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Report No: PGD39

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (IBRD) AND

INTERNATIONAL DEVELOPMENT ASSOCIATION (IDA)

PROGRAM DOCUMENT FOR A

PROPOSED IDA CREDIT
IN THE AMOUNT OF SDR 3.7 MILLION
(US$5 MILLION EQUIVALENT)

AND A PROPOSED IBRD LOAN
IN THE AMOUNT OF US$5 MILLION

TO THE

REPUBLIC OF CABO VERDE

FOR THE

CABO VERDE DISASTER RISK MANAGEMENT DEVELOPMENT POLICY FINANCING WITH CATASTROPHIC DEFERRED DRAWDOWN OPTION

May 8, 2019

Social, Urban, Rural And Resilience Global Practice
Africa Region

(Cabo Verde)

Republic of Cabo Verde

GOVERNMENT FISCAL YEAR

January 1 – December, 31

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of March 31, 2019)

Currency Unit	=	Cabo Verdean Escudo (CVE)
US$1.00	=	CVE 98.39
US$1.00	=	SDR 0.720

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ABBREVIATIONS AND ACRONYMS

BCV	Central Bank of Cabo Verde *(Banco de Cabo Verde*)
Cat DDO	Catastrophe Deferred Drawdown Option
CCA	Climate Change Adaptation
CNPC	National Civil Protection Council
CPF	Country Partnership Framework
CPI	Consumer Price Index
CPT	Social Housing Program *(Casa Para Todos)*
CVE	Cabo Verdean Escudos
DNOT	National Directive for Territorial Planning
DPF	Development Policy Financing
DPF1	First State-Owned Enterprises Reform and Fiscal Management Development Policy Financing Operation
DRM	Disaster Risk Management
DSA	Debt Sustainability Assessment
EIA	Environmental Impact Assessments
ENRRD	National Disaster Risk Reduction Strategy
EROT	Regional Framework for Territorial Planning
EU	European Union
FEED	Special Stabilization and Development Fund
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GFDRR	Global Facility for Disaster Reduction and Recovery
GRS	Grievance Redress Service
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IDE-CV	Spatial Data Infrastructure of Cabo Verde
IFH	Real Estate and Housing Fund *(Imobiliária Fundiaria e Habitat*)
IMC	Multi-objective Continuous Survey
IMF	International Monetary Fund
INE	National Institute of Statistics
INGT	National Institute for Territorial Planning
IPCC	Intergovernmental Panel on Climate Change
LDP	Letter of Development Policy
MAI	Ministry of Internal Administration
MoF	Ministry of Finance
MoU	Memorandum of Understanding
NPL	Non-performing Loan
PD	Detailed Plan
PDM	Municipal Master Plan
PDU	Urban Development Plan
PEDS	Strategic Plan for Sustainable Development *(Plano Estratégico de Desenvolvimento Sustentável)*
PEFA	Public Expenditure and Financial Accountability

PFM	Public Financial Management
POT	Tourist Development Plans
PSIA	Poverty and Social Impact Analysis
PV	Present Value
REER	Real Effective Exchange Rate
SCD	Systemic Country Diagnostic
SDR	Special Drawing Rights
SEN	National Statistical System
SINAGERD	National System for Disaster Risk Management
SOEs	State-owned Enterprises
SSA	Sub-Saharan Africa
TA	Technical Assistance
TACV	Cabo Verde Airlines *(Transportes Aéreos de Cabo Verde*)
UASE	State-Owned Enterprise Unit *(Unidade de Acompanhamento do Setor Empresarial do Estado)*
UN	United Nations
UNDP	United Nations Development Programme
UN-HABITAT	United Nations Human Settlements Programme
UNISDR	United Nations Office for Disaster Risk Reduction
VAT	Value-Added Tax
WB	World Bank
WBG	World Bank Group
ZDTI	Integrated Tourism Development Areas

REPUBLIC OF CABO VERDE

CABO VERDE DISASTER RISK MANAGEMENT DEVELOPMENT POLICY CREDIT AND LOAN WITH CAT DDO

TABLE OF CONTENTS

The credit and loan were prepared by a World Bank Group team led by of Oscar A. Ishizawa (Task Team Leader, GSU19) and Robert Reid (Co-Task Team Leader, GSU19) and consisting of Joaquin Muñoz (GSU19), Martin Luis Alton (GFCCR), Rossella Della Monica (GFDRR), Paul Blanchard (GSU10), Edson Medina (GMTA2), Sandro De Brito (GFCCR), Rohan Longmore (GMTA2), Robertus A. Swinkels (GPV07) and Africa Eshogba Olojoba (GEN07). This operation was undertaken under the general guidance of Louise Cord (AFCF1), Meskerem Brhane (GSU13), Sylvie Debomy (GSU19), Lars Moller (GMTA2), Barbry Keller (GSU19), Fatou Fall (AFCF1), Paolo Zacchia (AFCF1), Eric Lancelot (AFCF1), Ivan Velev (AFCSN) and Niels Holm-Nielsen (GSU13). Peer reviewers were Tiguist Fisseha (GSU13), Rashmin Gunasekera (GSU10) and Nathan Engle (GCCSO).

1. SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Project ID	Programmatic
P160628	No

Proposed Development Objective(s)

(a) Strengthening the institutional and legal framework to ensure risk-informed sectoral and territorial planning; and (b) Increasing the financial capacity to manage impacts associated with disaster and climate-related shocks.

Organizations

Borrower: MINISTÉRIO DAS FINANÇAS

Implementing Agency: MINISTÉRIO DAS FINANÇAS

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Financing	**10.00**

DETAILS

International Bank for Reconstruction and Development (IBRD)	5.00
International Development Association (IDA)	5.00
IDA Credit	5.00

INSTITUTIONAL DATA

Climate Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks

Overall Risk Rating

Substantial

Results

Indicator Name	Baseline	Target
Annual progress report of implementation of the ENRRD strategy presented to the National Civil Protection Council[1]	N/A [2018]	Published for 2019, 2020 and 2021
All new municipal detailed plans (PD) incorporate disaster and climate-related risk management considerations	N/A [2018]	All (22 estimated) [2022]
Proportion of Integrated Tourism Development Areas (ZDTI) with Tourist Development Plans (POT) that incorporate disaster and climate-related risk management considerations	0 [2018]	56% (15 of 27) [2022]
Number of monthly request forms to access INE data from registered institutional users	N/A [2018]	10 [2022]
Number of memorandum of understandings (MoU) signed between INE and public institutions/sectors to systematically share data with INE	1 [2018]	8 [2022]
Report on contingent liabilities including those associated with disaster and climate-related shocks published together with the medium-term fiscal framework	None [2018]	Published at least one time before 2022
Allocation to the National Emergency Fund included annually in national budget	N/A [2018]	Exists in 2019, 2020, 2021 and 2022 budget
Annual activity and accounting report for the National Emergency Fund approved by its Board	N/A [2018]	Approved for 2019, 2020 and 2021

[1] Including the monitoring of approved sectoral infrastructure management plans incorporating disaster and climate-related risk reduction measures.

**IBRD AND IDA PROGRAM DOCUMENT FOR A PROPOSED
DISASTER RISK MANAGEMENT DEVELOPMENT POLICY CREDIT AND LOAN
WITH A DEFERRED DRAWDOWN OPTION FOR CATASTROPHE RISKS
TO THE REPUBLIC OF CABO VERDE**

1. INTRODUCTION AND COUNTRY CONTEXT

1. **The proposed operation is a stand-alone single-tranche US$10 million Disaster Risk Management Development Policy Credit and Loan with a Deferred Drawdown Option for Catastrophe Risks (US$5 million IDA and US$5 million IBRD).** It has been designed to support the efforts of the Government of The Republic of Cabo Verde (the Government) to quickly mobilize resources in the aftermath of a natural catastrophe and to strengthen the disaster and climate-related risk management systems in the country.

2. **Geological and climate-related disasters pose major challenges for sustainability of growth and resilient development of Cabo Verde.** Cabo Verde is an archipelagic nation of 10 volcanic islands located in the mid-Atlantic Ocean, 570 km off the west coast of the continent of Africa. Due to its location and geography, Cabo Verde is exposed to a wide range of natural hazards including volcanic eruptions, droughts, hurricanes, tropical storms, landslides and flash floods. The country faces high vulnerability to adverse natural events exacerbated by rapid rural-urban migration, continuous land degradation, and climate change. With a third of the population engaged in agricultural activities, drought is the natural hazard posing the biggest threat to human development in Cabo Verde. In recent years, Cabo Verde has suffered from: (i) Hurricane Fred in 2015 which caused damages estimated at US$2.5 million[2]; (ii) a volcanic eruption in 2014-15 in Fogo which lasted for 88 days, displaced all 994 people living in the caldera, and resulted in damages and losses estimated at US$28 million[3] (about 2 percent of the country's Gross Domestic Product (GDP); (iii) low levels of precipitation in 2017 which led to a drought event that has affected up to 70,000 people according to the Government's estimates[4]; and (iv) several floods across the country in São Nicolau (2009), Boavista (2012), São Miguel (2013, with damages estimated at US$2.6 million), and Santo Antão (2016, with damages estimated at US$7 million). The 2016 World Risk Report ranked Cabo Verde 31st out of 171 countries in terms of risk to natural disasters.[5] This elevated level of risk is evidenced in recurrent adverse natural events that affect the population. The report also ranked Cabo Verde as the 64th most vulnerable country, 92nd in terms of lack of coping capacities, and 43rd in terms of lack of adaptive capacities. Cabo Verde's rankings in these areas are lower than those of aspirational peers such as Seychelles and Mauritius.[6]

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[2] Jenkins et al. 2017. *Hurricane Fred (2015): Cape Verde's First Hurricane in Modern Times, preparation, observations, impacts and lessons learned.* Bulletin of the American Meteorological Society, 2017.

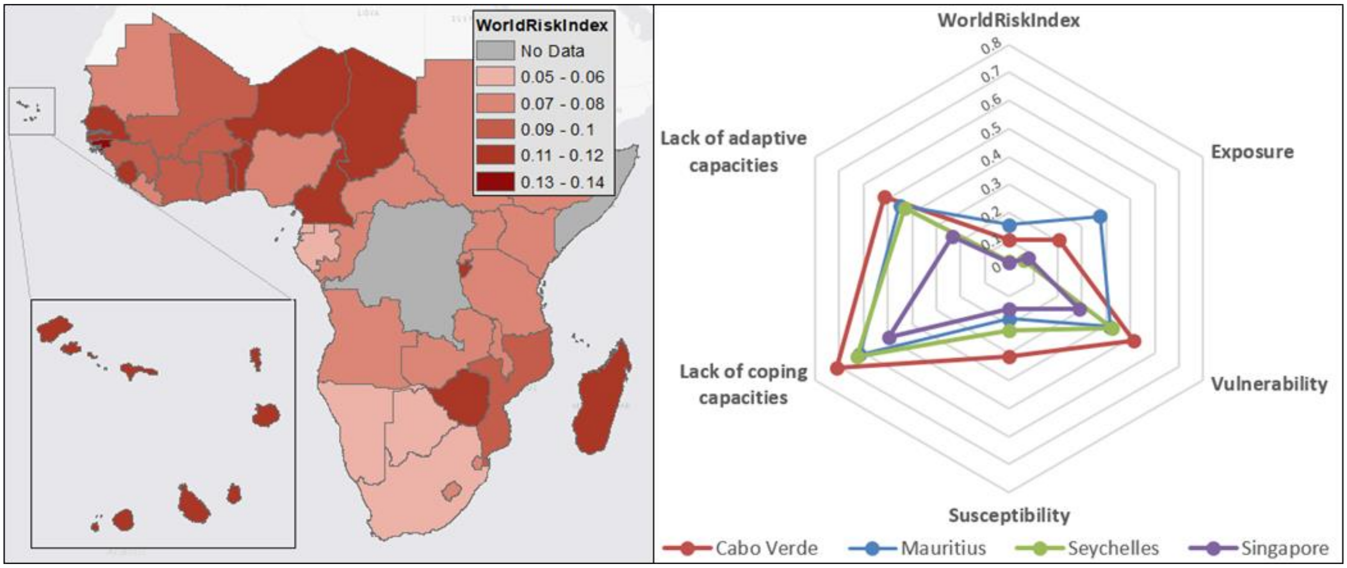
[3] A recovery strategy was designed after the eruption. The implementation of short-, medium-, and long-term interventions required an overall investment of US$6.51 million. Source: PDNA Fogo Volcanic Eruption 2014-2015.

[4] To alleviate the effects of the drought, Cabo Verde approved an emergency plan with interventions totaling US$8.2 million (resolution no. 110/2017).

[5] "*The World Risk Index is calculated with 28 individual indicators and rates the disaster risk for 171 countries owing to five natural hazards: Earthquakes, cyclones, floods, droughts, and sea-level rise. The disaster risk refers to a combination of potentially prone areas or countries and the social, economic and ecological conditions within the respective countries*." The country with the highest level of risk is ranked 1st in the World Risk Index. World Risk Report 2016. Welle, T. and Birkmann, J. 2015. *The World Risk Index – An approach to assess risk and vulnerability on a global scale*. Journal of Extreme Events, 2(1).

[6] **Coping capacities** comprise various abilities of societies and exposed elements to minimize negative impacts of natural hazards and climate change through direct action and the resources available. **Adaptation** is understood as a long-term process that includes

Figure 1: World Risk Report Ranking of Cabo Verde



Left: Cabo Verde is ranked as the 9th country facing higher risk out of the 44 countries assessed in Sub-Saharan Africa.

Right: Cabo Verde ranks higher in terms of susceptibility, vulnerability and lack of adaptive and coping capacities when compared to aspirational Small Island Developing States peers such as Mauritius and Seychelles. Source: World Risk Report 2016.

3. **Cabo Verde is a Small Island Developing State that will be highly exposed to the expected negative impacts of climate change.** Climate change is expected to affect Cabo Verde in several ways: (i) through a projected sea level rise of 0.26m to 0.98m for 2081-2100[7], which would increase coastal submergence, erosion, flooded lands, and salinity of small estuaries, streams, and coastal waters. These changes are expected to affect the population settled on the country's 1,000 km coastline, as well as the key ecosystems that play a part in the development of the tourism industry; (ii) by modifying rainfall patterns. Rainfall is concentrated in summer—with 56 percent of the precipitation between July and September—and is very erratic, generally associated with storms. Storm intensity is positively correlated with sea surface temperatures, which is expected to increase by 0.7 to 2.5°C by the 2060s, and by 1.2 to 3.7°C by the 2090s.[8] This would fuel more energetic storms, affecting rainfall patterns and potentially leading to stronger and more frequent associated disasters such as landslides and floods; and (iii) through extended dry seasons leading to seasonal water shortages, droughts, reduction of plant cover and the degradation of the ecosystem, thereby negatively impacting the livelihoods of the poor and those engaged in agricultural activities.

4. **Multiple factors contribute to Cabo Verde's high vulnerability to disasters and climate-related shocks.** Cabo

structural changes, measures and strategies dealing with and attempting to address the negative impacts of natural hazards and climate change in the long run. **Vulnerability** relates to social, physical, economic and environmental factors, which make people or systems vulnerable to the impacts of natural hazards and the adverse effects of climate change or other transformation processes. Source: World Risk Report 2016.

[7] Relative to 1986-2005. Intergovernmental Panel on Climate Change (IPCC), 2013: *Summary for Policymakers*. In: Climate Change 2013: The Physical Science Basis. Contribution of Working Group I to the Fifth Assessment Report of the Intergovernmental Panel on Climate Change [Stocker, T.F., D. Qin, G.-K. Plattner, M. Tignor, S.K. Allen, J. Boschung, A. Nauels, Y. Xia, V. Bex and P.M. Midgley (eds.)]. Cambridge University Press, Cambridge, United Kingdom and New York, NY, USA.

[8] McSweeney, C. N. (2010). *The UNDP Climate Change Country Profiles: Improving the Accessibility of Observed and Projected Climate Information for Studies of Climate Change in Developing Countries.* Bulletin of the American Meteorological Society, 91, 157-166.

Verde is a country of 540,000 people scattered across nine islands that are up to 300 km apart. In Cabo Verde municipalities are autonomous bodies, with their own responsibilities and finances. However, public and private assets and population are concentrated in Santiago, and there are significant connectivity challenges between the islands. Institutional capacity in the country is rather limited with under 10 percent of population age 25 and over having attained or completed at least short-cycle tertiary education. Like many other Small Island Developing States, Cabo Verde has a narrow economic base and strongly relies upon tourism, an activity that is weather-dependent. Furthermore, the fiscal sector is highly vulnerable to natural disasters because of the high indebtedness level and the absence of risk financing instruments to deal with natural shocks. Recent natural catastrophes in Cabo Verde and a broader recognition of the potential effects of climate change have raised awareness of the importance of taking proactive measures to effectively manage and reduce disaster and climate-related risks and incorporate them into the development process.

5. **Natural catastrophes can hamper poverty reduction efforts and threaten advances in shared prosperity.** Cabo Verde witnessed an important reduction in poverty rates between 2001 and 2015, driven by high economic growth of the service sector. From 2001 to 2015, poverty headcount—using the national poverty line—decreased from 57.6 percent to 35.0 percent, while extreme poverty dropped from 30.2 percent to 10.6 percent. Poverty is mainly a rural phenomenon: in 2015 poverty rates in urban areas was 27.7 percent, while in rural areas it was 48.3 percent. Shared prosperity indicators have also improved, although income inequality remains high. The Gini Index dropped from 52.5 in 2001 to 47.2 in 2007, a level that is high but typical for Sub-Saharan Africa (SSA). On the other hand, while in 2001 expenditures of individuals in the bottom 40 percent added up to 9 percent of total expenditures, in 2014 they accounted for 14 percent. Even though many people have moved out of poverty, they remain at risk of slipping back if affected by adverse natural events, against which they cannot protect or insure themselves. A third of the population—65.3 percent of them living in rural areas—belong to a family that is engaged in agricultural activities and is therefore directly exposed to droughts. Moreover, the tourism industry has become the main driver of economic growth, going from 4 percent of the GDP in 1999 to an estimated 21 percent in 2014, and accounting for 20 percent of the labor demand. Coastal erosion and natural disasters such as volcanic eruptions, tropical storms or floods can damage touristic facilities and attractions, reducing tourist inflow and limiting tourism's growth, subsequently impacting the economy and poverty reduction efforts.

