



Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 10-Dec-2018 | Report No: PIDC25497



BASIC INFORMATION

A. Basic Project Data

Country Angola	Project ID P166564	Project Name Angola Growth and Inclusion DPF (P166564)	Parent Project ID (if any)
Region AFRICA	Estimated Board Date May 15, 2019	Practice Area (Lead) Macroeconomics, Trade and Investment	Financing Instrument Development Policy Financing
Borrower(s) Ministry of Finance	Implementing Agency Ministry of Finance		

Proposed Development Objective(s)

The Operation will support the Government of Angola to achieve more sustainable and inclusive growth, through (i) a macro-financial and institutional environment that is conducive to private-sector led growth; and (ii) financial and social inclusion.

Financing (in US\$, Millions)

SUMMARY

Total Financing	250.00
------------------------	--------

DETAILS

Total World Bank Group Financing	250.00
World Bank Lending	250.00

Decision

The review did authorize the preparation to continue

B. Introduction and Context

Country Context

The proposed Development Policy Financing (DPF) series supports the Government of Angola’s (GoA) efforts to maintain macroeconomic stability and lay the foundations for private-sector led economic diversification. The proposed operation is the first in a programmatic series of three IBRD loans. This first single tranche operation, in the amount of US\$ 250 million, is organized around two pillars: (i) laying the foundation for sustainable growth and (ii) promoting social and financial inclusion.



The Angolan economy is at a significant juncture. The current growth model based on oil wealth is nearly exhausted and has not delivered inclusive growth and shared prosperity. In addition, over-dependence on oil has made growth and macroeconomic management highly vulnerable to external shocks. The challenge for the new Administration of President João Lourenço, the first new leader in almost four decades and in office since September 2017, is to lay the foundations for a new growth model that is more open and inclusive, and less dependent on oil. Prospects of persistently low oil prices and potentially diminishing oil reserves over the longer-term make the call for economic diversification and inclusion even more pressing. Within this context, Angola faces two broad policy challenges that need to be urgently addressed:

- **Angola needs institutions that support more sustainable and less volatile growth.** 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 inhibiting the banking sector's ability to provide needed credit for the private sector, especially for small and medium enterprises. Inflation escalated in 2016, reaching a peak of 42 percent in December 2016, before retrenching to 25.1 percent in January 2018.
- **Angola needs a more inclusive growth model that promotes private-sector led diversification and protects the poor and vulnerable.** 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, which was destroyed during the long Civil War (1975-2002). 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. In 2016, about 30 percent of the Angolan population remained below the international poverty line (at \$1.90/ day and 55 percent if \$3.1/day is considered). Investment in human capital, effective institutions and a favorable business environment are critical for economic diversification and job creation.

The new Administration is aware of these challenges and has started to implement much needed reforms. Important steps have been taken towards restoring macro-stability and the medium-term National Development Plan (2018-2022) lays out a road map towards a more diversified and inclusive growth model that is open to supporting a young and growing population. The new Administration has also shown willingness to tackle entrenched interest and has undertaken several critical reforms, including the passage of laws for greater private sector investment and transparency. The new Administration further plans to open up important sectors to competition, including through privatizations of large scale state-owned enterprises. Macro-economic policies have been adjusted to reflect market realities and address imbalances; these include greater exchange rate flexibility; plans to reform and better target subsidies; and more effective management of natural resource wealth through the creation of a Sovereign Wealth fund with the dual objective of fiscal-stabilization and long-term saving. The proposed DPF series intends to support Angola in its ambitious and urgent reform strategy.

The proposed DPF is fully aligned with the government's priorities and reflects the World Bank's current engagement in Angola. The operation will support the GoA to achieve more sustainable and inclusive growth, through (i) a macro-financial and institutional environment that is conducive to private-sector led growth; and (ii) financial and social inclusion. The DPF builds on extensive policy dialogue structured around analytical work; this includes the recent Angola systematic country diagnostic (SCD), a broad range of technical assistance, and several ongoing and planned World Bank operations.

The DPF complements the recently approved IMF's Extended Fund Facility (EFF) program. The EFF, approved on December 7, 2019, supports macro-economic stability to pave the way for sustained and inclusive growth. The key objectives of the program are: (i) to entrench fiscal adjustment in 2018, followed by gradual fiscal consolidation to reduce public debt to sustainable levels; (ii) to liberalize the FX market, while gradually unwinding exchange restrictions and multiple currency practices; (iii) to modernize the monetary policy framework; (iv) to strengthen financial sector resilience; and (v) to foster private sector-led growth and economic diversification by improving governance and the business



environment. The EFF also supports reforms that target improvements in governance, such as enhancing transparency in debt management; restructuring the state oil company Sonangol; improving Public Financial Management (PFM); and strengthening the AML/CFT framework.

