Republic of Angola

Selected Policy Notes for Incoming Administration of Angola

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Executive Summary

Introduction

The Angolan economy is at a juncture. The current growth model based on oil wealth is nearly exhausted, and has not delivered inclusive growth and shared prosperity. The challenge for the administration is to restore macroeconomic stability and lay the foundations for a new, more inclusive growth model that can support a young and growing population. The new administration of President João Lourenço has taken important steps towards restoring macro-stabilty and the new medium-term National Development Plan is expected to outline a road map for a more diversified and inclusive growth model.

The objective of these Angola Policy Notes, written from the perspective of the World Bank Group, are to support the government in its reform agenda. The 15 concise policy notes range from consideration of short-term macro stability to policies in support of economic diversification and long-term inclusive growth. The policy notes reflect the World Bank's past and current engagement in Angola in several sectors, and provide a short diagnostic of the current situation and present policy options for reforms. Recommendations are assessed according to technical fesability and expected impact for the short to medium-term. Table 1 provides an overview of the different policy notes and their link to objectives in the government program, which will inform the new National Development Plan (Box 1).

Angola faces two broad policy challenges that need to be addressed urgently: The growing internal and external imbalances following the adjustment to lower oil prices pose an immediate challenge of **macro-stabilization**. Prospects of persistently low oil prices and potentially diminishing oil reserves over the longer-term call for a **new sustainable and inclusive growth model** that promotes economic diversification.

The first priority is to restore macroeconomic stability. Angola's macroeconomic framework is currently on a non-sustainable path, with widespread imbalances. The sharp and prolonged decline in oil prices since mid-2014 has reduced oil revenues, and caused GDP growth to decelerate. The current account deficit stood at 10 percent of GDP in 2015, large fiscal deficits have been recorded since 2014, public debt has doubled over the last three years. There is also an urgent need to safeguard financial system stability, as the undercapitalization of systemically important banks, the loss of direct U.S. dollar correspondent banking relationship, and non-performing loans are stressing the banking sector. Inflation escalated in 2016, reaching a peak of 42 percent in December 2016, before retrenching to 25.1 percent in January 2018. While the government's policy response from mid-2016 onwards has been able to contain a downward spiral in the short-term, sustained economic adjustment will be needed to restore the macroeconomic balance and to lay the foundation for a sustainable, long-term macro framework. The policy documents of the new Administration (*Plano Intercalar, Plano de Estabilização Macroeconómica e Proposta do OGE 2018*) are a clear step in the right direction.

Restoring macroeconomic balance is essential to providing a foundation for long-term sustainable growth. Current macroeconomic conditions and associated uncertainties are hampering economic activity. FX controls were introduced to stabilize the currency but have also restricted the import of inputs, led to misallocation of resources, the widening of the parallel market spread, and have restrained new investments due to the uncertainty if profits could be remitted abroad. High inflation is increasing the costs of doing business, poverty is also going up. High public debt is increasing interest rates, crowding out private investment, restricting monetary policy options and posing increasing macrofinancial risks as more government debt is placed in the domestic financial sector. Lastly, limited exchange rate flexibility prevents the exchange rate from playing a role as a shock absorber and hinders external competitiveness, as negative real interest rates discourage private savings. The government has recently started to dismantle the above picture.

The second priority calls for a new and more inclusive economic growth model to achieve sustained growth and to further improvements in human development and poverty outcomes. Up to now, Angola has relied on the oil industry and high oil prices to drive economic growth and to rebuild a large part of its infrastructure. Inequality remains high, with a Gini coefficient of 0.43 in 2016. In the 2015, Angola ranked 150 (out of 188) in terms of Human Development Indicators[1]. In 2016, about 30 percent of the Angolan population remained below the international poverty line (and 55 percent if $3.1/day is considered). The high capital and skill intensity of the oil industry partly explains why a large share of the population was not able to benefit from the oil boom, with developmental benefits from oil wealth being limited and Angola remaining a highly unequal society. The poor development outcomes of the current oil-driven growth model in terms of poverty reduction and shared prosperity make a more inclusive growth model essential. Furthermore, changing global demand and new players, including the US shale and gas industries, are rebalancing the global oil sector, and lower oil prices are therefore likely to persist into the foreseeable future. Even if oil prices were to recover over the medium-term, oil reserves will likely be exhausted by 2032 with current oil production levels.

Sustainable inclusive growth and economic diversification require strong institutions... The Mo Ibrahim index of African governance ranks Angola at the lower end in the overall governance indicator in 2016 (39.4 out of 100), with a declining trend in the last five years, and well below the African average (50.8). Despite recent reforms to the business environment, including the Simplified Companies Incorporation Process Law, the Private Investment Law, and the new General Labor Law, Angola continues to score at the low end on most competitiveness and investment climate indicators. For example, Angola ranked 175 (out of 190 countries) in the World Bank Doing Business report for 2018. Among the most problematic factors for doing business are inefficient government bureaucracy and corruption. The burden of government regulation is also a constraining factor, with limited management capacity.

…and a more conducive environment for greater private sector participation. A state-led development mindset is widespread and partly results from the economy's reconstruction needs and the heritage of a centrally-planned economy until 1991. Although there is continued popular support for a strong state footprint, a real private sector able to cope with high youth unemployment is unlikely to develop without more market-oriented policies, such as elimination of *de jure* and *de facto* barriers to entry in most markets. Economic management in Angola has favored large-scale planned projects and state-owned enterprises remain present in key sectors of the economy. For example, *Sonangol*, the national oil company, has activities in diverse sectors of the economy such as airlines, real estate, insurance and the banking system. The development of a private corporate sector is also constrained by challenging relations with domestic banks that mainly lend to households and to private firms that are indirectly linked to the government sector.

The new Administration is well aware of these challenges and has started to carry-out much needed adjustment. The current reform agenda is embodied in three policy documents released since the new Administration took office: The first one was the *Plano Intercalar* in October - a six-month interim plan, followed by the the macro stabilization program (*Programa de Estabilizacão Macroeconómica PEM*) for 2018, and the 2018 budget proposal. The policy documents are aligned; the overall objective is to achieve macroeconomic stability, to create an environment conducive to economic growth and job creation, and to address the most pressing social problems – while giving special focus to the development of the non-oil economy. In particular, short-term economic policies are aimed at addressing the imbalances in the

[1] 2016 Human Development Reports (HDR) Report.

foreign exchange (FX) market and in the current account. They are also intended to promote fiscal consolidation, ensure debt sustainability and rein in inflation. These policies are already being implemented as can be seen by the recent exchange rate devaluation and figures from the proposed budget.

Table 1: Overview of Policy Notes and Link to Objectives in MPLA Government Program

	Peace, Democracy, Civil Society	Macro-economic stability and Economic diversify-cation	Competitiveness and private-sector led growth	Good Governance	Human Development and Social Welfare	Human Capital and Skills	Public Safety and Security	Regional Development and Decentralization	Internationalization
Exchange rate and Monetary Policy									
Fiscal Policy and Fiscal Consolidation									
Public Financial and Investment Management									
Financial Sector Stability									
Natural Resource Management									
SOE Corporate Governance									
Business Environment									
Towards More and Better Jobs									
Access to Finance and Financial Inclusion									
Infrastructure									
ICT									
Agriculture									
Education									
Health									
Social Protection									

Box 1: MPLA Government Program 2017-2022 and National Development Plan (2018-2025)

The MPLA (Popular Movement for the Liberation of Angola) Government Program 2017-2022 was presented on May 10th, 2017 as part of the general elections of August 23. The document summarizes the actions advocated by the party over the next five years, referring to the 2017 election campaign: "Improving what is right, correcting what is wrong". In short, the government plan outlines strategic policies to consolidate peace, strengthen democracy, citizenship and civil society. It promotes sustainable and diversified human development and aims to reduce inequalities. The plan also emphasizes economic development and the reform of the State including good governance and the fight against corruption, to ensure regional development and to strengthen Angola's role in the international context. The program is structured along nine chapters, each with an overarching objective, with a total of 870 measures. The government program will inform the medium-term **National Development Plan (NDP) 2018-2025**. It will be crucial to set priorities in the NDP to balance different dimensions of sustainable development outlined in the government program and to find synergies; potential conflicts should be addressed, and trade-offs made as necessary. Furthermore, the NDP should be integrated into budget processes to generate the budget support required; and implementation should be decentralized to subnational levels with adequate resources and capacity for effective implementation.

The nine principal objectives of the MPLA Government program are:

- Consolidate peace, strengthen democracy, citizenship and civil society.
- Promote a sustainable and diversified development agenda, with economic and social inclusion to reduce inequalities
- Promote human development and well-being of Angolans, with economic and social inclusion.
- Guarantee state reform, good governance and fight corruption.
- Stimulate the transformation of the economy, the development of the private sector, economic productivity and competitiveness.
- Optimize human capital and promote skilled employment and remuneration
- Ensure national and citizen's defense and security.
- Ensure regional development, including decentralization.
- Strengthen Angola's role in the international context.

Towards a sustainable macro-economic framework as a foundation for long-term growth

The first set of policy notes focuses on five key topics for supporting a sustainable macroeconomic framework that goes beyond short-term macro stabilization: (i) a flexible exchange rate regime and a new monetary policy framework, (ii) fiscal consolidation, (iii) restructuring of state-owned enterprises, (iv) sustainability of public finances, focusing on oil wealth management, and (v) financial sector stability.

Exchange Rate Regime and Monetary Policy

Angola needs a more flexible exchange rate regime to foster economic diversification and to open the path for sustainable growth. The country exited the U.S. dollar fixed peg in January 2018, with an outright depreciation of about 33 percent vis-à-vis the Euro (about 22 percent relative to the U.S. dollar) in two weeks. The new exchange rate regime introduces some flexibility by allowing the currency to fluctuate within (unannounced) trading bands. The regime change has been appropriately supported by tightened monetary policy and an announced fiscal consolidation plan for 2018. Both set of measures will help contain the inflationary pressures from the currency depreciation.

The exit from the peg is a step in the right direction, but there is much uncertainty about the new exchange rate regime. It is unclear the extent to which the BNA will continue to determine the sectoral allocation of the proceeds of the foreign currency auctions. While the imposed two percent limit on the extent of variations in the exchange rate vis-à-vis its reference rate for bids within each auction can reduce the possibility of an overshooting of the exchange rate, it restricts the volatility in FX markets and brings significant uncertainty about the scope for exchange rate fluctuation. In fact, it is not clear if the new exchange regime will close the gap with the parallel rates, if FX shortages will diminish, or even if the distortions associated with the management of exchange rates will continue to hamper economic activity and constrain sustainable growth.

One policy option is to consider an intermediate step toward greater exchange rate flexibility. Given the possibility of high oil price volatility in the short to medium term, Angola may be well served by pegging to a basket that contains main trading partner currencies as well as the oil price. Such a system would provide flexibility to adjust to external shocks, while providing the credibility of a currency peg.

The changes in the exchange rate regime towards greater flexibility need to be part of a comprehensive policy strategy, requiring substantial capacity-building and policy coordination. Key complementary reforms should aim at: (i) establishing a coherent and transparent FX market intervention policy; (ii) assessing and monitoring FX risks, especially in the private sector; (iii) developing a well-functioning FX market; (iv) implementing an alternative nominal anchor by re-designing the monetary policy framework; and (v) coordinating monetary and fiscal policies and strengthen fiscal institutions.

Fiscal Policy and Fiscal Consolidation

Lower oil prices have reduced government revenue contributing to fiscal imbalances and a rising debt burden. Fiscal consolidation in 2015 and 2016 led to a cut in overall budget deficit by 30 percent, or 2.1 percentage points of GDP - mainly investment spending and goods and services - to manage short-term revenue shock. Aggressive expenditure cuts on public investment and goods and services are not sustainable and can have negative welfare impacts over time. Gradual, but consistent fiscal consolidation is needed to adjust expenditures to the lower resource envelope, and to ensure debt sustainability by reducing financing needs.

With non-oil tax revenue well below peers, there is ample scope to scale-up. This will require reforms in tax policy and tax administration to broaden the tax base and strengthen taxpayer compliance. Angola is one of the 9 countries in Africa without a Value-Added Tax (VAT), and introducing a VAT can potentially add about 1.6 percent of GDP to revenue in net terms. and the introduction of a simplified tax regime for small taxpayers would help broaden the tax base and strengthen compliance of informal firms. On the expenditure side, the focus should be on expenditure rationalization and increasing expenditure efficiency, containing the public sector wage bill; phasing out subsidies; and greater efficiency of capital expenditure and goods and services would be crucial.

Public Financial and Investment Management

Public financial management (PFM) practices have improved in recent years, but significant weaknesses remain. While PFM practices have improved, there is still a lot of duplication of processes and existing systems are not used effectively, evidenced by the recurrent appereance and build-up of payment arrears. Poor PFM practices directly impact fiscal management and service delivery. Implementing the new public investment management system, adopting competitive methods for public procurement, and enhancing cash management and revenue forecasting practices would benefit overall PFM efficiency and reduce arrears build-up. The project preparation capacity of ministry staff should also be strengthened through a comprehensive capacity development program on investment project formulation and evaluation. Additionally, in alignment with the president's commitment to fight corruption and increase accountability, reforms are needed to provide legal autonomy to the Supreme Audit Institution (*Tribunal de Contas*) to conduct internal and external controls, strengthen the anticorruption framework and better protect whistleblowers.

Financial Sector Stability

Financial sector vulnerabilities have been on the rise and some banks are in need of recapitalization or restructuring. Credit concentration in public sector assets and the loss of direct U.S. dollar Correspondence Banking Relationships (CBRs) further compromise the stability of the financial system and its ability to support the broader economy. There is an urgent need to deal with high NPLs in the system which reached 28.5 percent as of November 2017 though these have been largely concentrated in state-owned banks, with one state-owned systemic bank in particular, Banco do Poupance e Credit BPC, accounting for the bulk of NPLs.

While significant efforts have been made to improve the regulatory and legal framework for bank supervision, adopted solutions have high fiscal costs, and require some reorientation. Operationalizing the **Bank Resolution Framework** to bolster crisis preparedness and to help resolve weaknesses in the banking system; adopting a risk-based supervision and applying a robust prompt correct action regimes are policy priorities. Options under a Bank resolution framework could include: bank closure and deposit payout; mergers & acquisitions; establishing a Bridge Bank; division into Good bank - Bad bank. To that end, the mandate of the recently established Bad Bank (Re-credit) should be re-evaluated to focus on resolving NPLs in BPC using market-based and transparent mechansims. Reforms to the corporate insolvency legal framework should also be accelerated to help deal with NPLs.

The ongoing **National Risk Assessment** should be concluded as soon as possible and should then provide the basis for identifying the underlying causes of the loss of direct U.S. dollar CBRs and to develop a risk-based Anti-Money Laundering/Combating the Financing of Terrorism (AML/ CFT) legal and regulatory framework. A more developed government bond market with higher trading volumes and liquidity would facilitate broader capital market development, and this should be supported by a Medium-Term Debt Strategy with domestic Annual Borrowing Plans as well as a more transparent and competitive auction system for government securities.

Towards a long-term fiscal framework for Natural Resource Wealth Management

The exhaustibility and volatility of oil revenue pose important challenges for economic management, including external shocks as a commodity-dependent economy, pro-cyclical fiscal policy and an uncertain future. In this regard, Angola faces simultaneous fiscal challenges to: (i) stabilize oil revenue flows in the short term and mitigate their pro-cyclical impact on fiscal policy, (ii) prepare for dwindling oil reserves, and a strong reduction of oil revenues over the next 15 to 20 years, and (iii) reduce foreign debt to levels that can be managed in a future without revenues from oil. These are closely related, yet separate, challenges.

Angola's Oil Price Differential Account (OPDA) has been set up specifically as an instrument for fiscal stabilization, but in its current form it falls short of its objective. OPDA rules need to be strengthened, and become part of a robust fiscal framework for natural resource management that reduces pro-cyclicality and reinforces fiscally responsible economic management for current and future generations. Angola's other two oil wealth funds (*Fundo Petrolifero* and *Fundo Soberano de Angola*) should also be made part of such a framework.

State Owned Enterprise (SOE) Corporate Governance

State-owned enterprises play an important role in Angola and their impact on the economy and budget is substantial. While the sector is profitable overall, this is largely driven by SONANGOL, Sub-Saharan Africa's largest SOE. Most other SOEs show significant losses despite continued state support in the form of price subsidies and direct transfers, which together account for about 0.8 percent of GDP in 2016 excluding implicit fuel price subsidies. Beyond risks to fiscal sustainability, a poorly performing SOE sector can lead to cost-ineffective operations, low service delivery and crowding-out of private investment.

To improve SOE sector performance and to ensure fiscal sustainability, it is recommended to prepare a SOE policy that clearly lays out the objectives for state ownership and targets for SOE (financial and non-financial) performance. This should be supported by an operational SOE reform plan that focuses on strengthening state ownership arrangements, performance monitoring, corporate governance and possibly ownership diversification. Adequate fiscal treatment of SOEs, by incorporating all explicit and implicit SOE subsidies in the government budget, would make the fiscal burden more predictable and manageable.

Towards Economic Diversification and Sustainable Growth

Sustainable inclusive growth requires economic diversification, especially in the face of depleting oil reserves. The current oil-dependent growth model is not sustainable due to depleting oil reserves. Sustainable growth and employment requires a diversified economy and a competitive private sector. Angola has a young population; the high-capital and skill-intensive oil industry cannot absorb its growing workforce. Economic diversification in non-oil sectors will broaden the base for government revenue, thus reducing the country's dependence on the oil sector and its exposure to the volatility of the global oil market.[2]

Sectoral policies to support economic diversification and sustainable growth should focus on: (i) an enabling business environment for private sector-led growth, (ii) enabling infrastructure (iii) the role of ICT as catalyst for inclusion, efficiency, and economic growth, (iv) better access to finance and financial inclusion, (v) agriculture as a key driver for food security and economic diversification beyond oil, (vi) education, (vi) health, and (vii) social protection:

Business Environment

A favorable business environment is critical for increasing private investment, economic diversification and job creation. While the Government has taken important steps in recent years to reform the regulatory and institutional framework, Angola still presents a challenging regulatory and institutional environment for businesses, as illustrated by its 175th ranking out of 190 countries in the Doing Business 2018 report. Private sector activity would further benefit from reduced red tape and a consistent application of regulations. Expanding the information on government procedures available online at *Portal do Cidadao*; implementing the legal framework for e-signatures; and streamlining procedures and introducing online platforms for business registration, filing and payment of taxes and property registration, are important steps in this regard.

Reforms in **trade facilitation** are critical to open opportunities to exports and to increase the competitiveness of domestic sectors, such as agriculture, that rely on imported inputs. Completing the implementation of ASYCUDA World at all border posts and streamlining import and export procedures would be an important measure to facilitate trade.

An **effective competition policy framework** is needed to ensure that government policies and programs are designed to encourage competition and minimize market distortions, a review of existing policies and

[2] The oil sector can also be a basis for vertical diversification. This is not being explored for in these policy notes, given our limited lack of understanding of the oil and gas sector in Angola. Ongoing analytical studies are intending to shed further light on this.

programs that target access to foreign exchange, tax and tariff exemptions, subsidized credit, public guarantees, risk capital and training are a priority in this regard.

While the investment policy and promotion framework from 2015 offers a more welcoming policy for **foreign investors**, important shortcomings remain, the government may wish to review requirements for mandatory joint ventures with local firms in key sectors, increase transparency in investment approval procedures, simplify visa restrictions, streamline the institutional framework for investment promotion, facilitation, and aftercare, and consider international arbitration for dispute resolution.

Towards More and Better Jobs

Angola has a high dependency ratio and a working-age population that is growing slowly. Angola is unlikely to experience a demographic dividend any time soon. Young people are increasingly more educated but productive employment opportunities are few. To create more and better jobs, Angola needs to improve the investment climate to encourage entry and growth of firms. An active jobs strategy would support an adaptable labor market that balances worker protection and flexibility. Policy focus and *Active Labor Market Programs* are required to increase job opportunities in the largest employment sectors of agriculture and services with a focus on youth, women and the informal sector.

Access to Finance and Financial Inclusion

Access to and cost of finance are critical binding constraints for economic development in Angola. An inclusive financial system that provides cost-effective access to financial services is therefore crucial for supporting economic and social development, particularly within the context of economic diversification beyond the oil economy. The Government should build on recent initiatives for micro, small and medium-sized enterprises (SMEs), such as the savings and financial education campaigns for those firms and households currently underserved or financing schemes for SMEs that focus on economic diversification, but should remain cognizant of the current challenges to financial stability in the financial sector (see above). Ongoing Government sponsored SME finance programs should be evaluated with a view to move to more sustainale and transparent criteria for supporting SME, with the ultimate goal being to crowd in private bank finance. Within this context, policy initiatives in support of financial inclusion should target reforms that broaden the credit information infrastructure, improve the insolvency regism , strengthen payment systems and promote retail payments (especially mobile payments), and improve consumer protection and financial literacy. Measures to promote the introduction of financial services such as leasing, factoring, warehouse receipts should also be pursued. The reform which can have the most immediate impact on inclusion would be to enable and promote retail payment and mobile financial services.

Infrastructure

Infrastructure is a critical enabling factor for economic diversification. The economy requires affordable and reliable energy; adequate access to water and sanitation; efficient transport and logistics systems to produce, move and commercialize goods and to deliver basic services. The institutional and regulatory framework needs to be established or improved: (i) to attract private financiers and operators, and to relieve the budget, (ii) to plan and build resilient, cost-effective infrastructure and enable trade facilitation for national and regional markets, and (iii) to provide access to basic services to support social development.

For the **transport sector**, improving domestic and international connectivity is key. There is a need to identify the primary and critical road network and associated maintenance standards to improve access to lagging regions. Addressing overloaded trucks; as well as establishing a sustainable financing mechanism for a Road Fund and a strategy to scale up performance-based contracts for maintenance are also crucial. The development of a regional transport corridor with DRC and Zambia would support regional trade.

Angola's long-term **energy** strategy, *Angola Energia 2025*, aims to double electricity infrastructure capacity and coverage by 2025. In this regard, the following measures are essential: strengthening the performance of existing energy utilities and ensuring their financial vialbility; defining a rural electrification strategy; and increasing private sector involvement in power generation.

The rapid expansion of **water supply** requires adequate sanitation system. Strengthening Provincial Water and Sanitation Utilities and ensuring their financial viablilty; a transparent tariff regulation scheme; and a national sanitation strategy to scale up access in urban and rural areas will be important to ensure adequate access to water and sanitation.

To attract private investment in infrastructure across sectors, existing legislation and procedures should be reviewed to to ensure that the PPP framework is fully operational. Establishing PPP units at Technical Ministries would help to develop a PPP pipeline.

Information and Communication Technology (ICT)

ICT has the potential to be a catalyst for inclusion, efficiency, and economic growth. A digital economy in Angola has potential to create jobs, generate economic output, increase export revenue, and support social inclusion. It can help drive the use of ICT across sectors, including in healthcare, education, financial services, and public financial management through operational reforms, digital leap-frogging, and innovation. The benefits of ICT-based development rely on good infrastructure, namely access to mobile phones, high-speed internet, and digital clouds. Although Angola's mobile sector has shown remarkable growth, availability of high-speed internet is limited. The government may prioritize a policy review of the ICT sector of Angola, with a lens of supporting a digital economy, improving the country's digital infrastructure, using ICT in government, promoting technology and innovation for Angola's development, and safeguarding people's digital information. Further work on a market assessment of the country's digital economy, and conducting a diagnosis of the country's preparedness for cybersecurity can provide additional inputs to the country's policymakers on ways to advance the ICT sector of the country.

Agriculture

Agriculture development is a key component for Angola's strategy to diversify the economy, to promote export competitiveness and to ensure food security, but the sector has underperformed in recent decades. Agriculture has been a priority in past national development plans as a means to economic diversification. To realize this potential, sector competitiveness needs to be improved. This requires a shift in agricultural policies and programs to improve the quality and supply of agriculture public goods and services and strengthen incentives for investments in agriculture and agribusinesses. As high tariffs on agricultural goods preventing the sector from joining regional or global value chains, there is also a need for agricultural trade policy reform. Streamlining procedures for obtaining and transacting land-use rights (concessions) would also bring more state-owned land into productive use.

Education

Notwithstanding the significant progress in increasing access to education, outcomes of the sector in Angola lack behind peers with similar levels of education spending. While net primary school attendance rates improved from 56 percent in 2005 to 78 percent in 2014, one in six school-aged children are not attending school. Less than 50 percent of the youth have access to secondary education, with particular challenges in rural areas and among girls. Currently, more than 60 percent of students in grade 3 are unable to read a single word in Portuguese due to poorly trained teachers and limited learning materials.

Repetition rates as high as 20 percent and low scores on learning assessments also point towards significant issues in the quality of education.

In order for Angola to achieve its goal of universal access to a quality based education, the Government needs to increase access to education, improve education quality and strengthen governance. To increase access to education – especially in rural areas and among girls – alternative forms of service delivery should be considered, including online programs and public private partnerships. Quality of education should be improved through greater investment in teacher training, while skills development programs should be expanded and tailored to the needs of the labor market. Strategic planning and budgeting processes should be streamlined across all stakeholders at the central, provincial and municipal level to ensure coordination and effective service delivery.

Health

Despite significant long-term achievements in improving health outcomes, Angola underperforms peers in a range of areas, including life expectancy, and maternal, infant and under five mortality rates. These results reflect systemic failures in the delivery and access to health care services and medicines in a complex and decentralized system. Quality-related issues, such as the scarce supply and inadequate distribution of trained health staff and low quality pharmaceutical products also undermine health care outcomes. All these challenges are magnified in the poor communities and rural areas of the country.

The Angolan health sector is underfinanced, underscoring the need to increase its efficiency and to strengthen its governance framework in order to maximize the health returns from the scarce resources available. Strengthening its primary care system is particularly critical, as it can deliver high-return programs such as maternal and child health, and disease prevention, which can yield the greatest short term impact on health outcomes, but also simultaneously help address the challenges imposed by non-communicable diseases, which are gaining importance in the country's epidemiological profile. Better management and more effective purchasing and delivery strategies and partnerships across the pharmaceutical sector can reduce expenditures and increase access and availability of medicines. Changes in the financing of healthcare facilities can increase efficiency and performance. In addition, the highly fragmented institutional arrangements should be streamlined to strengthen the overall governance framework.

Social Protection

Mitigating measures to protect the poor are largely absent. The Government needs to combine short-term and medium-term social protection and productive inclusion measures to protect the poorest from the effects of the recent crisis, prevent other vulnerable households to fall into poverty, and promote economic opportunities for the poor. An increased budget allocation for poverty-targeted social safety net programs with direct links to productive inclusion initiatives is called for. To achieve this, the Government needs to reduce the current agency and program fragmentation, shift regressive government funding for subsidies to pro-poor programs, and promote a stronger decentralization of social protection and productive inclusion programs to provide municipalities a leading role in program implementation.

Cross-cutting policy issues that are critical for a broad set of policy measures:

A sustainable macro-economic framework is essential for long-term sustainable growth. Current macroeconomic conditions and associated uncertainties are hampering economic activity. The private sector needs adequate access to foreign exchange to increase productivity and output, this is particularly important for agriculture, which relies heavily on imported inputs. Greater exchange rate flexibility allows the exchange rate to take on the role as shock absorber and a real exchange rate close to equilibrium enhances external competitiveness. Stabilizing inflation will lower the costs of doing business, while sustainable public debt dynamics will ensure space for private investment and limit macro-financial risks to the banking sector. Lower inflation and public debt levels will benefit private investment and domestic credit supply.

Fiscal space for progress on social outcomes. Relative to peers, Angola overspends on subsidies and underspends on agriculture, education, health and social protection. While there is significant room for increasing efficiency through better targeting and improved public investment management, social expenditures will also need to be increased for Angola to achieve its ambitious targets in universal primary education and social protection. Experience from fiscal consolidation during 2015 and 2016 shows that cutting expenditure across the board can run counter-productive to longer-term development. Fiscal consolidation should not only be mindful of longer-term development objectives, but also ensure that social protection policies are in place to mitigate the impact of macroeconomic adjustment on the population, in particular the poor.

Decentralization can help improve service delivery, but requires coordination. In the aftermath of the war, Angola embarked on a process of administrative decentralization of public services, including education and health services. Decentralization can help improve service delivery, but it presupposes coordination, policy alignment, and accountability. One lesson behind the low expenditure efficiency in education and health is that the "decentralization" of services lacks mechanisms to ensure effective coordination across the different levels involved in budget planning and execution. Parallel responsibilities and insufficient alignment between resource distribution at the central level and budgeting at the municipal level weakens planning and execution. Empty classrooms, teacher absenteeism, poor distribution of school materials, and under-used and under-staffed health facilities are the result of inefficient planning and use of resources.

Public sector management skills and capacity. Overall, the Angolan public sector is weak and inefficient, as evidenced by a range of indicators. Improving public sector management capacity is therefore critical for delivering on any public policy, from frontline service delivery to broader regulatory performance. There is a need to address public sector capacity constraints. In doing so, authorities need to consider the enabling environment to transform capacity investments into better policy design and implementation – as measured by functional improvements in service performance. A first step in this process is to encourage behavioral change to solidify the ethos of public service, including dealing with citizens, efficient management of public resource, and prevention of unethical and corrupt practices. Creating a higher performing bureaucracy will also require the authorities to link skills development programs with career paths of public sector professionals, thereby providing incentives for stronger performance.

Transparency and clear communication. Better communication and transparency is key to ensure policy effectiveness and safeguard investor confidence. Clear and predictable rules for business start-ups and operations are critical for increasing private investment, and supporting economic diversification and job creation. A transparent, clear, and consistent communication policy by, for example, the central bank is crucial to guide the expectations of market participants, while a transparent regulatory framework (e.g.for SOE board selection, OPDA operations, and FX and government security auctions) will re-assure investors.

Box 2: Policy priorities with cross-cutting implications:

- ✓ ***Continue to move towards greater exchange rate flexibility and develop a well-functioning foreign exchange market***
- ✓ ***Optimize public expenditures***
  - Increase spending for human development sector (health, education, social protection), based on absorptive capacity.
  - Increase public investment efficiency through stronger technical screening of investment proposals, and implementation, monitoring and control of approved projects.
  - Strengthen SOE performance through an annual analytical monitoring report on the portfolio; develop SOE sector policy with clear social or other objectives, principles for SOE performance, governance and transparency.
  - Eliminate explicit and implicit price subsidies.
  - Broaden the tax base by (i) increasing compliance (updated tax registry, increased tax audits, small taxpayer regime) and (ii) a gradual implementation of broad-based VAT.
- ✓ ***Strengthen fiscal institutions and governance***
  - Establish a long-term fiscal framework and strengthen PFM as needed.
  - Improve budget planning (revenue forecasting, link sector policy with multi-year budget planning process) and execution (strengthen commitment/ expenditure controls to avoid arrears).
- ✓ ***Strengthen public service delivery***
  - Reduce institutional fragmentation in social protection, health and education.
  - Use ITC for service delivery (e.g. for education, government procedures), and strengthen e-government (e.g. for tax administration, PFM).
  - Introduce performance-based service delivery options.
  - Increase transparency through better access to administrative data (including education, health, social protection, SOEs).
- ✓ ***Support the business environment***
  - Simplify government procedures (e.g. streamlining, online platforms).
  - Promote competition by adopting a clear competition policy framework and addressing potential market distortion in existing programs (e.g. for credit, SMEs or priority sectors).
  - Reform the investment policy and investment promotion framework.
  - Strengthen public-private sector dialogue by engaging the private sector in the identification of reform priorities and implementation monitoring (e.g. agriculture).
- ✓ ***Promote financial sector stability and access to finance***
  - Improve the bank resolution framework and enhance crisis preparedness.
  - Re-evaluate and re-design *Recredit*'s business model.
  - Strengthen and modernize the payments system and facilitate retail electronic payments.
- ✓ ***Establish an operational PPP framework to promote public-private partnerships in infrastructure and other sectors of the economy***

Exchange Rate and Monetary Policy Framework

The exchange rate and monetary policy framework have been on a non-sustainable path and have led to distortions in monetary policy and, external and internal competitiveness. The recent change in the exchange rate regime is a move in the right direction to restore macroeconomic stability. Nonetheless, the new regime seems to have retained a number of features from the old regime. Angola needs to continue moving towards greater exchange rate flexibility. A successful transition toward greater exchange rate flexibility requires a coordinated policy effort on several fronts as establishing a new policy and institutional framework requires substantial capacity-building.

Background

Angola's exchange rate and monetary policy framework has been on a non-sustainable path. The US dollar value of exports dropped by more than half since 2014 and external accounts moved from surplus to deficit in 2015 (10 percent of GDP). Reduced availability of foreign exchange (FX)[3] and the consequent pressures on the Kwanza were met with import restrictions and sizable FX controls, which in turn gave rise to a significant spread between the official and the parallel exchange market rate, reaching over 200 percent in 2016. To contain inflationary pressures, the Kwanza was re-pegged in April 2016 (at 166Kz/$), and monetary conditions were tightened: the BNA raised interest rates between 2015 and 2016 to a then multi-year high of 16 percent and increased banks' mandatory reserve requirements in local currency from 15 percent in 2014 to 30 percent as of January 2018. The new Administration further raised interest rates by 200 basis points in November 2017 to 18 percent. Despite the monetary tightening, inflation has remained high (at 26.3 percent in December 2017), real interest rates are still in negative territory, FX pressures have persisted (the parallel market spread stood at around 160 percent in December 2017), and the latest estimates (from late 2017) point to a real exchange rate overvaluation of about 20 percent. International reserves have continued to decline (to about US$14 billion in December 2017, an eight-year low) and the current account deficit is expected to widen to US$6 billion in 2017, down from a surplus of US$8 billion prior to the oil price shock in 2013.

Amid these significant imbalances, the BNA announced the adoption of a new exchange rate regime. The exchange rate misalignment and depleting foreign reserves prompted the Central Bank to abandon the peg to the U.S. dollar and ease currency controls on January 4, 2018. In the new system, the economy's benchmark exchange rate (against the Euro, instead of the U.S. dollar) is determined through (arguably competitive) auctions with commercial banks in a primary market, and is expected to remain fixed between auctions. The authorities refer to the new system as a floating regime with trading bands. They will define the minimum and maximum exchange-rate bands, though these will not be disclosed to the public. According the BNA statements, the currency market will be managed in a way that guarantees the sustainability of external accounts and stable prices.

The greater exchange rate flexibility is welcomed and has been appropriately supported by monetary and fiscal policies. The new exchange rate regime is a step in the right direction as it has introduced some exchange rate flexibility: it brought an outright depreciation within its first two FX auctions (on January 9 and 16, 2018) of about of about 33 percent vis-à-vis the Euro (or about 22 percent relative to the U.S. dollar); the currency is now allowed to fluctuate within (unannounced) trading bands. The move towards greater exchange rate flexibility is in fact part of the new Administration commitment to promote short-term macroeconomic stability. Ahead of the exchange rate regime change, in November 2017 the BNA

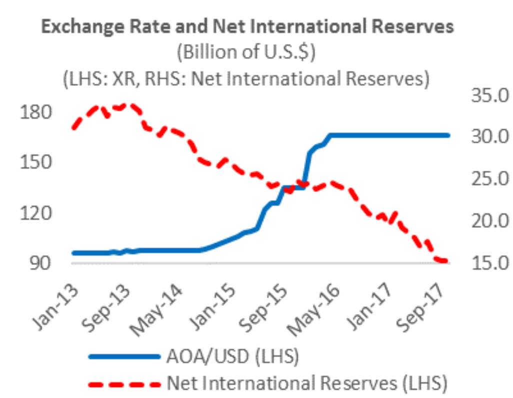
[3] The FX shortage due to the decline in the proceeds from oil exports was further exacerbated by the loss of correspondent banks, in which several overseas banks cut the supply of FX coming into the country at end- 2015. This resulted in a significant drop of FX being supplied to commercial banks in Angola. The amount of dollars sold by the BNA to the local banks fell about 66 percent, from a monthly average of US$1,457 million sold throughout 2015 to abut to about US$493 million in January 2016.

tightened monetary policy and formally adopted base money as their operational instrument to closely monitor economy-wide liquidity. The recently approved budget for 2018, targeting an overall fiscal deficit of 2.9 percent of GDP, indicates that the GoA is also pursuing tightened fiscal policies. Both set of measures indicate coordination in fiscal and monetary policies and will help contain inflationary pressures from the currency depreciation.

However, there is much uncertainty about the new exchange rate regime and some features of the old regime seem to persist. On January 19, following two cancelled auctions, in which bids were in fact submitted by commercial banks, the BNA imposed a 2 percent band on the extent of fluctuations in the exchange rate vis-à-vis its reference rate for bids within each auction. A limit of 2 percent over the reference rate was also imposed on the transactions of the commercial banks with its clients. These measures effectively limit the pace of the exchange rate depreciation in the short run, and, thereby can reduce the possibility of an overshooting of the exchange rate. However, they also restrict volatility in FX markets and bring significant uncertainty about the scope for exchange rate fluctuation . While the spread between the official and parallel exchange rates declined since the adoption of the new regime, it is still substantial at about 100 percent (by mid-February). It raises some uncertainties on whether the new exchange rate regime will close the gap with the parallel rates or even if FX shortages will diminish. Thus far, it seems that the BNA will continue to determine the sectoral allocation of the proceeds of the auctions as it announced that there will still be direct sales through commercial banks for certain transactions (food, medicine, and private operations). However, it is not clear how large these allocations are or at what rates they are conducted. A stamp tax on a wide range of foreign currency transactions also adds to potentially distortive allocative inefficiencies.

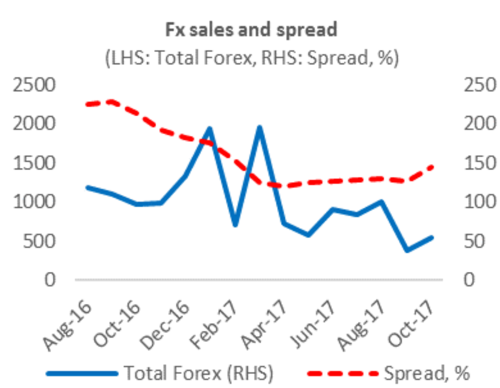
Many of the features of the new regime can still arguably have a significant detrimental impact on the real side of the economy. For instance, if FX shortages and the black market premium were to persist, they can lead to (i) inefficient FX allocations with profitable arbitrage opportunities for some; (ii) diminished efficacy of monetary policy as the role of the official exchange rate in price formation and inflation expectations is weakened; and (iii) loss of competitiveness and reduced prospects for export diversification (see Box 1 in the Annex and the case of Argentina). Such distortions can hamper economic activity in the short-run and constrain sustainable growth in the long term. High inflation increases the costs of doing business and adversely impacts the poor. Negative real interest rates discourage savings, especially by the private sector, and affect the markets for real assets that serve as a store of value. Angola has already been affected by these channels to some extent.