6. **The Program Development Objective of the proposed operation is to support the Government of the Republic of Cabo Verde in: (a) Strengthening the institutional and legal framework to ensure risk-informed sectoral and territorial planning; and (b) Increasing the financial capacity to manage impacts associated with disaster and climate-related shocks.** The policy reforms included in the proposed operation are aimed at increasing long-term resilience to and ability to recover from the adverse impacts of disasters, thereby helping support the sustainability of the development program and the Government's efforts to eliminate extreme poverty and boost shared prosperity. The supported policy areas align with the Government's efforts to make Cabo Verde more resilient to climate change—following its Sustainable Development Strategic Plan 2017-2021. The Government is demonstrating its commitment to strengthen the Disaster Risk Management (DRM) and Climate Change Adaptation (CCA) agenda by adopting a National Disaster Risk Reduction Strategy, building its institutional capacity and improving coordination among stakeholders to respond in the aftermath of a natural catastrophe, setting up the framework to develop contingency plans, improving the management of fiscal impacts of disaster and climate-related risks, investing for the safety and resilience of existing school infrastructure and roads, and redesigning its territorial planning instruments to address the ongoing urbanization and land use challenges. The World Bank is supporting this agenda through the implementation of Technical Assistance (TA) activities with the Government.

2. MACROECONOMIC POLICY FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

7. **Cabo Verde's economy is recovering from a protracted and deep economic slowdown which followed the 2008 global crisis.** After growing at annual average rate of 6.4 percent between 2000 and 2008, economic activity decelerated sharply on the back of the European sovereign debt crisis.[9] The country struggled to achieve growth rates above 2 percent between 2009 and 2015. The deceleration of economic growth was marked by a sharp decline in net inflows of foreign direct investment (FDI), which was only partly compensated by increased debt-financed countercyclical capital spending by the Government. In addition, returns on private and public investments contracted[10], highlighting weaknesses in the quality of some investments undertaken after the crisis. From 2016 onwards, real GDP growth accelerated, reaching 4.7 percent on average in 2016-2018, driven mostly by the strong performance of private consumption and investment (Table 1). At the sectoral level, GDP expanded thanks to the dynamism tourism activities in the wake of the economic recovery in Europe and the recovery of domestic non-tradable services. This favorable performance was achieved in spite of the 2017 drought that continues to affect the agriculture sector, which contracted by 40 percent between 2016 and 2018.

8. **Low inflation in Cabo Verde and monetary conditions in the Euro Area have provided space to relax monetary policy and support growth.** Annual inflation approximated 1.3 percent in 2018, compared to 0.8 percent in 2017, reflecting higher transport, energy and household prices. Core inflation remained contained at 1.5 percent year-on-year. Cabo Verde's monetary and exchange policy is closely aligned with Europe as the local currency is pegged to the Euro, with the Portuguese Treasury providing access to a short-term credit facility to support the country's foreign exchange reserves. The International Monetary Fund's (IMF) 2018 external stability assessment concluded that the real effective exchange rate (REER) is broadly in line with fundamentals and reserves remain adequate. The REER has been relatively stable over the past two years. With relatively low inflation expectations and limited pressure on the peg since 2014, the Central Bank has maintained an accommodative monetary policy stance. The main policy rate was lowered by 200 basis points in 2017 to a low 1.5 percent. The reserve requirement was also reduced from 15 percent to 13 percent in January 2018. Credit to the economy is responding to this accommodative stance, albeit very slowly, growing at approximately 2.6 percent in 2018.

[9] Europe provides most of the country's remittances (11 percent of GDP), tourism (47 percent of total exports of goods and services), and FDI (7 percent of GDP).

[10] Estimated returns on private investment contracted an average of 43.8 percent in 2002-2008 to an average of 34.3 percent in 2009-2012; on public investment, estimated returns declined from 28.5 percent to 17.3 percent on average over the same periods.

Table 1: **Contribution to GDP Demand and Supply Side, 2017-2022 (Percentage Points)**

Demand Side	2017	2018	2019	2020	2021	2022
Private consumption	7.5	1.0	1.6	2.1	2.5	2.6
Public Consumption	0.0	0.4	1.5	0.1	0.1	0.2
Investment	2.6	3.4	4.1	3.5	3.6	3.7
Public	1.1	-2.0	0.9	-0.4	0.0	0.2
Private	1.9	5.9	3.2	3.9	3.6	3.5
Exports	4.4	5.3	3.8	3.6	3.2	2.7
Imports	10.5	4.6	5.3	3.4	3.4	3.2
GDP Growth	**4.0**	**5.5**	**5.7**	**5.9**	**6.0**	**6.0**
Supply Side						
Agriculture	-2.1	-1.1	0.3	0.3	0.4	0.4
Industry	1.6	1.7	0.6	0.9	0.6	0.7
Services	4.5	5.0	4.8	4.7	5.0	4.9
GDP Growth	**4.0**	**5.5**	**5.7**	**5.9**	**6.0**	**6.0**

Source: Cabo Verdean authorities and World Bank Group (WBG) estimates and projections (April 2019).

9. **Expansionary fiscal policy in the aftermath of the global crisis and increasing support to loss-making** State-owned Enterprises **(SOEs) led to growing fiscal financing needs and rapid public debt accumulation.** With a small fiscal multiplier, the scaling up of the public investment program which followed the global crisis led to a ballooning of the overall fiscal deficit of the central government (which peaked at 12.4 percent of GDP in 2012, up from 1.6 percent of GDP in 2008). Public debt rose rapidly, climbing from 57 percent of GDP in 2008 to peak at 127.8 percent of GDP in 2016. Weak central government fiscal performance was compounded by increasing financial support to loss-making SOEs, notably the airline Cabo Verde Airlines (TACV) and the Real Estate and Housing Fund (IFH). In addition to current transfers to SOEs, government financing needs from below the line linked to SOE recapitalization and on-lending operations have been one of the main underlying causes of the rapid accumulation of public debt. Overall, the SOE sector represents a very significant source of fiscal risks. At the end of 2018, contingent liabilities from the six largest SOEs amounted to 39 percent of GDP.

10. **Since 2014, the Government has embarked on a decisive fiscal consolidation plan to reduce fiscal imbalances and risks, including through SOE reform.** The fiscal deficit declined steadily from 7.6 percent of GDP in 2014 to 2.8 percent of GDP in 2018, and the primary deficit declined by 5.2 percentage points of GDP (Tables 2 and 3). Furthermore, fiscal financing needs, including on-lending to SOEs and recapitalization, more than halved to less than 3.0 percent of GDP over the same period. Containment of on-lending has been tied to the rationalization of the public investment pipeline while capitalization is been driven by support to TACV. Notably, overall support to TACV through capitalization in 2018 approximated 2.0 percent of GDP (Table 4). The authorities also are taking major steps to reduce the fiscal burden and risks linked to SOEs. In 2017, the Government launched an ambitious plan to disengage the State from SOEs and improve risk assessment and monitoring capacities. The SOE Reform and Fiscal Management Development Policy Financing (DPF) (P165631) series supports key reforms in this area.

11. **Driving the narrowing of the fiscal deficit, total revenue expanded from 22.9 percent of GDP in 2014 to 28.1 percent of GDP in 2018.** Tax revenue accounted for most of this increase, rising steadily by 4.5 percentage points to reach 22.1 percent of GDP in 2018. This improvement reflects the harmonization of value added tax (VAT) rates at 15 percent

across all sectors, the introduction of a new tax framework for micro and small enterprises as well as new taxes (on tourism and ecological related activities). The Government has also introduced electronic filing as part of ongoing efforts to improve tax administration to reduce income and value-added tax evasion. Domestic revenue mobilization was also enhanced as non-tax revenues, especially the sale of public goods and services, increased by 1.2 percentage point between 2014 and 2018. Higher grants, related to rehabilitation work in Fogo and Santo Antão following the volcanic eruption and flooding of 2014 and 2016, also had a positive impact on revenues.

12. **Total expenditure reached 30.9 percent of GDP in 2018, 0.3 percentage point above 2014 levels**. Notwithstanding the slight increase expenditure composition has changed in favor of current spending, which, at an average of 25.7 percent of GDP, is much higher than comparable structural peers.[11] This momentum has been driven by current transfers—reflecting increased payments to municipalities with population below 15,000 and upgrading and reinforcing strategic foreign missions—, social benefits, interest payments and other expenses consistent with the Government efforts to settle tax refunds. Capital spending, on the contrary, has declined gradually in the past few years—although this trend was interrupted in 2017 and 2018 following the Government's acquisition of a combined 4.0 percent of GDP in assets from the social housing program *Casa para Todos* (Social Housing Program, CPT) as part of the ongoing restructuring of the program.

13. **After climbing up rapidly for several years, public debt-to-GDP started declining in 2017, but Cabo Verde remains one of the most heavily indebted countries on the continent.** Following an increase from 116 percent of GDP in 2014 to 128 percent in 2016, public debt-to-GDP declined to 123.9 percent in 2018.[12] This was driven primarily by the acceleration in growth, favorable exchange rate movements and fiscal restraint. Approximately 73 percent of central government debt is denominated in foreign currency, of which two-thirds is denominated in Euros. Because of its concessional nature, public debt is characterized by long maturity profiles and low interest rates. The average interest rates on domestic and foreign debt amount to 5 percent and 1.3 percent, respectively.

14. **The external current account deficit has narrowed in recent years, despite a brief deterioration in 2017.** The current account deficit is estimated at 4.5 percent of GDP in 2018, relative to a deficit of 6.6 percent of GDP in 2017. This improvement reflected reduced income and interest outflows by foreign-owned companies. Tourism receipts and private remittances increased by 5.6 percent and 8.8 percent, respectively. Grants declined by more than 20 percent, reflecting the normalization of inflows as the situation in Fogo and Sao Antão was addressed. The goods balance remained largely unchanged in 2018 despite higher fuel imports. The current account continues to be financed mainly through official inflows and foreign direct investment. As a result, international reserves are adequate at 5.1 months of prospective imports.

[11] Structural peers have similar economic characteristics as Cabo Verde and include Sao Tome and Principe, Bhutan and Samoa.

[12] Total public debt includes central government external and domestic debt and external debt contracted by the central government on behalf of SOEs (referred to as "onlending"). It also includes external debt contracted directly by SOEs that carry a central government guarantee. Domestic debt contracted directly by SOEs and by local governments that carry a central-government guarantee are not included.

Table 2: Key Macroeconomic and Financial Indicators, 2014-2022

	2014	2015	2016	2017	2018e	2019p	2020p	2021p	2022p
Income and prices	Annual change unless otherwise indicated								
Real GDP growth	0.6	1.0	4.7	4.0	5.5	5.7	5.9	6.0	6.0
CPI Inflation	-0.2	0.1	-1.5	0.8	1.3	1.6	2.0	2.0	2.0
Fiscal Accounts	Percent of GDP, unless otherwise indicated								
Revenues	22.9	26.9	26.6	28.6	28.1	31.9	29.9	28.1	27.5
Expenditures	30.5	31.4	29.6	31.5	30.9	34.9	32.1	30.0	29.2
Primary balance	-5.4	-2.0	-0.5	-0.4	-0.2	-0.1	0.5	0.6	0.4
Overall fiscal balance	-7.6	-4.6	-3.0	-3.0	-2.8	-2.9	-2.2	-1.9	-1.7
Balance of Payment	Percent of GDP, unless otherwise indicated								
Current Account Balance	-9.1	-3.2	-3.9	-6.6	-4.5	-4.5	-4.1	-3.9	-3.6
Exports	48.0	41.3	43.3	46.2	48.9	49.5	50.4	51.8	53.3
Imports	66.4	56.7	59.9	67.2	67.7	69.0	68.8	69.2	69.6
Foreign Direct Investment	9.7	7.0	7.7	6.3	5.0	4.4	5.5	6.6	6.4
Gross reserves in months of imports	6.2	6.0	6.2	5.5	5.1	5.4	5.6	5.5	5.5
Selected Monetary Accounts									
Credit to the economy (change in percent of broad money)	0.2	1.8	2.3	4.5	1.7	3.2	3.3	3.4	3.3
Broad Money (percent change)	7.8	5.9	8.4	6.6	1.6	6.4	6.8	6.3	6.5
Emigrant deposits/total deposits (percent)	38.0	38.5	37.7	36.8	36.7	36.6	36.6	36.6	36.6
Memorandum items									
GDP (nominal – billion CVE)	154.4	158.7	165.8	173.4	183.8	199.3	215.3	232.8	251.7
Gross international reserves (Euro millions)	420	453	541	518	531	*568*	*627*	*677*	*737*

Source: Cabo Verdean authorities, IMF and WBG estimates and projections (April 2019). The Cabo Verdean Exchange rate has been pegged to the Euro since 1999 at a rate of 110.265 CVE/EUR.

Table 3: Key Fiscal Indicators, 2014-2022 (% of GDP)

	2014	2015	2016	2017	2018e	2019p	2020p	2021p	2022p
					In percent of GDP				
Total Revenues	**22.9**	**26.9**	**26.6**	**28.6**	**28.1**	**31.9**	**29.9**	**28.1**	**27.5**
Tax Revenues	17.6	19.3	19.5	20.7	22.1	22.3	21.8	21.9	22.1
Tax on income and profit	5.0	6.1	6.1	6.5	6.6	6.9	6.3	6.4	6.5
Tax on goods and services	8.3	8.8	9.0	9.7	10.8	10.7	11.1	11.0	11.1
Tax on trade	3.7	3.8	4.1	4.2	4.2	4.3	4.1	4.1	4.0
Other tax	0.5	0.5	0.3	0.3	0.4	0.4	0.4	0.4	0.4
Grants	1.8	2.5	2.7	3.7	1.4	2.7	1.9	0.9	0.8
Other revenues	3.5	5.1	4.4	4.2	4.7	6.9	6.2	5.3	4.6
Total Expenditure	**30.5**	**31.4**	**29.6**	**31.5**	**30.9**	**34.9**	**32.1**	**30.0**	**29.2**
Current expenditure	24.3	25.9	26.3	25.8	26.4	29.7	27.6	25.8	25.0
Compensation to employees	11.1	11.0	11.1	10.9	11.0	11.6	11.0	10.4	10.0
Goods and services	3.7	4.7	4.6	4.0	4.1	5.4	4.9	4.7	4.6
Interest payments	2.2	2.6	2.5	2.6	2.6	2.8	2.7	2.5	2.2
Subsidies	0.1	0.1	0.1	0.1	0.1	0.3	0.2	0.2	0.2
Current transfers	2.8	3.0	3.0	3.5	3.4	3.1	3.3	2.9	2.9
Social benefits	2.8	3.0	3.1	3.2	3.4	3.5	3.5	3.3	3.4
Other expenses	1.5	1.5	1.9	1.6	1.9	2.9	2.1	1.9	1.9
Net acquisition of nonfinancial assets	6.2	5.6	3.4	5.7	4.4	5.2	4.5	4.1	4.2
Primary balance	**-5.4**	**-2.0**	**-0.5**	**-0.4**	**-0.2**	**-0.1**	**0.5**	**0.6**	**0.4**
Budget balance	**-7.6**	**-4.6**	**-3.0**	**-3.0**	**-2.8**	**-2.9**	**-2.2**	**-1.9**	**-1.7**
Net other liabilities	**-3.3**	**-3.2**	**-3.4**	**-0.4**	**-1.0**	**-4.2**	**-1.4**	**-0.8**	**-0.3**
Onlending	-3.2	-2.3	-2.5	0.3	1.1	-1.8	-0.8	-0.4	-0.3
Capitalization	-0.1	-0.9	-0.9	-0.7	-2.0	-1.9	-0.5	-0.5	0.0
Net errors and omissions	-0.1	0.1	-0.9	0.8	-0.8	0.0	0.0	0.0	0.0
Total financing (incl. onlending and capitalization)	**10.9**	**7.8**	**5.6**	**4.2**	**2.8**	**7.2**	**3.6**	**2.7**	**2.0**
Net domestic financing	0.7	1.2	2.9	0.2	1.4	2.2	0.7	0.3	0.1
Net external financing	10.2	6.7	2.7	4.0	1.5	5.0	2.9	2.5	2.0

Source: Cabo Verdean authorities and WBG estimates (April 2019).

Table 4: Estimated Government Support to Cabo Verde Airlines, 2017-2020

(% of GDP)

	2017	2018	2019	2020
Guarantees	2.7	2.8	0.7	0.0
Capitalization	0.4	2.0	1.3	0.0
Onlending	0.0	0.0	0.0	0.0
Subsidies, Transfers and Other	0.7	0.0	0.0	0.0
Total	**3.7**	**4.8**	**2.1**	**0.0**
Memo:				
Stock of Debt*	8.9	8.2	N/A	N/A

Source: Government of Cabo Verde (April 2019). * The numbers for 2018 are provisional.

15. **Legacy issues from the global financial crisis continue to affect Cabo Verde's financial system.** Asset quality, which deteriorated due to extensive exposures to a downturn in the tourism real estate sector, remains a concern. As of end of 2018, non-performing loans (NPLs) in the banking system remained elevated at 12.2 percent of total loans (down from 17.5 percent in 2017), much higher than the SSA countries average (6.2 percent) and lower-middle income countries average (4.2 percent). The authorities have taken regulatory measures, which are under implementation, to facilitate the resolution of NPLs which in the past was hindered by long judicial delays and shallow markets for distressed assets. Despite recent improvement, profitability is still low due to weak bank balance sheets and high operating costs. On the positive front, provisions for NPLs remain relatively strong at about 60 percent. Furthermore, commercial banks, mostly foreign owned, maintain a high capital adequacy ratio (over 18 percent in 2018), well above the Basel II minimum capital requirement of 8 percent and the regulatory minimum of 10 percent in Cabo Verde. Liquidity is relatively high, particularly in the smaller banks and the new entrants, and relies heavily on emigrant deposits. Local banks have been experiencing a loss in several correspondence bank relationships with international banks, which has led to an increase in costs of international transactions.

2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

16. **Real GDP growth is projected to pick up further and average 5.9 percent over 2019-2022 on the back of ongoing structural reforms.** The Government is implementing significant reforms to improve the quality of growth-enhancing essential services in infrastructures and enhance digital and transport connectivity. This is central to the Government's plan to transform the country into a services hub. Continued strengthening in the services sector, particularly tourism, is expected to drive economic growth. One goal is to reduce the reliance of the tourism sector—which is central to the economy of Cabo Verde—on European arrivals to enhance sustainability. As a first step, in March 2019, Cabo Verde Airline launched new flights connecting several countries in West Africa to Europe, North or South America with the option to stay over in Sal. The tourism sector will therefore benefit from increased and more diversified visitor arrivals as new routes are being developed. In addition, the ongoing construction of several hotels across the archipelago should support job creation and further stimulate economic activity. In parallel, efforts to improve the attractiveness of the sector, including the 2018 approval of visa-free access for most European visitors to Cabo Verde, are expected to start yielding benefits. Furthermore, transportation and distribution activities should expand in the context of the recently awarded maritime concession for inter-island transportation, which aims to broaden and improve the range and reliability of maritime services offered to both tourists and business users. These reforms are expected to play a major role in deepening the linkages between the tourism sector and producers of agricultural products across the archipelago. In the fisheries sector, the signing of the long-awaited fishing agreement with the European Union (EU) will also boost activity.