The DPF series is aligned with the Bank’s Maximizing Finance for Development (MFD) framework and the Digital Economy for Africa (DE4A) initiative. The operation supports MFD-enabling reforms, including macro-financial stability; improvements to the business climate; SOE reform and tariff reform. The DPF series further supports reforms in the telecommunications sector which are expected to enhance competition and market structure, and as such improve the availability, quality and cost of telecommunications services. Increased competition in telecoms, supported by financial inclusion measures, are expected to spur the development of new digital products and services, such as mobile financial services, and foster digital entrepreneurship. This is in line with the Bank’s Digital Economy for Africa (DE4A) initiative; as part of this initiative the Bank is supporting the GoA with a Digital Infrastructure Reform Roadmap.

The macroeconomic framework in Angola is sustainable over the medium term and adequate for the proposed operation. The depreciation of the currency and the removal of FX restrictions has allowed the current account to reach equilibrium and brought the real effective exchange rate close to fundamentals. The adoption of a market-based exchange rate will allow the exchange rate to respond to oil price fluctuations bearing most of the adjustment in the future. Domestic equilibrium has not yet been achieved as inflation and debt levels are still high. However, the policy response since late 2017—anchored in the macro stabilization program (*Programa de Estabilização Macroeconómica PEM*) – has been adequate and effective in reducing these imbalances. If implemented successfully, the PEM is expected to strengthen fiscal and debt sustainability, reduce inflation, and improve financial sector stability over the medium term. The economic diversification agenda—backed by the NDP 2018-22—will be instrumental to enhance private sector-led growth and competitiveness over the medium term, which will help reduce the volatility and pro-cyclicality from commodity dependency and support macroeconomic stability.

The overall risk associated with the proposed DPF is assessed as substantial. Most of the reforms supported by the operation are part of the NDP and benefit from strong ownership of the government. The most relevant risks are related to macroeconomic, including a sharp decline in oil prices and a stronger than expected reduction in oil production, institutional capacity limitations and stakeholder risks from potential resistance to reform from vested interest.

Relationship to CPF

The DPF series reflects the priorities and objectives of the proposed FY20-25 Country Partnership Framework (CPF), which is under preparation and due for Board approval in Q4 of FY19. Key focus areas of the CPF aim to strengthen governance and institutions for an inclusive economic and social model which is more diversified and less reliant on oil revenues; foster private sector investments for sustainable private sector-led growth; and protect and strengthen human capital through social protection, the provision of basic services, and investing in education and health.

The policy areas of the DPF series will contribute to all three focus areas of the CPF, complement investment lending under the CPF, and create the policy underpinnings that can, together with IFC, harness private sector opportunities. For example, the DPF support to establish an Oil Revenue Differential Financial Reserve aligns to the CPF objective to improve fiscal management and reduce pro-cyclicality of fiscal expenditures, and builds on an Oil Price Differential Account ASA (P159791). Support to strengthen the management and commercial viability of SOEs—including pricing and subsidy reform for financial sustainability and effective service provision of providers, increase access to finance, and improve the competition framework reflect CPF objectives to improve the enabling environment and increase private sector-led growth, especially in sectors that have previously been dominated by SOEs. This relates closely with ongoing ASA including the country economic memorandum CEM (P162993) and the country private sector diagnostic CPSD (P167838), the



subsidy reform project (P168918), business environment RAS, information and communication technology ICT and energy sector analytics, as well as lending for smallholder and commercial agriculture, which is expected to catalyze IFC support for private sector investments in agribusiness.

The agenda on financial and social inclusion and improved service delivery under DPF Pillar 2 is aligned with the CPF objective on strengthening human capital through social protection and the provision of basic services. It relates to the WB projects in social protection and health, including a local development project and a rapid social response (RSR) project in social protection.

C. Proposed Development Objective(s)

The Operation will support the Government of Angola to achieve more sustainable and inclusive growth, through (i) a macro-financial and institutional environment that is conducive to private-sector led growth; and (ii) financial and social inclusion.

Key Results

In line with these objectives, the key expected results of this operation are as follows. For Pillar 1, are expected an increase in the number of quarterly fiscal accounts published per calendar year; a higher share of the total deposit accounts insured by a deposit guarantee fund; a decrease in the SOE revenue as a share of GDP; the implementation of new fuel pricing and utility tariff-setting mechanisms, where costs and revenues collected are aligned; and an increase in the number of enforcement decisions issued by the Competition Regulation Authority. For Pillar 2, are expected an increase in the number of poor households registered in the social registry (*Cadastró Único*) and benefiting from cash transfers; and a higher share of the adult population with a transaction account.