Figure 1: International reserves on a declining path during the pegged regime.



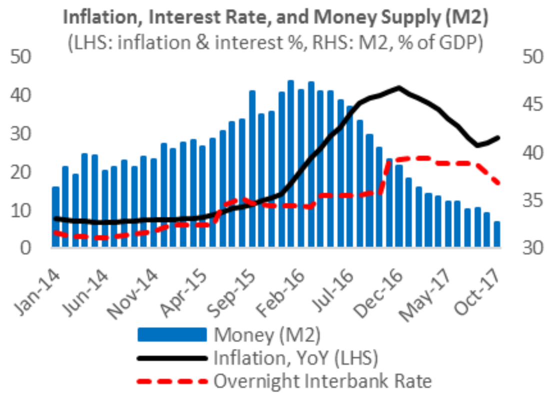
Source: Angolan Authorities, October 2017

Figure 2: After the elections, forex sales have declined, leading to a higher parallel market spread.



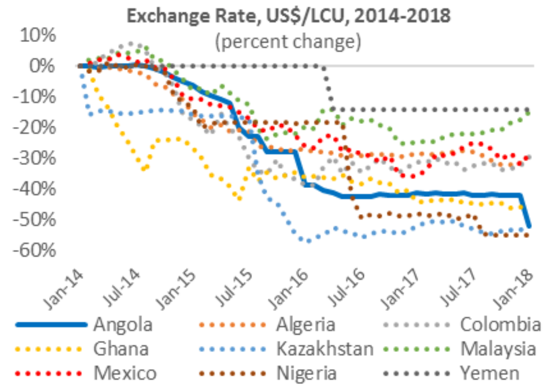
Source: Angolan Authorities, October 2017

Figure 3: Despite some monetary tightening, real interest rates have been negative.



Source: Angolan Authorites, October 2017

Figure 4: Comparing to some benchmark countries, the Kwanza had a significant nominal depreciation by April 2016, but stabilized in its aftermath, until its recent deprecitation with the regime change.



Source: IMF, IFS, January 2018

Policy options

Regime Choice

Angola needs to continue to move towards increased exchange rate flexibility to foster economic diversification and open the path for sustainable economic growth. For an oil-dependent country like Angola, that is subject to a high degree of volatility in the terms of trade, the exchange rate should act as a shock absorber.[4] The currency should depreciate when the price of oil declines, cushioning the shortfall in oil receipts on government revenues. In other words, Angola's exchange rate regime should deliver a high correlation between the exogenous price of oil and the real effective exchange rate, thus acting counter-cyclically (whereas a pegged regime would not). For example, the increased exchange rate flexibility from a floating regime would reduce the need for local prices to fluctuate with the price of oil, thus insulating the domestic economy from oil price volatility and creating additional space for monetary policy to adjust based on domestic conditions.[5]

To the extent that adoptiong a (managed) floating regime is not feasible in the short run, one policy option is to consider an intermediate step toward greater exchange rate flexibility by adopting some form of a basket peg that allows coping with commodity price shocks.[6] One possibility is to peg the currency to a basket composed of some currencies (such as those of major trading partners) and the export price of oil.[7] Such a basket peg would simultaneously deliver automatic accommodation to terms of trade shocks, while retaining the credibility-enhancing advantages of a pegged regime by allowing the exchange rate to continue its role as a nominal anchor while authorities develop a market-based monetary

[4] Exchange rate flexibility has helped commodity-exporting economies manage large terms of trade shocks. See Broda (2004), Edwards and Levy-Yeyati (2005), Setser (2007), Rafiq (2011), and Céspedes and Velasco (2012). Empirical evidence shows that the currencies of commodity-exporting countries that float do in fact fluctuate together with the global prices of their relative commodities. See for example Cashin, Céspedes, and Sahay (2004), Chen and Rogoff (2003), Frankel (2007), and Habib and Kalamova (2007).

[5] However, a limited exchange rate pass-through or high foreign currency debt can reduce the capacity of floating exchange rate regimes to buffer against external shocks. See for example, Mussa et al. (2000), Obstfeld (2002), Devereux et al. (2006), and Towbin and Weber (2013).

[6] Some countries adopted basket peg regimes before moving to floating regimes—e.g. Australia (1974-83), Iceland (1989-2001), New Zealand (1979-85), and Norway (1978-92).

[7] See Frankel (2017). The currency-plus-commodity basket: a proposal for exchange rates in oil-exporting countries to accommodate trade shocks automatically. CID Working Paper No. 333.Harvard University.

policy framework. For instance, a declining oil price would automatically translate into a depreciation of the kwanza and boost exports, thus minimizing the impact of the terms of trade shock on the economy. It could also support competitiveness by limiting the impact of an appreciation against other trading partners. In addition, basket pegs can encourage the development of FX markets that would be key to an eventual float.[8] Operationally, implementing such a proposal would entail daily announcements of the exchange rate and a firm strategy to defend it as needed; this likely would require some capacity building. This regime however has its drawbacks. It may create volatility for the other sectors in the economy. Importantly, there is little historical evidence on the challenges associated with the operationalization of such a regime, but simulation by Frankel (2017) for six Gulf countries show significant benefits in terms of macro-stability.

Broader Policy Reforms in Support of Greater Exchange Rate Flexibility

The changes in the exchange rate regime should be part of a comprehensive policy strategy. Establishing a new policy and institutional framework takes time and requires substantial capacity-building, but there is merit to the process. In fact, setting-up the supporting elements for a new exchange rate regime can be mutually reinforcing. For example, allowing for two-way variation in the exchange rate at an early stage (e.g. by a gradual widening exchange rate bands and limiting central bank intervention) can help stimulate activity in FX markets, provide incentives for better risk management, and helps to build capacity with floating. Historical country experiences suggest that FX market development began only after some exchange rate flexibility was introduced. Overall, the degree of preparation along the key policy priorities outlined in this Note should guide the authorities in setting the pace in which to move to greater exchange rate flexibility.

Specifically, a successful transition toward greater exchange rate flexibility, and in the medium term, toward a sustainable (managed) floating regime, needs the following key set of complementary reforms:

(i) establish a coherent and transparent FX market intervention policy;
(ii) assess and monitor FX risks, especially in the private sector;
(iii) develop a well-functioning FX market;
(iv) implement an alternative nominal anchor by re-designing of the monetary policy framework;
(v) coordinate fiscal policies and strengthen fiscal institutions.

(i) The transition toward a more market-determined exchange rate requires clear and transparent policies on the objectives, timing, and extent of FX market intervention. Under more flexible regimes, intervention is more discretionary than under a peg. There are legitimate reasons for interventions—e.g. to correct misalignments from the long-run equilibrium rate; to calm disorderly markets (especially if the capital account is not fully liberalized or if illiquid markets trigger excessive exchange rate volatility); to accumulate reserves; or to provide market liquidity. However, interventions should be selective as they may not fully address the problem[9], can send mixed signals about policy intentions, and require international reserves. Moreover, smoothing short-term fluctuations may obstruct price discovery mechanisms and suppress market signals. Infrequent intervention signals a commitment to exchange rate flexibility and improves the effectiveness of occasional interventions; both are essential for building credibility. In fact, clearly communicating the overall principles of the new regime (and the intervention policies) can be helpful in achieving an orderly transition. While determining the appropriate level of

[8] The basket pegs adopted by Israel (1985-2005) and Poland (1991-2000), for example, have arguably encouraged risk management, as market participants understood the need to hedge against cross-exchange rate movements.

[9] The empirical evidence on the effectiveness of intervention in influencing the exchange rate is mixed, and the impact of intervention on the exchange rate level appears to be short-lived.

transparency in communicating the exchange rate strategy can be challenging, it is crucial for the credibility of the new regime.

(ii) Assess and monitor FX risks, and strengthen the financial sector, if needed. Forward-looking monitoring and management of FX risks should become part of the macroeconomic policy framework. That is, adequate prudential and supervisory arrangements and enforcement capacity should be developed so that banks' direct and indirect FX exposures and related risks can be monitored.

(iii) Greater exchange rate flexibility requires a deep and efficient FX market.[10] Absence of a well-functioning FX market could lead to long lasting episodes of excessive volatility and large deviations from the equilibrium exchange rate. A key measure in this regard is to phase out administrative FX controls, thereby fostering the flow of information in the market and stimulating price discovery. The authorities should allow the exchange rate to respond to market forces, even if greater exchange rate flexibility is only gradually adopted. The exchange rate should be allowed to fluctuate in both directions to foster risk management expertise and minimize destabilizing trading strategies.

(iv) An alternative nominal anchor needs to be established. To respond to potential inflationary pressures from this initial FX realignment and greater exchange rate flexibility, BNA will need to step up monetary policy.[11] Tight monetary conditions should provide a nominal anchor to the economy by reducing inflationary pressures while also addressing, at least in the short run, the economic and financial distortions associated with negative real interest rates.

The monetary policy framework will need to be redesigned around that anchor. Recent developing country experiences suggest that an inflation targeting regime is an effective nominal anchor.[12] In Angola, however, until the pre-conditions to adopting such a regime are met, monetary targeting (e.g. base money) with the goal of achieving low inflation rate may be more adequate. In November 2017, Angola moved in the right direction by formally adopting base money as their operational instrument to closely monitor economy-wide liquidity and achieve price stability. Some caution is warrented though as the weak relationship between monetary aggregates and inflation limits the overall effectiveness of money targets.

The credibility and transparency of the monetary authorities and the monetary policy framework is critical for managing expectations and inflation dynamics under a more flexible exchange rate regime. Fraga et al. (2003) argue that expected inflation and, consequently, actual inflation tends to be higher if the credibility of the monetary authority is low. The BNA should therefore clearly commit to the price stability objective. Central Bank independence can further enhance credibility as it insulates monetary policy from short-term political pressures.[13] Transparency constitutes an important pre-condition for

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[10] See for example Duttagupta, Fernandez, and Karacadag (2004).

[11] In fact, the pass-through from the exchange rate to domestic prices has been an enduring concern of the authorities and one long-standing reason to avoid devaluations. Recent IMF estimates suggest that the pass-through from the exchange rate to domestic prices is not as high as many expect, with an upper bound of around 50 percent. Lariau et al. (2016) provides some evidence that the long-run exchange rate pass-through in Angola, though still high, has weakened in recent years reflecting a trend toward de-dollarization of the economy. See Aron et al. (2014) for a survey on the exchange rate pass-through for developing and emerging economies, including Sub-Saharan countries. See also Razafimahefa (2012), Caselli and Roitman (2016), and Rahimov et al. (2017).

[12] Frankel (2017) argues that for oil-exporters should not target CPI, but rather a price index that includes the price of the export commodity and exclude the main import commodity; for oil exporters, this would help avoid a pro-cyclical monetary response to terms of trade shocks. An alternative can also be a basket peg that includes the export commodity.

[13] Central bank independence takes on a variety of specific institutional forms, but there are two key dimensions of independence: goal independency (freedom in defining its policy objectives) and instrument independency (freedom in the implementation of policies in the pursuit of the monetary policy objectives). While goal independency varies significantly across countries (especially among those well-stablished and credible central banks), instrument independency is typically observed.

central bank accountability, a key requirement of independency. In a study conducted in 2010, Angola was among the six least transparent central banks in the world (Dincer and Eichengreen, 2014). The Government should place great priority in enhancing transparency, enabling the public to assess whether the actions of the central bank are consistent with its mandate. Importantly, a transparent, clear, and consistent communication policy by the central bank is also crucial to guide the expectations of market participants and bring them into line with the central bank's objectives and actions.[14]

Review of administrative price setting policies. Government-set prices such as for utilities and government fees should be based on cost-recovery or opportunity-cost levels. Pricing rules need to be transparent and adhered to, while prices changes need to be announced with reasonable anticipation. Any perception that the government is delaying price increases or setting prices unrealistically low to control inflation can undermine the credibility of monetary policy. In the case of Angola, it is advisable that fuel prices be adjusted in accordance with the automatic price adjustment mechanism in place and price changes are given full and timely disclosure (see also Fiscal Policy Note).

De-dollarization policies could alleviate the inflationary pressures from greater exchange rate flexibility. Dollarization increases financial market risks, weakens the monetary policy transmission mechanisms and complicates the central bank’s role as a lender of last resort.[15] Dollarization in Angola is still around 30 percent of loans and deposits. The development of local debt markets and of a domestic investor base (e.g. pension and mutual funds) would help to support long-term local currency markets and provide incentives for de-dollarization. Macro-prudential policies (such as caps on loan-to-value ratios, capital requirements, and higher provisions for dollar lending) would also support de-dollarization. It is also advisable to review any legislation that allows the private or public sector to set prices in foreign currency.

(v) Close coordination between the Ministry of Finance and monetary authorities is important to avoid fiscal dominance.[16] Recent policy actions taken as part of the new Administration’s macroeconomic stabilization plan indicate an alignment in fiscal and monetary policies. Continuing and fostering such coordination in policies is important to mitigate the effects of fiscal operations on monetary conditions, as fiscal policy, through its impacts on aggregate demand, can affect inflation, interest rates, spreads, and the exchange rate. Strengthening fiscal institutions (for instance, by reducing the degree of discretionary spending) should give greater confidence that fiscal policy will deliver smaller deficits and put less pressure on the BNA for effective monetary policies.

[14] Many countries, especially those with inflation target regimes, adopt such transparent communication strategy, for instance, by publishing frequent inflation reports and interest rate-setting meeting minutes (e.g. Brazil, Chile, Czech Republic, Philippines, South Korea, Sweden, United Kingdom). See for example Fracasso, Genberg, and Wyplosz (2003) and Blinder et al. (2008).

[15] For example, evidence suggests that the de-dollarization process of Peru and Uruguay have improved the effectiveness of monetary policy. See, for example, Acosta-Ormaechea and Coble (2011) and Medina et al. (2011).

[16] Sargent and Wallace (1981) highlight the difficulties of conducting monetary policy in an environment where fiscal policy is unsustainable. If a central bank is often required to finance public sector deficits (including those arising from quasi-fiscal activities), then an inflationary bias arises. For example, Bianchi and Ilut (2017) show that historically in the United States, if the monetary authority tried to dis-inflate without the backing of the fiscal authority, inflation barely moved.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Continue to move towards greater exchange rate flexibility and develop a well-functioning FX market.		
Establish and clearly communicate the overall principles and features of the new exchange rate regime.	Medium	Short-term
Gradually phase out controls on FX sales.	High	Short-term
Allow the exchange rate to appreciate and depreciate in response to market forces to foster risk management expertise.	High	Short-term
Assess and monitor FX risks, especially in the private sector. Implement forward-looking monitoring and management of FX risks in the economy by re-assessing the regulatory and supervisory frameworks.	High	Short-term
Broader policy reforms in support of greater exchange rate flexibility.		
Establish a coherent FX market intervention policy. The transition toward more market-determined exchange rate requires clear policies on the objectives, timing, and amount of FX market intervention.	Medium	Short-term
Implement an alternative nominal anchor by re-designing of the monetary policy framework. Tighten monetary policy (to respond to potential inflationary pressures from greater exchange rate flexibility) and adopt a new monetary policy regime.	Medium	Long-term
Adopt a consistent, clear, and transparent communication framework for monetary policy to anchor expectations. Announce and commit to a calendar of publications going forward. Publish more high-frequency, timely and user-friendly data in the web, allowing open data access.	High	Short-term
To build credibility and limit inflationary pressures, **set government controlled prices at cost-recovery or opportunity-cost level**, giving transparency to the formulas used.	High	Short-term
Consider granting **de facto autonomy and independence to BNA**.	Medium	Medium term
Coordinate monetary and fiscal policies (promote regular meetings between BNA and Minfin, including its technical staff, to coordinate policies so as to mitigate the impact of fiscal operations on monetary conditions) and **strengthen fiscal institutions** by reducing the degree of discretionary spending.	High	Short-term
Foster De-dollarization		
Set more stringent macro-prudential policies for bank lending in dollars to foster de-dollarization and soften the negative effects on banks from the change in exchange rate regime.	High	Medium term
Review legislation and government practices to **curb any practice of setting prices in foreign currency.**	Medium	Medium term

Annex: Multiple exchange rate regimes

Box 1: Multiple exchange rate regimes are not recommended

The FX market segmentation is often considered in response to significant external imbalances, but they are rarely effective and difficult to sustain. Multiple exchange rate regimes, where the market is divided into a number of segments, each with its own exchange rate, are often adopted in response to significant imbalances in external accounts and strong exchange rate pressures. Their objective is to limit the (potentially large) short-term effects of exchange rate adjustment on domestic prices, while maintaining some degree of control over the capital account and international reserves. They typically require complex legislation and burdensome administration (specially to deal with FX scarcity), and are subject to frequent re-assessments and changes that raise uncertainty and contribute to overall FX market instability; this restricts the ability of multiple exchange rates to act as a nominal anchor for the economy. Uncertainties surrounding exchange rate determination and FX availability in the different FX markets may further affect expectations and even exacerbate domestic inflationary pressures. Furthermore, large spreads between different exchange rates not only create distortions and encourage rent-seeking and corruption, but can also negatively affects confidence in the FX regime, even threatening its continued viability. Argentina and Nigeria recently adopted *de facto* multiple exchange rate regimes and their experience deserve some attention:

Argentina. Pro-cyclical expansionary policies contributed to GDP growth in 2005-11, but also produced significant imbalances in the economy (double-digit inflation, real peso appreciation, and a deterioration of the balance of payments). Amid currency pressures, Argentina resorted to foreign-exchange, import and capital controls, as well as ad hoc interventionism in 2011. In this context, a parallel FX market, with large spreads over the official exchange rate, emerged. The controls led to allocative and price distortions. For example, the large black market premium created arbitrage opportunities that resulted in the widespread selling of dollars in the parallel market, shifting resources from the productive sector to the informal financial sector (Coppola et al, 2016). After several years of a *de facto* dual exchange rate regime, Argentina implemented a process of currency adjustment in December 2015. The central bank rapidly eliminated foreign-exchange and capital controls and simultaneously devaluated the currency, while shifting from a heavily managed float to a “dirty float”, allowing for only occasional intervention (in the event of severe currency volatility). The government argued that such a rapid change would provide clarity, transparency and a strong signal of a commitment to change. The day that controls were removed, the peso depreciated by 30 percent and the spread between official and parallel rates virtually closed. Since then, amid moderate volatility, the parallel FX market has disappeared and the peso has weakened further in nominal terms. Notwithstanding a widening current-account deficit, foreign reserves have grown steadily. The exchange rate regime change was supported by a tightening of fiscal and monetary policies and a commitment by the central bank to tackle economic distortions and lower inflation.

Nigeria implemented a major reform of monetary and exchange rate policy in early 2006, with the introduction of an auction system for FX provision by the central bank. However, some restrictions on FX sales by the central bank led to a multiple exchange rates system, with marked spreads across the different segments. The decline in oil prices in 2014-15 was a large terms of trade shock to Nigeria (as oil receipts dominate fiscal revenues and exports) and the existing FX regime did not bring an orderly adjustment to the shock. By early 2015, there had been a two-step exchange rate devaluation (of almost 30 percent), the central bank closed the official FX auction system, the exchange rate was fixed. While transactions moved to the interbank market, the imposed restrictions by the central bank led to FX shortage. Pressures on the currency continued to mount, and international reserves declined further. In mid-2016, there was another FX depreciation to reduce the real exchange rate misalignment and the FX regime was partially liberalized. In particular, the central bank introduced a primary dealer system for the interbank FX market in an effort to increase exchange rate flexibility and to restore market liquidity. The interbank rate depreciated against the U.S. dollar in subsequent months, significantly narrowing the spread with the parallel market. However, FX restrictions remained in place, with prioritized allocation of foreign exchange to certain sectors and a ban on importers of 41 categories of goods and services from accessing the regulated FX market. As international reserves recovered in the first half of 2017, supported by stronger oil revenues, the availability of FX increased in recent months. In addition, the central bank no longer prioritizes or allocates sales of FX to specific sectors of the economy. This has helped bring down the parallel market premium from 60 percent in February to about 20 percent in June, where it has since stabilized. However, the FX market continues to be tightly regulated, with significant import restrictions and multiple exchange rates in place.

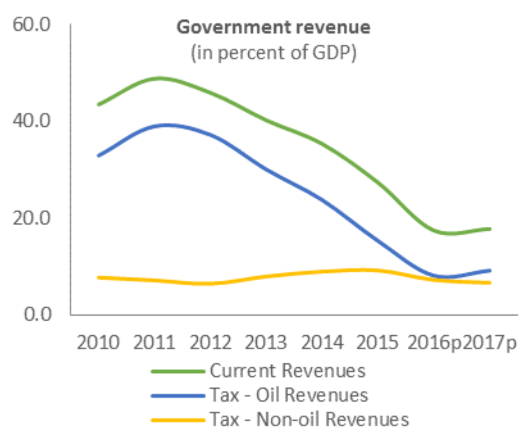
Fiscal Policy and Fiscal Consolidation

The decline in oil prices has reduced government revenue and led to fiscal imbalances and rising debt. It will be critical to mobilize additional non-oil revenue and to continue with a gradual but persistent fiscal consolidation to adjust to lower oil prices; to shield the budget from oil price volatility; and to ensure debt sustainability. There is ample scope to increase tax revenues, but it requires reforms (in tax policy and tax administration) to broaden the tax base and strengthen taxpayer compliance. On the expenditure side, the focus should be on expenditure rationalization and increase of efficiency, including the containing the growth of the public-sector wage bill; increasing the efficiency of expenditures on of goods and services, and public investments; and phasing out subsidies.

Background

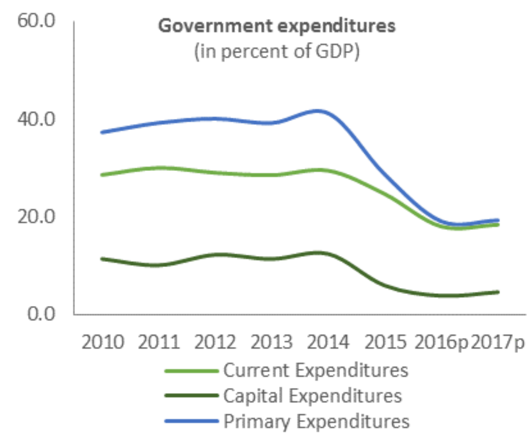
The decline in oil prices has both reduced oil and non-oil revenue, giving rise to fiscal imbalances and a rising debt burden. Current revenue declined steadily since 2014 in percent of GDP (from 32.9 percent to 15.6 percent in 2016), in line with lower oil revenue and depressed non-oil revenue from the ensuing slow. The overall deficit peaked at 6.6 percent in 2014. Fiscal consolidation in 2015 and 2016, mainly through cuts in spending on investment, goods and services, and subsidies, as well as measures on the revenue side narrowed the deficit to 4.5 percent in 2016. Fiscal consolidation was however short-lived and a more expansionary stance to revive the ailing economy pushed the deficit to 5.3 percent in 2017 (preliminary). The budget for 2018 foresees a reduction of the fiscal deficit to 3 percent of GDP, mainly through a cut in payroll and capital expenditure and an increase in oil and non-oil revenue. The public debt has doubled over the last three years—when including the debt of the state-owned oil company *Sonangol*, it reached almost 80 percent of GDP at the end of 2016. Concerns about debt sustainability are aggravated by the shortening maturity of debt and the issuance of debt to settle payment arrears. Most of Angola's external debt is held by China and other bilateral creditors, while Eurobonds account for about US$1.5 billion.

Figure 1: Government revenue decreased steadily since 2012 in percent of GDP, in line with the oil price.



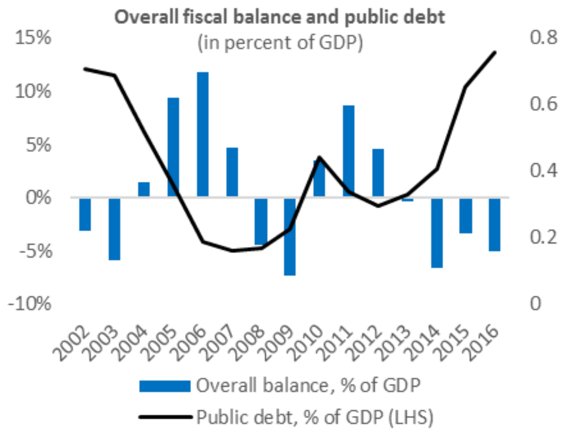
Source: Ministry of Finance

Figure 2: Prior expenditure levels became unsustainable. The GoA reacted in 2015 with large expenditure cuts, mainly in capital expenditure and goods and services …



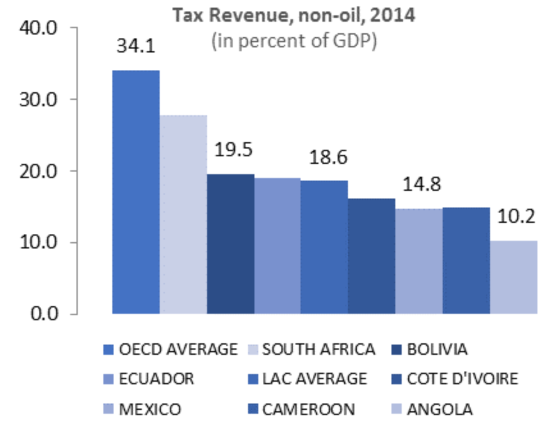
Source: Ministry of Finance

Figure 3: … which resulted in a lower fiscal deficit in 2015. However, preliminary data shows a widening of the deficit in 2016 and 2017, and public debt in percent of GDP is increasing rapidly.



Source: World Economic Outlook Database, October 2017

Figure 4: Non-oil tax revenue in Angola is well below regional and oil-producing peers.



Source: Angola Public Expenditure Review (PER), 2016

The Projecto Executivo da Reforma Tributária (PERT) tax reform program has brought some improvements in tax policy and administration to boost non-oil tax revenue. Tax administration practices have improved substantially with the ongoing implementation of the tax reform program PERT and the creation of the single revenue authority (Administração Geral Tributária, AGT) in 2014. In 2016, the tax regimes for income tax and indirect taxes was partly revised with a focus on simplification, expanding the tax base, reducing distortions and enhancing equity. AGT has recently approved a tax administration strategy, that focuses on measures to enhance voluntary compliance (through taxpayer services); to detect new potential taxpayers (especially outside of Luanda); and to strengthen tax auditing efficiency.

Compared to regional and oil-producing peers, non-oil tax revenue is low, which is partly due to a narrow tax base. The current consumption tax has a narrow tax base with rates ranging from 2 percent to 80 percent applicable on both imports and locally produced commodities. Angola is one of the nine African countries (out of 53) that does not have a VAT, but is currently in the process to introduce it. Furthermore, tax laws foresee multiple tax exemptions and credits. Current tax laws are complex and create opportunities for both tax evasion and avoidance due to loopholes: the corporate income tax (CIT) standard rate at 30 percent is relatively high by international standards, but the tax base is riddled with multiple exemptions[17]. Low tax collection is also a result of administrative constraints: The taxpayer registry – which represents the taxpayer base and the core on which all other tax administration functions are build – is outdated and inaccurate. Although AGT adopted a unique taxpayer identification number (TIN) across all tax-types – which is considered best practice – there is a lack of procedures to update and maintain the integrity and completeness of the register. Non-registration of taxpayers (especially taxpayers outside of Luanda) who should be paying tax contribute to low revenue collection and the overall compliance gap.

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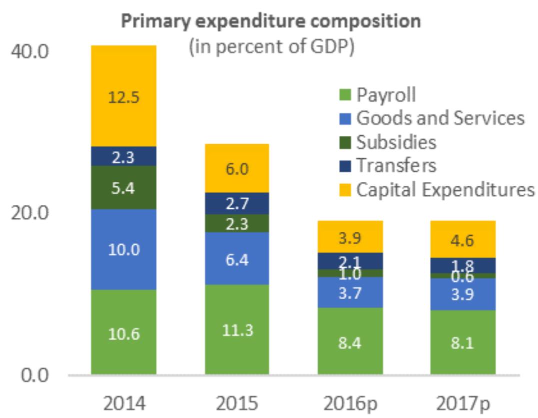
[17] For Investment income tax (*Imposto sobre a Aplicação de Capitais* or IAC), numerous types of income are exempt – depleting the base and aggravating the issue of equity: Interest on deferred payments regarding commercial transactions; Payment of dividends to Angolan CIT taxpayers that hold a participation higher than 25 percent for more than one year; and some other types of interest incomes.

Low tax collection is also linked to weak taxpayer compliance since tax enforcement mechanisms are ineffective and compliance costs high - especially for small and medium taxpayers. Tax audit activities – which ensures taxpayer compliance and has a deterrent and preventive effect on taxpayers[18] – are performed manually and almost exclusively confined to desk audits, which results in low audit effectiveness and efficiency. Furthermore, the tax regime is complex (the personal income tax regime has multiple tax rates and 12 income brackets) and there are no mechanisms that allow for simplified tax returns for small and medium taxpayers – which often lack the economies of scale and the technical capacity to assess and fulfil their tax liabilities under the conventional tax system – resulting in high compliance costs.

On the expenditure side, the public wage bill accounts for the bulk of public spending. The public wage bill is the largest current expenditure item in the budget (8.4 percent of GDP in 2016 and 8.1 percent in 2017)[19], down from its peak at 11.3 percent in 2015 due to inflation (nominal wage increase was lower than inflation in both years, such that wages have decreased in real terms). Goods and services are the second biggest expenditure item and increased from 8.2 percent of GDP in 2010 to a peak of 11.9 percent in 2012, before declining to 3.7 percent in 2016. Capital expenditures, which peaked in 2014 at 12.5 percent of GDP, more than halved in 2015 (to 6 percent of GDP) and decreased further to 3.9 percent in 2016 due to fiscal consolidation.

Figure 5: Primary expenditure composition, 2014-2017



Source: Ministry of Finance

[18] Tax audit also guarantees fairness in the tax system, and has a deterrent (discover and stop taxpayers from continuing to under-declare or manipulate their liability) and preventive effect (higher declaration rate from those not audited).
[19] The civil service payroll represents about half of the wage bill, while wages for military personnel and for public safety and security forces (the national police, border control, and firefighters) each account for roughly a quarter.

Historically, subsidies represented a large share of the budget, but falling oil prices and the fuel subsidy reform at end 2014[20] greatly reduced fiscal costs since 2015[21]. Direct subsidy spending (fuel and price subsidies) declined from a peak of 7.8 percent of GDP in 2011 to 0.8 percent in 2016[22]. The Government implemented a well-designed fuel subsidy reform, which eliminated subsidies on most fuels[23] by end-December 2015 – with only residual and targeted subsidies remaining in place. However, no fuel price adjustment was made since 2015 despite the devaluation of the kwanza and the gradual recovery of international oil prices, which led to the emergence of implicit fuel price subsidies (size unknown): Sonangol is selling fuel below market prices and is not being compensated by the government through the budget. In addition to the high fiscal costs, fuel and price subsidies are also poorly targeted and mostly benefit the better-off: while 77 percent of fuel price subsidies benefit the richest 40 percent households, only 10 percent accrue to the bottom 40 percent. Operational subsidies (i.e. transfers) to SOEs further consume a significant share of the central government budget (see policy note on SOEs).

Policy options

Broaden tax base and increase compliance[24]

Reforming consumption taxes, by introducing a broad-based VAT and streamlining excise taxes, is a top priority to broaden the tax base. VAT is considered a less distortive form of taxation and has built-in tracking mechanism to mitigate the underreporting risk. Ideally, VAT should have very few exemptions (except for certain items regarded as hard-to-tax), and tax goods and services with one single rate. Estimates show that the VAT implementation could increase non-oil tax revenues in net terms by as much as 1.6 percent of GDP. A gradual approach of VAT implementation is recommended, starting with large taxpayers and gradually expanding the VAT to other taxpayers[25]. As a modern consumption-based tax system should consists of two levels (a VAT for general consumption and an excise tax for selective goods and services), the Government should review the entire indirect consumption-based system, including the excise tax regime, when introducing VAT.

Improve reliability and accuracy of taxpayer registry to strengthen taxpayer base. The authorities should clean the current taxpayer database (physical identification of taxpayers outside Luanda) and implement procedures to keep it updated (identify non-registered, inactive and dormant taxpayers or duplicated registrations), for instance through (regular) cross-checks of other external databases and public registries (e.g. registry of the telecom and energy company). Activities aimed at detecting unregistered taxpayers (outside Luanda) including physical inspection of business premises and private residences should be continued. An updated taxpayer database with (i) activity status (active or inactive taxpayer across different taxes CIT, PIT, etc.), and (ii) appropriate means to register new taxpayers and record their basic

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[20] IMF (2016). The Government has been implementing a well-designed fuel subsidy reform and domestic fuel prices were increased in four steps during September 2014 and end-December 2015. With the last adjustment at end-2015, subsidies on diesel were also fully eliminated and the price of diesel liberalized, adding to products to were already liberalized earlier: gasoline, asphalt, and light and heavy fuel oil prices. LPG and kerosene domestic prices were increased, but remain subsidized at about 40 percent and 10 percent, respectively.

[21] Spending on subsidies procyclical: rising oil prices boost exports and GDP growth, but also give rise to higher subsidies to keep domestic fuel prices low.

[22] Subsidy spending according to Boost (2017) stands at 0.8 percent of GDP in 2016 (including price subsidies and operational subsidies to SOEs). This is slightly lower than estimates from the budget proposal for 2018, where subsity spending amounts to 1 percent of GDP.

[23] Subsidies on diesel, gasoline, asphalt, and light and heavy fuel oil prices were fully eliminated by end-December 2015. LPG and kerosene domestic prices were increased, but remain subsidized at about 40 percent and 10 percent, respectively.

[24] As there is no recent diagnostic of Angola's tax policy and the tax administration system available, the following policy options draws on recent engagements between the World Bank and the GoA, including the ongoing Reimbursable Advisory Services (RAS) in tax administration.

[25] This is in line with IMF technical assistance on the VAT implementation.

attributes will facilitate planning for tax administration activities (and revenue projection) and the VAT implementation, since it is the basis on which all other functions are built.

Improve audit function to ensure taxpayer compliance. Tax audits should ideally be driven by a risk-based approach to use scarce resources effectively, that is, to target the highest risk segments and activities[26]. In order to increase audit coverage and effectiveness, AGT needs to develop and adopt a risk-based audit strategy, which requires better access to third party information[27], and capacity to promote automatic data cross-checking (in IT system[28]). Auditors should receive specialized trained since audit activities require strong technical capabilities. The ability to promote timely audits is also key for a successful implementation of the VAT due to the need to refund VAT quickly.

Introduce a simplified tax regime for small and microenterprises to facilitate tax compliance alongside the implementation of the VAT. Simplified tax regimes for micro- and small enterprises can facilitate voluntary tax compliance and business formalization, and are common practice in economies with large semi- and informal sector [29]. The design and operation of small business tax regimes requires however careful analysis, and Box 1 in the Annex provides an overview of the literature. A common approach is to use the VAT threshold as a natural threshold for simplified tax regime. After the VAT introduction, there would be a normal regime and two special regimes for small and microenterprises.

Improve IT system to effectively support core functions of tax administration and implementation of VAT. The current IT system does not support the introduction of a VAT or more advanced tax administration functions such as data cross-checks and risk-based taxpayer audits. The existing system should be replaced by an IT system that consists of a single, integrated system that covers all the needs of AGT and fully supports the implementation of VAT. AGT should closely monitor the sourcing, implementation and use of a new IT system[30]. The system should ideally be able to allow for the extension to additional systems/modules at a later stage (e.g. front-end electronic interfaces for taxpayers including e-filing, back-end control capabilities including automated risk profiling, tailored compliance interventions, matching with third party data). Another critical IT measure for the successful implementation of VAT is the automatic information exchange between the IT systems for taxes and custom administration ASYCUDA[31].

Reduce and optimize public expenditures

Reform the wage system to reduce public sector wage bill to more sustainable levels, and move towards performance-based wage system. Maintaining effective control over the public-sector wage bill should be an ongoing task of the government and part of the medium-term fiscal strategy. The Government has conducted a biometric census of civil servants and re-registered all employees to identify ghost workers. These controls should be continued and strengthened through sound monitoring of the number of

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[26] Risk-based audit approaches use a range of information (electronic information on tax returns, historical information, third party) and risk criteria (e.g. size of the taxpayer's turnover/net profit) to identify the riskiest declarations or non-compliant taxpayers for audit, and allocate these in priority risk to available resources.

[27] Data sources include Government procurement information; Information on imports and exports; Information about vehicle owners; Information about real estate owners.

[28] This tool should automatically check all tax returns (IRC and IRS, later VAT) and indicate inconsistencies, including logical errors, inconsistent financial indexes (e.g. sales in percent of purchases) and discrepancies derived from the cross-checks with information from third parties.

[29] IMF (2017). RA-FIT, 2nd round (2013). For LICs, 95 percent of respondents have small taxpayer regime (20 respondents), LMICs 64 percent (25 respondents), UMICs 56 percent (27 respondents). Although there is no formal survey on informality in Angola, anecdotal evidence and government authorities confirm that economic informality is high.

[30] AGT signed a contract to source a new IT system with a Chinese company.

[31] Customs works under Asycuda, which is a standard integrated government tax administration system and widely used among customs administrations.

employees and payroll in all parts of the public sector[32]. Furthermore, the government should put in place a strategy for wage bill management, which should be informed by a diagnostic of all public-sector wages and benefit legislation, the size of the civil service, and human-resource management. Pay structures[33] should be streamlined and gradually introduced at all levels of the government, thus enhancing payroll oversight. It is crucial to improve the predictability of the wage bill and avoid *ad hoc* increases in wage. Improving the flexibility and performance components of public sector pay agreements—through more merit and performance-based pay, recruitment and management systems—would help to align wages to productivity and could improve the performance of the public sector (efficient provision of public goods).

Reform spending on goods and services to increase its efficiency and ensure funding for priority programs. The large cuts to spending on goods and services since 2015 will not be indefinitely sustainable, and there is already evidence that they may be eroding the quality of public goods and service (Angola Health and Education PER, 2017). For instance, real spending in the health sector increased fifteenfold between 2010 and 2014, while nominal expenditures were cut from 8 Billion Kwanzas in 2014 to 2.4 Billion in 2015. Spending on immunization programs halved in 2015 (from 4 Billion Kwanzas in 2014 to 2 Billion), and data from the 2015/16 Multiple Indicator Cluster Surveys (MICS) suggest that vaccination rates for DTP and Polio-3 have already dropped to about 40 percent in 2015. Spending on goods and services should be subject to a thorough efficiency analysis to identify the necessary funding to sustain the government's priority programs. The Government should link financial allocations to performance indicators, focusing on evaluating recurrent purchases of goods and services to identify the least cost-effective expenditures. The authorities should then move on to evaluating large one-off purchases.