17. **On the demand side, private consumption and investment in transport, tourism, energy and ICT linked to ongoing and planned structural reforms will drive growth acceleration.** These reforms will be anchored in the gradual implementation of projects presented in the December 2018 Partnership Conference in support of the 2017-2021 Government strategy combined by a strong pipeline of private sector projects. As the Government actively seeks to refocus its role in the economy towards regulation and policy aspects, private investment is being mobilized to expand and modernize the operation of several important SOEs through public private partnerships (PPPs), direct sale and concession arrangements. The proposed SOE Reform and Fiscal Management DPF (P165631) series supports some key aspects of these structural reforms. Consumption will also be supported by continued increases in remittances, including from the USA.

18. **Inflation is expected to increase only slightly to 2.0 percent over the medium-term as new capacity is added to the economy.** The increase in inflation will stem from moderately stronger domestic demand and the impact of a gradual recovery in global commodity prices. It is nevertheless expected to remain contained, supported by continued fiscal consolidation and the strong nominal anchor provided by the peg. The primary objective of monetary policy in Cabo Verde is ensuring price stability while supporting the hard exchange rate peg. The central bank has been working to shorten the current transmission lag.

19. **The authorities are committed to reducing the fiscal deficit to under 2 percent of GDP by 2022 and to put the debt to GDP ratio decisively on a downward trend.** The Government intends to support enhanced macroeconomic stability as an important condition for boosting private investment. In this context, the overall fiscal deficit is projected to decrease from 2.8 percent of GDP in 2018 to 1.7 percent of GDP in 2022. The Government is targeting a primary surplus by 2020.

20. **On the revenue side, the Government is deploying a range of measures to improve tax collection and tax administration to ensure that revenues remain strong at around 22 percent of GDP over the medium term.** The measures are expected to counter an estimated 0.5 percent of GDP fall in tax receipts related to the recently approved reduction in the corporate income tax rate from 25 percent to 22 percent effective 2019. Notable measures include: (i) a restriction on some fiscal and customs benefits for financial institutions to reduce tax expenditures by a total of 1 percent of GDP by 2020; (ii) revamping of the micro and small enterprises framework to reduce evasion; and (iii) an increase in the excise tax rates for tobacco and alcohol. The Government is also strengthening the tax and customs units to improve tax collection efficiency and fight tax evasion. This includes developing a data-matching platform to detect tax fraud, reinforcing tax arrears recovery, and strengthening technical skills and capacity of the units. In parallel, non-tax revenue will progressively increase, averaging 5.7 percent of GDP in 2019-2022, compared to 4.4 percent of GDP between 2014 and 2018. Grants will temporarily increase in 2019 reflecting donations from the Government of China.

21. **Total expenditures are projected to peak in 2019 before returning to their previous levels over the medium-term**. In 2019, both current and capital expenditures are expected to increase from 30.9 in 2018 to 34.9 percent of GDP. Current spending will increase partly due to one-off payments for goods and services related to the planned upgrade in border security systems as well as specialized consultancy services in the context of ongoing reforms. The Government has also decided to temporarily boost allocations to selective foreign missions as part of its strategy to enhance the marketing of the country to potential tourists and investors. The public wage bill will also increase in 2019, driven by the final stage of the ongoing upgrade of select categories of workers. However, it is expected to decline in real terms over the medium term, reflecting an agreement with Unions for tighter restraint on new hiring. In the next few years, capital expenditure should also gradually decrease from 5.2 percent in 2019 to 4.2 percent of GDP in 2022. This reflects the completion of the transfer of properties to central government from the CPT program and the decision of the Government to rationalize both foreign and domestically financed public investments. New projects are also being subjected to stricter selection criteria consistent with the use of the public investment management system being supported by the SOE Reform and Fiscal Management DPF (P165631) series.

22. **In support of further fiscal consolidation, decisive steps are also being taken by the Government to gradually reduce the net financing needs stemming from loss-making SOEs.** The privatization of TACV is a major step forward and is instrumental for reducing costs over time. This is to be followed by proactive restructuring and privatization of the other 22 SOEs as per the privatization program of the Government (Annex 6 of the proposed First SOE Reform and Fiscal Management DPF - P165631). However, the SOEs reform program will also imply some costs to the Government in the short-term. In particular, the Government will support the airline's business plan in 2019 and has committed to take over

the company's liabilities as at the end of 2018. While significant upfront costs associated with the restructuring of SOEs will increase total financing (above and below the line) for 2019 to 7.2 percent of GDP, the net fiscal impact of the privatization program is expected to be positive over the medium-term.[13]

23. **Additional reforms are being implemented to improve fiscal and debt management and to enhance the productivity of public investments.** Reforms to improve SOE oversight and monitoring will be crucial for enhancing governance and transparency and to mitigate fiscal risks. Notable reforms underway include: (i) the reintroduction of performance-based contracts for SOEs; and (ii) boosting the technical capacity of the SOE ownership unit, State Commercial Sector Oversight Unit (*Unidade de Acompanhamento do Setor Empresarial do Estado,* UASE), to closely monitor SOE financial and operational performance. This includes the development of tools to better assess the realism/quality of proposals and reports presented by SOEs (including business plans), and to carry out SOE performance benchmarking aimed at informing government decisions regarding recapitalizations and restructuring options. With the support of the SOE Reform and Fiscal Management DPF (P165631) series, the Government has also taken steps to improve the legislative framework for budget and debt management. This will also help to increase debt transparency thanks to expanded debt data coverage. The authorities are also committed to enhancing the efficiency of public investment through a full use of the new Public Investment Management System (PIMS), to ensure an adequate evaluation and prioritization of public investments based on expected returns and alignment with the country's strategic priorities. Notwithstanding the authorities' strong commitment to these policy actions, this is a gradual process, and reaping the full benefits of these reforms will require time.

24. **The external current account deficit is expected to average 4.1 percent of GDP over 2019 -2022 down from 5.5 percent of GDP between 2014-2018.** The lower deficit will be driven by robust growth in tourism receipts and remittance flows. This will help to contain the impact of higher spending on imports tied to new FDI projects, including hotel constructions. The Government is notably implementing an active marketing strategy to promote tourism in the country. External financing needs are projected to be met primarily by FDI and official borrowing. In net terms, official borrowing will decline (Table 5), reflecting higher public debt amortization outflows, increased reliance on domestic sources of financing, and fiscal consolidation. Nevertheless, international reserves are expected to remain above 5 months of imports.

Table 5: Balance of Payments Financing Requirements and Sources, 2014-2022

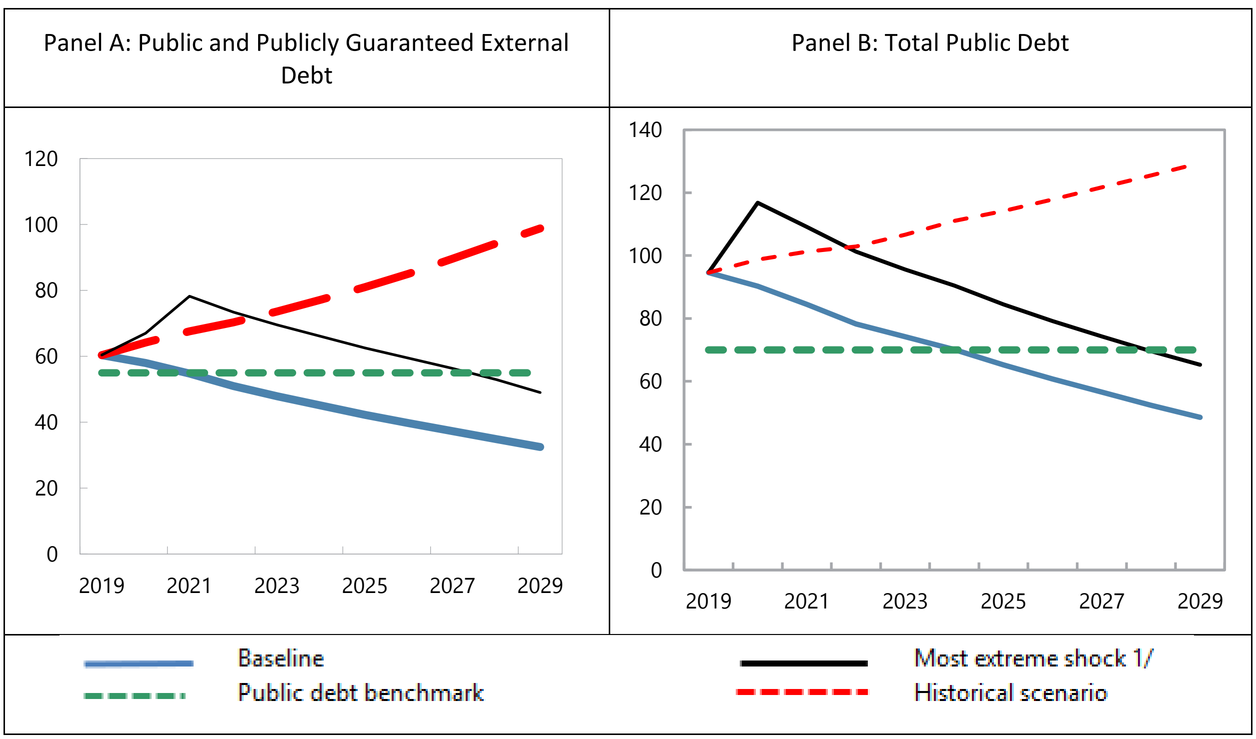
in Million US$	2014	2015	2016	2017	2018e	2019p	2020p	2021p	2022p
Financing Requirements	**237.9**	**182.0**	**91.3**	**175.9**	**169.1**	**143.2**	**145.8**	**175.0**	**181.3**
Current Account Deficit	194.1	51.0	65.3	113.3	87.5	96.8	94.5	98.0	98.0
Amortization	24.5	24.5	26.2	32.8	37.3	46.4	51.4	77.0	83.3
Errors and omission	19.3	106.5	-0.2	29.9	44.3	0.0	0.0	0.0	0.0
Financing Sources	**237.9**	**182.0**	**91.3**	**175.9**	**169.1**	**143.2**	**145.8**	**175.0**	**181.3**
FDI and portfolio investments (net)	71.1	76.3	75.8	56.2	36.8	48.4	81.5	122.8	153.5
Capital Grants	6.6	19.0	12.7	16.1	15.4	29.5	14.2	14.2	14.2
Long term debt disbursements (excl. IMF)	251.0	122.1	94.6	88.5	130.1	108.9	119.8	97.0	84.5
Change in reserves (- means accumulation)	-90.8	-35.4	-91.7	15.1	-13.2	-43.7	-69.7	-59.0	-70.8

Source: Bank of Cabo Verde, IMF and WBG estimates and projections (April 2019).

[13] Total financing needs is the sum of above and below the line balances.

25. **The latest Debt Sustainability Assessment (DSA) updated by the WBG—in collaboration with the IMF—in April 2019, concluded that Cabo Verde's risk of external debt distress remains high.** Compared to the joint IMF/WBG DSA published in the 2018 Article IV report, the updated DSA reflects a higher growth rate (of 6 percent over the medium-term) and the impact of the rationalization in tax expenditure (1.0 percent of GDP in 2020-2022). The present value (PV) of public and publicly guaranteed external debt to GDP reached 61.9 percent in 2018. It breaches the 55 percent threshold (applicable for strong policy performers) over 2 years (Figure 2, panel A). Moreover, the DSA shows that the PV of total public debt to GDP gradually declines but remains above the 70 percent benchmark until 2025. These breaches point to a high risk of debt distress (Figure 2, panel B). Debt service will rise significantly over the medium-to-long-term as the grace period for several concessional loans will end. Furthermore, external debt service could easily exceed the threshold under export shocks. Nevertheless, the external debt service-to-revenue ratio is expected to remain below its threshold by a significant margin over the medium term. Prudent debt management with a strong focus on concessional borrowing remains essential to maintain debt service ratios at manageable levels. Debt risks are compounded by the existence of non-guaranteed domestic debt contracted by SOEs, which is not included in the debt coverage of the DSA.[14] Building on the recently approved debt legislation supported by the SOE Reform and Fiscal Management DPF (P165631) series, efforts are being made to increase transparency in debt recording by broadening the coverage of contingent liabilities under Component 2 of the recently approved SOE Related Fiscal Management Project.

Figure 2: The Public and Publicly Guaranteed External Debt and Public Debt Indicators (2019-2029) — World Bank DSA



Source: IMF and WBG estimates and projections (April 2019).
1/ Extreme shock" refers to the most extreme stress test that includes a shock to GDP and the exchange rate. The "baseline" forecasts refer to a business-as-usual case without reform. The "historical" scenario looks at fiscal performance over history.

[14] This reflect concerns about incomplete detailed SOE balance sheet information. The domestic debt of SOEs is however included in the contingent liability tailored stress test.

Table 6: Debt Composition in Cabo Verde, 2014-2022

	2014	2015	2016	2017	2018	2019	2020	2021	2022
Public Debt	115.9	126.0	127.8	125.8	123.9	124.1	116.1	110.1	103.9
External Debt	89.0	97.0	96.1	93.7	91.0	91.5	85.0	81.1	77.0
Domestic Debt	26.9	29.0	31.7	32.1	32.9	32.6	31.1	29.1	26.9

Source: Government of Cabo Verde, IMF and staff estimates (April 2019).

26. **The macroeconomic outlook is favorable, but downside risks are high.** Domestically, political and social pressure against further fiscal consolidation and SOEs restructuring could derail ongoing efforts to boost growth, address fiscal and external imbalances and reduce the debt burden**.** Failure to sustain program implementation would trigger further accumulation of public debt and heightened debt risks.

27. **Furthermore, external risks remain considering country's persistent vulnerability to global conditions and natural disasters.** Higher-than-anticipated commodity prices, tighter global financial conditions and natural disaster shocks could significantly weigh on external and fiscal balances. The reliance on Europe for most of tourist arrivals also exposes Cabo Verde to a deterioration in the economic situation in Europe. Slower-than-anticipated economic growth could derail the fiscal and debt dynamics and would require stronger adjustment efforts to maintain a downward trajectory for public debt, which may be politically difficult. The country is at a critical juncture where a key challenge is to find an adequate balance between preserving fiscal sustainability and supporting growth, while ensuring that the population benefits from the gains of growth. The response of the private sector to ongoing and planned reforms will be particularly critical.

28. **The macroeconomic framework is deemed adequate for the proposed operation.** As a small open economy, the country remains vulnerable to a range of shocks, but the medium-term growth outlook is positive. Growth is projected to average 5.9 percent in the next few years, supported by an impressive program of structural reforms. Key structural reforms are being undertaken to improve growth-supporting service delivery and lay out a better-leveled playing field for investors. Further, monetary policy is expected to continue to be effective at supporting price stability and the exchange rate peg. The real effective exchange rate is broadly in line with macroeconomic fundamentals. In addition, the authorities have demonstrated their ability to implement fiscal consolidation and meet their fiscal targets. They are committed to achieving a primary surplus from 2020 onwards. The Government is also working on reducing financing needs associated with SOEs. In this context, public debt is expected to fall by 20 percentage points over the medium-term. While the risk of external debt distress is high, public debt is sustainable. Furthermore, international reserves are expected to remain at a comfortable level over the medium term.

2.3. IMF RELATIONS

29. **The last Article IV Report was presented to the IMF Board on March 26, 2018**. The World Bank has been working closely with the IMF and the authorities to strengthen the legislative framework for debt and budget management. Additionally, the IMF and the World Bank teams are coordinating in key areas such as debt management, reforms of the SOE sector and overall macroeconomic stability. The IMF and World Bank teams meet regularly to discuss and exchange views on relevant issues. Coordination between the IMF and WBG will continue to ensure that the authorities receive consistent advice and information in developing and implementing their program. The Government of Cabo Verde is exploring opportunities to strengthen its relationship with the IMF, particularly to support the implementation of the authorities' macro-fiscal program.

3. GOVERNMENT PROGRAM

30. **In the past year, the Disaster Risk Management System in Cabo Verde has mainly focused on emergency preparedness and response activities for adverse natural events.** Some references to prevention and disaster risk reduction have been included in major national development frameworks—such as the Strategic Document for Growth and Poverty Reduction III (2012-2016) and the Transformation Agenda 2030 launched in 2014 with the support of UNDP—and across different sectoral plans with no major implementation and without been carried out in a systematic way across its development planning. There is no institution with the official mandate and resources to promote and support the mainstream of disaster risk management and climate change adaptation across sectors. This has resulted in past DRM reforms largely not being implemented. For instance, in line with international recommendations, a National Platform for Disaster Risk Reduction was created in 2007, but never became operational.

31. **Law no. 12/VIII approved in 2012 provides the legal foundation for the Civil Protection System of Cabo Verde (SNPC).** It gives the mandate of preparedness and emergency response to all kinds of disasters and climate-related events, crises, major accidents to the National Civil Protection Service and Fire Department (SNPCB), overseen by the National Civil Protection Council (CNPC) within the Prime Minister Office. In practice, the SNPCB has implicitly assumed the leading role for DRM without the appropriate technical and human resources capacity nor specific funding through the national budget.

32. **The Strategic Plan for Sustainable Development 2017-2021 (*Plano Estratégico de Desenvolvimento Sustentável,* PEDS) presented to the Parliament in December 2017, identifies vulnerability and resilience as one of the four key challenges to sustainable development of Cabo Verde.** The PEDS is a policy-planning document that builds on the Government's program for the Ninth Legislature (2016-2021)[15], and has been elaborated through a participatory process, including consultations with local governments, central authorities, civil society and private stakeholders to refine the development objectives and generate national ownership. The PEDS identifies climate change vulnerability and environmental fragility—driven by the lack and irregularity of precipitation—as constraints to sustainable development. The PEDS materializes into 35 sectoral programs with explicit references to DRM, climate change, and resilience to be implemented by the Directorates of Planning, Budget and Administration of corresponding ministries.