D. Concept Description

The series' Program Development Objectives (PDOs) are to support the government to achieve more sustainable and inclusive growth, through (i) a macro-financial and institutional environment that is conducive to private-sector led growth; and (ii) financial and social inclusion. The reforms under the two objectives mutually reinforce each other and are expected to make the country more resilient to shocks, raise investor confidence, and foster fiscal sustainability and private-sector-led growth over the medium-term. The operation is organized around two pillars, each including several policy areas:

- **Pillar 1: Strengthening the macro-financial and institutional environment.** Policy areas include: strengthening natural resource management; strengthening financial sector resilience; strengthening management and commercial viability of SOEs; supporting pricing and subsidy reform for financial sustainability and effective service provision; and leveling the playing field for private investment.
- **Pillar 2: Protecting the poor and vulnerable.** Policy areas include: protecting the poor and vulnerable from shocks; and increasing access to finance.



E. Poverty and Social Impacts and Environmental Aspects

Poverty and Social Impacts

Overall, the proposed DPO supports policy and institutional changes that are likely to have poverty-reducing effects in the medium- to long-term. Yet, there will also be distributional effects in the short-run that should be addressed. Reforms to improve oversight and privatization of SOEs as well as reforms on fuel, electricity, and water tariffs are likely to improve the fiscal position of the government and to improve macro-stability and economic growth in the medium to long-term. In turn, this could help prevent economic crisis-induced increases in poverty. Policy reforms regarding fuel, electricity, and water tariffs are expected to have the largest direct and indirect impact among the proposed changes, increasing poverty in the short-run. Targeted cash transfers under the social protection program Cartão Kikuia were introduced to tackle adverse impacts of the tariff reforms. These are likely to have poverty-reducing effects, depending on several factors, including size of the transfers, coverage, and targeting. Reforms seeking to improve public service delivery and improving access to finance could have positive impacts on poverty. Reforms aimed at improving competition and introducing a higher level of foreign investment could also help decrease poverty through the channels of prices, wages of the employed, and potential job creation.

The fuel, electricity, and water tariff are expected to contribute to poverty reduction and have positive distributional impacts in the medium- to long-term. In the short-run, they are likely to have negative distributional effects. Tariff structure adjustments will increase available fiscal space, and consequently may have welfare-improving effects in the medium- to long-run. The tariff reform could also allow the fuel, electricity, and water providers to become more financially sustainable and to use additional revenue to expand and improve access, mainly to underserved rural areas. Previous analyses carried out by the World Bank (2016) and the IMF (2015) on the fuel subsidies reform had pointed out that the latter have mainly benefitted the rich. Similar studies by IMF and by the WB indicated that this is also the case in Mozambique. Fuel subsidies were benefiting those in the top income quintiles as well as people, i.e. truck drivers, from the neighboring countries. A recent IMF study (IMF, 2012) confirmed this finding for most developing countries. Yet, the World Bank study on Angola, carried out in 2016 (WB, 2016) concluded that through direct (lower household consumption) and indirect (higher prices of goods and services due to higher fuel expenditures) effects, the poverty headcount rate is likely to increase due to the envisioned fuel tariff reform. A similarly careful analysis would be necessary for the electricity and water tariffs using the same household consumption survey (IBEP, 2008).

A full-fledged PSIA will be carried out during the period of implementation of the DPF, soon after the price and tariff increases accompanying the subsidy reform are determined and the new household survey data are accessed (expected in mid-2019).

Improving the current social protection system by introducing one that consists of cash instead of in-kind transfers is to be welcomed, and is more likely to tackle the adverse impact of the fuel, electricity, and water tariff reform than the current system in place (Cartão Kikuia). The poverty-reducing effect of the envisioned cash transfer will crucially depend on the exact size of transfers, targeting, transparency of allocation mechanisms, as well as other practical considerations. The current system in place, Cartão Kikuia, had multiple problems serving the poor as a recent WB (2016) illustrated. The main problems consisted of (i) too low transfers, (ii) non-transparent targeting, as well as the (iii) in-kind nature of the transfers. Latter consists of vouchers to be redeemed in so-called Kikuia stores or to be used for a set of products that can be purchased with the card. The main problems being: (i) the number of available stores are concentrated in the capital city, (ii) the supply of products in existing stores is low, and (iii) there are reported technical problems in card recognition. All of the above explains why most beneficiaries are not able to use the 10,000 Kwanza available on the card. The latter amount is far below the 60,000 (close to \$200) needed to effectively reduce poverty – because family size is currently not taken into account. Hence, planning for transfer amounts to compensate for the average expected subsidy-removal loss in income among the two bottom quintiles and hence increase coverage are to be welcomed. Going forward, it will also