Strengthen Public Financial Management (PFM) practices to increase efficiency of capital expenditure. Given lower projected oil revenue, the Government will need to increase efficiency of public investments to boost their impact on the economy and close the infrastructure gap[34] despite a constrained capital budget. The policy note on PFM presents policy options for enhancing the allocative and technical efficiency of Angola's public investments. The note also addresses the built-up of domestic arreas and outlines policy options to strengthen expenditure controls.

Reduce subsidies by setting government controlled prices to market levels, or international prices in the case of commodities, and use the resulting fiscal savings for well-targeted social programs. Government-controlled prices of subsidized goods and services (including water, electricity, and transport) should correspond to world market or cost recovery prices, or replaced by market-determined prices. Current subsidies (explicit and implicit ones) should be reviewed with respect to their intended objective, beneficiaries, administration and costs, and their distributional incidence should be assessed with the help of the upcoming household survey. Price reforms should be accompanied by institutional reforms (e.g. the removal of *ad hoc* government control and the adoption of automatic price mechanisms) as well as an information campaign to communicate stakeholder impact (e.g. lower tax burdens and better-functioning markets). As subsidy reforms can have adverse social effects (sudden drop in standards of living, especially for low-income households), the government is encouraged to redirect fiscal savings from subsidy reforms to existing social assistance programs (e.g. conditional cash transfers) as well as health and education programs.

[32] For instance, through biometric and badges controls.
[33] Pay structures reflect the salary range structure (or salary structure) within an organization.
[34] Capital expenditure is higher compared to peers, but the focus on investment is appropriate given Angola's large infrastructure deficit. There is no estimate of investment needs, but evidence suggests that the current level of investment is low compared to the country's needs.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Broaden the tax base		
Implement broad-based VAT, streamline excise taxation and incorporate public health tax.	Medium	Medium-term
Improve reliability and accuracy of **taxpayer registry** to strengthen taxpayer base, facilitate planning for tax administration activity (and revenue projection) and the VAT implementation.	High	Short-term
Strengthen tax compliance		
Improve **tax audit function** to ensure taxpayer compliance: develop risk-based approach and train tax officials in audit activities.	Medium	Short-term
Introduce a **simplified tax regime for small and microenterprises** to facilitate tax compliance alongside the implementation of the VAT.	High	Medium-term
Improve the tax administration's **IT system** to effectively support core functions of tax administration and implementation of VAT.	Medium	Medium-term
Reduce and optimize public expenditures		
Reform the wage system to reduce public sector wage bill to more sustainable levels, and move towards performance-based wage system.	Medium	Medium-term
Reform spending on goods and services to increase its efficiency.	Medium	Short-term
Strengthen Public Financial Management (PFM) practices to increase efficiency of capital expenditure.	Medium	Short-term
Eliminate remaining (explicit and implicit) price subsidies, while using savings for well-targeted programs (social protection, health, education programs).	Medium	Short-term

Annex: Simplified regimes for small taxpayers

Box 1: Simplified regimes for small taxpayers

The design and operation of small business tax regimes requires careful analysis. Micro and small business taxpayers are not a homogenous business segment across countries, thus the challenge is to set appropriate size-based thresholds to partition taxpayers into distinct groups, reflecting their differing capacities (education levels, bookkeeping practices, use of bank accounts) and those of the revenue administration, and to determine the appropriate treatment (base, rate, obligations and administrative approaches) within each group. There is no optimal system for small business tax regimes, and regimes tend to change as countries grow and public and private sector capacity improves. While forfait and simplified participation are most common among lower income groups, indicator-based regimes are more common among higher income groups (IMF, 2017). Some **types of simplified regimes** are summarized below:

- **Turnover (or 'gross receipts'):** presumptive profit taxes or single taxes (replacing a number of other taxes) based on turnover, either with the tax liability calculated as a percentage of turnover or with net profit calculated by applying a standardized cost deduction from turnover to account for business expenses
- **Forfait (Agreed) regime**: liability is based on a range of indicators—purchases, sales, number of employees, number of cars owned by the taxpayer, and so on—with the sum due agreed between tax authorities and individual taxpayers, this amount then applying for two years.
- **Standard assessment systems** use mechanical rules to assess tax on the basis of a range of indicators of activity (floor space, location)
- **Simple patent**: a patent (or 'fixed tax') system simply charges a fixed fee—often varying with location and type of activity
- **Asset based methods** impute income as a return on some measure of an enterprise's assets. This is most appealing for small businesses that are dependent upon commercial assets with respect to which the government has good information and control. For example, in urban areas with good real estate cadasters, small businesses that operate from fixed premises could be taxed based upon imputed rents.

A recent working paper from the IMF refers to the **VAT threshold as the natural threshold** for the design of the simplified regime, with the reasoning that businesses with a level of turnover above the threshold are also able to cope with the regular income tax. Further, the paper recommends using a **simple turnover tax below the VAT threshold** (levied at one or two rates differentiated across sectors) serving as a simple form of income tax replacing the VAT and a **modest fixed charge for the smallest (micro) enterprises** to provide attachment to tax system and government, rather than source of revenue.

There are also disadvantages to simplified regimes: For instance, taxpayers can abuse simplified regimes by declaring employed labor as self-employment (which affects the social security system and reduces wage withholding tax collection), larger businesses can hide in small business tax regimes or split-up businesses artificially to reduce business turnover of individual entities to a level below the small business threshold.

Source: ITD (2013); IMF (2015); RA-FIT, 2nd round (2013); WB (2016).

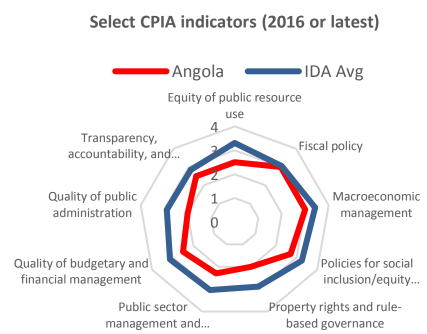
Public Financial and Investment Management

Public financial management (PFM) practices have improved in recent years, mostly through greater transparency and publication of budget data. Significant public management and coordination weaknesses remain and examples include limited implementation of the new public investment management system; limited use of competitive methods for public procurement; unrealistic revenue projections; and weak cash management practices lead to a build-up of arrears. In alignment with the President's commitment to fight corruption and increase accountability, reforms are needed to strengthen internal and external controls, with a focus on giving these control institutions greater autonomy.

Background

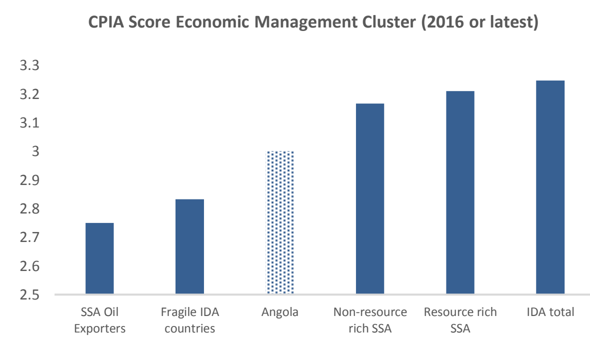
Despite some progress, overall Public Financial Management remains weak, as evidenced by a relatively low CPIA score on the Economic Management Cluster (see Figure 1). Periodic build-ups of significant payment arrears indicate weaknesses in the expenditure chain and there are weaknesses in overall public financial management, and specifically public procurement and corruption controls.

Figure 1: Select CPIA indicators



Source: World Bank

Figure 2: CPIA Score Economic Management



Source: World Bank

Public expenditure management cycle: Previous efforts by the Government to reform its public financial management (PFM) systems have been noted.[35] Public financial management in Angola is underpinned by a relatively new, evolving legal and regulatory framework. With the 2000 constitution at the apex of this framework, relevant laws and regulations have been developed over the last few years to guide the implementation of these principles for PFM. The government has also undertaken reforms to strengthen the budget preparation process by adopting an effective budget classification system and by ensuring that budget proposals presented to the legislature contain most of the standard components, such as information on macro-economic assumptions, the fiscal deficit, debt stock, and explanations of budget implications of new policy initiatives. In addition, reforms include the revision of the framework for internal control; regulations for the Inspectorate General of Finance (IGF); reforms to the Government's Financial Management Information Systems (SIGFE); strengthening of budget reporting; and efforts to build institutional and human skills capacity for public sector management. In addition, external controls by the Supreme Audit Institution and the scrutiny over public financial management by the legislature have strengthened. However, the last PEFA (2016) shows that there are still areas to improve including the need to expand the coverage of the budget to include extra-budgetary funds and state-owned enterprises. One key weakness in the budget is the limited extent to which it reflects a multi-annual

[35] IMF: Angola Selected Issues November 2015; African Economic Outlook 2017.

perspective, which results from a lack of sectoral strategies, failure to determine the budgetary implications of government policies, and a weak integration of the recurrent and the investment budget.

Domestic payment arrears: Domestic arrears in Angola stood at 3 percent of GDP in 2016. The existence of these domestic arrears is a symptom of some of the existing weaknesses in broader PFM arrangements referred to above. While commitment controls have been strengthened in recent years, some commitments are still being made outside the formal budget execution process. When resources were plentiful, many suppliers were willing to deliver goods and services without formal contracts. This is no longer as prevalent, but some contracts continue to be signed outside the formal approval chain. This reduces the role of the integrated financial management system (SIGFE) to an accounting instrument that merely records expenditure ex post; it does not facilitate the determination of the availability of funds or to ensures a clear accountability framework for approving and tracking commitments and payments. The government has addressed payment arrears in the past by issuing debt to pay government suppliers and by tightening controls on expenditure authorization.

Public Investment Management (PIM): A functional PIM system should have standards and systems in place for investment project preparation, appraisal, selection, and monitoring and evaluation. The Angolan PIM system has advanced over the past three years, notably through the preparation of manuals for project appraisal and monitoring, and the new project template for investment projects under the 2017 PIP cycle. While these are essential elements of a PIM system, many weaknesses remain throughout the PIM cycle:

- At the *preparation stage*: pre-feasibility studies are not required; sectoral ministries duplicate the first two steps of the project preparation process (Approval of the Project File and Declaration of Eligibility); and proposals are not required to include alternative investments, details on beneficiaries, or expected maintenance costs. Ministries do not comply with minimal project information requirements, which creates information gaps and inconsistencies in SIGFIP. Coordination between the recurrent and investment budgets remains weak. Low capacity in the sectorial ministries has led to a high dependence on external consultants in project preparation.
- During *implementation* several weaknesses compromise good project execution: the use of open/ competitive tenders is limited and negotiated processes are the preferred option; many projects/contracts are under execution without signed contracts, and projects/contracts often undergo revisions (addendums) including cost adjustments over 15 percent, without a new contract being signed as required by national standards. Physical execution of the projects often bears no relation to the financial execution and some fully paid projects/contracts have not been implemented at all, which suggests weak expenditure controls. MINFIN has adopted a rule whereby unused resources under the quarterly payment quotas are lost if they are not executed in the respective quarter; this may generate the wrong incentives to prioritize spending over quality. Finally, the DNIP does not evaluate project completion, and *ex post* outcome evaluations are not required.

Public Procurement: Angola updated its legal and regulatory framework in 2016, with the aim of modernizing its public procurement system. This update is supplemented by implementing regulations covering access to bidding documents; procedures for procurement of real estate; registration and certification of State suppliers; procedures for execution of framework contracts, and the establishment of public procurement units. The law is applicable to central and local governments, as well as state-owned enterprises (SOEs). A new set of standard bidding documents has also been adopted, to support the proper implementation of the law.

The public procurement system is under the oversight of a dedicated body, the Serviço Nacional da Contratação Pública (SNCP). There is an electronic procurement portal with adequate information, but information on awarded contracts is missing. An e-procurement module/system is under development to manage the entire procurement cycle including bid submission, electronic copies of all contracts with e-signature abilities, and the ability to provide approvals and controls at each stage of the process. The planned system aims to identify and prevent frequent contract revisions, and cost overruns by establishing firm contract limits. It also includes a service provider database (cadastro de fornecedores) managed by the Direccao do Patrimonio do Estado which will keep a record of corporate and individual service providers with a view to ensuring quality and eventually ban individuals or companies found guilty of illegal practices.

SNCP first published procurement statistics in 2014, and its most recent reports (2015) are of very good quality, including detailed analysis on system weaknesses and areas for improvement. It notes that over 80 percent of contracting entities use direct negotiation or other forms of limited bidding procedures, and that only 11 percent of contracting entities conform fully with legislation when purchasing goods and services. It also finds that only around 12 percent of contracts were signed with registered service providers as of end 2015, and that only around 5 percent of procurement contracts (1.5 percent of total value) are awarded to small, medium and micro enterprises, despite a stated objective of promoting such companies through public procurement. The report also estimates that there would have been potential savings of nearly a third of the contract values signed if more competitive procedures had been used, although the methodology for this estimate is unclear.

Issues to be improved are identified in internal and external controls, as follows: (i) SNCP is involved in procurement transactions which can compromise its role as oversight agency, (ii) the Public Financial Management internal control entity (General Inspectorate of Finance – IGF) lacks capacity in procurement and its reviews are usually ex-post and not systematic, and (iii) there is not a dedicated and independent procurement entity in charge of quality review of procurement processing. However, 2016 was the first year of procurement audits held by SNCP. There is no independent administrative body to review complaints, which may impact the confidence of the private sector. However, appeal to the courts is possible. The procurement law calls for ethical behavior and stipulates sanctions for non-compliance.

Anti-Corruption: According to Transparency International’s corruption index and the WGI Control of Corruption indicator, Angola improved in recent years, but remains within the lowest decile and well below the SSA average. Angola signed and ratified the United Nations Convention Against Corruption (UNCAC) in 2003 and 2006, respectively. Angola established a specialized anti-corruption unit in the Prosecutor General’s office (Office for Preventing and Combating Corruption) in 2012. The unit, which became operational in 2013, is headed by an Assistant Prosecutor General and is staffed by two magistrates and six technical experts. In 2016, Angola underwent its first UNCAC Peer Review[36]. The review finds that the basic legal framework is in place to combat corruption, but important gaps remain: legislation that criminalizes bribing public officials needs to be brought into line with the UN Convention; the scope of corruption-related crimes (e.g. bribery, embezzlement, money laundering, fraud) needs to be widened; provisions for the protection and anonymity of witnesses needs to be introduced. Insufficient capacity to handle complex financial and economic crimes together with weak cooperation between those authorities in charge of combating economic and financial crimes present important operational weaknesses. These weaknesses are exacerbated by inadequate information systems and databases that prevent the exchange and triangulation of information.

[36] Phase I reviews focus on the legal framework

Policy options

Reinforce public financial management arrangements and expenditure controls. The Government should continue implementing reforms intended to enhance the capacity of public sector management, strengthen the internal control environment for public expenditures and ensure compliance with established procedures for public expenditures, including processing all expenditures through the established systems and channels. Contracts signed outside of the established process should be reviewed to establish their legality. The Government may consider to cancel some contracts to discourage such practices in the future.

Increase the credibility of revenue forecasts to provide a more realistic budget envelope for expenditure commitments, and to reduce the margin for over-commitments and arrears. While there no single methodology for forecasting revenues, the Ministry of Finance could contract external experts to help develop forecasting models for the main revenue components. Ideally, underlying studies, assumptions and yearly forecasts should be published. Following the example of other countries, revenue projections and scenario analyses should be based on externally sourced macroeconomic assumptions and/or scrutinized by independent third-party.

Strengthen the project preparation capacity of ministry staff through a comprehensive capacity development program on investment project formulation and evaluation. The project preparation process needs to be simplified. Investment proposals should be required to include alternative options, and detailed information on beneficiaries and maintenance costs, they should also have screening and reject/revise options for non-compliant projects. The government should promote the use of competitive procurement for public investment projects and limit the use of direct negotiation. The public investment department of the Ministry of Finance should clean the SIPIP database and prepare periodic analytical reports on financial and physical execution, including information on progress towards annual targets, overcharges and project delays. The Government should also eliminate the rule on quarterly payment quotas and consider adopting a medium-term expenditure framework that sets out medium-term spending priorities and budget constraints; this could help reduce the pro-cyclicality of investment spending.

Strengthening internal and external controls and increasing transparency can support the President's flagship promise to fight corruption. While several control institutions have been strengthened in recent years, greater autonomy to determine their own activities and more resources would likely improve outcomes. The Supreme Audit Institution (*Tribunal de Contas*) should have legal autonomy to carry out audits and controls by itself, and should be encouraged to conduct more performance and value-for-money audits. There are also opportunities to strengthen and modernize further the audit methodologies and approaches used by the Supreme Audit Institution, Tribunal de Contas, including a realignment to focus audits on risk, performance and ex-post controls. Government should also consider discontinuing its pre-approval of procurement contracts, which can be done gradually (e.g. by establishing thresholds first). Greater transparency of Angola's various anti-corruption and control institutions[37] would also strengthen their mission of increasing public accountability. In general, a central priority for the Government should be shift away from a 'pedagogical' approach, whereby control institutions see their role primarily as providers of guidance on proper public management to a more punitive approach that holds public officials accountable for the mismanagement of public resources. Finally, there is a need to align the legal framework with UNCAC requirements, including the need for measures to protect

[37] Tribunal de Contas, Inspeccao Geral do Administracao do Estado, Tribunal Supremo, Ministerio Publico, Policia Economica, Unidade de Informacao Financeira, Inspeccao Geral das Financas

informants and whistleblowers which have been shown to be the most important sources of information on corruption around the world.

Ensure completeness of diagnostic knowledge for public financial management and elaborate a national PFM reform strategy. The Public Expenditure and Financial Accountability (PEFA) diagnostic review undertaken by the Government with the support of the ADB was an important initial step required to build up the diagnostic knowledge of the strengths and weaknesses of the public financial management system. It could provide a means to measure and monitor the performance of important public financial management institutions, systems, and processes. It is also an additional reflection of the government's commitment to address the weaknesses and build on the reforms already undertaken. To achieve the objectives of the reforms however, it is necessary that the government undertakes a structured process to ensure completeness of the diagnostic knowledge on PFM. It is also recommended that such knowledge forms the basis for the elaboration of a formal National PFM Reform strategy, a process that should involve all the relevant stakeholders.

Increase the availability, quality and timeliness of government finance statistics for transparency and decision making. The Government regularly produces and publishes information on public finances. However, improvements in the financial reporting regime, in particular, in the ability to offer a more comprehensive picture of the Government's assets and liabilities, would equip public officials with better information with which to make decisions. It would also ensure that information on government assets and liabilities is available for legislative and public scrutiny, thereby enhancing transparency and accountability in their management.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Budget Credibility		
Improve revenue forecasting to provide a more realistic budget envelope. Commission external experts to develop statistical models to forecast the main revenue items and publish the underlying analyses.	High	Short-term
Strengthen commitment/ expenditure controls to avoid arrears. All expenditures should be processed through the established systems and channels. The SIGFIP should be used to process the entire expenditure chain from budget ceiling allocations to commitments, payments, and budget reconciliation.	High	Short-term
Public Investment Management		
Ensure comprehensive diagnostic study and elaborate a national PFM reform strategy. Complete the Public Expenditure and Financial Accountability (PEFA) review and undertake a dialogue and consultation process leading to the development of a national PFM reform strategy.	High	Short-term
Increase public investment monitoring. Prepare periodic reports on financial and physical execution, compliance with annual targets, overcharges, contract adjustments and project delays.	Medium	Short-term
Conduct a benchmarking study. Carry out an analysis of public investment project costs, including benchmarking across domestic regions and internationally.	Medium	Medium-term
Promote the use of competitive procurement and streamline process. Increase the use of competitive procurement for investment projects and limit the use of direct contracting; approve and deploy the e-governance procurement system; define the profile of public procurement practitioners, including performance indicators (KPI) for the contracting entities. Consider discontinuing pre-approval of procurement contracts.	High	Short-term
Internal and External Controls		
Increase autonomy of control institutions (e.g. *Tribunal de Contas*) to determine their own activities. For instance, the Supreme Audit Institution (Tribunal de Contas) should have legal autonomy to carry out audits and controls by itself. Strengthen audit methodologies and approaches and increase focus on risk and performance based audits.	High	Medium-term
Increase the availability, quality and timeliness of government finance statistics for transparency and decision making. Enhance financial reporting regimes and the availability and timeliness of information for decision making, accountability and transparency.	High	Short-term
Revise anti-corruption laws, with focus on criminalizing bribery and expanding the range of predicated offenses, include provisions to protect whistleblowers. Increase transparency of anti-corruption and control institutions to strengthen their mission of increasing public accountability.	High	Medium-term

Financial Sector Stability

Financial sector vulnerabilities have been on the rise and some banks, particularly the state-owned banks, are in need of recapitalization/restructuring. The concentration of credit in public sector assets and the loss of direct U.S. dollar correspondence banking relationships (CBRs) are compromising the stability of the financial system and its ability to support the broader economy. While significant efforts have been made to Improve the regulatory and legal framework for bank supervision, adopted solutions have high fiscal costs. Operationalizing the bank resolution framework, enhancing banking supervisory efficiency and adopting a risk-based supervision are policy priorities for financial sector stability. The findings of the National Risk Assessment for AML/CFT should be used to identify and mitigate the underlying causes of the loss of CBRs. Capital Market development would benefit from a more transparent and competitive auction system for Government securities.

Background

Angola has the third largest financial sector in sub-Saharan Africa. The financial system is dominated by banks, which represent 99 percent of assets in the sector. Credit growth has been concentrated in real estate, consumer lending, and trade, which limits the financial sector's role in diversification and attenuating exposure to cyclical shocks**.** The state has a significant role in the banking sector: it directly owns three banks (including one of the top of five), and in *SONANGOL*, which has a significant stake in six banks (including one of the top five banks). The large role played by *SONANGOL* in the banking sector poses a systemic risk to the financial sector. Additionally, there is a considerable ownership stake by politically exposed persons (PEPs)[38] in the banking system.

The financial system is vulnerable to shocks as a result of the heavy economic dependence on oil and a high percentage of state-owned and state-linked financial institutions. Lower oil prices since 2014 have contributed to the deterioration of key financial soundness indicators. Delays in Government payments to suppliers created liquidity problems among the latter and resulted in higher non-performing loans (NPLs), especially in the construction sector. Spending cuts by oil companies and the Government increased delinquency in household loans, as these two employ a large share of the labor force. Finally,the dominance of Portuguese foreign shareholdering can also be a vulnerability as was borne out in the failure of BES bank in 2014 whichhad reprucssaion to its Angola substsidairy - BESA.

Financial sector vulnerabilities have been rising, but they are mainly concentrated in one legacy problem bank and one systemically important state-owned bank. System NPLs reached 28 percent as of November 2017, up from about 10 percent in 2013. The five largest banks accounted for 93 percent of NPLs as of August 2017 but there is significant variation in NPLs and provisions. In August 2017, *Banco de Poupanca e Credito* (BPC-state-owned) accounted for 81 percent of the top five banks' NPLs and nearly 75 percent of total system NPLs. When adding the two smaller state-owned banks' (*Banco de Desenvolvimento do Angola* – BDA and *Banco de Industria e Comercio* – BCI) NPLs to BE and BPC NPLs, almost 82 percent of system NPLs would be accounted for. There is an urgent need to resolve NPLs in the state-owned banks to minimize fiscal liabilities and avoid spillovers to the rest of the banking system. It should be noted that not all banks are reporting according to IFRS as of end 2017, including BPC, rendering assessments of the soundness of the sector challenging, and masking potential vulnerabilities due to high tolerance of risks within current CONTIF accounting and reporting systems.

[38] Domestic PEPs are defined, according to the FATF Guidelines, as individuals who are or have been entrusted domestically with prominent public functions, for example Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of state owned corporations, important political party officials. http://www.fatfgafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf.

Banking sector profitability declined markedly in the past five years. ROA (Return on Assets) fell from 1.6 percent in 2012 to 1.2 percent by August 2017, while ROE (Return on Equity) fell from 12.5 percent to 7.7 percent over the same period, though there was a slight uptick towards the end of 2017 (driven by year-end profit taking). High returns in previous years were primarily due to the wide spread between lending and deposit rates and a significant weight of investments in the high yielding Government securities. The BESA resolution in 2014, and growing NPLs and provisioning, especially of the state-owned banks, contributed to the decline.

Capital adequacy remains above the regulatory minimum, but some banks need re-capitalization. The risk weighted sector-wide Capital Adequacy Ratio (CAR) was 17.8 percent as of November 2017. It has been above the minimum 12 percent for the past five years, but there is significant variation between banks and several need recapitalization. Of the five largest banks, *Banco Economico* (successor bank to BESA) and BPC currently do not meet the minimum CAR of 12 percent. Following the completion of a partial Asset Quality Review (AQR) in 2015, the BNA asked all three state-owned banks to submit recapitalization plans. In addition to the state-owned banks, two middle-sized banks are also reportedly under-capitalized.

The loss of direct U.S. dollar Correspondent Banking Relationships (CBRs) could further compromise the stability of the financial system. Jurisdictional risk, weaknesses in Angola's AML/CFT legal framework, and reduced risk appetite by global banks have contributed to CBR withdrawals. The high concentration of shareholdings in key banks by domestic PEPs and general concerns around weak growth and vulnerabilities in the Angolan financial system have also likely contributed to the hesitation of global banks to engage directly with local banks.

The loss of direct U.S. dollar CBRs has affected most sectors, but was partly mitigated by a switch to Euros and "nesting". Most sectors were affected by the withdrawal of direct U.S. dollar CBRs, including the supply of food and medicine. The provision of US dollar currency has been maintained, but not in the same proportion as before. US dollar clearing has been made possible through nested relationships, where subsidiaries of Angolan banks in Portugal and South Africa take on the role of a correspondent bank. Western Union and Moneygram have reduced operations, which has impacted remittances. The limited supply of dollars has further affected small entrepreneurs who do business with the Emirates, South Africa, Brazil and China. The need for operations to be denominated in euros increases the cost to the end user (due to conversion from US dollars to euros). Trade finance has not been overly affected. It should not be noted that the oil companies were not affected by the withdrawal of CBRs due to their largely offshore financing arrangements.

Authorities have been actively exploring options to address the loss of direct U.S. dollar CBRs. The authorities started a National Risk Assessment (NRA) for AML/CFT in 2017, which is coordinated by the Financial Intelligence Unit (FIU). The NRA is expected to contribute to the effective implementation of the 2012 Financial Action Task Force Recommendation, and the implementation of the main recommendations of the AML/CFT assessment report[39]. These were carried out as part of the FSAP in October 2012. BNA has reportedly subjected systemically-relevant banks to enhanced scrutiny including conducting onsite AML/CFT supervision, while banks themselves have taken measures to stregthen internal controls. The authorities have also taken steps to strengthen the AML/CFT regime and Angola was removed from the FATF "grey list" in February 2016. Most recenty in January of 2018 the BNA has announced that additional scrunity will be undertaken for foreign exchange transactions conducted by PEPs through the banking system.

[39] World Bank-ESAAMLG (Eastern and Southern Africa Anti-Money Laundering Group) AML/ CFT assessment.

The recent exit from the dollar peg may exacerbate vulnerabilities in the banking system. As the banking system as a whole has a "long position" in foreign currency, a depreciation would in principle benefit system-wide capital, but individual banks' foreign currency positions vary substantially: according to the BNA data from August 2017, seven banks - one of them systemically important (i.e. BE) - are "short" in foreign currency, which could make them vulnerable to depreciation. The overall impact of depreciation on bank's capital adequacy will also depend on bank's liability, the impact on loan quality and market reactions. In light of significant informal trading in foreign currency, authorities need to remain vigilant and AML controls need to be improved. BNA should engage with banks to identify currency mismatches.

The recapitalization of troubled state-owned banks has had a significant fiscal cost. Re-capitalization of State-Owned Banco Popular de Crédito (BPC) and of other small banks has required public debt issuance. The BPC was re-capitalized in 2015 and 2016 by issuing long-term treasury securities in local currency. The two smaller state-owned banks, BCI and BDA, which faced long running problems before the recent macro and system wide developments were recapitalized in January 2016 at a total cost to the Treasury of about one-fourth of a percent of GDP. In 2017, the Ministry of Finance announced the creation of a publicly funded state-owned asset management company (Recredit) as a "bad bank" to buy bank NPLs. Recredit initial focus was on BPC, but its remit was expanded to include all banks with elevated NPLs. A major difficulty is the valuation of NPLs and the determination of the market recoverable value. Recredit has been capitalized through two government securities issuances of 380 billion Kwanzas.[40]

Since the 2012 FSAP, the authorities have made significant efforts to improve the legal and regulatory framework for bank supervision. These include:

- A new Financial Institutions Law includes improvements in corporate governance, internal control, and calls for the establishment of a deposit guarantee fund. It also sets up a National Council of Financial Stability
- Domestic banks are required to adopt IAS / IFRS reporting standards
- Prudential regulations for Basel II-related requirements on liquidity risks, solvency ratios, and large exposures are under preparation. As of January 2017, banks are required to periodically report to BNA on interest rate risk.
- The Asset Quality Reviews of the banking system was concluded in 2015, and a second is ongoing.

The six-month Government Plan (*Plano Intercalar*) includes measures to strengthen the financial sector. Specifically, the plan calls for the implementation of the financial sector development strategy, the adoption of risk-based bank supervision and an increase of the minimum capital requirements for banks, this will prepare the ground for system-wide consolidation. The Plan also requires quality reviews and stress testing for banking assets, as well as a performance evaluation of Recredit. The interim plan calls for a more competitive and transparent auction system for the issuance of Government securities, and a continued effort to address the loss of US dollar correspondent banking relationships by improving the AML/CFT framework and outreach to the global banks.

Policy options

Operationalize the Bank Resolution Framework, to bolster crisis preparedness and to resolve weaknesses in the banking system. The Financial Institutions Law (FIL) has introduced significant enhancements to bank resolution, including the creation of a deposit guarantee fund (DGF), the introduction of corrective measures and recovery plan. Additional steps needed to strengthen the bank resolution framework include:

[40] June 16: 231 Billion, maturity 25 years, 5 percent i-rate and July 17: 150 Billion, maturity 7 years, 7 percent i-rate

- *Enhance crisis preparedness* by creating: operational arrangements for the recently formed "*Conselho Nacional de Estabilidade*; regulation and operational procedures for emergency liquidity assistance under a Lending of Last Resort (LOLR) scheme; and a Crisis Simulation Exercise and regular Stress Tests. A full AQR should also be conducted to acertain the health of the banking system as a whole.
- *Improve the Bank Resolution scheme and apply Bank resolution options to banks in difficulty* by better differentiating between systemic and non-systemic outcomes, and by specifying adequate resolution alternatives (e.g. bank closure and deposit payout; restructuring; mergers and acquisitions; bridge bank; division into good bank-bad bank). Provide clear guidelines for the regulations and operational procedures for the Bank Resolution scheme. The outcome of the Crisis Simulation Exercise should help inform the operationalization of the Bank Resolution scheme.
- *Re-evaluate Recredit's model of operation.* While an Asset Management Company can help address NPLs in the system, the "purchase price" of NPLs should be based on clear market criteria where the recoverable value is established objectively prior to any purchase of NPLs. An appropriate price for NPLs should include a margin to cover Recredit costs. Reflecting the true collection value and Recredit's full recovery costs in the pricing of NPLs would lower the fiscal burden of dealing with problem banks. Additionally, having a sunset clause would help keep Recredit's mandate narrowly focused on BPC so it does not become a system wide permanent warehouse of NPLs, which could create a moral hazard and potentially undermine credit discipline, by transferring the burden of bad debts to the state as opposed to resolving it on a market basis.
- *Establish a Deposit Guarantee Fund (DGF) in line with best practices* to: (i) ensure independence of the DGF Board of Directors; (ii) establish a coverage amount; establish a range for the annual contribution that member institutions may be required to pay to the DGF, establish a clear timeframe for the reimbursement of deposits; (iii) define the Fund investment strategy; and (iv) develop and approve operational procedures and tools. Any issues with banks need to be resolved prior to launching the DGF.

Enhance supervisory effectiveness and move to risk-based supervision. Areas for further enhancement encompass the establishment of a consolidated supervision framework, including the systematic monitoring of related party lending, as well as the operationalization of prompt corrective action procedures:

- *Operational procedures for prompt corrective actions are needed.* The FIL grants BNA discretionary powers to enforce early corrective actions in case of prudential breaches, but policies and procedures for the operationalization of these powers have yet to be established to ensure that effective measures are taken in timely manner and in a standardized and consistent way.
- *A comprehensive framework for consolidated supervision should be established.* Although the legal framework grants BNA the power for consolidated supervision, the specific regulations or procedures are not in place to perform this on an ongoing basis. Related party lending is not permitted, however, any information on related parties that is received is not reported by banks on a regular basis and there are no systematic procedures in place to verify the existence of related party exposures.

Address the loss of U.S. dollar Correspondent Banking Relationships. The ongoing National Risk Assessment (NRA) is an important step towards a comprehensive and effective AML/CFT strategy. The findings of the NRA should be used to develop a multi-disciplinary risk-based AML/CFT strategy that would enhance ML/FT prevention, detection and repression; set short and medium-term objectives; and prioritize Customer Due Dilligence (CDD) measures to sectors that are highly sensitive to ML/FT. A dedicated authority/mechanism should be established to take charge of implementing and reviewing the strategy.

Develop the domestic capital market. A deep and liquid kwanza denominated capital market would help to provide long-term financing to the private sector and contribute to financial sector stability by insulating the economy from exchange rate shocks. Deficiencies remain on both demand and supply sides of the market. The institutional investor base and in particular the pension system would need to be strengthened; at the same time, the government should build a more liquid yield curve through regular government issuances with defined benchmark maturities, and incentivize new issuers to enter the market and provide diversified investment opportunities. Capacity bulding will be needed to support the development of the market eco-system.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Operationalize the Bank Resolution Framework to bolster crisis preparedness, to help resolve weaknesses in the banking system, and address high NPLs and banks in difficulty.		
Improve the Bank Resolution Framework and apply new bank resolution powers to banks in difficulty, especially state-owned and systemic banks.	Medium	Short-term
Enhance crisis preparedness by developing regulation and operational procedures for emergency liquidity assistance under a Lending of Last Resort (LOLR) scheme, conducting a crisis simulation exercise and an updated Asset Quality Review (AQR).	High	Short-term
Re-evaluate Recredit's business model such that it operates on a sustainable, market basis with a focused mandate on BPC and sunset clause.	Medium	Short-term
Establish a deposit guarantee scheme in line with best practices.	Medium	Medium-term
Enhance banking supervisory effectiveness and move to risk-based supervision.		
Develop and apply operational procedures for prompt corrective actions.	Medium	Short-term
Establish a comprehensive framework for consolidated supervision including related parties and financial groups (groups that own banks, insurance companies, pension funds, etc.).	Medium	Medium-term
Address underlying causes of loss of US$ Correspondent Banking Relationships.		
Conclude the National Risk Assessment (NRA) for AML/CFT.	High	Short-term
Adopt and implement a risk-based AML/CFT legal and regulatory framework to enhance Customer Due Diligence (CDD) measures in sectors that are highly vulnerable to ML/FT. Simplify and/or exempt CDD measures where there is a proven low risk of ML/FT.	High	Medium-term
Develop the domestic capital market to reduce capital-flow volatility.		
Promote the reforms, policies and regulations necessary for local capital markets and create access to long-term, local-currency finance and reduce dependency on foreign currency debt.	High	Medium-term

Annex: Financial sector overview

Angola has the third largest financial sector in sub-Saharan Africa with US$65 billion in assets as of June 2017[41], third only to South Africa and Nigeria. The financial system is dominated by banks, which represent 99 percent of assets in the sector. The financial sector is comprised of 30 licensed banks (and 6 representation offices of foreign banks), 25 insurance companies, 6 pension fund management companies, 40 microcredit institutions, 4 credit cooperatives, 2 mobile money services providers, 82 foreign exchange bureaus (from which 42 are authorized to undertake remittances services) and 18 remittances companies. Despite increase in the number of banks, the system remains concentrated, with the top five banks accounting for 63 percent of sector assets[42]; credit growth has been concentrated in real estate, consumer lending, and trade, limiting the financial sector's role in diversification and attenuating exposure to cyclical shocks**.** The state has a significant role in the banking sector, both through direct ownership of three banks (including one in the top of five), and through Sonangol, which has a significant stake in six banks (including one of the top five banks). The large role currently played by Sonangol in the banking sector poses a systemic risk to the financial sector. Additionally, there is a considerable ownership stake by politically exposed persons (PEPs)[43] in the banking system.

The insurance, pensions, and capital markets remain a small percentage of the financial system and the authorities are keen to diversify the financial system to support economic growth and open new and long-term sources of financing. The main securities currently offered and traded in the market are government securities. Currently, there is only a platform for government bond markets (GBMs) managed by the BNA. There are no corporate bonds and Institutional investors are scarce. A market for equity securities is expected to be in place by 2018.. The social security system (Instituto Nacional de Seguranca Social) is underfunded; its current assets can only sustain its liabilities for only approx. 24 months, and current inflows cover only approx. 90% of outflows. Given limited investment choices including by regulation and market structure, over 80% of its funds are held in bank short term deposits, over 90% are in BPC. With a premium volume of almost US$850 million in 2015 and 25 licensed insurances (2017), Angola is the fourth largest insurance market in Sub-Saharan Africa. In recent years, the authorities have been establishing a more robust legal and regulatory framework and supervisory capacity for capital markets and the insurance/pensions sectors. They have also been actively exploring, both domestically and internationally, how to bring in new entrants in this space.

The financial sector regulatory framework provides the Central Bank (*Banco Nacional de Angola* – BNA) authority in banking and credit institutions supervision. The BNA has supervision responsibility for all banks and non-bank credit financial institutions (such as microfinance, credit cooperatives, and leasing companies). The Capital Markets Commission (CMC) regulates the capital markets. The Agency for Regulation of Insurance and Pensions (ARSEG) regulates the insurance and pensions sectors. Both CMC

[41] Source: BNA, Statistics Boletim. Total Financial System Assets at 10,719,457 million Kwanzas converted at official rate of 165 KW/US$.

[42] The five largest banks in the system as of 2016 were: *Banco de Poupance e Credit* (state-owned); *Bano Angola de Investimentos* (domestic private with Sonangol shareholding); *Banco de Fomentao Angola* (Portuguese and domestic private shareholding); *Banco BIC* (Portuguese and domestic private shareholding); *Banco Economico* (former Portuguese BESA Bank that was put under Central Bank administration in 2014 and now has domestic shareholding including Sonangol). The merger in 2016 of *Banco Millenium Angola* and *Banco Privado Atalantico* likely propelled the resulting bank of *Banco Millenium Atantico* into the top tier of banks though 2017 balance sheet data is not yet available.