33. **Recent disasters along with the growing awareness of the potential risks caused by climate change have prompted the Government to adopt a more comprehensive approach to disaster and climate-related risk management through a set of "first-generation" DRM reforms to build institutional capacity at the national and local levels and address underlying disaster risk factors.** The Government has passed several reforms to the SNPC seeking to establish a National System for DRM (SINAGERD) setting up the institutional framework to guide DRM. Ministry of Finance (MoF) has taken a leading role on the disaster risk finance agenda seeking to reduce natural disasters and climate-related risks impacts to macroeconomic stability and fiscal consolidation. In addition, as part of the sectoral programs specified in the PEDS the Government plans to (i) strengthen institutional capacity to monitor and measure hydrometeorological and geophysical activity, as well as promptly and efficiently disseminate risk information; (ii) increasing safety in public critical infrastructure to be resilient to disaster and climate-related events; and (iii) advance towards a more productive and sustainable agriculture to increase ecosystems and rural population resilience to land degradation and climate change impacts. Furthermore, the Government emphasizes the protection of towns and cities against the risks of mass movements, pollution, and floods through structural measures (protection of hillsides, afforestation, drainage and urban

[15] The Government's program for the Ninth Legislature (2016-2021) recognizes and assumes human security as an essential responsibility of the state and identifies as a priority the strengthening of the existing DRM and Civil Protection systems.

regeneration) and non-structural measures (prevention of river occupation and construction supervision, integrated planning and management of watersheds and water resources, contingency planning and the dissemination of climate and meteorological information). This Development Policy Operation is designed to encourage effective policy reforms in key sectors to support the Government in implementing this program.

34. **As a Small Island Developing States , Cabo Verde is highly vulnerable to climate change, and identifies climate resilience as a priority in its development planning agenda**. Cabo Verde is committed to low-emission climate-resilient development, as agreed during the twenty-first Conference of the Parties to the United Nations Framework Convention on Climate Change (COP21). The Government's National Action Plan for CCA (2008-2012) identifies the chronic shortage of water resources for human consumption and agriculture as a serious adaptation challenge. In addition, the Plan highlights the vulnerability of key economic sectors such as tourism and agriculture, caused by the occupation and degradation of coastal zones and salinization of soils and aquifers. The adaptation proposals focus on three strategic areas: water resources; agriculture and forestry; and coastal areas and tourism. This operation is supportive and in-line with these main priorities. Cabo Verde has also signed the United Nations (UN) Convention to Combat Desertification and the UN Convention on Biological Diversity.

4. PROPOSED OPERATION

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

35. **The development objective of the proposed operation is to support the Government of the Republic of Cabo Verde in: (a) Strengthening the institutional and legal framework to ensure risk-informed sectoral and territorial planning; and (b) Increasing the financial capacity to manage impacts associated with disaster and climate-related shocks.** In providing support for DRM and CCA, the proposed operation supports the Government first set of policy reforms towards a comprehensive approach to managing disaster and climate-related risks. The policy framework for the proposed operation is framed under the PEDS 2017-2021. The Government's program is set forth in the Letter of Development Policy (LDP) (Annex 3).

36. **The proposed operation provides a line of contingent financing and will support the Government in being better financially prepared to respond to a disaster and climate-related shocks.** Disaster and climate-related risks represent a contingent liability for the Government, which historically has not been explicitly considered when managing the country's fiscal risks. A review of the financial response to past disasters prepared by the World Bank and the Government indicates that: (i) the gap to fund disaster response and recovery can be of up to 75 percent of the resources required[16]; (ii) the insurance market is limited, with the premiums issued in 2016 amounting to only 1.4 percent of GDP[17]; and (iii) the Government does not have a functional contingent mechanism available dedicated to effectively finance response, recovery and reconstruction processes in the aftermath of natural disaster and climate-related event. To reduce disaster and climate-related contingent liabilities, the Government aims to increase the resilience of public critical infrastructure and buildings, which will reduce the costs of their rehabilitation and reconstruction. To strengthen the management of the residual disaster and climate-related contingent liabilities, this operation will support the Government in providing timely financial response in the aftermath of a catastrophe by securing access to financing before an adverse natural event strikes. As a base layer of financial protection, a dedicated contingency fund has been established to respond to

[16] Which was the case of Fogo eruption in November 2014 to February 15, where the reconstruction needs were estimated at US$30.2 million, and as of mid-2015, the total mobilized was close to US$7.5 million.
[17] Banco de Cabo Verde, 2016.

high-frequency, low-intensity shocks. The Catastrophe Deferred Drawdown Option (Cat DDO) itself will act as an intermediate layer of financial protection, which will increase the availability of immediate liquidity to the Government in the aftermath of a natural catastrophe of medium intensity and frequency, reducing the potential financing gap. The top layer of financial protection to low-frequency, high-intensity disasters is yet to be defined by the Government, for which TA is being provided to consider increased fiscal preparedness in the case of a disaster and climate-related event. The instruments that have been historically used to respond to disasters by the Government are summarized in Table 7, as well as the instruments that will be made available under the Government's plan and supported by the proposed operation.

Table 7: Summary of Disaster Risk Financing instruments available to the Government of Cabo Verde

Frequency of Event	Intensity of Event	Disaster Risk Layer	Past Financing Instrument	Future Financing Instrument
Low	High	**Low frequency & high intensity** (e.g. major earthquake, cyclone, or drought)	International aid and ad-hoc response[18]	Under review
↕	↕	**Medium frequency & intensity** (e.g. flood, minor-moderate earthquake, moderate drought)	International aid, Budget re-allocation	Contingent line of credit (Cat DDO)
High	Low	**High frequency & low intensity** (e.g. localized floods, landslides, minor droughts)	Budget allocation	Dedicated contingency fund

37. **The Cat DDO allows to secure rapid access to financing in the event of a natural catastrophe.** The Cat DDO can be used as bridge financing while funds from other sources are being mobilized. The Cat DDO has a "soft" trigger which means that Loan and Credit Proceeds may be withdrawn upon a declaration of a "*State of Calamity*"[19] that has been issued through a Resolution of the Council of Ministers to respond to an imminent or occurring natural catastrophe, under article 20 of Law no. 12/VIII/2012 of March 7th, and under no. 2 of article 265 of Cabo Verde's Constitution, last revised in 2010. The Government has chosen to fund the US$5 million IDA Cat DDO using the Concessional Core option. Under this option, 50 percent (US$2.5 million) of the IDA Cat DDO amount would come from the country's Concessional Core IDA envelope. Terms and conditions of the Cat DDO are specified in the financing and loan agreements. These agreements describe the drawdown[20], financial[21], and renewal[22] conditions of the Cat DDO.

[18] For instance, for the Fogo eruption the Government resorted to an ad-hoc increase in VAT.
[19] *Situação de Calamidade.*
[20] The proposed operation includes a deferral period of up to three years. During this time, the World Bank will monitor that the Government is continuing to implement the program being supported in accordance with its LDP.
[21] The IBRD portion of a DPF with a Cat DDO would have a revolving feature by which the amounts repaid before the closing date would be available for drawdown in accordance with the terms of the loan agreement.
[22] A Cat DDO may be renewed if the implementation of the program set out in the LDP remains satisfactory to the World Bank and macroeconomic policies are adequate. The IDA portion of the Cat DDO may be renewed one time for a total of six years, the IBRD portion of the Cat DDO, four times for up to three years each time, for a total deferral of 15 years.

38. **The Cat DDO complements the First State-Owned Enterprises Reform and Fiscal Management DPF1 (P165631).** The DPF1 is designed to support the Government to reduce fiscal risks from SOEs while promoting private-sector led provision of infrastructure services and strengthening accountability and effectiveness in fiscal management. The Cat DDO especially compliments the first pillar of the DPF1 by addressing the strengthening of the Government to manage fiscal risks associated to disaster and climate-related shocks. Together, the DPF1 and the Cat DDO represent a coherent package of support to help the Government manage contingent liabilities from different sources.

39. **Climate change adaptation considerations are included in all the Prior Actions (PA) of the operations**. Cabo Verde being a Small Island Developing State is greatly exposed to the expected negative impacts of climate change, which will likely increase the frequency and severity of hydrometeorological hazards (riverine floods and droughts) and dramatically increase sea level rise (and hence coastal floods). The policy actions included in the proposed operation will support strengthening the country's resilience and capacity to adapt to climate change.

40. **The design of the proposed operation takes into account lessons learned from many years of World Bank operations in the area of DRM and preparation of Cat DDOs, as reflected in the Independent Evaluation Group Report *'Hazards of Nature, Risks to Development'*.**[23] The proposed operation also incorporates key lessons learned from prior DPFs, such as the Cat DDOs in Panama and El Salvador in 2011, the Philippines in 2011 and 2015, Sri Lanka in 2014, Peru in 2012 and 2015, Seychelles in 2015, the Dominican Republic and Serbia in 2017 as well as the DRM DPF in Bolivia in 2015. Key lessons learned include the following: (a) a successful Cat DDO operation needs to align actions and activities with government priorities; (b) DRM policy is most effective when based on adequate risk identification, including both physical and fiscal risks; and (c) the implementation of a DPF with a Cat DDO should be set within a broader financial protection strategy against disasters and climate-related shocks. This is particularly relevant for Small Islands State countries as Cape Verde following the lessons learned from the implementation of the Seychelles Cat DDO.

4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

41. **The proposed operation will support the Government's ongoing reforms to disaster and climate-related risk management system to mainstream and incorporate disaster risk reduction and climate resilience as a cross-cutting requirement through the sector and development planning.** The program has two pillars: Pillar A - Strengthening the institutional and legal framework to ensure risk-informed sectoral and territorial planning; and Pillar B - Increasing the financial capacity to manage impacts associated with disaster and climate-related shocks. The policy reforms supported by the proposed operation represent a substantial commitment by the Government to a holistic approach to disaster risk reduction and climate resilience.

Pillar A: Strengthening the institutional and legal framework to ensure risk-informed sectoral and territorial planning

42. **Through the reforms included in Pillar A, the Government is establishing the necessary institutional structures and legal framework to mainstream DRM and CCA in sectoral and territorial planning**. To ensure an efficient management of emergency situations and to mainstream DRM and climate resilience in the design of public policies it is critical to set up the right institutional structures that have the mandates, competences, and accountabilities to oversee risk assessments and coordinate the different entities within and outside each sector. Similarly, to reduce the long-term human and economic impact of disasters it is crucial to reduce disaster and climate-related risk in public and private

[23] World Bank. 2006. *Hazards of Nature, Risks to Development: An IEG Evaluation of World Bank Assistance for Natural Disasters.* Independent Evaluation Group. Washington, DC: World Bank.

infrastructure. The costs of investing in disaster-resilient infrastructure are much lower than repairing, retrofitting, and reconstructing buildings and infrastructure in the aftermath of a disaster, and disaster-resilient infrastructure is also key to ensure business and services continuity and enable a quick recovery in the aftermath of a disaster. Under this pillar the operation will support the adoption of the National Disaster Risk Reduction Strategy (ENRRD[24]) 2018-2030, a reform of the territorial planning legal framework integrating disaster and climate-related risk management considerations, and a reform to the National Statistical System (SEN) strengthening the legal framework and technical standards for effective data-driven decision making in DRM.

Prior Action 1: The Government has adopted the National Disaster Risk Reduction Strategy.

Legal Evidence*: Resolution no. 114/2018 adopting the National Disaster Risk Reduction Strategy approved by the Council of Ministers on April 12, 2018 and published in the Official Gazette dated October 20, 2018.*

43. **Despite several reforms undertaken in the past years to strengthen the DRM system in the country, establishing a comprehensive system still requires additional critical policy reforms coupled with the strengthening of institutional capacity at national and subnational level.** The SNPCB faces institutional and human resource capacity challenges. As a volcanic archipelago, the geographical complexity of the country poses significant logistical challenges for the coordination of emergency response. Emergency operation plans including activities related to disaster preparedness, emergency response and evacuation plans are not systematically developed and updated at the regional and municipal level. The creation of a National Emergency Call Center established to have a centralized control center to support municipalities in case of a natural catastrophe will be operational at the beginning of 2019. Standard operating procedures need to be defined and aligned across different levels of government to ensure coordination and logistical support. The role of sectoral ministries and MoF are critical to promote and implement risk reduction activities in the country.

44. **In recognition of these challenges and shortcomings, the Government has adopted the ENRRD, a comprehensive policy framework to guide the institutionalization of the appropriate governmental structures to manage and reduce disaster and climate-related risks.** The Government has taken actions to build a more proactive and transversal approach to incorporate disaster and climate-related risk management considerations in development and sectoral planning and avoid the creation of new risks. The SNPCB in consultation with a wide range of Government stakeholders[25] coordinated the preparation of the ENRRD. In the ENRRD, the Government recognizes the current absence of a legal and institutional framework to guide DRM in the country and establishes the SINAGERD to develop effective institutional arrangements, planning tools, an information system and coordination mechanisms with well-defined roles, responsibilities and capabilities and proposes the definition of appropriate financing mechanisms for its implementation. The ENRRD is aligned with the timeline of the Sendai Framework for Disaster Risk Reduction 2015-2030 and the Economic Community of West African States Action Plans for Disaster Risk Reduction. Under the SINAGERD, the National Council for Disaster Risk Reduction and Management will be established to coordinate the integration of DRM into sectoral programs across the ministries and promote inter-sectoral coordination and policy oversight. The Council will be composed of sectoral and line ministries and agencies. A Special Office for DRM will be established within the Ministry of Internal Administration (MAI) to coordinate the implementation of the strategy, coordinate the SINAGERD and serve as

[24] Estratégia Nacional de Redução de Riscos de Desastres.

[25] With financial support from the Governments of Japan and Luxembourg and technical support from the United Nations Development Programme (UNDP) and other development partners.

Secretariat to the Council.[26] This will be complemented by the re-launch of the multi-stakeholder National Platform for Disaster Risk Reduction, which will involve the Government, private sector, civil society and development partners. The strategy was approved by the Council of Ministers on April 12, 2018 and published in the official Gazette dated October 20, 2018.

45. **To ensure capacity for implementation and sustainability of the reforms, the ENRRD proposes several financial mechanisms** such as including a line for DRM in the annual budget or integrating the reforms under the sectoral programs of the PEDS—for which financing is secured annually in the national budget. The costing and financing mechanisms of the reforms are yet to be completed by the Government. Additional policy reforms would be necessary to effectively operationalize the ENRRD, a World Bank TA program has also been mobilized to assist the Government in the operationalization of the strategy and complement the support from other development partners like UNDP.

46. **Expected Results.** The ENRRD will encourage a more comprehensive disaster risk management system, vertically at the national and sub-national levels, as well as horizontally, across sectors. Among others, it is expected that sectors will incorporate DRM into their infrastructure management plans, thus reducing contingent liabilities. This will be tracked through the annual progress report of implementation of the ENRRD.

Prior Action 2: The Government has amended the Territorial Planning Legal Framework to incorporate the use of disaster and climate-related risk information in the development of territorial planning instruments.

Legal evidence*: Decree-Law no. 4/2018 reforming the Territorial Planning Law (LBOTPU) promulgated on July 6, 2018, published in the Official Gazette dated July 6, 2018, and in force on July 9, 2018.*

47. **Cabo Verde is experiencing a rapid urbanization process increasing the country's-built environment** which may lead to an increase in damages in the case of a natural catastrophe, if public and private investments are not accompanied by measures to mitigate vulnerabilities. While almost 50 percent of the population lived in urban areas in 1996, by 2016 this number increased to 67 percent. The underlying rural-urban migration process has been mainly driven by lack of job opportunities in the rural areas but also by land degradation, and significant drought events that have affected the Cabo Verdean population in recent years. Monitoring and assessment of the effectiveness and efficiency of territorial and urban planning and land management have been limited. Improperly regulated urbanization could have a negative impact on ecosystems and the environment, which would hinder the development of the tourism industry.

48. **Existing territorial planning instruments do not appropriately integrate and enforce the use of disaster and climate-related risk considerations.** Decree-Law no. 1/2006, amended by Decree-Law no. 6/2010, sets the basis for territorial planning in Cabo Verde. The national and regional territorial planning instruments are the National Directive for Territorial Planning (DNOT) and the Regional Framework for Territorial Planning (EROT), respectively. At the municipal level, there are three key instruments: The Municipal Master Plan (PDM), the Urban Development Plan (PDU), and the Detailed Plan (PD). Coordination among the different instruments is key to avoid duplication and ensure alignment of different levels of government around the use and management of the territory. This has proved to be extremely complex and difficult, particularly at the municipal level between the PDM, PDU and PD, as their scope was not well-defined and the mechanisms for implementation not aligned. In addition, until now, all municipal instruments were required to be ratified and approved by national authorities, which slowed down the implementation process. Moreover, the different instruments were not required to integrate DRM and CCA considerations in their design and preparation which prevented

[26] To be composed of two DRM specialists, and a director.

a proactive management of disaster and climate-related risks focusing on reducing existing risks and avoiding the creation of new risks.

49. **The Government is implementing a set of policy reforms that will strengthen urban, territorial planning by streamlining and systematizing regulations.** The PDU will be removed to reduce duplication in territorial planning instruments, and municipalities will not be required to submit their PDs for central government approval as established until now. This will allow for a more decentralized territorial planning process and shortening the approval time of the territorial planning instruments. Following the reform, disaster and climate-related risk considerations will have to be incorporated into updated territorial and urban planning instruments at different levels of government to comply with the new regulations. The DNOT is reformed to include directives and guidelines for incorporation disaster and climate-related risks in territorial planning. Regional (EROTs) and municipal (PDMs and PDs) instruments will need to comply with the national guidelines and include targeted hazard and risk information.[27] Territorial Plans for Integrated Tourism Development Areas (ZDTI) —which are often located along the shoreline—will also have to comply with this regulation. Integrating DRM considerations into the territorial planning instruments will require reliable hazard and risk information with a specific spatial resolution depending the instrument, as well as sociodemographic and geographical information. This builds on the Government's efforts to strengthen the framework for managing and openly sharing information[28] for data-driven decision making and the recently establishment of the Spatial Data Infrastructure of Cabo Verde (IDE-CV) led by National Institute for Territorial Planning (INGT) which creates the framework of geographic data, metadata, users and tools that are interactively connected in order to use spatial data in an efficient and flexible way. The IDE-CV will enable the different sectoral and governmental levels to share relevant information and strengthen the use of disaster risk information for territorial planning.

50. **Expected Results.** Following the new territorial planning framework, the Government will first need to update the DNOT to incorporate DRM and CCA considerations. With a new DNOT in place at the national level, all other territorial planning instruments described above will need to be updated. Municipalities will have developed updated or new PDMs and PDs complying with the national directive and regional frameworks. Key indicators to measure the implementation of this critical reform will be to ensure that all new PD incorporate disaster and climate-related risk management considerations as well as the proportion of ZDTI with Tourist Development Plans (POT) that incorporate disaster and climate-related risk management considerations, in line with this new framework. In the medium and long-term these measures are expected to reduce the impact of disaster and climate-related events and avoid the creation of new risks.

Prior Action 3: The Government has reformed the National Statistical System which incorporates open data standards, protocols and procedures.

