinancing women inclusive firms under this sub-component.

Sub-component 1.3. Working Capital and Investment Credit Line (US$29.5 million IDA equivalent)

21. **This facility supports investments in Rwanda to facilitate economic recovery, and the preservation and creation of jobs through the provision of long-term sources of funding currently lacking in the market.** In particular, support under this sub-component is expected to enable increased investments and exports regionally and globally and/or substituting imports with local production, including supporting jobs that can transition the population from subsistence agriculture. Project flexibility allows for both working capital and investment loans.

Sub-component 1.4. Sustainability Linked Financing (US$25 million IDA equivalent)

22. **It is proposed to include an additional component in the project to increase PCM and support BRD's lending activity.** BRD will use project resources to develop a sustainability-linked bond issuance program in local currency. This approach is designed to leverage the additional AFIRR financing further to allow BRD to borrow in the local capital market by establishing a credit enhancement structure to support the issuance program. The BRD sustainability-linked issuance program is expected to align closely with BRD's broader strategic objectives of promoting sustainable economic development in Rwanda and reducing poverty alongside measurable Key Performance Indicators (KPIs). The SLB will help to boost investment and support the broader agenda of institutional development in Rwanda through increased accountability to the market, diversification, development of the corporate bond markets, and expansion of development finance.

23. **Component 2 – Risk Sharing Facility (US$3 million IDA equivalent).** This component supports enhancing and scaling up the existing PCG scheme in BDF, and the development of two new de-risking schemes to provide liquidity and insurance instruments in support of MSMEs in the event of climatic shocks**.** Project support to the enhancement of the PCG scheme is designed around the accomplishment of performance based conditions (PBCs). The design of de-risking instruments aims at strengthening the financial resilience of target beneficiaries and PFIs to future shocks to support increased access to finance

in vulnerable sectors. No additional resources are being requested to support implementation of subcomponent 2.1. Additional US$ 3 million have been requested to scale the rollout of the BLW instrument and the Backstop insurance mechanism envisaged under sub-component 2.2.

24. **Component 3 – Institutional Strengthening and Implementation Support. (US$2 million IDA equivalent).** This component focuses on three key areas to strengthen capacity at various levels to support project implementation: (i) technical assistance to project beneficiaries; (ii) technical assistance and capacity building for implementing agencies, and (iii) project management and monitoring. Additional funds are being requested to increase the support and activities aimed at further strengthening BDF implementation capacity and to support project management and monitoring.

Legal Operational Policies

	Triggered?
Projects on International Waterways OP 7.50	No
Projects in Disputed Areas OP 7.60	No

Summary of Assessment of Environmental and Social Risks and Impacts

E. Implementation

Institutional and Implementation Arrangements

25. **The Project will be implemented by the BRD and the BDF as the parent project and MINECOFIN will play a coordinating role for the overall project.** The implementing agencies will lead the implementation of the project components as follows: (a) BDF will implement sub-component 1.1 - Micro-businesses Credit Line and component 2 - Risk-sharing Facility, and (b) BRD will be responsible of sub-component 1.2 - Refinancing Credit Line and sub-component 1.3 - Working Capital and Investment Credit Line. Component 3 will be implemented by MINECOFIN, BRD and BDF, with dedicated technical assistance activities for each agency. The agencies will also be responsible for day-to-day project implementation, including project reporting, M&E, FM, procurement, and implementation and monitoring of Environmental and Social Standards (ESS) instruments prepared under the project. MINECOFIN will be responsible for convening other relevant counterparts and coordinating the project's activities, including preparation of the project implementation manual through the project coordination team (PCT). The PCT will mainly comprise of a Project Coordinator, an M&E Specialist, and an E&S Coordinator. The Project Coordinator will report to and act under the direction of the Financial Sector Development Department for ERF policy related matters. The main tasks of the PCT will include (a) overall responsibility for day-to-day coordination and management, including direct support to the two implementing agencies; (b) project management; (c) overall project M&E; and (d) progress reporting on a quarterly basis. To strengthen

environmental and social risk management under the project, the E&S Coordinator to be based at MINECOFIN will coordinate environmental and social risk management across two Project Implementation Unit (PIUs), one under BDF and the other under BRD.

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