[43] Domestic PEPs are defined, according to the FATF Guidelines, as individuals who are or have been entrusted domestically with prominent public functions, for example Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of state owned corporations, important political party officials. http://www.fatfgafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf.

and ARSEG report to the Minister of Finance, but they have their own autonomous structure and boards of directors.

Table 1: Selected financial soundness indicators

	2012	2013	2014	2015	2016	Aug 2017
Capital adequacy						
Regulatory capital to risk-weighted assets	18.3	19.5	19.8	19.8	19.18	22.76
Capital (net worth) to risk-weighted assets	13.6	14.3	13.9	13.8	14.26	17.33
Asset quality						
Foreign exchange loans to total loans	42.7	37.8	27.4	30.8	29.53	25.38
NPLs	6.8	9.7	11.7	11.6	13.08	25.02
Earnings and profitability						
Return on assets (ROA)	1.6	1.4	0.6	1.7	2.19	1.17
Return on equity (ROE)	12.5	10.9	4.9	12.9	15.56	7.69
Total Cost/Total Income	99.4	99.6	99.9	99.8	99.71	99.81
Lending rate minus demand deposit rates	13.3	13.9	14.9	9.9	15.19	16.20
Saving deposit rates	7.0	4.1	4.9	3.5	4.81	8.89
Liquidity						
Liquid assets/total assets	26.3	30.1	33.9	39.7	46.30	41.15
Liquid assets/short term liabilities	33.7	36.9	43.2	50.6	59.22	54.85
Loan/deposits	65.5	63.3	59.9	59.0	51.56	51.00
Foreign currency liabilities/total liabilities	50.7	43.0	33.1	33.6	34.42	33.80
Net open position in foreign exchange to capital	—	—	23.7	34.4	42.89	33.98

Source: BNA

Towards a long-term fiscal framework for Natural Resource Wealth Management

Angola faces simultaneous fiscal challenges of i) preparing for dwindling oil reserves, and a strong reduction of oil revenues over the next 15-20 years; ii) reducing foreign debt to levels that can be managed in a future without revenues from oil; and iii) stabilizing the non-oil fiscal position in the short term (3-4 years). These are closely related, yet separate, challenges. Whereas the focus of the Oil Price Differential Account (OPDA) should be exclusively on short-term stabilization, long-term fiscal challenges resulting from strongly reduced oil revenues will require in-depth fiscal reform. To make the OPDA an efficient instrument for fiscal stabilization, OPDA rules need to be strengthened, and be part of a robust fiscal framework for natural resource management that reinforces fiscally responsible economic management for current and future generations.

Background

Fiscal policy has been highly pro-cyclical due to volatile oil prices. Fiscal volatility, sudden changes in public spending, and pro-cyclicality in fiscal policy contribute to macroeconomic volatility and uncertainty. There is a strong macroeconomic case for smoothing public expenditure and the non-resource balance in the face of resource revenue fluctuations. Lower levels of policy-induced volatility help to reduce macroeconomic volatility, which benefits growth and development[44]. A recent paper showed that fiscal policy in Angola has been highly pro-cyclical (expansionary fiscal policy in good times, contractionary in bad times), which has exacerbated the effect of resource price volatility on the economy [45]. Figure 1 illustrates that expenditure volatility in Angola is high for 2001-16 and is not isolated from oil price and revenue volatility. Other countries including Norway and Chile have mitigated the negative impact of revenue volatility with fiscal rules and strong institutions, resulting in less volatile public spending (see Figures 2-3).

Fiture 1: Angola has experienced high expenditure volatility …

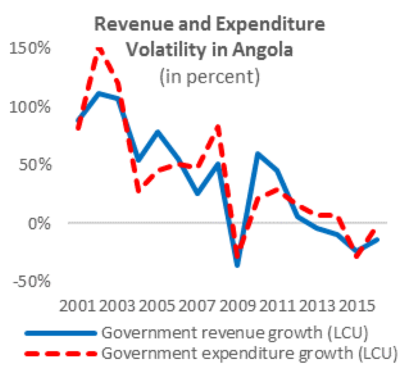
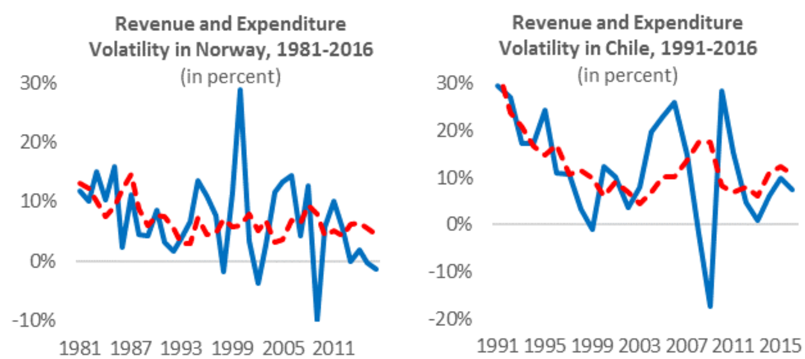


Figure 2-3: …whereas countries, including some with fiscal rules, have managed to mitigat against commodity volatility, e.g. Norway and Chile.



Source: IMF WEO, October 2017. Norway established a fiscal guideline in 2001, which limits the central government's structural non-oil deficit over time to 4 percent. Fiscal policy in Chile has been built on the concept of a central government structural balance (SB) since 2001, supported by a fiscal guideline targeting that balance.

44 IMF, (2011). Fiscal Management in Resource-Rich Countries.

45 Fiscal policy in Angola was highly procyclical over 2000-09. The nonoil primary deficit continued to deteriorate through 2012 before starting to come down in 2013 in the context of very strong growth in the nonoil economy.

Persistently low oil prices and the expected depletion of oil reserves in the not-too-distant future pose a concern for fiscal sustainability and intergenerational equity. Angola's oil production horizon is relatively short, with proven oil reserves expected to be exhausted by 2032[46]. Changing global demand and the entry of new producers, including the US shale and gas industries, are rebalancing the global oil sector; lower oil prices may persist into the foreseeable future. The World Bank currently projects that crude oil will average US$56/bbl in 2018 and remain around US$60/bbl through 2020. The average oil price was US$92/bbl from 2010 to 2014.

Reduced oil revenues have led to an increase in public debt. If oil revenues continue to fall, it will be more difficult to service the debt. Angola's gross public sector debt (including Sonangol) is 72 percent of GDP; the non-oil primary deficit is 10 percent of GDP. As an indicator of future debt servicing capacity, public sector debt as a share of non-oil GDP is 91 percent including Sonangol, whereas the non-oil primary deficit is 13 percent of non-oil GDP[47].

Angola has set up special fiscal institutions for oil revenue management. Box 1 provides an overview of the different instruments and their objectives. While the Sovererign Wealth Fund (FSDEA), the Oil Fund (FP) and the National Development Fund (FND) are set up to promote intergenerational equity and long-term development, the Oil Price Differential Account (OPDA) was set up for the purpose of fiscal stabilization. The Sovereign Wealth Fund (FSDEA), which can invest domestically and abroad, was set up in 2012 with an initial endowment of US$ 5 billion. The Oil Fund (FP) and the National Development Fund (FND) finance infrastructure projects in Angola and abroad, while the National Development Fund (FND) finances domestic private sector projects. OPDA was set up after the Global financial Crisis to reduce pro-cyclicality of fiscal policy by channeling oil revenue into the fund when actual oil revenue exceeds budgeted oil revenue; OPDA funds serve as a fiscal buffer for the government.

Box 1: Oil wealth funds and stabilization accounts in Angola

The government has several reserve accounts and autonomous funds with different purposes and funding sources. There are three funds or accounts that derive their funding from oil revenues. These funds are:

1. **Oil Fund** *(Reserva Financeira Estratégica Petrolífera para Infra-Estruturas de Base – RFEPIEB[48], former Fundo Petrolífero – FP):* The FP receives revenues from 50,000 oil barrels per day (down from 100,000 barrels in February 2013), irrespective of oil price and budget assumptions. Its objective is to finance infrastructure projects, both in Angola and abroad. The FP is managed by the BNA on behalf of the Treasury. The size of the FND declined from US$3.4 billion end 2014 to US$2.9 billion end of July, 2017[49].
2. **Angola Sovereign Wealth Fund** *(Fundo Soberano de Angola – FSDEA):* The FSDEA was established in 2012 with an initial endowment of US$5 billion. Its main objective is to promote intergenerational equity of oil resources. FSDEA can invest its resources domestically and abroad. FSDEA's total assets at the end of the September 2017 were valued at US$5.03 billion. Asset allocation by region was as follows: Sub-Saharan Africa (48%), North America (31%), Europe (15%) and other (6%). Net fixed income represents 15% of the total portfolio, while net variable income makes up 18% of the total portfolio.
3. **National Development Fund** (Fundo Nacional de Desenvolvimento – FND): The FND was established in 2006, and aims to finance domestic private sector projects within the country's development programs. The fund is managed by the Angolan Development Bank and receives 5 percent of annual revenue from taxation on oil

[46] Proven oil reserves (end-2016) at current output levels are equivalent to 17.5 years of production at current rates (Source: BP Statistical Review of World Energy).
[47] IMF 2016 Article IV Consultation Report, February 2017.
[48] Also called Receita Estratégica Petrolífera de Infra-estrutura de Base (REPIB),
[49] Based on 2014 state general account (CGE 2014) and Oil Revenue Conciliation Reports.

activity, 2 percent of annual revenue from diamond taxation, and other resources and credit lines from the Ministry of Finance. The size of the FND at end-2014 was US$2.4 billion[50].

4. **Oil Price Differential Account** *(Fundo do Diferencial do Preço do Petróleo – OPDA):* Angola created the OPDA after the Global Financial Crisis of 2008-2009 to aid fiscal stabilization. The main objective is to deposit resources in the OPDA when actual oil revenues exceed budgeted ones, and to withdraw resources to finance the government budget in times of need. The current mechanism does not make clear when resources can be used by the government as a fiscal buffer (see Box 2 for OPDA mechanism). OPDA is managed by the BNA on behalf of the Treasury. OPDA assets were about US$4.5 billion at end-2014, recent estimates indicate that assets may have fallen below US$800 million in July 2017.

The current OPDA mechanism falls short of its fiscal stabilization objective and lacks a broader fiscal anchor. The withdrawal rules of the current OPDA mechanism lack clarity and are discretionary. Any withdrawal must be requested by the Minister of Finance and approved by the President, which limits flexibility, and fiscal stabilizers may not kick in when needed. Furthermore, the deposit rule based on oil price and quantities is rigid and does not take into account fiscal outcomes[51]. The adoption of a fiscal framework – coupled with a fiscal rule – could help limit pro-cyclicality and ensure medium- and long-term fiscal sustainability, given that some revenues are finite and non-renewable.

The OPDA lacks transparency and the legal framework is weak. The OPDA is not part of permanent legislation, which creates uncertainty about its rules and tenure. It also lacks transparency and standardized procedures, for example, the reference price (and quantities) used to determine budget transfers to the OPDA is based on an informal consensus between different government stakeholders[52]. The Oil Revenue Conciliation Report, available since 2014, provides information on the amounts transferred to the OPDA, but not on the account balance; it is also published with significant delays. There are no policies to help determine the optimal size of the fiscal buffer or the investment of the fund's resources, OPDA resources are also reported as part of the country's international reserves, which leads to double counting as both fiscal and exchange rate buffers, and this misrepresents the country's ability to withstand shocks.

[50] Based on 2014 state general account (CGE 2014).

[51] For instance, the government could incur (expensive) debt to deposit revenues into the OPDA, while at the same it is holding or accumulating assets in the OPDA. An analysis of budget outcomes for 2014 and 2015 shows that actual deficits could have been much smaller or even avoided entirely had resources not been deposited in the OPDA (World Bank 2017).

[52] Price and volume are projected by the Ministry of Petroleum for each oil field, using internal knowledge and external forecasts (PLATTS), and then sent to the tax office (*Administração Geral Tributária* – AGT), which makes tax revenue forecasts for each tax and oil field. Given the relevance of the oil price forecast in the budget, projections are discussed and approved by higher government authorities.

Box 2: OPDA mechanism

The current OPDA mechanism is outlined in Presidential Decree 83/15, which set the conditions for the inflow and outflow of OPDA resources. Resources are placed in the OPDA when the actual oil revenue exceeds the revenue projected in the budget – i.e. when the amounts resulting from equation (1) are positive. Actual revenues can exceed the budgeted figures due to higher prices and/or volume of production. The differential is calculated every month, but resources are only deposited every quarter. No offsetting between quarters is allowed. Thus, for example, if the average oil price for the entire year is below the price assumed in the budget, but the oil price in the first quarter is above that in the budget, resources will be accumulated in the OPDA during Q1 despite a revenue shortfall over the whole year.

$$\textit{Oil Price Differential} = (P_t * Q_t) - (P_B * Q_B), \quad \text{where} \qquad (1)$$

P_t = actual oil price in period t,
Q_t = actual oil production in period t,
P_B = oil price projection for budgetary purposes, and
Q_B = oil production projection for budgetary purposes.

The decree lays out the **necessary conditions for the use (outflow) of OPDA** resources:

a. Financial needs (i.e., contracting new debt) would push the debt stock to above 60 per cent of GDP;
b. Contracting new debt would lead to an excessive concentration of debt service or an increase in the country risk premium, which would affect the country's cost of funding.

The use of resources from the OPDA should not increase current expenditures by more than 10 percent in any five-year interval – unless a State of Emergency is declared – nor should it finance expenditures that have been growing faster than the average in the last two budget cycles. Furthermore, resources should be used for capital expenditures. Resources accumulated in the OPDA can be utilized only after being authorized by the President and at the request of the Minister of Finance.

Policy options

Designing an effective long-term strategy to manage natural resources is a complex task. A key challenge is to reconcile long-term strategic, national objectives with the need to manage the volatility and uncertainty of resource revenue. Policy makers need to decide how best to leverage this wealth for economic development; how to allocate finite natural resource wealth across generations; and how best to insulate the economy from large and unpredictable commodity price swings.

Angola has set up fiscal institutions to manage the uncertainty surrounding its oil wealth, these institutions should be linked to a long-term fiscal framework consisting of a long-term fiscal anchor, short and medium-term fiscal targets, strong fiscal institutions and financial stabilization buffers:

- **A long-term objective to guide fiscal policy.** Long-term anchors must reflect country circumstances and long-term policy objectives, including views on intergenerational equity, as the temporary nature of natural resource wealth creates a trade-off between how much resource wealth to consume and how much to save/invest in financial or other assets (e.g. infrastructure, human capital, or both). The long-term objective is particularly important for Angola as prospects of dwindling oil revenues and high levels of external debt pose long-term fiscal challenges. In the absence of a dynamic, non-oil economy, such a debt level would likely be much lower than today, sustained fiscal consolidation would be required to place debt on a firm downward trajectory before oil revenues come to an end. Forward looking debt sustainability analysis, with scenario analyses around different assumption for oil prices and production as well as oil and non-oil growth could help gauge an appropriate long-term level of debt and help guide the appropriate fiscal stance in the medium-term.

- **Short- and medium-term fiscal targets.** Fiscal targets should be linked to the long-term benchmark and framed in a way to avoid distortion by oil price volatility (see Box 3). For example, a non-oil primary balance (NRB) as a ratio to non-oil GDP, or government expenditure could be targeted (with safeguards to prevent the weakening of no-oil revenue). Fiscal policy would also have to be set in coordination with other policy objectives, for instance a NRB would have to take into account the absorption capacity of the economy. The fiscal target would need to be recalibrated every few years. Given the fiscal vulnerability and sustainability issues in Angola, one possibility might be to target a gradually declining non-oil deficit, to put the debt on a downward path (and thus also contribute to the build-up of the financial stabilization buffers over time) and gradually bring the non-oil deficit to sustainable levels[53].
- **Stabilization buffers to help weather large and persistent shocks.** A long-term strategy should ensure an appropriate level of precautionary savings to weather large and persistent oil price shocks. Properly-sized financial (stabilization) buffers allow for a counter-cyclical response to protect expenditure from shocks and promote long-term development. Benchmarks will need to account for the uncertainty that surrounds the returns to natural resource wealth. OPDA’s objective is fiscal stabilization, but its optimal size is undetermined, and there are no rules on how to handle excess capital.
- **Strong fiscal institutions will ensure longer-term objectives. A comprehensive medium-term fiscal framework can help to demonstrate and ensures consistency between the longer-term objective, fiscal targets and the annual budget.** Effective public financial investment management (PIM) practices are needed to ensure that government spending yields the expected growth dividends. Formal, numerical fiscal rules can enhance the credibility of fiscal policy and reduce pro-cyclicality, they also require effective PFM institutions to ensure consistency between the proposed budget and the fiscal rule; appropriate reporting and corrective action during budget execution; and adequate and transparent enforcement mechanisms.[54] If PFM institutions are not up to the task, it may be preferable to postpone the formal adoption of a numerical fiscal rule. Provided there is adequate political commitment, a first step could be shadowing the fiscal rule for policy guidance, while undertaking the necessary efforts to strengthen PFM institutions.

[53] The IMF's latest (2017) Article IV Staff Report (para. 13) recommended this approach: "Targeting a non-oil primary fiscal consolidation path of 1 percent of GDP annually over the medium term which, under current assumptions regarding international oil prices, would be consistent with eliminating the overall fiscal deficit by 2018 and placing debt on a clearly declining path."

[54] A. Corbacho and T.Ter-Minassian (2013): Public Financial Management Requirements for Effective implementation fo Fiscal Rules, in R.Allen, R/ Hemming and B. Potter (eds.):”The international handbook of public financial management, Palgrave Macmillan, 2013.

Box 3: Fiscal rules for resource rich-countries

Non-oil primary balance rules (Norway, Timor-Leste). If non-resource primary balance is viewed as a share of non-resource GDP, instead of overall fiscal balance, this could lead to a more stabilizing fiscal policy. The target would need to be set in line with long-term fiscal sustainability goals. This is especially relevant for countries with limited years of commodity reserves. For others, the target could be set to ensure appropriate levels of precautionary savings and be adjusted gradually to converge to the long-term benchmarks.

Expenditure rules (Namibia, Peru) Target the nominal or real growth of expenditures or its ratio to non-resource GDP over the medium-term. Expenditure rules can help contain spending growth during boom years. The rules can reduce the degree of pro-cyclicality and can be set to be consistent with absorptive capacity constraints. If combined with a debt rule, expenditure rules can allow for some counter-cyclicality and provide a link to debt sustainability.

Structural balance budget rules (Chile, Colombia). An alternative rule is based on a structural balance, correcting for both the economic cycle and the commodity price cycle. This approach is especially relevant to countrieswith a significant non-resource economy and where the business cycle is not highly correlated with the commodity cycle. It can help avoid pro-cyclical fiscal policy and should be set to ensure an appropriate level of net financial savings. In practice, the rule is heavily dependent on how the level of the "structural" commodity price is computed.

Price-smoothing rules (CEMAC)**.** Typically, the rule will set commodity reference prices based on a specific formula. If actual revenues exceed expected revenues, the difference is deposited in a resource fund that can be used in periods of shortfalls. However, there are also weaknesses to these rules: they are not usually linked to sustainability benchmarks;they are not able to deal with sudden large shocks; they tend to disregard other shocks (those.g., related to production and reserves of natural resources). This type of rule should be set to be consistent with a fiscal anchor and should ensure that financial buffers are appropriate.

Based on IMF (2012, 2015a,b), Ossowski, Rolando, and Havard Halland. 2016. Fiscal Management in Resource-Rich Countries. World Bank.

OPDA, FP, FSDEA, and FND should be reviewed with respect to their overall objectives and their relationship to the long-term fiscal framework. If the government decides to maintain the fiscal stabilization function for the OPDA and leave long-term capital management with FSDEA, it needs to address the question of the optimal size for OPDA and establish clear rules of how to handle any excess capital:

- As liquid assets required for stabilization purposes offer low returns and are costly to hold, OPDA should only hold sufficient assets to cover expected price and production shocks over a defined period of time. For example, OPDA's objective could be to protect the government budget from shortfalls at an 85 percent likelihood, over a period of three years.
- Excess capital beyond the optimal buffer could be used to pay down debt, which may be appropriate to ensure long-term debt sustainability in a post oil economy, or it could be transferred to FSDEA/FP for longer-term investment. If assets in the current OPDA are insufficient for precautionary savings purposes, the government could transfer liquid resources from FSDEA into OPDA; the accumulation of liquidity through debt financing should be avoided since public debt levels are already high.
- As is not uncommon for national oil funds to combine a fiscal stabilization and a savings function, combining fiscal stabilization with a savings function, by revamping OPDA with two different portfolios – a portfolio with liquid assets for stabilization, and a more long-term portfolio for future generations, may also offer benefits in better of efficiency and transparency.

Once embedded in an appropriate longer-term fiscal framework, OPDA could be restructured to allow for more flexible inflow/outflow rules; this would strengthen is function as a stabilization buffer. With a medium-term fiscal target in place, the non-oil fiscal policy would be stabilized through the fiscal rule. The OPDA could then be restructured to a *current account,* held abroad, with very flexible inflow/outflow rules to protect expenditure from shocks. OPDA deposits and withdrawals would then result from the interplay between the adopted fiscal rule and volatile oil revenue.

A restructured OPDA needs a well-defined legal framework and transparent governance. To strengthen governance and transparency of the OPDA, the Government should submit an OPDA law to parliament to support its effective operation; develop and publish an operations manual; and regularly release relevant information on OPDA assets, inflows and transfers in a timely manner (e.g. within 45 days). Annual financial statements should be externally audited and published.

Prudential investment rules for OPDA resources should be established, and managed by an independent entity. OPDA resources should be invested in highly liquid, low-risk external assets, which ideally correlate negatively with the country's economic cycle and/or the price of oil. The objective is to ensure that resources are available at short notice and without suffering large capital losses when they need to be withdrawn from the OPDA. OPDA investments should not induce pro-cyclicality. Furthermore, OPDA resources need to be managed by an independent entity such as the Central Bank or an external asset manager, which reports to the political authorities in a regular and timely manner. If the fund is to function as a stabilization mechanism and financial buffer, its assets cannot be held domestically. Investing domestically during a boom or to liquidate domestic assets during a slump, would exacerbate macroeconomic volatility.

OPDA resources should not be reported as international reserves. The OPDA is a sub-account of the Single Treasury Account of the Central Bank, and OPDA resources are counted as international reserves, thus serving a secondary purpose of exchange rate and monetary stabilization. This arrangement obscures both the amount of international reserves and the size of the fiscal stabilization buffer, thereby reducing transparency and accountability. OPDA resources are to be used solely for fiscal stabilization purposes and should not be reported as international reserves.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Establish a fiscal framework and strengthen PFM as needed.		
Set up a fiscal framework with a long-term anchor, a medium-term fiscal target, and stabilization buffer as feasible. This framework could be supported by a fiscal rule embedded in a rule-based fiscal framework (RBFF) – however this depends on the capacity of public financial management (PFM) institutions and political commitment. A fiscal rule/guideline should be tailored to this country's specific circumstances.	High	Medium-term
Restructure OPDA and improve its governance, legal framework and transparency.		
Define a transparent procedure to set reference oil price and production volume: Establish a mechanism to set the oil price (and quantities) projected in the budget, which is transparent and allows the projected value to be contestable. This can be based on a projection made by an external expert organization.	Medium	Short-term
Legislation of the OPDA: Submit to parliament a specific law on the OPDA. This law would turn the OPDA into a permanent policy. Define its objectives, operational rules and governance, transparency and accountability framework.	High	Medium-term
Increase transparency of the OPDA: Publish regular information on OPDA assets, inflows and transfers, together with information on oil prices, volumes and revenues, at least on a quarterly basis and with lags no longer than 45 days. Publish annual externally-audited financial statements.	High	Short-term
Establish standardized procedures for the OPDA: Draft a detailed procedures manual. This manual should be made public.	Medium	Short-term
Improve OPDA investment rules and accounting practices.		
Establish prudential investment rules for OPDA resources, which should be managed by an independent entity. Enact prudential rules for the investment of OPDA resources. Investment should be in low-risk highly liquid assets abroad, which are negatively correlated with Angola's economic cycle (or oil prices), and the Fund managed by an independent entity which is subject to strict reporting guidelines to political authorities.	Medium	Medium-term
OPDA resources should not be reported as international reserves. Make a clear division between OPDA resources – a fiscal buffer – and international reserves – a monetary/exchange rate buffer.	High	Short-term

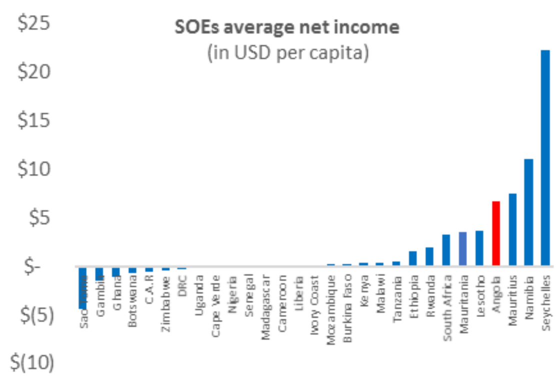
State Owned Enterprise (SOE) Corporate Governance

The SOE sector in Angola is large and its impact on the economy and budget is substantial. The sector overall is profitable, but this is largely driven by SONANGOL, Sub-Saharan Africa's largest SOE. The rest of the sector shows losses despite continued state support through price subsidies and direct transfers. It is recommended to prepare an SOE policy with clear objectives and targets for SOE performance and state ownership. This should be supported by (a) sector diagnostics and viability analysis of natural monopolies to inform necessary institutional, legal and regulatory reforms, and (b) an operational SOE reform plan that focuses on strengthening corporate governance, SOE performance (both financial and in terms of on service delivery), mechanism for tariff and rate adjustments, adequate fiscal treatment, and rationale for state ownership.

Background

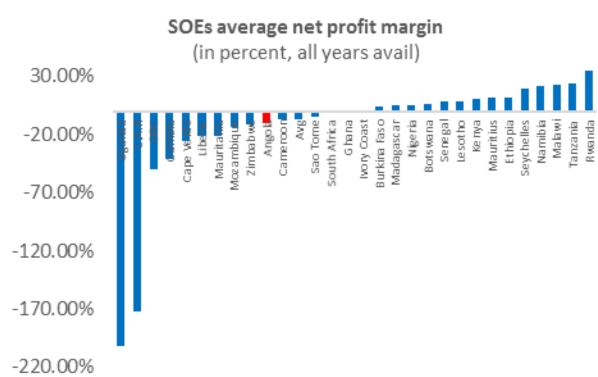
State-owned enterprises play an important role in Angola, but average performance is poor. Financial information on SOEs in Angola is fragmented and incomplete, but data from the latest ISEP (Instituto para o Sector Empresarial Público) report (2012 data) shows that 44 (out of a total of 72) SOEs generated revenues of around 30 percent of GDP, which is over twice the average for SSA. The SOE sector has been profitable on average generating US$6.6 annual net profit per capita, which was the fourth highest in the region (Figure 1), although this is driven by oil profits (Sonangol, see Box 1). However, the average performance of public enterprises is poor. Without Sonangol – which made up 91 percent of total SOE revenues in 2012 – the SOE sector would have posted net losses of approximately US$200 million in 2012 (latest data available). Also, most SOEs show net losses, as evidenced by overall negative net profit margins for most companies in most years (-9.8 percent) which is low from a regional perspective (Figure 2).

Figure 1: Angola's SOE sector has been profitable on average.



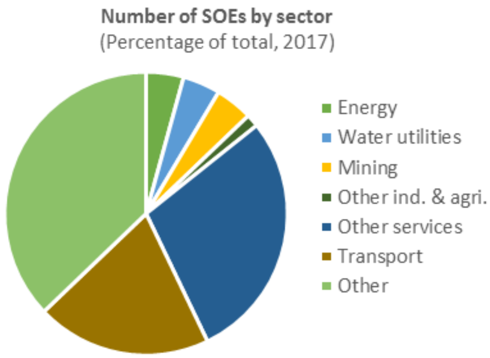
Source: Regional SOE Database (forthcoming) and author's calculations

Figure 2: This has been driven by oil profits and the national oil company Sonangol.



Source: Regional SOE Database (forthcoming) and author's calculations

Figure 3: Number of SOEs by sector



Source: ISEP (Instituto para o Sector Empresarial Público) (2012)

A large and poorly performing SOE sector not only poses significant fiscal risks, but also leads to cost-ineffective operations, low service delivery and crowds out private sector investment. International evidence suggests that performance of SOEs has improved in many cases due to greater competition, exposure to capital market discipline, and better governance practices. Yet many SOEs continue to underperform, with high economic, financial, and opportunity costs for the wider economy. Inefficient provision of critical inputs and services can increase costs for local businesses and divert scarce public sector resources and taxpayers' money away from social sectors that directly benefit the poor. Other fiscal risks arise from explicit and implicit liabilities.

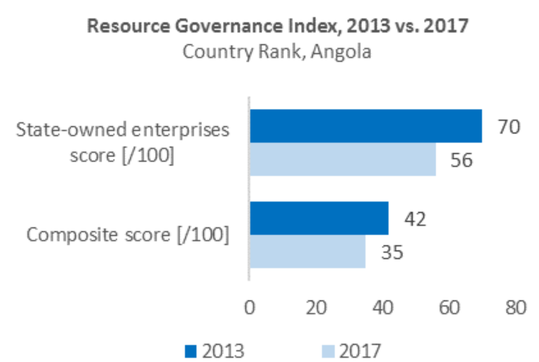
The government plan for 2017-2022 outlines measures to restructure and resize the SOE sector and to strengthen state oversight and ownership. Important advances on SOE oversight and monitoring were made with the establishment of the Angolan central ownership unit (*Instituto para o Sector Empresarial Público,* ISEP) in 2011; the new SOE framework law in 2013; and several complementary laws to strengthen SOE accountability. ISEP issued a detailed consolidated report on the SOE portfolio for the years 2011-12, but this initiative was not sustained. To right-size and restructure the SOE sector, the government plan entails measures to (i) optimize subsidy mechanisms and other financial support to public sector enterprises; (ii) gradually reduce the state presence in strategic sectors, ensuring that public enterprises are adequately capitalized and managed effectively and efficiently (in line with best management and accounting practices), (iii) continue the restructuring process of public enterprises, with a focus on structurally important companies such as Sonangol, and divest from non-viable operations and non-strategic sectors (full or partial privatization).

Box 1: Sonangol

The fall in oil prices since-mid 2014 has profoundly changed the prospects for the state oil company Sonangol. Sonangol's performance has suffered as a result of decreasing oil prices. Between 2012 and 2016 revenues were cut in half, from US$33 Bn to US$14 Bn, and net profits decreased from US$6.7 Bn to just over US$75 million in 2016. Sonangol's position is at the intersection of public policy and commercial activity, and inherits economic risks which have been more pronounced under the low oil price regime.

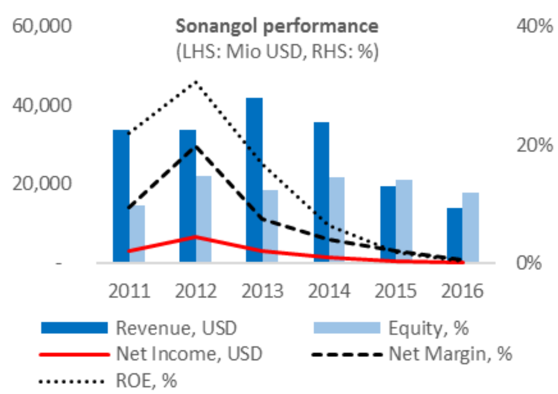
- **Fiscal risks:** There have been delays in transferring oil revenues from Sonangol to the Treasury, which complicate fiscal policy. The government assumed a Chinese Development Bank loan (US$10 billion over 2015-2017) and used the proceeds to capitalize Sonangol.
- **Commercial risks:** Sonangol deferred payments to oil majors and contractors in 2016/17, which negatively impacted relations between the national oil company and the country's most important investors.
- **Concentration risks:** Sonangol has a wide network of subsidiaries and related companies in the non-oil sector, outside its comparative advantage (including an airline, banks and insurance companies). Sonangol's presence can crowd out other investors (market entry) and could amplify adverse shocks from the oil sector through second round effects.

Figure 4: Resource governance index



Source: Resource governance index (2013,2017)

Figure 5: Sonangol performance



Source: Sonangol annual reports

With oil prices likely to remain low for a number of years, Sonangol must reconsider its strategy and ambitions. Investors will be more cautious, and exploration projects might be put on hold or canceled. For oil majors with a presence in Angola, the most crucial aspects that will influence the decision to remain invested in the country are the actual implementation of the announced legal revisions; the level of co-ordination between the newly established bodies regulating the oil industry and the level of transparency in the oil industry regulations going forward.

The current environment offers an opportunity for the government and Sonangol to refocus its efforts on defining a mandate that supports the national vision and priorities. The Angolan government has implemented a series of wide-ranging reforms which redefine the company's role in the sector. In June 2016, Sonangol launched a two-year restructuring plan to improve efficiency by focusing on core business of hydrocarbons exploration and production and increase transparency. More recently, the government established an oil sector reform plan, created a supervisory agency for the petroleum sector, and assigned a new board for Sonangol in November 2017 to streamline the operations and improvement management. Sonangol should focus on strong accounting and reporting standards and increase transparency. The board should carefully define a strategy that it can execute and adhere to it, with a focus on its oil and gas core business and limit non-core activities where it has no competitive advantage. Sonangol should further reduce its burden to the Treasury, and transfer oil tax revenue on a timely basis, and reduce its financing needs.

Policy options

State ownership arrangements, performance-monitoring

Develop an ownership policy to ensure public value. A first step to improve SOE management and to inform potential restructuring (including disinvestment) is to establish a clear vision for government ownership via an SOE ownership policy. Such a policy should clearly articulate the rationale for the state presence in each SOE or sector (for strategic, social or other objectives). The policy should further outline the core principles and performance targets (i.e. profit benchmarks for commercial SOEs, competitive neutrality). On this basis, the government should then decide if operations of existing enterprises should be continued, or if they should be restructured, privatized or liquidated.

Strengthen the central ownership unit's role and SOE performance monitoring. Evidence from the OECD shows that a strong central ownership units enhances SOE performance. The mandate and performance of ISEP should be assessed and adjusted if necessary. Its capacity to systematically monitor SOE activities and performance should be built up (access to information and mandatory flow of information from SOEs, capacity to analyze information, development of tools, training) to mitigate fiscal risks at an early stage and provide informed advice to the authorities. ISEP should also actively monitor and manage potential fiscal risks of SOEs and require SOEs to disclose their contingent liabilities.

Conduct sector diagnostic reviews and sector viability analysis of natural monopolies. The diagnostics and sector viability analysis of sectors with natural monopoly SOEs (electricity, water, housing, airports, ports, rail, etc) will inform sector restructuring which could include structural, institutional, legal and regulatory reform. The viability analysis would include willingness and ability to pay studies; analysis of capital required for infrastructure expansion; maintenance and renewal to meet specific levels of service; and reviews of mechanisms to adjust tariffs and rates for overall sector viability. This may require the introduction of legislation to remove monopolies (either immediately or after certain targets or time period(s) is met) and create a sector regulator. Opening up the sector/ SOE for private sector participation through concessions or PPPs could crowd in private investments[55] and bring in technical expertise and efficient operators for cost-efficient operational and financial performance and improved service delivery.

Conduct SOE diagnostic reviews and establish performance targets. Diagnostic reviews should target the largest SOEs, with a focus on SOEs that are structurally loss making and/or pose big fiscal risk[56]. Diagnostic reviews should be tailored to the enterprise and cover cost-effectiveness of service delivery, fiscal sustainability, the adequacy of legal/regulatory frameworks as well as of governance practices. When necessary, reviews should lead to the preparation and implementation of restructuring and/or performance improvement programs. In addition, performance indicators and targets (both financial and nonfinancial) should be developed, against which SOEs can be assessed and held accountable. SOE performance targets should eventually evolve into performance agreements[57] between SOE boards and the government to facilitate periodic performance monitoring by the ownership unit.

[55] Commercial SOEs benefit from state protection which stifles competition and blocks competition from the private sector by enjoying indirect subsidies (which are typically 4-6 times higher than direct subsidies/subventions).

[56] In 2012, the following SOEs had net losses larger than US$10 Mio (according to size): Empresa Nacional de Electricidade de Angola (ENE); Empresa Pública de Águas de Luanda (EPAL); Angola Telecom; Linhas Aéreas de Angola (TAAG); Entreposto Aduaneiro de Angola (EAA); Transporte Colectivo Urbano de Luanda (TCUL).

[57] Examples of performance agreements include statements of corporate intent, performance contracts, memorandums of understanding (MOUs), statements of expectations, shareholders' letters, letters of agreement, and business plans.

Transparency and disclosure

Increase transparency and accountability of SOEs through the regular and timely publication of financial and operational performance reports, both by individual companies and the central ownership unit. Clear transparency and public reporting requirements help mitigate fiscal risks from poor performance, structural losses, and build-ups of arrears and debt. An annual report that covers both the state ownership policy as well as the portfolio, value and the (non-) financial and operation performance indicators of all SOEs is considered best practice. The report should also include an assessment of corporate governance practices, including board and management selection, performance evaluation and remuneration. SOEs should further be subject to independent audits and audited financial statements should be publish audite on a regular basis. This would demonstrate to the public and potential investors that the state is fulfilling its ownership role and is taking appropriate action to ensure that SOEs are well managed. The authorities should further conduct independent audits for all SOEs and publish audited financial statements on a regular basis to improve accountability, transparency and reliability of company accounts.

SOE boards

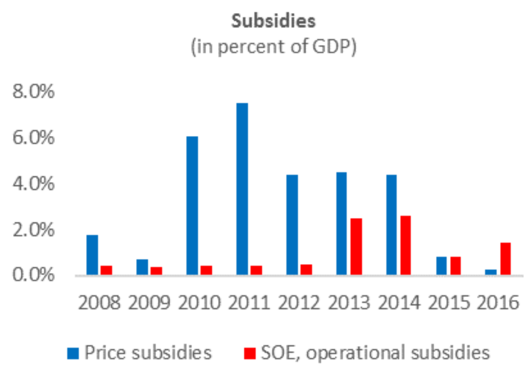
Professionalize SOE boards of directors. A common feature of SOEs around the world is a high concentration of public servants or political appointees in the board of directors. While some level of state representation is needed, diverse boards, with a mix of managerial and technical skills, are often found to enhance SOE performance. The government should therefore develop clear criteria for board selection, performance monitoring and remuneration, and put in place a transparent and competitive process to identify the most suitable candidates to manage their SOEs.