***Legal evidence**: Law no. 48/IX/2019 reforming the National Statistical System approved by Parliament in January 2019 and published in the Official Gazette dated February 19, 2019.*

51. **A comprehensive statistical system is a critical component of building resilience in a country.** Cabo Verde lacks the appropriate mechanisms to collect and share data and information from different sources to provide a framework for data-driven decision making. The legal and institutional framework for the SEN is limiting and does not allow stakeholders to access the sociodemographic information of the Cabo Verdean population. This not only hampers the

[27] Article VIII specifies that (i) the DNOT and EROTs are approved by Resolution of the Council of Ministers; (ii) the PDMs are approved by the Municipal Council and ratified by the Government; and (iii) the PDs are approved by the Municipal Council.
[28] Supported by PA3.

ability of the sectors and local governments to access critical socioeconomic data to allow for better targeting of services and social programs, but also limits the scope of post-disaster interventions, and targeted risk reduction measures and projects. Reliable and readily available household socioeconomic data are required to rapidly identify the population most likely to be affected by drought conditions and inform the design of adequate interventions to increase the resilience of these households. Improvements in the targeting process and timeliness of interventions undoubtedly result in economic as well as social benefits with efficiency gains achieved for emergency actors and limited income and welfare losses for affected populations. The prioritization of specific areas for disaster risk reduction and coastal management programs require socio-economic data to define specific criteria to ensure that policy outcomes support the achievement of poverty reduction targets and participate in building resilience of the poorest and most vulnerable. At the sectoral and local levels, the availability of top-quality socioeconomic information is thus essential for the design of disaster risk management measures and post-disaster interventions that contribute to build resilience of the poorest and most vulnerable.

52. **The legal framework that supports the SEN dates from eight years ago and does not align with the country's recent efforts to integrate data-driven decision making in the design of public policies**. The Government recognizes that a statistical system capable of consistently producing high-quality information that can be used to support data-driven decision-making is key to operationalize the sectoral programs of its Sustainable Development Strategic Plan. The National Strategy for Statistical Development (ENDE) 2017-2021 was approved by the National Statistical Council in June 26, 2018 and has been allocated a budget line for its implementation. The ENDE is the planning tool for the official short-, medium- and long-term statistical activity of the SEN and for the coordination of partnerships for official statistics, capable of ensuring adequate predictability of resources for statistical activity in the country and promote the open data agenda. Making high-quality statistical information public can directly contribute towards more informed decision-making on public policies to better manage and reduce disaster risk.

53. **Recognizing the limitations of the current legal framework, the Government has reformed the SEN through Law no. 48/IX/2019 to strengthen the mandates of the country's statistical organizations, promote a comprehensive management and harmonization of statistical data in the country, and establish the institutional arrangements for sharing data among different agencies and Ministries.** Currently, sociodemographic information produced by the SEN is aggregated at the municipal level before public disclosure. Data at the statistical unit level is available only within the National Institute of Statistics (INE) laboratory in Praia, preventing other administrative institutions at the sectoral and municipal level from accessing this information. The approved reform supersedes Law no. 35/VII/2009, previously governing the SEN. The reform strengthens the institutional framework to enhance the data collection, management, and distribution processes while raising the standards of statistical confidentiality. Main changes and improvements to the legislation are (i) giving the SEN the mandate to disclose anonymized data—private data without personally identifiable information—at the statistical unit level upon request for national interest and scientific purposes; (ii) including among the SEN's objectives to collect and harmonize the statistical information available across different public institutions; (iii) including the National Data Protection Commission in the National Statistical Council (governing body of the SEN); and (iv) allowing the Government to create a National Fund for Statistical Development as a special financing source for the SEN to ensure the production of high-quality official statistics. The ENDE will support the operationalization of this new legal framework for statistical data in the country. Promoting data sharing protocols will directly contribute to (i) the understanding of risk, through better identification of Cabo Verdean communities highly vulnerable to natural catastrophes; (ii) informing the design and targeting of DRM and CCA interventions; and (iii) the monitoring and evaluation of the impact of these policies on the population. To achieve these objectives, the Government is preparing a dissemination strategy to promote the use of statistical data.

54. **Expected results.** Under a strengthened legal framework to produce official statistics and the adoption of Open Data standards, protocols and procedures, it is expected that the newly anonymized statistical information generated by the SEN will build the framework for data-driven decision making for the management and reduction of disaster and climate-related risks. It is anticipated that the data will more frequently underpin decision-making and be systematically used for the monitoring and evaluation of impacts and benefits from DRM interventions. It is also expected that the adoption of new protocols and procedures will improve cost-effectiveness for data collection, management and analysis. The open data produced by INE is expected to provide critical information to develop risk applications and decision support tools used for territorial planning, and to better target beneficiary groups that are vulnerable to disaster shocks and climate change impacts across the sectors and municipalities. The Government presented in June 2018 the Voluntary National Report for the implementation to the 2030 agenda for Sustainable Development[29], which is framed in a close collaboration between the MoF and INE in the use of geographical, socioeconomic and geospatial information to measure effectiveness and implementation of public policies. A registration system will be established for users to request specific data and describe the objectives of its use. INE will provide description and general metadata of the data in their website to promote its use in several applications.

Pillar B: Increasing the financial capacity to manage impacts associated with disaster and climate-related shocks

55. **Under this pillar, the Government is putting in place key institutional structures and taking actions towards the management of fiscal risks to increase its preparedness, response capacity, and fiscal resilience to disaster- and climate-related shocks.** The Government has adopted a set of policy reforms to improve the management of the fiscal costs associated with natural disasters. The proposed operation will support the establishment of a Risk Management Unit within the Treasury Department of the MoF, and the creation of a dedicated contingency fund to finance emergency response and recovery in the aftermath of a natural catastrophe.

Prior Action 4: The Government has created a Risk Management Unit in the Treasury Department of the Ministry of Finance.

Legal evidence*: Decree-Law no. 28/2018 creating the Risk Management Unit approved by the Council of Ministers on March 23, 2018, promulgated May 21, 2018, published in the Official Gazette dated May 24, 2018, and in force on July 9, 2018.*

56. **As a Small Island Developing State with a high debt-to-GDP ratio, natural catastrophes affecting Cabo Verde pose a significant risk to the sustainability of public finances.** However, until now the MoF has not had a dedicated unit to identify, quantify, and manage fiscal risks, including those due to disaster and climate-related shocks. MoF has in the past financed disaster response and recovery in an ad-hoc manner. Part of the reason for this is that neither MoF nor any other Government body has had a clear institutional mandate on the management of fiscal risks associated to disaster and climate-related shocks. There is a need to quantify the potential fiscal costs of natural disasters, a key step in developing a comprehensive disaster risk finance strategy as part of the overall fiscal risk management framework, which is being supported under the DPF1.

57. **To manage operational and fiscal risks—including those associated to disaster and climate-related shocks—in an ex-ante and comprehensive manner, the MoF has created a Risk Management Unit in the Treasury Department of the MoF.** The mandate of this new unit is to identify and manage all risks that could negatively affect MoF systems and operations, as well as any risks that could negatively affect fiscal outcomes, including those related to potential disaster

[29] https://sustainabledevelopment.un.org/index.php?page=view&type=30022&nr=909&menu=3170

shocks. In relation to disaster and climate-related shocks more specifically, the Government requested support from the WB to include as part of the mandate of the unit to (i) quantify the socioeconomic and financial impacts of disasters, in particular through the impact of disaster on public and private assets; (ii) develop a sovereign disaster risk financing strategy to manage disaster related contingent liabilities; and (iii) oversee the implementation of the strategy. The creation of this unit builds on the diagnostic on Cabo Verde's current state of financial protection against disasters undertaken in preparation of the Cat DDO by the Government with World Bank TA and embeds the creation of the new disaster contingency fund in wider Government efforts to put in place a strong institutional framework for increased financial resilience against disasters. The Government is currently working in the Operational Manual of the unit with support from the World Bank and it is expected to establish and have an operational Risk Management Unit in early 2019.

58. **Expected Results.** Going forward, the Government will systematically and periodically quantify disaster related contingent liabilities to inform its wider fiscal risk management strategy. A better understanding of the potential fiscal cost of disasters will be a crucial input for the MoF's development of a cost-efficient strategy for financial protection against disasters. The operationalization of the Unit will be measured by the publication of an annual report presenting the quantification of operational and fiscal risks that could arise from different type of external and internal shocks.

Prior Action 5: The Government has created the National Emergency Fund to finance emergency response and recovery in the case of a disaster or climate-related shock.

Legal evidence*: Decree-Law no. 59/2018 creating the National Emergency Fund approved by the Council of Ministers on October 30, 2018 and published in the Official Gazette dated November 16, 2018.*

59. **Analysis on Cabo Verde's fiscal vulnerability to disasters has shown that recent natural catastrophes have had important economic and fiscal impacts.** Cabo Verde has no adequate ex-ante financial instrument to cover the costs of recurrent events and would face severe funding shortfalls in the case of larger events. Recent events such as Hurricane Fred and the 2014/2015 volcanic eruption at Fogo had significant economic and fiscal impacts. Direct and indirect losses associated to the Fogo eruption were equivalent to 2 percent of GDP. The fiscal impacts of these events were also sizable, but the authorities did not have adequate financial provisions to finance response and recovery operations. Instead, they had to resort to international assistance and, in the case of the Fogo eruption, an ad-hoc increase in VAT (of 0.5 percentage points) for both immediate response and recovery financing. As with the above-mentioned events, the Government has historically relied on international assistance to deal with the effects of droughts. To finance the implementation of the drought contingency plan in 2017, various donors—including the EU —contributed a total of CVE 800 million (approximately US$9 million). The Government allocates funds for contingencies in its annual budget[30] that can be used to respond to relatively small and recurrent events. In 2018, such allocations amounted to CVE 200 million (approximately US$2.2 million). If such allocations are not sufficient to cover costs for unforeseen events, experience indicates the Government resorts to budget re-allocations or, as already mentioned, international assistance. Both can lead to important delays in response, potentially exacerbating negative social and economic impact. Following the volcanic eruption in Fogo and hurricane Fred, the Government recognized the need to increase available resources for disaster response, improve tracking of disaster response expenditure, and harmonize procedures for the mobilization, allocation, and execution of resources for disaster response.

[30] Funds for contingencies are allocated in both the recurrent and investment budgets.

60. **The Government has decided to create the National Emergency Fund (FNE) to finance emergency response and recovery in the aftermath of a disaster or climate-related shock.** A 1998 law provides for the Special Stabilization and Development Fund *(FEED*[31]*)* to finance disaster response through the provision of loans, but this fund has never been operationalized. The decision to create a dedicated disaster contingency fund rather than operationalize the FEED was taken for two reasons: (i) the *International Support for Cabo Verde Stabilization Trust Fund* was going to be closed in August 2018, which removes the financing source of the FEED (the August 2018 deadline has not been met but the closure of the Trust Fund is currently under review by the Government and is expected to happen soon); and (ii) the FEED was created with the purpose of providing post-disaster response through loans, limiting the speed and flexibility for immediate emergency response. The FNE—which was created under the Law on Autonomous Funds no. 109/VIII/2016—will not face this limitation. Furthermore, it will be financed through a defined annual budget allocation, ensuring greater predictability of inflows. The by-laws of the fund establish the annual budget allocations to the emergency fund which has been set at 0.5 percent of non-earmarked revenues collected two years prior to the year for which the budget is being prepared. They also establish beneficiaries of the fund; eligible expenditures; potential beneficiaries of the fund; rules for accessing fund resources; rules for reporting on, and accounting for executed fund resources; and auditing requirements. The new disaster contingency fund, in combination with the Cat DDO, represents a significant step toward strengthening Cabo Verde's fiscal resilience against disasters and climate-related events.

61. **Expected Results.** The FNE is expected to lead to a consolidation of recurrent disaster response spending under one "account" through which resources will flow, thus facilitating tracking of and accounting for such resources. This is expected to increase accountability and transparency of post-disaster spending vis-à-vis citizens and donors who will continue to play an important role in financing the response to medium-sized and large events in Cabo Verde. Information on spending will be collated and analyzed in an annual report produced and published by the MoF. Furthermore, predictable source of funds for preparedness, emergency response and recovery, and clear rules on the allocation and execution of resources are expected to lead to faster preparation of and execution of contingency plans and/or disaster response projects/programs. The allocation to the FNE has been setup based on the current budget line dedicated to emergency response that the Government has established few years ago. It is expected that this allocation will remain constant over the years, but the amount allocated will depend on several factors including the country's macroeconomic situation.

62. **The policy reforms supported under the Cat DDO are grounded in sound analytical work, as described in the analytical underpinning Table 8.** PA1 was informed by international frameworks, in particular the Sendai Framework for Action; PA2 is supported by evidence to suggest that effective land-use planning has wide-ranging economic benefits; PA3 is supported by widespread evidence and international experience to demonstrate the impacts of open data policies to empower individuals and the private sector to consider disaster risk management in day-to-day decision-making; PA4 and PA5 are informed by case studies from other countries around the world, particularly small island states, that demonstrate the effectiveness of mitigating against the fiscal risks of natural disasters through the establishment of contingency funds.

Table 8: Cat DDO Prior Actions and Analytical Underpinnings

[31] Fundo Especial de Estabilização e Desenvolvimento. As originally conceived, the FEED was to be initially capitalized with privatization proceeds and then to receive 5 percent of the annual returns of the "International Support for Cabo Verde Stabilization Trust Fund". However, the FEED was never regulated and the transfers from the Stabilization Trust Fund never materialized.

<table>
<tr><th>Prior Actions</th><th>Analytical Underpinnings</th></tr>
<tr><td colspan="2">Operation Pillar A: Strengthening the institutional and legal framework to ensure risk-informed sectoral and territorial planning</td></tr>
<tr><td>Prior Action 1</td><td>- Sendai Framework for Disaster Risk Reduction 2015-2030.
- Hallegatte, Stephane; Bangalore, Mook; Bonzanigo, Laura; Fay, Marianne; Kane, Tamaro; Narloch, Ulf; Rozenberg, Julie; Treguer, David; Vogt-Schilb, Adrien. 2016. Shock Waves: Managing the Impacts of Climate Change on Poverty. Climate Change and Development; Washington, DC: World Bank.
- Hallegatte, Stephane; Vogt-Schilb, Adrien; Bangalore, Mook; Rozenberg, Julie. 2017. Unbreakable: Building the Resilience of the Poor in the Face of Natural Disasters. Climate Change and Development; Washington, DC: World Bank.
- World Bank, 2013. Building Resilience: Integrating climate and disaster risk into development. Lessons from WBG experience. The World Bank, Washington DC.</td></tr>
<tr><td>Prior Action 2</td><td>WBG. 2016. Investing in Urban Resilience: Protecting and Promoting Development in a Changing World. World Bank, Washington, DC. This report illustrates how building urban resilience is critical for poverty reduction and shared prosperity.
- Tanner, T.M., Surminski, S., Wilkinson, E., Reid, R., Rentschler, J.E., and Rajput,S. (2015) The Triple Dividend of Resilience: Realising development goals through the multiple benefits of disaster risk management.</td></tr>
<tr><td>Prior Action 3</td><td>- OpenDRI, Open Data for Resilience Initiative. Policy Notes and Principles. Washington, DC: World Bank. This World Bank publication describes five principles that have guided the OpenDRI team on the creation, management and use of risk information to design and enact impactful and sustainable projects.</td></tr>
<tr><td colspan="2">Operation Pillar B: Increasing the financial capacity to manage impacts associated with disaster and climate-related shocks</td></tr>
<tr><td>Prior Action 4</td><td>- OECD, World Bank (2016). Climate and Disaster Resilience Financing in Small Island Developing States.
This report spells out the trends in concessional financing available for climate and disaster resilient development in Small Island Developing States and contributes to understanding what financing resources are already made available to Small Island Developing States and main access challenges.
- Mitchell T, Mechler R, & Harris K (2012). Tackling exposure: Placing disaster risk management at the heart of national economic and fiscal policy.</td></tr>
<tr><td>Prior Action 5</td><td>- Joint G20 Publication by the Government of Mexico and the World Bank. Improving the Assessment of Disaster Risk to Strengthen Financial Resilience.
- The Government of Cabo Verde and the World Bank (forthcoming). Diagnóstico do risco de catástrofes naturais nas finanças públicas.
This document provides a diagnostic of the disaster risk financing in Cabo Verde including options for consideration in developing a Disaster Risk Financing Strategy.
- Lederman, Daniel, and Justin T. Lesniak. 2017. Open and Nimble: Finding Stable Growth in Small Economies, Summary.
This publication notes that for small economies limited territory plays a role in shaping how economies are affected by natural disasters. Aside from direct impacts on GDP growth, disasters exacerbate many other macroeconomic problems small states face. They create trade and fiscal imbalances that can lead to higher levels of debt, and they may also decrease savings and investment in the region because of the uncertainty they cause. Thus, exposure to natural disasters does not just increase external</td></tr>
</table>

	volatility but is also a potentially important factor in the remaining two sets of common challenges to small states: fiscal management and low long-term savings rates. - World Bank. 2012. *FONDEN: Mexico's Natural Disaster Fund—A Review*. Mexico's fund for natural disasters, was established in the late 1990s as a mechanism to support the rapid rehabilitation of federal and state infrastructure affected by adverse natural events. FONDEN was first created as a budget line in the Federal expenditure budget of 1996 and became operational in 1999. Funds from FONDEN could be used for the rehabilitation and reconstruction of: 1) public infrastructure at the three levels of government (federal, state, and municipal); 2) low-income housing; and 3) certain components of the natural environment. It channels resources from the federal expenditure budget to specific reconstruction programs. - Clarke, D. J., & Dercon, S. (2016) *Dull Disasters? How planning ahead will make a difference*. This report makes the case that financial and budgetary planning, ahead of disasters, can lower losses from extreme events. It also emphasizes the importance of quick liquidity post-disaster, which is the purpose of this DPF, and the need for having multiple sources of post-disaster financial resources, which this prior action aims to achieve.

4.3. LINK TO CPF, OTHER WORLD BANK OPERATIONS AND THE WBG STRATEGY

63. **The proposed operation is aligned with the 2018 Systemic Country Diagnostic (SCD)[32], which will inform the objectives and outcomes of the upcoming FY20-25 Country Partnership Framework (CPF).[33]** The SCD identified five binding constraints for growth and shared prosperity, including among them: (i) lack of resilience of households and the economy to external shocks, natural disasters and climate change; and (ii) weak public-sector performance, with the Government inefficient in delivering the needed policy reforms. The proposed operation supports reforms to strengthen institutional and legal framework to increase disaster and climate resilience, addressing these specific constraints.