be crucial to clearly communicate eligibility criteria through social media and municipalities, as well as improving targeting mechanisms. Setting up the social registry (Cadastró Único) is a step in the right direction. Depending on the start date of the new social protection program and availability of the most recent household survey (mid-2019), the poverty-reducing effect of the cash transfer could be studied.

There are potentially poverty-reducing effects that could arise from leveling the playing field for private investment and removing barriers for foreign investors as well as anti-competitive practices. Moving from a market structure dominated by incumbent operators to a competitive one could have welfare-improving effects through prices, wages of the employed, and job creation. Going forward, these effects can only be verified and quantified once the specifics of the reforms become clearer.

Improved access to finance has been found to support growth and income equality. Modern development theory sees the lack of access to finance as a critical mechanism for generating persistent income inequality and slower growth (Demirgüç-Kunt and Levine 2008). Small enterprises and poor households face much greater obstacles in their ability to access finance all around the world but more so in developing countries like Angola. The difficult access to the banking system by the poor occurs because banks focus on areas that offer economies of scale. In other words, the spread of formal banking services rises with income. Reforms to expand mobile payments will have a positive impact on vulnerable groups by expanding financial services in these areas and by reducing transactions costs (e.g. traveling costs) through electronic systems. This allows accounts to be maintained at relatively low costs to savers and borrowers located in these underserved areas.

Environmental Impacts

Angola's environmental legal framework is in place; however, further efforts are needed to strengthen the administrative capacity and implementation framework for the management of environmental risks. The Environment Framework Law (EFL) and relevant subsequent decrees, establish the general conditions for public consultations, enforcement, prevention and control of pollution, and lay out requirements for prior environmental assessment. Strategic Environmental Assessments, which may provide necessary information on environmental and social safeguards implications of the policy documents, do however not exist. Environmental Impact Assessment (EIA) is a legal requirement and it is a necessary condition to obtain the approval to implement any development project. The decree on ESIA provides a list of projects subject to ESIA and categorizes them into different sectors. General ESIA guidelines to assist developers and practitioners with the ESIA process in Angola are available and specific ESIA guidelines exist for some sectors such as water, mine, gas pipeline, road and house building sectors. However, there is a need for specific ESIA guidelines for other relevant sectors including but not limited to electricity, transport, agriculture, fishery. The National Environmental Assessment Directorate, which, among other things, is responsible for reviewing and commenting on ESIA reports, is under-staffed and insufficiently financed to ensure environmental compliance and enforcement. Furthermore, the existing framework is not harmonized with WB and best international environmental and social practices.

Overall, the prior actions supported by the DPF are not likely to have significant adverse effect on the environment, forests and natural resources. As the government plans to improve the business climate for private investment (Prior action 5), this can attract business, and may also contribute to improved environmental impact assessments.

Increased competition, as a result from a strengthened legal and institutional framework for SOE oversight and privatization (Prior action 3), may indirectly generate environmental benefits as more modern production technologies are employed. The privatization of certain companies may also contribute to better environmental and social management



in Angola. As part of the SOE diagnostic, a scorecard will be developed for SOEs which as part of Key Performance Indicators (KIPs) will also include social, welfare, human and environmental aspects.

The other prior actions in the DPF are unlikely to have any significant environmental effects. Possible environmental concerns may relate to expanded private sector growth. As such, in supporting the private sector, emphasis should be given to ensuring an efficient process of Environmental and Social Assessment, and adequate monitoring and enforcement of the regulatory framework, including in the area of environment and natural resources.

CONTACT POINT

World Bank

Norbert Matthias Fiess, Mazen Bouri
Lead Economist

Borrower/Client/Recipient

Ministry of Finance

Implementing Agencies

Ministry of Finance
Dr. Osvaldo Joao
Director, GERI
osvaldo.joao@minfin.gov.ao

FOR MORE INFORMATION CONTACT

The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 473-1000
Web: <http://www.worldbank.org/projects>

APPROVAL

Task Team Leader(s):

Norbert Matthias Fiess, Mazen Bouri



Approved By

Country Director:	Elisabeth Huybens	21-Dec-2018
-------------------	-------------------	-------------