Financial and fiscal discipline

Normalize financial relations between the state and SOEs, and actively monitor fiscal risks from SOEs. Direct subsidies to SOEs are a major public expenditure and fiscal risk and need to be addressed. The GoA spent on average 0.9 percent of GDP on direct transfers to SOEs (operational subsidies, covering operational costs, salaries) between 2013 and 2016, and 2.5 percent of GDP on price subsidies (Figure 6). Actual expenditure on price subsidies has exceeded budget estimates in several years, and more recently also direct transfers (Figure 7)[58]. To account properly for financial relations between the state and SOEs in the budget process, it is recommended to identify and calculate the true cost of public service obligations and to use these as the basis for state support. All direct and indirect SOE subsidies should be clearly identified in the government budget as this would provide a more predictable and manageable fiscal burden. It will also facilitate the assessment/analysis of company performance and efficiency since all loss making or non-commercial activities would be fully covered by subsidies.

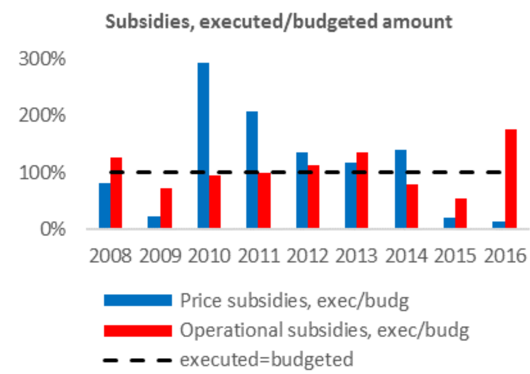
[58] Boost (2017). Price subsidies were above budgeted estimates for the years 2010 to 2014 (with an average of 79 percent). For direct transfers, executed amounts were higher in 2012, 2013 and 2016 (77 percent above budgeted amounts).

Figure 6: Price subsidies, operational subsidies/transfers



Source: Boost (2017)

Figure 7: Budget vs. execution



Source: Boost (2017)

Special issues in mixed-ownership companies

The authorities should develop a "shareholder strategy" to (i) reassess the need to maintain a minority stake in companies, (ii) explore opportunities for divestments, and (iii) provide a framework for the use of public-private partnerships (PPP) in strategic sectors. In some cases, full or partial privatization may be an option, depending on the company, sector and public service objectives[59]. Even in companies, where state-participation is considered strategic, it might be possible to achieve this with lower shares of the capital. Introducing competition in regulated sectors (which may require introduction respective regulation in existing monopoly sectors) would attract efficient operators and drive efficiencies in the sector and thereby pushing incumbents to perform better. Use of well structured management contracts could be an option to restore the SOEs' operational capacity and to bring in valuable technical expertise; empirical evidence shows a strong correlation between increased private ownership and higher net margins in state-owned companies across Africa. However, the privatization (full or partial) process requires careful management and technical capacity to be successful. When privatization is not the preferred policy option, governments could expose SOEs to capital market discipline through partial listing procedures or private debt financing.

[59] Assessments of whether to privatize should consider the economic performance of each entity - for example, profit/earnings potential, market conditions, and its relevance from a strategic or a national security point of view, and social context.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Sonangol restructuring		
Re-focus Sonangol on core business and limit non-core activities. The board should streamline operations and improve management, with a focus on its oil and gas core business and limit non-core activities where it has no competitive advantage. Sonangol should further reduce its burden to the Treasury, and transfer oil tax revenue on a timely basis, and reduce its financing needs. Sonangol should focus on strong accounting and reporting standards and increase transparency.	Medium	Medium-term
Policy and sector reform strategy		
Develop an SOE sector policy: Develop SOE policy with clear justification for state intervention, policy and social objectives, principles for SOE performance, governance and transparency.	Medium	Short-term
SOE sector reform plan: The reform plan should include actions to improve SOE performance by establishing clear and detailed targets for individual SOE's operational and non-operational performance.	Medium	Medium-term
Strengthen SOE ownership, transparency and reporting		
Strengthen the state's ownership role: evaluate ISEP performance, clarify mandate and strengthen capacity as necessary.	High	Short-term
Establishing a monitoring system: regular and timely publication of financial and operational performance reports, by individual companies and by the central ownership unit.	High	Short-term
External audit and control. Require independent audits for all SOEs and publish audited financial statements.	High	Short-term
SOE corporate governance, restructuring and privatization		
Professionalizing SOE boards of directors: developing clear criteria for board selection, performance monitoring and remuneration and to put in place a transparent and competitive process to find the most suitable candidates to manage their SOEs.	Medium	Medium-term
Sector SOE review and sector viability analysis of monopoly sectors. Sector viability analysis, to include willingness and ability to pay studies, analysis of capex and tariffs required to meet specified Levels of Service obligations, and reviews of mechanisms for tariff adjustments. Sector restructure may require creation of sector regulator.	High	Medium-term
Individual SOE diagnostic reviews. Diagnostic reviews should be completed for the largest SOEs and restructuring/performance plans prepared with clear targets.	High	Short-term
Diversification of ownership and privatization: Review SOE portfolio and identify companies with potential. Assess value and test market appetite for partial or full privatization. As an alternative to privatization, expose SOEs to capital market discipline through partial listing or private debt financing.	Low	Long-term
Improve fiscal risk management		
Normalize financial relations between the state and SOEs. Calculate the cost of public service obligations and use them as the basis for predictable and transparent state support through the budget process.	Medium	Short-term

Annex: SOE toolkit

Box 2: Key Corporate Governance Elements for SOEs

The key governance elements provide an overarching framework for the corporate governance of SOEs.

Establishing a sound **legal and regulatory framework** for corporate governance by

- Bringing SOEs under company law and applying other laws and regulations to SOEs to create a level playing field.
- Listing them on the stock markets to create capital market discipline.
- Developing modern SOE laws and regulations.
- Uniting SOEs under a national code of corporate governance or creating a specific SOE code to codify good practices.

Creating proper **state ownership arrangements** for effective state oversight and enhanced accountability by

- Identifying and separating the state's ownership functions from its policy-making and regulatory functions.
- Developing appropriate arrangements for carrying out ownership functions.
- Creating safeguards against government interventions.
- Centralizing the state's ownership functions to bring focus, consistency, and good practices to the SOE sector.

Developing a sound **performance-monitoring** system by

- Defining SOE mandates, strategies, and objectives.
- Developing key performance indicators and targets, both financial and nonfinancial.
- Establishing performance agreements between SOE owners and SOE boards.
- Measuring and evaluating performance with the goal of holding SOEs accountable for results and ensuring good performance.

Promoting **financial and fiscal discipline** by

- Reducing preferential access to direct and indirect public financing.
- Identifying, computing, and financing the true cost of public service obligations.
- Monitoring and managing the fiscal burden and potential fiscal risk of SOEs.

Professionalizing **SOE boards** by

- Developing a structured and transparent process for board nominations.
- Defining the respective roles of the state, as owner, of boards, and of management and empowering boards with core responsibilities such as strategy setting, choosing and overseeing the chief executive officer (CEO), and managing risks.
- Enhancing board professionalism through the separation of chair and CEO, development of board committees, and the like.
- Putting in place board remuneration and evaluation policies and practices.
- Providing training to members of boards of directors.

Enhancing **transparency and disclosure** by

- Applying private sector principles and international standards to SOEs.
- Improving SOE reporting and disclosure.
- Strengthening the control environment.
- Carrying out independent external audits.

Protecting shareholder rights in **mixed-ownership companies** by

- Overseeing minority government stakes.
- Promoting shareholder participation and equitable treatment of shareholders.
- Encouraging participation in shareholders' meetings.
- Ensuring representation of minority shareholders on SOE boards.
- Protecting against abusive related-party transactions.

Business Environment

A good business environment, and providing clear and predictable rules for businesses start up and operations, is critical for increasing private investment, in support to economic diversification and job creation. Those rules need to be applied consistently and impartially, enabling competitive markets and allocation of resources to the most productive activities. The Government has already taken important steps in recent years to reform the regulatory and institutional framework that underpins private sector activity. Improving information and streamlining administrative requirements, followed by expanding ICT systems that interconnect government agencies, can reduce red tape and inconsistency in the application of regulations. Reforms in trade facilitation are critical to increase the competitiveness of domestic sectors like agriculture that rely on imported inputs, and to open opportunities for export. Increasing access to credit, a major constraint for businesses, requires strengthening financial infrastructure and the debt recovery framework. Finally, foreign direct investment (FDI) can contribute to economic diversification, and would benefit from an attractive investment policy and promotion framework, with clear rules and incentives. Following the example of successful reformers, scaling up business environment reforms will require leadership at the highest Government levels, accountability, and private sector engagement in reform prioritization and implementation oversight.

Background

Economic diversification has been part of the government agenda, but targeted investment programs and reforms to improve the business environment have only had limited success. Oil exports continue to account for more than 95 percent of exports (one of the highest levels export concentration in the world), while almost all goods consumed in Angola are imported. Angola's long-term vision "Angola 2025" seeks to accelerate economic diversification and structural transformation towards inclusive growth through competitive domestic production chains, import substitution, export incentives and protection for sensitive products. The diversification strategy to date has largely been based on import substitution and discretionary investment incentives with low transparency.[60] However, as explained in the Public Investment Management policy note project selection, project preparation and implementation have not been transparent and the few industries and agricultural enterprises that have been developed are not efficient; they generally rely on subsided credit, tax breaks, favorable access to markets and foreign exchange, and other benefits (Soares de Oliveira, 2015).

Competitiveness is hampered by an unfavorable regulatory and institutional environment for the private sector. Angola ranked 140 out of 144 countries in the World Economic Forum's Global Competitiveness Index in 2014-15, the last time the country was included. It is not among the top 25 countries in Ernst and Young's Africa Attractiveness Index which measures relative investment attractiveness. A difficult regulatory environment, as well as a challenging macroeconomic framework, infrastructure and human capital weaknesses, are behind Angola's relative low competitiveness. This is further illustrated by Angola's 175th ranking out of 190 economies in the Doing Business 2018 report (Figure 1). Other indicators of regulatory quality and the rule of law, which underpin the functioning of markets, also suggest Angola's need for improvement (Figure 2). Obtaining approvals and permits is burdensome and there is little information sharing among Government entities, resulting in duplicate and/or confusing requests. A heavy bureaucracy opens opportunities for discretionary application of regulations and corruption.

Difficult import and export procedures undermine Angola's ability to join regional and global value chains. The country ranks 139 of 180 countries in the Logistics Performance Index, a comprehensive

[60] As an example, the government has initiated a targeted program (*Angola Investe* Program) for SMEs in sectors with high import-substitution or export-promotion potential (agriculture, industry, fishing, geology, and telecommunication).

measures of the efficiency of international supply chains, compared to regional peers such as South Africa (20), Mozambique (84), and Zambia (114). In particular, Angola underperforms in the customs indicator of this index, with a global ranking of 157 out of 180. Completing requirements to import and export takes longer and is more costly in Angola than the regional average[61]. Licensing procedures for each shipment, linked to tracking the flow of foreign exchange, add to the time and cost of trade. This adds to the overall high cost of doing business in Angola, undermining the country's competitiveness.

Figure 1: Angola's ease of doing business

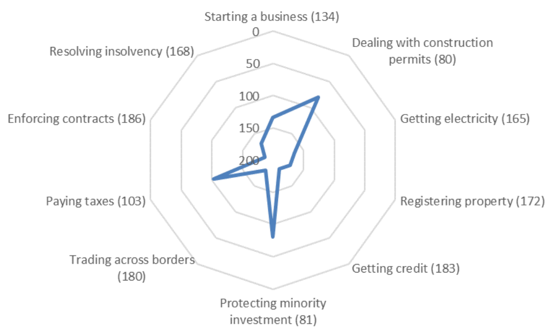
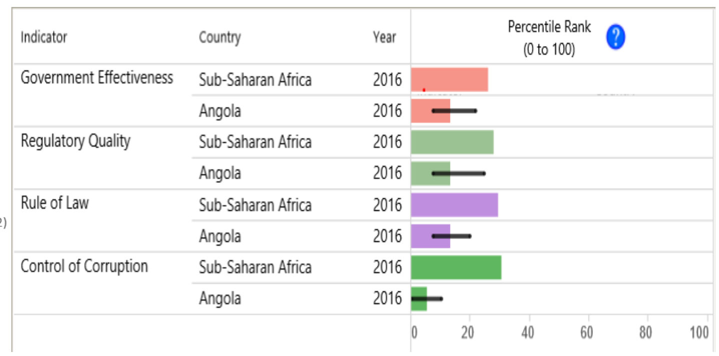


Figure 2: Angola's governance indicators



Source: Doing Business database; 2017 World Governance Indicators.

The challenging business environment constraints market competition. For markets to allocate resources to the most productive activities, institutional governance must establish sound "rules of the game" that assure the transparency, predictability and consistency needed to take appropriate business risks. Moreover, efficient business regulations support trade and domestic production diversification, by reducing the costs associated with discovery and by improving allocative efficiency. Available indicators for Angola—such as the Global Competitiveness Index (GCI) and the Operational Business Risks index published by the Economic Intelligence Unit—suggest that market players perceive a low degree of competitive pressure in internal markets and that firms believe the ability to compete may be impaired by government rules and practices that increase business risks and affect competition based on merit; in 2014/2015, the GCI ranked Angola last (out of 144 countries) in terms of competition dynamics. As Angola lacks a functional antitrust framework to tackle anticompetitive behavior, competition dynamics depend largely on the impact of Government regulation.

The authorities have made progress in modernizing the regulatory and institutional framework for businesses. A new labor law in 2015 provided additional flexibility for employers while maintaining employee protections. Significant progress was achieved in reducing the cost of business registration and eliminating the minimum capital requirement. Efforts are also underway to reform property registration; to register the state-owned housing stock; to improve the cadaster and to link it to the property registry. The corporate tax rate and the number of advance payments were reduced, alongside other improvements in tax policy and administration. The time to obtain construction permits has dropped due to an improved online application system. Overall investments in infrastructure and ICT systems have improved the availability of information and the efficiency of complying with regulations. Creating specialized commercial benches is part of the recent justice sector reform, although implementation has slowed due to budget constraints. The World Bank Group is supporting business environment reforms through two Reimbursable Advisory Services programs.

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[61] Source: Doing Business database.

Underdeveloped legal frameworks and institutional weaknesses hamper land and credit markets. Angola still underperforms in the Doing Business registering property indicators, especially in the time and quality dimensions. Access to finance is cited as the top binding constraint by businesses surveyed in the 2014 Global Competitiveness Report. According to the World Bank-supported Financial Sector Strategy, access to credit is constrained by significant gaps in Angola's financial infrastructure and the lack of a legal and institutional framework for insolvency; both are important pillars of a well-functioning credit market, especially for micro, small and medium-sized enterprises (SMEs). Moreover, credit markets are hampered by weaknesses in commercial justice. See Policy Note on Access to Finance and Financial Inclusion for a more detailed assessment and policy recommendations.

The investment policy and promotion framework approved in 2015 offers a more welcoming policy for foreign investors, but challenges remain. The private investment law eliminated the minimum amount for foreign investment but keeps a US$1m investment threshold to qualify for incentives (compared to a US$500k for domestic investors). The law provides important protections covering expropriation, repatriation, and entry of key foreign personal. However, other aspects are less attractive for investors, such as (i) maintaining a case-by-case approval process for granting tax, customs, and exchange control incentives under a negotiated contract, (ii) mandatory joint ventures with local firms in key sectors (power and water, hotels and tourism, transport and logistics, construction, telecommunications), and (iii) lack of clear rules on non-discrimination, equal treatment, avoidance of performance requirements (e.g. requirement to hire local workers), fair and equitable treatment (transparency provisions). Appropriate dispute resolution practices (international arbitration) are also lacking. In addition, a restrictive visa policy discourages investors and poses a binding constraint to the development of the tourist sector.

The institutional reform for investment promotion and facilitation is only partially implemented. The legal reform of 2015 replaced the existing promotion agency, the National Private Investments Agency (ANIP), with 4 different entities that comprise 22 institutions, including one national investment promotion agency, one technical unit dedicated to large investments (UTIP), 12 sectoral technical units for small and medium investments (UTAIPs), and 8 regional technical units (UTAs). As the myriad of investment promotion and facilitation entities is not effectively structured, supported, coordinated and capacitated, the new and partially implemented institutional framework is not delivering the expected contribution to investment promotion.

Policy options

The Government should improve information and streamline administrative procedures for businesses. Angola's citizen portal (*Portal do Cidadão*) already provides information on many administrative procedures from reserving a company name to obtaining a commercial license and the Govenrment has created Citizen Service Centers (SIACs). Expanding the transparency of information to cover all government procedures and including information on costs would reduce the time spent by firms in complying with government requirements. Information should be made available both online and at Government offices. An inventory of government procedures would help identify other unnecessary and duplicate requirements or opportunities to reduce fees.

Angola could also consider introducing performance measures and feedback loops to reduce red tape and to improve the application of regulations. Improving the exchange of information between agencies would reduce the need to provide the same information multiple times. Interconnected government systems, such as the envisioned online platform for business registration, would facilitate information exchange across agencies; it would also provide the basis for online procedures, for which Angola would need to implement the existing legal framework for electronic signatures. Well-enforced service delivery standards and mechanisms to collect, and act upon, user feedback, can contribute to reduce delays and inconsistency in the application of regulations.

Reforms in critical areas such as trade facilitation should accelerate. Reducing the time and cost to comply with import and export procedures is essential to enable more competitive domestic production, including in agriculture (since most inputs are imported). The ongoing implementation of ASYCUDA World at customs could set the stage for faster and less paper-heavy procedures. A mapping of import and export procedures and costs can help identify opportunities for streamlining customs procedures (e.g. eliminating import/export licenses; reducing fees and other charges; strengthening risk-based approaches to border compliance). An electronic single window for trade could be developed over the medium-term.

The Government should develop an effective competition policy framework and ensure that government policies and programs are designed to encourage competition. This would require a well-designed competition law; a new mandate for the *Institutio de Preços e Concorrência* (IPREC) (or the agency designated to promote competition by the law); and investments in capacity building for the competition agency. It will be important to ensure that market rules, policies and regulations account for the specific characteristics of affected markets and are designed to minimize potential distortions. Policy-makers need further be mindful that government interventions might restrict market dynamics by: (i) reinforcing dominance or limiting entry, (ii) facilitating collusive outcomes, and (iii) discriminating among competitors and/or protecting vested interests. A review of existing policies and programs should be undertaken to ensure that they complement market mechanisms and minimize distortions. A priority would be policies and programs that target access to foreign exchange, tax and tariff exemptions, subsidized credit, public guarantees, risk capital, training, and are directed at firms in priority sectors (e.g. programs to support agriculture credit, *programas dirigidos*) and/or SMEs (e.g. *Angola Investe*, PROCRED). Identifying the market failure that these programs seek to address should be identified and action should be taken to ensure these programs deliver their objective with minimal distortions to markets and incentives. The Government is developing a new program to Support Production, Export Diversification and Import Substitution (PRODESI), which can learn from experience in industrial policies globally, which call for strong fundamentals, and market-based mechanisms including sunset clauses to crowd in the private sector and avoid capture by entrenched interests. The reform of the SOE sector should also contribute to promote competition. See Policy Note on State Owned Enterprise (SOE) corporate governance.

The Government could adapt the investment policy and promotion framework to maximize FDI's support to diversification. The institutional structure, comprised of over 22 agencies, should be streamlined and adequately resourced to deliver effective investment promotion—with well-targeted efforts, facilitation, and investor aftercare functions. Moreover, the Government should consider reviewing the legal framework in line with good practice. Fewer procedural steps required to establish wholly foreign-owned, domestically-incorporated companies, and fewer restrictions to the FDI arbitration process are associated with higher FDI stock (Wagle, 2011). Restrictions on foreign acquisitions, discrimination in licensing, limits on the repatriation of earnings can deter foreign investment (World Bank, 2018). The Government could also review mandatory local content requirements and increase policy coherence between FDI linkages and investment incentives.

Sustaining a business environment reform program will require leadership, accountability, and engaging the private sector. Countries that succeeded in reforming business regulations set up strong coordination and monitoring mechanisms with clear responsibilities and oversight from the highest levels of Government. A high-level inter-ministerial coordination mechanism, established under the State Minister for Economic and Social Development, could be charged with defining reform priorities and overseeing implementation based on an action plan with clear targets. Technical working groups could be established for areas that involve several agencies, such as trade facilitation. Engaging the private sector in reform prioritization and implementation monitoring should be a priority to ensure that improvements respond to private sector needs. Any regulatory changes should be accompanied by training of officials and relevant private stakeholders, and a broad dissemination strategy.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Streamline regulatory requirements and improve access to information on government procedures.		
Improve transparency of information on government procedures, especially on costs to start a business, to obtain construction permits and sectoral licenses, and for registering property, both at government offices and online (e.g. *Portal do Cidadão)*.	High	Short-term
Implement the legal framework for e-signatures to enable online completion of procedures.	High	Short-term
Streamline procedures and introduce online platforms to complete government transactions for business registration; filing and payment of taxes; and property registration.	Medium	Medium-term
Accelerate reforms in trade facilitation.		
Complete the implementation of ASYCUDA World at all border posts.	High	Short-term
Based on a detailed mapping, streamline import/export procedures and reduce fees.	High	Short-term
Foster regional integration and reduce tariff and non-tariff barriers for regional trade.	High	Medium-term
Promote competition.		
Develop a competition policy framework.	Medium	Medium-term
Review existing programs providing credit and other support to SMEs and priority sectors to reduce restrictions in market dynamics and improve their effectiveness.	Medium	Medium-term
Reform the investment policy and promotion framework.		
Reduce visa requirements and costs (e.g. longer visas, visa on arrival, eliminate visa requirements for certain countries and visitors).	Medium	Short-term
Reform private investment legal framework to introduce good practice principles (e.g. equal treatment, non-discrimination, performance requirements, arbitration) and to remove mandatory domestic shareholding requirements; streamline institutional framework for investment promotion & facilitation.	High	Medium-term
Create an institutional framework to support business environment reforms.		
Set up an inter-ministerial mechanism for business environment reforms with clear responsibilities and a monitoring system.	High	Short-term
Improve public-private dialogue and private sector engagement in reform prioritization and monitoring both economy-wide and specific sectors.	High	Medium-term
Develop environmental & social standards and corporate governance framework for the private sector.		
Enhance Government capacity to develop and monitor compliance with E&S and CG policy framework for fast growing sectors such as Agriculture, Manufacturing, Real Estate and Infrastructure	High	Medium-term

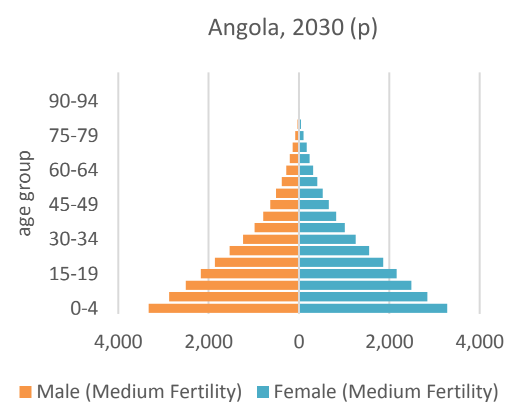
Towards More and Better Jobs

Angola has a high dependency ratio and a working-age population that is growing slowly. It is unlikely to experience a demographic dividend any time soon. The oil-driven rapid growth experienced until recently did not create commensurate employment. Young people are increasingly more educated but productive employment opportunities are few. To create more and better jobs, Angola needs to improve the investment climate to encourage entry and growth of firms. An active jobs strategy would support an adaptable labor market that balances worker protection and flexibility. Policy focus and Active Labor Market Programs are required to increase job opportunities in the largest employment sectors of agriculture and services with a focus on youth, women and the informal sector.

Background

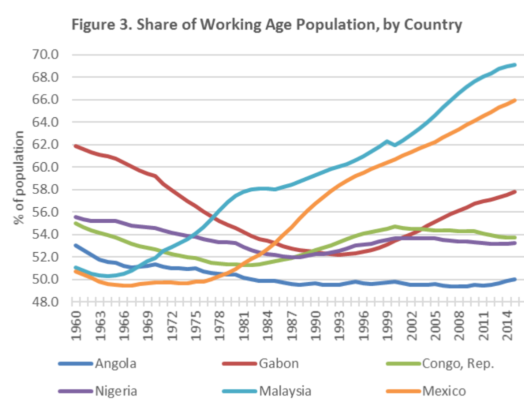
Angola's population is young and growing quickly. Angola has persistently high fertility rates, a high dependency ratio and a demographic structure that can become a liability for economic growth if not managed. Although the fertility rate has noticeably declined over the last 10 years, Angola has the 7th highest fertility rate in the world, at 6.0 children per woman. Among selected comparator countries, Angola is one of the few where the share of the working-age population (WAP), 15-64 years of age, has shrunk noticeably in recent years (see Figure 2).

Figure 1: Angola has a high dependency ratio



Source: World Bank, Jobs diagnostic (2017)

Figure 2: Share of the working age population



Source: World Bank, Jobs diagnostic (2017)

Oil-driven rapid growth has not created corresponding levels of employment. Real value added increased by 229 percent in 1992–2015, but employment increased by only 116 percent. A relatively low employment-growth elasticity (0.51) implies that improved economic performance was due to a sharp rise in labor productivity and not the result of a larger labor force. This created a large increase in real income but had little effect on employment. Net job creation between 2008 and 2014 totalled 1,538,406 (about 256,400 per year). After 'Other services', which created 1,185,580 jobs, Public Administration was the second largest job generator, with 240,473 jobs, followed by Construction (151,253 jobs). Agriculture, Manufacturing, and Transport & Communications decreased employment over that period.

There have been little gains in labor productivity. Labor productivity in Angola increased at an annual rate of 0.57 percent between 2008 and 2014. This reflects poor growth in within-sector productivity. Low levels of labor productivity in the industry sector reduced the overall rate of annual labor productivity growth by 4.1 percentage points; within-in changes in labor productivity in the agriculture and the service sectors contributed positively, adding 0.85 and 0.69 percentage points respectively (Figure 4). Gains in labor productivity came mostly from the movement of workers across sectors, which contributed 3.1 percentage points to the annual growth in labor productivity. Labor shifted from agriculture—the least productive sector of the economy—to services. The service sector increased its employment share by 9.9 percentage points from 2008 to 2014. Output per worker more than doubled from 2008 to 2014 in agriculture, but grew by only 11 percent in services (Figure 5).

Angola's population has become more educated but unemployment has increased. More than 40 percent of Angolans aged 50 to 54 have no education, this figure drops to 20 percent for 20 to 24-year olds. Available data suggest that unemployment increased from 2.6 percent in 2008 to 5.6 percent in 2014.[62] The majority of Angolans were self-employed in 2014 (51.6 percent), 37.7 percent were in paid employment and only 4.8 percent were employers. In 2008, Angola relied heavily on agriculture with 53.9 percent of employment occurring in this sector, closely followed by the services sector with 41.3 percent. By 2014 the service sector had become the largest employer with a share of 51 percent of the total workforce, followed by agriculture with 42.8 percent (Figure 3). The employment share of the more productive industry sector remains low.

Young women and men have difficulties in accessing the labor market and are increasingly self-employed. Younger workers are more likely to be self-employed and in unpaid jobs than workers aged 25 to 64[63]. Paid employment is significantly higher for men (47.2 percent) than for women (25.9 percent). Looking at the informal sector, where the self-employed often attempt to establish their own businesses, three types of constraints stand-out, particularly for young people: (i) lack of experience and skills (see also Policy Note on Education); (ii) lack of finance (see also Policy Note on Financial Inclusion) and contacts; and (iii) low self-confidence among young people to develop and implement business ideas. Furthermore, evidence points to significant constraints to starting a business (see Policy Note on Business Environment).

Angola's labor laws were reformed to increase labor market flexibility but rigidities remain in laying off workers. Deteriorating labor market conditions in part prompted reforms in labor regulations, resulting in the approval of the new General Labor Law in 2015 (Law No. 7/15, of 15 June 2015). An important innovation of the new law, which seeks to redefine the employment relationship, is the differentiation of regulation according to firm size. This is especially beneficial to micro and small firms who are the most vulnerable, but tend to create the most jobs, at least in the formal sector.

Under the new law, working time arrangements are more flexible as it allows employers to introduce different work regimes[64]. The new law is however especially burdensome for micro and small business as it envisages several days of additional paid family leave. Employers may also face rigid procedural requirements and justification thresholds that affect the number of layoffs and the speed at which layoffs can be executed. For example, third party approval by the General Labor Inspectorate, and in the case of collective dismissals also by the Ministry of Labor, is required before the employer can make a worker redundant.

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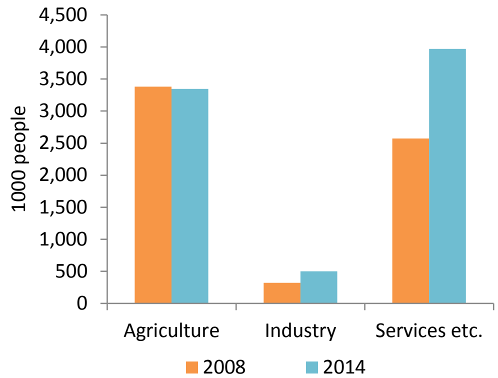
[62] The first data set comes from the household survey called the Integrated Survey of the Welfare of the Population (IBEP) 2008. This dataset was standardized by I2D2 to make results comparable across countries. The second data set comes from a 10 percent sample of the population census for 2014. The data has missing observations for earnings and informality in 2008 and 2014, and for consumption in 2014. The data differs considerably on the labor force status between 2008 and 2014. As a result, in the following the results for 2008 and 2014 are being presented separately and no comparison made.

[63] For 15-24 age group, 54 percent are self-employed, 11.2 percent non-paid employees, and 30 percent paid employees. For 25-64 age group, 51 percent are self-employed, 4 percent non-paid employees, and 39.5 percent paid employees.

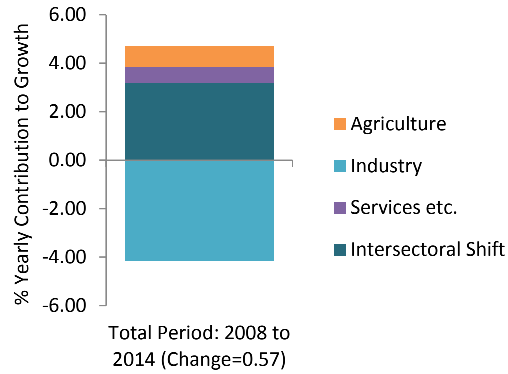
[64] For example, the duration of the fixed-term employment contract was extended, and they are now allowed for permanent tasks as well.

Figure 3: Total employment by sectors of economic activity, Angola 2008-2014



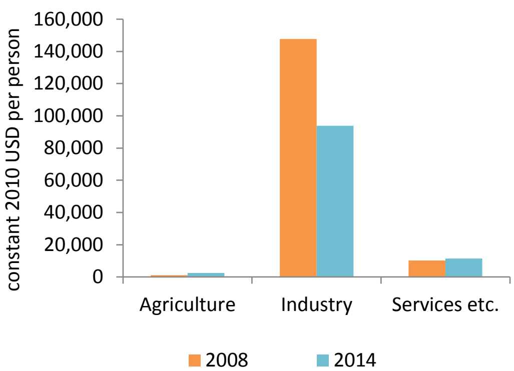
Source: World Bank, Jobs diagnostic (2017)

Figure 4: Productivity change decomposition: Annual contribution to per capita value added growth by major sector



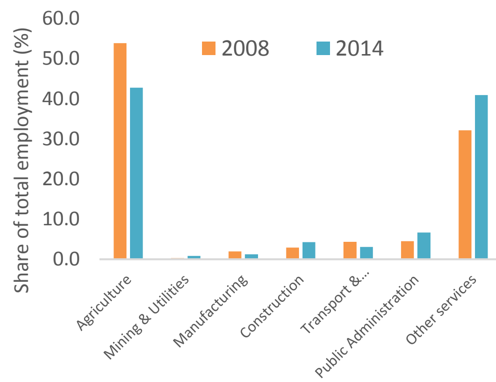
Source: World Bank, Jobs diagnostic (2017)

Figure 5: Value Added per Worker by Sector, Angola 2008-2014



Source: World Bank, Jobs diagnostic (2017)

Figure 6: Employment share by subsector



Source: World Bank, Jobs diagnostic (2017)

Policy options

Angola must create more and better jobs. The more educated younger population can help the country move from fragility and toward stability and diversification of the economy. The challenge is to create more productive jobs in the private sector for the burgeoning youth population, who are very large in number, better educated, and are not finding good jobs**.** The analysis presented here points to broad jobs challenges. Policies that have worked elsewhere to address these challenges include the following:

Policies that increase investments to strengthen a firm's demand for labor have a role in achieving different jobs outcomes. Supporting business expansion (for small and medium enterprises, entrepreneurs, family businesses, farmer's cooperatives) can lead to general improvement in labor market indicators. The sectoral/regional focus of demand-side interventions is important for creating more jobs and fostering the structural change that leads to economy-wide productivity gains. Equally, or arguably more important, such focalization is imperative to address the distributional and quality aspects of jobs challenges. Not all investments necessarily generate the number, distribution and types of jobs needed to address problems such as youth unemployment, low female participation rates, urban/rural inequality and poverty – all notably present in the case of Angola. Improving jobs outcomes entails investing in private sector development while explicitly pursuing job creation, job quality and job access for specific population groups. Examples of targeted investments are[65]: matching grants for young (female) entrepreneurs; technical assistance and financial incentives for value chain development that integrates different farmers' cooperatives with the exporting sector; cash transfers, assets and training to beneficiaries of productive inclusion programs; and business support services and/or wage subsidies to small and medium enterprises (SMEs).

The choice of intervention depends on the characteristics of the labor-intensive sector that will receive support and on the nature of challenges to job creation, job quality improvement and/or job access. The Jobs Diagnostic identified subsectors of economic activity where labor productivity is increasing more than in agriculture. It also identified sectors that are net job creators. Activities in manufacturing, and in transport and communication have comparatively high productivity, but have shed labor in the past years. Public administration and some services have a net increase in jobs, but their productivity is lagging. Construction has relatively high labor productivity and positive net job creation. Despite decreasing employment, the agriculture sector continues to be the largest employer. Programs that respond to the particular challenges of each sector and region can support the creation of more and better job opportunities to absorb new market entrants and workers from other sectors. For those economic activities that absorb workforce while struggling to enhance productivity, policies and programs should focus on investments that target both (this is the case of business-strengthening demand-side interventions, such as value chains).

Active Labor Market Programs (ALMP) can be particularly supportive of labor market integration for young people. The objective of youth-focused Active Labor Market Programs (ALMP) would be to support the productive inclusion of vulnerable youth in rural and urban areas. Such programs should include four interrelated elements:

- **Fostering Youth Entrepreneurship.** The ALMP should focus on key strategic interventions in information/skills, entrepreneurship development/coaching, and finance. More specifically, it should include: (a) information campaigns for households, youth and communities to create awareness of local business opportunities and interest in the program, it should also address cultural constraints especially for women entrepreneurs; (b) delivery of short-term skills development programs with technical, planning and life-skills development tailored to local needs; (c) support to the preparation of business plans, assisted by coaching to develop viable productive ideas; and (d) access to seed capital through grants, micro-finance schemes or small savings and credit associations). These types of interventions have proven effective in addressing constraints similar to those faced by youth in other countries: in Uganda more than 6,000 unemployed young people have started their own businesses and improved their economic livelihoods; in India more than 1,200 youth entrepreneurs have emerged, generating more than 11,700 jobs. The outcome for Angola will depend on intervention design, quality and combination of support, and a good contextual "fit". This should be informed by a detailed assessment of the youth labor market.
- **Promoting on-the-job training for first time labor market participants.** Evidence suggests that finding a good job later in life depends on how the work life starts. On-the-job training in formal and semiformal enterprises can be key to the professional development among young people.

Reform labor market institutions to create an adaptable labor market that balances worker protection and flexibility of human resources management at the firm level. This would give employer's incentives to hire workers and would incentivize workers to take available jobs. To increase flexibility in working time arrangements at the firm side, Angola may permit flexibility of working hours when required by the nature

[65] See also Policy Note on Education.

of the business. It would also seem prudent to reduce unnecessary workers' protection, especially when costly to the employer; in the case of family leave, the payment for family leave could be determined in collective agreement or individual employment contract, or could be provided as unpaid leave. Also, rigid procedural requirements for layoffs should be improved. This would allow employers to better adjust the labor force to market conditions.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Increase private sector jobs to provide productive employment		
Improve the investment climate and lower cost of doing business to encourage entry and growth by firms (see Policy Note on Business Environment).	Medium	Medium-term
Foster youth entrepreneurship, particularly in the service and agricultural sector.	Medium	Short-term
Promote on the job training for first time labor market participants, particularly in the service sector	High	Short-term
Increase job training opportunities in formal and semi-formal enterprises.	High	Short-term
Pay special attention to the constraints to job opportunities and productive inclusion of young women.	Medium	Short-term
Reform labor market institutions to create an adaptable labor market		
Increase flexibility: permit re-scheduling of working hours according to business needs.	High	Short-term
Family leave: family leave may be determined in collective agreement or individual employment contract, or may be provided as unpaid leave.	Medium	Medium-term
Procedural requirements for layoffs: employers could have more freedom to adjust the labor force according to market conditions.	High	Medium-term
Strengthen enforcement of and compliance with labor regulations.	Medium	Medium-term

Access to Finance and Financial Inclusion

An inclusive financial system with access to and use of financial services plays an essential role in supporting economic and social development. The authorities should build on recent progress, yet be cognizant of the ongoing challenges facing the financial sector. Key policy initiatives to improve financial inclusion are: enactment of reforms that broaden the collateral framework and credit infrastructure; strengthening of payment systems and promotion of retail payments (especially mobile payments); and improvement of the scope, governance, and monitoring of access to finance initiatives.