64. **The objectives of the proposed operation are aligned with the ongoing WBG operations in the country.** The policy reforms included in the proposed operation include inputs from different sectors and complement the overall World Bank lending and TA program in the country. The proposed operation is closely aligned with the First Fiscal Management and Growth DPF (P165631) operation which aims to reduce fiscal risks and enhance fiscal management in support of sustainable private-sector led growth. The following ongoing operations have contributed to the design of the proposed operation: (i) the Cabo Verde Education and Skills Development Enhancement Project (P164294) and Education Technical Assistance (P162445) which assists the Government in the operationalization of its Education Strategic Plan and strengthening their School Infrastructure Rehabilitation Plan; (ii) the First Additional Financing to the Cabo Verde Transport Sector Reform Project (P161248), which supports the Government's efforts to improve efficiency and management of its national road assets; and (iii) the Social Inclusion Project (P165267), which supports the Government's efforts in building a robust social protection system that promotes social and productive inclusion.

4.4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

65. **The Government program supported by the proposed operation is embodied within two national strategies—the PEDS and the ENRRD—which were developed through extensive consultation and citizen engagement.** The policy reforms supported by the proposed Cat DDO will contribute to reducing Cabo Verde's vulnerability to natural disaster and climate-related risks, which has been identified as a critical challenge for sustainable development in the PEDS. The

[32] Report Number: 130289
[33] Expected Board presentation in FY20.

PEDS is the result of an extensive participatory process that engaged actors from different spheres of society through workshops and multi-stakeholder dialogues, including the public sector, local governments, civil society, private sector and development partners. Furthermore, the National Disaster Risk Reduction Strategy—which provides the general framework of the policy areas being supported by the operation—was also crafted in a participatory manner, with consultations from key stakeholders and policymakers leading to the seven priority areas identified for disaster risk reduction.

66. **The WBG maintains active dialogue with development partners engaged in DRM and technical cooperation in Cabo Verde.** The proposed operation builds upon and complements past and ongoing work from other agencies on DRM and CCA. The program supported by the Cat DDO was discussed with partners to ensure complementary in planned interventions and has been designed to ensure the integration with these initiatives. The preparation of the ENRRD by the SNPCB had technical support from UNDP and financing from the Governments of Japan and Luxembourg. The policy reforms led by INGT have received technical and financial support from UN-HABITAT and UNDP. UNISDR has also provided technical support to SNPCB on the development of an historical national disaster database. For emergency response, following its longstanding partnership with Cabo Verde, in 2017 the EU contributed about US$8 million to finance a drought mitigation plan, along with contributions by the African Development Bank and the Food and Agriculture Organization.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

67. **The overall poverty and social impacts of the policies supported by this Cat DDO are expected to be positive**. The series of reforms supported by the proposed Cat DDO are expected to contribute in building resilience to disaster and climate-related events of the most vulnerable by (i) setting up the adequate institutional and legal framework for managing disaster and climate-related risks and avoid the creation of future risks; (ii) providing timely and sufficient financial resources to effectively implement post-disaster interventions; and (iii) the increased ability to access and produce relevant risk information to support the design of interventions limiting disaster-related human and welfare losses. In Cabo Verde, disasters and climate-related shocks can increase poverty directly by damaging productive assets and increasing unemployment, or indirectly through higher inflation, lower economic growth, and the disruption of public utilities. Droughts are undoubtedly the most significant threat to the population. 30 percent of the population is rural—of which 48.5 percent are poor—a situation exacerbated by recent repeated drought episodes (2014, 2017) leading to extensive crop failures. Other hydro-meteorological and geological events can have substantial impacts on physical infrastructures, which in turns often disproportionately affect the poorest. The 2014-2015 Fogo eruption caused substantial income losses for those relying on agriculture and tourism-related activities as their main sources of revenues.[34] On the other hand, floods are reported to not only cause damages to crop but also disrupt access to markets for households engaged in agricultural production. Targeted studies were undertaken to support the Poverty and Social Impact Analysis (PSIA), including (i) citizen consultations in the form of focus group discussions with farmers and population engaged in tourism-related activities from various income groups and livelihood zones; and (ii) a quantitative study using the annual Multi-objective Continuous Surveys (IMC) aimed at capturing the effects of drought conditions on the labour market in rural areas.[35]

[34] Post-Disaster Needs Assessment (PDNA), Fogo volcanic eruption, 2014-2015.
[35] Estimations of the impact of droughts on monetary poverty (income or consumption) were impossible due to data limitations in the IMC.

68. **Under Pillar A of the operation, key reforms seeking to strengthen the institutional and legal framework to ensure risk-informed sectoral and territorial planning are expected to have positive social impacts**. The design of the National Disaster Risk Strategy (PA1) was informed by extensive consultations, including various community and vulnerable groups. It will benefit the most vulnerable including women, children and the elder by setting up the platform for the development of agricultural insurance products and adequate early warning systems, as well as the implementation of strengthened social protection mechanisms. Facilitating access to socio-economic microdata will support the targeting of such interventions in the aftermath of drought events by promoting the development of thorough vulnerability analyses. In Cabo Verde, droughts push subsistence farmers towards more precarious and underpaid activities (e.g.: collection of waste food in landfill and reselling to pork farmers, temporary road construction/refurbishment works among others), or simply unemployment. Estimations for the island of Santiago indicate that, on average, drought conditions cause an 8 percent decrease in rural employment levels every year—compared to a situation with normal conditions. Furthermore, one standard deviation decrease in precipitation is associated with a 20 percent fall in employment levels.[36] Moreover, focus groups on the islands of Santiago, Fogo, and Santo Antão revealed that recent drought events significantly eroded livelihood means (soil degradation, livestock losses, lower access to irrigation). Additionally, a gender wage gap was consistently reported, which exacerbates the vulnerability of women-led households to disaster and climate-related shocks and contribute to explain the gender-differentiated impacts of disasters. The implementation of a dedicated institutional structure defining clear mandates in emergency situations, along with the development of an efficient drought early warning system provided for in the ENRRD will allow for timely interventions limiting welfare losses as well as the adoption of adverse coping strategies. The analysis showed that the recent drought episodes led to an increase in inter-island and rural-out migration, and in farmers' risk aversion who stopped cultivating and preferred to engage in low-productivity and precarious jobs. The design of the amended legal framework that incorporates disaster and climate-related risk management considerations into the territorial planning legal framework under PA2, was also informed by extensive consultations. This PA will likely curb the direct impacts of floods on the housing sector, which tend to disproportionately affect the poorest. The integration of risk information in the development of territorial planning instruments will also contribute to limit disruptions of crucial public services for the poor: access to markets, schools, health centres among others. While overall poverty and social impacts under this policy reform are expected to be positive, limited social impacts could arise from the implementation of different territorial planning instruments. The potential impacts have been assessed as reversible, limited in time and space, and manageable under the current regulatory and institutional frameworks in place in the country and the national grievance redress mechanisms. All potential social impacts would be examined in compliance with existing national regulations and procedures—more particularly Legislative-Decree no. 3/*2007 (Public Utility Expropriation Law)* which guarantees fair compensation in case of involuntary resettlement. For grievance redress, the Mediation Scheme (Decree-Law no. 31/2005) and the Arbitration Scheme (Law no. 76/VI/2005) set the basis through which a voluntary agreement may be reached with assistance from the National Mediation and Arbitration Center and the Conciliation and Monitoring Municipal Commissions. PA1 will support reducing gender gaps and specific challenges identified above in the case of disaster and climate-related shocks.

69. **Under Operation Pillar B, measures taken to increase the financial capacity to manage the impacts of disaster and climate-related risks are expected to bring positive social impacts**. Positive impacts will mainly stem from the

[36] A logit model was estimated considering an employment dummy for a sample from the annual IMC surveys, consisting of 6,374 rural individuals between 15 and 60 and not enrolled in school on the island of Santiago. Surveys rounds span over the period 2011-2017 and were carried out between October and December. Precipitation anomalies at the district level were calculated based on gridded data from the Climate Hazard Group.

creation of a contingent fund under PA5. The timely availability of sufficient resources for post-disaster emergency response and recovery will shorten the transition back to pre-disaster living conditions of the affected households, in particular women-led households, and limit potential medium to long-term impacts on human capital. Addressing contingent liabilities under this Pillar could potentially support scalable, disaster-responsive social protection measures, which will support the most vulnerable including women, children and elder, to reduce implicit liability and bring about positive social impacts. In this respect, the 2017 drought epitomizes the need for an integrated risk financing strategy. A US$10 million mitigation plan was established entirely relying on international aid, which significantly slowed down the implementation process. Although greatly affected by drought conditions, some individuals have reported not receiving support yet.

5.2. ENVIRONMENTAL ASPECTS

70. **Over the last 25 years, the Government has made significant strides in developing a framework for environmental management and mainstreaming environmental sustainability.** Law no. 6/IV/93 is the Basic Law of Environmental Policy of Cabo Verde. Articles 30, 31 and 32 establish the objectives and required content of Environmental Impact Assessments (EIAs) for new operations and projects, while article 33 establishes Environmental Licensing. Legislative-Decree no. 14/97 defines the content of an EIA report and establishes the fundamental principles for environmental management and protection with the objective of enhancing the natural resources and combating the different sources of pollution. EIAs must maintain the balance among various natural environment components. EIAs must include: (i) a study of the local environment; (ii) a study of modifications resulting from the implementation of the project; and (iii) a full inventory of foreseeable impacts, and measures to suppress, reduce and compensate for the possible impacts on the environment. The General Directorate of Environment in the Ministry of Agriculture and Environment is institutionally saddled with reviewing and clearing EIAs. Decree-Law no. 29/2006 establishes the institutional and legal framework and regulations for the environmental evaluation of public and private projects that might have environmental effects.

71. **The policy reforms supported by the proposed operation are unlikely to have significant negative impacts on the country's natural assets.** All the actions supported throughout the operation are policy-oriented; they do not support direct investment in environmentally impactful projects or involve policy actions with significant environmental consequences. Under Pillar A, the proposed reforms are aimed at strengthening the institutional framework and improving regulations for increased resilience and reduction of disaster and climate-related risks. The policy reforms under this Pillar will promote natural resource and environmental management and are likely to reduce environmental degradation. The design and operationalization of sectoral and municipal strategies following the adoption of the ENRRD will contribute to strengthen the institutional framework for DRM, including a better understanding of the environmental impact of disasters. This will help inform environmental protection policies that aim to achieve increased climate and disaster resilience. The reform to the Territorial Planning Law has been designed to strengthen zoning regulations and resilient and sustainable spatial planning, therefore reducing environmental degradation. Although unlikely, potential harmful environmental impacts derived from this policy reform will be limited in time and space and will be monitored and addressed through the Environmental Assessment procedures in place and under the guidance and supervision of the General Directorate of Environment. In case of conflict, a voluntary agreement may be reached under the Mediation and Arbitration Schemes. Under Pillar B, the proposed reforms aim at increasing the financial capacity to manage the impacts of disaster and climate-related risks will not induce—directly or indirectly—negative environmental effects.

5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS

72. **The Public Financial Management (PFM) systems in Cabo Verde has undergone positive changes, as evidenced by the findings of the 2015 Public Expenditure and Financial Accountability (PEFA)**. The PEFA report documented clear progress made with respect to the comprehensiveness and transparency of the budget, policy-based budgeting and internal controls, as well as accounting and reporting. The authorities have made significant efforts in devolving some budget responsibilities to line ministries. Directorates in charge of Planning, Budget and Administration have been installed in sector ministries to support the decentralization of PFM and manage the control aspects necessary for proper execution of the budget. The Financial Management Information System has been revamped through the introduction of Integrated Budget and Financial Management System (*Sistema Integrado de Gestão Orçamental e Financeira,* SIGOF). This has given the authorities a strong management tool and has the potential to speed up budget execution, develop accountability mechanisms and boost the quality of reporting. The Government's budget is now publicly available on the Ministry's website, as are quarterly budget-execution reports. The merger of the Ministries of finance and planning and the introduction of program-based budgeting have greatly contributed to aligning the budgeting and planning processes. Both functions are now more integrated, and the link between the national plans and strategies and the budget is being continually reinforced. Significant progress has also been made over the last few years in implementing a Treasury Single Account (TSA). Several bank accounts have been closed, and payment systems have been modernized through near-full automation. Cash and debt management have also been reinforced.

73. **Greater budgetary credibility will nevertheless be necessary to better align actual spending with the government's development agenda**. Weak budget credibility, lack of transparency in the in-year reallocation of funds and limited enforcement of the recommendations of the auditor general highlighted in the PEFA assessment are areas still requiring strengthening.

74. **The IMF's most recent safeguards assessment of the Central Bank of Cabo Verde (*Banco de Cabo Verde,* BCV) was carried out in 2008 but the BCV is regularly audited by an international auditing firm which issued a clear opinion on the 2017 financial statements.** According to the external auditor, the accompanying financial statements present fairly and appropriately, in all material respects, the financial position of the BCV on December 31, 2017 and its financial performance and flows for the year then ended in accordance with the accounting principles applicable to the BCV. In addition, BCV has taken steps to strengthen its internal control environment, including the adoption of International Financial Reporting Standards (IFRS), the development of reserves-management procedures, the introduction of an internal audit function, and the rotation of external auditors.

75. **Fiduciary Risk**: Overall the World Bank has assessed implementation performance of the public financial management reform program to date and Government's commitment to its improvement as moderately satisfactory. The fiduciary risk associated with the proposed operation is therefore rated as moderate. This rating is based on the status of the PFM system and the BCV's internal control framework, accounting systems and auditing arrangements. Continuing efforts to reinforce the public financial and budgetary management are supported by development partners.

76. **The MoF will follow disbursement procedures of the World Bank to handle the DPO with Cat DDO proceeds.** The Cat DDO is the disbursement mode for this operation. Credit and Loan proceeds will be disbursed if the pre-specified trigger defined in the financing and loan agreements is met and will not be tied to any specific purchase. Once the financing and loan agreements are declared effective, if drawdown conditions for a natural catastrophe are met, MoF may submit a withdrawal application requesting the World Bank to deposit the proceeds of the Credit and Loan into the budget account that forms part of the country's official foreign exchange reserves held with the Central Bank and

acceptable to the World Bank. The World Bank will monitor the implementation of the DRM program (see Annex 1). If it is not being implemented in a satisfactory manner, the Borrower may not be eligible to submit a disbursement request. This will be communicated in writing to the MoF. The adequacy of the macroeconomic framework is assessed at effectiveness and reconfirmed at renewal, but it is not required for drawdown. Further information of the drawdown triggers, financial features, drawdown period, and renewals are detailed in the financing and loan agreements. The Government may have the option of drawing down Credit and Loan proceeds for up to three years. The renewal will follow the applicable World Bank procedures for extending closing dates. The Government will ensure that upon receipt of the Credit and/or Loan proceeds, an equivalent amount will be credited in the Government's budget management system to finance budgeted expenditures. The financing and loan agreements will include a clause for the provision, upon the World Bank's request, of an audit of the deposit account. Due to the described conditions, no additional fiduciary arrangements are deemed necessary for this operation.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

77. **The MoF is the main counterpart agency of the World Bank for the proposed operation.** MoF is involved in the coordination and monitoring of the proposed operation, with a key leading role in the preparation and coordination of the proposed Cat DDO program. The implementation of the program is a shared responsibility with the MoF, the SNPCB, and other agencies and ministries involved.

78. **The results indicators selected to monitor and evaluate implementation progress and the achievement of program outcomes stem from the institutional reform agenda of the institution that takes the coordination lead for that prior action.** The indicators will be tracked by the associated line ministry or public agency. Some of them are used as results indicator in their institutional progress reports. In this context, the operation builds on the existing monitoring and evaluation systems of the Government, which should ensure that program performance is monitored at minimal additional burden to the institutions. The General Directorate of Planning within the MoF will be the main counterpart with the primary responsibility to monitor program progress and to ensure the accountability of relevant institutions to the commitments made.

79. **To ensure sustainability of the program, a comprehensive TA program has been mobilized to support the Government in the implementation of the proposed policy actions.** EU financing from the Africa Disaster Risk Financing Program, through the Global Facility for Disaster Reduction and Recovery (GFDRR), is supporting MoF to design and operationalize the dedicated disaster contingency emergency fund and in the establishment of the Risk Management Unit focused on strengthening the capacity to manage contingent liabilities associated with disaster and climate-related risks. The team has also received funding from the Government of Luxembourg, through the GFDRR with three key objectives: (i) at sectoral level, to support the Ministry of Education in the incorporation of disaster and climate-risk management considerations in the design and construction as well as rehabilitation and reconstruction of school infrastructure; (ii) support SNPCB to undertake a disaster preparedness and response capacity needs assessment and provide TA in the design standard operating procedures for emergency response; (iii) support INGT to strengthen hazard and risk information for enhanced territorial planning.

Table 9: Link between Prior Actions, ENRRD Priority Areas, and Technical Assistance Activities

Prior Action	Relevant ENRRD Priority Area	Associated WBG Technical Assistance
PA 1 on National Disaster Risk Reduction Strategy	Strengthen disaster risk governance	Support the development of emergency preparedness and response capacity needs assessment and standard operating procedures. Support to incorporate disaster and climate-related risk reduction into infrastructure sectoral plans.
PA 2 on Territorial Planning Legal Framework incorporating disaster and climate-related risk management considerations	Integrate risk reduction into development and sectoral planning	Support to develop hazard and risk information. Support to increase technical capacity to manage and use hazard and disaster risk information for territorial planning purposes.
PA 3 on National Statistical System reform which incorporates open data standards, protocols and procedures	Improve the understanding of disaster risk	Support to strengthen collaboration between INE and INGT on issues related to resilience to disaster and climate-related risks. Support to increase Statistical Capacity of INE (under other TA program led by WB).
PA 4 on establishment of a Risk Management Unit in the Treasury Department of the Ministry of Finance and **PA 5** on the creation of a dedicated contingency fund to finance emergency response and recovery in the aftermath of a natural catastrophe	Finance disaster risk reduction and manage financial/fiscal risks	Technical assistance to MoF on disaster risk finance.

80. **Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit *http://www.worldbank.org/GRS*. For information on how to submit complaints to the World Bank Inspection Panel, please visit *www.inspectionpanel.org*.

6. SUMMARY OF RISKS AND MITIGATION

81. **There are substantial risks to achieving the development objective of the proposed operation.** Areas of special concern include macroeconomic risks; the adequacy of strategies, policies and governance at the sectoral level; and the lack of institutional capacity for implementation and sustainability of the proposed program in the long term (Table 10). The risk rating of the proposed operation is closely aligned with the First SOE Reform and Fiscal Management DPF (P165631).

82. **Macroeconomic risks are high.** Actions to ensure the effective transfer of significant fiscal risks stemming from SOEs to the private sector will help mitigate fiscal risks. However, delays in reforming SOEs would derail efforts aimed at reducing fiscal financing needs. Furthermore, external and natural shocks, as well as potential delays in tax reforms could increase fiscal pressures and result in fiscal slippages. However, the Government has shown a strong commitment to achieving fiscal consolidation targets and is making a considerable effort to strengthen its oversight of SOEs. These efforts are supported by the SOEs Related Fiscal Risk Management Project. This is to be complemented by the implementation of a comprehensive strategy for improved debt management, with the support of the World Bank and the IMF. Furthermore, the new budget and debt management legislations will help to improve fiscal responsibility. With the support of the proposed operation, the Government has also established a Risk Management Unit within the Treasury Department of the MoF to identify and manage all risks that could negatively affect fiscal outcomes, including those related to potential disaster shocks. The authorities have also advanced with the creation of a dedicated contingency fund to finance emergency response and recovery in the aftermath of a natural catastrophe, which will enable more predictable funding for preparedness, emergency response and recovery.

83. **There is a substantial risk to the development objective stemming from inadequate sector strategies and policies.** With the approval of the ENRRD, a DRM office under the MAI will be created, assuming the function of managing and reducing disaster and climate-related risks, and the role of coordinating DRM across sectors and provide technical support to municipalities. If not adequately implemented, the new institutional framework and DRM office will undermine progress towards the project objectives. Similarly, the recent reform of the organigram of the MoF modifying the structure and mandates of the different directorates needs to be effectively implemented to achieve the objectives of the prior action, namely to manage operational and fiscal risks, including those associated with disaster and climate-related risks. The proposed operation provides support to the MAI and MoF and has leveraged resources to continue supporting the Government through a TA Program that will contribute to implement ongoing reforms, thus helping mitigate these risks.

84. **Risks related to the institutional capacity for implementation and sustainability are substantial.** The institutional capacity of the public sector of Cabo Verde is high when compared to other SSA IDA countries, as suggested by the Country Policy and Institutional Assessment score of 3.8 on the "*Public Sector Management and Institutions*" cluster. However, sectors and municipalities still have limited technical and financial resources—exacerbated by weak inter-island connectivity and inter-ministerial coordination—which affect the capacity of the Government to move forward with planned reforms. Implementing the policy reforms supported by the operation will require strong commitment and increased technical capacity from the sectors and local governments. The proposed operation seeks to mitigate these risks by: (i) focusing on key policy reforms that have strong Government buy-in; and (ii) providing a TA to strengthen the institutional capacity of the Government in selected areas.

Table 10: Summary Risk Ratings

Risk Categories	Rating
1. Political and Governance	Moderate
2. Macroeconomic	High
3. Sector Strategies and Policies	Substantial
4. Technical Design of Project or Program	Moderate
5. Institutional Capacity for Implementation and Sustainability	Substantial
6. Fiduciary	Moderate
7. Environment and Social	Moderate
8. Stakeholders	Moderate
9. Other	
Overall	Substantial

ANNEX 1: POLICY AND RESULTS MATRIX

Prior Actions	Results Indicator	Baseline	Target
***Operation Pillar A* - Strengthening the institutional and legal framework to ensure risk-informed sectoral and territorial planning**			
Prior Action 1. The Government has adopted the National Disaster Risk Reduction Strategy.	Annual progress report of implementation of the ENRRD strategy presented to the National Civil Protection Council.[37]	N/A [2018]	Published for 2019, 2020 and 2021
Prior Action 2. The Government has amended the Territorial Planning Legal Framework to incorporate the use of disaster and climate-related risk information in the development of territorial planning instruments.	All new municipal detailed plans (PD) incorporate disaster and climate-related risk management considerations.	N/A [2018]	All (22 estimated) [2022]
	Proportion of Integrated Tourism Development Areas (ZDTI) with Tourist Development Plans (POT) that incorporate disaster and climate-related risk management considerations	0 [2018]	56% (15 of 27) [2022]
Prior Action 3. The Government has reformed the National Statistical System which incorporates open data standards, protocols and procedures.	Number of monthly request forms to access INE data from registered institutional users.	N/A [2018]	10 [2022]
	Number of MoUs signed between INE and public institutions/sectors to systematically share data with INE.	1 [2018]	8 [2022]
***Operation Pillar B* – Increasing the financial capacity to manage impacts associated with disaster and climate-related shocks**			
Prior Action 4. The Government has created a Risk Management Unit in the Treasury Department of the Ministry of Finance.	Report on contingent liabilities including those associated with disaster and climate-related shocks published together with the medium-term fiscal framework.	None [2018]	Published at least one time before 2022
Prior Action 5. The Government has created the National Emergency Fund to finance emergency response and recovery in the case of a disaster or climate-related shock.	Allocation to the National Emergency Fund included annually in national budget.	N/A [2018]	Exists in 2019, 2020, 2021 and 2022 budget
	Annual activity and accounting report for the National Emergency Fund approved by its Board.	N/A [2018]	Approved for 2019, 2020 and 2021

[37] Including the monitoring of approved sectoral infrastructure management plans incorporating disaster and climate-related risk reduction measures.

ANNEX 2: LETTER OF DEVELOPMENT POLICY

Ministério
das Finanças
Gabinete do Ministro das Finanças

Ms. Kristalina Ivanova Georgieva-Kinova
Interim President of the World Bank Group
WASHINGTON, DC

N. Ref: 286 /GMF/2019

Praia, April 2nd, 2019

Subject: **Letter of Development Policy**

Dear Ms. President,

1. This development policy letter presents the reforms being implemented by the Government of Cabo Verde to reduce fiscal risks and enhance fiscal management in support of sustainable private-sector led growth. The letter also highlights reforms to strengthen the institutional and legal framework to increase disaster and climate resilience, as well as incorporating disaster and climate resilience considerations into the management of critical infrastructure and territorial planning.

2. The government of Cabo Verde is strongly committed to boosting private sector led growth and tackling the high ratio of public debt over Gross Domestic Product by implementing critical structural reforms. To that end, the Government will need sustained funding support from its strategic partners while it continues to implement its strategy to be less dependent on the development partners financial support. This Fiscal Management and Growth Development Policy Financing (DPF) series and the Disaster Risk Management Development Policy Credit and Loan with a Cat DDO are fully aligned with the objectives of Sustainable Development Strategic Plan (PEDS). The DPF supports government reforms to reduce fiscal risks in key State-Owned Enterprises (SOEs), while boosting private-sector led provision of infrastructure services. The DPF also supports government efforts to strengthen efficiency, accountability and transparency in fiscal management. This will support government´s efforts for fiscal consolidation and enhanced fiscal sustainability.

3. The letter focuses on the following aspects: (i) the PEDS; (ii) the economic context and outlook; and (iii) the reform agenda under implementation by the Government.

I. PEDS - Sustainable Development Strategic Plan

4. The PEDS sets challenging targets for the 2017/2021 period, using a consistent long-term approach that is based on four structural objectives: (i) making Cabo Verde a MidAtlantic circulation economy; (ii) guaranteeing Economic & Environmental Sustainability; (iii) assuring social inclusion and reducing inequalities and asymmetries; and (iv) reinforcing sovereignty, valuing democracy and guiding diplomacy towards the country's development challenges.

5. The PEDS, in defining as an objective "making Cabo Verde a Mid-Atlantic circulation economy", responds to the imperative to be part of the World Economic System (SEM) by focusing on the political, institutional and social stability of the country so as to capitalize on the on the country's geo-strategic location. Cabo Verde is a country with a strategic location for efficient and potentially cost efficient connections between Africa, Europe and America, open to the world, cosmopolitan and safe with low political, social and health risks, with a strong focus on building a knowledge and innovation economy, to function as an air, maritime, digital and innovation, financial, commercial and industrial and investment platform for its greater contribution to the World Economic System

6. This additional contribution to the World Economy requires a positive attitude toward development and a belief by the citizens on the country's potential a predisposition to change the current state of affairs and build a shared future that benefits current generation while not undermining future generations. Transformative reforms are thus required. Reform requires clarity of purpose, strategy, intent, consistency, courage and good time management to make transformative changes to the institutional, economic and social environment needed to achieve the development objectives.

7. For an effective and efficient implementation of the PEDS, it requires : (i) a model of economic growth based on private investment, which foster debt sustainability, and brings about shared prosperity and on social and territorial inclusion; (ii) a major focus on local and regional development via greater decentralisation, mindful of sustainable development goals and with the State partnering with enterprises and with non-governmental organisations; (iii) a competent public administration focused on a mission of public service and guided by the supremacy of law; and (iv) political and governing action aimed at stimulating families' autonomy and self-sufficiency via employment, production and income generation and instruments that define clear objective and impartial rules for citizens' access to benefits and social and programmes.

8. The key performance indicators in the PEDS are ambitious: increasing the average income of Cabo Verdeans, reducing public debt, reducing the unemployment rate, significantly improving the Human Development Index, and reducing social inequalities and absolute poverty. We are confident we will achieve them.

II. Macroeconomic policy framework

9. During the period of 2010-2015, economic growth decelerated significantly to an average of 1.5 percent (compared to 7.6 percent in the 2004-2009 period), a result of the protracted impact of the global financial crisis. Countercyclical fiscal measures did not restore growth but instead led to a sharp increase in the stock of debt. GDP growth recovery started in 2016 and was consolidated in 2017, as information from the Institute of National Statistics shows GDP grew by 4.7 percent and 4 percent, respectively. Recent information for the 2018 indicates that the economy grew by 5,5 percent, with a strong increase in the fourth quarter of 2018 around 7.6 percent. Investors and consumers' confidence indicators are also positive and improving.

10. With inflation expectations low and limited pressure on the peg, monetary policy has been accommodative. The Central Bank will remain vigilant, adjusting policy as needed to ensure price stability while supporting growth.

11. On the fiscal front, this Government inherited a country in 2016 with the highest debt to GDP ratios and among the slowest growing on the continent. However, the fiscal strategy adopted by the current Government in focused in a medium term fiscal consolidation with the overall fiscal deficit decreasing from 4.6 percent of GDP in 2015 to 2.8 percent of GDP in 2018. We have been working to address the fiscal imbalance in a more holistic way. This includes: (i) implementation of a proactive fiscal consolidation strategy based notably on improved tax collection; (ii) enhanced public investment prioritization to ensure that selected projects are aligned with the PEDS and will yield the highest development impact; and (iii) strengthened legislative underpinnings for budget and debt management.

12. While public debt is high, debt service remains manageable due to the high level of concessionality of external debt. This was confirmed by the International Monetary Fund Article IV assessment. In fact, the sustainability of the debt was confirmed. Nevertheless, the Government is committed to further reducing the debt level and maintaining a decreasing debt trajectory. Recent estimation shows a reduction from 126 percent of GDP in 2015 to 122.8 percent of GDP in 2018 and the target is to achieve 100% by 2025 based on: (i) the sustained implementation of our ambitious SOEs divestiture program which will be instrumental to reduce net public sector financing needs while generating revenues from divestiture proceeds; and (ii) real GDP growth acceleration. The Government is also working on the new medium-term debt management strategy to better guide its annual borrowing in line with clearer targets.

III. Reforms agenda

Reducing fiscal risks arising from SOEs while unlocking binding constraints to accelerating growth and supporting private-sector led growth. The Government of Cabo Verde intends to foster private sector-led growth while consolidating public finances to reduce the deficit and debt levels. Our policy is to divest from State-Owned Enterprises (SOEs) as a mean to bring about increased competitiveness and service delivery, and reduced fiscal risks from SOE-related contingent liabilities. The Government believes that it is critical that key service providers in the economy be owned and managed by private operators, as they bring increased investment, technical and managerial know-how and a drive for better quality and performance. In addition, the divestiture from key sectors, will allow the operational, commercial and financial risks associated with the operations in these sectors to be shifted to the private operators, who are better equipped to turn around these enterprises into profit making entities. Furthermore, the divestiture program will help the Government reduce public debt by generating revenues from the sale of public assets, and bringing down SOE-related net financing needs for the general government, and reducing SOE debt.

13. To better monitor the SOEs, a Public Enterprise Reform Unit (UASE) was set up within the Ministry of Finance in 2016. UASE is the result of the merger of the SOEs Department, formerly housed in the Treasury Department, and the Privatization and Public, Private Partnership (PPP) unit. Its mission is to implement a wide ranging privatization program and enforce a rigorous oversight on SOEs, to not only ensure improved efficiency, but also mitigate the fiscal risks tied to these companies until they are divested from.

14. An action plan has been prepared for the divestiture of key SOEs. A list of 23 enterprises to be divested from or restructured has been approved by the Cabinet and published in the Official Gazette. The Government has also undertaken important measures to accelerate this process. In addition, we have undertaken prompt action on the SOEs posing the most critical risks to help foster growth and which can have a negative impact on debt sustainability.

15. First, the Government has taken decisive measures to mitigate fiscal risks arising from the national airline, TACV (now Cabo Verde Airlines - CVA). In preparation for privatization, CVA has been proactively restructured through [ongoing] substantial employee retrenchment, debt restructuring, and the development of new strategies to enhance its core business. CVA's domestic operations were discontinued as of August 1st, 2017 after establishing a partnership agreement with Binter, a Spanish carrier, to provide inter-island air transport services. Binter was selected considering its substantive experience in offering inter-islands services in the Canary Islands, where the overall flight conditions are quite similar to those of Cabo Verde. The State has no involvement in the domestic air transportation and does not provide any subsidy to the operator who has agreed to provide services to all islands. It is worth noting that for domestic air service transportation, the current operator does not have any exclusive right to be the sole operator. As such, any operator who wish to operate in Cape Verde simply needs to meet the requirements to be granted a certification by the regulatory agency.

With respect to the international operations, the Government entered in 2017 into a one-year management contract with Icelandair to get CVA ready for its privatization. In parallel to having a management contract while privatization was being prepared, the company has undergone a complete restructuring, as explained in paragraph 17. In addition, and as per Law Nº 47/IV/92 of July 6, the company was the object of a valuation and based on the terms set out, as per Decree Law Nº 45/2017 of September 21, 2017, the airline was offered to privatization.

16. The first phase of the privatization process of CVA is concluded,Loftleider Cabo Verde (a company owned 70% by Loftleidir Icelandic and 30% by investors) acquired 51 percent of CVA equity. As per Law Nº 47/IV/92 of July 6, 10% of the shares will be offered to the airline´s employees and the diaspora. The Government will also proceed with the sale of the remaining 39 percent of the company in 2019.

17. In parallel, the retrenchment plan of CVA is being implemented and the ongoing debt restructuring process - a renegotiation process with the main creditors of the company - is concluded. In the context of the reform to CVA, the financial support to the entity from the Government budget will fully cease by this year – this support amounted to 2.5 percent of GDP in 2017. By selling 51% of the shares to a strategic partner the State as already reduced its operational and financial risk. The sale of the remaining 49% in 2019 will bring the State exposure to none.

18. The Government as concluded its plans to divest from the inter-island maritime transport sector to improve service delivery and promote private sector investment and growth. The transaction was concluded in January 2019 and the concession contract was signed in February with the company Transisular. SA & Transisular Lda. After a several negotiations between the Government, the company Transisular and the National Ship-owners, the parties have reached an agreement to increase from 25% to 49% the capital share reserved to the National Ship-owners in the new concessionaire company. Nine National Ship-owners have signed with the company Transisular the new concessionaire company subscription agreement. Between April and June the new concessionaire company will initiate the implementation of the new routes. From August to December, the new concessionaire company will bring a new vessel to Cabo Verde, as determined by the concession contract.

19. The Government has also moved swiftly to minimize fiscal risks associated with the construction, management and sale of social housing by the SOE Imobiliária, Fundiária e Habitat (IFH), under the Casa para Todos (CPT) program. We inherited a program whose financial

viability was not established and led to increasing demands on the Government budget. The Government took the decision to restructure the program to spin-off the social housing component of the program (Class A) to the municipalities, and market houses of classes B and C to the public. The municipalities will now be responsible for the management of Class A houses. The transfer process has already been finalized, and the municipalities are receiving all the necessary support to ensure that the program continues to be managed with discipline and that the transition occurs smoothly. In parallel, the new commercial plan for classes B and C houses has already shown positive results. As a result, IFH will be better positioned to comply with its medium-term financial obligations with the Portuguese Government (which is the originator of the credit line for the program Casa para Todos financed through the Caixa Geral de Dépositos Bank). In relation to these obligations, the Government also instructed IFH to open a separate dedicated bank account for collecting the proceeds of the sale of those units remaining with IFH (classes B and C) for enhanced transparency. Furthermore, to generate more proceeds from the sale of Class B and C houses, the Government will remove the current ceiling imposed on the sale prices.

20. As a Government, we have also taken the decision to address fiscal risks and service delivery issues in the energy sector, introducing reforms to improve the governance and weak financial position of the utility. The energy company (ELECTRA) has recently signed a performance-based management contract with clear targets, results indicators and incentives which will be reviewed annually. The salary of the management team is now linked to the achievement of these targets. UASE will monitor compliance. To reduce the cost of electricity, we are pursuing a three-pronged strategy involving (1) the implementation of a commercial loss-reduction plan, (2) technical loss reduction through grid rehabilitation investments, and (3) a switch from diesel-based power plants to heavy fuel oil-based generators. It is the commitment of this Government to lower commercial losses below 20 percent by 2020. In parallel, the tariff structure will be reviewed to ensure both affordability and financial sustainability. Moreover, the State will divest from ELECTRA. A study by an internationally renewed firm was carried out to prepare for the privatization and recommended that a management contract be signed. Now that this intermediary step has been completed, the Government is accelerating the pace for the divestiture as unsolicited expression of interest from potential buyers have been received. To that end, a valuation of ELECTRA has been completed. The task force team that is implementing the privatization process, is finalizing the process of hiring a Transaction Advisor that will help to implement the process of divestment. The process is expected to be concluded until the end of 2019.

21. The Government will continue to adopt institutional reforms and policy measures to stimulate private investment, both domestic and foreign. This strategy includes: (i) enhanced synergies between private and public investment; and (ii) export facilitation and investment promotion. This strategy will be complemented by the development of a suitable policy, legal and institutional framework for the implementation of privatization operations and PPPs approved by the Government. The Government is currently moving forward on this agenda by assessing the PPP pipeline, so that sound PPP transactions can be carried out to bring private investment and management in several sectors. Regarding investment promotion, the former investment promotion agency was transformed into an agency to foster both trade and investment, known as Cabo Verde Trade Invest (CVTI). Furthermore, CVTI has developed an investor's after care system, which will allow to provide additional hands on support to investors after the investment is made. In fact, the day to day operations of CVTI now emphasizes providing support to investors through the after care.