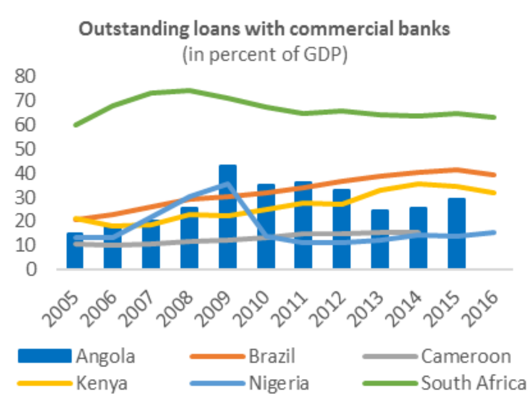
Background

Access to finance remains low, with large disparities across regions, types of businesses, and gender. Even though Angola has a relatively high number of automated teller machines (ATMs) and commercial bank branches per inhabitants, the percentage of adults with a transaction account in a financial institution is less than 30 percent. Women and adults in rural areas have even more restricted access (only 22 and 18 percent, respectively). Mobile payments, which could help reduce the rural-urban gap have not been taken up, mostly due to a lack of interest from the dominant telecom player. Luanda, with 27 percent of the population, accounts for 90 percent of total credit and 95 percent of total deposits in the entire country.

Financial literacy levels are low. According to the 2014 Global Financial Literacy Survey, Angola ranked 139th (out of 143 countries surveyed) and only 15 percent of adults are considered financially literate[66]. This compares with financial literacy rates of 26 percent for Nigeria, 40 percent for Kenya and 42 percent for South Africa.

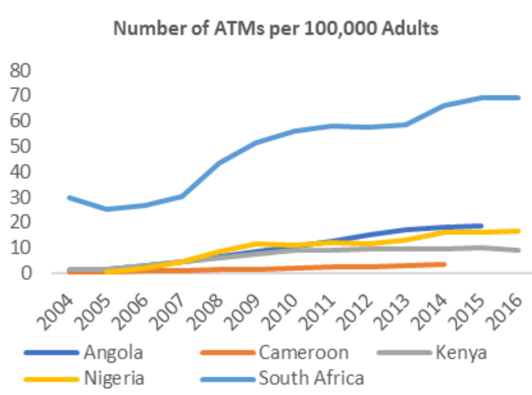
Access and cost of finance is arguably one of the most binding constraints for economic development. Based on the 2010 World Bank Enterprise Survey, firms (especially SMEs) ranked access to finance as one of the top three constraints, after corruption and access to land. The 2014–2015 Global Competitiveness Report ranks Angola 143rd out of 144 in availability of financial services and 128rd in affordability of financial services, while 2018 Doing Business Report ranks Angola 183rd out of 186 in access to credit.

Figure 1: Outstanding loans with commercial banks



Source: IMF Financial Access Survey

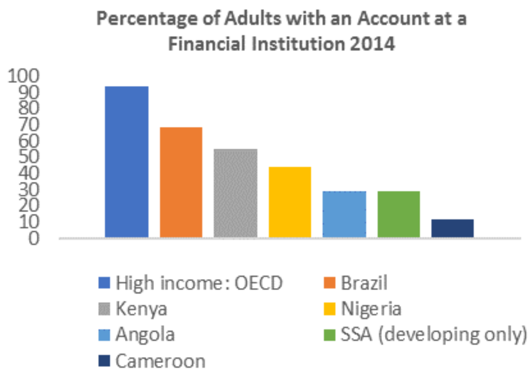
Figure 2: Number of ATMs per 100,000 adults



Source: IMF Financial Access Survey

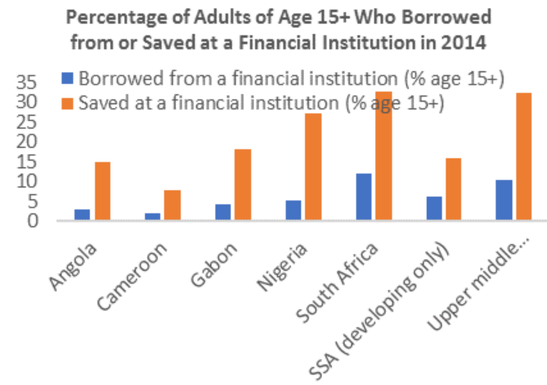
[66] Standard & Poor's Ratings Services Global Financial Literacy Survey: https://www.spglobal.com/corporate-responsibility/global-financial-literacy-survey.

Figure 3: Percentage of adults witn an account at a financial institution



Source: Global Findex

Figure 4: Percentage of adults who borrowed from or saved at a financial institution



Source: Global Findex

Banks are cautious to lend to the private sector. Private credit as a percentage of GDP has increased significantly and outstanding loans with commercial banks reached 22 percent of GDP in 2014, up from about 15 percent in 2005. Despite this significant increase, credit to the private sector still remains below the respective averages for Sub-Saharan Africa (24 percent) and South Africa (67 percent). Commercial banks keep more than a half of their domestic assets at the BNA or in government securities. The loan to deposit ratio is also relatively low, at 59 percent in 2015. By comparison, South Africa, Brazil, Kenya and Nigeria show loan to deposit ratios of 76 percent to 155 percent in 2015. Lack of corporate transparency and an appropriate legal protection framework along with high credit risk are believed to have discouraged banks from extending loans to the private sector. Banks appear to have a particularly high degree of risk aversion when dealing with SMEs and typically require high levels of liquid collateral which most SMEs lack. An additional constraint to lending to SMEs is banks' general lack of specialised appraisal skills and systems for lending to small businesses. There is also a need to build the capacity of SMEs in general business management, financial statement preparation, and business planning.

Credit growth has recently declined as a result of a more challenging environment. Foreign exchange restrictions have curtailed access to imports by trading businesses and access to inputs and equipment for other industries. This has made banks even more reluctant to lend to these market segments. Credit has contracted by nearly 23 percent in real terms since 2014 and, bank credit, as a percentage of GDP, declined from 29.2 in 2015 to 23.1 in 2016.

As banks restrict lending to the private sector, investment in Government securities has increased. Greater public financing needs have pushed up rates on government securities; 1 year government securities are at 23.9 percent, compared to 16 percent for lending rates. While treasuries are seen as a secure investment, it can expose banks to abrupt changes in government yields. At the same time, nominal rates on deposits have remained flat, resulting in negative real deposit rates due to double-digit inflation and this reduces incentives to save in the banking system.

The micro finance sector, an important tool to reach under-served markets and vulnerable groups, remains undeveloped. The sub-sector consists of one credit cooperative, one inactive leasing institution, and five microfinance institutions (MFIs) of which only three are currently operating. Although the International Finance Corporation (IFC) estimates the potential market for the sector at 1.5 million clients, the number of micro finance borrowers was less than 100,000 in 2014. While a number of international micro finance networks have attempted to establish operations in recent years, efforts were short-lived. High operating costs, shortages of qualified staff, predominance of informality, and lack of fixed addresses for many urban residents were identified as the main obstacles to develop successful operations in

Angola. The regulatory framework for micro finance is a further binding constraint, as, for example, credit cooperatives are the only non-bank financial institutions allowed to take deposits.

Financial intermediation faces regulatory, operating, and institutional constraints. According to Doing Business 2018, Angola scores 1 out of 12 (with 12 being best practice) on the Strength of Legal Rights Index. The Index measures the degree to which collateral and bankruptcy laws protect the rights of borrowers and lenders and thus facilitate lending. Angola is also one of the few economies with a "no practice" ranking for the Resolving Insolvency Legal Indicator of Doing Business. This reflects weaknesses in the existing bankruptcy law and the main procedural and administrative bottlenecks in the insolvency process.[67] In fact, Angola's legal framework on bankruptcy dates from Portuguese colonial times and is heavily focused on liquidation with little space for modern reorganization procedures.

Over the past five years, the authorities have embarked on several ambitious programs to enhance access to finance and promote financial inclusion. Important government efforts include: savings and financial education campaigns; improvements to consumer protection; restructuring of the development bank; financing schemes that extend credit lines and guarantees to small businesses; training and skills development for entrepreneurs; and improvements to the business environment, payments systems, and credit infrastructure. In 2012, BNA launched the credit information system (CIRC), a unit within the Prudential Supervision Department responsible for the dissemination and collection of information relevant to credit providers (credit information system). Although this has been an important reform to improve access to credit, there have been significant challenges related to data collection, data quality, and fair reporting to credit providers. Furthermore, CIRC is currently both the service provider of credit information products and the industry's regulator. The government has also been directly involved in the provision of micro credit, by providing loans on a subsidized basis through two state-owned banks (BPC and BCI). Many of the micro-credit programs operate on a loss basis (due to low repayment, subsidized interest rates, high operating costs) and rely on continued government support.

Policy options

Payment systems should be strengthened and electronic payments should be promoted. The BNA should promote access to payment accounts by encouraging payment service providers to offer innovative products, such as mobile payments and prepaid cards, while promoting competition and safety of the systems. Advancing mobile payments should be seen as a high priority given the ability to promote financial inclusion for the unbanked in both rural and urban areas. The use of electronic payments should be encouraged by a continuous upgrade of clearing and settlement infrastructures, promoting the development of access points, mostly in underserved rural areas, and leveraging government payments to catalyze volumes. The National Payments Council (NPC) – which is considered international best practice – should be re-activated to mobilize all relevant stakeholders and kick-off a strategic initiative to increase the access and usage of payment accounts.

The CIRC should be enhanced. Additional data sources should be incorporated into the system (such as MFIs, telecommunication companies, and utilities), while more granular data should be provided to credit providers to enhance the decision-making process. Equal and fair access to information should be ensured for all stakeholders that participate in the financial system[68]. The CIRC should build capacity with all the

[67] Effective insolvency regimes should save viable businesses and ensure that non-viable businesses can quickly exit the market, allowing the deployment of assets to more productive firms. Angola's ranking is due in part because no cases have been reported over the past five years involving a judicial reorganization, a judicial liquidation or debt enforcement procedures (foreclosure). In fact, practitioners have reported that no cases have taken place since 1975 (post-independence), indicating that "creditors are unlikely to recover their money through a formal legal process (in or out of court)"

[68] Currently only banks are reporting data and using the system, therefore the conditions are the same, but once new sources of data are incorporated into the system, similar rules of equality should apply to all.

relevant regulators on supervisory guidelines for the use of credit information by their regulated entities (e.g. banks, insurance companies, MFIs, other non-bank regulated entities).

The secured transactions regime should be improved and a collateral registry established by developing the necessary legal and institutional framework. The majority of SMEs do not have land to use as collateral, but they have moveable assets (such as machinery, inventory, accounts receivable and equipment) that could be pledged as collateral. To increase access to credit, it would be important to develop a legal system that allows businesses to use moveable assets as collateral. Setting-up an electronic registry and ensuring appropriate training for all stakeholders would be an important support measure.

A modern insolvency legal framework should be introduced, based on international best practices, to provide an orderly process for the reorganization or liquidation of insolvent entities. Effective insolvency regimes have a dual aim: to save viable businesses and to ensure that non-viable businesses can quickly exit the market, allowing the deployment of assets to more productive firms. Insolvency law provides an orderly process for the reorganization or liquidation of insolvent entities in a collective manner. Achieving the balance between debtor protection and creditor recovery is one of the main challenges that policy-makers face when designing an insolvency law. An effective insolvency regime would not only help banks in NPL workouts, but would also help promote access to finance by strenghten banks confidence in a clear process for dealing with insolvent borrowers.

The legal and institutional framework underpinning access to credit should be strengthened. As part of a broader strategy to develop the financial sector, the credit information system should be reinforced and broadened. Eventually, in line with the most advanced countries in this area, a hybrid public-private system could be established with a public credit registry at the National Bank of Angola (BNA) and a private credit bureau that includes data from supervised and non-supervised credit providers (e.g. utilities). In addition, the Government should establish a robust insolvency and creditor rights regime, including a notice-based, collateral electronic registry.

Financial sector regulations should be developed to introduce new financial products (factoring, leasing and warehouse receipts). Restrictions that currently prevent microcredit (micro-insurance/micro-housing) institutions from providing savings and other microfinance products should be lifted. This may require a revision to the Financial Institutions Law, a revised Decree on Microfinance, and amended regulations from the BNA. These regulations should be based on established industry best practices.

Given importance of agriculture for economic diversification and poverty reduction, a holistic approach for the promotion of agricultural finance is needed. This would entail identifying priority value chains and ensure the delivery of expertise and technical assistance to build capacity of smallholders and SME agribusinesses, build linkages between smallholders and agribusinesses, and develop “bankable” business plans. Reforms related to leasing, collateral registry, and warehouse receipts are directly relevant to the agriculture sector, as are risk sharing guarantees. Finally, risk mapping and insurance should be an integral part of agriculture finance promotion.

Consumer protection should be strengthened and financial education improved to increase financial literacy and capability. The authorities should conduct a financial inclusion and capability survey to establish a baseline against which progress can be measured and monitored and which allows for prioritization of policy interventions. There are several ongoing initiatives from other regulators that promote financial education, including Capital Markets Commission (CMC), Agency for Regulation of Insurance and Pensions (ARSEG), and the National Institute for Consumer Protection (INADEC) of the Ministry of Commerce. The BNA Financial Education Department conducts media campaigns and national and regional workshops to raise consumer awareness and has included financial education as a curriculum. Enhanced consumer protection in the financial sector will also help build trust and uptake of financial products.

Government should shift its support towards more market-based instruments. As a first step, the Government should evaluate and consolidate the ongoing public SME finance and microcredit programs (including *Angola Investe*) and move towards market-based mechanisms of support, working through private banks as much as possible. The Government could promote risk sharing guarantees through the Credit Guarantee Agency with commercial banks that can lower collateral requirements and encourage bank lending to the private sector; and pursue programs with private sector investors that promote linkages with SMEs and help build their capacity.

Policy recommendations

Measures	**Technical feasibility**	**Timeframe policy impact**
Strengthen the regulatory and institutional framework for access to credit.		
Develop the legal framework for secured transactions and create a notice-based electronic collateral registry at the BNA.	Medium	Medium-term
Strengthen public credit registry at the BNA and eventually move to a public-private credit information system.	Medium	Medium-term
Introduce an insolvency regime. Complete the drafting of an insolvency law and associated regulations, provide training to judges and legal professionals.	High	Medium-term
Carry out a legal and regulatory review of consumer protection and financial literacy covering banking, microfinance, and non-banking sectors (insurance, pensions, and capital markets) and develop road map to implement necessary changes.	High	Medium-term
Promote access to finance for both enterprises and households.		
Strengthen and modernize the payments system and enable retail electronic payments. Expand access to finance for the unbanked through fintech and digital financial services (e.g. mobile money).	Medium	Short-term
Expand access to microfinance and SME finance.	Medium	Medium-term
Develop financial sector regulations to introduce new financial products (factoring, leasing, warehouse receipts, collateral commodity financing and housing finance).	Medium	Medium-term
Adopt a holistic approach for the promotion of agricultural finance that tackles supply, demand, and the enabling environment.	Medium	Medium-term
Evaluate and re-design government SME finance programs such that they operate on a sustainable and transparent basis allowing for "crowding in" of private sector finance.	Low	Medium-term

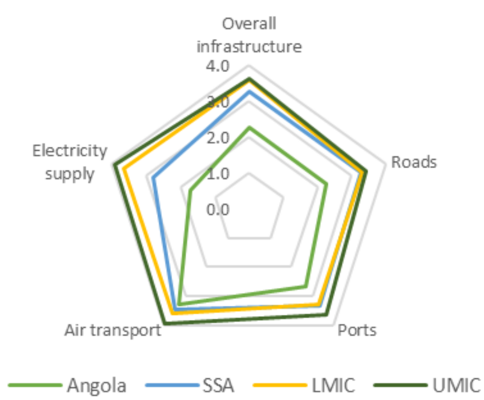
Infrastructure

Infrastructure is a critical enabling factor for economic diversification. The economy requires affordable and reliable energy, adequate access to water and sanitation, efficient transport and logistics systems to produce, move and commercialize goods and to deliver basic services. The institutional and regulatory framework needs to be established or improved: (i) to attract private financiers and operators, and to relieve the budget; (ii) to plan and build resilient, cost-effective infrastructure and enable trade facilitation for national and regional markets; and (iii) to provide access to basic services to support social development.

Background

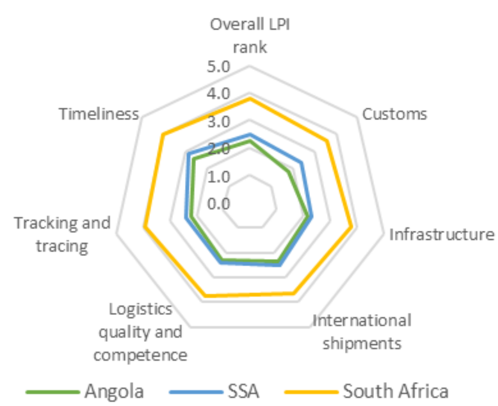
Angola has made substantial progress in developing its infrastructure, but the infrastructure gap remains substantial. As a post-conflict country, Angola has shown strong commitment to financing the reconstruction and expansion of its infrastructure, supported by a strong revenue windfall from mineral exports. Despite this effort, the infrastructure gap remains large when compared with peers. Angola's overall infrastructure score stands at 2.2 out of 4 and ranks 141 out of 144 countries according to the Global Competitiveness Report 2014–2015 (World Economic Forum), well below the SSA average (Figure 1). The report highlights that inadequate supply of infrastructure is the 3rd most problematic factor for doing business after access to financing and an inadequately educated workforce.Angola ranks 139th overall and 129th on the infrastructure component[69] (out of 160 countries) in the 2016 Logistics Performance Index (LPI) (Figure 2). While the quality of overall infrastructure has improved in recent years, the LPI score deteriorated despite significant investments (as shown in Figure 3 and 4).

Figure 1: Global Competitiveness Index (GCI), Infrastructure Pillar



Source: Global Competitiveness Index: World Economic Forum

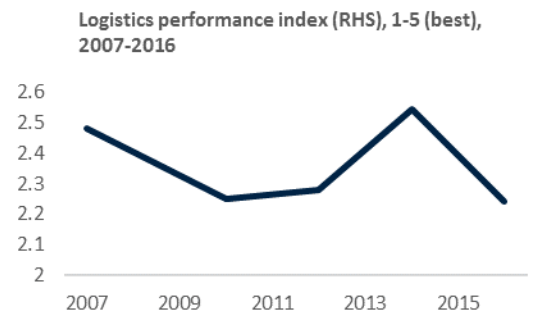
Figure 2: Logistics Performance Index (LPI)



Source: WDI: World Bank and Turku School of Economics Logistic Performance Index Surveys

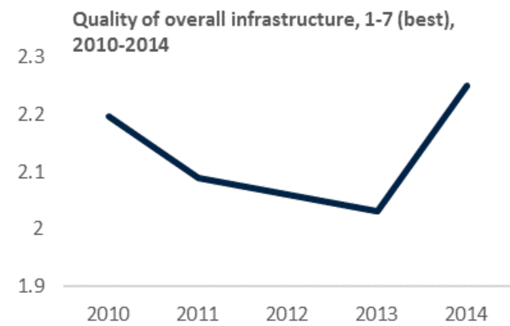
69 Defined as quality of trade and transport related infrastructure (e.g., ports, railroads, roads, information technology);

Figure 3: Angola Logistics Performance Index (LPI), 2007-2016



Source: WDI: World Bank and Turku School of Economics, Logistic Performance Index Surveys

Figure 4: Angola Global Competitiveness Index (GCI), 2010-2014



Source: Global Competitiveness Index: World Economic Forum

Private investment in infrastructure remains limited. There has been public investment investments in roads, energy, water and sanitation, undertaken with limited private sector involvement. Angola adopted the law on public-private partnerships (PPP) in 2011, and the new procurement law in 2016 added specific provisions for PPP. However, only nine projects have reached financial closure[70] since 1990 for a total investment of $2,456 million (of which 90.8 percent are in ICT)[71]. The current fiscal crisis underscores the urgency to increase private sector involvement in the infrastructure program, both to relieve budget pressures and to protect infrastructure program implementation from volatile government revenues. It is critical to understand the current gaps in the PPP framework (including institutional arrangements and procedures) to attract more private financing in the transport and energy sectors.

Transport Sector

Transportation is an important bottleneck for economic activity, including poor connectivity and transport logistics, resulting in high transport costs. Only 24 percent of classified and urban roads are paved (Box 1). Despite considerable progress in improving the main road network, the road density and connectivity in the provinces outside of Luanda and rural areas are poor. Angola scores 2.3 in quality of roads infrastructure[72] in the Global Competitiveness Index (GCI), well below the LMIC and SSA average (3.3). Furhermore, the regional road corridors are weak, and this constrains regional trade with surrounding countries and limits Angola's role as a central geographic location for surrounding (landlocked) countries.

The government is developing a comprehensive transport strategy and investment plan[73], which will help the government to shift from infrastructure rehabilitation to comprehensive sector development. The plan will formulate an overall strategy for the national transport network (including roads, railways, inland waterways, ports and airports), and identify priority projects. To date, investments in transport infrastructure are not sustainable: the exisiting maintainance framework to preserve both existing and planned road assets is neither efficient nor sustainable, a road fund was created in 2015 that covers only

[70] For greenfield projects included in the PPI database, financial closure is the date that whereby a) there is the existence of a legally binding commitment of equity holders and/or debt financiers to provide or mobilize funding for the full cost of the project; and b) the conditions for funding have been met and the first tranche of funding is mobilized. If this information is not available, construction start date is used as an estimated financial closure date.

[71] See WB Private Participation in Infrastructure data base (http://ppi.worldbank.org/snapshots/country/angola).

[72] Quality of railroad infrastructure. Global Competitiveness Index (GCI). How would you assess the railroad system in your country? From 1 = extremely underdeveloped to 7 = extensive and efficient by international standards.

[73] National Transport Sector Master Plan study, financed by the AfDB.

a small part of the total network and relies mostly on transfers from the state budget[74]. As a result, some recently rehabilitated major road assets are already deteriorating.

Transportation costs are high in Angola, and this negatively affects access for domestic road users to local and foreign markets and services, and transit competitiveness. Modernization of central highways and the railways infrastructure will help the country compete for more transit cargo in the region and capitalize on its strategic geographic position for land-locked countries. Development of main transport corridors, along with relevant logistical services, will help local producers deliver their products to local and international markets faster and cheaper. Reduced transportation costs are also expected to spur investment as investors will take advantage of lower costs.

Box 1: Angola's transport sector

Roads: Angola's road network is quite extensive with about 76,000 km of which 18,000 km are paved. Angola is also part of an international road corridor that connects to neighboring Democratic Republic of Congo and Zambia. The *Instituto Nacional de Estradas de Angola* (Angola Roads National Institute INEA) is responsible for planning and managing the primary road network.

Railways: The government operates three separate railroad lines: Luanda (425 km northeast), Benguela (1,344 Km) and Moçamedes (857 km). Those lines connect the main ports on the Atlantic Ocean (Luanda, Lobito and Namibe) to the hinterland (up to the border with DRC) and are managed by separate SOEs that report to the Ministry of Transportation. While a Presidential Decree (195/10) in 2010 opened the door to private concession for railroad operation and maintenance, there has been no uptake so far. Government has plans to build logistical platforms to connect railway lines to trunk roads. The AfDB funded Master Plan study include the feasibility of railway interconnection with Zambia.

The **air transport system** relies on 31 airports with paved runway and a new international airport is under construction in Luanda. While the latter is expected to be equipped with all safety equipment, other airports are not necessarily up to standard.

The **port system** consists of 4 main deep-water ports (Cabinda, Luanda, Lobito and Namibe) that are instrumental for international and regional trade. Regional shipping is mainly to Zambia, Zimbabwe and DRC.

Electricity sector

Angola has embarked on a significant energy sector reform, however private sector participation is still limited. In 2014, the electricity sector was unbundled with the creation of three new public operators *Produção de Electricidade (Prodel), Rede Nacional de Transporte de Electricidade (RNT)* and *Empresa Nacional de Distribuição de Electricidade (ENDE)*. The new entities are in charge of generation, transmission and distribution respectively. The oversight role as well as the autonomy of the national regulatory agency, *Instituto Regulador do Sector Eléctrico* (IRSE) has been strengthened, and its mandate was extended to the water sector in 2016 (*Instituto Regulador dos Servicos de Electricidade e Agua e Saneamento de Aguas Residuais IRSEA)*. The Government further established *GAMEK (Gabinete de Aproveitamento do Médio Kwanza)* to oversee the development and construction of large hydropower projects in the Kwanza river basin. The Government initiated a National Electricity Sector Action Plan which is entirely publicly financed – to address the electricity generation deficit and has made significant

[74] The Angolan Road Fund reported spending about 10 billion kwanzas (US$60 million) in 2017 to maintain 2,200 kilometers of national and secondary roads (a total of 76,000 km of which 18,000 is paved, AfDB Angola Country Strategy Paper 2017-2021), 17% of the amount spent came from revenues collected through road tax in 2016, with the remaining 83% of that amount coming from transfers from the State Budget.

progress in achieving the plan's target[75]. The energy sector is not financially sustainable, and it needs a transparent tariff regulation scheme: the sector needs an average tariff of around $110/MWh (in 2014 real terms) to cover its costs[76], this compares to a current tariff of $33.5/MWh.

Access to electricity and quality of electricity supply are low compared to peers. Despite these achievements, the supply-demand balance is precarious, with most businesses relying heavily on diesel generators for power. The quality of electricity supply[77] (see Figure 1) and access to electricity (Figure 5) is low when compared with LMIC and UMIC, and lags the SSA average. Also, there is a significant gap in access to electricity between the rural and urban population.

Angola's long-term energy strategy, *Angola Energia 2025*, aims to double electricity infrastructure capacity and coverage by 2025, which comes with significant planning and operational challenges. Angola could face significant challenges to doubling the electricity infrastructure capacity and coverage by 2025, as envisaged under its long-term strategy *Angola Energia 2025*[78]. The energy plan requires significant investments of around US$23.3 billion for generation, transmission, and distribution (see Figure 6). The government plans to pay for $8.9 billion with private investments, mainly in generation and distribution, however, the PPP framework is weak and there are currently no Independent Power Projects (IPPs) in place. Also, the new energy mix foreseen in the energy strategy, which relies mostly on hydropower and gas in addition to 800MW renewable energy (mainly biomass, solar, wind and mini-hydro), requires strong planning and operational capacity to deal with a high level of variable/intermittent energy sources.

Figure 5: Access to electricity, 2014

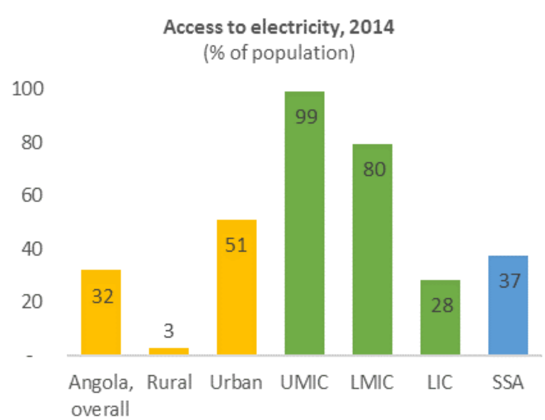
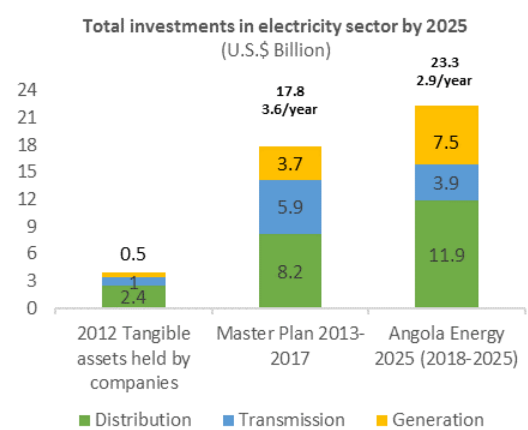


Figure 6: Investments in electricity sector



Source: World Development Indicators WDI, WB (2018)

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[75] The action plan aimed to reach 5 gigawatt (GW) of installed capacity by 2017, up from 830 megawatt (MW) in 2002. Generation capacity reached 1,7GW in 2013 and 3GW in 2017, with the recent power plants partially commissioned between June and August 2017. The planned target may be reached when the total capacity of 3,42GW currently under construction is completed by end-2018.

[76] Figures on the *Angola Energia 2025*.

[77] Quality of electricity supply, Global Competitiveness Index (GCI): "How would you assess the quality of the electricity supply in your country (lack of interruptions and lack of voltage fluctuations)? From 1 = insufficient and suffers frequent interruptions to 7 = sufficient and reliable." Angola scored 1.7 in 2014/15.

[78] The energy strategy targets 9.9GW by 2025 to cope with a 12 percent demand growth and a 60 percent electrification rate target in 2025 from a current 43 percent in cities and less than 10 percent in rural areas.

Water supply and sanitation

There is a significant rural-urban divide in access to water and improved sanitation services. The government's Vision 2025 aims for universal service access in urban areas. Although access to water and improved water services has almost doubled since the end of the civil war (see Table 1), half of the population still lacks access. This is well below the SSA and LMIC average (see Figure 7). Most of the improvements occurred in urban areas, but there has been little progress in rural areas. Even in urban areas, direct household connection for water services remains low at 32 percent, coverage has mainly increased through public standpipes and water tanker services. Almost half the population does not have access to improved sanitation, while 30 percent still use open defecation (JMP, 2015). There is no conventional sewerage except in part of the central area of Luanda, thus most urban households and businesses rely on septic tanks and pit latrines emptied by unregulated private providers.

Table 1: Access to improved water and sanitation service

Year	Access	Urban	Rural	Total
2001	Improved water source	42%	18%	27%
2015	Improved water source	75%	25%	49%
	Improved sanitation	89%	22%	52%

Figure 7: Access to improved water source, 2015

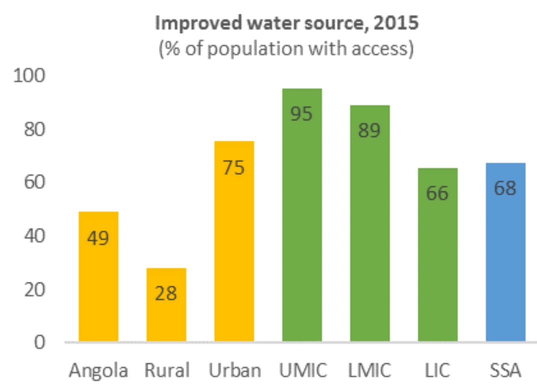
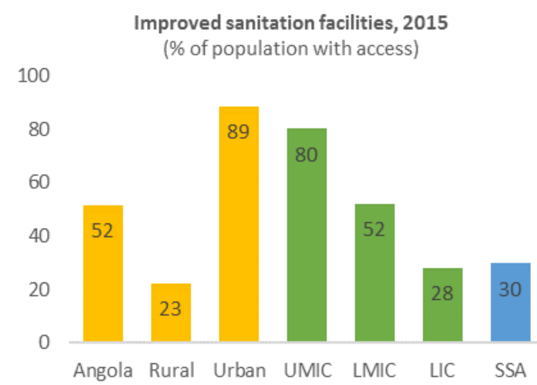


Figure 8: Access to improved sanitation facility, 2015



Source: WDI: WHO/UNICEF Joint Monitoring Programme (JMP) for Water Supply and Sanitation

The GoA has started to separate policy, regulatory, and service delivery functions to promote equitable service delivery and to ensure sustainability of investments[79]. It has also established a regulatory office for water supply within IRSEA in 2016. In the area of water resource management, the GoA formally created the *Instituto Nacional de Recursos Hidricos* (INRH—National Institute for Water Resources) in 2010, with support from the Water Sector Institutional Development Project, funded by the World Bank. Between 2013 and 2016, 16 Provincial Water and Sanitation Utilities (PWSUs) were created that now provide services in urban areas, 12 of which have water master plans to address infrastructure requirements. Sanitation master plans for eight provincial capitals continue to be updated and there is an ongoing process to introduce performance-based management contracts in a number of these utilities. The water regulator, PWSU, and the INRH have been established but are not yet fulfilling their mandates as the policy and legal frameworks are still being developed.

[79] The water law mandates cost-recovery tariffs, the professionalization of service delivery and the devolution of service responsibility to provincial governments.

The significant investment in sanitation will require a conducive institutional and regulatory framework to enable a mix of public and private financing, and financially viable utilities. Investment needs in the water sector are estimated at about US$22 billion for the next 5 years (2017-2022).[80]

Policy options

Inadequate supply of infrastructure is a major binding constraint to Angola's long-term development vision. *Angola 2025* is based on two pillars: *"Rehabilitation and development of Infrastructure to support economic development"* and *"Promotion of economic diversification and competitiveness".* Policies and programs based on the existing PPP law and used to improve development and financing of infrastructure are critical. Sector-specific issues that hinder the delivery of high quality, affordable and equitable services to the entire population also need to be addressed.

Transport sector

Imroving domestic and international connectivity. Provincial and local roads should be rehabilitated in a cost efficient and sustainable manner. The ongoing master plan should be used to identify the primary and critical road network. In parallel, the Government should complete implementation of the ongoing modernization program for highways and railways, and develop a modern logistics system. Angola needs to capitalize on its strategic geographic location as an access point for surrounding (landlocked) countries and create regional economic corridors to unlock the potential for private sector activities. A regional transport corridor development framework with DRC and Zambia could spur the activities of the Lobito/Benguela corridor.

Improve efficiency and sustainability in the transport sector. The Government needs to establish an institutional framework for the adequate preservation of investments and to provide incentives for a gradual engagement of the private sector in the management and maintenance of transport assets. The following measures would support this agenda:

- **Review and benchmark the economic and operational performance of transport SOEs** in the rail, port and airport sectors to determine the level of efficiency and need for reform.
- **Improve and operationalize the PPP arrangements for the transport sector** (see cross cutting issues below).
- The rehabilitation efforts for the transport infrastructure, for roads and railways, requires adequate financing for maintenance in addition to a modern asset management system. Based on the results of the ongoing master plan study, the primary and critical road network and associated maintenance standards need to be defined to estimate required annual financial resources for its upkeep. The government needs to establish a **sustainable financing mechanism for the Road Fund** that relies less on the government budget and is mainly funded through revenues from road user charges (e.g. fuel levy, vehicle license fees).
- Define and create a strategy to scale up current **performance based contracts for maintenance**.
- **Review and benchmark economic and technical regulations of land freight services**, including truck and rail services.

[80] Global Infrastructure Outlook, investment forecasts for Angola, https://outlook.gihub.org/countries/Angola

Electricity sector

Improve and operationalize PPP arrangements for the electricity sector (see cross cutting issues below). Angola needs to attract private investment to help fund the $23.3 billion of investment required to achieve the government's vision for 2018-2025. The capacity of the energy utilities as power purchaser "offtaker" in the sector should be strengthened by improving its technical and financial performances. Capacity building is provided on the regulatory side by donors; sector bodies require improved capacity to undertake bidding processes and negotiate power purchase agreements (PPA) tif they are to mobilize more than a $1 billion of private financing per year. A feed-in-tariff mechanism needs to be considered, given the ambitious plans for 800MW renewable energy generation capacity (excluding hydro power).

Define a rural electrification strategy and the adequate institutional set-up to achieve universal access. Extension of access to electricity requires, in addition, last mile connections and off-grid solutions for remote areas in collaboration with private players; this is in addition to transmission and distribution investments. The electrification strategy targets provincial capitals and municipal townships first (expected to be 97 percent of the 3.7 million household clients in 2025), mainly through grid expansion. Increasing the customer base by a factor of three by 2025 will require a comprehensive strategy and action plan, and the technical and commercial capacity of the distribution utility will need to be strengthened. A specific rural electrification agency could be created to implement the electrification strategy laid-out in the agenda 2025.

Establish a coordinated power sector planning process after the unbundling of the sector, and clarify the role of the different stakeholders in the process**.**

Strengthen regional connectivity. Angola is currently a non-operative member of the Southern African Power Pool (SAPP) but interconnection lines are planned through Namibia and the Democratic Republic of the Congo to allow cross border energy trading. Regional cooperation in power projects would also help to unify the national transmission system –currently fragmented into three separate grids – and allow for energy exports and imports to mitigate energy supply risks.

Water supply and sanitation

Strengthen capacities of PWSUs in the areas of planning, operation and commercialization of water services, while ensuring their financial viablilty. The nascent nature of PWSUs is one of the most urgent institutional challenge for the sector. PWSUs need to develop institutional structures with the capacity to manage utilities effectively. There needs to be greater focus on service delivery, asset management and planning, efficiency, comprehensive financial management, and cost recovery. Commercial and operating capacity should be strengthened, both in terms of human resources and system capacity. Investments in financial management systems, billing software and operational reporting systems are also needed.

Develop and implement a national sanitation strategy to ensure adequate access to water and sanitation and support social development. The rapid expansion of water supply requires adequate sanitation systems.

Cross cutting issues

Establish an operational PPP framework. The Government may wish to revisit existing legislation and procedures to ensure that an appropriate operational PPP framework is in place to facilitate (i) PPP project preparation, (ii) standardization of documents, (iii) the treatment of unsolicited proposals, and (iv) efficient procurement and contract management. The establishment of PPP units at the level of technical ministries could also be explored to assist the Government in developing a PPP pipeline.[81]

Undertake sector diagnostics focusing on priority sectors (energy, transport and water) with a view to address bottlenecks for private sector participation.

Improve the regulation of the energy and water sector. Minimum quality of service standards should be defined and incentives should be put in place to enhance the performance of utilities. IRSEA should be charged with the enforcement of service standards and should also take on the technical oversight of the market to ensure that operators are complying with contractual obligations.

Implement a transparent tariff regulation scheme for utility tariffs (electricity and water), with clear procedures for timely adjustment and revisions to ensure cost-reflective pricing. The institutional and regulatory framework needs to be established, and the role of IRSEA, utilities and government bodies (Ministry of Finance, technical ministries) should be clarified; open consultation processes and clear time schedule would help ensure transparency among all stakeholders. As part of the tariff setting process, an effective **targeted subsidy mechanism** should be designed to protect low income households[82].

Vocational training and human capacity building. The Government should conduct a needs assessment of existing institutions to define a comprehensive institutional development and capacity building strategy.