22. Finally, the Government is currently working with development partners on improving the investment climate, facilitating access to finance for MSME firms, and increasing the productivity and the competitiveness of the economy. In that sense, two important projects, Access to Finance for the MSME and the SOE's Reform project were approved by the WB and their implementation are key for the reform agenda of the Government.

Strengthen efficiency, accountability and transparency in fiscal management

23. The main feature of our policy regarding the public administration is the realization of a two-prong paradigm shift which entails (i) establishing a public administration underpinned by a culture of excellence and (ii) transforming the public administration into a set of agencies which support enterprises and tax payers in their day-to-day activity. In parallel, we are committed to enhancing the legal and institutional frameworks governing public financial and debt management for enhanced efficiency, accountability and transparency in the use of scarce resources.

24. Following the Public Expenditure and Financial Accountability (PEFA) exercise that was concluded in 2016, the Government has elaborated its new public reform agenda that will continue to be implemented in the next few years. Making public management (including, planning, budgeting, debt management, and tax administration) more effective are the priorities. On the legislative front, a new Organic Budget Law and a new Debt Law were recently approved by the Council of Ministers. The Debt Law was also approved by Parliament. A Court of Auditors Law was also approved by the Parliament last year, reinforcing transparency in the access to public accounts and information on budget execution.

25. In addition, the Government has made considerable progress to meet the global tax transparency standards and joined the Global Forum on Tax Transparency in July 2018. This highlights the country's commitment to increase tax transparency and ensure exchange of tax information with our counterparts. This administration is also exploring options to enhance the efficiency of tax expenditures, including plans to adopt a tax model for tax exemptions and revoke and/or eliminate unjustified tax incentives and exemptions. The authorities will be able to more systematically review tax expenditures and plan to streamline the regime starting with the 2020 budget law.

26. Finally, we are undertaking measures to increase efficiency of public investment by reinforcing our current public investment management system (PIMS). As we are committed to enforce the 2014 Planning Law and 2018 budget decree law, we have recently started implementing new PIM tools for improved selection and execution of public investment projects. All new projects must now be incorporated in the PIMS and must be selected according to more rigorous criteria, starting with the 2019 budget. This will help us to monitor the size and quality of our public investment budget by (i) linking more systematically sectoral projects to national investment priorities; (ii) assessing project financial costs; and (iii) ensuring that projects comply with technical standards. The new PIMS will significantly support our efforts to sustain fiscal and debt sustainability.

27. We have worked over the past two years to lay the ground to firmly advance towards a balance budget over the medium-term. Consistent with the new pieces of the legislation described above, the Government intends to issue in 2019 a revised MTFF for 2019-2021 reflecting fiscal and public debt medium-term targets that are consistent with sustained fiscal

consolidation and declining public debt/GDP ratios. We are committed to reduce the overall fiscal deficit by the next years, below the 3% of GDP.

Disaster and Climate Risk Management Reforms

28. Geological and climate-related disasters pose major challenges for sustainability of growth and resilient development of Cabo Verde. As a Small Island Developing State (SIDS) the country is highly exposed to the potential negative impacts of climate change. Recognizing this, the government is adopting the National Disaster Risk Reduction Strategy 2017-2030 (Estratégia Nacional de Redução de Riscos de Desastres - ENRRD), in order to effectively manage and reduce disaster and climate-related risks. Up until now, the Government has mainly focused its efforts on emergency preparedness and response. Recent adverse natural events have prompted the Government to have a more proactive and transversal approach to mainstream disaster and climate-related risk management considerations in development planning. With this objective, the National Civil Protection Agency and Firefighters (Serviço Nacional de Proteção Civil e Bombeiros — SNPCB) led the Government efforts of developing the ENRRD in consultation with a wide range of stakeholders and sectors. The overall objective is to establish an effective framework for managing disaster and climate-related risks, minimizing losses associated with natural catastrophes and avoiding the creation of new risks.

29. In the ENRRD, the Government proposes to create a National System for Disaster Risk Management (SINAGERD) to establish effective institutional arrangements, planning tools, information systems and coordination mechanisms with well-defined roles, responsibilities and capabilities and supported by appropriate financing mechanisms and instruments. Under the SINAGERD, the National Council for Disaster Risk Management composed of sectoral and line ministries and agencies that will be established to coordinate the integration of DRM into sectoral programs across the ministries and promote inter-sectoral coordination and policy oversight. A Special Office for Disaster Risk Management will be created within the Ministry of Internal Administration (MAI) to coordinate the implementation of the strategy and serve as Secretariat to the Council. This will be complemented by the re-launch of the multi-stakeholder National Platform for Disaster Risk Reduction, which will involve the Government, private sector, civil society and development partners.

30. The ENRRD includes a comprehensive set of reforms to reduce disaster risk. To ensure capacity for implementation and sustainability of the reforms, the ENRRD proposes several financial mechanisms such as including a line for DRR in the annual budget or integrating the reforms under the sectoral programs of the PEDS—for which financing is secured annually in the budget. The new strategy will encourage more effective disaster risk management, at the national and sub-national levels, as well as, across sectors. The number of sectors and municipalities incorporating DRR into their strategic development plans will be tracked and used as an indicator of progress in the implementation of this agenda. In addition, to measure the impact of these reforms at the local level, the number of municipal development plans incorporating disaster and climate-related risk management considerations including specific actions will be tracked.

31. We are mainstreaming DRR in priority sectors. The Ministry of Education is working with technical assistance from the WB to incorporate disaster and climate resilience considerations in the 2016 National Plan for the Rehabilitation of School Infrastructure. The main objective of the Plan is to rehabilitate, strengthen and expand school infrastructure in the country by 2021integrating climate and disaster risk considerations.

32. The country's dense road network is vulnerable to a range of disaster risks including volcanic eruptions, flash floods and landslides, and there is a significant emergency works backlog caused by such events. In line with an ongoing World Bank Transport project, the Government is rehabilitating and upgrading of the transport network, including strengthening the maintenance, rehabilitation and emergency repair of the road networks, due to disasters and climate change. A road maintenance fund has been established to manage road assets in the country and the government wishes to strengthen this further to address disaster risk management considerations. Construction standards and guidelines are also being reviewed to improve integrate disaster resilience considerations into the overall management of public school infrastructure.

33. This Government is advancing reforms to territorial planning, coastal management and open data. We inherited a fragmented land management system where existing land-use instruments do not appropriately integrate and enforce disaster and climate-related risk considerations. The Maritime and Ports Authority (Agência Marítima e Portuária - AMP) has authority 80 meters inland from high water, while the National Institute for Territorial Planning (Instituto Nacional de Gestão do Território — INGT) is responsible for territorial planning, urban development and land use policies in the rest of the territory. For simplification, we have decided to transfer the territorial planning mandate of all lands (including coastal land) to INGT and establishing a new legal framework for territorial planning in the country.

34. The Government has implemented a set of policy reforms that will strengthen urban and land-use planning by streamlining and systematizing regulations. Part of this reform will ensure that disaster and climate-related risk considerations will be incorporated into updated territorial and urban planning instruments at the national and sub-national levels. The National Directive for Territorial Planning (Directiva Nacional de Ordenamento do Território — DNOT) will be reformed, including directives and guidelines for managing disaster risk for territorial planning at the national level. The Regional Scheme for Territorial Planning (Esquema Regional de Ordenamento do Território — EROT), the Municipal Master Plan (Plano Diretor Municipal — PDM), and the Detailed Plan (Plano Detalhado — PD), which govern territorial planning, will also be reformed, to include local disaster risk assessments to inform the territorial planning process.

35. Integrating DRM considerations in the territorial planning instruments will require reliable and detailed sociodemographic and disaster risk information, which builds on (i) the National Institute of Statistics (Instituto Nacional de Estatística — INE) efforts to strengthen the framework to update of Open Data standards, protocols and procedures. Main modifications to the legislation are (i) giving the SEN the capacity to disclose anonymized data—private data without personally identifiable information—at the statistical unit level upon request; (ii) including among the SEN's objectives to collect the statistical information available across different public institutions; (iii) including the National Data Protection Commission in the National Statistical Council (governing body of the SEN); and (iv) allowing the Government to create a National Fund for Statistical Development (Fundo Nacional para Desenvolvimento de Estatística) as a special financing source for the SEN to ensure the production of high-quality official statistics. Enforcing Open Data standards will directly contribute to (i) the understanding of risk, through better identification of Cabo Verdean communities highly vulnerable to a natural catastrophe; (ii) informing the design and targeting of DRM and CCA interventions; and (iii) the monitoring and evaluation of the impact of these policies on the population.

36. We are striving to reduce the fiscal impact of disaster and climate-related risks. In order to manage operational and fiscal risks—including those from disasters—in a pro-active and

comprehensive manner, the MoF has established a Risk Management Service in the Treasury Department of the MoF. The mandate of this new service is to identify and manage all risks that could negatively affect MoF systems and operations, as well as any risks that could negatively affect fiscal outcomes, including those related to potential disaster and climate-related risks. In relation contingent liabilities related to disaster and climate-related risks more specifically, the mandate of the unit will be to (i) quantify the socioeconomic and financial impacts of disasters, in particular through the impact of disaster on public and private assets; (ii) develop a sovereign disaster risk financing strategy to manage disaster and climate-related contingent liabilities; and (iii) oversee the implementation of the strategy.

37. In this line, the Government has decided to establish a new contingency fund for disaster and emergency response. This newly established fund will be financed through an annual budget allocation, ensuring predictability of inflows. The by-laws creating the fund, establish the rules for determining annual budget allocations to the emergency fund; rules for prioritizing funding sources to finance disaster response, including contingent credit—and thus the Cat DDO; potential beneficiaries of the fund; rules for accessing fund resources; rules for reporting on, and accounting for executed fund resources; and auditing requirements. The new disaster contingency fund, in combination with the Cat DDO, represents a significant step toward strengthening Cabo Verde's fiscal resilience against disasters and climate-related events.

Conclusion

38. In light of the above, Ms. President, the World Bank Group's Fiscal Management and Growth DPF and CAT DDO operation are important in consolidating the gains of our previous reforms. They also support sustained economic growth by improving the impact of our current agenda of structural reforms, by reinforcing the competitiveness of our economy and the efficacy of investments, and by supporting the promotion of private sector development.

39. Therefore, on behalf of the Government of Cabo Verde, I hereby request a DPF operation in the amount of US$40 million and a Cat DDO operation in the amount of US$10 million (US$5 million equivalent IDA and US$5 million IBRD) for this calendar year. The operations will support the implementation of the PEDS 2017/2021, particularly the program of reforms included in the Government's Program for the medium term. The Cat DDO will also provide immediate liquidity to the Government in the event of a natural catastrophe.

40. I would like to reiterate our commitment to further strengthening the cooperation between the World Bank Group and the Government of Cabo Verde and we look forward to your continuous support to the Cabo Verde's development process.

Please accept, Ms. President, the assurance of my highest consideration.

Ministério das Finanças
Gabinete do Ministro

Olavo Correia
Deputy Prime Minister and Minister of Finance

Cc: Mr. Jean-Claude Tchatchouang, Executive Director for Cabo Verde – World Bank

Mr. Gilberto Barros, Secretary of State of Finance – Ministry of Finance of Cabo Verde
Ms. Carla Cruz, National Director of Planning – Ministry of Finance

ANNEX 3: IMF RELATIONS ANNEX

Cabo Verde—Assessment Letter for the World Bank
April 24, 2019

The assessment of economic and financial developments as well as medium-term outlook presented below are based on the outcome of the March 2019 IMF mission to Cabo Verde. The authorities have requested a new program under the Policy Coordination Instrument (PCI) and discussions initiated in Praia continued during the Spring Meetings. The Executive Board meeting is tentatively scheduled for late June.

1. **Economic and financial developments are positive**. Real GDP growth is estimated at 5.5 percent for 2018 (4 percent in 2017) driven by strong activity in the industry and tourism sectors as well as private investment. Inflation rose to 1 percent (y/y) at end-December 2018 (0.3 percent at end-2017) due to higher food and energy prices. The current account deficit narrowed to 4.5 percent of GDP in 2018 (from 6.6 percent of GDP in 2017), mostly reflecting strong performance in tourism and fishery sectors, higher remittances, and a deceleration in import demand. Gross international reserves rose to €531 million, equivalent to 5.1 months of prospective imports. In the financial sector, stability indicators improved, and banks' profitability increased though asset quality continues to be weak. Despite improving compared to 2017 ratios, non-performing loans remain elevated, standing at 12.2 percent of total loans at end-December 2018.

2. **The overall fiscal deficit narrowed in 2018, while support from the budget to State-Owned Enterprises (SOEs) increased**. Tax and nontax revenue rose from 24.9 percent of GDP in 2017 to 26.7 percent of GDP in 2018. However, total revenue declined slightly to 28.1 percent of GDP (28.6 percent of GDP in 2017), reflecting a drop in budget grants. Revenue collection benefitted from tax administration reforms and improved collection of tax arrears. Expenditure stood at 30.9 percent of GDP (31.5 percent of GDP in 2017), mostly reflecting a decline in capital outlays. As a result, the overall budget deficit narrowed to 2.8 percent of GDP (3 percent of GDP in 2017). Support from the budget to financially-strained SOEs rose to 2 percent of GDP (0.7 percent of GDP in 2017), mostly related to the national airline company (TACV). Staff projections as well as the authorities' revised data for 2019 indicate that the overall budget deficit would decline to 2.2 percent of GDP (3 percent of GDP in the budget) consistent with the expected continued strong revenue performance supported by an efficient implementation of measures introduced in the budget including: airport security and maritime fees, special consumption excise tax, registration fees, increase in the corporate income tax rate for off-shore banks from 2.5 percent to 10 percent, sale of land, and enhanced collection of tax arrears. The projected narrowing of the budget deficit reflects also the scaling back of spending in goods and services, and of capital outlays.

3. **Budgetary support to SOEs is expected to remain elevated in 2019 before sharply declining in 2020**. Following the restructuring of the social housing program managed by the real estate company (IFH) in 2018 and the privatization of the airline company (TACV) in early March 2019, the authorities plan to divest the remaining 49 percent of the State's shares in the new airline company by end-2019, and to privatize

five additional SOEs, including the power company (ELECTRA) in 2019-20. Part of the privatization receipts will be used to clear TACV liabilities (about 1.5 percent of GDP). Until the second wave of privatization is completed, the authorities will be covering TACV's debt obligations, based on debt negotiations currently carried out by a new entity set up for this purpose (Newco). On this basis, Staff's projections assume that financial support from the budget to SOEs will amount to 1.9 percent of GDP in 2019, and 0.5 percent of GDP in 2020 and 2021.

4. **The risk of debt distress is assessed as high**. Although in decline since 2016, public debt remains high, totaling 123.9 percent of GDP at end-December 2018. Based on the end-December 2018 data, results from the debt sustainability analysis (DSA) carried out jointly by IMF and World Bank staff make the same assessment as the 2018 joint IMF/World Bank DSA, that Cabo Verde's risk of debt distress is high. However, the medium-to-long term outlook has improved compared with the macroeconomic framework underlying the 2018 DSA, mainly on account of higher growth, and lower fiscal and current account deficits.

5. **The monetary policy stance has been appropriate and consistent with the objective of protecting the peg and price stability**. The central bank (BCV) maintained an accommodative monetary policy in 2018 because the level of reserves **has been** adequate, and inflation low. Nonetheless, the BCV should continue to monitor economic conditions, particularly in the Euro area, and stand ready to change the monetary policy stance if it becomes necessary. The BCV will also need to take further actions to strengthen the monetary policy transmission mechanism. The external stability assessment suggests that in 2018, Cabo Verde's external position was weaker than implied by medium-term fundamentals and desirable policy settings. Regarding gross international reserves, results from the Fund's LIC/MIC framework suggests that the optimal level of reserves for Cabo Verde is about 3.6 months of prospective imports of goods and services. However, as noted in the 2018 assessment, fragilities arising from the economy's small size, lack of export diversification, and vulnerability to exogenous shocks call for a higher level of reserves than implied by the LIC/MIC framework.

6. **The medium-term outlook is encouraging**. Under the current macroeconomic framework, further improvements in the fiscal position are needed to consolidate gains made in recent years, improve debt sustainability, increase fiscal space for capital expenditure, and build fiscal buffers. This will require sustained implementation of reforms to broaden the tax base, increase efficiency in tax administration, improve tax compliance, strengthen capital expenditure management, and maintain a tight control on current expenditure. Such a fiscal adjustment, combined with effective implementation of structural reforms to improve the business environment and restructure SOEs would help boost investor confidence, enhance medium-term growth prospects, and put public debt on a sustained downward path. Staff's projections indicate that under these assumptions, a 5 percent real GDP growth can be sustained over the medium term, with inflation remaining below 2 percent. In the external sector, the current account deficit would narrow, and gross international reserves would reach 5.5 months of prospective imports.

7. **Risks to the outlook**. The medium-term outlook is subject to risks, with the balance tilted to the downside because Cabo Verde is highly vulnerable to adverse exogenous shocks. Key risks include worse than expected external conditions, particularly a slowdown in the Euro area, and a sharp tightening of global financial conditions that could impact growth prospects, and the external position. Domestically, downside risks are related to Cabo Verde' high vulnerability to weather-related shocks, flickering fiscal consolidation efforts, and delays in structural reforms implementation. Stronger performance in tourism as well as increased FDI-driven investment in relation with the implementation of the authorities' Strategy for Sustainable Development (PEDS) are the main upside risks.

8. **Engagement with the IMF**. The staff team that visited Praia during March 11-25, 2019 completed the mission work for the 2019 Article IV Consultation with Cabo Verde and in response to the authorities' request, initiated discussions on a PCI-supported program. A second round of discussions for the PCI took take place in Washington during the Spring Meetings. The Board meeting is tentatively scheduled for late June.

ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior Actions	Significant Positive or Negative Environment Effects (Yes/No/To be determined)	Significant Poverty, Social, or Distributional Effects Positive or Negative (Yes/No/To be determined)
Operation Pillar A: Strengthening the institutional and legal framework to ensure risk-informed sectoral and territorial planning		
Prior Action 1: The Government has adopted the National Disaster Risk Reduction Strategy.	No	Yes, Positive
Prior Action 2: The Government has amended the Territorial Planning Legal Framework to incorporate the use of disaster and climate-related risk information in the development of territorial planning instruments.	Yes, positive	No significant effects
Prior Action 3: The Government has reformed the National Statistical System which incorporates open data standards, protocols and procedures.	No	Yes, Positive
Operation Pillar B: Increasing the financial capacity to manage impacts associated with disaster and climate-related shocks		
Prior Action 4: The Government has created a Risk Management Unit in the Treasury Department of the Ministry of Finance.	No	No
Prior Action 5: The Government has created the National Emergency Fund to finance emergency response and recovery in the case of a disaster or climate-related shock.	No	Yes, Positive