[81] The PPP Knowledge Lab provides key information on public-private partnership readiness, laws, units, and infrastructure indicators for Angola. The asssement there can be used to inform reforms to Angola's existing PPP framework: https://library.pppknowledgelab.org/documents/3945/download?ref_site=kl

[82] Subsidized tariff for a first block of energy covering basic needs of poor households.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Transport sector		
Put in place a regime to prevent truck overloading, define a sustainable financing mechanism for a Roads Fund, and a strategy to scale up performance-based maintenance contracts.	High	Short-term
Define a regional transport corridor development framework in collaboration with DRC and Zambia.	High	Medium- term
Identify the primary and critical road network and define associated maintenance standards to establish the level of annual financial resources needed.	High	Medium-term
Review and benchmark (i) economic and technical regulations for land freight services, including truck and rail services, and (ii) the economic and operational performance of transport SOEs in the rail, port and airport sectors.	High	Short-term
Energy sector		
Strengthen the performance of electricity utilities and ensure their financial viability.	High	Medium-term
Define a rural electrification strategy.	High	Medium-term
Establish a coordinated planning process after the unbundling of the energy sector.	High	Medium-term
Water sector		
Define and implement a strategy to improve access to sanitation services and prepare a program to increase access to water services in rural areas.	High	Medium-term
Strengthen Provincial Water Utilities and ensure their financial viability.	High	Medium-term
Regulation of the electricity and water sector		
Establish a transparent tariff setting mechanism, design an optimal/targeted subsidy mechanism, and monitor utilities' performance on a regular basis.	Medium	Short-term
Strengthening IRSEA capacity and its procedures.	Medium	Medium-term
PPP framework		
Undertake sector diagnostics for energy, transport and water. Operationalize PPP framework in those sectors by improving existing procedures and methodologies and by establishing dedicated PPP units.	High	Short-term
Vocational training and human capacity building	Medium	Medium-term

Information and Communication Technology (ICT)

ICT has the potential to be a catalyst for inclusion, efficiency, and economic growth in Angola. Although Angola's mobile sector has shown remarkable growth, it lags regional peers in terms of market penetration. The availability of high-speed internet is limited. Digital clouds and online services are yet to take scale. The Government may want to prioritize a policy review of the ICT sector of Angola, with a lens of supporing a digital economy, improving the country's telecommunications infrastructure, attracting private investment, using ICT in government, promoting technology and innovation for Angola's cross-sectoral development, and safeguarding people's digital information. A market assessment of Angola's digital economy with a focus on cross-sectoral development, and a diagnostic of Angola's preparedness for cybersecurity can provide inputs to policymakers on ways to advance the ICT sector.

Background

Angola has potential to tap a growing digital economy, with the aim of creating jobs, generating economic output, and raising export revenue, while promoting inclusion, efficiency, and innovation: Worth US$11.5 trillion globally in 2016, the digital economy comprises 15.5 percent of global GDP and has potential to transform key industries.[83] This digitization across sectors of the economy is having a transformational impact on development, boosting access to information, expanding access to government and financial services, and connecting businesses and individuals to markets. Countries in Africa have been at the forefront of using digital technologies to create innovative solutions to development problems, investing in the potential of mobile payments, using drones for delivery of public services, and creating technology hubs for young entrepreneurs. The digital economy provides an opportunity to leapfrogging over older technologies and business models.

Angola is home to a nascent digital economy, of local ICT firms, and use of ICT by firms and government, though would rely on modern digital infrastructure of mobile phones, internet, and digital clouds: The use of ICT by the private sector in Angola is limited. Angola ranks 145th out of 148 countries in the use of ICT by local firms, 146th in innovation, and 144th in business-to-business internet use.[84] An unfavorable business and investment climate, as well as insufficient skills are binding constraints for the growth of Angola's digital economy.[85] Angola has to further modernize its digital infrastructure, promote a competitive, free-market economy for the ICT sector, and support training for high-level IT skills amongst the country's youth beyond basic digital literacy programs currently being introduced. Angola has the opportunity to grow its digital economy to create jobs for the youth, foster local skills and content development, and generate economic output and export revenue.

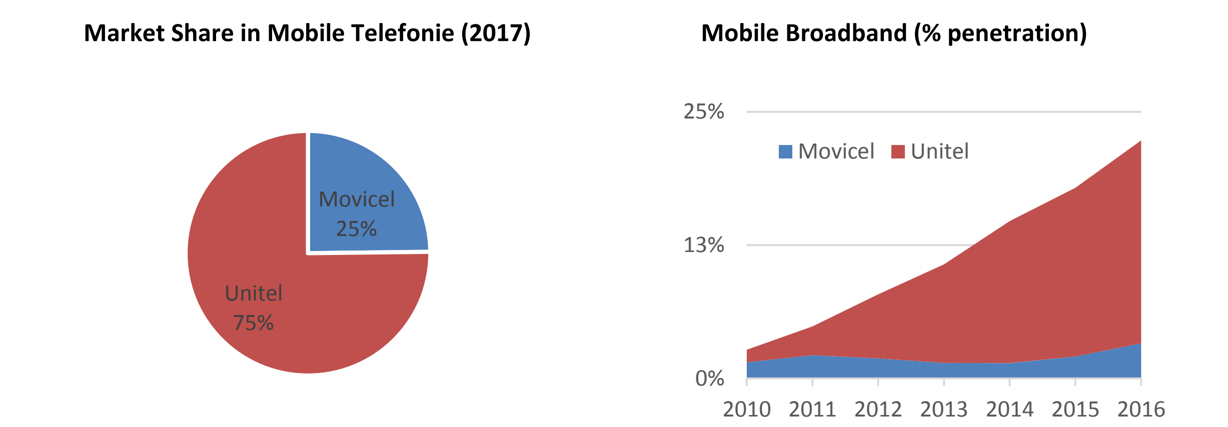
Angola's mobile sector has shown remarkable growth, but it faces limited competition and lags behind regional peers in market penetration. The iberalization of the telecommunications market in 2001 triggered fast growth, particularly in the mobile sector. The Government passed the Basic Telecommunications Law and awarded a GSM license to *Unitel* in an effort to introduce competion with *Movicel*, which then was owned by the incumbent operator, *Angola Telecom*. In 2003, Angola Telecom spun off *Movicel* into a separate mobile subsidiary, and partially privatized the subsidiary in 2009; Angola Telecom continues to hold a 45 percent stake in *Movicel*. Mobile phone penetration has reached 55 percent in 2016, compared to 74 percent in Sub-Saharan Africa, or 142 percent in South Africa (see Figure

[83] Huawei Technology and Oxford Economics. 2017. *Digital Spillover: Measuring the true impact of the digital economy*. Available at http://www.huawei.com/minisite/gci/en/digital-spillover/files/gci_digital_spillover.pdf (last accessed February 15, 2018).
[84] see World Economic Forum's Global Information Technology Report 2014.
[85] According to Doing Business 2017, Angola ranks 182 out of 190.

1). The mobile market displays limited competition, with *Unitel* holding 75 percent of the market and *Movicel* the remaining 25 percent. In 2018, the Government announced privatization of Angola Telecom.

Broadband availability is very limited in Angola, and is necessary for a digital economy. The Government has taken significant steps to improve access to high-speed internet (or broadband), albeit results have been limited. To build international links, Angola connected with the undersea international cable SAT-3/WASC in 2002. Initially, only Angola Telecom had access to the cable. In 2009, the Angola Cables Consortium was set up to manage international linkages and it invested in additional fiber infrastructure: the West Africa Cable System (WACS) and the South Atlantic Cable System (SACS). The Government completed deployment of the north-south Angola Domestic Cable Network System (ADONES) undersea cable in 2009.[86] To carry internet traffic domestically, Angola has built about 25,000 km of optical fiber network. By 2012, a nationwide fiber program deployed 10,000 km of backbone optical fiber to connect to provincial capitals. By 2014, all provincial capitals and 343 locations nationwide were connected. In 2017, 12 operators were offering broadband services in Angola, including 10 internet service providers (ISPs) and two mobile operators. Despite these efforts, only 0.5 percent of the population were using fixed-broadband (such as DSL, or wired internet) and 22.3 percent mobile internet (such as 4G) in 2016 (see Figure 1). The fixed broadband market is largely dominated by *Angola Telecom*.

Figure 1: Telecommunication in Angola



	2010	2011	2012	2013	2014	2015	2016
Mobile Subscribers (per 100 people)							
Angola	48.1	59.8	61.4	61.9	63.5	60.8	55.3
South Africa	97.9	123.2	130.6	145.6	149.2	164.5	142.4
Sub-Saharan Africa	44.4	53.1	59.7	66.0	70.9	76.1	74.4
World	76.5	84.2	88.5	93.1	96.7	98.2	101.6
Fixed Broadband Subscribers (per 100 people)							
Angola	0.1	0.1	0.1	0.1	0.3	0.7	0.5
South Africa	1.4	1.7	2.1	3.1	3.2	2.6	2.8
Sub-Saharan Africa	0.2	0.3	0.2	0.3	0.4	0.4	0.4
World	7.9	9.0	9.4	9.9	10.3	11.6	12.5
Mobile Broadband Subscribers (per 100 people)							
Angola	2.7%	4.9%	7.9%	10.7%	14.8%	17.9%	22.3%
Movicel	1.5%	2.2%	1.9%	1.5%	1.4%	2.1%	3.3%
Unitel	1.2%	2.7%	6.0%	9.2%	13.3%	15.8%	19.0%

Source: World Bank (2018), GSMA (2018)

[86] Source: Telegeography (2018).

The Government has actively promoted the use of ICT in government services. In 2005, the Government set up the National Centre for Information Technology (CNTI) to coordinate the use of information and communication technology (ICT) within the government. CNTI established a *Strategic Plan for eGovernment*, which was updated it in 2013 to guide strategic initiatives during 2013-2017. The strategic plan outlines four areas of interventions and ten programs (see Figure 2). The Government has since established an official government portal that includes Ministries and provincial governments; promoted online networks for knowledge and innovation within the public administration; advanced digital literacy; and established government data centers. Despite these efforts to promote the use of ICT in government, Angola ranks in 142nd place (out of 193) on the UN's e-Government development index in 2016. While Angola's ranking has improved in recent years, it continues to lag regional peers including South Africa (76th), Botswana (113th), Kenya (119th) and Namibia (125th).

Table 1: Strategic Plan for eGovernment (2013-2017)

Lines:	Programs:
A. Focus on the provision of services to all citizens	1. Centralization of citizen services
	2. Communication and Information to citizens
B. Improve government efficiency and efficacy	3. Shared services
	4. Modernization of systems and processes for citizen support
	5. Systems and processes to improve public administration internal operations
C. Capacity building for civil servants and public institutions	6. Online Civil Servant
	7. Mobilization and skills development for public administration
D. Ensure Government IT interoperability and security	8. Public Administration Interoperability
	9. Cybersecurity
	10. Services and equipment for public administration communications

While broadband is growing in Angola, it has yet to trigger digital transformation. The ICT sector in Angola has experienced some growth, but Angolans have not yet adopted ICT in their daily lives or in business operations. This is partly due to insufficient availability of broadband internet connections, but lack of competition lead to insufficient service quality with regards to speed and network availability. Relatively high prices of broadband internet packages, particularly in more remote areas, further restrict the uptake.

Angola needs to achieve a critical mass of users for digital services. Although mobile phones are used more widely and international bandwidth is becoming available, Angola has yet to scale up the adoption and use of digitally enabled services. Internet use is low and according to ITU, only 19 percent of Angolans uses the internet; albeit up from 10 percent in 2010. With respect to use of virtual social networks (e.g., Facebook, Twitter, LinkedIn) for professional and personal communication, Angola ranks 123rd (out of 148) with a score of 4.8 out of 7, indicating significant use for this purpose.[87] However, by 2012, there were less than 650,000 Facebook users in Angola.

[87] see World Economic Forum's Global Information Technology Report 2014.

Policy Recommendations

The use of ICT in service delivery can offer productivity and efficiency gains across several economic and social sectors in Angola, including agriculture, health, education, transport, and financial services. The market for these services requires local content, services and applications. The main hurdle in the deployment of e-enabled services is the availability of affordable high-speed internet. In addition, good financial infrastructure is needed, in the form of digital payment services and financial access points through-out the country. The development of local talent and skills plays an important role in creating local services and solutions. The Government of Ghana has made strides in this area, by employing the use of ICT to automate taxation and business registration, and is currently working to use ICT to improve education and healthcare. Similar developments in Kenya and Rwanda are noteworthy, where respective governments are working to use ICT for improved service delivery. The Government of Angola may consider a policy review of its ICT sector, with a focus on ICT infrastructure, digital services, cybersecurity, and digital economy, as a way to inform the country's policymakers on policy reforms necessary to further develop the ICT sector of the country.

The Government should aim to ensure that everyone in Angola has access to affordable, quality high-speed internet. Although the Government has supported improvement in ICT infrastructure, including by building fiber networks, further work is needed to increase competition in the mobile market, facilitate private sector-led development of fiber backbone throughout the country, support open access policies and infrastructure sharing for broadband internet, and ensure universal access to broadband internet including in remote and rural areas. Internet remains a development challenge across Africa, with the need to open up access and markets, and to build the necessary telecommunications infrastructure. Several countries in Africa, including Kenya, Tanzania, Guinea, Liberia and Sierra Leone, have taken a staged approach to broadband development, starting with achieving good access to international links for high-speed internet (while replacing cumbersome and expensive satellite-based connections). The next step remains leveraging existing fiber backbones and building new ones to increase capillarity of broaband networks and extending the benefits of high-speed internet throughout each country. The Government of Angola may prioritize the development of broadband, by using a mix of policy reforms, public-private partnerships, and a supportive environment for private sector investment, including foreign direct investments. The Government of Angola could consider partnering with independent private sector operators, on a transparent, competitive basis, to commercialize and expand existing state owned fiber assets to enable wholesale open access networks that can be accessed by all operators on a non-discriminatory basis, in conformance with open access policies, and with a competitive market place.

The Government should promote the use of ICT in government, to support good governance, efficient delivery of services, and to facilitate private sector development. Despite some some progress in digital government initiatives, further efforts are needed to achieve digital delivery of public services. The Government could promote e-government, e-commerce and e-society applications so that citizens and businesses may interact with the government digitally, without the need for face-to-face contact. Cost savings can be achieved by focusing on cross-cutting infrastructure; facilitating the deployment of shared communications infrastructure; automating revenue, customs and business registration; and digitizing government records. By implementing an aggressive e-transformation agenda, the Government can promote growth of its digital economy by outsourcing part of its e-government services and introducing more transaction-based e-services in the country. The local digital economy could benefit from this transformation, with the Government itself becoming an engine for the development of the local industry.

Angola needs a National Cybersecurity Policy and Strategy to strengthen its capacity in cybersecurity. Cybersecurity, to protect data privacy and consumers, and to prevent financial fraud, is paramount to ensure trust in the digital economy. The growing use of ICT applications and services requires an effective approach to cybersecurity, including mitigation, prevention, protection, awareness, detection, response, and recovery. This will require: (i) updated legal and regulatory measures on cybersecurity; (ii) the designation of a lead government agency responsible for cybersecurity; (iii) timely execution of actions dealing with instituting, managing, and strengthening cybersecurity; (iv) definition of roles and responsibilities for respective government agencies; (v) capacity building and public awareness raising; (vi) a framework for cooperation within government, with the private sector, and with international partners; and (vii) adequate budgetary allocation for cybersecurity. Since cybersecurity poses a new development challenge, countries in Africa are starting to build effective strategies to prepare for cybersecurity. The World Bank has partnered with governments in Ghana, Burkina Faso, Armenia, Kosovo and Myanmar, to carry out a diasnotic of cybersecurity preparedness in each country, and to prepare a strategy for strengthening cybersecurity, including with legislations, institutional strengthening, and operational preparedness. The Government of Angola may consider a diagnostic to assess the country's preparedness and develop its own methodology to protect digital information in the country.

The Government should foster a vibrant digital economy where ICT is used to develop local skills and generate jobs for the youth. The ICT sector can be used as an enabler for increased economic competitiveness and job creation in Angola. Today, the digital innovation ecosystem in Angola is still in an early stage of development. The Government should consider the following: (i) introduce appropriate guidelines on digital/ICT skills curriculum for all levels of education and for vocational training; (ii) help match demand and supply for IT jobs within Angola; (iii) support innovation and start-up development in partnership with the private sector; and (iv) implement enabling policies and systems for digital commerce and related digital payment services. India serves as a good example of a country where digital economy, fueled by a growing IT-services industry, has created economic output, export revenue, jobs, and social inclusion, including for women and minorities. Within Africa, Ghana, Mauritius, Kenya, South Africa and Senegal have worked to develop digital economies that can outsource IT-enabled services, according to 2017 AT Kearney Global Services Location Index. The World Bank is currently working with the East African Community (EAC) to develop a regional program for growing digital economy in participating countries. The Government of Angola may consider a review of its digital economy as a first step, in order to develop necessary policies, support skill development, and promote the local industry.

Policy recommendations

Measures	Technical feasibility	Timeframe policy impact
Prepare a policy review of the ICT sector of Angola, with a focus on digital economy, digital infrastructure, digital services, and cybersecurity.	Medium	Short-term
Carry out a diagnostic of cybersecurity in Angola.	Medium	Short-term
Undertake an assessment of digital economy in Angola.	Medium	Short-term

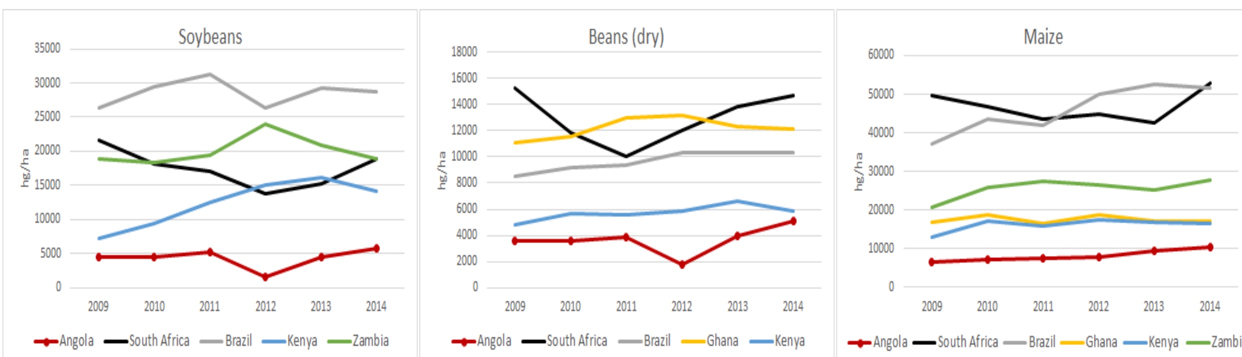
Agriculture

Agriculture is the main opportunity and government priority for diversification of the economy. To realize this potential, sector competitiveness needs to be improved. This requires a shift in agricultural policies and programs to not only enhance the quality and supply of public goods and services but also to to improve incentive structures for investments in agriculture and agribusinesses. As high agricultural tariffs preventing the sector from joining regional or global value chains, there is also a need for agricultural trade policy reform. Streamlining procedures for obtaining and transacting land-use rights would also allow to bring more state-owned land into productive use.

Background

Agriculture development is a key component of Angola's strategy to diversify the economy, to promote export competitiveness and to ensure food security, but the sector has underperformed in recent decades.[88] Even though agriculture accounts for 10 percent of GDP and employs over half of the workforce,[89] only about 8 to 14 percent of arable land is currently in use. Agricultural production shows signs of underperformance. After the departure of the Portuguese, in the 1990s, Angola was producing less than 1 percent of the volume of coffee it had produced in the early 1970s, while production of cotton, tobacco and sugar cane had ceased almost entirely.[90] Yields in several crops remain low compared to other countries. Figure 1 illustrates Angola's relatively low recent productivity levels for maize, beans and soybeans compared to both agriculture-rich economies (Brazil and South Africa) and other lower middle income countries in Africa such as Kenya, Ghana and Zambia.

Figure 1: Yields of Maize, Beans and Soybeans for Angola and selected countries (2009-2014)



Source: Elaborated by the authors based on data from the Food and Agriculture Organization.

Most of the agriculture output in Angola is produced by smallholder farmers. Small-scale family farms produce primarily for subsistence and market the surplus production; output is hampered by limited access to inputs, low levels of mechanization and limited productivity.[91] Smallholders also face several challenges key for innovation and productivity growth, including: (i) limited access to finance and market information; (ii) agricultural extension services ; (iii) lack of local industry processing.

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[88] See, for example, LCG/ISEG (2015). Estudo de Diversificação da Economia Angolona. Estratégia para a Diversificação da Economia Angolana.

[89] Angola Agricultural Economic Fact Sheet. Foreign Agricultural Service. United States Embassy in Angola (updated May 2015). Agriculture, forestry and fishing 10.4percent (2009), 10.1percent (2010); 10.2percent (2011), 12.2percent (2012). US$ 1,749 million in 2010 (9.6percent of total imports) African Development Bank (2012). Angola Private Sector. Country Profile. Pp 9-10.

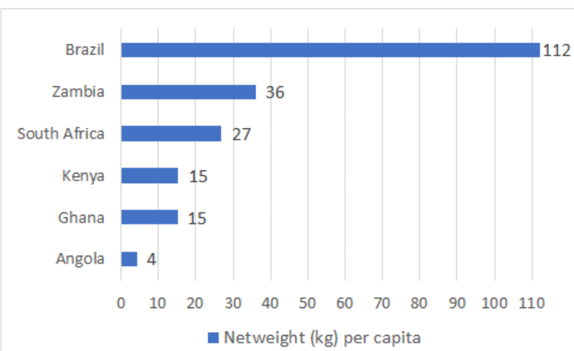
[90] Jose de Assuncao Sambo Tomas (2013). Agriculture as a tool for development in Angola. African Journal of Agricultural. Vol. 8(50), pp. 6643-6644.

[91] See Jose de Assuncao Sambo Tomas (2013). Agriculture as a tool for development in Angola. African Journal of Agricultural. Vol. 8(50), pp. 6643.

Extension services are provided by the Government. Smallholder agriculture and extension services are supported by the Agricultural Development Institute (IDA) of the Ministry of Agriculture (MINAGRI) through a network of technical personnel, with extension officers covering all of Angola's provinces. The role of the IDA has changed gradually from that of distributing inputs and equipment to one of training and supporting rural families. The Government employs about 700 agronomists/ technicians to serve a population of about 4 million smallholder farmers: a ratio of one extension officer to 5,722 producers. This is low compared to other countries, where respective ratios range from 1:280 farmers in some Asian countries (China, Vietnam), to 1:1000 in Nigeria and 1:2500 in Malawi. There is clear evidence of the importance of extension services in Angola, where yields of cereals, potato and beans are on average higher for farmers who received extension services. The average yield of maize was 720kg/ha compared to 600 kg/ha were no services were provided.

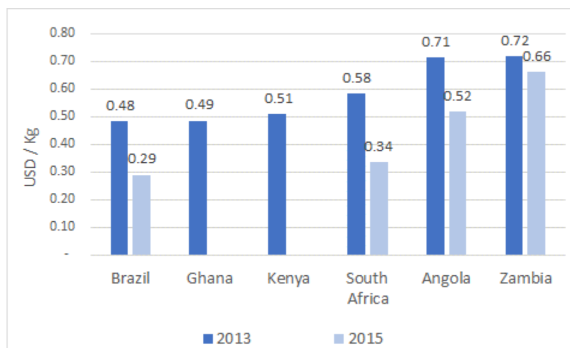
The low level of productivity in food crops is partially explained by the poor performance of agriculture input markets in Angola. Agriculture input markets, such as for improved seeds, fertilizers, tools and machinery, are relatively underdeveloped in Angola. Taking the fertilizer market as an illustration (Figure 2), Angola uses significantly less fertilizer per capita than comparator countries – lower middle income countries in Africa such as Kenya and Ghana use more than three times the amount in Angola; Zambia uses up to nine times more. [92] At the same time average import prices of fertilizers in Angola are higher than in most comparator countries (see Figure 3). Margins between commercial retail prices and import prices are also high, and the large resale mark-ups seems at odds with regional trends on imported fertilizer markups – in 2007, for example, the International Fertilizer Development Center identified that, for seven African countries examined, international prices of fertilizer constituted on average 65 percent of the final retail price. [93]

Figure 2: Consumption of Fertilizer for selected countries. Volume imported in Kg per capita (2013)



Source: Elaborated by the authors based on data from UNCOMTRADE and World Bank. Data consider volumes of 4 different harmonized system codes: 3102 (Mineral or chemical fertilizers, nitrogenous), 3103 (Mineral or chemical fertilizers, phosphatic), 3104 (Mineral or chemical fertilizers, potassic), 3105 (Mineral or chemical fertilizers containing two or three of the fertilizing elements).

Figure 3: Weighted average prices of imported fertilizers (FOB, USD 2013-2015)



Source: Elaborated by the authors based on data from UNCOMTRADE. Data consider prices and volumes of 4 different harmonized system codes: 3102 (Mineral or chemical fertilizers, nitrogenous), 3103 (Mineral or chemical fertilizers, phosphatic), 3104 (Mineral or chemical)

[92] This comparison considers volume of imported fertilizers as a proxy for consumption. The most updated figures for Angolan consumption of fertilizers from FAO date back to the year 2000 – the pattern of low usage by Angola compared to other countries is similar.

[93] See International Fertilizer Development Center (IFDC). 2007. "Fertilizer Supply and Costs in Africa." Report for the Bill and Melinda Gates Foundation (June 21).

Policy options

Public spending in the sector has been low and has declined over time. The share of agriculture in the national budget in 2013 was 1.1 percent (US$702 million) and has declined to 0.4 percent (US$544 million) in 2015. The space for fiscal expansion within the sector is limited given the need for fiscal consolidation over the medium term to restore macro-fiscal stability. This has made the agenda for leveraging private investments into the sector ever more important and urgent.

Domestic support to the agricultural sector takes various forms, including subsidized credit, the lending of material and equipment, subsidies for draught power and irrigation costs; and the provision of veterinary services free of cost to small producers. The Government has promoted various programs to support the agricultural sector including subsidized credit, subsidized fertilizer, lending for material and equipment, subsidies for processing facilities, irrigation and draught power and veterinary services for small holder farmers. However, the improvement of agriculture information systems (agroclimatic systems, market price information, surveys and census, production statistics, etc.) has been generally lacking, and there is an urgent need for conducting an assessment of primary agriculture production and productivity, strengthen extension services and provide capacity building for farmers' organization, as well as mapping the supply and demand of most significant supply chains to guide investors.

Government supported agri-credit programs in Angola have high rates of non-performing loans and there is political interference in credit allocation. Only 2 percent of farmers have access to agriculture credit. Although the availability of agriculture credit has increased in recent year, it has not reached the smallholder segment. Therefore, Angola, like other countries in the region, should focus on improved capacity building within financial institutions and ensure the crowding-in of private financial capital to help develop agri-finance markets as part of an effort to expand sector investments.

Many of the agriculture support programs and policies fall under the MINAGRI, where the State is envisaged as the main investor and actor in infrastructure and agro-industrial activities. This strategy[94] is designed to cut post-harvest losses, which can be as much as 50 percent of agricultural output owing to inadequate storage and transport infrastructure. However, the Ministry is severely restricted in terms of human resources, as salary levels inhibits the attraction and retention of qualified staff.

The Government has a National Irrigation Plan (PLANO IRRIGA) that focuses on the development of irrigation infrastructure on the main river basins. This plan only deals with major irrigation systems and is managed by the national Directorate of Hydraulics at the MINAGRI. The country has an important potential to develop small scale gravity fed irrigation systems in the central region. However, to date there is no policy for smaller scale systems, with no mechanism or policy instrument in place to allow for concession and operation of such systems.

The Angolan Land Law establishes that all land belongs to the State. The law (Article 5 of the Land law 04/04) provides user rights to the community that have traditionally inhabited certain lands – known as (non-transferable) rights of useful customary domain. Economic operators may exploit land under concession contracts (land-use rights) with a maximum but renewable duration of 60 years. Foreign natural and legal persons may be granted land-use rights, provided they have a representative in Angola (Land Law of November 2004). However, the procedures for obtaining and transacting land-use rights (concessions) are cumbersome, expensive, and slow, and few transfers come with legally-defensible documents to prove that dwellers own the land they have acquired or been allocated.

[94] This strategy was developed in 2012 and is reflected in the PMDSA 2022.

Information on available land is underdeveloped. The current state of land information in Angola constrains the ability of government and investors to identify potentially promising land for investment. Most rural lands are not formally registered and absent from any database, and the practice of registering land rights or transactions is not common. No statistics are available on what percentage of land is under private tenure as opposed to communal tenure. There are no reliable records of customary land ownership, or use of land under concession. Furthermore, the boundaries of community land, and of land under concession, are generally not formally mapped and recorded, causing frequent disputes.

Agriculture trade policy is characterized by high tariffs, preventing the sector from joining regional or global value chains.[95] The agriculture sector has the highest average MFN duties (23.3 percent). This not only restricts the use various agricultural inputs (and therefore makes it difficult to join value chains) but may also prevents the import of necessary food items[96]. The Government is currently reviewing trade policy and is proposing substantial reduction in duties.[97] Continued review of import tariffs for inputs may be required given the importance of importing seeds, fertilizers and other inputs to local food production. Agriculture input tariffs levels may be reduced to increase agriculture technology adoption and productivity. Non-tariff barriers, including licensing and other charges, increase the cost of importing agriculture inputs. A review of these fees could identify opportunities for reducing the cost of imported goods.

Efforts to address the scarcity of foreign exchange to import agriculture inputs is an example of a policy that may unintentionally restrict market dynamics and should be reviewed. Since 2015, scarcity of foreign exchange appears to have accentuated market concentration in the supply of agricultural inputs, generating shortages and significant price increases.[98] The government has also conditioned access to foreign exchange on a commitment by importers to adhere to government-determined retail prices in the domestic market.[99] While this policy has improved the availability of products and lowered prices, it can

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[95] Angola has been a member of the WTO since November 1996, and is also a member of two regional economic communities: the Economic Community of Central African States (ECCAS) and the Southern African Development Community (SADC). Angola withdrew from COMESA in 2007. According to WTO, Angola has not ratified the SADC Trade Protocol or signed the SADC draft Protocol on Trade in Services, but has signed the SADC harmonized seed policy. Angola is part of several bilateral trade agreements, which has increased from 30 to 38 framework or cooperation agreements. Angola participated, as part of the SADC group, in the negotiations for an Economic Partnership Agreement (EPA), but did not sign the Agreement concluded by the European Union with the six other SADC members in July 2014. Angola is a beneficiary of the United States' African Growth and Opportunity Act (AGOA) and as a least developed country, of the GSP schemes of other countries. However, due to its lack of competitiveness Angola has not taken advantage of preferential access under AGOA. Under the Global System of Trade Preferences among Developing Countries (GSTP), Angola has conducted negotiations with Mozambique and Cuba. For the time being, however, Angola accords no trade preferences.

[96] "Cesta basica" products are tariff exempt.

[97] Import tariffs overall remain in a range of 2-50 percent, but some reductions have been proposed for meat and live animals which have a current level of duty of 20 percent plus a consumption tax of 10 percent for meat. The Government is proposing to cut the duty to 2 percent and to maintain the consumption tax. Irish potatoes seed is subject to a 50 percent import tax and the current revision proposes a reduction to 30 percent.

[98] "Foreign exchange availability in the market during 2016 averaged $890.5 million per month, a substantial decrease, (almost half of the 2015 monthly average of $1.46 billion per month average and 2013/2014 $1.6 billion monthly averages. Per the February 24, 2016, Presidential Decree No. 40/16, foreign exchange availability in 2016 was expected to meet only 63 percent of demand." See U.S. Department of State. Bureau of Economic and Business Affairs. 2017 Investment Climate Statements – Angola. Report. June 29, 2017

[99] "Programas Dirigidos" allocated around USD 500 million in Forex to the acquisition of agriculture goods, including inputs, between 2016 and 2017.The program contemplated 691 companies in 2019 and planned to cover 950 in 2017.[99] "Apenas em Moxico, relativamente à disponibilidade de factores de produção para o apoio a campanha agrícola 2016/2017, foram recepcionadas e distribuídas 29 990 kg de milho e 24 999,8 kg de NPK, em um programa do governo (Programa de Extensão e Desenvolvimento Rural (PEDR)" . Universidade Católica de Angola (2016). Relatório Económico de Angola 2016. pp 253-254.

negatively affect the market performance, as it potentially create barriers to entry for new bidders, facilitates collusion and favors some competitors over others.

Given its extreme vulnerability to Climate Change, Angola's Nationally Determined Contributions (NDC) includes priority adaptation actions to foster resilience. Adaptation measures in the following main sectors are foreseen in the NDC: Agriculture, Coastal Zone; Land-Use, Forests, Ecosystems and Biodiversity; Water resources; and Health. The NDC commitments are an important target for Angola's agriculture sector to achieve in order to address sustainability and resilience challenges posed by climate change, and to ensure medium to long-term sector competitiveness.

Angola has the opportunity to diversify its economy (while providing jobs and incomes to the rural poor) through a shift in agricultural policies and programs. Given the current fiscal constraint and the need to diversify, this can be an opportunity to gradually open to trade of agriculture inputs and products, while shifting public spending towards more targeted interventions. These interventions could focus on policies and programs to: (i) improve and expand agriculture public goods and services (irrigation, land animal plant and health, agriculture research, a transparent and predictable regulatory framework); (ii) deregulate the agriculture and agribusiness markets (including trade policies), (iii) reform the agriculture input support policies (including credit, insurance, technologies, seeds, fertilizers, etc.) from distortionary towards non-distortionary subsidies.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Introduce differentiated salary scales for MINAGRI (similar to MINFIN) to attract and retain qualified staff.	High	Short-term
Link the National Agriculture Policy (national policies for the next 5-10 years) to a multi-year budget planning process. The MINAGRI has 5-year mid-term agriculture sector development plans (for 2008-2012 and for 2013-2017) that can also serve as guidance for budget preparation.	High	Medium-term
Improve agriculture public goods and services		
Implement irrigation policy instruments to promote the creation and operation of Water Users Associations.	High	Medium-term
Improve the land concession and management system, including legal/regulatory actions to avoid a destructive competition for land between agriculture and natural ecosystems.	High	Medium-term
Reform the land tenure/ administration system (legal/regulatory system) to reduce land insecurity (direitos comunitarios sobre as terras). Address land allocation and titling issues to facilitate asset collateralization.	High	Medium-term
Improve the agriculture innovation system through improved policies on agriculture R&D and need to improve seed and tariff regulation waivers, seed quicker and greater impact in small scale output, education, and extension, including the participation on regional agriculture R&D forums and the development of PPPs for agriculture R&D.	Medium	Medium-term
Agriculture trade deregulation policy		
Reform agriculture tariffs and other non-tariff measures. This would require a gradual approach to tariff reduction needs to be negotiated with the sector, with clear transition support plans for farmers to adapt to new market signals within our outside the agriculture sector. Policies to streamline the import tariffs on agriculture inputs are needed. Agriculture products face high import tariffs (price support measure), and in order for the sector to become competitive, specific policies need to be put in place to bring down the tariffs while improving the competitiveness of the sector to face international prices.	Medium	Short-term
Assess the current management, financial and economic feasibility, and opportunities for privatization or PPPs of public agribusiness investments in large-scale production, agro-processing, storage and warehouse facilities, development of logistics cold chains, irrigated perimeters, which have been estimated at between US$1.5-2 bn.	High	Medium-term
Create a platform for discussions between private and public sector (camara agropecuaria) to facilitate communication and agreement on sector policies/programs. This is one activity included in the CADP.	High	Short-term
Agriculture input support policies		
Shift from distortionary towards non distortionary subsidies, focusing on positive externalities, such as environmental impact (i.e. climate smart agriculture), by allowing for Banks and other financial institutions to channel such support.	High	Medium-term

Education

Notwithstanding the significant progress in increasing access to education, education outcomes in Angola lag behind peers with similar levels of education spending. For Angola to achieve its goal of universal access to a quality based education, the government needs to increase access to education, improve education quality and strengthen governance of the education sector. To increase access to education – especially in rural areas and among girls – alternative forms of service delivery should be considered, including online programs and public private partnerships. Quality of education should be improved through greater investment in teacher training, while skills development programs need to be expanded and tailored to the needs of the labor market. Strategic planning and budgeting processes should be streamlined across all stakeholders at the central, provincial and municipal level to ensure coordination, monitoring and effective service delivery.

Background

Greater attention to the importance of education has led to higher rates of access, but Angola still lags behind peers. Since the end of the civil war, access to education has rapidly improved with primary school enrollment increasing from only 500,000 to over 5 million children between 2001 and 2015. However, education outcomes are still behind those of countries with comparable or even lower levels of public education spending. While net primary school attendance rates improved from 56 percent in 2005 to 78 percent in 2014, one in six school-aged children is not in school. This is four times higher than the UMIC average. Between 2009 and 2011, secondary school completion rates in Angola were the second-lowest among LMCs at just 25 percent. Similarly, the youth (ages 15 to 24) literacy rate in Angola is 75 percent, compared to 99 percent for peers. Repetition rates as high as 20 percent and low scores on learning assessments also point to shortcomings in the quality of education.

Significant additional investments will be required to expand access of the current system to meet targets. The 2016 education law extends universal education from primary school (grades 1-6) to pre-school (children aged 5) and lower secondary school (grades 7-9). The recently adopted National Education Development Plan (*Educar Angola 2030*) establishes ambitious targets to accelerate the expansion of the current system. According to population growth estimates, to reach the enrollment targets set for 2030, the current system will need to accommodate more than 3 million additional students. Significant resources will be required to construct additional classrooms, recruit and train qualified teachers, while also taking measures to ensure that this huge influx of students does not further deteriorate education quality and compromise learning outcomes.

Table 1: Access to Education in Angola: Net Enrollment Rates (Actual in 2014 and Targets for 2030)

Level	2014	Goal by 2030
Pre-school (Age 5)	67.7%	90%
Primary Education	77.7%	90%
Secondary Education – 1st Cycle/Lower	26%	60%
Secondary Education – 2nd Cycle/Upper	15.2%	40%
Secondary Education – TVET only	1.9% (1st cycle) 5% (2nd cycle)	15% (1st cycle) 16.7% (2nd cycle)

Source: Ministry of Education, O Plano Nacional de Desenvolvimento da Educação 2017-2030.

Public and private spending on primary and secondary education is low in Angola. Public expenditures in education increased significantly between 2010 and 2013, from 2.9 to 4.1 percent of GDP. However, education spending was cut by more than 30 percent between 2013 and 2015 due to the economic crisis, reaching 2.7 percent of GDP in 2016. The share of household expenditures in education is also much lower than in most comparable countries. Given that half of Angola's population is under the age of 14, the need for more primary and secondary education spending is unlikely to diminish over the medium-term and current and projected expenditures will not be sufficient to achieve Angola's objectives in the education sector.

Poor education quality and learning outcomes in both primary and secondary education remain a serious concern. Evidence of poor eduaction quality is reflected in high repetition rates (as high as 20 percent) and low completion rates in both primary and secondary education. An early grade reading assessment administered in 2011 and repeated again in 2016 found that as many as 60 to 80 percent of grade 3 students were unable to read a single word in Portuguese.[100] In almost all provinces, scores for girls and students in rural areas were much lower on average.[101] Evidence shows that poor education outcomes are linked to the high percentage of unqualified and poorly trained teachers, high pupil/teacher ratios, a lack of learning materials, and weak Portuguese language skills of teachers.

The supply of adequately trained teachers is insufficient for all levels of education. In primary education, significant efforts have been made to improve the capacity of teacher trainers and properly trained pre-service teachers. Similar efforts are needed at other education levels. The lack of qualified professionals to teach pre-school, secondary education and Technical and Vocational Education and Training (TVET) courses are a significant barrier to better educational outcomes. For example, in 2015, the current system only trained 770 pre-school teachers; far short of the more than 10,000 teachers/educators required to teach the over 1 million 5-year-olds in the country. Investments in in-service training are very limited as well. From 2010 to 2015, investments in teacher training represented only 1 percent of total MoE expenditure.

Disparities in access and learning outcomes among girls and communities in rural areas need greater attention. In rural areas, attendance rates and education quality are negatively affected by distances between schools and lack of transport, inadequate supply and inequitable distribution of classrooms, and a mismatch between teachers and classroom availability. In pre-school education, while net enrollment rates are as high as 68 percent, attendance rates in rural areas are as low as 7 percent. Data from the recent DHS survey also show significant geographic and gender disparities in the education system, particularly at the secondary education level. The probability of girls living in rural areas having completed secondary school is only 1 percent.[102] Due to late entry, high repetition rates, and teenage pregnancies, many girls drop out of school before completing their education.

Decentralization can help improve service delivery, but it presupposes coordination, policy alignment, and accountability, all of which need to be improved. The decentralization of education services in Angola lacks mechanisms to ensure effective coordination across the different levels involved in budget planning and execution process. For instance, the MoE is in principle responsible for strategic planning, but in practice provincial and municipal governments have wide latitude over planning, budget allocation, and execution. The co-existence of parallel responsibilities greatly complicates the planning, monitoring and oversight process. Additionally, weak alignment between resource distribution from the central level and budgeting at the municipal level weakens the system's capacity to execute activities based on

[100] Results vary by province, ranging from 95 percent of students unable to read a single word in Bie to 39 percent in Luanda.
[101] Ministry of Education, Early Grade Reading Assessment (EGRA) and Service Delivery Indicators (SDI) Technical Report (Draft), 2017.
[102] MICS, 2015-16.

operational planning. Findings demonstrate that on average, only 34 percent of schools receive the expected number of textbooks and more than 36 percent of teachers are absent and not in their classrooms when they should be teaching.[103] In rural areas, teacher absenteeism rates climb as high as 54 percent.

In addition to shortcomings in basic education, Angola's skills sector needs greater attention. Major skills mismatches and shortages in the labor market undermine growth prospects. The key constraints faced by Angola's TVET sector include poor quality and relevance of existing programs, limited access to job-relevant skills development programs, and overall poor coordination and governance. As Angola aims to diversify its economy, there is a need in key growth sectors, such as agriculture, to increase the supply of quality training programs to produce well-qualified graduates.

Policy Options

Increasing the supply of quality preschool education, and early stimulation and nutrition programs would be a highly cost-effective intervention in the medium-term. Investing in preschool education and early childhood development can increase the efficiency of education resources by improving school readiness, lowering repetition rates and reducing the need for remedial education later. Expanding preschool education through a combination of public and private service provision could be particularly effective in improving educational outcomes at a moderate cost. To increase supply and improve quality, more pre-service training programs should be developed in this area. Efforts to expand pre-school education should be complemented by interventions to increase parental education and public awareness of the importance of early education and nutrition, particularly among poor households (potentially leveraging the community development agents (ADECOs) and safety net programs).

Expanding secondary-school access and improving graduation rates are vital for long-term growth and economic diversification. Angola should implement complementary strategies to expand secondary education: explore alternative service-delivery mechanisms, promote more private schooling, increase the availability of TVET schools with special emphasis on targeted sectors (e.g. Hospitality, IT, oil & gas technicians), and shift resources from the tertiary to the secondary level. The use of alternative delivery mechanisms such as distance learning programs could expand the supply of education services in rural areas, while more private schooling could improve supply in urban areas. Additional TVET schools offering courses aligned with the Government's National Training Plan with strong links to the labor market would help to improve student motivation and provide greater employment opportunities for Angola's youth. Given current disparities in access in rural areas and high drop-out rates among girls, targeted social programs should be developed to alleviate demand-side constraints for school attendance. Government interventions should especially promote institutions that provide training and education that enhance the employability of students.

Encouraging the use of public-private partnerships is essential to meet the growing demand in the education sector. As a complement to increased government expenditures spent on education to reach enrollment targets, public-private partnerships in education should be encouraged. A strong quality-assurance framework to govern private education should be adopted and the authorities could explore options for granting tax incentives or even opening credit lines for new private schools. Angola has some experience in publicly subsidizing private primary schools, which can be further built on. In TVET, public private partnerships are particularly attractive given the generally high private rates of return and closer linkages with the labor market.

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[103] Ministry of Education, Early Grade Reading Assessment (EGRA) and Service Delivery Indicators (SDI) Technical Report (Draft), 2017.

Greater investments in teacher training and strengthening the knowledge base and teaching skills of Angola's teaching force is paramount to improve the quality of primary and secondary education. Given the high number of unqualified teachers in the system, greater resources must be allocated for both pre-service and in-service teacher training programs. For in-service teachers, a national database with information on teachers' current level of training and qualifications should be established. Based on this, in-service training programs, targeted to unqualified teachers, should be developed. In Angola, an effective new model for primary education has been the development of a national training program that is certified and aligned with the Teacher Career Ladder. Teacher training institutions and Zones of Pedagogical Influence (ZIP) Coordinators at the provincial and municipal levels oversee the implementation of the new program using the ZIP model/structure. [104] Alignment with the Teacher Career Ladder is essential to create the necessary incentives for teachers to be motivated and actively participate in training activities. Based on the positive outcomes from this program, it is recommended to expand these opportunities to additional teachers and develop a similar model for other education levels. In primary education, a strong focus should be on improving teachers' skills in Portuguese and methodologies to effectively teach literacy and numeracy skills.

Improved monitoring and human resources management could greatly enhance the efficiency of education spending. A stronger policy on teacher deployment would help align the distribution of secondary-school teachers and classrooms within provinces and could leverage scarce physical and human resources. Involving municipal education directorates in teacher-recruitment and school-location decisions could also help in this process. The current inspection system should be revamped to be closer to the school level and include mechanisms to increase transparency and monitor overall service delivery including teacher performance and distribution and availability of textbooks. To improve availability of learning materials, a national policy on textbooks that includes a possible loan program and a detailed dissemination plan should be developed.

The government should streamline the education sector's budgeting and planning processes and address the lack of administrative data. Roles and responsibilities at the central, provincial and municipal levels should be clarified and training programs developed to strengthen capacity at the municipal level for education planning/budgeting and collecting school level data. Enhancing the quality and availability of education statistics and ensuring that they are widely available and utilized would help improve planning efforts and facilitate monitoring and evaluation.

Lastly, the Government should increase investments in the skills sector and expand access to quality training programs that meet the needs of the labor market. Investments should focus on (i) increasing access to training programs in priority sectors; (ii) enhancing the quality and ensuring job-relevancy of existing programs; and (ii) strengthening overall governance and management of the sector.

[104] Every ZIP includes 4-5 schools, with an average of 18 teachers per school. The ZIP model has been implemented in all the country's provinces and benefits an estimated 270,000 students.

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Increase access to education		
Increase the supply of preschool education and early stimulation and nutrition interventions. Programs should include interventions to increase the provision of school feeding and public awareness of the importance of early education and nutrition, particularly among poor households.	High	Medium-term
Expand secondary education through a cost-effective secondary education strategy, which draws on alternative forms of service delivery such as semi-present and online programs (while ensuring appropriate quality controls) and establish public private partnerships.	Medium	Short-term
Increase public sector financing and the use of public private partnerships in education. Put in place a strong quality-assurance framework and encourage more public-private partnerships in pre-school, primary and secondary education. Explore options for granting tax incentives or open credit lines for new private schools, and possibly create additional incentives for opening schools in rural areas and enrollment of girls in secondary education.	Medium	Medium-term
Improve education quality and learning outcomes		
Improve children's school readiness by enhancing the quality of pre-school programs. Develop a national curriculum and increase the number of institutions offering pre-service training programs in this area.	Medium	Medium-term
Invest greater resources in both pre-service and in-service teacher training. Establish a national database with information on all teacher's current level of training and qualifications. Develop national in-service training programs and increase the number of training opportunities, particularly for unqualified teachers (coordinate with ZIP coordinators provincial and municipal levels).	High	Short-term
Expand access to quality skills development programs that meet the needs of the labor market. Increase access to training programs in key growth areas, ensuring quality and job-relevancy of existing programs.	Medium	Short-term
Strengthen governance and service delivery in the education sector		
Improve coordination among the MoF, MoE, and provincial and municipal education directorates in strategic planning, budgeting, and monitoring in the education sector. Support activities to build capacity in budgeting and planning at the municipal level; establish stronger links between municipal level planning and budgeting and the MoF allocation; support the collection of school level data to inform decision making; and continue to conduct assessments of student learning outcomes to monitor education quality and use the results to guide policy reforms.	Medium	Short-term
Strengthen teacher management. Improve the policy on teacher deployment and teacher incentives to improve school quality in poor and rural areas by lowering student-to-classroom ratios and better alignment of teachers and classrooms. Support the development of mechanisms to track and report teacher attendance.	Medium	Short-term
Increase the availability of learning materials by developing a national policy on textbooks, which should cover central-level procurement, a detailed dissemination plan that ensures delivery at the school level, and a textbook lending program that allows students from all income levels to access textbooks and learning materials at each education level.	High	Short-term

Health

Angola's health sector is underfinanced, both at public and private levels, and there is a need to increase its efficiency and to strengthen its governance framework to maximize healthcare outcomes in light of the scarce resources available. Strengthening the primary care system is critical, as it can deliver high-return programs with the greatest short-term impact on health outcomes. Strengthening the primary care system can simultaneously help address the challenges imposed by infectious diseases and non-communicable diseases, which are gaining importance in the country's epidemiological profile. Better management, more effective service delivery and new purchasing strategies in the pharmaceutical sector can reduce expenditures and increase access and availability of medicines. Changes in the financing of healthcare facilities can increase efficiency and performance. The highly fragmented institutional arrangements should be streamlined to strengthen the overall governance framework.

Background

While key health outcome indicators are improving, Angola continues to lag comparator countries. Life expectancy at birth has increased by more than ten years during 1990 and 2014, maternal mortality has decreased by more than half and infant mortality has dropped by 67 percent. Despite this progress, the gap to regional peers and middle income countries remains large (see Table 1). The Multiple Indicator Cluster Survey (MICS) for 2015-2016 further shows that 38 percent of under-5 children in Angola suffered from chronic malnutrition (low height for age) and 34 percent of children ages 6-59 months have moderate or severe anemia.

Table 1: Life expectancy and mortality rates in Angola, Sub-Saharan Africa (SSA), lower-middle-income countries (LMIC), and upper-middle-income countries (UMIC), 1990-2014

	1990	2000	2010	2014
Life Expectancy at birth				
Angola	41	45	51	52
SSA	50	50	56	57
LMIC	60	63	66	67
UMIC	68	71	74	74
Infant Mortality Rate (per 1,000 live births)				
Angola	134	128	110	*44* (2015)*
SSA	109	94	66	58
LMIC	83	66	47	41
UMIC	42	31	18	15
Maternal Mortality Rate (per 100,000 live births)				
Angola	1,160	924	561	477 *(2015)*
SSA	987	846	625	560
LMIC	533	410	284	257
UMIC	114	86	63	55

Source: World Bank Development Indicators database data.worldbank.org; (*) MICS 2015-16

Challenged health outcomes reflect failures in service delivery, symptomatic for a dysfunctional health system in need of more effective and efficient primary health care service delivery. While municipal directors are involved in developing, implementing and supervising annual health plans, limited communication with the Ministry of Health (MoH) constrains more informed technical decisions at the local level. There is also a lack of accountability on how funds are used by the provinces and municipal directorates, as they are transferred by the Ministry of Finance (MoF) without any links to national goals or performance. Budget execution rates at the municipal level are high, but there are many signs of inefficient resource use: health posts and municipal hospitals are not always functional, health workers' classifications are frequently outdated, and staff are frequently absent.

Several quality-related issues undermine healthcare outcomes. Quality is hampered by a scarce supply of trained health staff: the number of doctors and nurses per capita has been declining, and about 85 percent of doctors are concentrated in regional and general hospitals in Luanda and provincial capitals. The quality of pharmaceutical products is also a concern, as storage conditions are often inadequate, especially for products requiring temperature control, and Angola has no national quality-control laboratory and counterfeit medicines are in circulation. As the 10 mini-laboratories that were introduced in 2012 to screen the quality of medicines at entry points are insufficient to cover all imported pharmaceuticals, some products must be sent to laboratories in Portugal and Brazil for screening. A 2005 USAID report estimated that 70 percent of drugs were purchased in informal markets, 35 percent of them were counterfeit drugs.[105]

Health services and outcomes are a particular concern in poor communities and rural areas. The provision of health services in Angola is uneven: wealthier households spend more and are more likely to use private facilities, while poor households often forgo treatment due to lack of resources. Health facilities are also unevenly distributed, leading to a shortage of health units and services in the more remote provinces (e.g. Cuando Cubango) and rural areas. The rural/urban disparity is also visible in 2015 figures that show that about 75 percent of births in urban areas were attended by a skilled professional, compared to only 25 percent in rural areas; a disparity that has remained broadly unchanged since 2008.[106] Supply-chain problems related to the procurement, storage and distribution of drugs, combined with a lack of resources, have severely restricted the availability of drugs and vaccines. Angola is currently facing a severe shortage of tuberculostatic drugs, some parts of the country have not received rabies vaccines for the last two years, and even the availability of antimalarial drugs has been compromised. Due to the limited supply of drugs, the share of out-of-pocket spending on pharmaceuticals is as high as 76 percent in rural areas.

Health spending (both total and public) compares unfavorably with countries at the same or lower income levels. Over the past fifteen years (2000-2014), total health expenditures in Angola, both in per capita terms and as a percentage of GDP, fall short of that of regional peers and the average middle income country (see Table 2); health expenditure as a share of GDP are even lower than in much poorer Mozambique. Differences in health expenditures between Angola and peers widened in recent years (2010-2014), and even prior to the significant crisis related cuts. Public spending accounted for about 60 percent of total health expenditure between 2000 and 2014. While this level is similar or even higher than in most comparators, the government allocates a very small share of the budget (slightly less than 6 percent) to the health sector. This explains the overall low levels of health spending in Angola compared to other mineral-rich countries outside SSA, such as Bolivia, Ecuador, Colombia, Mexico and Malaysia.

[105] In September 2015, the Criminal Investigation Service (*Serviço de Investigação Criminal*) apprehended over 11,000 kg of counterfeit medications, including antibiotics, anti-malarial medications, analgesics, TB medications, and steroids.
[106] MICS 2015-16 and Inquérito Integrado Sobre o Bem-Estar da População (IBEP) 2008/09.

Table 2: Healthcare expenditure in Angola, SSA, LMIC, and UMIC, 1995-2014

	1995	2000	2005	2010	2014
Total Health Expenditure per capita (current US$)					
Angola	18	17	65	132	179
SSA	40	33	57	88	98
LMIC	48	58	96	198	265
UMIC	88	112	175	379	518
Total Health Expenditure per capita (% of GDP)					
Angola	6.5	2.8	4.1	3.4	3.3
SSA	6.1	5.5	5.8	5.8	5.5
LMIC	4.7	4.9	5.3	5.6	5.8
UMIC	5.2	5.5	5.6	6.0	6.2
Public Health Expenditure (% of government expenditure)					
Angola	5.2	2.8	6.1	5.4	5
SSA	-	-	11.6	11.8	-
LMIC	-	-	-	-	-
UMIC	-	-	-	-	-
Out-of-pocket Health Expenditure (% of total expenditure on health)					
Angola	20	22	39	28	24
SSA	35	30	31	31	34
LMIC	42	46	43	38	36
UMIC	51	48	49	54	55

Source: World Bank Development Indicators database data.worldbank.org

Recent progress in health outcomes is threatened by crisis-related cut-backs to health spending. Per capita public spending in the health sector increased by more than four times in real terms during the oil boom years of 2000 and 2013, but the share of public spending on health declined with lower growth post 2014. This pattern was reinforced by public spending cuts in 2014 and 2015 which lowered government spending on health by 19 and 39 percent, respectively. According to the MoF, public health expenditures declined from 2.6 percent of the GDP in 2013 to 1.5 percent in 2015. Spending on immunization programs fell by 50 percent from 2014 to 2015, and data from the 2015/16 MICS suggest that vaccination rates for DTP and Polio-3 have dropped to about 40 percent in 2015.

After the civil war, Angola embarked on a process of decentralization, which involved the administrative decentralization of the public health system (*Sistema Nacional de Saúde*, SNS). The SNS encompasses the MoH; Provincial Governments with their Provincial Health Directions and Provincial Hospitals; and the Municipal Administrations which run the Municipal Health Directions, Municipal Hospitals, and Health Care Units and Posts. The MoH is responsible for the development of health policies; the preparation, evaluation and monitoring of annual strategic plans; and the promulgation of regulations. Provincial governments have the responsibility to manage the provinces' network of health services, and have to ensure that all units operate within their allocated provincial budgets. Municipal governments are increasingly managing the primary health care network and basic health care activities. However, the limited administrative and technical capacity at the local level remains a constraint to tackle the challenges imposed by the decentralization process.

Lack of accountability and coordination mechanisms between central and local authorities in the formulation of the health budget make it difficult to address deficiencies across the different levels of the health system. Angola has a single consolidated budget for central and local levels of governments. The General State Budget (*Orçamento Geral do Estado*, OGE) comprises the budget for central government agencies, such as the MoH, as well as the budget for all provincial governments. Per the Budget Framework Law and the Law on Local Governments, provincial governments are responsible for several public services, such as health, which includes the construction and maintenance of provincial hospitals and health centers. As part of the budget process, provincial governments submit budget proposals from the provincial directorates of health and education (*Delegação Provincial de Ensino e de Saúde*) to the MoF. The MoH also submits its own budget proposal to the MoF which covers support operations and policy departments, and the financing of services for which the ministry is directly responsible; these include the construction and maintenance of regional and national hospitals. There is little coordination between local and central levels when defining priorities, and in turn, formulating budgets. Instead, the MoF sets initial expenditure limits for both local and central budget proposals, and consolidates all budget submissions. At the provincial level, provincial governments allocate relevant budgets to hospitals, health centers, and municipal administrations; as a result hospitals and municipal administrations are becoming *de facto* budgetary units, responsible for executing their own budgets. While provincial and municipal level have complete autonomy over health services under their responsibility, the lack of coordination misses the opportunity to agree on shared priorities that should be addressed across the entire national health system.

Policy options

There is significant scope to improve the efficiency of health expenditures. To improve the efficiency of health expenditures and in general effectiveness and efficiency of health care, some interrelated priority issues to be addressed including the limited and declining share of national funding for maternal health, child health, and immunization programs; the weak delivery at the local level of maternal and child health care; the low quality, unevenly distributed, and poorly utilized primary healthcare facilities; the inadequate supply and distribution of doctors and skilled healthcare professionals, magnified in rural areas; and the high cost, low quality and frequent stock-outs of pharmaceuticals.

Improving the quality of primary healthcare and investing in primary healthcare in poor communities and rural areas will generate the greatest impact. A focus should be placed on financial support for high-return programs and reactivating community development agents. In the short-term, the development of an investment case for priority issues such as reproductive, maternal, neonatal, child and adolescent health (RMNCAH) could guide sectoral efforts and harmonize external resources for the health sector, which could be increasing as a share of total expenditure in health. These priority issues should be supported through a revised national primary health care strategy and potential reorganization of the health system. To that end, focusing on financial support for high-return programs (maternal and child health, disease prevention) with a focus on epidemiological surveillance and training of health staff could greatly improve value for money. Moreover, the reactivation of the community development agents (ADECOS) program could improve effectiveness and contribute to a more resilient primary health system, while narrowing human resources gaps.

Efficiency gains can be explored in the health sector by using innovative financing mechanisms. The introduction of innovative financing, such as performance-based financing (PBF) schemes or contracting agreements could be used as tools for results-orientation and to change the behavior of health providers and administrators. Under a PBF approach, healthcare facilities would be financed according to the quantity and quality of services they provide, increasing both the quality and utilization of health care services. Individual facilities would also receive significant autonomy over their own expenditure decision. A well-designed pilot could help identify the key characteristics of a PBF model for Angola. Nonetheless improving the sector's resource allocation (financial, human and physical) according to population size and epidemiological needs and strengthening financial management capacity will be necessary conditions for the implementation of innovative financing schemes.

The governance framework of the health system can be strengthened through more efficient purchasing strategies and partnerships across the pharmaceutical sector. In 2016, pharmaceutical sales amounted to US$234 million, equivalent to 7.9 percent of total health expenditure or 0.24 percent of GDP.[107] Recentralizing the purchasing of pharmaceuticals could generate large savings to the system and to private households.[108] Recentralization, strategic purchasing, or pooled purchasing strategies could also free up resources for investment in other priority areas. Given past challenges, management of pharmaceutical supply chain should be explored as a potential area for public-private partnerships.[109]

From a PFM perspective, there is an opportunity to strengthen the planning and budgeting process at the municipal level. While decentralization has empowered municipalities, disaggregated budget control is complicating the annual allocation process and this affects the adequacy and efficiency of funding for primary health services. Currently, funds are transferred from provinces to the municipal directorates or municipal hospitals according to historic costs or local budget projections which do not take into account the real cost of services and/or quality indicators. The influence of municipal budgeting exercises on final allocations is unclear, as the results of municipal-level planning are not clearly linked to final allocations from the MoF. In a context where health already receives a small share of the government budget (only 5 percent in 2014), lack of accountability mechanisms pose the risk that already limited health resources are being drawn away from their intended use.

From a broader governance perspective, the Government should streamline highly fragmented institutional arrangements and address the lack of administrative data. The large number of sectoral actors and the lack of clearly defined roles and responsibilities underpins many of the structural deficiencies outlined above. The institutional fragmentation of the health sector is exacerbated by the lack of a common classification system for public health spending, which undermines strategic planning and complicates program implementation. Improving the quality and availability of administrative statistics and ensuring they are widely available and utilized, would help sharpen the focus of the health care system on outcomes, and monitoring and evaluation.

Private investment in healthcare should be actively promoted including PPPs. Promoting private sector investment in healthcare will enable the Government to leverage limited public resources, enabling the private sector to play a complementary role in the sector. The Government could provide incentives for sub-sectors such as diagnostics, private clinics and hospitals to encourage investment. The Government would still be responsible for approval and monitoring of private health care providers. Long-term incentives could include tax holidays, deferred taxes, and reduction of import duties on importation of equipment used in private health facilities.

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[107] Research and Markets: Angola Pharmaceuticals and Healthcare Report. *Business Wire*, 2017. https://store.bmiresearch.com/angola-pharmaceuticals-healthcare-report.html

[108] Data from 2011 on household spending show that the most common expense for households was for medicine (only 33 percent of users did not pay), which had an average user cost of Kz 2,500. This was followed by labs and consultation fees, which cost the user an average of Kz 1,000.

[109] There are limited experiences in introducing PPPs for supply chain management or procurement of pharmaceuticals http://www.msh.org/sites/msh.org/files/mds3-ch08-supply-strategies-mar2012.pdf , https://www.ifc.org/wps/wcm/connect/05551753-10f5-4b84-bf73-ec69cf207d31/Pharma+Distribution+%26+Retailing_FINAL.pdf?MOD=AJPERES

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Improve the efficiency of the health sector		
Focus on primary health care. Focus on providing financial support for high-return programs (maternal and child health, disease prevention) with an emphasis on epidemiological surveillance. Improve the geographical distribution of health centers and (qualified) health personnel; and the quality and utilization of health professionals at the local health facility level.	High	Medium-term
Increase the availability and improve distribution of Human Resources for Health (HRH). Increase the number and improve distribution of doctors, but also seek alternative HRH for the provision of health services such as community health workers and the use of mobile brigades.	High	Medium-term
Shift from input-based to performance focus. Adjust the health policy focus from *inputs* to *results* through the piloting of performance-based financing approaches, focusing on providing a consistent quality package of maternal and child health services across municipalities, while addressing the need for more and better quality of administrative data supported with public expenditure monitoring surveys and studies of service delivery indicators.	High	Medium-term
Actively promote private investment in healthcare including PPPs. Develop a framework and enabling environment for private investment in health care including PPPs.	Medium	Medium-term
Strengthen the health sector governance framework		
Streamline the institutional fragmentation of the health sector and address the lack of administrative data. Simplify and consolidate the institutional framework for the health sector. Establish a harmonized classification system for health sector expenditure and ensure transparency and availability of administrative data.	High	Short-term
Strengthen the planning and budgeting process at the municipal level. Incorporate a technical role for the MoH to support municipalities in their planning and budgeting for the health sector and establish a link between municipal level planning and budgeting, and MOF allocation and transfers.	Medium	Short-term
Increase focus on the pharmaceutical sector. Explore purchasing strategies across the pharmaceutical sector and public-private partnerships which can contribute to reducing the cost of medicines and in helping to ensure the availability of essential medicines.	High	Short-term

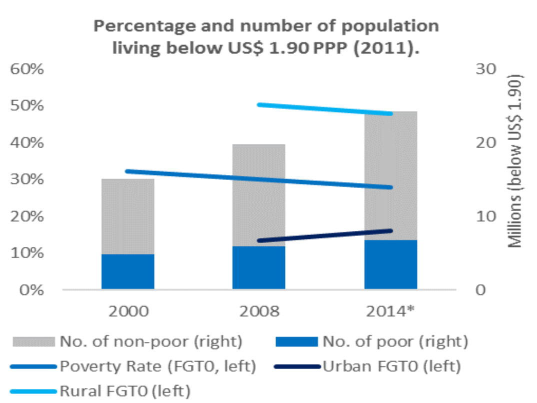
Social Protection

Mitigating measures to protect the poor are largely absent. The Government needs to combine short-term and medium-term social protection and productive inclusion measures to protect the poorest from the effects of the recent crisis, prevent other vulnerable households to fall into poverty, and promote economic opportunities for the poor. An increased budget allocation for poverty-targeted social safety net programs with direct links to productive inclusion initiatives is called for. To achieve this, the Government needs to reduce the current agency and program fragmentation, shift regressive government funding for subsidies to pro-poor programs, and promote a stronger decentralization of social protection and productive inclusion programs to provide municipalities a leading role in program implementation.

Background

Poverty remains widespread while inequality (though declining) has proved persistent. A third of Angola's population is poor with poverty concentrated in rural areas. Remarkably for a higher middle-income country with a per capita income of over US$3,500, an estimated 28 percent of the population in 2014 still lived below the international poverty line of US$1.90 (PPP 2011)[110]. Poverty reduction was ineffective between 2008 (30 percent poverty) and 2014 (28 percent poverty) with the absolute number of poor increasing from 6.0 million to 6.7 million due to large population growth. Angola's income Gini coefficient stands at 42.7 (2008) while the country ranks 150 (out of 177 countries) in its Human Development Index. Despite the lack of data, Angola's current economic crisis suggests that the poverty incidence likely increased in recent years due to the fical contraction, lower employment and incomes, as well as higher inflation, which reached 26.3 percent in December of 2017, and food prices increased by 20.2 percent.

Figure 1: Poverty population (below US$ 1.90 PPP), 2011



Source: IBEP 2008. (*) estimated by IBEP 2008 and Census 2014 data.

Figure 2: Progress in Development Indicators

Indicator	2000-2005	Most	Year
Population (million)	14.7	25.8	2016
Population <= 20 years	60%	57%	2016
Pop below poverty line US$ 1.90/day	32%	28%	2014
Pop below poverty line US$ 3.10/day	54%	55%	2014
Life expectancy at birth	42.4	52.6	2015
Under-5 mortality (per 1000 live births)	250	68	2015
HIV/AIDS prevalence	3.90%	2.20%	2015
Pop knowing 3 ways avoiding HIV	18%	45%	2014
Adult literacy rate	33%	71%	2015
Maternal mortality rate	705	477	2015
Net primary school attendance rate	56%	84%	2011
HDI rank (of 177 countries)	166	150	2014
Gini coefficient (income, 1995)	0.54	0.42	2008

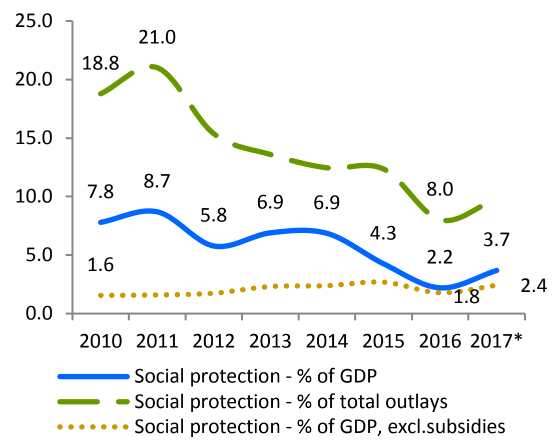
Source: IDR 2000; UNICEF (2003); Census 2014; World Bank; UNAIDS (2014); UNDP (2005, 2015).

Social protection spending has decreased significantly and is highly regressive. Social protection spending (including pensions, subsidies and social assistance) decreased in the past few years from 7.8 percent of GDP in 2010 to 2.2 percent of GDP in 2016 - from 19 percent to 8 percent of total government expenditure (see Figure 3). The share of social assistance spending increased in war-related assistance rather than social assistance targeted to the poor and vulnerable. Government spending on energy price subsidies has by far exceeded spending on (contributory and non-contributory) social transfers. As a

[110] While Angola is likely to be downgraded to a lower-middle-income-country in FY18, the comparison with upper middle-income countries remains useful in terms of Angola's aspirations.

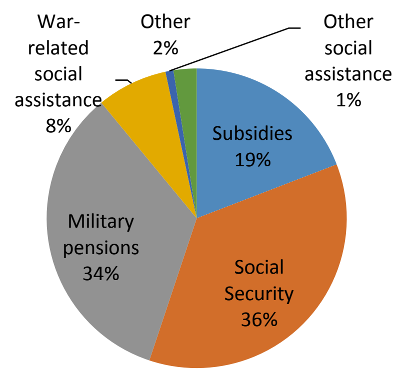
consequence, Angola's social protection spending is highly regressive, since energy price subsidies–which mainly benefit the better-off[111]–accounted for almost 64 percent of total social protection spending between 2010-2017. In 2016, the share of energy price subsidies in social protection spending decreased to 20 percent, so that the contributory pension schemes (military and social security pensions for the public sector) account for 70 percent of expenditure in the sector. Only 0.3 percent of GDP was dedicated to social assistance targeting the poorest, which is significantly below the average allocation for Africa (1.3 percent), resource rich oil countries, and middle income countries (Figure 5). Overall, the poor and the young do not seem to be well served by Angola's social protection system and the country's social protection spending could be much better aligned with its social needs.

Figure 3: Social Protection Expenditure (% of GDP), 2010-17



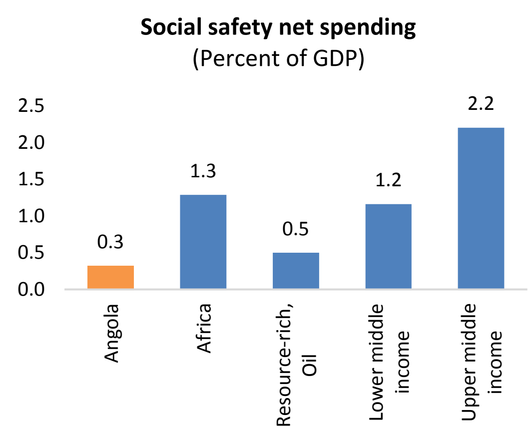
Source: Ministry of Finance. Note: 2017 data are budget figures

Figure 4: Distribution of social protection spending (% of total sector spending), 2016



Source: Ministry of Finance

Figure 5: Social safety net spending as percentage of GDP in Angola and other country groups in Africa, 2016



Source: Ministry of Finance and Kathleen Beegle, Aline Coudouel, and Emma Monsalve, editors. forthcoming. Realizing the Full Potential of Social Safety Nets in Africa. Washington, DC: World Bank

[111] While 77 percent of fuel price subsidies benefit the top 40 percent households, only 10 percent accrues to the bottom 40 percent.

In addition to regressive spending, Angola's social protection system is highly fragmented, with a variety of small-scale programs and activities involving a wide range of institutions[112]. The Government took a first important step to reduce fragmentation with the merger of two institutions - the Ministry of Social Assistance and Reinsertion (MINARS) with the Ministry of Family and Promotion of Women (MINFAMU) - into the new Ministry of Social Action, Family and Promotion of Women (MASFAMU). As part of Angola's *2025 Strategy* [113]**,** the Government has now re-launched the Integrated Local Development and Poverty Reduction Program (*Programa Integrado de Desenvolvimento Local e Combate à Pobreza - PIDLCP*), comprising several multi-sectoral interventions, which is now coordinated by the MASFAMU. However, there are persistent challenges with the implementation, harmonization and effectiveness of programs.

Policy Options

The Government needs to deploy short- and medium-term social protection policies and programs to protect the poorest from the effects of the crisis, to prevent vulnerable households from falling into poverty, and to promote economic opportunities for all.

Angola needs to improve the effectiveness of the overall social protection system through (i) better coordination of sectors involved in social protection to reduce the current agency and program fragmentation; (ii) the harmonization of targeting instruments and delivery mechanisms; (iii) the decentralization of social assistance to provide municipalities a leading role in program implementation; and (iv) an increased budget allocation for poverty-targeted social safety net programs with direct links to productive inclusion activities.

In the short term, the Government needs to reduce fragmentation in the social protection sector and improve the effectiveness of its expenditures. While the merger of the MINARS and MINFAMU into the MASFAMU marks an important first step in reducing fragmentation, the Government needs to prioritize three other on-going initiatives to minimize fragmentation, namely (i) the redefinition of the Integrated Local Development and Poverty Reduction program, and its harmonization with the remaining sectoral social protection programs previously implemented by MINARS and MINFAMU ; (ii) the consolidates of the merged MASFAMU, (iii) the further reduction of the number of programs and prioritization of two or three key social protection programs for the poor that would be scalled up progressively; and (iv) the approval of a unified household targeting instrument (based on objective and transparent criteria) and its operationalization through a social registry (*Cadastro Único*) as a tool to support outreach, intake, registration, and determination of potential eligibility for social programs. These measures would enable MASFAMU to have a better absorptive capacity to receive additional funds for an increase in coverage of social assiatnce programs.

A unified household targeting instrument should be introduced (based on objective and transparent criteria) and operationalized through a social registry. The social registry (*Cadastro Unico*) would be the tool supporting outreach, intake, registration, and determination of potential eligibility for social programs. The social registry would be populated with information from potential beneficiary households and, in addition to administrative data, collect data on indicators with a direct correlation to poverty and

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112 Institutions include the Ministry of Public Administration, Labor and Social Security (MAPESS), the Ministry of Social Assistance and Reinsertion (MINARS), the Ministry of Defense, the Ministry of Ex-Combatants and Veterans of the Motherland, and the Ministry of Family and Promotion of Women (MINFAMU).

113 The country's National Long Term Development Strategy, *Angola 2025,* defines a series of strategic policy actions to promote local sustainable development and reduce regional disparities. To achieve this, the strategy defines five main axes: (i) promote social cohesion; (ii) create employment opportunities; (iii) develop and rehabilitate local infrastructure; (iv) support local entrepreneurship; and (v) promote territorial development.

constituting a Proxy Means Test that would allow to determine eligibility of beneficiaries for poverty reduction programs.

Institutional and administrative capacity for well-targeted and scalable social assistance programs for the poor - such as cash transfers and productive inclusion initiatives – should be build at the decentralized level to enable the poor and vulnerable population to participate in the country's development and growth process. The decentralization of programs and services should be complemented with increased financial autonomy of municipalities based on the development of municipal plans. Angola's Social Action Fund (*Fundo de Apoio Social*, FAS) should continue investing in capacity building of municipal officials for resource allocation and transparent resource management and continue providing basic social and productive infrastructure and services to the poorest provinces and municipalities. The recently created unit of Social and Community Development Agents (ADECOS) should have a prominent role in providing intermediation between beneficiaries and social services.

In the mid-term, the Government should re-channel part of the savings from the energy subsidy reform to well targeted social safety net programs and reassess the social protection expenditures of the military. By using 10 percent of the 2014-2015 savings from the fuel subsidy reforms, the Government could double the spending on non-war related social assistance and scale up rapidly the coverage of the safety net programs. Also, social protection expenditures of the military should be reassessed.

MASFAMU should transform the *Cartão Kikuia* program (in-kind program) into a poverty-targeted safety net program with national coverage, based on cash transfers. Evidence from both within the region and internationally has shown that the use of cash transfers can reduce poverty, improve economic welfare and promote human development outcomes. In Angola, food-based programs (*Cartão Kikuia, Programa de Apoio Social, school kits, uniforms and sandals program, the milk and porridge program)* as well as the school feeding program represent 86 percent of the total social assistance spending, while cash programs (guardian mothers program and war veterans benefits) only account for 14 percent of total spending. The transformation of the *Cartão Kikuia* program as the MASFAMU's largest sectorial program, into a poverty-targeted cash transfer program should initially benefit the 100,000 vulnerable households that are already enrolled in the program. For additional beneficiaries, the Government should use the social registry (*Cadastro Unico*) instrument that has been developed.

Social safety net programs should be enhanced with productive inclusion activities to promote self-employment, entrepreneurship and increase local productivity. These interventions would be aligned with the government's diversification strategy and would link to other initiatives on youth productive inclusion (e.g. the new commercial agriculture initiative, farmer field schools).

Policy recommendations

Measure	Technical feasibility	Timeframe policy impact
Increase budget allocation for social assistance programs targeting the poor	High	Short-term
Define the institutional roles and responsibilities for policy and program implementation with the MASFAMU in charge of policy and program development, sector coordination and monitoring and evaluation; the Ministry of Territorial Administration (MAT) and the Social Action Fund (FAS) in charge of capacity building of provincial and municipal authorities; and municipalities in charge of the implementation of social programs and transparent resource management.	High	Short-term
Transform the Cartão Kikuia program into a poverty-targeted cash transfer program with national coverage and direct links to productive inclusion initiatives.	High	Short-term
Decide on a **national household targeting instrument** such as a Proxy Means Test combined with geographical targeting using poverty maps, and establish a social registry (*Cadastro Único*).	Medium	Short-term
Promote a stronger decentralization of social safety net and productive inclusion programs through the Integrated Local Development and Poverty Reduction Program to provide municipalities a leading role in program implementation, under clear guidelines for implementation and accountability.	Medium	Medium-term
Re-channel part of the savings from the subsidy reforms to well targeted social safety net programs and reassess the social protection expenditures of the military.	High	Short-term